Realizing Ambitions
Creating Value

Bahrain Development Bank

Annual Report 2018

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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

Overview

Bahrain Development Bank (BDB) provides a variety of financial services that are tailored to meet the needs of small and medium businesses in Bahrain.

BDB commenced its operations in 1992 as a specialist Bank. BDB's activities are focused on financing and developing small and medium businesses in addition to encouraging and supporting the entrepreneurship activities in the Kingdom of Bahrain.

Working in-line with Bahrain Economic Vision 2030, BDB adopts a dynamic and effective strategy for stimulating entrepreneurial activity in implementing its plans for financing and developing small and medium businesses.

This strategy is in line with the Bank’s mission of being an active participant in national strategy by supporting this sector of the economy. BDB’s role in this context is especially significant given the growing size and contribution of this important segment to domestic economic activity.

BDB adopts a dynamic and effective strategy for stimulating entrepreneurial activity.

Vision

To support projects that yield substantial economic, social and environmental benefits.

Mission

To promote entrepreneurship and innovation in the Kingdom, by encouraging Bahraini professionals, enterprising women and ambitious youth, who demonstrate strong business acumen and leadership qualities in promoting the growth and prosperity of Small and Medium Enterprises (SMEs) through financial support and advisory services.

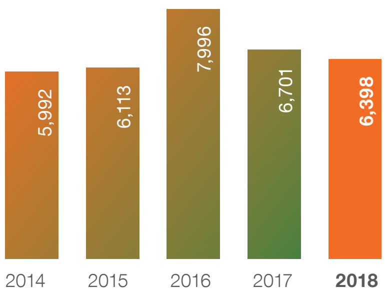
Financial Highlights

	2018	2017	2016	2015	2014
Income Statement (BD thousands)					
Net islamic finance and interest income	**6,398**	6,701	7,996	6,113	5,992
Other income	**3,788**	3,115	2,201	4,351	5,197
Operating expenses	**7,551**	9,335	9,279	8,954	7,204
Expected credit losses / provision / impairment	**4,074**	8,152	1,971	477	3,280
Net profit (loss)	**(1,326)**	(7,671)	(1,053)	1,033	705
Dividend (percent)	**0%**	0%	0%	0%	0%
Balance Sheet (BD thousands)					
Total assets	**158,205**	176,170	211,333	198,140	174,306
Islamic financing and loans to customers	**85,866**	114,535	139,221	144,308	110,048
Investments (securities, properties, associates)	**43,403**	27,595	26,903	23,533	19,290
Total deposits	**35,001**	46,440	69,216	67,184	57,137
Customers' deposits	**35,001**	35,084	58,541	49,098	38,321
Total Equity	**67,491**	72,685	80,361	81,233	75,822
Profitability					
Return on average equity	**-1.89%**	-10.02%	-1.30%	1.32%	0.96%
Return on average assets	**-0.79%**	-3.96%	-0.51%	0.55%	0.42%
Earnings (Loss) per share (fils)	**-20**	-118	-16	16	11
Cost-to-income ratio	**74%**	95%	91%	86%	64%
Capital					
Equity/total assets	**43%**	41%	38%	41%	43%
Total deposits/equity (times)	**0.52**	0.64	0.86	0.83	0.75
Capital adequacy	**46.56%**	39.80%	38.61%	37.98%	44%
Business Indicators					
Islamic financing and loans to customers/total assets	**54%**	65%	66%	73%	63%
Investments/total assets	**27%**	16%	13%	12%	11%
Islamic financing and loans to customers/customer deposits	**2.45**	3.26	2.38	2.94	2.87
Number of employees	**166**	182	188	203	200

Key Ratios

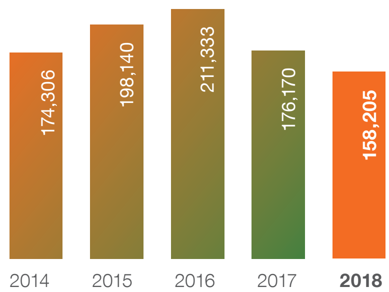
Net Islamic Financing and Interest Income (BD Thousands)

6,398



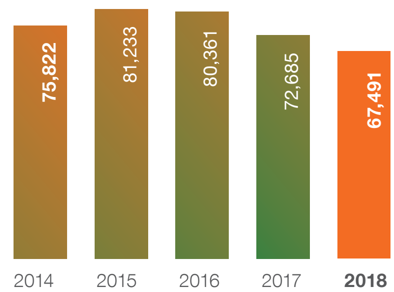
Total Assets (BD Thousands)

158,205

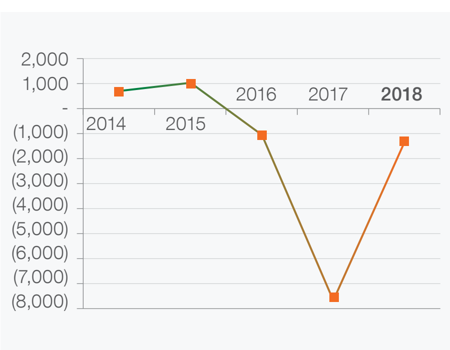


Total Equity (BD Thousands)

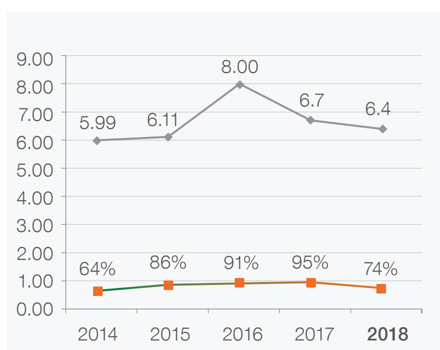
67,491



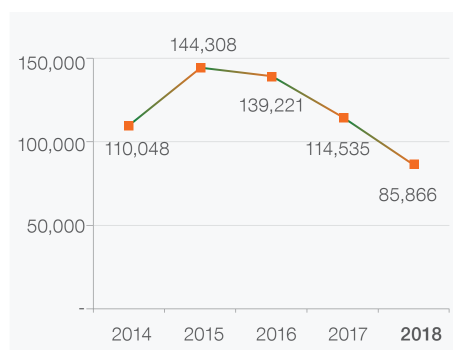
Net Profit (loss) (BD Thousands)



Net Interest Income (BD Millions)
Cost to Income Ratio



Islamic Financing and Loans to Customers (BD Thousands)



Creating Value

Bahrain Development Bank's activities are focused on financing and developing small and medium businesses in addition to encouraging and supporting the entrepreneurship activities in the Kingdom of Bahrain.

Financial Review

Overview

The Net Loss reported by the Bank for 2018 BD 1.33 million, was much lower than that of the previous year (2017: BD 7.67 million). This reduction in net loss was achieved mainly due to reduction in the charge for expected credit Losses (ECL)/ provisions by 51% and operating expenses by 19%.

Balance Sheet size as at year-end 2018 BD 158.21 million was lower by 10% compared to end of the previous year (2017: BD 176.17 million). This decline was mainly due to repayment of high cost deposits.

Net Islamic Finance and Interest Income

Net Islamic finance and interest income of BD 6.40 million was lower by 5% (2017: BD 6.70 million) mainly on account of the reduction in size of the financing portfolio.

Other Income

Total other income generated during the year BD 3.79 million was higher (2017: 3.12 million) mainly on account of higher recoveries from impaired financing portfolio and also profit on sale of an investment.

Operating Expenses

Operating expenses BD 7.55 million were lower by 19% compared to the previous year (2017: 9.34 million) mainly due to the closure of branches, reduction in the staff and exercising strict control over costs.

Expected credit losses / impairment

Aggregate charge towards allowance for Expected credit losses /Provisions and impairment BD 4.07 million for the year ended 31 December 2018 was substantially lower than of the previous year (2017: BD 8.15 million).

Equity

The equity attributable to the Bank's shareholders, at BD 67.49 million, was lower than that of the previous year (Dec. 2017: BD 72.69 million) mainly on account of the transition adjustment to retained earnings on adoption of IFRS 9 at the beginning of the year and also the losses incurred for the year. The Bank's shareholder's are Ministry of Finance (89.74%), SIO (5.13%) and Pension Fund (5.13%).

Capital Adequacy Ratio

As against minimum capital adequacy ratio (CAR) of 12.5% prescribed by the Central Bank of Bahrain (CBB), the Bank's ratio at year end 2018 was 46.56% (2017: 39.80%). The ratio, based on guidelines issued by CBB, which are compatible with those of the Basel Committee on Banking Supervision, measures total qualifying capital held by an institution in relation to its risk weighted assets. The improvement in CAR was on account of the change in the Risk Profile of the Assets Portfolio.

Board of Directors

01.
Khalid Al Rumaihi
Chairman

Appointed the Chairman of the Bahrain Development Bank in March 2016. Mr. Al Rumaihi was appointed as Chief Executive of the Bahrain Economic Development Board (EDB) in March 2015 and Chairman of Edamah in December 2017. Mr. Al Rumaihi currently serves as a Board Director of the National Bank of Bahrain, Bahrain Mumtalakat Holding Company, Bahrain Tourism and Exhibitions Authority and Education and Training Quality Authority. He remains a Board Director of the EDB.

Mr. Al Rumaihi previously spent more than 10 years at Investcorp as a Managing Director, a member of the Management Committee and Head of the Institutional Placement Team covering Investcorp's clients in the Gulf. Before joining Investcorp, Mr. Al Rumaihi spent 9 years serving at J.P. Morgan as head of the private client group in the Gulf. He Chaired the Board of Bahrain Airport Company and held previous Board positions at Gulf Air and Securities Investment Company (SICO).

He holds a Master's degree in Public Policy, specialising in Economic Development, from Harvard University, and a Bachelor of Science degree in Foreign Service from Georgetown University.

02.
Sabah Khalil Al-Moayyed
Member

Managing Partner of Intellect Resources Management W.L.L., a Management Consultancy firm. Recognized as a veteran banker and an advocate of promoting innovation, leadership and entrepreneurship within industries and organizations and is a regular speaker at various regional and international forums.

Mrs. Almoayyed holds a Bachelor of Science degree in Economics and Business Administration from the American University of Beirut, Lebanon and Masters in Business Management Finance degree from Kelastat Business School, University of De Paul, Chicago and has attended Executive Management programs at Wharton School at University of Pennsylvania and Darden College at University of Virginia in the USA.

Mrs. Almoayyed previously held the position of Chief Executive Officer at Eskan Bank Bahrain. Currently she is holding the position of Board Member of Lazurde Company for Jewelry (publicly listed) in Saudi Arabia and Chair of the Audit committee, Member of the Audit Committee for National Bank of Bahrain, Chairman of Flat 6 Labs Bahrain, Member and Chair of the Finance and Administrative Committee of the Board of Trustees of the Council for Higher Education Bahrain, Member of the Advisory Board of Suliman Olayan Business School American University of Beirut, Lebanon and member of the Board of Directors Institute for GCC. She has held as well numerous Board memberships such as Board Member Mumtalakat Holding Company President of the Bahrain Banker's Association. Chairman of Pinebridge Middle East Bank (Private Equity), Member of the Executive Committee of EBDAA Bank, Member of the Board and Chair of the Risk Committee at Naseej, Board Member of the Vocational Training Committee for the Banking Sector, The Deposit Scheme of Bahrain, Bahrain Chamber of Commerce Foreign Trade Committee, Consultative Council for the Heads of the Gulf States, Society of Honour "Deltamiu" USA, Global Women Corporate Directors, New York. Founding Member, The GCC Women Corporate Directors Gulf Chapter and Norway-Bahrain Business Council, Member and Head of Economics Committee Supreme Council for Women and Board of Trustees Bahrain Bayan School.

03.
Saleh Hassan Ali Hussain
Member

Holds a Master's degree in Business Administration from Brunel University in United Kingdom with over 35 years of banking experience. He is the President of Saleh Hussain Consultancy and holds the following memberships:

Board Member and Head of Audit Committee of ABC Islamic Bank, Bahrain, Board Member of Solidarity Holding Company, Bahrain, Head of Audit Committee of Alkhabeer Capital, KSA, Head of Audit Committee of AlMajdouie Group, KSA, Member of Audit Committee of Saudi Hollandi Bank, Board Member of Saudi Solidarity Takaful Company, KSA.

04.
Tariq Jaleel Al Saffar
Member

Graduated with a Bachelor of Business, Marketing and Entrepreneurship from Edith Cowan University in Perth, Australia, where he achieved distinctions in Enterprise and Creativity.

Mr. Al Saffar comes from a merchant family which focuses on FMCG products and food distribution. He has worked very closely with multi-nationals like P&G, Clorox, Gillette, Kellogg's, etc. He has a passion for technology; Mr. Al Saffar set up the first electronic payment platform that allows payment of utility bills and mobile top-ups. He has over 24 years of experience working with local and multi-national companies in the communications arena and is active in real estate, electronic payments, health care and distribution. He is a board member of Mohamed Ebrahim Al Saffar Company (MES), the Bahrain Economic Development Board (EDB), the Telecommunication Regulatory Authority (TRA), Board member of the Executive committee of Bahrain International Circuit (BIC), Chairman KKT Bahrain Clinic, Chairman KKT MENA Holding BSC (c), Chairman and CEO of Harbour Investment Holding Company (HIH), Chairman of Arabian Taxi and Chairman of Payment International Enterprise B.S.C (PIE).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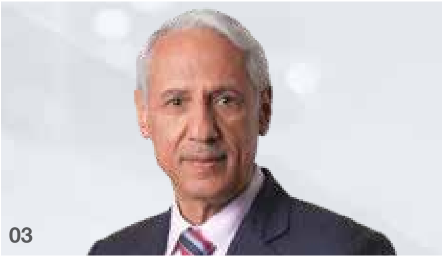
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05.
Marwan Khalid Tabbara
Member

Co-founder and Managing Partner of Stratum, a management consulting firm headquartered in the Kingdom of Bahrain, and represents distinguished experience in strategic, financial, and transaction advisory. He has advised the firm's clients on significant transactions both regionally and internationally and has supported the development and growth of a range of businesses and real estate developments. Having previously worked in the Global Corporate and Investment Banking division of Citigroup in New York, London, and Bahrain, he has also supported large private and public sector clients on transactions within the Middle East and internationally. He currently serves as Vice Chairman of the Board and Audit Committee Member of Bahrain Bourse B.S.C.(c) (Bahrain's national stock exchange), and as Board Member, Risk Committee Chairman, and Investment and Credit Committee Member of Bahrain Development Bank B.S.C.(c), and as Board Member and Investment Committee Member of publicly listed Bahrain Flour Mills Company B.S.C. (Al-Matahin). Mr. Tabbara holds a Master of Engineering Management and a Bachelor of Science in Electrical Engineering and Economics from Duke University, North Carolina, in the United States of America.

06.
Tala Abdulrahman Fakhro
Member

The Executive Director of the Market and Strategy Intelligence department at the Economic Development Board. Ms. Fakhro is a seasoned government administrator, fixed income product specialist and legal professional with extensive experience of structuring and portfolio management at Morgan Stanley in London, Gulf International Bank, the Saudi National Commercial Bank and NCB Capital in Bahrain. She has a Bachelor in Economics from Smith College, Northampton, holds a Juris Doctor from the Georgetown University Law Center in Washington DC, and has passed the New York bar exam. Ms. Fakhro was appointed as a director of the board of Bahrain Development Bank in 2016. She is also a member of the Board of Directors of the Benefit Company.

07.
Ghassan Ghaleb Abdulaal
Member

Currently serves as the Chief of Staff within the placement and relationship management team at Investcorp. This is Mr. Abdulaal's second stint at Investcorp having served with the firm for six years previously between 2003-2009. In the intervening period between 2009 and 2012, he worked as an Investment Manager with Bahrain Mumtalakat Holding Company. Prior to joining Investcorp in 2003, Mr. Abdulaal worked at KPMG Consulting where he was a Consultant within the Business Performance Improvement Group. Prior to that, he worked briefly with the HEC School of Management in Paris.

Mr. Abdulaal holds a BA (Hons) in Accounting and Finance from the University of Kent at Canterbury, UK, and an MSc in Analysis, Design and Management of Information Systems from the London School of Economics.

08.
Maryam Adnan Al Ansari
Member

Joined the Office of the First Deputy Prime Minister upon its establishment, in May 2013, as a member of the Projects Department. She is now Chief of Strategic Projects where she is in charge of strategic Housing and Infrastructure projects. Prior to that, Ms. Al Ansari worked at the Economic Development Board as part of the Reform Projects department, where she contributed to revising the National Economic Strategy, and worked closely with the Ministry of Housing and the Ministry of Transportation and Telecommunication on key strategic projects. Ms. Al Ansari holds a degree in commerce from McGill University.


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Shaping The Future

The year witnessed the launch of a number of initiatives and programs designed to stimulate and support emerging projects in the Kingdom of Bahrain.

Khalid Al Rumaihi
Chairman

Cumulative Financing

BD 592m

The total amount of cumulative financing done by the Bank is BD 592 million since it commenced operations in 1992.

Development Services Beneficiaries

2,695

Enterprises benefited from the development services.

I have the pleasure in submitting Bahrain Development Bank Group's report (the Bank and its subsidiaries) accompanied by the consolidated financial statements for the year ended 31 December 2018.

In addition to the consolidated financial statements of the Group, the report covers the financing and development operations, including the funding and development of Small and Medium Enterprises (SMEs) and other financing programs that are provided by the Bank.

The Bank financed a number of projects and activities in the industrial, trade and service sectors through direct and indirect financing and equity participation in addition to funding the Country's Agricultural, Fisheries and Education Funding Programs. A total of BD 26.49 million was financed during the year, bringing the total amount of cumulative financing done by the Bank to BD 592 million since it commenced operations in 1992.

I am pleased to report that 2,695 enterprises benefited from the Bank's development services and programs which include training, coaching, mentoring, and entrepreneur events.

The year also witnessed the launch of a number of initiatives and programs designed to stimulate and support emerging projects in the Kingdom of Bahrain. There was a particular focus to support entrepreneurial projects that are based on innovation and new technologies. At the forefront of these initiatives was the launch of a US$100 million fund of funds (Al Waha Fund) by the Bank to build venture capital capability and provide access to funding to technology startups in the region. The Bank has partnered with various institutions to support, develop and stimulate the local and regional entrepreneur eco-system and has deployed investment into five funds since Al Waha Fund's closing in April 2018.

Seed Fuel-Rowad, one of Bahrain's pioneer funding programs developed by BDB provides startups at seed and early stages with coaching, mentoring and training, access to investors and networks, special startup services and perks, and up to BD 25,000 in equity investment funding. The program has 7 investments in its portfolio since its launch.

The Bank also initiated its Cloud journey in 2018 by partnering with AWS Professional services to perform a migration readiness assessment. BDB will adopt next year a serverless website which is a cloud native approach allowing the Bank to benefit from the improved agility, scalability and latency potential in the cloud as well as providing our clients with improved experience in terms of time efficiency and lowering costs for the Bank.

As part of the Bank's commitment to support the Kingdom's future in environmental and agricultural innovation, BDB proudly launched The Farmers Market in Hoorat A'ali in February, 2018 with the cooperation of the Ministry of Works, Municipalities Affairs and Urban Planning, and the National Initiative for Agricultural Development (NIAD). The market is designed to embrace a wide range of locally produced fruits, vegetables, dates, roses, etc.

The Group will continue to align its efforts with the substantial national efforts and initiatives to develop SME sector performance and provide support to this burgeoning sector. It will introduce and implement more pioneering programs, and provide the tools needed to improve its performance and enable it to play an even greater role in the Kingdom's economic development and diversification process. Simultaneously, the Group will work on joint initiatives with the public and private institutions with the shared vision of an elevated SME sector.

I would like to take this opportunity to extend my sincere thanks and gratitude to His Majesty King Hamad bin Isa Al Khalifa, the King of the Kingdom of Bahrain, His Royal Highness Prince Khalifa bin Salman Al Khalifa, The Prime Minister, His Royal Highness Prince Salman bin Hamad Al Khalifa, The Crown Prince, Deputy Supreme Commander and First Deputy Prime Minister, for their continued support and wise leadership.

I would also like to express my appreciation to the members of the Board of Directors, the Group's employees and all partners. We look forward to sharing more successes together in the future.

Khalid Al Rumaihi

Chairman

A Focused Strategy for Growth

As part of BDB's continued efforts to assist entrepreneurs and the private sector, the Banking Division works closely with the Development Division and the Investment Division to identify opportunities and offer a complete platform for entrepreneurs.

Executive Management

01.
Sanjeev Paul
Group Chief Executive Officer

Sanjeev Paul took over as Group Chief Executive Officer of Bahrain Development Bank B.S.C (BDB) in May 2018.

He has over 30 years of international banking experience with Standard Chartered Bank (SCB) and was a member of SCB's global leadership team. Sanjeev was based in Singapore where he served as Managing Director and Regional Head of Commercial Banking for ASEAN and South Asia, heading the bank's commercial banking business across nine countries, including markets such as Singapore, India, Malaysia and Indonesia. Prior to that, he served as Global head for Local Corporates and Commodity Traders- a business spanning over 30 countries in SCB's global franchise. He has also headed SCB's structured trade finance business as Global Head of Structured Trade Finance and Financing Solutions. Earlier to that Sanjeev was responsible for setting up the Standard Chartered Bank's Middle Market Business in India and also served as a risk approver for Standard Chartered Bank for five years in India.

Sanjeev also served as the Chairman and Non-Executive Director on the Board of Directors for Standard Chartered Bank Vietnam Ltd. He is also an NED on the Board of Ebdaa Bank for Microfinance since October 2018.

Sanjeev graduated with a Bachelor's degree in Engineering from Delhi College of Engineering and an MBA in Finance and Marketing from FMS, University of Delhi in India.

02.
Sh. Hesham Bin Mohamed Al-Khalifa
Chairman and Managing Director, Bahrain Business Incubator Company

Joined Bahrain Development Bank in 2011.

Sh. Hesham is a leading industry specialist on entrepreneurship, SME and economic development holding over 27 years of experience. Throughout his career, he has contributed to the development of numerous economic and social strategies and programs, namely the development and institutionalization of Bahrain-Arab Model for Enterprise Development and Investment Promotion in coordination with Bahrain Development Bank (BDB) and The United Nations Industrial Development Organization (Unido) and BDB's Rowad program, the development of Bahrain Business Incubator Centers, Riyadat (Women Incubator Center), Art Cluster and Farmers Market and various strategies in economic development and entrepreneurship.

Sh. Hesham serves as board member of various steering committees and societies in support of entrepreneurship such as MENA Inc, AIESEC, and KPMG Entrepreneurship.

