بيت التمويل الكويتي
Kuwait Finance House
Bahrain B.S.C.(c) البحرين ش.م.ب (م)

Licensed as an Islamic Retail Bank by the Central Bank of Bahrain

EMBRACING DIGITAL

SIMPLY SMARTER

ANNUAL REPORT 2020

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, Prime Minister and Deputy Supreme Commander

RECOGNITION

The Next 100 Global Awards 2020 - Best Digital Banking App (KFH Jazeel Banking)
Global Banking & Finance Review
2020

The Next 100 Global Awards 2020 - Best Islamic Retail Bank
Global Banking & Finance Review
2020

Abdulhakeem Y. Alkhayyat, CEO, Kuwait Finance House Bahrain B.S.C. (c) - Banking CEO of the Year Bahrain
Global Banking & Finance Review
2020

KFH Jazeel Banking
Best Digital Bank Bahrain
Global Banking & Finance Review
2020

KFH Jazeel Banking
Best Digital Islamic Bank Bahrain
Global Banking & Finance Review
2020

KFH Jazeel Banking
Most Innovative Retail Banking App Middle East
Global Banking & Finance Review
2020

KFH Jazeel Banking
Most Innovative Retail Banking App in Bahrain
Global Banking & Finance Review
2020

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EMBRACING DIGITAL

KFH-Bahrain is a wholly-owned subsidiary of KFH-Kuwait who manages its operations in the GCC, Asia, and Europe through over 480 branches. The Group offer services to clients in Kuwait, Bahrain, Turkey, Malaysia and Manheim in Germany.

VISION

Our vision is to improve people's lives through ethical and Shari'a compliant solutions by continuously innovating for the future while staying true to our foundation.

MISSION

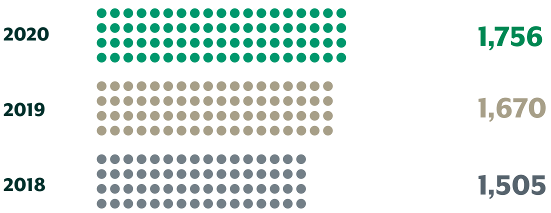
Our Mission is to provide "Simply Smarter Banking" through a focus on excellence and innovation, offering our valued customers a wide range of Shari'a compliant products and services based on a long standing robust financial position and a heritage based on integrity and ingenuity.

THREE YEAR HIGHLIGHTS

Built on the same strengths and vision that made KFH-Kuwait a leader in the Islamic banking industry for more than 40 years, KFH-Bahrain is committed to the creation of assets and wealth for its stakeholders.

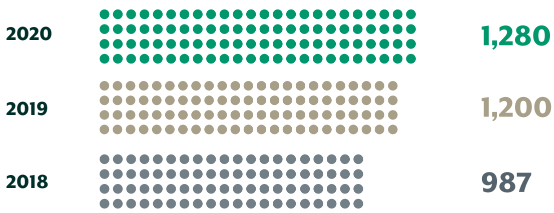
TOTAL ASSETS

BD MILLION



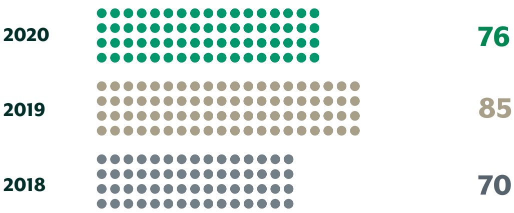
CUSTOMER DEPOSITS

BD MILLION



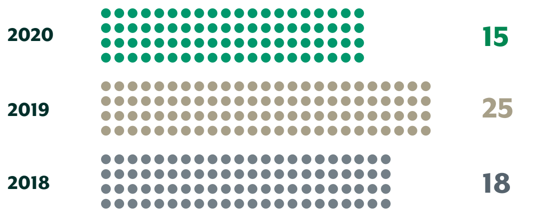
OPERATING INCOME

BD MILLION



NET INCOME

BD MILLION

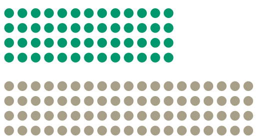


KEY FINANCIAL RATIOS

The Stage 3 non-performing facilities ratio reduced to 0.88 percent for the year ended 2020 compared to 3.7 percent in 2019. The improvement was achieved with a customer-centric approach, and by working out a 'win-win', sustainable solution for both the customer and KFH-Bahrain.

RETURN ON EQUITY

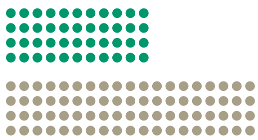
YEAR ENDED



2020	8.9%
2019	13.8%

RETURN ON ASSETS

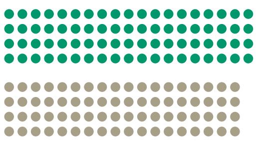
YEAR ENDED



2020	0.9%
2019	1.6%

CAPITAL ADEQUACY

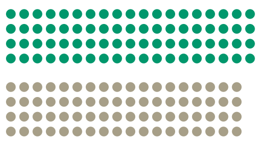
YEAR ENDED



2020	21.8%
2019	21.2%

NET STABLE FUNDING

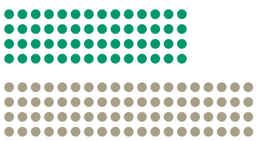
YEAR ENDED



2020	112.0%
2019	108.0%

LIQUIDITY COVERAGE

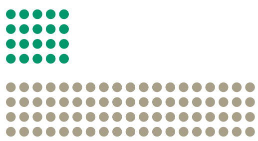
YEAR ENDED



2020	605.0%
2019	811.0%

NON PERFORMING FACILITIES

YEAR ENDED



2020	0.88%
2019	3.7%

KUWAIT FINANCE HOUSE - BAHRAIN
DELIVERING EXCELLENCE IN ISLAMIC BANKING

Kuwait Finance House - Bahrain (KFH-Bahrain) brings to the market a compelling concept in Islamic Banking, combining both Islamic Investment Banking and Islamic Commercial Banking facilities. Established in October 2002 as the first fully-owned subsidiary of Kuwait Finance House - Kuwait, KFH-Bahrain's mission is to deliver excellence and innovation through a broad and integrated range of financial products and services that comply with Shari'a principles.

Built on the same strengths and vision that made KFH-Kuwait a leader in the Islamic banking industry for more than 40 years, KFH Bahrain is committed to: the creation of assets and wealth for its stakeholders; participation in the advancement and growth of the Gulf Cooperation Council (GCC) and broader Middle Eastern economies; and the promotion of Islamic banking worldwide.

KFH-Bahrain's uncompromising view towards Shari'a compliance, maintaining a robust financial position, and honouring its long history of ingenuity and leadership, is proven on a daily basis as the Bank strives to meet the needs of a fast-growing market.

With demand steadily growing for Shari'a compliant products and services, KFH-Bahrain is playing a pioneering role in developing new groundbreaking services, financing structures, and investment vehicles that can effectively meet these needs and deliver attractive risk-adjusted returns.

While it is the aim of any institution to capitalise on important market opportunities, KFH-Bahrain's mission is to create even greater opportunities and demand in new areas, which have yet to be explored. Since its establishment, the Bank has created a strong portfolio of products and services and devised a number of important innovations that have gained the confidence of a strong, fast-growing customer and investor base throughout its Consumer Banking and Finance, Corporate Banking, and Investment Banking operations.

These include finance facility innovations, such as, the 25 years real estate finance, which allows double the financing period available to individuals and families in the Bahraini market; and the introduction of Tamweely Personal Finance that adheres strictly to the principles of Shari'a allowing customers to fulfil their personal financing requirements. In addition, the Social Housing Scheme "Mazaya" in collaboration with the Ministry of Housing provide customers with convenient mortgage financing. Furthermore, KFH Bahrain's Corporate Finance and Retail Activities continue to garner attention as the Bank begins innovative new projects and takes Islamic banking and finance in new global directions. The Bank continues to create investment opportunities and funds, and actively participates in Bahraini development projects.