He graduated with a Bachelor's degree in Economics from The American University of Washington in USA.

03.
Khalid Yousif Meshkhas
Deputy General Manager – Head of Support Services

Joined Bahrain Development Bank in 2011.

Khalid has gained more than 28 years of combined banking experience from conventional and Islamic Banks. During his career he has worked with National Bank of Bahrain and Al Salam Bank in various Operation Departments such as Loans, Time Deposit, Money Transfer, Commercial Services, Customer Services and Treasury back office. He also worked in the marketing field which includes Retail and Commercial Banking.

He serves as board member of Bahrain Specialist Hospital BSC (C) and Estate Company for Health Services WLL and Gulf Diabetes Specialist Centre.

Khalid graduated with an Associate Diploma in Accounting from University of Bahrain and also holds Advanced Banking Diploma from Bahrain Institute of Banking and Finance (BIBF).

04.
Hasan Khalil Al-Binmohamed
Senior Vice President – Head of Human Resources and Corporate Communications

Joined Bahrain Development Bank in 2005.

Hasan has 17 years of banking experience; his areas of expertise are Human Resources, PR and corporate communications. He joined KFH-Bahrain in January of 2003 in the formation phase of KFH-Bahrain.

He holds a Bachelor's degree in Government from Eastern Washington University, USA; and a Diploma from Spokane Falls Community College, USA. Hasan has obtained his CIPD in 2012 and attended Harvard Business School's Executive Program in 2013.

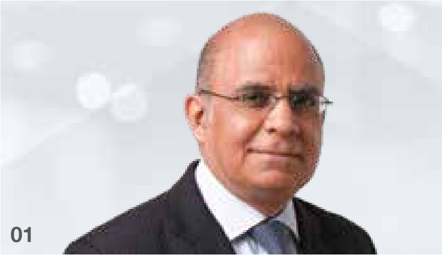
05.
Areije Karim Al-Shakar
Senior Vice President, Head of Development Services

Joined Bahrain Development Bank in 2010.

With over 16 years of experience in banking and entrepreneurship, currently Areije leads both the Development Services Division and the Fund Management team of the Al Waha Venture Capital Fund of Funds. Her role at the bank includes entrepreneur development, seed funding, and fund management. She has been involved in the development of several programs namely; BDB's Rowad Program, Seed Fuel-Rowad, and the launch of the Al Waha Fund platform. She also serves on the board for several startup companies and is the working group representative in the SME Board Committee Bahrain.

Areije has worked in reputable organizations including Investcorp, Citibank, BNP Paribas and Lehman Brothers.

She holds a Master's of Science in Public Policy and Management, School of Oriental and African Studies (SOAS), University of London, a Bachelor of Commerce in Finance, John Molson School of Business, Concordia University, and is a Certified Business Coach and Mentor, Chartered Management Institute, UK.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Maytham A. Hameed Abbas
Senior Vice President – Head of Business Development

Joined Bahrain Development Bank in 2017. He has 14 years of working experience. Before joining BDB, Maytham held a number of roles in Kuwait Finance House in corporate banking and credit risk management, as well as having held previous posts working on investment promotion and entrepreneurship with UNIDO and strategy consulting with BDO.

Maytham Abbas is the Head of Business Development and the Board Secretary in the Bahrain Development Bank. In his role he leads the formation and implementation of the Bank's strategy, product development and digitization initiatives.

Maytham is a graduate of McGill University in Economics and Physics, and holds professional qualifications in finance and risk management.

07.
Vijay Kumar T.
Senior Vice President - Chief Risk Officer

Joined Bahrain Development Bank in 2016.

He has over 26 years of experience in banking and financial services industry and widely exposed to Financial Risk Management, IFRS 9 and Basel II/III implementation. His areas of expertise include Enterprise Risk Management, Risk Management Policies and Procedures, IFRS 9 Expected Credit Loss models, Credit Portfolio Management, Operational Risk Management, Risk Analytics, Credit Scoring/Rating Models, Risk Appetite, Risk Strategy, Risk Architecture, Economic Capital, ICAAP and Stress Testing. Prior to joining BDB, Vijay was the Head of Risk Analytics for a commercial bank in UAE. He has conducted several training programs and is a key note speaker at Risk Management events. He joined Bahrain Development Bank in 2016.

Holds an MBA in Finance from Osmania University, India.

08.
Samuel Verghese
Vice President - Chief Financial Officer

Joined Bahrain Development Bank in 2007.

At his early years with BDB, Samuel was appointed as Financial Control Senior Manager and then promoted to be Head of Internal Audit from 2008 till April 2015. He was designated as CFO in 2015.

Samuel has experience of over 29 years of which 23 years has been in the banking sector. Before joining BDB he has worked with Remya Plastics as Finance and Account Manager, Steel Authority of India Ltd (SAIL) as Budget and MIS Junior Manager, The South Indian Bank Ltd as Corporate Financial Management Chief Manager, Kerala Financial Corporation as Finance General Manager and Oman Development Bank as Chief Accountant.

Holds a Bachelor of Commerce degree from University of Calicut, India; and FCA from Institute of Chartered Accounts of India.

09.
Siddharth Chaudhary
Vice President- Head of Internal Audit

Joined Bahrain Development Bank in 2018

Siddharth has over 15 years of experience in internal audits, assurance engagements and other financial advisory services. He worked with SICO, a leading Investment Bank in Bahrain for seven years in the Internal Audit Department. He began his career with Ernst and Young India, followed by holding a post with the Risk Consulting division of BDO Bahrain, where he led risk-based internal audits for various financial service companies, firms, and other entities.

Siddharth is a Chartered Accountant, a Certified Internal Auditor and a member of the Institute of Internal Auditors (USA). He holds a Masters of Commerce degree from Kanpur University in India.

10.
Isa Ahmed Al Doseri
Senior Manager - Head of Investment Division

Joined Bahrain Development Bank in 2011

Isa collectively has nine years of professional experience in venture capital, private equity, investments, retail, operations and financial control.

He serves as a member of board of directors of Tenmou, Food Corp WLL., Bahrain Business Incubator Center, Al Dar Wood Furniture Manufacturing WLL, Al Waha Venture Capital Fund Company and Bahrain Agriculture Foods amongst others.

He is a BSc honors graduate majoring in Accounting and Finance from Ahlia University, a Certified Public Accountant from the State of Colorado, USA and a Series 79 investment banking certificate holder accredited by the Central Bank of Bahrain.

11.
Dana Abdulrahman Alsendi
Senior Manager - Head of Legal

Joined Bahrain Development Bank in 2018.

Has gained more than 8 years working experience. She has commenced her professional career as an associate in Haya Rashed Al Khalifa Law Firm. She then joined the Legal and Corporate Affairs Department at Aluminum Bahrain (ALBA) as Legal Counsel and an assistant to the Board Secretary.

Dana is a qualified Bahraini lawyer who has obtained her Bachelors' Degree in Law (LLB) from the University of Leicester (UK) and her Masters' Degree (LLM) in International Corporate Governance and Financial Regulation from the University of Warwick (UK).


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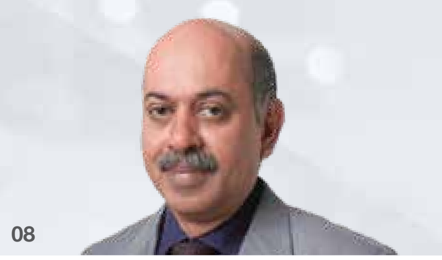
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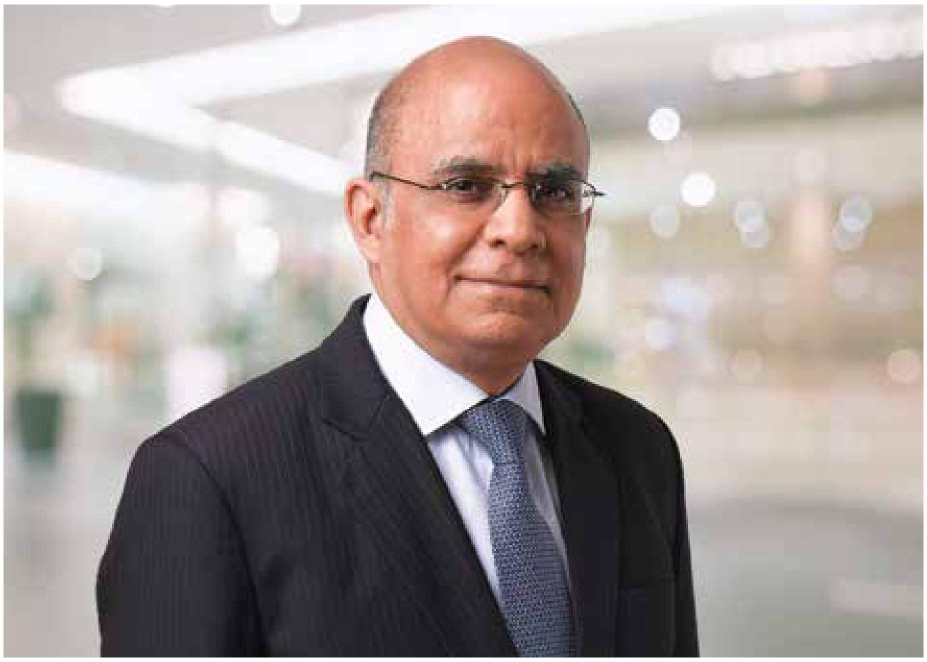
A Clear Vision

"The Bank has a clear vision of contributing to Bahrain's economy through the support and development of Bahrain's small and medium size enterprises (SMEs) across industries and sectors."

Sanjeev Paul
Group Chief Executive Officer



Expected New Jobs

3,191

The Bank's contribution to funding SMEs will help in creating approximately 3,191 expected new jobs.

Expected Value Added

BD 18.9m

BDB funding to SMEs will help generate BD 18.9 million value added to Bahrain's economy.

It is my pleasure to present to you the Annual Report of Bahrain Development Bank Group (the Bank and its Subsidiaries) for the year ended December 31, 2018. The Bank has demonstrated significant improvement in its financial position and successfully fulfilled its business objectives over the past year.

The Bank has a clear vision of contributing to Bahrain's economy through the support and development of Bahrain's small and medium size enterprises (SMEs) across industries and sectors. In 2018, the Bank funded across all loan categories (project finance, fisheries, and agricultural) BD 26.5 million, benefitting 821 projects led by SMEs in the country. We anticipate that the Bank's contribution to funding SMEs will generate BD 18.9 million of value added to the economy, BD 19.2 million of export growth and create approximately 3,191 new jobs in the upcoming two years.

In addition to providing financial services, the Bank also offers business incubation services to help support both early stage and growing entrepreneurs to develop their businesses. The support provided includes coaching and consulting, financial restructuring and advisory services. This programme was targeted at a diverse customer base and benefitted 180 companies - 78 business owners in Bahrain Business Incubator Centre, 51 in The Business Women Incubator Centre (Riyadat) and 51 in the Agriculture sector.

Seed Fuel-Rowad, established by the Bank, is one of Bahrain's pioneer funding programs, providing start-ups with access to angel investment funding, investors, networks, special start-up services, and other services. Seed Fuel-Rowad is a member of the Global Accelerator Network (GAN) and aims to bring together the start-up communities. The current portfolio comprises of seven seed stage businesses, out of which four companies were able to obtain further funding from other angel investors, accelerators, and Venture Capital Funds. Three companies are preparing to expand into GCC in the coming year.

Furthermore, the successful launch of Al Waha Venture Capital Fund of Funds (Al Waha Fund) was a milestone for the ecosystem in 2018. Al Waha Fund is a USD 100 million Venture Capital Fund of Funds which aims at building the venture capital capability and creating access to funding - ultimately boosting the start-up ecosystem in Bahrain and the MENA region. The fund has deployed USD 45 million into four regional funds and one fintech thematic fund in 2018.

The Bank continues to encourage and support the role of female entrepreneurs in the Kingdom. The Bank offers a finance scheme catered to women led SME businesses in collaboration with Tamkeen and the Supreme Council for Women. The Riyadat Women Business Finance Scheme was established to support the growth of female led businesses and further encourage their contribution to the economic growth of Bahrain. The scheme has financed 52 female entrepreneurs totalling BD 1.2 million of finance.

In collaboration with The National Initiative for Agricultural Development (NIAD) and the Ministry of Works, Municipalities Affairs and Urban Planning, the Bank launched the Farmers Market in February of 2018 under the patronage of Her Royal Highness Princess Sabeeka bint Ibrahim Al Khalifa. The Farmers Market, located in Hoorat A'ali, is the first permanent farmers market in Bahrain. The initiative has created a destination for not only farmers to be able to continuously display their fresh produce, but also for consumers to be able to visit the farmers and enjoy the ambience and F&B offerings. This has rapidly turned into a popular place for residents and a tourist destination attracting 146,000 visitors in 2018. The Farmer's Market aims to build the capacities of the farmers to be able to distribute and ultimately contribute to Bahrain's agricultural sustainability and food security.

To align with global changes in technological advancement, the Bank is proud to be implementing the nationwide cloud first policy by beginning with the successful migration of the Bank's website in 2018 to AWS cloud. The Bank has also succeeded in launching an SMS service to enhance customer service by providing them the ability to access details via their smart devices.

I would like to take this opportunity to thank the leadership of the Kingdom of Bahrain for their continued support. I would like to also express my gratitude to the Chairman and the members of the Board of Directors for their continuous guidance and support in allowing us to achieve our mandate. I would like to also take this opportunity to highlight and thank our stakeholders for their support, The Ministry of Finance and National Economy, Bahrain Economic Development Board and The Ministry of Industry, Commerce and Tourism, as well as our strategic partners Tamkeen, National Initiative for Agricultural Development and the Supreme Council for Women. On a final note, I would like to express my warmest appreciation to the Executive Management Team and to all the employees of the Group for their commitment and energy invested in 2018 as we strive to achieve our development goals.

The regional and global economic challenges witnessed in 2018 are likely to continue in 2019. However, we are confident that the Bank, with its clear strategy and strong commitment to deliver financial services to SMEs integrated with development services, will thrive in the coming years and remain a solid partner to the country's entrepreneurs.

Sanjeev Paul
Group Chief Executive Officer

An Evolving Proposition Based on Trust

Bahrain Development Bank is committed to the highest level of corporate governance practices. The Bank's corporate governance framework is formed by global corporate governance standards as well as guidelines issued by the Central Bank of Bahrain, and the Bahrain corporate governance code.

BDB remains committed to render all possible assistance to SMEs to enable, support and encourage young Bahraini men and women entrepreneurs to lead their own businesses with financing solutions that cater to their needs and serve their business requirements.

Banking Services

Bahrain Development Bank has been playing a vital role in the development of SME sector in Bahrain. During the year, the Bank continued to finance start-ups, small and medium businesses and ventures. The Bank encourages and motivates more Bahraini youth and women to venture into the challenging careers of entrepreneurship.

Our specialized financing products such as BDB-Tamkeen Joint Finance Scheme remain favored and sought after by the SME segment. The Bank continues to provide funding for this sector including this scheme and others that fit clients' needs.

During the year, the Bank's "Tamweel Plus Scheme" assisted SMEs in financing expansion projects and unique mega start-up projects at competitive pricing. The product has been well received by the SME sector.

BDB made a total disbursement of 742 loans to the SME sector. The Bank's financing is expected to contribute foreign currency worth BD 13.1 million and import substitution of BD 1.2 million over the next two years.

The Bank continued its financial assistance to other priority sectors like fisheries and agriculture, professional services such as healthcare, training and consultancy services, etc. thereby enabling the clients to acquire self-employment, and improve their standard of living. The Bank has also contributed towards enhancing the education level of Bahraini youth through its Education Finance Scheme.

The Bank also remains committed to render all possible assistance to the SMEs that are facing difficulties or challenges due to market conditions, to enable them to overcome their problems and conduct smooth business. The Bank's strategy of supporting Bahraini youth and women to start their own entrepreneurship ventures shall continue with strong focus and dedicated efforts.

Development Services Division

The Development Services Division at BDB plays a key effective role within the Bahrain entrepreneurial ecosystem, reaching out to the public in an effort to inspire and grow entrepreneurship and innovation. The division highlights the importance of developing a national economy driven by the private sector

Total disbursement of SME loans

742 loans

through the organization's core objectives and mandate of supporting entrepreneurs and enterprises in Bahrain. The products and services offered by the Development Services Division include the BDB Rowad Program, Seed Fuel-Rowad, and the Invested Platform.

Development Services Overview

Rowad is a comprehensive platform run by the Development Services division of Bahrain Development Bank designed to assist and empower entrepreneurs in starting their business. The program aims to support entrepreneurs and startup eco-system by providing product and services at any stage of the business cycle starting as early as the idea stage. The program's objective is to foster the creation and development of enterprises and provide support to enhance the productivity and growth of enterprises and individuals by providing a holistic eco-system for entrepreneurs. The Rowad Program offers a variety of solutions supporting the needs of entrepreneurs to help start or grow their business through the BDB Rowad Program, Seed-Fuel, and the Invested platform.

BDB Rowad Program: The program offers solutions supporting the needs of entrepreneurs to help start or grow their business through 8 pillars which include coaching, training, mentoring, funding, partners, networking events, and Rowad tools. The program is available to startups, SMEs, and entrepreneurs from as early as idea stage all the way to growth and beyond. The program offers its services through various packages that provide tools to startups and SMEs at any stage of the business cycle. The program acts as an eco-system builder working closely with the startups and SMEs in Bahrain.

Seed Fuel: Seed Fuel-Rowad is one of Bahrain's pioneer funding programs developed by Bahrain Development Bank, providing startups at seed and early stages with coaching, mentoring, training, access to investors and networks, special startup services and perks, and up to BD 25,000 in equity investment funding. Seed Fuel-Rowad is part of the Global Accelerator Network (GAN) as a pioneer accelerator building startup communities.

Invested™: Invested is an investor community platform established in 2016. The Invested Platform provides investors access to tools and knowledge to support them through their startup investment journeys. Invested has a growing investor population that includes angels, VCs, and corporates. Invested hosts educational events twice a year targeted at current angels and potential startup investors as part of the aim to further develop the startup eco-system pillars.

The investor community is brought together through an online platform www.rowad.co/invested which is owned and managed by the team at Bahrain Development Bank.

Rowad Events: Rowad Events was launched in 2015 to play an instrumental role in building and connecting the local and regional entrepreneur community. A suite of events are hosted throughout the year that include Rowad Majlis™, Rowad Talk™, Rowad Workshops™, The Speed™, Pitched™, and Invested™.

LOOKING BACK AT 2018

243
BDB Rowad Coaching Sessions 2018

2,522
BDB Rowad Events Attendees 2018

65
BDB Rowad Mentor Network 2018

300
BDB Rowad Invested Network 2018

1,791
Entrants to the BDB Rowad since Launch of Program in 2015

18
BDB Rowad Partners Network 2018

3,200
BDB Rowad Total Network and Community 2018

173
BDB Rowad Program New Entrants 2018

23
BDB Rowad Events Hosted 2018

7
Seed Fuel-Rowad Companies

Investment Division

In line with The Economic Vision 2030 for Bahrain to promote economic diversification, Bahrain Development Bank, currently supports the private sector through a number of business support services, research, and financing.

As part of BDB's continued efforts to assist entrepreneurs and the private sector, the Investment Division manages equity investment products and Venture Capital Funds. The equity investment's aim is to assist the entrepreneurs in achieving their goals.

The Investment Division is responsible for managing BDB's equity investments portfolio in line with its overall mission, where the Bank plays a significant role as sponsor and manager. Investments are made in order to create a robust and diversified private sector in The Kingdom of Bahrain, supporting industries and projects that provide food security, transportation, services, microfinance, healthcare, business incubators and others.

Investment selection is based on specific criteria depending on the unique needs of a company.

The Investment Division invested and continues to invest in Startups, scale ups and SMEs, in addition to other strategic investments. BDB holds a diversified investment portfolio in 28 companies supporting industries such as food security, transportation and services, microfinance, healthcare, business incubators and others, with a total fair value of BD 6.8 million.

Support Services Division

Support Services Division contributes greatly to back and support the execution of banking services to carry ongoing business activities, strategies and assist in achieving Bahrain Development Bank Group goals through Information Technology, Operations and Administration Departments.

Information Technology

Year 2018 witnessed the achievement of numerous successful projects that focus on technological advancement in order to support the Bank's business to offer better and faster services to our customers in compliance with legal and regulatory requirements and in line with the Bank's strategy of adopting innovative digital solutions. The IT department has achieved the following:

1) Designed the Amazon Web Services (AWS) infrastructure for BDB's cloud migration plan.
2) Implementation of IFRS9 Financial Reporting Standard.
3) Implementation of Credit Risk Evaluation System.
4) Replication Setup and Testing for the Business Continuity Plan (BCP) and Disaster Recovery Plan (DRP) projects.
5) Efficiency in the control of expenditures based on budgets and available limits, and improved Email Notification by revisiting and enhancing the entire process flow in the Enterprise Resource Planning (ERP) application.
6) BDB launched 2 Way SMS Banking Feature which allows clients to obtain their finance information including Current and Loan Accounts Balance Inquiry, Branch Information, register their emails, and many other services.

And in line with CBB and BENEFIT compliance requirements, several projects were introduced including:

1) Implementation of Benefit Pay the National E-Wallet Payment System which enable Fawri and Fawri+ Transaction for BDB current account holders to pay at various merchants who offer the service.

2) Fawateer Payment which enables clients to payment to service providers including, but not limited to, telecommunication companies, Electricity & Water Authority (EWA) and others.
3) RTGS/SSS Private Network Project with CBB.
4) CRS Project Implementation for CBB Portal.

Information Security remains a focus area for IT department, and further measures were taken to adopt and implement the industry's best practices. This included a number of projects to strengthen the Bank's systems security, and continued Information Security awareness training provided to the Bank's employees to ensure customers' information is highly secured and protected against cybercrime.

Operations

The Bank has taken important steps in aligning its operations and streamlining its processes to achieve a pleasant and positive customer experience through:

1) Strategic relocations of the Bank's branches network in order to strengthen its reach to clients.
2) The Department was also engaged in the preparation and testing of the anticipated launch of CBB's upgraded RTGS settlement system through a VPN network.
3) KYC review for due diligence to comply with the requirements of FATCA and CRS and updating the Account Opening form to comply with CBB guidance.
4) Utilisation of Downey Day and Co Platform that enables the Bank to buy and sell commodities by the system for Islamic transaction placement and borrowing transactions.

Anti-Money Laundering

Bahrain Development Bank's policy prohibits and work actively to prevent money laundering and any activities that facilitates it or the funding of terrorist or criminal activities. For this purpose, the Bank has defined strict policies and procedures in compliance with the Financial Crimes Regulations issued by the CBB. These policies and procedures apply to all employees, branches and subsidiaries of the Bank. BDB has adopted specific initiatives and measures to facilitate implementation of these policies and procedures. The Bank's Money Laundry Reporting Officer (MLRO) independently enforces Anti-Money Laundry (AML) policies and reports any incidents to the Board of Directors and the applicable regulatory authorities. Moreover, all employees undergo compulsory AML training with regular refresher courses.

Know Your Customer

The Bank conducts appropriate and accurate due diligence to ensure that the financial services of BDB Group are provided to customers in accordance with the guidelines issued by the regulatory authorities. The Bank further enhanced all aspects of transactions monitoring and due diligence practices including the modification of deposit / transfer slips, and amendment of account opening forms to ensure more transparency and to build a solid customer profile.

Disaster Recovery and Business Continuity Plan

BDB has in place a clear Disaster Recovery and Business Continuity Plan in line with the Bank's policy to ensure that BDB continues its critical activities following any disastrous event. This provides a plan for continuity of business operations at all times in case of any potential disruptions resulting from unanticipated loss of services or infrastructure. Disaster Recovery Sites have been set up within the Kingdom of Bahrain and the premises are well equipped with the required infrastructure. Disaster Recovery and Business Continuity Implementation Committee has been set up to oversee the testing and implementation of the Business Continuity Plan in BDB.

Administration

Administration Department plays a key assisting role in maintaining all day-to-day services, and the successful completion of significant projects, by providing support to BDB Group, this has contributed to the increased productivity and efficiency of the Group including completing the construction of Farmers Market project, new installation of Fire Alarm Panel, upgrading the CCTV for BDB branches and linking it with Ministry of Interior and major renovation of the Bank's Headquarters. The department constantly pursues innovative means for practical cost optimization of operational expenses, while maintaining utmost efficiency. The department maintains transparency toward all service providers to offer the best services for all departments of the Bank.

Human Resources

Recognizing that staff members are the key asset of any organization, the Bank continued to significantly invest in the staff welfare and the provision of the necessary training and development opportunities. During the year 2018, all BDB employees benefited from the training and development courses provided by the Bank which included in-house training courses, external training courses, professional programs, specialized workshops and conferences.

Staff members were trained on VAT Implementation, Data Protection Law, Corporate Governance, Anti-Money Laundering, Islamic Financing, Complaints Handling Procedures, IFRS9, Code of Conduct, Whistle Blowing, Credit Rating Scorecard, SWIFT CSP, AWS, Smart Leadership, Business Continuity Plan, and Information Technology Awareness.

Building Long-Term Relationships

Working in-line with Bahrain Economic Vision 2030, BDB adopts a dynamic and effective strategy for stimulating entrepreneurial activity and implementing its plans for financing and developing small and medium businesses.

Organization Chart

Corporate Governance

BDB is committed to full compliance with the values and the best international practices/standards of personal and professional ethics. Fulfilling this commitment requires that everything done by the group, either collectively or individually, is consistent with the highest ethical and professional standards.

BDB's Board of Directors have validated the Corporate Governance principles and practices in the policy documents, (1) Commitment by Board of Directors and Management of BDB Group to the Code of Conduct and (2) the Code of Ethics and Business Conduct, which are endorsed by BDB employees.

BDB's Board of Directors, nominated by a Royal Decree, presently comprises of eight non-executive directors, including the Chairman. On joining the Board, all Directors are provided with a Directors' Induction File which includes the Bank's Memorandum and Articles of Association, the Charters of the Board and its subcommittees, the latest annual report, the Corporate Governance and other key policies, and the Bank's strategy document. Induction sessions are also held with the Chairman and Chief Executive Officer which focuses on a broad overview of the Bank, its direction, challenges and opportunities and may be supplemented by sessions on the special characteristics of development banking and its role in economic development. Select meetings may then be arranged with members of the senior management on an as needed basis, as well as a tour of the Bank's facilities.

The Board is guided by its Charter framed in accordance with applicable regulations. The Board establishes the objectives of the Bank, provides guidance, approves the strategy and budgets for achievement of the Bank's objectives, adopts and reviews the systems and controls framework, monitors the implementation of strategy by the management and overall group management performance, ensures accurate preparation and disclosure of the financial statements, monitors conflicts of interest in preventing suspicious transactions. The Board also provides assistance in securing funding from government and semi-government institutions and continues to focus on long term strategic issues; growth and diversification of BDB group's activities, and the achievement of its vision and mission.

The Board of Directors is assisted by following Board Committees: (1) Remuneration and Governance Committee (RGC) (2) Audit Committee, (3) Risk Committee (BRC) (4) Credit and Investment Committee, and (5) Sharia Supervisory Board. The members of Senior Management regularly attend Board and Committee meetings. The responsibilities of these committees for oversight are governed by their respective Charters, terms of reference and functions under its supervision that are reviewed and updated periodically. While RGC is assisting the Board in strengthening the corporate governance standards and implementation of sound remuneration and HR practices, the Audit Committee assists the Board in carrying out its duties regarding the integrity of the Bank's financial reporting system, the adequacy of the Bank's internal control processes, the performance of independent auditors and internal audit function, the independent auditor's qualifications and independence, and the Bank's compliance with legal obligations. The Board Risk Committee develops the Board's risk appetite statement and ensures an appropriate risk management and reporting framework is in place to allow implementation and monitoring of the Bank's risk profile and alignment of this to its risk appetite. The BRC is additionally responsible for the appointment and remuneration of the Chief Risk Officer and the development of the Bank's business continuity and disaster recovery plans. The Board Investment and Credit Committee reviews credit and investment proposals, exercises oversight of credit and investment related activities, reviews and recommends the Bank's business strategy and operational plan, reviews and approves appropriate asset allocation strategy and evaluates the investment and credit portfolio of the Bank. The Sharia Supervisory Board comprising three Islamic scholars provides guidance, reviews and supervises the Bank's Islamic financing activities to ensure that they are in compliance with Islamic Sharia's rules and principles.

Further more, the Remuneration and Governance Committee, Investment and Credit Committee and Audit and Risk Committee also assist the Board in conducting self-evaluation of the Board and Committees achieving a high level of involvement and understanding among Board members of its roles and responsibilities, and offer suggestions for further improvements.

BDB Disclosure on HC Module

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 not complied with certain guidance under HC-4 pertaining the appointment of the Board of Directors. This is due to the fact that the members of Board of Directors of the Bank were appointed as per the Royal Decree resolution No. 2 for 2016, issued in 8th March 2016.

The section HC-5.3 states that members of the remuneration committee must have independence of any risk taking function or committees. The Bank is not complying with this requirement as two (2) Remuneration and Governance Committee members Mr. Tariq Jaleel Al Saffar and Ms. Tala Abdulrahman Fakhro are also represented on the Investment and Credit Committee of the Board. This has been permitted by CBB in view of the fact that the Board members are limited to eight (8) who were appointed through a Royal Decree resolution and to meet independency more members should be appointed which is not deemed practical given the current Board structure which is commensurate with the Bank's size and activities.

Board Meetings and Attendance

Details of meetings held during 2018 and attendance of directors are as follows:

No.	Name	Position	27 Feb	29 April	11 June*	23 Sept	4 Nov
1.	Khalid Al Rumaihi	Chairman	✓	✓	✓	✓	✓
2.	Sabah Khalil Al-Moayyed	Director	✓	✓	✓	×	✓
3.	Saleh Hassan Ali Hussain	Director	×	✓	✓	✓	✓
4.	Tariq Jaleel Al Saffar	Director	×	✓	✓	✓	✓
5.	Marwan Khalid Tabbara	Director	✓	✓	✓	✓	✓
6.	Tala Abdulrahman Fakhro	Director	✓	×	×	✓	✓
7.	Ghassan Ghaleb Abdulaal	Director	✓	✓	✓	×	✓
8.	Maryam Adnan Al Ansari	Director	✓	✓	✓	✓	✓

* Emergency Board Meeting

Board Audit Committee (BAC) Meetings and Attendance

No.	Name of the Director	18 Feb	18 March	22 Apr	23 July	28 Oct
1.	Saleh Hassan Ali Hussain	✓	✓	✓	✓	✓
2.	Ghassan Ghaleb Abdulaal	×	✓	✓	×	✓
3.	Maryam Adnan Al Ansari	✓	✓	✓	✓	×

Board Risk Committee Meetings and Attendance

No.	Name of the D irector	22 Jan	21 Feb	11 Apr	25 Apr	27 Jun	9 Sep	30 Oct	28 Nov
1.	Marwan Khalid Tabbara (Chairman)	✓	✓	✓	✓	✓	✓	✓	✓
2.	Ghassan Ghaleb Abdulaal (Member)	✓	×	×	✓	×	✓	✓	×
3.	Maryam Adnan Al Ansari (Member)	✓	✓	✓	✓	✓	✓	✓	✓

Board Investment and Credit Committee Meetings and Attendance

No	Name of the Director	17 Jan	22 Feb	22 Mar	17 Apr	25 Apr	15 May	25 Jun	19 Jul	03 Sep	16 Sep	21 Oct	28 Oct	29 Nov	19 Dec
1.	Sabah Khalil Al-Moayyed (Chairperson)	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
2.	Marwan Khalid Tabbara (Member)	✓	✓	✓	✓	✓	✓	✓	×	✓	✓	✓	✓	✓	✓
3.	Tariq Jaleel Al Saffar (Member)	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
4.	Tala Abdulrahman Fakhro (Member)	×	×	✓	✓	✓	✓	✓	✓	×	✓	✓	×	✓	✓

Board Remuneration and Governance Committee Meetings and Attendance

No.	Name of the Director	27 Feb	18 July	24 Dec
1.	Khalid Al Rumaihi (Chairman)	✓	✓	✓
2.	Tala Abdulrahman Fakhro (Member)	✓	✓	✓
3.	Tariq Jaleel Al Saffar	×	✓	✓

Shari'a Board Meetings and Attendance

No.	SSB Member	16 Jan	20 Feb	8 May	12 July	24 Sep
1.	A. Nasser Almahmood	✓	✓	✓	✓	✓
2.	Mohammed Arbouna	✓	✓	✓	✓	✓
3.	Omar Alaani	✓	✓	✓	✓	✓

Remuneration Report

BDB follows a total compensation approach to remuneration for rewarding performance as well as providing competitive fixed remuneration for attracting and retaining talents. It is the Bank's basic compensation philosophy to provide a competitive level of total compensation to attract and retain qualified and competent employees. These elements support the achievement of the objectives through balancing rewards for both short-term results and long-term sustainable performance. The strategy is designed to share the success, of the Bank and to align employees' incentives with the risk framework and risk outcomes.

The quality and long-term commitment of all of the employees is fundamental to the success of the Bank. The Bank, therefore aims to attract, retain and motivate the very best people who are committed to maintaining a career with the Bank, and who perform their role in the long-term interests of its shareholders.

Bank adopted regulations concerning sound remuneration practices issued by the Central Bank of Bahrain. The revised policy framework and incentive components were approved by the shareholders in the Annual General Meeting.

Unlike commercial banks, BDB is a "not-for-profit" development banking institution, with core objective of supporting economic development of Bahrain in line with Bahrain 2030 Vision. Bank's remuneration policy has no variable components as per the contractual obligation and the performance bonus will be paid at the discretion of the Board of Directors. There is no separate policy for business and controlling staff of the Bank. As such, the need to "defer" variable remuneration does not apply in case of BDB. Consequently, there are no "claw-back" or "malus" stipulations as well. The exceptions were approved by the Central Bank of Bahrain.

Details of Remuneration Paid for the Financial Year Ended 2018

Categories	No.	Fixed Remuneration (BD)			Variable Remuneration (BD)	Total Amount (BD)
		Salaries and Wages	Other Benefits/ Allowances	Total	Performance Bonuses (in cash)	
1. Members of the Board	11		69,000	69,000	0	69,000
2. Approved Persons (not incl in 1,3 to 7)	5	331,209	91,530	422,739	84,350	507,089
3. Approved Persons in Risk Management, Internal Audit, Operations, Financial Control, AML, Compliance Functions	5	191,140	88,623	279,763	39,450	319,213
4. Employees Engaged in Risk taking activities (Business Areas)	37	983,756	102,306	1,086,061	88,678	1,174,740
5. Employees other than approved persons engaged in functions under 3	23	277,112	57,243	334,354	48,357	382,711
6. Other Employees	97	1,198,193	247,823	1,446,016	188,750	1,634,767
7. Outsourced Empl./ Service providers (engaged in risk taking activities)						
Total	**178**	**2,981,410**	**656,525**	**3,637,934**	**449,585**	**4,087,520**

The details of remuneration paid to auditors for audit and other assignments are available at the BDB corporate office.

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 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.

Financial Statements 2018

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Corporate Information

Commercial Registration No.	26226 obtained on 20 January 1992
Directors	Mr. Khalid Al Rumaihi – Chairman Ms. Sabah Khalil Al-Moayyed – Board Member Mr. Saleh Hassan Ali Hussain – Board Member Mr. Tariq Jaleel Al Saffar – Board Member Mr. Marwan Khalid Tabbara – Board Member Ms. Tala Abdulrahman Fakhro – Board Member Mr. Ghassan Ghaleb Abdulaal – Board Member Ms. Maryam Adnan Al Ansari – Board Member
Registered Office	Building 170 Road 1703 Diplomatic Area P.O. Box: 20501 Manama Kingdom of Bahrain
External Auditors	Ernst & Young P.O. Box: 140 Manama Kingdom of Bahrain

Independent Auditors’ Report to the Shareholders

Bahrain Development Bank B.S.C(c)
Manama, Kingdom of Bahrain

Report on the Audit of the Consolidated Financial Statements

Opinion

We have audited the accompanying consolidated financial statements of Bahrain Development Bank B.S.C. (c) (the “Bank”) and its subsidiaries (together «the Group»), which comprise the consolidated statement of financial position as at 31 December 2018, and the consolidated statements of profit or loss, other comprehensive income, changes in equity and cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

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

Other Matters

The consolidated financial statements of the Group for the year ended 31 December 2017 were audited by another auditor who expressed an unmodified audit opinion dated 27 February 2018 on those consolidated financial statements.

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 Auditor’s Responsibilities for the Audit of the Consolidated Financial Statements section of our report. We are independent of the Group 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.

Other Information

Other information consists of the information included in the Group’s 2018 Annual Report, other than the consolidated financial statements and our auditor’s report thereon. The Board of Directors is responsible for the other information.

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

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If, based on the work we have performed, 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 Consolidated Financial Statements

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

In preparing the consolidated financial statements, the Board of Directors is responsible for assessing the Group’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 Group or to cease operations, or has no realistic alternative but to do so.

Auditor’s Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor’s 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 consolidated financial statements.

Independent Auditors' Report to the Shareholders (Continued)

Bahrain Development Bank B.S.C(c)
Manama, Kingdom of Bahrain

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 consolidated 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 Group'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 Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated 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 auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated 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 Group to express an opinion on the consolidated 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.

Report on Other Legal and 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 consolidated financial statements are in agreement therewith;

b) the financial information contained in the Report of the Board of Directors is consistent with the consolidated financial statements;

c) we are not aware of any violations of the Bahrain Commercial Companies Law, the Central Bank of Bahrain and Financial Institutions Law, the CBB Rule Book (Volume 1 and applicable provisions of Volume 6) and CBB directives, or the terms of the Bank's memorandum and articles of association during the year ended 31 December 2018 that might have had a material adverse effect on the business of the Bank or on its consolidated financial position; and

d) satisfactory explanations and information have been provided to us by the Board of Directors in response to all our requests.

Ernst + Young

Partner's registration no. 45
24 February 2019
Manama, Kingdom of Bahrain

Consolidated Statement of Financial Position

As at 31 December 2018

	Note	2018 BD '000	2017 BD '000
ASSETS			
Cash and balances with Central Bank of Bahrain	7	**2,218**	2,873
Placement with banks and other financial institutions	7	**21,917**	27,011
Islamic financing and loans to customers	8	**85,866**	114,535
Investment securities	9	**31,144**	15,143
Investment in associates	10	**259**	419
Investment properties	11	**12,000**	12,033
Property and equipment	12	**1,155**	1,216
Other assets	13	**3,646**	2,940
TOTAL ASSETS		**158,205**	176,170
LIABILITIES AND EQUITY			
Liabilities			
Term loans	14	**50,607**	51,674
Deposits	15	**35,001**	46,440
Other liabilities		**5,106**	5,371
Total Liabilities		**90,714**	103,485
Equity			
Share capital	16	**65,000**	65,000
Statutory reserve	17	**1,186**	1,186
Other capital contribution	18	**4,048**	4,048
Other reserves		**(150)**	181
(Accumulated losses) / retained earnings		**(2,580)**	2,280
Equity attributable to owners of the Bank		**67,504**	72,695
Non-controlling interest		**(13)**	(10)
Total Equity		**67,491**	72,685
TOTAL LIABILITIES AND EQUITY		**158,205**	176,170

Khalid Al Rumaihi
Chairman

Saleh Hassan Ali Hussain
Director

The accompanying notes 1 to 39 form part of these consolidated financial statements.

Consolidated Statement of Profit or Loss

As at 31 December 2018

	Note	2018 BD '000	2017 BD '000
Income			
Islamic financing and interest income	19	8,268	9,004
Islamic financing and interest expense	20	(1,870)	(2,303)
Net Islamic Financing and Interest Income		6,398	6,701
Fee and commission income	21	231	407
Investment income	22	379	177
Rental income		2,007	2,005
Other income	23	1,171	526
Total Operating Income		10,186	9,816
Expenses			
Staff costs		(4,324)	(4,626)
Other operating expenses		(3,227)	(4,709)
Total Operating Expenses		(7,551)	(9,335)
Allowance for expected credit losses / provision - net	24	(3,982)	(8,152)
Impairment on investment in associates	10	(92)	-
Total Expected Credit Losses / Impairment		(4,074)	(8,152)
Net Operating Loss		(1,439)	(7,671)
Share of profit from associates	10	113	-
Net Loss for the Year		(1,326)	(7,671)
Net Loss for the Year Attributable to:			
- Owners of the Bank		(1,323)	(7,660)
- Non-controlling interest		(3)	(11)
		(1,326)	(7,671)

Khalid Al Rumaihi
Chairman

Saleh Hassan Ali Hussain
Director

The accompanying notes 1 to 39 form part of these consolidated financial statements.

Consolidated Statement of other Comprehensive Income

For the year ended 31 December 2018

	Note	2018 BD '000	2017 BD '000
Net Loss for the Year		**(1,326)**	(7,671)
Other Comprehensive Income:			
Items that will not be reclassified to profit or loss in subsequent periods:			
Fair value through other comprehensive income reserve (equity instruments)	25	**1**	-
Items that will be reclassified to profit or loss in subsequent periods:			
Changes in fair value of investments classified as fair value through other comprehensive income	25	**(312)**	-
Total Comprehensive Loss for the Year		**(1,637)**	(7,671)
Total Comprehensive Loss Attributable to:			
- Owners of the Bank		**(1,634)**	(7,660)
- Non-controlling interest		**(3)**	(11)
		(1,637)	(7,671)

The accompanying notes 1 to 39 form part of these consolidated financial statements.

Consolidated Statement of Changes in Equity

For the year ended 31 December 2018

	Equity Attributable to Owners of the Bank							
	Share Capital BD '000	Statutory Reserve BD '000	Other Capital Contribution BD '000	Other Reserves BD '000	Retained Earnings / (Accumulated Losses) BD '000	Total BD '000	Non - Controlling Interest BD '000	Total Equity BD '000
As at 31 December 2017	65,000	1,186	4,048	181	2,280	72,695	(10)	72,685
Impact due to recognition of expected credit losses under IFRS 9 (note 6.17.4)	-	-	-	-	(3,557)	(3,557)	-	(3,557)
Impact due to reclassification of investment securities - debt under IFRS 9 (note 6.17.4)	-	-	-	(20)	20	-	-	-
Restated opening balance as at 1 January 2018	65,000	1,186	4,048	161	(1,257)	69,138	(10)	69,128
Total comprehensive loss for the year	-	-	-	(311)	(1,323)	(1,634)	(3)	(1,637)
As at 31 December 2018	65,000	1,186	4,048	(150)	(2,580)	67,504	(13)	67,491

	Equity Attributable to Owners of the Bank							
	Share Capital BD '000	Statutory Reserve BD '000	Other Capital Contribution BD '000	Other Reserves BD '000	Retained Earnings BD '000	Total BD '000	Non - Controlling Interest BD '000	Total Equity BD '000
As at 1 January 2017	65,000	1,186	4,048	181	9,940	80,355	6	80,361
Total comprehensive loss for the year	-	-	-	-	(7,660)	(7,660)	(11)	(7,671)
Movement in non controlling interest	-	-	-	-	-	-	(5)	(5)
As at 31 December 2017	65,000	1,186	4,048	181	2,280	72,695	(10)	72,685

The accompanying notes 1 to 39 form part of these consolidated financial statements.

Consolidated Statement of Cash Flows

For the year ended 31 December 2018

	Note	2018 BD '000	2017 BD '000
OPERATING ACTIVITIES			
Loss for the year		(1,326)	(7,671)
Adjustments for:			
Depreciation		893	919
Allowance for expected credit losses / provision - net	24	3,982	8,152
Impairment on investment in associates	10	92	-
Changes in fair value of investments classified as fair value through profit or loss	22	(84)	(60)
Dividend income	22	(90)	(117)
Share of profit from associates	10	(113)	-
Loss on foreign currency translation		76	51
Operating profit before changes in operating assets and liabilities		3,430	1,274
Changes in operating assets and liabilities:			
Placement with banks and other financial institutions having original maturity of more than 90 days		1,841	2,811
Islamic financing and loans to customers		22,114	16,534
Other assets		(1,630)	(174)
Deposits		(11,439)	(22,776)
Other liabilities		(265)	(235)
Net Cash From / (Used in) Operating Activities		14,051	(2,566)
INVESTING ACTIVITIES			
Purchases for property and equipment	12	(364)	(412)
Purchase of investment securities		(32,065)	(3,068)
Proceeds from sale of investment securities		16,019	2,200
Addition to investment properties *	11	(435)	(250)
Dividend income received	22	90	117
Net Cash Used in Investing Activities		(16,755)	(1,413)
FINANCING ACTIVITIES			
Repayment of term loans	14	(5,780)	(4,476)
Loan drawn down	14	4,713	-
Net Cash Used in Financing Activities		(1,067)	(4,476)
NET DECREASE IN CASH AND CASH EQUIVALENTS		(3,771)	(8,455)
Cash and cash equivalents at beginning of the year		16,524	24,979
CASH AND CASH EQUIVALENTS AT END OF THE YEAR	7	12,753	16,524
Additional Information:			
Islamic financing and interest received		7,840	9,072
Islamic financing and interest paid		1,872	2,375

* The addition to investment properties includes a non-cash item of BD 348 thousand (2017: BD nil).