In 2018, KFH Bahrain had introduced KFH Jazeel Banking application which is the first integrated FinTech digital banking platform in the Kingdom of Bahrain. Available across all Android and iOS systems, Jazeel is a first of- its-kind app in Bahrain. It provides new and existing customers with integrated end-to-end solutions to all the highest volume transactions the Bank provides while creating a financing community among individuals and companies in the Kingdom and informing them of about new offers and promotions. The groundbreaking platform mainly targets GCC nationals residing in 5 GCC countries, and the residents of Bahrain, who are able to open accounts within an average of less than 5 minutes without having to visit a physical branch (the first cross border banking eKYC in MENA).

In 2019, the Bank revamped Jazeel with new key features that comes in line with KFH Bahrain's strategy to support the FinTech sector in the Kingdom of Bahrain. These features include the customer's ability to apply for Tamweely Personal Finance with an immediate initial approval, a more fluid and intuitive user - friendly interface that can be navigated in both Arabic & English. In addition, customers can re-activate dormant accounts, update the account holder information, known as KYC (Know-Your-Customer). Furthermore, customers also have the option to transfer money using mobile numbers of KFH Jazeel users and notify those who want to conduct any money transfers. KFH Jazeel Banking platform is evolving every quarter to bring to clients more products and services thereby providing a true holistic digital banking experience.

Hamad Abdul Mohsen Al-Marzouq
Chairman

Praise be to Allah Almighty, and Peace and Blessings be upon our Prophet Muhammad (PBUH), his Family and Companions.

On behalf of the Board of Directors (the "Board"), it gives me great pleasure to present the 2020 Annual Report of Kuwait Finance House – Bahrain (the "Bank").

Resilience, determination, collaboration, and cooperation

The year 2020 was a year of exceptional circumstances. With the COVID-19 pandemic resulting in near-total lockdown across many parts of the world, individual lives and businesses were changed beyond recognition as they adapted to the 'new normal'.

The Government of Bahrain's various support programs towards businesses and individuals affected by the pandemic, and the Central Bank of Bahrain mandated deferment of finance repayments no doubt helped mitigate the damage to the economy and stimulate business. Moreover, the Kingdom of Bahrain, which had already begun the shift towards a digital economy with good information technology infrastructure, was well-placed to make the necessary transition to digital and contactless transactions, which helped the economy and contributed in safeguarding public health.

Throughout the year, Kuwait Finance House-Bahrain (KFH-Bahrain) was pleased to play a supporting role in these efforts by making it easier for customers to stay in control of their finances. At the same time, KFH-Bahrain honored its commitments to its stakeholders by continuing to innovate and deliver outstanding products and services.

KFH-Bahrain has always taken a visionary approach towards banking and financial services, developing a robust IT infrastructure and a comprehensive digital strategy to improve its competitiveness. These efforts, which were recognized with several prestigious international awards, enabled us to meet our customers' banking needs even during the nationwide lockdown.

The pandemic demonstrated KFH-Bahrain's expertise in risk management and the efficiency of its business continuity and emergency response plans. Our transition to working from home to ensure our team's safety was seamless and highly effective, while our prudent approach to risk management helped create a buffer against volatile and unfavorable market conditions as well as improve KFH-Bahrain's Asset Quality.

KFH-Bahrain continued to play a prominent role in community development. We supported many national initiatives during this period to alleviate the pressure arising as a result of COVID-19 pandemic as illustrated later in this statement.

We extend our sincere gratitude to our staff in both Bahrain and Kuwait and all stakeholders for their exceptional efforts and continued dedication throughout the year, and we look forward to seeing the world economy recovering on the successful deployment of the COVID-19 vaccine.

Retail and Private Banking

Throughout 2020, KFH-Bahrain customers were able to open bank accounts, apply for financing, make payments and transfers, and subscribe to our entire suite of market-leading services through our website and our award-winning KFH Jazeel app, completing a record BHD 180 million worth of online banking transactions during the year. To further support our customers, we strengthened our call center's service level to provide round-the-clock support, while our Private and Retail Banking sectors paid special attention to meet each client's banking requirements.

Our Retail Banking team focused on improving customer experience, launching several new services via our ATMs, and branches, and collaborated with Benefit to offer our customers contactless Tap&Go payment facilities, while our Open Banking infrastructure is ready to be deployed, which will further enhance our service offering. A new Libshara campaign was also launched with a new set of prizes which emphasized rewarding our customers for their relationship with us.

Corporate & SME Banking

Our Corporate & SME Banking department worked very closely with our clients during the year providing support, feedback and advice on funding needs and requirements. KFH-Bahrain endorsed a proactive approach to realign installments with the clients' repayment capability.

Our Corporate & SME Banking department witnessed 14.3 percent growth in revenues and our corporate credit portfolio grew by 2.5 percent from BHD 434 million to BHD 445 million in 2020 with cautious and detailed assessment of any new disbursements to ensure our Asset Quality. Our NPF ratio was improved significantly during 2020 and stands now at 2.4 percent at the corporate portfolio level.

To better serve our clients, we have launched phase I of our digital Corporate Banking Jazeel App which enhances the client interface and overall customer experience. We have also launched our Shari'a compliant "Cash Line" product to better serve Corporate clients' needs and short-term liquidity requirements.

Wealth Management

Our Wealth Management department grew its assets under management by 25 percent during the year, driven mainly by clients' non-discretionary sukuk portfolio which witnessed a record volume of over BHD 113.1 million during 2020. Furthermore, it launched a first-of-its-kind Shari'a-compliant Securitization Program, offering financial institutions and state-owned entities a solution to manage both their liquidity positions and balance sheets as well as ratio adherence requirements through the issuance of a Series of Mudaraba Sukuk under a trust structure. This program is timely and the valuable products that can emerge from it would not only be beneficial for the Bank, but also the entire industry. Moreover, it provides an opportunity for our clients to diversify their portfolio allocation strategy and enhance their risk-adjusted returns by having exposure to a different combination of assets.

Kingdom of Bahrain – Economic Highlights

Supporting national initiatives

KFH-Bahrain is pleased to support the Government of Bahrain in its efforts to strengthen the economy through various infrastructure and development projects.

As a key partner of the Mazaya social housing scheme, our campaign to extend housing finance to buyers in Phase 1 of the Deerat Al Ayoun project in Diyar Muharraq proved highly successful. We secured a significant share of phase I due to favorable terms, the speed of our financing process, and our outstanding relationship with the clients.

KFH-Bahrain Financial Results

Focused on success

Financial results for the year ended 2020 were positive despite the unfavorable economic conditions, underscoring KFH-Bahrain's solid market position, financial standing and prudent risk management approach.

Our net profits for the year decreased 39 percent, from BHD 25.0 million in 2019 to BHD 15.2 million for the year ended 31 December 2020. This was due to various factors including deferral of the planned sukuk sale, additional provisions recorded during 2020, reduced NFMs due to stimulus related factors including the lowering of prices/rates globally.

Operating income for the period decreased by 11 percent, from BHD 85.1 million in 2019 to BHD 76.0 million in 2020. Total assets under management increased by 16 percent to BHD 685.2 million in 2020, while customer deposits reached 1.28 billion, a 7 percent increase compared to the end of 2019. In addition, the financing portfolio reached BHD 1.0 billion, an increase of 10 percent from the previous year, of which 2 percent was from Corporate, 14 percent from Consumer, 30 percent from Treasury Capital Markets, and 34 percent from Wealth Management.

Keen on participating in the country's sovereign and institutional fund raising, KFH-Bahrain continued to grow its BD sovereign sukuk holding by a sizeable 20 percent year-on-year with a portfolio reaching BHD 324.7 million as of 31 December 2020, supporting the Bank's profitability and liquidity profile amid the challenging environment posed by the pandemic and lower oil prices. Furthermore, the Bank started participating in a BHD 150 million syndicated financing deal for Eskan Bank which was arranged by KFH-Bahrain's Treasury & Capital Markets Department.

By proactively adopting, and robustly implementing risk-based actions pre and post COVID-19 pandemic, KFH-Bahrain has improved its Asset Quality. The Stage 3 non-performing facilities ratio reduced to 0.88 percent for the year ended 2020 compared to 3.7 percent in 2019. The improvement was achieved with a customer-centric approach, and by working out a 'win-win', sustainable solution for both the customer and KFH-Bahrain.

Embracing Digital

An easy banking experience

Through our award-winning flagship offering, KFH Jazeel, KFH-Bahrain was the first bank in Bahrain to enable customers to open an account and conduct nearly 90 percent of their banking transactions online.