The accompanying notes 1 to 39 form part of these consolidated financial statements.

Notes to the Consolidated Financial Statements

31 December 2018

1. INCORPORATION AND ACTIVITIES

Bahrain Development Bank B.S.C. (c) ("the Bank" or "BDB") was established as a Bahraini closed shareholding company by Legislative Decree number 19 dated 11 December 1991 and commenced operations on 20 January 1992. The Bank is registered with the Ministry of Industry, Commerce and Tourism (MOICT) under commercial registration (CR) number 26226. The Bank's registered office is in the Kingdom of Bahrain. The Bank is operating as a retail bank with special waivers under a license issued by the Central Bank of Bahrain ("CBB").

The core activities of the Bank consist of advancing loans for project finance, working capital, premises and equipment for developing industries and service sectors such as Tourism, Health and Education in the Kingdom of Bahrain. As part of this activity, the Bank also renders management consultancy services and subscribes to ordinary and preference shares in locally incorporated companies. Additionally, loans are advanced for Agriculture, Fisheries and Higher Education purposes. Other activities of the Bank comprise making a direct contribution towards the economic development of the Kingdom of Bahrain.

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

2. BASIS OF PREPARATION

2.1 Statement of Compliance

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) issued by the International Accounting Standards Board (IASB) and in conformity with the Bahrain Commercial Companies Law and the CBB and Financial Institutions Law, the CBB Rule Book (Volume 1 and applicable provisions of Volume 6) and CBB directives, regulations and associated resolutions, or the terms of the Bank's memorandum and articles of association.

2.2 Accounting Convention

These consolidated financial statements are prepared on a historical cost basis, except for certain investment securities carried at fair value through profit or loss, or through other comprehensive income, that have been measured at fair value.

These consolidated financial statements are prepared in Bahraini Dinars which is the functional and presentation currency of the Bank.

2.3 Basis of Consolidation

These consolidated financial statements incorporate the financial statements of the Bank and its subsidiaries (the "Group"), all of which have 31 December as their year end and are incorporated in the Kingdom of Bahrain. The Bank has the following principal subsidiaries:

	Ownership Interest		
Name	2018	2017	Principal Activity
Bahrain Business Incubator Centre S.P.C.	100%	100%	Development and assistance to emerging Bahraini entrepreneurs
BDB SME Fund Company B.S.C. (c) **	-	99%	Managing SME funds
Bahrain Export Development Center S.P.C.	100%	100%	Management consultancy activities
Al-Waha Venture Capital Fund Company	99%	99%	Trusts, Funds and Similar Financial Entities - Fund Company
Middle East Corner Consultancy Co. W.L.L. (MECC) *	28.60%	28.60%	Consultancy to small and medium enterprises

* The Bank is exposed, or has rights, to variable returns from its involvement with MECC; and has the ability to affect those returns through its power over MECC and thus is deemed as a subsidiary of the Bank.

** BDB SME Fund Company B.S.C. (c) was liquidated during the year.

Subsidiaries are fully consolidated from the date on which control is transferred to the Group. Control is achieved when the Group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Specifically, the Group controls an investee if and only if the Group has:

a) Power over the investee (i.e. existing rights that give it the current ability to direct the relevant activities of the investee);
b) Exposure, or rights, to variable returns from its involvement with the investee; and
c) The ability to use its power over the investee to affect its returns.

2. BASIS OF PREPARATION (Continued)

2.3 Basis of Consolidation (Continued)

When the Group has less than a majority of the voting or similar rights of an investee, the Group considers all relevant facts and circumstances in assessing whether it has power over an investee, including:

a) The contractual arrangement with the other vote holders of the investee;
b) Rights arising from other contractual arrangements; and
c) The Group's voting rights and potential voting rights.

The Group re-assesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control. Consolidation of a subsidiary begins when the Group obtains control over the subsidiary and ceases when the Group loses control of the subsidiary. Assets, liabilities, income and expenses of a subsidiary acquired or disposed of during the year are included in the statement of comprehensive income from the date the Group gains control until the date the Group ceases to control the subsidiary.

Profit or loss and each component of other comprehensive income (OCI) are attributed to the equity holders of the parent of the Group and to the non-controlling interests, even if this results in the non-controlling interests having a deficit balance. When necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with the Group's accounting policies. All intra-group assets and liabilities, equity, income, expenses and cash flows relating to transactions between members of the Group are eliminated in full on consolidation.

A change in the ownership interest of a subsidiary, without a loss of control, is accounted for as an equity transaction. If the Group loses control over a subsidiary, it:

a) Derecognises the assets (including goodwill) and liabilities of the subsidiary;
b) Derecognises the carrying amount of any non-controlling interests;
c) Derecognises the cumulative translation differences recorded in equity;
d) Recognises the fair value of the consideration received;
e) Recognises the fair value of any investment retained;
f) Recognises any surplus or deficit in profit or loss; and
g) Reclassifies the parent's share of components previously recognised in OCI to profit or loss or retained earnings, as appropriate, as would be required if the Group had directly disposed of the related assets or liabilities.

3. SIGNIFICANT ACCOUNTING JUDGMENT AND ESTIMATES

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

Going Concern

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

Fair Value of Financial Instruments

Where the fair values of financial assets and financial liabilities recorded in the consolidated statement of financial position cannot be derived from active markets, these are determined using a variety of valuation techniques that include the use of mathematical models. The inputs to these models are derived from observable market data where possible, but where observable market data is not available, judgment is applied to establish fair values. These judgment include considerations of liquidity and model inputs such as volatility for longer dated derivatives and discount rates, prepayment rates and default rate assumptions for asset backed securities.

Business Model

In making an assessment of whether a business model's objective is to hold assets in order to collect contractual cash flows, the Group considers at which level of its business activities such assessment should be made. Generally, a business model is a matter of fact which can be evidenced by the way business is managed and the information provided to management.

3. SIGNIFICANT ACCOUNTING JUDGMENT AND ESTIMATES (Continued)

In determining whether its business model for managing financial assets is to hold assets in order to collect contractual cash flows, the Group considers:

a) Management's stated policies and objectives for the portfolio and the operation of those policies in practice;
b) Management's evaluation of the performance of the portfolio; and
c) Management's strategy in terms of earning contractual interest revenues or generating capital gains.

Impairment of Financial Instruments

Assessment of whether credit risk on the financial asset has increased significantly since initial recognition and incorporation of forward-looking information in the measurement of ECL. Refer note 4 for further details.

The measurement of the ECL for financial assets measured at amortised cost and FVTOCI is an area that requires the use of complex models and significant assumptions about future economic conditions, credit behavior (e.g. the likelihood of customers defaulting and the resulting losses), estimation of the amount and timing of the future cash flows and collateral values. These estimates are driven by a number of factors, changes in which can result in different levels of allowances.

The Group's ECL calculation are outputs of complex models with a number of underlying assumptions regarding the choice of variable inputs and their interdependencies. A number of significant judgments are also required in applying the accounting requirements for measuring ECL, such as:

a) Determining criteria for significant increase in credit risk;
b) Choosing appropriate models and assumptions for the measurement of ECL;
c) Determination of associations between macroeconomic scenarios and, economic inputs, such as unemployment levels and collateral values, and the effect on PDs, EADs and LGDs;
d) Selection and relative weightings of forward-looking scenarios to derive the economic inputs into the ECL models;
e) Establishing segments of similar financial assets for the purposes of measuring ECL; and
f) Determining relevant period of exposure with respect to the revolving facilities and facilities undergoing restructuring at the time of the reporting date.

4. NEW STANDARDS AND INTERPRETATIONS ISSUED BUT NOT YET EFFECTIVE

The standards and interpretations that are issued, but not yet effective, up to the date of issuance of the Group's consolidated financial statements are disclosed below. The Group intends to adopt these standards, if applicable, when they become effective.

- IFRS 16 Leases (effective 1 January 2019)
- IFRIC Interpretation 23 Uncertainty over Income Tax Treatment (effective 1 January 2019)
- Amendments to IFRS 9 Prepayment features with negative compensation (effective 1 January 2019)

Annual improvements 2015-2017 cycle (issued in December 2017)

- IFRS 3 Business combinations (effective 1 January 2019)
- IAS 12 Income taxes (effective 1 January 2019)
- IAS 23 Borrowing costs (effective 1 January 2019)

The Group does not expect any significant impact on the Groups' financial position and results for the standards that are not yet adopted.

5. NEW STANDARDS AND INTERPRETATIONS ISSUED AND EFFECTIVE

The accounting policies used in the preparation of these consolidated financial statements are consistent with those used in previous year, except for the adoption of the following new standards or amendments to existing standards, applicable to the Group, and which are effective for annual periods beginning on or after 1 January 2018:

- IFRS 9 Financial Instruments
- IFRS 15 Revenue from Contracts with Customers

5. NEW STANDARDS AND INTERPRETATIONS ISSUED AND EFFECTIVE (Continued)

- IFRIC Interpretation 22 Foreign currency transactions and advance considerations
- IFRS 7 (revised) Financial instruments: Disclosures (IFRS 7R)

The above new standards, interpretations and amendments to IFRSs which are effective for annual accounting periods starting from 1 January 2018 did not have any material impact on the accounting policies, financial position or performance of the Group, except for the adoption of IFRS 9 which is detailed in note 6.17 below and the adoption of IFRS 7R that resulted in additional disclosures.

6. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

6.1 Investment in Associates

The Group's investments in its associates are accounted for using the equity method. Under the equity method, the investment in an associate is initially recognised at cost.

The carrying amount of the investment is adjusted to recognize changes in the Group's share of net assets of the associate since the acquisition date. Goodwill relating to the associate is included in the carrying amount of the investment and is neither amortised nor individually tested for impairment.

An associate is an entity over which the Group has significant influence. Significant influence is the power to participate in the financial and operating policy decisions of the investee, but is not control or joint control over those policies.

The statement of profit or loss reflects the Group's share of the results of operations of the associate. Any change in OCI of those investees is presented as part of the Group's OCI. In addition, when there has been a change recognised directly in the equity of the associate, the Group recognises its share of any changes, when applicable, in the statement of changes in equity. Unrealised gains and losses resulting from transactions between the Group and the associate is eliminated to the extent of the interest in the associate.

The aggregate of the Group's share of profit or loss of an associate is charged to the statement of profit or loss outside operating profit and represents profit or loss after tax and non-controlling interests in the subsidiaries of the associate.

The financial statements of the associate or joint venture are prepared for the same reporting period as the Group. When necessary, adjustments are made to bring the accounting policies in line with those of the Group.

After application of the equity method, the Group determines whether it is necessary to recognise an impairment loss on its investment in its associate. At each reporting date, the Group determines whether there is objective evidence that the investment in the associate is impaired. If there is such evidence, the Group calculates the amount of impairment as the difference between the recoverable amount of the associate and its carrying value, then recognises the loss in the consolidated statement of profit or loss.

Upon loss of significant influence over the associate, the Group measures and recognises any retained investment at its fair value. Any difference between the carrying amount of the associate upon loss of significant influence and the fair value of the retained investment and proceeds from disposal is recognised in profit or loss.

6.2 Property and Equipment

All items of property and equipment are initially recorded at cost. Depreciation is provided on a straight-line basis over the estimated useful lives of all premises and equipment, other than freehold land which is deemed to have an indefinite life.

6.2.1 Recognition and Measurement

Items of property and equipment are measured at cost less accumulated depreciation and any accumulated Impairment losses.

If significant parts of an item of property and equipment have different useful lives, then they are accounted for as separate items (major components) of property and equipment.

Any gain or loss on disposal of an item of property and equipment (calculated as the difference between the net proceeds from disposal and the carrying amount of the item) is recognised within other income in consolidated statement of profit or loss.

6.2.2 Subsequent Costs

Subsequent expenditure is capitalised only when it is probable that the future economic benefits of the expenditure will flow to the Group. Ongoing repairs and maintenance are expensed as incurred.

Notes to the Consolidated Financial Statements (Continued)

31 December 2018

6. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

6.2 Property and Equipment (Continued)

6.2.3 Depreciation

Depreciation is calculated to write off the cost of property and equipment less their estimated residual values using the straight-line method over their estimated useful lives, and is generally recognised in consolidated statement of profit or loss. Leased assets are depreciated over the shorter of the lease term and their useful lives unless it is reasonably certain that the Group will obtain ownership by the end of the lease term. Land is not depreciated. The estimated useful lives of significant items of property and equipment are as follows:

Buildings on freehold premises	15 - 30 years
Furniture, fixtures, vehicles, computers and office equipment	3 - 5 years

Depreciation methods, useful lives and residual values are reviewed at each reporting date and adjusted if appropriate.

6.2.4 Reclassification to investment property

When the use of a property changes from owner occupied to investment property, the property is classified to investment property and carried at cost in line with accounting policy as per note 6.3.

6.3 Investment Property

Investment properties are those which are held by the Group to earn rental income or for capital appreciation or both. Investment properties are stated at cost less accumulated depreciation and any impairment losses. Depreciation is calculated on cost by the straight-line method at annual rates which are intended to write off the cost of the investment property over their estimated useful lives. Any gain or loss on disposal of investment property (calculated as the difference between the net process form the disposal and the carrying amount of the item) is recognized in consolidated statement of profit or loss.

6.4 Accounts Receivable

Accounts receivable are stated at original invoice amount net of discounts and provisions for any uncollectible amounts. An estimate for doubtful debts is made when collection of the full amount is no longer probable. Bad debts are written off when there is no possibility of recovery.

6.5 Term Loans

Term loans are initially measured at fair value minus incremental direct transaction costs, and subsequently measured at their amortised cost using the effective interest method.

6.6 Deposits

Deposits are initially measured at fair value minus incremental direct transaction costs, and subsequently measured at their amortised cost using the effective interest method.

6.7 Provisions

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

6.8 Employees' end of Service Benefits

Pension rights (and other social benefits) for Bahraini employees are covered by the General Organisation for Social Insurance scheme to which employees and employers contribute monthly on a fixed-percentage-of salaries basis. The Group's share of contributions to this scheme, which is a defined contribution scheme under IAS 19 - Employees Benefits, is recognised as an expense in the consolidated statement of profit or loss.

Expatriate employees are entitled to leaving indemnities payable under the Bahraini Labour law for the Private Sector 2012, based on length of service and final remuneration. Provision for this which is unfunded, and which represents a defined benefit plan under IAS 19 - Employees Benefits, has been made by calculating the notional liability had all employees left at the reporting date. These charges are recognised as an expense in the consolidated statement of profit or loss.

6. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

6.9 Income Recognition

Interest income and expense are recognised in profit or loss using the effective interest method. The effective interest ratio is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or financial liability (or, where appropriate, a shorter period to the carrying amount of the financial asset or financial liability). When calculating the effective interest rate, the Group estimates future cash flows considering all contractual terms of the financial instrument, but not future credit losses.

The calculation of the effective interest rate includes transaction costs and fees paid or received that are an integral part of the effective interest rate. Transaction costs include incremental costs that are directly attributable to the acquisition of issue or a financial asset or financial liability.

6.10 Dividend Income

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

6.11 Fee and Commission Income

Fee and commission income and related expense that are integral to the effective interest rate on a financial asset or financial liability are included in the measurement of the effective interest rate.

Other fee and commission income including account servicing fees, investment management fees, sales commission, placement fees and syndication fees are recognised as the related services are performed. If a loan commitment is not expected to result in the draw-down of a loan, then the related loan commitment fee is recognised on a straight-line basis over the commitment.

Other fee and commission expense relate mainly to transaction and service fee, which is expensed as the service is received.

6.12 Rental Income

Rental income from investment property is recognised as revenue on a straight line basis over the term of the lease. Lease incentives granted are recognised as an integral part of the total rental income, over the term of the lease.

6.13 Other Capital Contribution

This represents non-reciprocal contribution, has no interest and no repayment terms and will only be repaid on liquidation of the Bank and accordingly, it has been classified as equity.

6.14 Foreign Currencies

Transaction in foreign currencies are translated into the functional currency at the spot exchange rates at the date of the transactions.

Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated into the functional currency at the spot exchange rate at that date. The foreign currency gain or loss on monetary item is the difference between the amortised cost in the functional currency at the beginning of the year, adjusted for effective interest and payments during the year, and the amortised cost in the foreign currency translated at the spot exchange rate at the end of the year.

Non-monetary assets and liabilities that are measured at fair value in a foreign currency are translated into the functional currency at the spot exchange rate at the date on which the fair value is determined. Non-monetary items that are measured based on historical cost in a foreign currency are translated using the spot exchange rate at the date of the transaction.

Foreign currency differences arising on translation are generally recognised in the consolidated statement of profit or loss.

6.15 Cash and Cash Equivalents

Cash and cash equivalents includes notes and coins on hand, unrestricted balances held with Central Bank and highly liquid financial assets with original maturities of three months or less from the date of acquisition that are subject to insignificant risk of changes in their fair value, and are used by the Group in the management of its short-term commitment. Cash and cash equivalents are carried at amortised cost in the statement of financial position.

6.16 Derivatives

In the ordinary course of business, the Bank enters into transactions that involve derivative financial instruments. A derivative financial instrument is a financial contract between two parties where payment is dependent upon movements in price in one or more underlying financial instrument, reference rate or index. Derivative financial instruments include forward exchange contracts.

Forwards are contractual agreements to either buy or sell a specified currency, commodity or financial instrument at a specific price and date in the future. Forwards are customised contracts transacted in the over-the-counter market.

6. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

6.17 Financial Assets and Financial Liabilities

Based on the adoption of IFRS 9, effective 1 January 2018, the following accounting policies are applicable replacing / amending or adding to the corresponding accounting policies set out in the annual audited consolidated financial statements for the year ended 31 December 2017.

The Bank has adopted International Financial Reporting Standard IFRS 9 - Financial Instruments (IFRS 9) issued by the International Accounting Standards Board (IASB) with a date of initial application of 1 January 2018. The requirements of IFRS 9 represent a significant change in accounting for impairment and credit losses. The key changes to the Bank's accounting policies resulting from its adoption of IFRS 9 are summarised below:

6.17.1 Impairment of Financial Assets

IFRS 9 replaces the 'incurred loss' model with an 'expected credit loss' model (“ECL”). The new impairment model also applies to certain loan commitments and financial guarantees. The allowance is based on the ECLs associated with the probability of default in the next twelve months unless there has been a significant increase in credit risk since origination, in which case, the allowance is based on the change in the ECLs over the life of the asset. Under IFRS 9, credit losses are recognized earlier than under the previous standard.

6.17.2 Transition

Changes in accounting policies resulting from the adoption of IFRS 9 have been applied retrospectively, except that the comparative information has not been restated. The difference in the carrying amounts of financial assets resulting from the adoption of IFRS 9 are recognized in retained earnings as at 1 January 2018. Accordingly, the information presented for 2017 is not comparable to the information presented for 2018 under IFRS 9.

6.17.3 Reconciliation of carrying amounts as at 31 December 2017 and 1 January 2018

The following table reconciles the carrying amounts as of 31 December 2017 to the carrying amounts determined by applying IFRS 9 on 1 January 2018:

	Carrying amounts as at 31 December 2017	Allowance for expected credit losses	Carrying amounts as at 1 January 2018
	BD '000	BD '000	BD '000
Financial Instruments at Amortised Cost			
Placement with banks and other financial institutions	27,011	(77)	26,934
Islamic financing and loans to customers	114,535	(3,226)	111,309
Other assets	514	-	514
Other liabilities (against off-balance sheet exposures)	5,371	(254)	5,625
	147,431	**(3,557)**	**144,382**

6.17.4 Impact on Other Reserves and Retained Earnings

	Other reserves BD '000	Retained earnings BD '000	Total BD '000
As at 31 December 2017	181	2,280	2,461
Recognition of expected credit losses under IFRS 9	-	(3,557)	(3,557)
Reclassification of investment securities - debt under IFRS 9	(20)	20	-
Restated Opening Balance as at 1 January 2018	**161**	**(1,257)**	**(1,096)**

6. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

6.17 Financial Assets and Financial Liabilities (Continued)

6.17.5 Reconciliation of provision recorded as at 31 December 2017 and 1 January 2018

The following table reconciles the previously recorded provision as at 31 December 2017 to the revised provision as of 1 January 2018 on transition to IFRS 9:

	As at 31 December 2017	Transition adjustment	As at 1 January 2018
	BD '000	BD '000	BD '000
Placement with banks and other financial institutions	-	77	77
Islamic financing and loans to customers	19,036	3,226	22,262
Other assets	1,392	-	1,392
Off-balance sheet exposures	-	254	254
	20,428	**3,557**	**23,985**

6.17.6 Classification and Measurement

IFRS 9 contains a new classification and measurement approach for financial assets that reflects the business model in which financial assets are managed and the underlying cash flow characteristics. Based on the Group's assessment, the Group had debt securities classified as fair value through profit or loss with a fair value of BD 6,012 thousand as of 31 December 2017. Under IFRS 9, the Group has designated these investments as measured at fair value through OCI. Due to this reclassification, an increase of BD 20 thousand in the statement of changes in equity along with a corresponding decrease in the fair value reserve (other reserves) due to reclassification of the fair value loss was made in the Group's statement of changes in equity. The Group adopted transitional classification and measurement under IFRS 9 on annual periods beginning on or after 1 January 2015.

6.17.7 Expected Credit Loss

The Bank recognises ECL on the following financial assets that are not measured at fair value through profit or loss:

a) Debt investments;
b) Placements with banks and other financial institutions;
c) Islamic financing and loans to customers;
d) Letters of credit and bank guarantees; and
e) Irrevocable undrawn commitments.

The Bank measures loss allowances at an amount equal to lifetime ECL, except for the other financial assets on which credit risk has not increased significantly since their initial recognition, for which ECL is measured as 12-month ECL. 12-month ECL are the portion of ECL that result from default events on a financial asset that is possible within the 12 months after the reporting date.

6.17.8 Measurement of ECL

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

Type of Financial Instrument	Measurement Basis
a) Financial assets that are not credit-impaired at the reporting date	As the present value of all cash shortfalls (i.e. the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Bank expects to receive).
b) Financial assets that are credit-impaired at the reporting date	As the difference between the gross carrying amount and the present value of estimated future cash flows.
c) Irrevocable undrawn commitments	As the present value of the difference between the contractual cash flows that are due to the Bank if the commitment is drawn down and the cash flows that the Bank expects to receive.
d) Letters of credit and bank guarantees	As the expected payments to reimburse the holder less any amounts that the Bank expects to recover.

The Bank measures an ECL at an individual instrument level taking into account the projected cash flows, Probability of Default (PD), Loss Given Default (LGD), Credit Conversation Factor (CCF) and discount rate.

6. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

6.17 Financial Assets and Financial Liabilities (Continued)

6.17.8 Measurement of ECL (Continued)

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

a) Probability of Default (PD);
b) Loss Given Default (LGD); and
c) Exposure At Default (EAD).

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

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

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

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

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

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

For facilities that include both a drawn and an undrawn commitment component, the Bank measures ECL over a period longer than the maximum contractual period if the Bank's contractual ability to demand repayment and cancel the undrawn commitment does not limit the Bank's exposure to credit losses to the contractual notice period. These facilities do not have a fixed term or repayment structure and are managed on a collective basis. The Bank can cancel them with immediate effect but this contractual right is not enforced in the normal day-to-day management but only when the Bank becomes aware of an increase in credit risk at the facility level. This longer period is estimated taking into account the credit risk management actions that the Bank expects to take and that serve to mitigate ECL. These include a reduction in limits, cancellation of the facility and / or turning the outstanding balance into a loan with fixed repayment terms.

6.17.9 Restructured Financial Assets

Where possible, the Group seeks to restructure loans rather than to take possession of collateral. This may involve extending the payment arrangements and the agreement of new loan conditions. Once the terms have been renegotiated, any impairment is measured using the original effective interest rate as calculated before the modification of terms and the loan is no longer considered past due. Management continuously reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur.

In project finance, there could be delays in implementation of the project and in some cases, the projects may take a longer time to generate surplus. The Bank has in such cases, where there is a genuine need and commitment from the customer, approves a restructuring.

Maximum tenor of the facility post restructuring does not exceed 15 years from the first disbursement of the facility. As has been prescribed by the CBB, restructured accounts are transferred to Stage 2 directly for a minimum period of 12 months.

6. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

6.17 Financial Assets and Financial Liabilities (Continued)

6.17.10 Credit-Impaired Financial Assets

At each reporting date, the Bank assesses whether financial assets carried at amortised cost are credit-impaired. A financial asset is 'credit-impaired' when one or more events that have a detrimental impact on the estimated future cash flows of the financial asset have occurred.

6.17.11 Presentation of Allowance for ECL in the Statement of Financial Position

Allowances for ECL are presented in the statement of financial position as follows:

a) financial assets measured at amortised cost: as a deduction from the gross carrying amount of the assets; and

b) where a financial instrument includes both a drawn and an undrawn component (as in the case of overdraft, letter of credit / bank guarantee limits etc.), the Bank presents a loss allowance for the approved limit of the facility in 'other liabilities'.

6.17.12 Write-offs

The Bank’s accounting policy for write-offs under IFRS 9 remains the same. Financial assets are written off either partially or in their entirety only when the Bank has thoroughly explored most avenues of recovery and it is recognized thereafter that the outstanding amount of the debt is clearly not recoverable. However, in all written-off cases, the Bank's efforts towards the recovery of the outstanding amount continues and periodic updates are provided to the Board of Directors. If the amount to be written off is greater than the accumulated loss allowance, the difference is first treated as an addition to the allowance that is then applied against the gross carrying amount. Any subsequent recoveries are credited to 'other income'.

6.18 Financial Risk Management

The Group’s financial risk management objectives and policies are consistent with those disclosed in the audited consolidated financial statements for the year ended 31 December 2017 except for changes applied in the adoption of IFRS 9 as explained in the notes below.

The Group's activities expose it to a variety of financial risks and those activities involve the analysis, evaluation, acceptance and management of some degree of risk or combination of risks. Taking risk is core to the banking business, and these risks are an inevitable consequence of participating in financial markets. The Group's aim is therefore to achieve an appropriate balance between risk and return and minimize potential adverse effects on the Bank’s financial performance.

The Group's risk management policies, procedures and systems are designed to identify and analyze these risks and to set appropriate risk mitigants and controls. The Bank reviews its risk management policies and systems on an ongoing basis to reflect changes in markets, products and emerging best practices.

Risk management is performed by the Risk Management Department under policies approved by the Board of Directors. The Risk Management Department identifies and evaluates financial risks in close co-operation with the Bank's operating units. The most important types of risks identified by the Bank are credit risk, liquidity risk and market risk. Market risk includes currency risk, profit rate risk, and price risk.

6.18.1 Credit Risk

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

6.18.2 Significant Increase In Credit Risk (SICR)

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

Using its expert credit judgment and, where possible, relevant historical experience, the Bank may determine that an exposure has undergone a significant increase in credit risk based on particular qualitative indicators that it considers are indicative of such an increase and whose effect may not otherwise be fully reflected in its quantitative analysis on a timely basis. The Bank monitors the effectiveness of the criterion used to identify SICR by regular reviews and validations.

6. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

6.18 Financial Risk Management (Continued)

6.18.2 Significant Increase In Credit Risk (SICR) (Continued)

The Bank classifies its financial instruments into Stage 1, Stage 2 and Stage 3, based on the applied methodology, as described below:

Stage 1: for financial instruments where there has not been a SICR since initial recognition and that are not credit-impaired on origination, the Bank recognises an allowance based on the 12-month ECL. All accounts at origination are classified as Stage 1.

Stage 2: for financial instruments where there has been a SICR since initial recognition but are not credit-impaired, the Bank recognises an allowance for the lifetime ECL for all financings and loans categorised in this stage based on the actual / expected maturity profile including restructuring or rescheduling of facilities.

Stage 3: for credit-impaired financial instruments, the Bank recognises the lifetime ECL. A customer is classified under Stage 3 based on a default identification process i.e. Days Past Due (DPD) of 90 days or more.

6.18.3 Generating the Term Structure of PD

The Bank collects performance and default information about its credit risk exposures analyzed by type of product and borrower as well as by credit risk grading.

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

This analysis includes the identification and calibration of relationships between changes in default rates and macro-economic factors as well as in-depth analysis of the impact of certain other factors (e.g. forbearance experience) on the risk of default. For most exposures, key macro-economic indicators include: gross domestic product / economic growth, interest rates, unemployment rates and inflation.

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

For the financing portfolio, through the yearly review of the corporate portfolio, the Bank observes yearly performances to compute a count based PD over the one year horizon for the past 5 years.

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

6.18.4 Definition of 'Default' and 'Cure'

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

a) significant financial difficulty of the issuer or the obligor;
b) material breach of facility covenants, conditions and contract (subject to management discretion);
c) grant to the borrower a concession that the lender would not otherwise consider except for economic or legal reasons relating to the borrower's financial difficulty;
d) imminent bankruptcy or other financial reorganization of the borrower;
e) significant downgrading in credit rating by an external credit rating agency;
f) disappearance of an active market because of financial difficulties;
g) presence of past due contractual payments of either principal or profit; or / and

6. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

6.18 Financial Risk Management (Continued)

6.18.4 Definition of 'Default' and 'Cure' (Continued)

h) deterioration in the value of security and likelihood of successfully realising it.

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

A financial instrument is considered as 'cured' and therefore re-classified out of Stage 3 when none of the default criteria have been present for at least twelve consecutive months. The decision whether to classify an asset as Stage 2 or Stage 1 once cured depends on the updated credit review, at the time of the cure, and whether this indicates there has been a significant increase in credit risk compared to initial recognition.

6.18.5 Incorporation of Forward Looking Assumptions

The Bank incorporates forward-looking assumptions into both its assessment of whether the credit risk of an instrument has increased significantly since its initial recognition and its measurement of ECL. The Bank annually sources macro-economic forecast data for various variables from many databases including the International Monetary Fund (IMF) database for Bahrain, Bloomberg, Reuters and World Bank.

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

7. CASH AND CASH EQUIVALENTS

	2018 BD '000	2017 BD '000
Cash and balances with Central Bank of Bahrain	**2,218**	2,873
Placement with banks and other financial institutions	**21,917**	27,011
	24,135	29,884
Less: reserve with Central Bank of Bahrain	**(1,530)**	(1,553)
Less: placements with banks and other financial institutions having original maturity of more than 90 days	**(9,913)**	(11,807)
Add: allowance for expected credit losses	**61**	-
Cash and cash equivalents at end of the year	**12,753**	16,524

8. ISLAMIC FINANCING AND LOANS TO CUSTOMERS

	2018 BD '000	2017 BD '000
Project finance - Islamic	**89,689**	114,841
Project finance - conventional	**15,360**	11,268
Fisheries and agriculture	**4,228**	4,596
Ijara receivable	**-**	534
Other loans	**1,159**	2,332
	110,436	133,571
Less: allowance for expected credit losses / provision *	**(24,570)**	(19,036)
	85,866	114,535

* This includes credit losses of BD 15,573 thousand (31 December 2017: BD 9,775 thousand) against Islamic financing to customers.

8. ISLAMIC FINANCING AND LOANS TO CUSTOMERS (Continued)

Below is the movement for expected credit losses on Islamic financing and loans to customers:

	2018				2017
	Stage 1 12-months ECL BD '000	Stage 2 Life time ECL not credit impaired BD '000	Stage 3 Lifetime ECL credit-impaired BD '000	Total BD '000	Total BD '000
Balance as at 1 January	754	186	18,096	19,036	14,995
Transition adjustment	112	996	2,118	3,226	-
Opening Balance as at 1 January (Restated)	866	1,182	20,214	22,262	14,995
Changed Due to Financial Assets Recognised in Opening Balances that have:					
- transferred to 12-month ECL	323	(87)	(236)	-	-
- transferred to Stage 2 (lifetime ECL not credit-impaired)	(38)	329	(291)	-	-
- transferred to Stage 3 (lifetime ECL credit-impaired)	(59)	(528)	587	-	-
Net re-measurement of loss allowance	147	521	3,976	4,644	10,628
Recoveries / write-backs	(495)	(416)	(523)	(1,434)	(2,476)
Allowance for expected credit losses - net	(122)	(181)	3,513	3,210	8,152
Write offs during the year	(2)	(3)	(897)	(902)	(4,111)
Balance at 31 December	742	998	22,830	24,570	19,036

At 31 December 2018, interest in suspense on past due loans that are fully impaired amounted to BD2,109 thousand (31 December 2017: BD 1,852 thousand) that are treated as a memorandum account.

The fair value of the collateral consisting of cash, securities and real estate that the Group holds relating to loans individually determined to be impaired at 31 December 2018 amounts to BD 9,011 thousand (31 December 2017: BD 9,695 thousand).

The contractual amount outstanding on financing assets written off by the Group as at 31 December 2018 and that are still subject to enforcement activity was BD 4,500 thousand (31 December 2017: BD 5,000 thousand).

9. INVESTMENT SECURITIES

	2018 BD '000	2017 BD '000
At Fair Value Through Profit or Loss:		
Conventional equities	4,612	5,375
Islamic equities	676	729
Sukuk	-	6,012
	5,288	12,116
At Fair Value Through other Comprehensive Income:		
Conventional equities	184	133
Conventional debt securities*	6,504	-
Sukuk*	6,093	-
	12,781	133
At Amortised Cost:		
Conventional debt securities*	13,075	2,894
	31,144	15,143

* These exposures to the home country sovereign i.e. Kingdom of Bahrain are considered to be low risk and fully recoverable and hence, no ECL is measured.

Notes to the Consolidated Financial Statements (Continued)

31 December 2018

10. INVESTMENT IN ASSOCIATES

The Group has a 20% (2017: 20%) equity interest in Arabian Taxi Company ("ATC"), incorporated in the Kingdom of Bahrain, which is engaged in operating and managing taxi services.

The Group has a 21.13% (2017: 21.13%) equity interest in EBDA Bank ("EBDB"), incorporated in the Kingdom of Bahrain, which is engaged in Providing microfinance and related advisory services.

Associates are accounted for using the equity method in these consolidated financial statements.

	2018 BD '000	2017 BD '000
Carrying Amount of Investment in Associated Companies		
At 1 January	419	419
Share of profit from associates	113	-
Changes in statement of changes in equity	(181)	-
Impairment on investment in associates	(92)	-
At 31 December	259	419

11. INVESTMENT PROPERTIES

	2018 BD '000	2017 BD '000
At 1 January	12,033	12,264
Additions during the year	-	250
Transfer from property and equipment (note 12)	435	-
Depreciation charge for the year	(468)	(481)
At 31 December	12,000	12,033

As of 31 December 2018, investment properties include 4 buildings (2017: 3 buildings) with a fair value of BD 17,498 thousand (2017: BD 14,121 thousand) as determined by the management (2017: external independent property valuer, having appropriate recognised professional qualifications and experience in the location and category of the property being valued).

The fair value measurement of the investment properties has been categorized as a Level 3 fair value based on the inputs to the valuation technique used. The discounted cash flows model considers the present value of net cash flows to be generated from the property, taking into account the expected rental growth rate, void periods, occupancy rate, lease incentive costs such as rent-free periods and other costs not paid by tenants. The expected net cash flows are discounted using risk-adjusted discounted rates. Among other factors, the discount rate estimation considers quality of a building and its location, tenant credit quality and lease terms.

12. PROPERTY AND EQUIPMENT

	Freehold land BD '000	Freehold premises BD '000	Furniture, fixtures, vehicles and office equipment BD '000	Total BD '000
Net Book Values:				
At 31 December 2018	**293**	**362**	**500**	**1,155**
At 31 December 2017	293	417	506	1,216

13. OTHER ASSETS

	2018 BD '000	2017 BD '000
Rent and other account receivables - net	**1,450**	831
Receivable from Ministry of Municipalities	**1,159**	1,159
Interest receivable	**566**	138
Receivable from Ministry of Finance	**222**	215
Prepayments and other assets	**249**	597
	3,646	2,940

As at 31 December 2018, the ECL on other assets is BD 1,942 thousand (31 December 2017: BD 1,229 thousand).

14. TERM LOANS

	2018 BD '000	2017 BD '000
Kuwait Fund for Arab Economic Development	**1,327**	2,608
Saudi Fund for Development	**8,526**	9,029
Arab Fund for Economic and Social Development	**40,754**	40,037
	50,607	51,674

The movement of the term loans during the year is as follows:

	2018 BD '000	2017 BD '000
At 1 January 2018	**51,674**	56,150
Loan drawn down	**4,713**	-
Repayment of loans	**(5,780)**	(4,476)
At 31 December 2018	**50,607**	51,674

14. TERM LOANS (Continued)

Kuwait Fund for Arab Economic Development

The Bank had obtained a loan from Kuwait Fund for Arab Economic Development (KFAED) in 1998. The entire facility has been drawn down and is repayable in thirty equal half yearly instalments, which commenced from 15 May 2005. This bears an interest and management fees of 1.5% and 0.5% (2017: 1.5% and 0.5%) respectively. The Ministry of Finance is a guarantor to the loan.

The loan proceeds were utilised by the Bank to advance loans to customers. One of the covenants of KFAED's loan agreement requires the Bank to repay KFAED any margin earned in excess of a spread of 4% ("interest differentials") on such loans to customers. The interest differentials are deposited into KFAED's bank account maintained by the Bank in a fiduciary capacity. The balance at year end was BD 2 thousand (2017: same). This account can be used only for development activities such as training, feasibility studies and technical assistance to borrowers agreed by both the parties. During 2018, no amount was utilised for such purposes (2017: same).

Saudi Fund for Development

During 2012, the Bank obtained a loan of SAR 100 million from Saudi Fund for Development. The facility has been fully availed and is repayable semi-annually in 25 years (5 years grace period for principal) at an interest rate of 2.0%. The Ministry of Finance is a guarantor to the loan.

Arab Fund for Economic and Social Development

During 2013, the Bank had obtained a loan of USD 30 million from Arab Fund for Economic and Social Development (AFESD). The facility has been fully availed and is repayable semi-annually in 10 years (3 years grace period for principal) at an interest rate of 3.0%. During 2014, the Bank had obtained a second loan of USD 50 million from AFESD. The facility has been fully availed and is repayable semi-annually in 10 years (3 years grace period for principal) at an interest rate of 3.0%.

During 2016, the Bank had obtained a third loan of USD 50 million from AFESD. The facility has been fully availed and is repayable semi-annually in 10 years (3 years grace period for principal) at an interest rate of 3.0%.

15. DEPOSITS

	2018 BD '000	2017 BD '000
Deposits from banks (note a)	-	11,356
Deposits from customers (note b)	**35,001**	35,084
	35,001	46,440

Note a: Deposits from banks include BD nil (31 December 2017: BD 3,701 thousand) from Islamic banks placed with BDB on a Wakala basis.

Note b: Deposits with customers include BD 1,250 thousand (31 December 2017: BD 1,729 thousand) kept as margin deposits against financings provided.

16. SHARE CAPITAL

	2018 BD '000	2017 BD '000
Authorized:		
100 million (2017: 100 million) shares of BD 1 each	**100,000**	100,000
Issued and fully paid-up:		
65 million (2017: 65 million) shares of BD 1 each	**65,000**	65,000

17. STATUTORY RESERVE

In accordance with the provisions of the Bahrain Commercial Companies Law and the Bank's articles of association, an amount equivalent to 10% of the net profit for the year is transferred to the statutory reserve. The Bank may resolve to discontinue such annual transfers when the reserve totals 50% of the paid up share capital. This reserve is not distributable, but can be utilised for the purposes of a distribution in such circumstances as stipulated in the Bahrain Commercial Companies Law and following the approval of the CBB. No such transfers have been made during the year ended 31 December 2018 and 2017, as the Bank made net loss for both the years.

Notes to the Consolidated Financial Statements (Continued)

31 December 2018

18. OTHER CAPITAL CONTRIBUTION

Other capital contribution mainly includes a contribution by a majority shareholder for a non-monetary asset in the form of a commercial property to the Bank. The property has been classified as an investment property (refer note 11) that was recognised at its fair value on the date of transfer and as a capital contribution in the statement of changes in equity of BD 3,623 thousand.

19. ISLAMIC FINANCING AND INTEREST INCOME

	2018 BD '000	2017 BD '000
Profit on Islamic financing	6,267	7,392
Interest on conventional loans	631	672
Profit and interest on securities	873	322
Profit and interest on placements	497	618
	8,268	9,004

20. ISLAMIC FINANCING AND INTEREST EXPENSE

	2018 BD '000	2017 BD '000
Interest on term loans	1,422	1,502
Interest on deposits from customers	388	708
Profit on deposits from Islamic banks	34	81
Interest on deposits from conventional banks	26	12
	1,870	2,303

21. FEE AND COMMISSION INCOME

	2018 BD '000	2017 BD '000
On Islamic financing and loans to customers	212	267
On contingent liabilities	19	140
	231	407

22. INVESTMENT INCOME

	2018 BD '000	2017 BD '000
Gain on sale of FVTPL investments*	205	-
Changes in fair value of investments classified as FVTPL	84	60
Dividend income	90	117
	379	177

* During the year, the Bank sold one of its conventional equity investments at a sales price of BD 1,390 thousand. The carrying value of such investment at the time of sale was BD 1,185 thousand. The sale proceeds are deposited in an escrow account maintained with a local bank.

23. OTHER INCOME

This mainly includes recovery of written-off non-performing loans amounting to BD 955 thousand (2017: BD 14 thousand).

Notes to the Consolidated Financial Statements (Continued)

31 December 2018

24. ALLOWANCE FOR EXPECTED CREDIT LOSSES / PROVISION - NET

	2018 BD '000	2017 BD '000
Placement with banks and other financial institutions	(16)	-
Islamic financing and loans to customers	3,210	8,152
Other assets	925	-
Off-balance sheet exposures	(137)	-
	3,982	8,152

25. TOTAL COMPREHENSIVE LOSS

	2018 BD '000	2017 BD '000
Net Loss for the Year	(1,326)	(7,671)
Other Comprehensive Income:		
Items that will not be reclassified to profit or loss in subsequent periods:		
Fair value through other comprehensive income reserve (equity instruments)	1	-
Items that will be reclassified to profit or loss in subsequent periods:		
Fair value through other comprehensive income reserve (debt securities and Sukuk)	(131)	-
Investment in associates	(181)	-
Total Comprehensive Loss for the Year	(1,637)	(7,671)

26. CONTINGENT LIABILITIES AND COMMITMENTS

The Bank issues letters of credit and guarantees to its existing customers. These instruments commit the Bank to make payments on behalf of customers in the event of a specific act, generally related to the import of goods.

Irrevocable commitments to extend credit are the Islamic financing and loans, which have been approved by the Bank but have not been disbursed as of the reporting date.

Details of contingent liabilities and commitments are given below:

	2018 BD '000	2017 BD '000
Contingent Liabilities:		
Letters of credit *	34	191
Letters of guarantee *	1,439	3,487
	1,473	3,678
Commitments:		
Irrevocable commitments to extend credit *	1,323	6,223
Commitment to invest in equity **	3,485	3,770
Lease rental commitments	363	435
	5,171	10,428
	6,644	14,106

* The Bank carries an allowance of ECL of BD 117 thousand (31 December 2017: nil) against these off-balance sheet items (refer note 30).

** This represents the Bank's commitment to invest a 10% equity portion in Al-Waha Venture Capital Fund established with a total value of USD 100 million (equivalent BD 37.7 million). During the year, the Bank paid BD 285 thousand (2017: nil) toward this commitment.

26. CONTINGENT LIABILITIES AND COMMITMENTS (Continued)

Lease rental commitments include lease rental payable on the land leased from Ministry of Industry, Commerce and Tourism, which is as follows:

	2018 BD '000	2017 BD '000
Future Minimum Lease Payments:		
Within one year	72	79
Later than 1 year but not later than 5 years	272	238
Later than 5 years	19	118
	363	435

27. FAIR VALUES OF FINANCIAL INSTRUMENTS

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. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- In the principal market for the asset or liability, or
- In the absence of a principal market, in the most advantageous market for the asset or liability, the principal or the most advantageous market must be accessible to by the Group.

Underlying the definition of fair value is a presumption that an enterprise is a going concern without any intention or need to liquidate, curtail materially the scale of its operations or undertake a transaction on adverse terms.

The Group 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 instruments where the valuation technique includes inputs not based on market observable data.

The fair values of financial assets and financial liabilities carried at amortised cost approximate the carrying values as at the reporting dates.