We are working to continuously update the KFH Jazeel app features and functionalities to make it an even more attractive proposition for our users. In addition to opening an account and making transfers and payments, customers can now also apply for certain finance requirements using their smartphones. It makes it easier than ever to do business in the region, offering seamless, borderless banking for all GCC nationals.

Our focus on fintech is in line with the government's economic vision 2030 and we aim to strategically leverage the power of technology to deliver an exceptional user experience through personalized, end-to-end, and fully automated services which are fast, secure, efficient and, above all, easy to access and use.

Operations

A team like family

Even more so during the challenges of 2020, KFH-Bahrain recognized the importance of taking care of its team. We were one of the first banks in the Kingdom to roll out a comprehensive work-from-home program which empowered our team members to balance their personal and professional commitments while staying safe. KFH-Bahrain immediately implemented a special program for working mothers which continues until today, offering them reduced office hours so that they can spend their mornings homeschooling and taking care of their children.

The transition to working from home was frictionless and highly efficient thanks to the foresight of our dedicated business continuity taskforce, which had been practicing disaster scenario drills every two months for the past ten years. All processes continued uninterrupted with minimal onsite staff, while remote team members could access all relevant data from a highly secure web-based platform.

In addition to social distancing measures and regular sanitization of all surfaces in the office, we arranged for a dedicated COVID-19 testing team to serve KFH-Bahrain staff. Every two weeks, fifty of our team members would volunteer to be tested to help protect the wellbeing of their colleagues and families.

KFH-Bahrain continued to invest in building and developing local talent. Our Bahrainization rate stands at 91 percent, with a comprehensive training and development strategy to ensure that all team members have the opportunity to build successful careers and assume leadership positions.

Regulation, Compliance & Governance

Industry best practices

The Bank continues to ensure that its corporate governance environment adheres to industry best practices. Key functions such as Audit, Risk, and Compliance saw the implementation and further enhancement of our digital solutions.

In 2020, we started the annual recertification process of PCI-DSS (Card Data Environment) and successfully renewed external audit certifications which were awarded previously, namely ISO 27001:2013 (Information Security Management System) and ISO 22301:2012 (Business Continuity Management System). KFH-Bahrain was among the first banks in the Kingdom to be certified for both these standards concurrently.

The Information Security Management Systems certification identifies security risks and sets appropriate controls for their management and disposal, which helps protect stakeholder and customer data.

The Business Continuity Management (BCM) System demonstrates the Bank's commitment to maintaining uninterrupted banking services, thereby enhancing customer satisfaction and the quality of customer service, while improving organizational performance and minimizing the recovery time necessary to resume operations in the event of any disruption. The BCM team is currently playing a leading role in the Bank's management of staff and operations during the ongoing COVID-19 pandemic disruptions.

In addition to the above improvement activities carried out in 2020, the Bank continued to significantly upgrade its IT hardware and software to the most advanced technologies or systems available in order to increase resilience and improve security and to ensure all staff are empowered to work remotely in a seamless manner.

Corporate Sustainability

Team Bahrain

The unique circumstances of 2020 required us to rally together to support not just our teams but also the wider community. As part of Team Bahrain, KFH-Bahrain supported key initiatives by Tamkeen and the Supreme Council of Women to offer financial assistance and medical supplies to families in need.

KFH-Bahrain also supported the Feena Khair national campaign, which saw more than 50,000 meals distributed daily to expatriates amid precautionary measures to combat COVID-19.

Education is a key area of focus for KFH-Bahrain. We are pleased to continue our participation in sponsoring the prominent Crown Prince's International Scholarship Program. Also and in addition to donating laptops for students to continue their studies online, we worked closely with the University of Bahrain to migrate more than 150 key study modules onto online platforms. More than 3,000 students benefited from this initiative, which will continue to serve students for years to come.

Furthermore, our flagship internship program, which is open to students from all universities in Bahrain, continued uninterrupted via remote work or socially distanced practices in the office. The two-month program prepares students for a career in financial services, and outstanding candidates are offered jobs at KFH-Bahrain upon graduation.

KFH-Bahrain participated in the Kingdom's National celebrations this year by launching a limited-edition ATM card featuring the Bahraini flag to coincide with the Bahrain National Day celebrations. The card proved very popular with our customers and was immediately oversubscribed.

Awards and Recognition

An industry leader

In 2020 KFH earned a total of seven awards from Global Banking & Finance Review, underscoring our market leading position and product offering.

These awards included Best Islamic Retail Bank, Best Digital Bank Bahrain, and Best Digital Islamic Bank. Our app, KFH Jazeel, was also lauded as the Best Digital Banking App, and was recognized as the Most Innovative Retail Banking App both in the Middle East and Bahrain categories. During the same period, our CEO Abdulhakeem Y. Alkhayyat was named Banking CEO of the Year Bahrain.

We also received an award for our excellence in Straight-Through Processing (STP) from leading global financial institution, J.P. Morgan.

Adherence to the Principles of Islamic Banking

On behalf of the Board I am once again pleased to recognize the excellent work of our Fatwa and Shari'a Supervisory Board, comprised of the well-respected scholars Sheikh Dr. Sayyed Mohammad Al-Sayyed Abdul Razzaq Al-Tabtaba'e (Chairman), Sheikh Dr. Mubarak Al-Harbi (Vice Chairman) and Sheikh Dr. Anwar Abdulsalam (Member) who continue to work tirelessly to ensure the Bank's products and services adhere to Islamic principles, supported by a hard working professional team within the Bank.

With Gratitude

On behalf of the Board and management, and with deep gratitude, I thank His Majesty King Hamad bin Isa Al Khalifa and His Royal Highness Prince Salman bin Hamad Al Khalifa, the Crown Prince, and Prime Minister. I would also like to extend my appreciation to the Central Bank of Bahrain and His Excellency the Governor, Mr. Rasheed Al Maraj for their valuable support and direction, and to the various ministries of the Government of Bahrain.

We are deeply thankful to our respected stakeholders for their continued support, trust and loyalty, and to our board members, management and staff for their continued dedication and professionalism.

May Allah grant everyone the best in this Life and the Hereafter. May the peace, mercy and blessings of Allah be upon you.

Hamad Abdulmohsen Al-Marzouq
Chairman

BOARD OF DIRECTORS

Hamad Abdul Mohsen Al-Marzouq

Chairman

Mohammed Naser Al-Fouzan

Vice Chairman

Abdulwahab Iesa Alrushood

Board Member

Shadi Ahmad Zahran

Board Member

Abdullah A. Al-Marzouq

Board Member

Noorur Rahman Abid

Board Member
(Until 14th September 2020)

Khalid Mohamed Alsaad

Board Member

Youssif Abdullah Taqi

Board Member

Abdulhakeem Y. Alkhayyat

Managing Director & CEO

FATWA AND SHARI'A SUPERVISORY BOARD

Sheikh Dr. Sayyed Mohammad Al-Sayyed Abdul Razzaq Al-Tabtaba'e

Chairman

Sheikh Dr. Mubarak Al-Harbi

Vice Chairman

Sheikh Dr. Anwar Abdulsalam

Member

EXECUTIVE MANAGEMENT

Abdulhakeem Y. Alkhayyat

Managing Director & CEO

Khalid Al Maarafi

Executive Manager
Retail & Private Banking

Yousif Al-Hammadi

Executive Manager
Financial Control,
Administration

Mahmood G. Al Mahmood

Executive Manager
Corporate & SME Banking

Mohammed F. Hamad

Executive Manager
Operations, IT & Corporate
Communications

Lilian Le Falher

Executive Manager
Treasury and Capital Market

Ahmad Saeed

Executive Manager
Investment & Real Estate
Project Management

Isa Al Duwaishan

Executive Manager
Internal Shari'a Audit

Amit Yashpal

Executive Manager
Risk Management, Credit Review, Credit
Administration, Collections
& Financing Restructuring

Raed Ajawi

Executive Manager
Internal Audit

RETAIL BANKING

INNOVATION TOWARDS SERVICE EXCELLENCE

We constantly enhance our technology and services to provide greater access to the Bank's products and seamless experience with regards to customer service excellence.