Term loans obtained by the Bank are from Development Funds in Kuwait and the Kingdom of Saudi Arabia. There is no secondary market for such loans which are at lower than market rates due to the nature of these loans. The Bank has estimated that its financing rates and terms are comparable to that of the objectives of other similar development banks in the region and accordingly believes the carrying value of term loans obtained are a close approximation of their fair values.

The fair value of deposits approximates the carrying value as at the reporting date given their short term nature.

There is no change in the valuation techniques used for valuation of investments during the period as compared to the year ended 31 December 2017.

The valuation technique for Level 2 financial assets is arrived on the basis of the market multiples approach and discounted cash flows. The key inputs used include a range of weighted average cost of capital used for discounting cash flows, discount for lack of marketability, control premium etc.

Notes to the Consolidated Financial Statements (Continued)

31 December 2018

27. FAIR VALUES OF FINANCIAL INSTRUMENTS (Continued)

The table below analyses financial instruments, measured at fair value as at both reporting dates, in the fair value hierarchy into which the fair value measurement is categorised:

Financial Assets Measured at Fair Value:	Level 1 BD '000	Level 2 BD '000	Level 3 BD '000	Total fair value BD '000	Total carrying value BD '000
31 December 2018					
Investment securities - equity	**96**	**580**	**4,796**	**5,472**	**5,472**
Investment securities - debt	**12,597**	**-**	**-**	**12,597**	**12,597**
Forward contracts	**-**	**35,114**	**-**	**35,114**	**35,114**
31 December 2017					
Investment securities - equity	153	576	5,508	6,237	6,237
Investment securities - debt	6,012	-	-	6,012	6,012
Forward contracts	-	34,284	-	34,284	34,284

Financial Instruments not Measured at Fair Value:	Level 2 BD '000	Level 3 BD '000	Total fair value BD '000	Total carrying value BD '000
31 December 2018				
Cash and balances with Central Bank of Bahrain	**2,218**	**-**	**2,218**	**2,218**
Placement with banks and other financial institutions	**21,917**	**-**	**21,917**	**21,917**
Islamic financing and loans to customers	**-**	**85,866**	**85,866**	**85,866**
Debt securities	**13,075**	**-**	**13,075**	**13,075**
Term loans	**-**	**50,607**	**50,607**	**50,607**
Deposits	**35,001**	**-**	**35,001**	**35,001**
31 December 2017				
Cash and balances with Central Bank of Bahrain	2,873	-	2,873	2,873
Placement with banks and other financial institutions	27,011	-	27,011	27,011
Islamic financing and loans to customers	-	114,535	114,535	114,535
Debt securities	2,894	-	2,894	2,894
Term loans	-	51,674	51,674	51,674
Deposits	46,440	-	46,440	46,440

The bank uses various valuation techniques such as discounted cash flows, market multiples and adjusted net assets value to arrive at the fair value of Level 3 financial assets. The key inputs used are discount rate and growth rate, price earning multiple and net assets value. The reasonable potential shift in any of the above mentioned inputs will not have any significant effect on the consolidated statement of profit and loss.

Below is the reconciliation of Level 3 financial assets carried at fair value:

	2018 BD '000	2017 BD '000
At beginning of the year	**5,508**	5,222
Changes in fair value recognised in the statement of profit or loss	**137**	152
Additions during the year	**336**	134
Sales made during the year	**(1,185)**	-
At end of the year	**4,796**	5,508

28. RELATED PARTY TRANSACTIONS

The Group enters into transactions with related parties which comprise major shareholders, associates, directors, senior management and entities controlled jointly or significantly influenced by such related parties in the ordinary course of business at agreed rates. Amounts due from related parties are unsecured.

The year end balances in respect of related parties included in the consolidated statement of financial position are as follows:

	Directors and key Management Personnel BD '000	Shareholders and Related Companies BD '000	Total BD '000
31 December 2018			
Islamic financing and loans to customers	295	12	307
Investment in associates	-	283	283
Other assets	-	222	222
Deposits	152	7,638	7,790

	Directors and key management personnel BD '000	Shareholders and related companies BD '000	Total BD '000
31 December 2017			
Islamic financing and loans to customers	239	79	318
Investment in associates	-	419	419
Other assets	-	215	215
Deposits	24	7,577	7,601

The transactions with related parties included in the consolidated statement of profit or loss are as follows:

	Directors and key management personnel BD '000	Shareholders and related companies BD '000	Total BD '000
2018			
Islamic financing and interest income	10	11	21
Islamic financing and interest expense	-	55	55
Share of profit for associates	-	113	113
Other expenses	-	27	27

	Directors and key management personnel BD '000	Shareholders and related companies BD '000	Total BD '000
2017			
Islamic financing and interest income	16	5	21
Islamic financing and interest expense	-	58	58
Other expenses	5	108	113

28. RELATED PARTY TRANSACTIONS (Continued)

Compensation of key management personnel is as follows:

	2018 BD '000	2017 BD '000
Board remuneration	80	80
Salary and short-term employee benefits	779	887
Termination benefits	148	113
	1,007	1,080

29. RISK MANAGEMENT

Risk is inherent in the Bank's activities but is managed through a process of ongoing identification, measurement and monitoring, subject to risk limits and other controls. In the course of its regular business, the Bank gets exposed to multiple risks notably credit risk, liquidity risk, market risk, operational risk and other risks like compliance risk, strategic risks and reputational risks. A well-established risk governance and ownership structure ensures oversight and accountability of the effective management of risk at the Bank. The Bank's risk governance is manifested in a set of established policies, procedures and controls through which the existing organizational structure meets its strategic targets. This philosophy revolves around the knowledge of various risks and their willingness to accept the same commensurating with their risk appetite and strategic plan approved by the Board of Directors.

a) Organizational Structure

A cohesive organizational structure is established within the Bank in order to identify, assess, monitor, and mitigate risks.

b) Board of Directors

The Board of Directors ("BOD") is responsible for the overall direction, supervision and control of the Bank. Oversight of the day-to-day management of the Bank is conducted by the BOD committees, the Chairman and the Chief Executive Officer ("CEO"). The BOD has overall responsibility for the Bank including approving and overseeing the implementation of its strategic objectives, risk strategy, corporate governance and corporate values within the agreed framework in accordance with relevant statutory and regulatory structures. The BOD currently comprises eight members.

c) Audit Committee of the Board

The Audit Committee ("AC") comprises three members of the Board and the Head of Internal Audit is the AC's Secretary. This AC is principally responsible for reviewing the internal audit program and assist the Board in carrying out its duties regarding the integrity of the Bank's financial reporting system, adequacy of the Bank's internal control and risk management processes, to oversee the external and internal audit functions, and the Bank's compliance with legal and regulatory requirements.

d) Remuneration & Governance Committee of the Board

The Remuneration & Governance Committee ("RGC") comprises three members of the BOD (including the Chairman) and the Head of Human Resources & Corporate Communications is the committee's Secretary. RGC has the overall responsibility of setting the criteria and processes for identification of candidates for the Board level committees and senior management. The Committee also assists the Board of Directors in establishing a fair and transparent process for the remuneration of directors, other Board Committees and the Chief Executive Officer and of the Executive Management. The Committee approves and oversees reward design and ensures that the reward is appropriate and consistent with the Bank's culture, business and risk strategy, performance as well as with any legal or regulatory requirements. RGC also overseas the Bank's HR policies and rewards policy framework, corporate governance practices.

e) Investment & Credit Committee of the Board

The Investment & Credit Committee ("ICC") comprises four members of the BOD. The Committee has overall responsibility of setting the criteria for managing credit and investment risks and oversee the investment and credit strategies and objectives of the Bank. The Committee assists the Board of Directors in managing credit risk and reviews internal credit policies, grants approvals for credit and investment facilities in addition to reviewing the quality and performance of the Bank's lending portfolio and investment in line with the agreed risk appetite and best credit risk management practices.

f) Risk Committee of the Board

The Risk Committee ("RC") comprises three members of the BOD. The Committee has overall responsibility of overseeing the Bank's enterprise risk management framework, approach and pertinent policies. The Committee recommends to the Board, guidelines in relation to the Bank's current and potential future risk exposures and risk strategy, determination of risk appetite including risk limits and tolerance levels as well as the Bank's capital and liquidity strategy.

29. RISK MANAGEMENT (Continued)

g) Executive Management

Executive Management is responsible for the day to day operations towards achieving the strategic goals within the pre-defined risk appetite and approved strategy as a whole.

h) Management Executive Committee

The Management Executive Committee ("MEC") is a senior management level committee that has been entrusted with the role of supporting the CEO to determine and implement the Bank's strategic plan as approved by the BOD. The responsibilities of MEC include approving and monitoring the Bank's various business activities in accordance with the strategic plan approved by the Board.

In order to fulfil its responsibilities, the Committee has appointed other Sub-Committees and delegated specific tasks and adequate powers and authorities for effectively and efficiently carrying out the responsibilities assigned to them. The composition, guiding principles and detailed roles and responsibilities of MEC are covered in the MEC's charter.

i) Risk Executive Committee

The Risk Executive Committee ("REC") has the primary responsibility of overseeing the Bank's activities in managing credit risk, market risk, liquidity risk, operational risk, legal risk and other risks. REC has to ensure that the Bank has adequate risk management framework, policies, procedures and processes in place in order to identify, measure, monitor, mitigate and manage risks across all of its operations.

j) Asset and Liability Committee

The Assets and Liabilities Committee ("ALCO") is mainly responsible for defining long-term strategic plans and short-term tactical initiatives for directing asset and liability allocation prudently for the achievement of the Bank's strategic goals. ALCO monitors the Bank's liquidity and market risks and the Bank's risk profile in the context of economic developments and market fluctuations, to ensure that the Bank's ongoing activities are compatible with the risk / reward guidelines approved by the Delegated Approval Authority / Board.

k) Credit Committee

The Credit Committee ("CC") has the responsibility to grant / approve credit facilities as within their Delegated Authority and also makes decisions relating to the execution of investments in line with the Banks investment strategy and management of credit and concentration risks. Proposals exceeding their Delegated Authority are escalated to the ICC for consideration.

l) Risk Management

Risk Management Department is an independent function responsible for the preparation, implementation and updating the policies and procedures within the framework of the Bank's strategy and in line with the guidelines of the CBB. They are also responsible for the identification and continuous evaluation of all significant risks, design and implementation of appropriate internal controls to mitigate the risks and the processes involved in the remedial function. The risk management department is overseen by the Chief Risk Officer.

m) Legal Department

The Bank has engaged a panel of external legal counsels to handle all legal cases initiated for recovery of difficult loan cases. The progress and outcomes on such cases are monitored by the Risk Executive Committee.

n) Internal Audit Department

Risk Management processes are audited annually by Internal Audit, which examines the adequacy of the controls in place in addition to compliance with the policies by the respective departments. The internal audit results are discussed with the MEC and the findings, together with recommendations, to mitigate the findings are presented to the Audit Committee of the Board.

o) Treasury Department

"The Treasury Department is responsible for the day to day operations necessary to fund banking activities and implement ALCO's strategies in managing / optimizing interest rate and liquidity risks.

29. RISK MANAGEMENT (Continued)

p) Risk Measurement and Reporting Systems

Monitoring and controlling risks is primarily performed based on the approved limits and the strong internal control structures established by the Board. The limits reflect the business strategy and the market environment in which the Bank operates as well as the level of risk that the Bank is willing to accept.

Strict assessment processes are factored during the review and approval processes. In addition, the Bank monitors and measures the overall risk bearing capacity in relation to the aggregate risk exposure across all risk types and activities. Specifically tailored risk reports are prepared and distributed to ensure that all business divisions have access to extensive, necessary and up-to-date information.

Quarterly updates are provided to the BOD and on a monthly basis to all other members of the management on the utilization of market limits, proprietary investments, liquidity and other developments.

q) Risk Mitigation

Significant risk mitigation activities are focused in the credit area. Risk mitigation process comprise of an appropriate and adequate structure for the credit facilities at the initial stage followed by ongoing and regular monitoring, enforceable documentation and collateral.

The various risks to which the Group is exposed to and how the Group manages them is discussed in the notes below.

30. CREDIT RISK

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Group's loans and Islamic financing to customers, placements and debt securities.

i) Limits and Concentrations

Limits are assigned for each individual counterparty group and for each industrial segment. The Bank also monitors credit exposures, and continually assesses the creditworthiness of counterparties to the transactions. In addition, the Bank obtains security, where appropriate, enters into master netting agreements and collateral arrangements with counterparties, and limits the duration of exposures.

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

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

ii) Maximum Exposure to Credit Risk Without Taking Account of Any Collateral

The table below shows the maximum exposure to credit risk as at reporting date.

	2018 BD '000	2017 BD '000
Balances with Central Bank of Bahrain	1,991	2,690
Placement with banks and other financial institutions	21,917	27,011
Islamic financing and loans to customers	85,866	114,535
Investment securities	25,672	8,906
Other assets	3,397	2,343
	138,843	155,485
Contingent liabilities	1,473	3,678
Commitments	4,808	9,993
	6,281	13,671
Maximum credit risk exposure	145,124	169,156

30. CREDIT RISK (Continued)

iii) External Credit Assessment

The Bank does not use any external credit assessment institutions and the risk rating for the exposures are based on the internal credit framework and policy guidelines of the Bank.

iv) Concentration of Credit Risk

Since the Group's operations are restricted only to the Kingdom of Bahrain, it is primarily effected by the changes in the economic and other conditions prevailing in the Kingdom of Bahrain.

	2018 BD '000	2017 BD '000
Industry Sector		
Banks and financial institutions	**49,580**	38,607
Trading and manufacturing	**49,856**	53,418
Education and health	**6,488**	9,308
Hospitality, media and transportation	**7,894**	4,156
Fisheries, agriculture and dairy	**5,457**	5,209
Food processing	**2,836**	4,937
Others	**23,013**	53,521
	145,124	169,156

v) Collateral and other Credit Enhancements

The amount and type of collateral required depends on an assessment of the facility structure and the associated credit risk of the counterparty. Guidelines are implemented regarding the acceptability of types of collateral and valuation parameters. The main types of collateral obtained are cash margin, bank guarantees and real estate title deeds.

Market value of collateral is closely monitored by the Bank in addition to requesting additional collateral in accordance with the underlying agreement and evaluation of the adequacy of the allowance for impairment / ECL.

It is the Bank's policy to normally dispose off repossessed collateral in an orderly fashion after due notice has been provided to the defaulting customer. The proceeds are used to reduce or settle the outstanding claim. The Bank did not occupy repossessed properties for its own business use, as at the reporting date.

The Group holds collateral and other credit enhancements against certain of its credit exposures. The following table sets out the principal types of collateral held against Islamic financing and loans to customers:

	2018 BD '000	2017 BD '000
Cash	**1,502**	1,729
Mortgage lending	**62,234**	68,508

vi) Carrying Amount per Class of Financial Assets Whose Terms Have Been Renegotiated

The Group sometimes makes concessions or modifications to the original terms of loans as a response to the borrower's financial difficulties, rather than taking possession or to otherwise enforce collection of collateral. The Group considers a loan forborne when such concessions or modifications are provided as a result of the borrower's present or expected financial difficulties and the Group would not have agreed to them if the borrower had been financially healthy. The table below shows the carrying amount for renegotiated financial assets during the year.

	2018 BD '000	2017 BD '000
Islamic financing and loans to customers	**89**	1,409

30. CREDIT RISK (Continued)

vii) Credit Quality Per Class of Financial Assets

The following table sets out information about the credit quality of financial assets measured at amortised cost. Unless specifically indicated, for financial assets, the amounts in the table represent gross carrying amounts.

	2018				2017
	Stage 1 12-months ECL BD '000	Stage 2 Life time ECL not credit impaired BD '000	Stage 3 Lifetime ECL credit impaired BD '000	Total BD '000	Total BD '000
Placement With Banks and Other Financial Institutions	21,978	-	-	21,978	27,011
Less: Allowance for ECL	(61)	-	-	(61)	-
	21,917	-	-	21,917	27,011
Islamic Financing and Loans to Customers					
Corporate	34,797	2,508	22,778	60,083	64,080
SME	15,171	1,721	6,902	23,794	28,785
Small business	13,033	1,246	5,444	19,723	27,987
Taxi loans	3	2	130	135	170
Education loans	552	56	1,112	1,720	5,625
Overdrafts	129	-	626	755	1,908
Others	2,386	404	1,436	4,226	5,016
	66,071	5,937	38,428	110,436	133,571
Less: Allowance for ECL	(742)	(998)	(22,830)	(24,570)	(19,036)
	65,329	4,939	15,598	85,866	114,535
Off-balance Sheet Exposures					
Letters of credit and bank guarantees	1,398	24	51	1,473	3,678
Undrawn commitments	1,323	-		1,323	6,223
Less: Allowance for ECL	(63)	(3)	(51)	(117)	-
	2,658	21	-	2,679	9,901
Other Assets	-	-	2,322	2,322	1,906
Less: Allowance for ECL	-	-	(2,232)	(2,232)	(1,392)
	-	-	90	90	514
Carrying Amount Including Unfunded	89,904	4,960	15,688	110,552	151,961

31. MARKET RISK

Market risk is the risk of loss attributable to adverse changes in the values of financial instruments, whether on or off-balance sheet, as a result of changes in market rates (such as interest rates and foreign exchange rates) or price.

i) Interest Rate Risk

Interest rate risk arises from the possibility that changes the interest rates will affect future profitability or the fair values of the financial instruments. The Bank is exposed to interest rate risk due to mismatches of interest rate repricing of assets and liabilities. Positions are monitored periodically to ensure that this is maintained within the established limits.

The Bank primarily deals with 4 currencies, namely Bahraini Dinars, Kuwaiti Dinars, Saudi Riyals and United States Dollars, in which the Bank's interest sensitive financial instruments are denominated predominantly. The following table demonstrates the Bank's sensitivity to a reasonable possible change in interest rates, with all other variables held constant.

	Change in Basis Points	Impact of Change on net Interest Income		Change in Basis Points	Impact of Change on net Interest Income	
		2018	2017		2018	2017
		BD '000	BD '000		BD '000	BD '000
Bahraini Dinars	+100	1,031	1,007	-100	(1,031)	(1,007)
Kuwaiti Dinars	+100	-	1	-100	-	(1)
Saudi Riyals	+100	(4)	1	-100	4	(1)
United States Dollars	+100	(405)	(52)	-100	405	52

ii) Currency risk

Currency risk is the risk that the value of the financial instrument will fluctuate due to changes in foreign exchange rates. Net open positions are monitored on a daily basis to ensure compliance within the established limits.

The Bank views the Bahraini Dinar as its functional currency. In the opinion of the Bank's management, the currency risk for any position held in US dollar is insignificant since the Bahraini Dinar is pegged to the US dollar. The Bank had the following significant net open exposures denominated in foreign currencies as of 31 December 2018 and 2017:

	Equivalent Long / (Short)	
	2018	2017
Kuwaiti Dinars	71	153
US Dollars	340	91
Euro	1	6
GBP	5	6
Saudi Riyals	(17)	26
UAE Dirhams	5	21

32. EQUITY PRICE RISK

Equity price risk is the risk that the fair values of equities or managed funds decrease as a result of changes in the corresponding value of equity indices or the value of individual equity stocks. The Group manages this risk through diversification of investments in terms of geographical distribution and industry concentration.

The effect on profit or loss (as a result of a change in the fair value of equity instruments held as FVTPL) due to a reasonably possible change in equity indices, with all other variables held constant, is as follows:

The effect on profit or loss (as a result of a change in the fair value of equity instruments held as FVTPL) due to a reasonably possible change in equity indices, with all other variables held constant, is as follows:

	Trading Equities		Effect on Profit or Loss		
	2018 BD '000	2017 BD '000	% change in Index	Total 2018 BD '000	Total 2017 BD '000
Bahrain Bourse	96	153	± 15%	14	23

33. MATURITY ANALYSIS OF ASSETS AND LIABILITIES

The table below summarises the maturity profile of the Group's assets and liabilities as at 31 December 2018 and 2017 based on expected maturities.

	Up to 1 month BD '000	1 to 3 months BD '000	3 to 6 months BD '000	6 months to 1 year BD '000	1 to 3 years BD '000	Over 3 years BD '000	Total BD '000	Carrying amount BD '000
31 December 2018								
Assets								
Cash and balances with Central Bank of Bahrain	2,218	-	-	-	-	-	2,218	2,218
Placements with banks and other financial institutions	13,029		618	8,270	-	-	21,917	21,917
Islamic financing and loans to customers	3,640	7,949	10,808	18,687	53,890	18,320	113,294	85,866
Investment securities	19,264	-	-	-	-	11,880	31,144	31,144
Investment in associates	-	-	-	-	-	259	259	259
Investment properties	-	-	-	-	-	12,000	12,000	12,000
Property and equipment	-	-	-	-	-	1,155	1,155	1,155
Other assets	-	-	3,646	-	-	-	3,646	3,646
Total assets	38,151	7,949	15,072	26,957	53,890	43,614	185,633	158,205
Liabilities								
Term loans	-	-	4,157	4,157	13,972	28,322	50,607	50,607
Deposits	13,880	2,397	7,445	1,279	-	10,000	35,001	35,001
Other liabilities	-	-	5,106	-	-	-	5,106	5,106
Total liabilities	13,880	2,397	16,708	5,436	13,972	38,322	90,714	90,714
Net liquidity gap	24,271	5,552	(1,636)	21,522	39,918	5,292		
Cumulative liquidity gap	24,271	29,823	28,188	49,709	89,627	94,919		

33. MATURITY ANALYSIS OF ASSETS AND LIABILITIES (Continued)

	Up to 1 month BD '000	1 to 3 months BD '000	3 to 6 months BD '000	6 months to 1 year BD '000	1 to 3 years BD '000	Over 3 years BD '000	Total BD '000	Carrying amount BD '000
31 December 2017								
Assets								
Cash and balances with Central Bank of Bahrain	2,873	-	-	-	-	-	2,873	2,873
Placements with banks and other financial institutions	16,310	3,630	7,071	-	-	-	27,011	27,011
Islamic financing and loans to customers	4,849	8,099	11,946	21,955	75,684	12,260	134,793	114,535
Investment securities	716	-	-	2,894	-	11,533	15,143	15,143
Investment in associates	-	-	-	-	-	419	419	419
Investment properties	-	-	-	-	-	12,033	12,033	12,033
Property, plant and equipment	-	-	-	-	-	1,216	1,216	1,216
Other assets	-	-	2,940	-	-	-	2,940	2,940
Total assets	24,748	11,729	21,957	24,849	75,684	37,461	196,428	176,170
Liabilities								
Term loans	-	251	2,635	2,886	15,307	30,595	51,674	51,674
Deposits	30,709	4,962	7,810	2,907	52	-	46,440	46,440
Other liabilities	-	-	5,371	-	-	-	5,371	5,371
Total liabilities	30,709	5,213	15,816	5,793	15,359	30,595	103,485	103,485
Net liquidity gap	(5,961)	6,516	6,141	19,056	60,325	6,866		
Cumulative liquidity gap	(5,961)	555	6,696	25,752	86,077	92,943		

34. LIQUIDITY RISK

Liquidity risk is the risk that the Group will encounter difficulty in meeting obligations associated with its financial liabilities that are settled by delivering cash or another financial asset.