KFH-Bahrain provides a broad range of retail banking services that combine innovative products with exceptional customer care. Our products and financing facilities cater to the long-term needs of customers, taking into account local market characteristics. Our growth is driven by a determination to continuously improve our service quality, while delivering superior Shari'a compliant products

We constantly enhance our technology and services to provide greater access to the Bank's products and seamless experience with regards to customer service excellence.

KFH Jazeel Banking is revolutionizing the way we do banking. KFH Jazeel is the Bank's flagship Fintech digital bank initiative that paves the way for the next generation of financial services at your fingertips. New updates rolled out during the year provided first-of-its-kind features in Bahrain including allowing KFH Jazeel community subscribers to apply for personal financing without the need to visit a branch. As a digital bank platform all clients can open a KFH Jazeel savings account in minutes and can have access to a portfolio of services anytime, anywhere, at their comfort and convenience. The customer onboarding experience is fully digitized though an E-KYC (electronic Know-Your Customer) process that can be done using smartphones. KFH Jazeel also offers customers access to a suite of account management services without needing to visit a branch. During the year, KFH Jazeel Banking received four prestigious awards from Global Banking & Finance for the year 2020. Best Digital Bank in Bahrain 2020, Most Innovative Retail Banking App Middle East 2020 & Most Innovative Retail Banking App Bahrain 2020, and The Next 100 Global Awards 2020 for the Best Digital Banking App.

In addition to our new products, we remain committed to building on our more established offerings. Well into its eighth successful year, our Libshara Investment Savings account continues to enhance its selection of valuable prizes. In the 2019-2020 edition, account holders stood the chance to win two grand prizes of $500,000 each, ten prizes of $100,000, and 960 cash prizes over 12 months. The account was recognized as the "Critics' Choice Best Prize-linked Islamic Retail Investment Product" for 2017 at the Islamic Retail Banking Awards by Cambridge IFA.

Our Wakala Investment Account is an innovative offering, designed according to the Islamic Shari'a principle of Al Wakala. The Bank invests in its general portfolio on the client's behalf, at no charge, for a pre-promised anticipated profit rate, which is shared on a monthly basis. The Wakala Investment Account opening process has also been digitized and introduced in KFH Jazeel Banking App, therefore allowing customers to instantly open this account at their own convenience.

As part of the Wakala Profit Sharing Investment Accounts family, the Bank has introduced a new long term Flexible Wakala PSIA named "Wakala Flexi" allowing customers to withdraw up to 20% of their investment amount without canceling the investment account. Whereby, profits are distributed based on the total average amount during the period of the investment, which is shared at the end of the investment period.

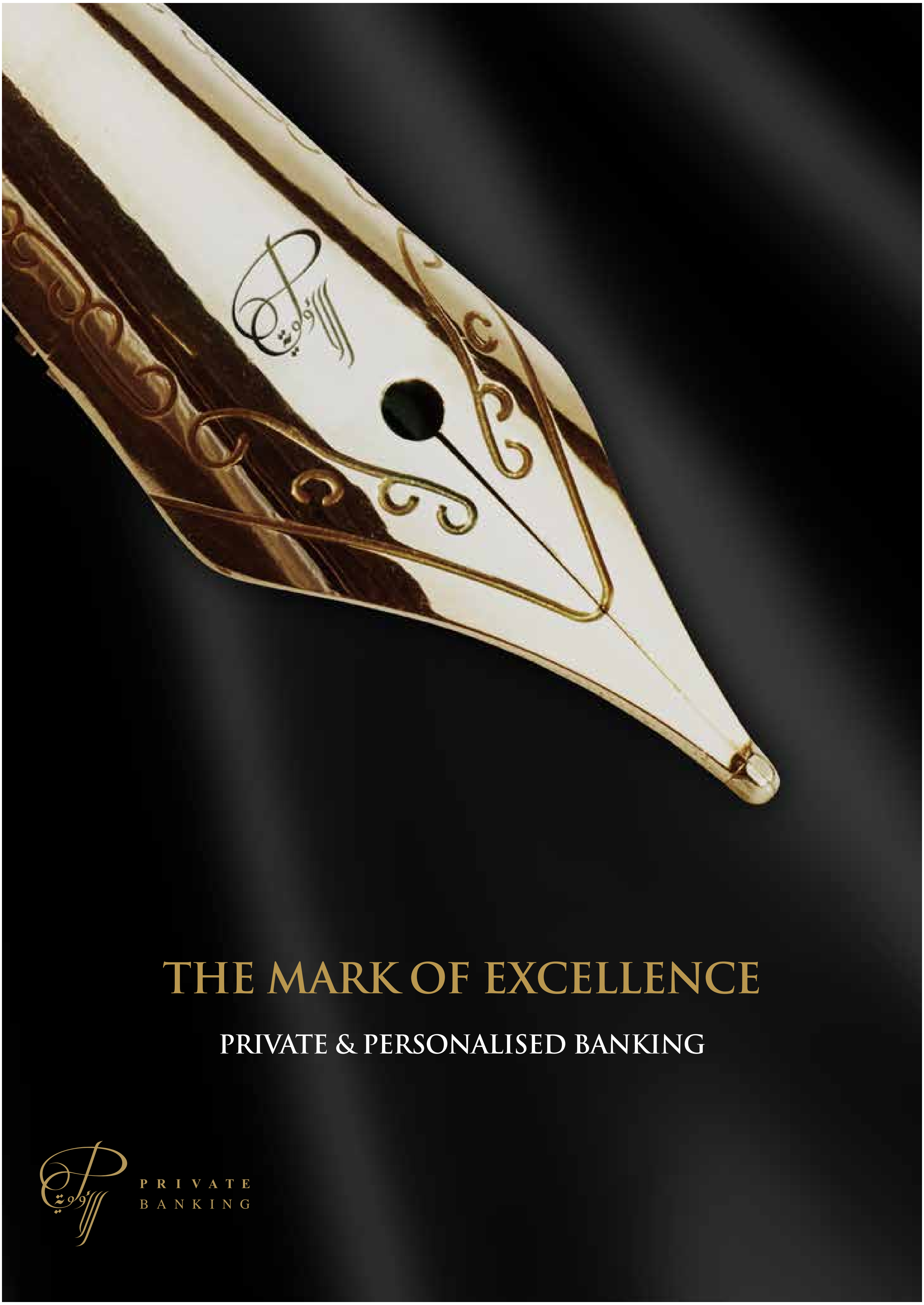
The launch of "Walaa Baytik", the Bank's loyalty rewards program for prepaid and credit card holders rewards clients with loyalty points when utilizing their cards, which can be redeemed for attractive and highly-demanded products and services, such as air-miles and cash-back. Moreover, clients can also travel the world with a host of benefits offered by our Signature, Gold and Classic Credit Cards, including access to over 1,000 airport VIP lounges worldwide exclusive to signature cardholders. Additionally, cardholders can avail of attractive discounts from our retail partners and service providers. Our credit cards received the "Outstanding Performance for Credit Cards Issued in Bahrain 2017" award from VISA for their superior market appeal.

In line with its growing popularity as a major credit card issuer, the Bank has introduced two new products to its cards suite, Visa Platinum "SmartPay" credit card and a prepaid card called "WorldPay". Our "SmartPay" card provides cardholders with a flexible credit solution by offering them a reliable way to manage their credit card payments in an easy payment plan ranging from 1 to 36 months. On the other hand, our Platinum "WorldPay" card offers our clients a global prepaid solution without worrying about the extra mark-up fees and withdrawal charges, making it a free and secure payment companion with a host of rewards and benefits.

Our array of financial products cater to all customer needs and aspirations; whether it's owning a dream home through our flexible real estate finance solutions or purchasing a new car with our auto murabaha product, our customer needs are addressed in personalized financing solutions. Additionally, our award winning "Tamweely" personal finance, a first of its kind Shari'a compliant Tawarruq facility, enables our clients to address all their other needs. Structured as an international commodity murabaha (the commodity in this case being palm oil purchased from the Malaysia Bourse through an international brokerage partner), Tamweely allows our clients to experience every step of the Tawarruq process in real time. It was recognized as the "Best Personal Finance" and "Best New Retail Financial Product" at the CPI Financials Banker Middle East Product Awards Bahrain 2014.

The Mazaya Programme is a social housing finance scheme offered by KFH-Bahrain in partnership with the Ministry of Housing. It gives beneficiaries the opportunity to own their dream homes through a real estate finance facility subsidized by the Government of Bahrain. This programme, which is in line with the Bank's commitment to social responsibility, enables us to assist the Government in meeting the growing housing demands of the country.

KFH-Bahrain's retail branches are strategically located for customer convenience and enable us to serve our clients throughout the Kingdom. In addition, every branch includes state of- the-art instant cash and cheque deposit ATMs to further enhance the customer experience. Our ATM network is continuously upgraded with new customized features and locations, such as the implementation of Chinese language in our Dragon Mall ATMs, which allow us to appeal to our Chinese clientele.


THE MARK OF EXCELLENCE
PRIVATE & PERSONALISED BANKING
PRIVATE
BANKING

PRIVATE BANKING

At Private Banking, we work to make the banking needs and objectives of our clients our first priority. Delivered by a dedicated team of highly experienced relationship managers, KFH-Bahrain Private Banking proudly offers its clients Shari'a compliant and personalized banking services.

The Advantages of Private Banking

At Private Banking our number one priority is to keep the client satisfied at all times. By capitalizing on the full range of the Bank's resources and tailoring solutions to suit individual needs with ease and flexibility while ensuring that we maintain transparency in all our offerings and preserve the values of Islamic Banking.

Private Services

In addition to a full range of products, the advantages of the Private Banking relationship extends to a host of selective features that ensures the needs of our Private clients come first in today's fast-paced world. Private Banking clients are offered a multitude of service enhancements and Personalized care, which includes several premium benefits.

Call Accounts

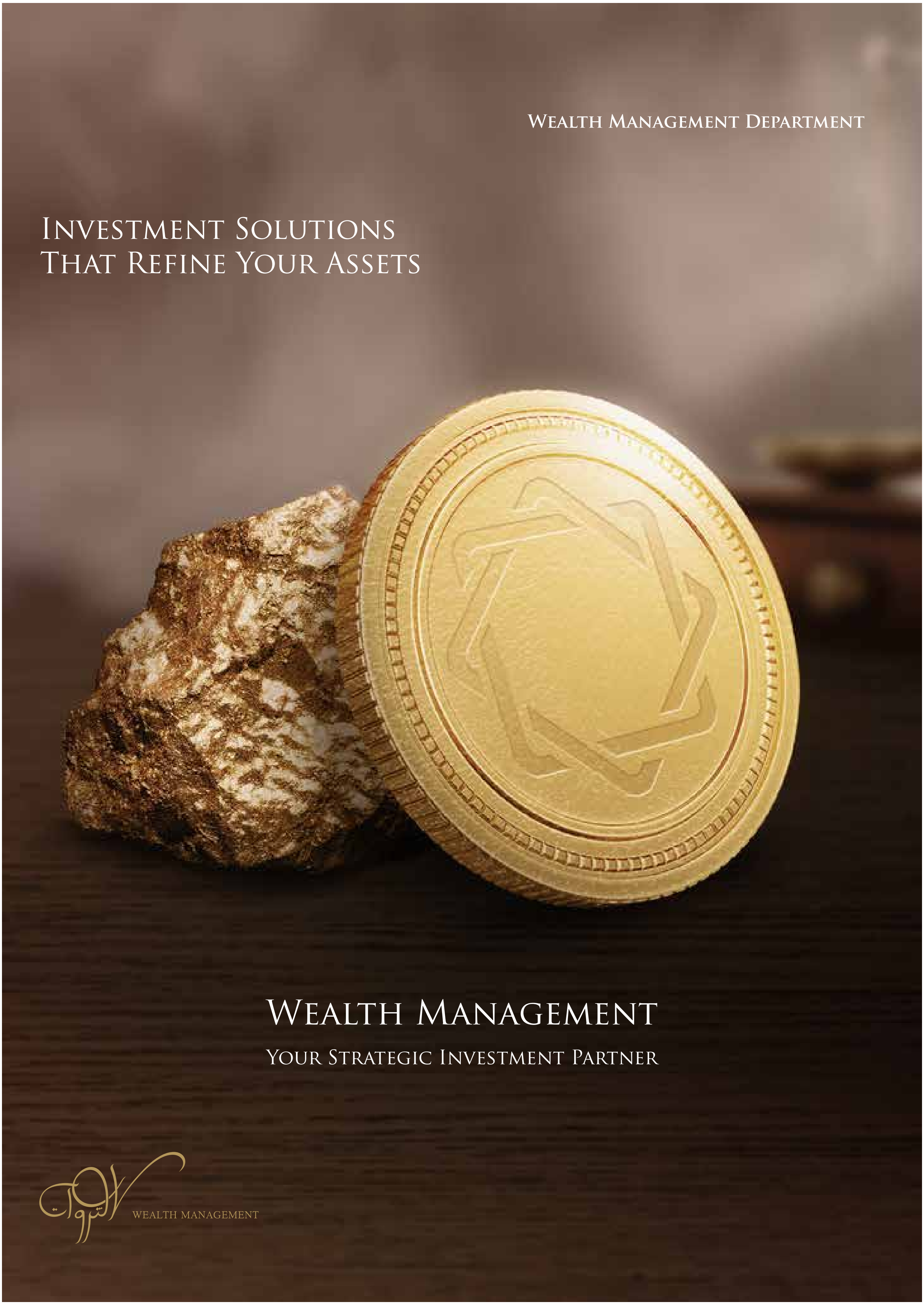
Based on the Islamic Investment Agency principle call accounts provide a solution that combines the benefit of savings and current accounts into one product. The call account calculates the realized profit on daily basis and distribute the realized profits on a monthly basis to investors. Clients can open a call account in Bahraini dinars and / or US dollars.

Wakala Investment Accounts

Wakala Investments accounts expands the choice of financial tools that can be invested in Bahraini dinars and/or US dollars. Realized profits are distributed to clients' accounts on a monthly basis

Wakala Flexi Investment Accounts

The new Flexi Wakala Investment accounts gives KFH-Bahrain clients the flexibility to withdraw up to 20% of the investment amount during the investment period. Clients can invest in Bahraini dinars and/or US dollars. Realized profits are distributed to the clients' accounts at maturity.


Wealth Management Department
Investment Solutions
That Refine Your Assets
Wealth Management
Your Strategic Investment Partner
WEALTH MANAGEMENT

WEALTH MANAGEMENT

During 2020, KFH-Bahrain's Wealth Management continued to grow its assets-under-management generating both scale and track record with its high net worth client base.

We continue to add to the unique suite of products and services across all major classes globally, catering to our valued clients risk apettite and liquidity needs.

With a clear understanding of evolving market requirements, wealth management provides objective investment advisory services and best in class portfolio management services across all asset classes. These include strategic investment management solutions that deliver results aimed at exceeding clients' expectations.

Strategic asset allocation, diversification, and a disciplined approach are crucial to preserve and grow clients' wealth. Over the past 5 years, the department has successfully developed a unique suite of products and services that are in line with clients' return expectations, liquidity needs, and risk profiles. The year 2020 witnessed the launch of a Securitization Program where a Series of Mudaraba Sukuk can be issued against a select pool of financing portfolio This provides an opportunity for clients to diversify their portfolio allocation strategy and enhance their risk-adjusted returns by having exposure to a combination of assets and becoming the ultimate beneficiaries of the financing portfolio.

The department has also developed innovative solutions for clients, giving them access to short-term lombard financing against their portfolio without interrupting their asset allocation and long-term investment strategy.

The Wealth Management department provides a one-stop shop for clients with unique products and services across all major asset classes, enabling them to benefit from investment diversification. The products include Sukuk, Asset-back Securities, Islamic Margin Finance, Restricted Investment Accounts (RIA), Lombard Finance, and Operational & Fixed Deposit Accounts. In addition, the department collaborates with the Bank's partner, KFH Capital, to give investors access to unique investment opportunities such as income generating Real Estate, and other alternative investments globally.

CORPORATE & SME BANKING

Corporate & SME Banking is keen to develop long term relationships/ partnerships with its clients and devise relevant financing and banking services that fulfill the client needs.