The table below summarises the maturity profile of the Bank's financial liabilities at 31 December 2018 and 2017 based on contractual undiscounted repayment obligations. See note 33 for the expected maturities of these liabilities.

	On demand BD '000	Up to 1 month BD '000	1 to 3 months BD '000	3 to 6 months BD '000	6 months to 1 year BD '000	1 to 3 years BD '000	Over 3 years BD '000	Total BD '000
31 December 2018								
Term loans	-	-	-	9,944	9,879	14,279	73,656	107,758
Deposits	-	13,880	2,397	7,445	1,279	-	10,000	35,001
Other liabilities	-	-	5,106	-	-	-	-	5,106
Total liabilities	-	13,880	7,503	17,389	11,158	14,279	83,656	147,865
31 December 2017								
Term loans	-	-	342	3,262	3,565	17,525	33,197	57,891
Deposits	19,576	11,133	4,962	7,810	2,907	52	-	46,440
Other liabilities	-	-	5,371	-	-	-	-	5,371
Total liabilities	19,576	11,133	10,675	11,072	6,472	17,577	33,197	109,702

The table below shows the contractual expiry by maturity of the Bank's contingent liabilities and commitments.

	On demand BD '000	Less than 3 months BD '000	3 to 12 months BD '000	1 to 5 years BD '000	Total BD '000
31 December 2018					
Contingent liabilities	382	122	701	268	1,473
Commitments	1,323	-	3,557	291	5,171
Total	1,705	122	4,258	559	6,644
31 December 2017					
Contingent liabilities	402	120	2,364	792	3,678
Commitments	6,223	-	3,849	356	10,428
Total	6,625	120	6,213	1,148	14,106

The Bank expects that not all of the commitments will be drawn before expiry of the commitments.

35. LEGAL AND OPERATIONAL RISK

Legal risk is the risk arising from the potential that unenforceable contracts, lawsuits or adverse judgments can disrupt or otherwise negatively affect the operations of the Group. The Group has developed controls and procedures to identify legal risks and believes that losses, if any will not be material.

Operational risk is the exposure to loss resulting from inadequate or failed internal processes, people and systems, or from external events. The Group has clearly defined operations procedures for each of its products and services. It also has computer systems that enable it to run operations with speed and accuracy. It conducts regular reviews of all business areas of the Bank and reports control deficiencies and exceptions to the Bank's policies and procedures. It also recommends measures to mitigate operational risk, which are implemented by management immediately. The Bank also has a contingency plan to take care of any failure of its computer systems. Regular back-ups are made for all important datasets, and stored outside the Bank's premises. This ensures that in case of any system failure, the Bank will be able to continue its operations without losing critical data or business transactions. As part of its disaster recovery plan, the Bank has established a back-up site which would and operate during an emergency.

The Bank has a specific Business Continuity Plan ("BCP"). The main objective of the BCP is to ensure that in the event of full or partial disaster, the Bank should be able to continue providing essential services to customers minimizing any adverse effects on the Bank's business, through business impact analysis, business restoration plans and procedures, for the identified critical functions. The Bank is conducting risk and control self assessments and capturing operational loss data in accordance with Basel III / CBB guidelines.

36. DERIVATIVES

A derivative is a financial contract between two parties where payments are dependent upon movements in the price of one or more underlying financial instrument, reference rate or index. In the ordinary course of business, the Group enters into forex forward contracts. The use of derivatives is governed by the Group's policies approved by the Board of Directors. The Group enters into derivative contracts for the purpose of reducing risks from potential movements in foreign exchange rates. The Group has entered into forex forward contracts with Central Bank of Bahrain with nominal value of BD 35,114 thousand (31 December 2017: BD 34,284 thousand).

37. CAPITAL ADEQUACY

The risk asset ratio, calculated in accordance with the capital adequacy guidelines approved by the CBB, for the Bank is as follows:

	2018 BD '000	2017 BD '000
Capital base		
Tier 1 capital	67,654	72,695
Tier 2 capital	2,024	940
Total capital base (a)	69,678	73,635
Risk-weighted assets (b)	148,451	185,028
Capital adequacy ratio (a/b*100)	46.56%	39.80%
Minimum requirement	14.0%	12.5%

The CBB sets and monitors capital requirements for the Bank as a whole. In implementing current capital requirements CBB requires the Bank to maintain a prescribed ratio of total capital to total risk-weighted assets. Capital adequacy regulations of CBB is based on the principles of Basel III of the IFSB guidelines.

The Bank's regulatory capital is analysed into two tiers:

AT1 comprise of instruments that meet the criteria for inclusion in AT1, instruments issued by consolidated banking subsidiaries of the Bank held by third parties which meet the criteria of AT1, and regulatory adjustments applied in calculation of AT1.

37. CAPITAL ADEQUACY (Continued)

Tier 2 capital, includes instruments issued by the Bank that meet the criteria for inclusion in Tier 2 capital, stock surplus resulting from issue of Tier 2 capital, instruments issued by consolidated banking subsidiaries of the Bank held by third parties that meet the criteria for inclusion in Tier 2, ECL held on stage 1 and 2 assets for inclusion within Tier 2, asset revaluation reserve from revaluation of fixed assets and instruments purposes and regulatory adjustments applied in the calculation of Tier 2 capital.

The regulatory adjustments are subject to limits prescribed by the CA module, these deductions would be effective in a phased manner through transitional arrangements from 2015 to 2018. The regulations prescribe higher risk weights for certain exposures that exceeds materiality thresholds. These regulatory adjustments required for certain items such as goodwill on mortgage service right, deferred tax assets, cash flow hedge reserve, gain on sale of related securitization transactions, defined benefit pension fund assets and liabilities, investment in own shares and reciprocal cross holdings in the capital of Banking and financial entities, investment in the capital of Banking and financial entities that are outside the scope of regulatory consolidation and where the bank does not own more than 10% of issued common shares capital of the entity and significant investments in the capital of banking and financial entities that are outside the scope of regulatory consolidation.

Banking operations are categorised as either trading book or banking book, and risk-weighted assets are determined according to specified requirements that seek to reflect the varying levels of risk attached to assets and off-balance sheet exposures.

Capital management

The primary objectives of the Bank’s capital management are i) to ensure that the Bank complies with externally imposed capital requirements ii) maintain healthy capital ratios in order to support its business and iii) to maximise shareholders’ value. The Bank manages its capital structure and makes adjustments to it in the light of changes in business conditions and the risk characteristics of its activities. In order to maintain or adjust the capital structure, the Bank may adjust the amount of dividend payment to shareholders or issue capital securities.

38. CLASSIFICATION OF ASSETS AND LIABILITIES

The following table provides a reconciliation between line items in the statement of financial position and categories of financial instruments.

	Designated as at FVTPL BD ’000	FVOCI – sukuk/debt instruments BD ’000	FVOCI – equity instruments BD ’000	Amortised cost / others BD ’000	Total BD ’000
31 December 2018					
Assets					
Cash and balances with Central Bank of Bahrain	-	-	-	2,218	2,218
Placements with banks and other financial institutions	-	-	-	21,917	21,917
Islamic financing and loans to customers	-	-	-	85,866	85,866
Investment securities	5,288	12,597	184	13,075	31,144
Investment in associates	-	-	-	259	259
Investment properties	-	-	-	12,000	12,000
Property and equipment	-	-	-	1,155	1,155
Other assets	-	-	-	3,646	3,646
Total assets	5,288	12,597	184	140,136	158,205
Liabilities					
Term loans	-	-	-	50,607	50,607
Deposits	-	-	-	35,001	35,001
Other liabilities	-	-	-	5,106	5,106
Total liabilities	-	-	-	90,714	90,714

Notes to the Consolidated Financial Statements (Continued)

31 December 2018

38. CLASSIFICATION OF ASSETS AND LIABILITIES (Continued)

The following table provides a reconciliation between line items in the statement of financial position and categories of financial instruments.

	Designated as at FVTPL BD '000	FVOCI – debt instruments BD '000	FVOCI – equity instruments BD '000	Amortised cost / others BD '000	Total BD '000
31 December 2017					
Assets					
Cash and balances with Central Bank of Bahrain	-	-	-	2,873	2,873
Placements with banks and other financial institutions	-	-	-	27,011	27,011
Islamic financing and loans to customers	-	-	-	114,535	114,535
Investment securities	12,116	-	133	2,894	15,143
Investment in associates	-	-	-	419	419
Investment properties	-	-	-	12,033	12,033
Property and equipment	-	-	-	1,216	1,216
Other assets	-	-	-	2,940	2,940
Total assets	12,116	-	133	163,921	176,170
Liabilities					
Term loans	-	-	-	51,674	51,674
Deposits	-	-	-	46,440	46,440
Other liabilities	-	-	-	5,371	5,371
Total liabilities	-	-	-	103,485	103,485

39. COMPARATIVE FIGURES

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

Risk and Capital Management Disclosures

For the year ended 31 December 2018

1. EXECUTIVE SUMMARY

This report has been prepared in accordance with Pillar 3 disclosure requirements prescribed by the Central Bank of Bahrain, herein referred to as "CBB". The report has been designed to provide BDB Group's stakeholders with detailed information on the Bank's approach in managing capital and risk, having due regard to the operating environment.

The Bank applies the Basel framework in the measurement of its capital adequacy, and in its capital management strategy and risk management framework. CBB's Basel III capital rules and guidelines became effective on 1st January 2015 as the common framework for the implementation of the Basel Committee on Banking Supervision's (Basel Committee) Basel III capital adequacy framework for banks incorporated in the Kingdom of Bahrain.

BDB has adopted the Standardized Approach for Credit Risk, Market Risk and the Basic Indicator Approach for Operational Risk to determine the capital requirement.

The disclosures in this report are in addition to the disclosures set out in the consolidated financial statements for the year ended 31st December 2018 presented in accordance with the International Financial Reporting Standards (IFRS).

2. INTRODUCTION TO THE BASEL III FRAMEWORK

The CBB's Basel III capital framework is based on three pillars consistent with the Basel III framework developed by the Basel Committee, as follows:

- Pillar 1: calculation of the Risk Weighted Assets (RWAs) and capital requirement.
- Pillar 2: the supervisory review process, including the Internal Capital Adequacy Assessment Process (ICAAP).
- Pillar 3: rules for the disclosure of risk management and capital adequacy information.

Amongst the three pillars, it is Pillar 1 that has been affected most and largely amended with the introduction of Basel III. Additional disclosure requirements have also been introduced under Pillar 3.

CBB CAPITAL ADEQUACY RULES:
CBB minimum required total capital adequacy ratio (including CCB) increased from 12 percent to 12.5 percent, compared to 10.5 percent recommended by the Basel Committee. Moreover, there are newly introduced limits and minima by the CBB under Basel III, such as minimum Common Equity Tier 1 Capital Ratio "CET1" of 9 percent (including CCB) and minimum T1 Capital Ratio of 10.5 percent (including CCB).

i) 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 a robust credit risk management architecture which is explained in greater detail in Note 2 of the consolidated financial statements.

The Bank does not use any external credit assessment institutions and the risk rating for the exposures are based on the internal credit framework and policy guidelines of the Bank.

For regulatory reporting purposes, BDB is using the Standardised Approach for credit risk.

Risk and Capital Management Disclosures (Continued)

For the year ended 31 December 2018

2. INTRODUCTION TO THE BASEL III FRAMEWORK (Continued)

ii) Market Risk

Market Risk is the risk of potential losses arising from movements in market prices of financial instruments as a result of changes in market rates (such as interest rates and foreign exchange rates).

For the regulatory market risk capital requirement, BDB is using the Standardised Approach for the calculation of regulatory market risk capital.

iii) 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 and activities.

Regulatory Reforms

The Bank is operating as a retail bank with special waivers under a license issued by the Central Bank of Bahrain ("CBB"), with headquarters and branches in Bahrain. The Bank's capital adequacy requirements are computed on a consolidated basis.

3. GROUP STRUCTURE

The Group's financial statements are prepared and published on a full consolidation basis, with all subsidiaries being consolidated in accordance with IFRS. The Group consists of the Bank and its following subsidiaries:

Name	Country of incorporation	Ownership interest	Year end
Bahrain Business Incubator Centre (S.P.C.)	Kingdom of Bahrain	100%	31 December
BDB SME Fund Company BSC (C) *	Kingdom of Bahrain	99%	31 December
Bahrain Export Development Center S.P.C	Kingdom of Bahrain	100%	31 December
Al-Waha Venture Capital Fund Company	Kingdom of Bahrain	99%	31 December
Middle East Corner Consultancy CO. WLL**	Kingdom of Bahrain	28.6%	31 December

* BDB SME Fund Company was liquidated during the year.

** The Bank is exposed, or has rights, to variable returns from its involvement with Middle East Corner Consultancy Co. WLL; and has the ability to affect those returns through its power over Middle East Corner Consultancy Co. WLL and thus is deemed as subsidiary of the Bank.

Restrictions on capital and transfer of funds within the Group

Since the Bank's subsidiaries are not regulated financial institutions, there is no regulatory impediment to the transfer of retained earnings to the Bank. However, as a separate legally incorporated entity, the transfer of paid in capital and mandatory reserves would require shareholder action. As the major shareholder (either direct or indirect) in the entity, the Bank has the power to undertake the legal processes for the transfer of such capital. The Bank's subsidiaries are registered and domiciled in Bahrain and there are no exchange controls or other restrictions on the transfer of funds.

Risk and Capital Management Disclosures (Continued)

For the year ended 31 December 2018

4. CAPITAL STRUCTURE AND CAPITAL ADEQUACY

The Bank's regulatory capital base comprises of (a) CET 1 capital which includes share capital, reserves and retained earnings. (b) Tier 2 capital which consist of general loan loss provisions.

Capital Structure, Minimum Capital and Capital Adequacy

The Bank's paid up capital consists only of ordinary shares and does not have any other type of capital instruments.

The Bank's regulatory capital base is as detailed below:

	As at 31 December 2018
Common Equity Tier 1 (CET1)	
Issued and full paid ordinary shares	65,000
Legal / Statutory reserve	1,186
Retained earnings	(1,257)
Other reserves	4,048
Current year Loss	(1,323)
Cumulative fair value changes on FVOCI investments (Debt)	(150)
Total Common Equity Tier 1 (CET1) (A)	67,504
Additional Tier 1 (AT1)	-
Total Tier 1 (T1)	67,504
Tier 2 Capital (T2)	
Expected Credit Losses (ECL)	1,612
Total Tier 2 (T2) (B)	1,612
Total Capital Base (Tier 1 + Tier 2) (C=A+B)	69,116

Capital Requirement for Risk Weighted Exposure

	Credit Exposure before credit risk mitigant	Eligible financial collateral	Credit Exposure after risk mitigant	Risk weighted exposure	Capital Requirement at 12.5%
As at 31 December 2018					
Cash items	227	-	227	-	-
Sovereigns	76,036	-	76,036	-	-
Banks	10,104	-	10,104	4,977	622
Corporates	71,977	859	71,118	69,843	8,730
Regulatory retail	-	-	-	-	-
Residential mortgages	-	-	-	-	-
Past due exposures	15,598	265	15,333	17,483	2,185
Investment in securities	4,715	-	4,715	7,025	878
Holding of Real Estate	13,671	-	13,671	26,687	3,336
Others assets	2,925	-	2,925	2,925	366
Total Credit Risk Exposure	195,253	1,124	194,129	128,940	16,118
Market Risk				88	11
Operational Risk				19,049	2,381
Total Risk Weighted Assets (D)				148,077	18,510
Capital Adequacy Ratio (B)/(D)				46.68%	
CET1 Capital Adequacy Ratio (A)/(D)				45.59%	

Risk and Capital Management Disclosures (Continued)

For the year ended 31 December 2018

5. CREDIT RISK – PILLAR 3 DISCLOSURES

This section describes BDB's exposure to credit risk, and provides detailed disclosures on credit risk in accordance with the CBB's Basel III framework, in relation to Pillar 3 disclosure requirements.

Definition of Exposure Classes

The Bank has a diversified funded and unfunded credit exposure. These exposures are classified as standard portfolio per CBB's Basel III requirements.

Brief description of applicable standard portfolio are as follows:

a. Claims on Sovereigns:

These pertain to exposures to governments and their central banks. Claims on Bahrain and GCC sovereigns are risk weighted at 0%. Claims on all other sovereigns are given a risk weighting of 0% where such claims are denominated and funded in the relevant domestic currency of that sovereign. Claims on sovereigns, other than those mentioned above are risk weighted based on their credit ratings.

b. Investment in Securities and Sukuk:

Investments in listed equities are risk weighted at 100% while unlisted equities are risk weighted at 150%.

c. Claims on Banks:

Claims on banks are risk weighted based on external rating agencies (S&P, Moody's Fitch, and Capital Intelligence). Short-term claims on locally incorporated banks are assigned a risk weighting of 20% where such claims on the banks are of an original maturity of three months or less and the claims are denominated and funded in either Bahraini Dinars or US Dollar.

Preferential risk weighting that is one category more favourable than the standard risk weighting is assigned to claims on foreign banks licensed in Bahrain of an original maturity of three months or less denominated and funded in the relevant domestic currency. Such preferential risk weight for short-term claims on banks licensed in other jurisdictions are allowed only if the relevant supervisor also allows this preferential risk weighting to short-term claims on its banks.

No claim on an unrated bank would receive a risk weight lower than that applied to claims on its sovereign of incorporation.

d. Claims on Corporates:

Claims on corporates are risk weighted based on credit ratings. Risk weighting for unrated (corporate) claims are assigned at 100%.

e. Impairment of Assets:

The Bank assesses at each reporting date whether there is any objective evidence that a specific financial asset is impaired. A financial asset is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred 'impairment event') and that impairment event (or events) has an impact on the estimated future cash flows of the financial asset that can be reliably estimated. Evidence of impairment may include indications that the borrower is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that it will enter bankruptcy or other financial reorganisation and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

f. Restructured Financing Facilities:

Where possible, the Bank seeks to restructure facilities rather than to take ownership of collateral. This may involve extending the payment arrangements and the agreement of new financing facility conditions. Management continuously reviews renegotiated financing facilities to ensure that all criteria are met and that future payments are likely to occur. The financing facilities continue to be subject to impairment assessment, calculated using the facility's original effective interest rate.

g. Past Due Exposures:

This includes claims, for which the repayment is overdue for more than 90 days. The risk weighting for such loans is either 100% or 150% is applied depending on the level of provisions maintained against the assets.

h. Equity Portfolio:

Investment in securities and financial entities are risk weighted at a minimum risk weight of 100% for listed entities or 150% for unlisted entities, unless such investments exceed 10% of the eligible capital of investee entity, in which case they are deducted from the Bank's capital.

i. Other Assets:

These are risk weighted at 100%.

5. CREDIT RISK – PILLAR III DISCLOSURES (Continued)

Definition of Exposure Classes (Continued)

j. Holding of Real Estate:

All other holdings of real estate by banks (i.e. owned directly, subsidiaries or associate companies or other arrangements such as trusts, funds or REITs) are risk-weighted at 200%. Investment in listed real estate companies and investment in unlisted real estate companies are risk-weighted at 300% and 400% respectively. Premises occupied by the Group are weighted at 100%.

k. Related Party Transactions and Balances:

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial and operating decisions. Related parties include entities over which the Bank exercises significant influence, major shareholders, directors and executive management of the Bank. Such related parties in the ordinary course of business at commercial interest and commission rates (Refer note 28 of the consolidated financial statements).

Amounts due from related parties are unsecured.

l. Highly Leveraged Counterparties:

The Bank does not lend to highly leveraged and other high risk counterparties as defined in PD-1-3-24(e).

6. FUNDED AND UNFUNDED TOTAL CREDIT EXPOSURE

	Total funded credit exposure	Total un-funded credit exposure	Average quarterly credit exposure
Sovereigns	40,946		38,587
PSE	-		-
Banks	10,082		11,244
Corporates	70,268	6,644	81,360
Regulatory retail	-		-
Mortgages	-		-
Past due exposures	15,598		15,618
Investment in securities	4,715		5,150
Holding of Real Estate	13,671		13,486
Other assets and Cash items	2,925		2,590
Total credit risk	158,205	6,644	168,033

7. CONCENTRATION OF CREDIT RISK BY INDUSTRY & REGION (EXPOSURES SUBJECT TO RISK WEIGHTING)

	2018			
	Region	Funded	Unfunded	Total
Government & public sector	GCC	40,946	-	40,946
Banks and financial institutions	GCC	10,950	-	10,950
Trading and Manufacturing	GCC	49,913	526	50,439
Educational Institutions & Healthcare	GCC	10,379	-	10,379
Hospitality, media and transportation	GCC	7,894	109	8,003
Fisheries, agriculture & dairy	GCC	5,588	-	5,588
Food processing	GCC	2,836	-	2,836
Others	GCC	29,699	6,009	35,708
TOTAL		158,205	6,644	164,849

Risk and Capital Management Disclosures (Continued)

For the year ended 31 December 2018

8. CREDIT CONCENTRATION GREATER THAN 15% INDIVIDUAL OBLIGOR LIMIT

Total credit exposures in excess of 15% individual obligor limit	2018
Sovereigns	76,057

9. COUNTERPARTY WISE BREAKDOWN OF NON PERFORMING LOANS AND IMPAIRMENT PROVISION

	Impaired loans (net of provision)	Stage 3: Lifetime ECL credit impaired	Charge for the period	Write off
Project finance	13,943	22,830	3,513	897
Fisheries and Agriculture	1,655	-	-	-
	15,598	22,830	3,513	897

10. RESIDUAL CONTRACTUAL MATURITY

Maturity analysis of assets

The table below summarises the residual contractual maturity profile of the Group's assets as at 31 December 2018

	Up to 1 month	1 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	Above 20 years	Total
2018										
Assets										
Cash and balances with Central Bank of Bahrain	2,218	-	-	-	-	-	-	-	-	2,218
Placements with banks and other financial institutions	13,029	-	618	8,270	-	-	-	-	-	21,917
Islamic financing and loans to customers	1,272	623	1,722	4,647	39,768	29,125	7,422	12	1,275	85,866
Investment securities	19,264	-	-	-	-	6,504	-	-	5,376	31,144
Investment in associates	-	-	-	-	-	-	259	-	-	259
Investment property	-	-	-	-	-	-	-	-	12,000	12,000
Property, plant and equipment	-	-	-	-	-	-	-	-	1,155	1,155
Other assets	-	-	3,646	-	-	-	-	-	-	3,646
Total assets	35,783	623	5,986	12,917	39,768	35,629	7,681	12	19,806	158,205

Risk and Capital Management Disclosures (Continued)

For the year ended 31 December 2018

11. PAST DUE AND IMPAIRED LOANS - AGE ANALYSIS

i) By Geographical Area

	2018			
	Three months to one year	One to three years	Over three years	Total
GCC	20,129	2,653	688	23,470
TOTAL	20,129	2,653	688	23,470

ii) By Counterparty Wise

	Three months to one year	One to three years	Over three years	Total
Project finance	18,890	2,173	413	21,476
Fisheries and Agriculture	1,239	480	275	1,994
TOTAL	20,129	2,653	688	23,470

12. GEOGRAPHICAL DISTRIBUTION OF IMPAIRMENT PROVISIONS FOR LOANS AND ADVANCES TO CUSTOMERS

The Bank and its subsidiaries operate and grant loans/financing facilities locally to Bahrain entities and persons only.