KFH–Bahrain continues to support the corporate sector of the country, aligning its growth targets with the Kingdom's continuous development and progress. Leveraging its expertise in a broad range of market sectors, Corporate & SME Banking is working diligently to serve the financing needs of its existing clients and attracting new clients aiming towards diversifying its portfolio, and improving the quality of its assets.

Corporate & SME Banking comprehensive knowledge of business trends, current market challenges and the unique characteristics and requirements of each sector, provide a solid foundation to capitalize on new opportunities. Accordingly, Corporate & SME Banking remains focused on introducing innovative new financing products that cater to evolving market needs. This year Corporate & SME banking has introduced its new Cashline product that avails Shari'a compliant funding instantly for its existing Corporate & SME clients to fulfill their immediate liquidity requirements.

KFH-Bahrain has set its strategic direction towards fintech and digitalization. KFH has launched its first version of Corporate Jazeel application which provides banking transaction services that fulfill corporate needs effectively and efficiently in a modernized way. KFH-Bahrain will continue developing this application with added services during 2021 to enhance the quality and the effectiveness of the Corporate & SME banking services.

Through its strengthened partnership with Tamkeen, the Corporate & SME Banking continues to provide effective financing solutions for Small and Medium Enterprises (SMEs) and is extending support to both SMEs and large corporate segments, enabling them to reach new levels of production and profitability.

Mindful of current market conditions and macroeconomic changes, the Corporate & SME Banking remains committed to working closely with its clients to ensure a firm understanding of their changing needs and requirements. Corporate & SME Banking is keen to develop long term relationships/partnerships with its clients and devise relevant financing and banking services that fulfill the client needs.

TREASURY & CAPITAL MARKETS

In 2020 KFH-Bahrain continued to grow its overall sovereign sukuk portfolio by recording a sizeable 21.6% increase year-on-year, which supported the Bank's profitability and liquidity profile.

Keen on participating in the country's sovereign and institutional funding requirements, the Bank's Treasury & Capital Markets Department continued to grow its sovereign sukuk holding with a notable rise of 21.6% year-on-year in terms of size, supporting KFH-Bahrain's profitability and liquidity profile amid the challenging environment posed by the pandemic and lower oil prices.

On the syndication side, the department successfully arranged and participated in a BHD 150 million syndication for Eskan Bank. Existing participations in large financing transactions for Bahrain GREs were maintained, together with new disbursements the Department's financing portfolio grew by 29.9%.

Overseeing KFH-Bahrain's asset and liability management function, the Treasury & Capital Markets Department manages a number of institutional relationships with entities of FI or quasi-sovereign nature. Responsible for the management of KFH-Bahrain's treasury lines (within the GCC and beyond) and financial institution counterparty network, the Department counts as a mission the organization of the Bank's institutional funding in an optimized, adequate and efficient manner (while considering liquidity ratio requirements).

Finally, the Treasury & Capital Markets Department maintained a strong communication line with KFH's parent as well as with sister companies at the Group level, particularly through a number of KFH Group Treasurers Committee Meetings held throughout 2020.

INVESTMENTS

The Bank's Investment Department continued to monitor owned and managed Investment assets with a view to realise these in an orderly manner.

COVID-19 has an unprecedented effect on global economies with business confined to remote contacts. The extent of the impact on the portfolio will depend on future developments, including the duration and spread of the outbreak and related advisories and restrictions on the financial markets and the overall economy, all of which are highly uncertain and cannot be predicted.

Despite the challenges indicated above, the Bank continued to focus on realization of the investment portfolio owned and managed by the Bank on behalf of the Group.

In line with its strategy to redeploy funds into core banking and strengthen the Bank's balance sheet, KFH-Bahrain continued to exit its non-core investments wherever possible. These efforts began in 2017 following the transfer of the majority of its real estate investment assets to an entity owned by KFH-Kuwait, which resulted in a reduction of the Bank's direct real estate exposure and optimized the Bank's capital structure, enabling it to focus on growing its core banking activities.

Following the asset transfer, the Bank continued to manage the portfolio and assisted the portfolio companies in successfully concluding a diverse range of deals - Social Housing Project in Diyar Al Muharraq and the sale of waterfront villas in Durrat Al Bahrain. The Bank also advised on and supervised activities of its real estate project companies during the year.

Key Owned Assets

Ishbiliya Village

Ishbiliya Village is located in close proximity to downtown Manama. Featuring over 240 villas, it offers prime land at competitive prices to meet the demands of Bahrain's housing needs for the local population. The Bank is continuously exploring development and realization options in light of the changing market conditions.

Jordan Portfolio

KFH-Jordan is an investment company established in 2008 in the Hashemite Kingdom of Jordan. Its subsidiaries and associate companies own a diverse real estate portfolio, which ranges from plots of land throughout Jordan to high-end mixed-use properties in prime locations in Amman. The company is focusing on controlled realization strategy for the assets within the portfolio.

RISK MANAGEMENT

KFH-Bahrain's Approach to Risk Management

The Board of Directors (BoD) manage risk by setting a comprehensive limit structure that aligns business and risk strategies to achieve targeted risk-adjusted returns. The Board Risk Committee (BRC) meets regularly to oversee the implementation of the BoD's approved risk management strategies, policies, procedures, risk profile and risk appetite. Through the Asset and Liability Committee (ALCO), the Bank's senior management develops and implements appropriate risk management and business processes to monitor and manage risks within the BoD-approved risk management framework.

Risk Management Group dedicates considerable efforts into gathering, monitoring and enhancing data into the Bank's systems to produce timely and meaningful snapshots of the Bank's risk profile in order to support the ALCO, the BRC and the BoD to take sound business and operating decisions by optimizing risk and return, while meeting regulatory requirements.

Risk Management Group believes that a robust, holistic and comprehensively implemented framework is necessary to safeguard our stakeholders' interests and to achieve tangible results. The Bank takes a prudent approach to risk management commensurate with the size and complexity of the Bank. Risk Management Group pursues strategies that build long-term shareholder value, while optimizing economic capital and meeting regulatory requirements. The Bank's risk management framework facilitates Risk Management Group to proactively manage risks throughout the life cycle of a financial transaction across the Bank's entire portfolio.

The Bank encourages, cultivates and disseminates a culture of risk management across its business, control, and support units. Business units are the first line of control and are the front line operators of risk management strategies, policies, procedures and practices. Support and control units are the second line of control for the risks that are taken by business units within the Bank's risk appetite. Risk Management Group provides various tools and an appropriate framework for business and support units to manage risks within their respective areas. The audit function is responsible for independently assessing and evaluating controls and the departments' adherence to the Bank's BoD-approved risk management strategies, policies and procedures.

Sophisticated and prudent risk models are periodically developed and refined to evaluate risks taken by the Bank and to project the impact of these risks on the Bank's business and operational goals.

Risk Management Group believes that a robust, holistic and comprehensively implemented framework is necessary to safeguard our stakeholders' interests

Tools such as rating systems, stress test models and frameworks, the Internal Capital Adequacy and Assessment Program (ICAAP) and others are essential in identifying, measuring and managing risk across the Bank's portfolio. In addition, the Bank uses models for Fund Transfer Pricing (FTP) and risk-adjusted performance measurement tools, including Risk Adjusted Return on Capital (RAROC), as vital elements for optimizing risk-adjusted returns.

Risk Management Group continues to focus on improving internal credit processes, enforcing stricter risk and credit eligibility requirements, diversifying the Bank's financing and credit portfolios, implementing innovative initiatives to align our clients' interests with the Bank's, ensuring closer and more regular monitoring of clients by business units and others. Risk Management Group's philosophy towards remedial management is to work closely with clients to reach a mutually beneficial outcome.

During 2020, Risk Management Group refined and enhanced its risk management framework and processes to identify, monitor, and manage risks more effectively. In addition, Risk Management Group expanded to include vital control areas of the Bank including Anti-Financial Crimes, Information Security and Business Continuity Planning in line with best practices and to ensure consolidated risk measurement and control. The Bank has completed a Central Bank of Bahrain (CBB) mandated independent review of the Bank's risk management function to assess adherence to the CBB Rulebook, in addition to a comprehensive internal and external validation exercise of the Bank's IFRS 9 methodology.

In response to the COVID-19 pandemic that adversely impacted local and regional economies, Risk Management Group prioritized preserving the Bank's asset quality. In this context, to mitigate against the impact of the COVID-19 pandemic, Risk Management Group established a temporary COVID-19 related policy framework, in line with the concessions granted by the Government of Bahrain. This framework stipulates regular discussion of impacted accounts to assess appropriate remedial strategies within the Bank's Financing Monitoring Task Force, conducting a dynamic and comprehensive COVID-19 impact assessment on the Bank's financing portfolio, proactive restructuring of impacted accounts, developing and implementing a risk-based Fast-Track Approval Process to expedite low credit risk restructurings and optimizing of the Bank's cost of risk.

CORPORATE SOCIAL RESPONSIBILITY

At KFH-Bahrain, Corporate Social Responsibility (CSR) and socio-economic development go hand in hand. Through its CSR strategy, the Bank provides practical and financial support to initiatives that contribute to the Kingdom's prosperity and enhance quality of life for its people.

The strategy is in line with the Bank's ethical values and is built around the pillars of Islamic banking and finance, sporting, and community. During 2020, although the year was difficult due to the COVID-19 virus outbreak, the Bank always showed its support to deserving causes, including charities, educational and cultural initiatives, and social events. In addition, it sponsored and participated in prominent banking-related events that promote the development of the financial sector and helped drive economic progress.

Some of our CSR activities during the year include:

Supporting Islamic Banking and Finance

- Sponsored Virtual ePay Summit
- Sponsored BIBF Islamic Finance Awareness

Developing Tomorrow's Sporting Champions

- Sponsored His Majesty the King's Football Cup & Nasser Bin Hamad Premier League
- Sponsorship of Al Najma Club for the GCC Handball Tournament 2020
- Sponsored the Bahrain's Football National Team Rewarding for Winning the 24th Arabian Gulf Cup
- Sponsored Bahrain Handball National Team in the 2021 World Cup

Promoting Health, Education and Leadership

- Sponsored the Shaikha Hessa Girls School.
- Sponsorship of Sh. Ebrahim bin Mohammed Cultural Center
- Sponsored the Kuwait National Day event, hosted by the Embassy of Kuwait
- Sponsored Bahrain Bayan School
- Supreme Council of Women
- Sponsored International Quran Recitation
- Sponsored Falak Unreasonable Thinking Summit 2020
- Sponsored The Euromoney Bahrain Conference (Associate Sponsorship Package)
- Bahrain Society for Training & Development Sponsorship
- Sponsored the Khalid Bin Hamad Innovation in Artificial Intelligence Competition
- Sponsored Bahrain FinTech Accelerastor Proposition

Community Support

- Sponsored Bahrain International Airshow
- Sponsored the Bahrain Food Festival 2020
- Sponsored of Sh. Ebrahim bin Mohammed Cultural Center
- Sponsored Smart Investor Program Sponsorship
- Sponsored Team Wheels of Arabia
- Sponsored Ministry of Health Lose your Weight Competition
- Sponsored the Bahrain International Airshow 2020
- Sponsored Association of Engineering Offices
- Sponsored Bahrain Cancer Society
- Sponsored Supreme Council for Youth & Sports
- Sponsored Afnan Zayani – Ramadan Show

Fatwa & Shari'a Supervisory Board Report

In the Name of Allah Most Gracious Most Merciful Praise be to Allah, Almighty, and Prayers and Peace be upon Prophet Mohammed, his family and Companions

To: The Shareholders of Kuwait Finance House-Bahrain
Al Salam Alaikum Wa Rahmatu Allah Wa Barakatuh

In compliance with the letter of appointment, we are required to submit the following report:
We have supervised the products and contracts relating the transactions and applications introduced by Kuwait Finance House – Bahrain (the Bank) during the period ended 31st Dec 2020. We have performed our supervision to form an opinion as to whether the Bank has complied with the Rules and Principles of Islamic Shari'a, as well as Fatwas, rulings and guidelines issued by us, Shari'a related policies and procedures of the Bank, AAOIFI Shari'a Standards, relevant rulings of the Centralized Shari'a Supervisory Board (CSSB), the Shari'a Governance (SG Module), resolutions and directives issued by the Central Bank of Bahrain (CBB).

Responsibility of Management

The Bank management is responsible for ensuring that the Bank conducts its business in accordance with the Rules and Principles of Islamic Shari'a. It is our responsibility to form an independent opinion based on our review of the operations of the Bank and preparing a report for you.

Scope of work of the Fatwa and Shari'a Supervisory Board

Through the periodic reports provided by the head of Internal Shari'a Audit Department and the head of Shari'a Advisory Department, The Fatwa and Shari'a Supervisory Board (The Board) confirmed that the Bank did not violate the Provisions, Rules and Principles of Islamic Shari'a. The reports contained the results of reviewed, approved contracts and agreements and the results of the Bank operations reviewed on a random sample selection in accordance to the annual audit plan for the Internal Shari'a Audit Department which was approved by The Board including the field visits, supervision of the workflow from Shari'a viewpoint and implementation of Fatwa and decisions issued by us.

We planned and performed our supervision to obtain all the information and explanations, which we considered necessary to provide us with sufficient evidence to give reasonable assurance that the Bank did not violate the Rules and Principles of Islamic Shari'a.

In our opinion

1. The contracts, transactions, and dealings entered into by the Bank during the year ended 31st December 2020 that we have reviewed are in compliance with the Rules and Principles of Islamic Shari'a.
2. The allocation of profits and charging of losses relating to investment accounts conform to the basis that had been approved by us in accordance with the Rules and Principles of Islamic Shari'a.
3. All earnings that have been realized from sources or by means of prohibited by the Rules and Principles of Islamic Shari'a have been set aside in an independent account and disposed of to charitable causes;
4. The calculation of Zakat is in compliance with the Rules and Principles of Islamic Shari'a; and
5. The Bank has committed to the Shari'a Principles, Fatawa and Directions given by us.

The Fatwa and Shari'a Supervisory Board approved the report based on the periodic reports provided by the Internal Shari'a Audit and Shari'a Advisory Departments.

The Fatwa and Shari'a Supervisory Board would raise the sincere thanks and appreciation to the senior management, the departments and the staff of Kuwait Finance House - Bahrain for their cooperation and commitment to the Board's decisions and guidelines, and asks Allah Almighty to bring them success and Rashad.

We pray to Allah Almighty to guide us to the righteous path.

Sh. Dr. Sayyed Mohammad Al-Sayyed Abdul Razzaq Al-Tabtaba'e
Chairman
Fatwa and Shari'a Supervisory Board

Sh. Dr. Mubarak Al-Harbi
Vice Chairman
Fatwa and Shari'a Supervisory Board

Sh. Dr. Anwar Abdulsalam
Member
Fatwa and Shari'a Supervisory Board

Independent Auditors' Report

to the Shareholders of Kuwait Finance House (Bahrain) B.S.C. (c)

Report on the Audit of the Consolidated Financial Statements

Opinion

We have audited the accompanying consolidated financial statements of Kuwait Finance House (Bahrain) B.S.C. (c) "the Bank" and its subsidiaries (together "the Group") which comprise the consolidated statement of financial position as at 31 December 2020 and the related consolidated statements of income, cash flows, changes in owners' equity and changes in off-balance sheet equity of investment account holders 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 2020, and the consolidated results of the operations, its cash flows, changes in owners' equity and changes in off-balance sheet equity of investment account holders for the year then ended in accordance with Financial Accounting Standards ("FAS") issued by the Accounting and Auditing Organisation for Islamic Financial Institutions ["AAOIFI"] as modified by the Central Bank of Bahrain ("CBB") ("FAS issued by AAOIFI as modified by CBB")

In our opinion, the Bank has also complied with the Islamic Shari'a Principles and Rules as determined by the Shari'a Supervisory Board of the Bank during the year under audit.

Basis for opinion

We conducted our audit in accordance with Auditing Standards for Islamic Financial Institutions (ASIFI) issued by AAOIFI. 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 AAOIFI's Code of Ethics for Accountants and Auditors of Islamic Financial Institutions, and we have fulfilled our other ethical responsibilities in accordance with this Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Other information included in the Group's 2020 Annual Report

Other information consists of the information included in the 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 mistatement, of this other information, we are required to report the fact. We have nothing to report in this regard.