	2018
GCC	
Specific impairment provision - Stage 3	22,830
TOTAL	22,830

13. RECONCILIATION OF CHANGES IN EXPECTED CREDIT LOSSES

	2018		
	Stage 3: Lifetime ECL credit impaired	Stage 1: 12-month ECL and stage 2: Lifetime ECL not credit- impaired	Total
Balance at 31 December 2017	18,096	940	19,036
Recognition of expected credit losses under IFRS 9	2,118	1,108	3,226
Balance at 1 January 2018	20,214	2,048	22,262
Amounts written off during the period	(897)	(5)	(902)
Charge for the period	4,036	608	4,644
Recoveries during the period	(523)	(911)	(1,434)
At 31 December 2018	22,830	1,740	24,570

Restructured Credit Facilities

The Bank has restructured credit facilities amounting to BD 89 thousands during the period ended 31 December 2018. Restructuring concessions mainly related to deferral of loan installments to assist customers overcome temporary cash crunch situations or to realign the repayment with the borrower's revised cash flow projections.

The above restructurings did not have a significant impact on the present or future earnings and were primarily extensions of the loan/financing tenor.

Risk and Capital Management Disclosures (Continued)

For the year ended 31 December 2018

14. 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. The main collaterals taken for risk mitigation on credit exposures are deposits held by customers, pledge of quoted shares, residential / commercial property mortgage, investment securities, counter-guarantees from other banks, etc. However, for purposes of capital adequacy computation, only eligible collateral recognized under Basel III is taken into consideration.

15. ELIGIBLE FINANCIAL COLLATERAL AND GUARANTEES

Eligible financial collateral, and guarantees, presented by standard portfolio are as under:

	Gross credit exposure	Financial collateral	Credit exposure after credit risk mitigant
As at 31 December 2018			
Sovereigns	76,036	-	76,036
PSE	-	-	-
Banks	10,104	-	10,104
Corporates	71,977	859	71,118
Regulatory retail	-	-	-
Residential mortgages	-	-	-
Past due exposures	15,598	265	15,333
Investments in equities/funds	4,715	-	4,715
Holding of Real Estate	13,671	-	13,671
Other assets and Cash items	3,152	-	3,152
	195,253	1,124	194,129

16. SENSITIVITY ANALYSIS - INTEREST RATE RISK (IRRBB)

Impact on net interest income for the period ended 31 December 2018

	2018
Bahraini Dinar	
Assets	178,365
Liabilities	143,634
(+) 200 basis points	695
(-) 200 basis points	(695)
US Dollar	
Assets	33,799
Liabilities	46,909
(+) 200 basis points	(262)
(-) 200 basis points	262
Kuwaiti Dinar	
Assets	1,419
Liabilities	1,331
(+) 200 basis points	2
(-) 200 basis points	(2)
Saudi Riyals	
Assets	8,596
Liabilities	8,599
(+) 200 basis points	(0)
(-) 200 basis points	0

Risk and Capital Management Disclosures (Continued)

For the year ended 31 December 2018

17. MARKET RISK, INTEREST RATE GAP

Market Risk

Market risk is defined as potential adverse changes in the fair value or future cash flows of a trading position or portfolio of financial instruments resulting from the movement of market variables, such as interest rates, currency rates, equity prices and commodity prices, market indices as well as volatilities and correlations between markets. As its primary tool, the Bank measures its market risk exposure using the Standardised Approach under Basel III.

The Bank uses the Standardised Approach for calculating market risk capital charges for the following market risk components:

- Equity exposure risk
- Interest rate exposure risk
- Foreign currency exposure risk
- Commodity risk

The Bank's market risk capital charge is largely composed of foreign currency risk arising from the Bank's foreign exchange exposure on investments denominated mainly in Kuwaiti dinars, Saudi riyals and USD, and interest rate risk arising on the bond portfolio. The capital requirement for market risk using the Standardised Approach as at 31 December 2018 was as follows:

	Capital Requirements			
	2018	Maximum	Minimum	Average
Risk Type				
Equity risk capital	-	-	-	-
Foreign exchange risk capital	7	18	7	13.25
Interest rate risk capital	-	-	-	-
Commodity risk capital	-	-	-	-

Interest Rate Risk

Interest rate risk arises from the possibility that changes the interest rates will affect future profitability or the fair values of the financial instruments. The Bank is exposed to interest rate risks due to mismatches of interest rate repricing on maturity of assets and liabilities. Positions are monitored periodically to ensure that this is maintained within the established limits. The Banks assets and liabilities reprice only on maturity.

The Bank's interest rate sensitivity position is based on the maturity dates, as follows

	Up to 1 month	1 to 3 months	3 to 6 months	6 months to 1 year	1 to 5 years	Over 5 years	Non-interest bearing	Total
2018								
Assets								
Cash and balances with Central Bank of Bahrain	-	-	-	-	-	-	2,218	2,218
Placements with banks and other financial institutions	13,029	-	618	8,270	-	-	-	21,917
Islamic financing and loans to customers	1,272	623	1,722	4,647	68,893	8,709	-	85,866
Other assets	19,264	-	-	-	6,504	5,376	17,060	48,204
Total Assets	14,301	623	2,340	12,917	68,893	8,709	2,218	158,205
Liabilities								
Term loans	-	251	3,876	4,187	27,194	15,099	-	50,607
Deposits	13,880	2,397	7,445	1,279	-	10,000	-	35,001
Other liabilities	-	-	-	-	-	-	5,106	5,106
Total Liabilities	13,880	2,397	7,445	1,279	-	10,000	5,106	90,714
Net Liquidity Gap	421	(1,774)	(5,105)	11,638	68,893	(1,291)	(2,888)	

Risk and Capital Management Disclosures (Continued)

For the year ended 31 December 2018

18. EQUITY POSITION IN THE BANKING BOOK

	2018	
	Net exposure	Capital requirement
Publicly traded	96	12
Privately held	4,907	613
TOTAL	5,003	625

19. GAINS ON EQUITY INVESTMENTS

	2018
(i) Realised Gains/ Losses in the statement of profit or loss	-
(ii) Realised Gains/ Losses in retained earnings	(20)
(iii) Unrealised Gains/ Losses in CET1 Capital	(311)

The Bank does not have any equity investments subject to supervisory transition or grandfathering provisions.

20. DERIVATIVES

	Foreign exchange contracts
Notional – Banking book	35,114

21. OPERATIONAL AND LEGAL RISKS

Operational risk is the risk of loss arising from errors that can be made in instructing payments or settling transactions, breakdown in technology and internal control systems. The Bank uses the Basic Indicator Approach under the Basel III framework for measuring and managing its operational risk. Currently, the Bank conducts its business from a single location. BDB is a retail bank with some restrictions and accordingly, the number of client relationships and volume of transactions at BDB are moderate on average.

BDB's operations are conducted according to well-defined procedures. These procedures include a comprehensive system of internal controls, including segregation of duties and other internal checks, which are designed to prevent either inadvertent staff errors or malfeasance prior to the release of a transaction. The Bank also engages in subsequent monitoring of accounting records, daily reconciliation of cash and securities accounts and other checks to enable it detect any erroneous or improper transactions which may have occurred. Specific limits are set up to mitigate and monitor the Bank's exposure.

Operational risk is managed by the Risk management department. 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. Products and services are reviewed by the Internal Audit department and assessed for operational risks. 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.

Bank's ICAAP limit of 16% has been fixed to absorb any unforseen event as compared to regulatory capital requirement of 12.5%.

Legal risk is the risk arising from the potential that unenforceable contracts, lawsuits or adverse judgments can disrupt or otherwise negatively affect the operations of the group. The Group has developed controls and procedures to identify legal risks and believes that losses will not be material.

22. FINES & PENALTY

	Amount in BHD Actual 2018
Penalty paid to Central Bank of Bahrain	-

Composition of Capital Disclosure Requirements

For the year ended 31 December 2018

Step 1: Disclosure of Balance Sheet Under Regulatory Scope of Consolidation

This step is not applicable to the Bank since the scope of regulatory consolidation and accounting consolidation is identical.

Composition of Capital Disclosure Requirements (Continued)

For the year ended 31 December 2018

Step 2: Expansion of the Balance Sheet Under Regulatory Scope of Consolidation

	Balance sheet as in published financial statements	Consolidated PIR data
Assets		
Cash and balances at central banks	2,218	2,218
Placements with banks and other financial institutions	21,917	21,978
Investment securities	31,144	31,144
Investments in associates	259	259
Total Investment	**31,403**	**31,403**
of which:		
Significant investments in capital of financials insitutions exceeds the 10% of CET1		
Amount in excess of 10% of CET1 to be deducted		
Amount in excess of 10% of CET1 to be deducted in year 1		
Investment property	12,000	12,000
Loans and advances	85,866	87,606
of which: General loan loss provision which qualify as capital	1,801	1,801
Prepayments, accrued income and other assets	3,646	3,646
Property, plant and equipment	1,155	1,155
Total Assets	**158,205**	**160,006**
Liabilities		
Deposits from banks and other financial institutions	-	-
Customer accounts	35,001	35,001
Term Loans	50,607	50,607
Repurchase agreements and other similar secured borrowing		
Derivative financial instruments		
Accruals, deferred income and other liabilities	5,106	5,106
Total Liabilities	**90,714**	**90,714**
Shareholders' Equity		
Paid-in share capital	65,000	65,000
Shares under employee share incentive scheme		
Total Share Capital	**65,000**	**65,000**
of which amount eligible for CET1	-	65,000
of which amount eligible for AT1	-	-
Retained earnings	(2,580)	(2,580)
Statutory reserve	1,186	1,186
Other Reserve	4,048	4,048
General reserve		
Share premium		
Donations and charity reserve		
General loan loss provision which qualify as capital		1,801
Available for sale revaluation reserve	(150)	(150)
Share of Available for sale revaluation reserve relating to associates not considered for regulatory capital		
Minority interest in subsidiaries' share capital	(13)	(13)
Total Shareholders' Equity	**67,491**	**69,292**
Total Liabilities & Shareholders' Equity	**158,205**	**160,006**

Composition of Capital Disclosure Requirements (Continued)

For the year ended 31 December 2018

PD 3 : Main Features of Regulatory Capital Instruments

1	Issuer	Bahrain Development Bank BSC
2	Unique identifier (Bahrain Bourse ticker)	BDB
3	Governing law of the instrument	All applicable laws and regulations of the Kingdom of Bahrain
	Regulatory treatment	
4	Transitional CBB rules	Common Equity Tier 1
5	Post-transitional CBB rules	Common Equity Tier 1
6	Eligible at solo/group/group & solo	Group
7	Instrument Type	Common Equity shares
8	Amount recognized in regulatory capital (currency in Millions, as of most recent reporting date)	BD65,000
9	Par Value of instrument	BD1.00
10	Accounting classification	Shareholders' Equity
11	Original date of issuance	Not Applicable
12	Perpetual or dated	Not Applicable
13	Original maturity date	Not Applicable
14	Issuer call subject to prior supervisory approval	Not Applicable
15	Optional call date, contingent call dates and redemption amount	Not Applicable
16	Subsequent call dates, if applicable	Not Applicable
	Coupons / dividends	Not Applicable
17	Fixed or floating dividend/coupon	Not Applicable
18	Coupon rate and any related index	Not Applicable
19	Existence of a dividend stopper	Not Applicable
20	Fully discretionary, partially discretionary or mandatory	Not Applicable
21	Existence of step up or other incentive to redeem	Not Applicable
22	Noncumulative or cumulative	Not Applicable
23	Convertible or non-convertible	Not Applicable
24	If convertible, conversion trigger (s)	Not Applicable
25	If convertible, fully or partially	Not Applicable
26	If convertible, conversion rate	Not Applicable
27	If convertible, mandatory or optional conversion	Not Applicable
28	If convertible, specify instrument type convertible into	Not Applicable
29	If convertible, specify issuer of instrument it converts into	Not Applicable
30	Write-down feature	Not Applicable
31	If write-down, write-down trigger(s)	Not Applicable
32	If write-down, full or partial	Not Applicable
33	If write-down, permanent or temporary	Not Applicable
34	If temporary write-down, description of write-up mechanism	Not Applicable
35	Position in subordination hierarchy in liquidation (specify instrument type immediately senior to instrument)	Not Applicable
36	Non-compliant transitioned features	Not Applicable
37	If yes, specify non-compliant features	Not Applicable

Composition of Capital Disclosure Requirements (Continued)

For the year ended 31 December 2018

PD 4: Capital Composition Disclosure Template

	Common disclosure template to be used during the transition of regulatory adjustments (i.e. from 30 June 2015 to 31 December 2018)		Amounts subject to pre-2015 treatment	Reference
	Common Equity Tier 1 capital: instruments and reserves			
1	Directly issued qualifying common share capital (and equivalent for non-joint stock companies) plus related stock surplus	65,000		
2	Retained earnings	(2,580)		
3	Accumulated other comprehensive income (and other reserves)	5,234		
4	Not Applicable	-		
5	Common share capital issued by subsidiaries and held by third parties (amount allowed in group CET1)	-		
6	**Common Equity Tier 1 capital before regulatory adjustments**	**67,654**		
	Common Equity Tier 1 capital: regulatory adjustments			
7	Prudential valuation adjustments	-		
8	Goodwill (net of related tax liability)	-		
9	Other intangibles other than mortgage-servicing rights (net of related tax liability)	-		
10	Deferred tax assets that rely on future profitability excluding those arising from temporary differences (net of related tax liability)	-		
11	Cash-flow hedge reserve	-		
12	Shortfall of provisions to expected losses	-		
13	Securitisation gain on sale (as set out in paragraph 562 of Basel II framework)	-		
14	Not applicable.	-		
15	Defined-benefit pension fund net assets	-		
16	Investments in own shares (if not already netted off paid-in capital on reported balance sheet)	-		
17	Reciprocal cross-holdings in common equity	-		
18	Investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions, where the bank does not own more than 10% of the issued share capital (amount above 10% threshold)	-		
19	Significant investments in the common stock of banking, financial and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions (amount above 10% threshold)	-		
20	Mortgage servicing rights (amount above 10% threshold)	-		
21	Deferred tax assets arising from temporary differences (amount above 10% threshold, net of related tax liability)	-		
22	Amount exceeding the 15% threshold	-		
23	of which: significant investments in the common stock of financials	-		
24	of which: mortgage servicing rights	-		
25	of which: deferred tax assets arising from temporary differences	-		
26	National specific regulatory adjustments	-		

Composition of Capital Disclosure Requirements (Continued)

For the year ended 31 December 2018

	Common disclosure template to be used during the transition of regulatory adjustments (i.e. from 30 June 2015 to 31 December 2018)		Amounts subject to pre-2015 treatment	Reference
	REGULATORY ADJUSTMENTS APPLIED TO COMMON EQUITY TIER 1 IN RESPECT OF AMOUNTS SUBJECT TO PRE-2015 TREATMENT	-		
27	Regulatory adjustments applied to Common Equity Tier 1 due to insufficient Additional Tier 1 and Tier 2 to cover deductions	-		
28	**Total regulatory adjustments to Common equity Tier 1**	**67,654**		
29	**Common Equity Tier 1 capital (CET1)**	**-**		
	Additional Tier 1 capital: instruments			
30	Directly issued qualifying Additional Tier 1 instruments plus related stock surplus	-		
31	of which: classified as equity under applicable accounting standards	-		
32	of which: classified as liabilities under applicable accounting standards	-		
33	Directly issued capital instruments subject to phase out from Additional Tier 1	-		
34	Additional Tier 1 instruments (and CET1 instruments not included in row 5) issued by subsidiaries and held by third parties (amount allowed in group AT1)	-		
35	of which: instruments issued by subsidiaries subject to phase out	-		
36	Additional Tier 1 capital before regulatory adjustments	-		
	Additional Tier 1 capital: regulatory adjustments			
37	Investments in own Additional Tier 1 instruments	-		
38	Reciprocal cross-holdings in Additional Tier 1 instruments	-		
39	Investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions, where the bank does not own more than 10% of the issued common share capital of the entity (amount above 10% threshold)	-		
40	Significant investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation (net of eligible short positions)	-		
41	National specific regulatory adjustments	-		
	REGULATORY ADJUSTMENTS APPLIED TO ADDITIONAL TIER 1 IN RESPECT OF AMOUNTS SUBJECT TO PRE-2015 TREATMENT	-		
42	Regulatory adjustments applied to Additional Tier 1 due to insufficient Tier 2 to cover deductions	-		
43	Total regulatory adjustments to Additional Tier 1 capital	-		
44	**Additional Tier 1 capital (AT1)**	**-**		
45	**Tier 1 capital (T1 = CET1 + AT1)**	**67,654**		
	Tier 2 capital: instruments and provisions			
46	Directly issued qualifying Tier 2 instruments plus related stock surplus	-		
47	Directly issued capital instruments subject to phase out from Tier 2	-		
48	Tier 2 instruments (and CET1 and AT1 instruments not included in rows 5 or 34) issued by subsidiaries and held by third parties (amount allowed in group Tier 2)	-		
49	of which: instruments issued by subsidiaries subject to phase out	-		
50	Provisions	1,801		
51	**Tier 2 capital before regulatory adjustments**	**1,801**		

Composition of Capital Disclosure Requirements (Continued)

For the year ended 31 December 2018

	Common disclosure template to be used during the transition of regulatory adjustments (i.e. from 30 June 2015 to 31 December 2018)		Amounts subject to pre-2015 treatment	Reference
	Tier 2 capital: regulatory adjustments			
52	Investments in own Tier 2 instruments	-		
53	Reciprocal cross-holdings in Tier 2 instruments	-		
54	Investments in the capital of banking, financial and insurance entities thatare outside the scope of regulatory consolidation, net of eligible short positions, where the bank does not own more than 10% of the issued common share capital of the entity (amount above the 10% threshold)	-		
55	Significant investments in the capital banking, financial and insurance entities that are outside the scope of regulatory consolidation (net of eligible short positions)	-		
56	National specific regulatory adjustments	-		
	REGULATORY ADJUSTMENTS APPLIED TO TIER 2 IN RESPECT OF AMOUNTS SUBJECT TO PRE-2015 TREATMENT	-		
57	**Total regulatory adjustments to Tier 2 capital**	**-**		
58	**Tier 2 capital (T2)**	**1,801**		
59	**Total capital (TC = T1 + T2)**	**69,455**		
	RISK WEIGHTED ASSETS IN RESPECT OF AMOUNTS SUBJECT TO PRE-2015 TREATMENT			
60	**Total risk weighted assets**	**148,077**		
	Capital ratios			
61	Common Equity Tier 1 (as a percentage of risk weighted assets)	45.59%		
62	Tier 1 (as a percentage of risk weighted assets)	45.59%		
63	Total capital (as a percentage of risk weighted assets)	46.68%		
64	Institution specific buffer requirement (minimum CET1 requirement plus capital conservation buffer plus countercyclical buffer requirements plus D-SIB buffer requirement expressed as a percentage of risk weighted assets)	9.00%		
65	of which: capital conservation buffer requirement	2.50%		
66	of which: bank specific countercyclical buffer requirement (N/A)	0.00%		
67	of which: D-SIB buffer requirement (N/A)	0.00%		
68	Common Equity Tier 1 available to meet buffers (as a percentage of risk weighted assets)	45.59%		
	National minima including CCB (if different from Basel 3)			
69	CBB Common Equity Tier 1 minimum ratio	9.00%		
70	CBB Tier 1 minimum ratio	10.50%		
71	CBB total capital minimum ratio	12.50%		
	Amounts below the thresholds for deduction (before risk weighting)			
72	Non-significant investments in the capital of other financials	961		
73	Significant investments in the common stock of financials	259		
74	Mortgage servicing rights (net of related tax liability)	-		
75	Deferred tax assets arising from temporary differences (net of related tax liability)	-		

Composition of Capital Disclosure Requirements (Continued)

For the year ended 31 December 2018

	Common disclosure template to be used during the transition of regulatory adjustments (i.e. from 30 June 2015 to 31 December 2018)		Amounts subject to pre-2015 treatment	Reference
	Applicable caps on the inclusion of provisions in Tier 2			
76	Provisions eligible for inclusion in Tier 2 in respect of exposures subject to standardised approach (prior to application of cap)	1,801		
77	Cap on inclusion of provisions in Tier 2 under standardised approach (1.25% of Credit Risk weighted Assets)	1,612		
78	N/A	-		
79	N/A	-		
	Capital instruments subject to phase-out arrangements (only applicable between 1 Jan 2020 and 1 Jan 2024)			
80	Current cap on CET1 instruments subject to phase out arrangements	-		
81	Amount excluded from CET1 due to cap (excess over cap after redemptions and maturities)	-		
82	Current cap on AT1 instruments subject to phase out arrangements	-		
83	Amount excluded from AT1 due to cap (excess over cap after redemptions and maturities)	-		
84	Current cap on T2 instruments subject to phase out arrangements	-		
85	Amount excluded from T2 due to cap (excess over cap after redemptions and maturities	-		

These disclosures have been prepared in accordance with the Public Disclosure Module ("PD"), CBB Rule Book, Volume I for Conventional banks.

These disclosures have been reviewed by the Bank's external auditors Ernst & Young based upon agreed-upon procedures as required under Para PD-A.2.4 of the PD Module.