Responsibilities of the Board of Directors for the consolidated financial statements

These consolidated financial statements and the Group's undertaking to operate in accordance with Islamic Shari'a Rules and Principles are the responsibility of the Bank's Board of Directors.

The Board of Directors is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with FAS issued by AAOIFI as modified by CBB 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 assesing 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 ASIFI issued by AAOIFI 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.

As part of an audit in accordance with ASIFI issued by AAOIFI, we exercise professional judgement 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 audit committee regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

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

Report on Other Regulatory Requirements

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

a) the Bank has maintained proper accounting records and the consolidated financial statements are in agreement therewith;
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 2 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 2020 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 management in response to all our requests.

The partner incharge of the audit resulting in this independent auditors report is Kazim Merchant.

Partner's registration no. 244
18 February 2021
Manama, Kingdom of Bahrain

CONSOLIDATED FINANCIAL STATEMENTS AND AUDIT REPORT

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

At 31 December 2020

	Note	2020 BD 000	2019 BD 000
ASSETS			
Cash and balances with banks and Central Bank of Bahrain	7	**61,277**	99,535
Due from banks	8	**123,590**	115,216
Financing contracts	9	**1,005,228**	913,907
Investments	10	**6,861**	6,156
Investment in sukuk	11	**324,739**	270,277
Investment in associate	12	**6,889**	8,461
Receivables and other assets	14	**223,377**	247,328
Premises and equipment		**3,703**	9,553
TOTAL ASSETS		**1,755,664**	1,670,433
LIABILITIES, EQUITY OF INVESTMENT ACCOUNT HOLDERS AND OWNERS' EQUITY			
LIABILITIES			
Customers' current accounts		**133,114**	128,258
Due to banks	15	**108,798**	101,783
Due to non-banks		**364,048**	222,965
Other liabilities	17	**16,298**	15,399
TOTAL LIABILITIES		**622,258**	468,405
EQUITY OF INVESTMENT ACCOUNT HOLDERS			
Banks		**182,948**	159,699
Non-banks and individuals	18	**783,229**	848,670
TOTAL EQUITY OF INVESTMENT ACCOUNT HOLDERS		**966,177**	1,008,369
OWNERS' EQUITY			
Equity attributable to shareholders of the Parent			
Share capital	19	**132,519**	132,519
Statutory reserve		**25,640**	24,115
Fair value through equity reserve		**1,018**	324
Proposed dividend		**-**	22,517
Retained earnings		**311**	3,587
		159,488	183,062
Non-controlling shareholders		**7,741**	10,597
		167,229	193,659
TOTAL LIABILITIES, EQUITY OF INVESTMENT ACCOUNT HOLDERS AND OWNERS' EQUITY		**1,755,664**	1,670,433
OFF-BALANCE SHEET			
EQUITY OF INVESTMENT ACCOUNT HOLDERS		**136,710**	135,145
CONTINGENT LIABILITIES AND COMMITMENTS	21	**75,649**	108,796

Hamad Abdul Mohsen Al-Marzouq
Chairman of the
Board of Directors

Abdulhakeem Yaqoub Alkhayyat
Managing Director and
Chief Executive Officer

The attached notes 1 to 40 form part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF INCOME

For the year ended 31 December 2020

	Note	2020 BD 000	2019 BD 000
Income from financing contracts	23	**59,521**	63,365
Income from investments	24	**2,065**	1,720
Income from sukuk		**14,855**	20,200
Share of loss from associate		**(463)**	(164)
OPERATING INCOME		**75,978**	85,121
Return on equity of investment account holders (wakala)		**(18,045)**	(22,017)
Return on equity of investment account holders (mudaraba) before Group's share as mudarib		**(12,381)**	(9,828)
Group's share as mudarib	18	**10,346**	7,945
Return on equity of investment account holders (mudaraba) after Group's share as mudarib		**(2,035)**	(1,883)
Profit on due to banks and non-banks	28	**(15,038)**	(12,490)
NET OPERATING INCOME		**40,860**	48,731
Staff costs		**11,933**	13,235
Depreciation		**1,493**	1,292
Provisions - net	26	**1,633**	(695)
Other expenses	27	**10,564**	9,889
TOTAL OPERATING EXPENSES		**25,623**	23,721
NET INCOME FOR THE YEAR		**15,237**	25,010
Attributable to:			
Shareholders of the Parent		**15,246**	25,019
Non-controlling shareholders		**(9)**	(9)
		15,237	25,010

Hamad Abdul Mohsen Al-Marzouq
Chairman of the
Board of Directors

Abdulhakeem Yaqoub Alkhayyat
Managing Director and
Chief Executive Officer

The attached notes 1 to 40 form part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended 31 December 2020

	Note	2020 BD 000	2019 BD 000
OPERATING ACTIVITIES			
Net income for the year		**15,237**	25,010
Adjustments for:			
Share of loss from associate		**463**	164
Net (gain) on sale of investments	24	**(359)**	-
Net unrealised (gain) on investments	24	**-**	(198)
Net gain on sale of premises and equipment		**-**	(5)
Foreign exchange gain	24	**(413)**	(839)
Depreciation		**1,493**	1,292
Provisions - net	26	**6,166**	(631)
Operating income before changes in operating assets and liabilities		**22,587**	24,793
Changes in operating assets and liabilities:			
Mandatory reserve with Central Bank of Bahrain		**2,966**	(605)
Due from banks		**454**	4,041
Financing contracts		**(137,084)**	(38,796)
Receivables and other assets		**18,502**	(1,613)
Financial support from government		**1,460**	-
Customers' current accounts		**4,856**	510
Due to banks		**7,015**	(13,944)
Due to non-banks		**141,083**	61,000
Other liabilities		**137**	1,619
Net cash flows from operating activities		**61,976**	37,005
INVESTING ACTIVITIES			
Disposal of investments - net		**3,452**	-
Purchase of sukuk - net		**(54,452)**	(226,066)
Sale proceeds from disposal of sukuk		**-**	178,384
Purchase of premises and equipment - net		**(463)**	(885)
Proceeds from disposal of a subsidiary		**4,760**	-
Net cash flows used in investing activities		**(46,703)**	(48,567)
FINANCING ACTIVITY			
Net movement in equity of investment account holders		**(42,192)**	105,554
Net cash flows (used) from financing activity		**(42,192)**	105,554
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS		**(26,919)**	93,992
Cash and cash equivalents at 1 January		**182,693**	88,701
CASH AND CASH EQUIVALENTS AT 31 DECEMBER	29	**155,774**	182,693

The attached notes 1 to 40 form part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN OWNERS' EQUITY

For the year ended 31 December 2020

	Equity attributable to shareholders of the Parent							
	Share capital BD 000	Statutory reserve BD 000	Fair value through equity reserve BD 000	Retained earnings BD 000	Proposed dividend BD 000	Total BD 000	Non -controlling shareholders BD 000	Total owners' equity BD 000
Balance at 1 January 2020	132,519	24,115	324	3,587	22,517	183,062	10,597	193,659
Net income for the year	-	-	-	15,246	-	15,246	(9)	15,237
Other comprehensive income for the year (note 20)	-	-	694	-	-	694	-	694
Total comprehensive income for the year	-	-	694	15,246	-	15,940	(9)	15,931
Dividend payout	-	-	-	-	(22,517)	(22,517)	-	(22,517)
Transfer to statutory reserve	-	1,525	-	(1,525)	-		-	-
Recognition of modification loss net of government grant (note 39)	-	-	-	(16,997)	-	(16,997)	-	(16,997)
Net movement in share of non-controlling shareholders	-	-	-	-	-	-	(2,847)	(2,847)
Balance at 31 December 2020	**132,519**	**25,640**	**1,018**	**311**	**-**	**159,488**	**7,741**	**167,229**
Balance at 1 January 2019	132,519	21,613	170	3,587	16,608	174,497	7,766	182,263
Net income for the year	-	-	-	25,019	-	25,019	(9)	25,010
Other comprehensive income for the year (note 20)	-	-	154	-	-	154	-	154
Total comprehensive income for the year	-	-	154	25,019	-	25,173	(9)	25,164
Dividend payout	-	-	-	-	(16,608)	(16,608)	-	(16,608)
Transfer to statutory reserve	-	2,502	-	(2,502)	-	-	-	-
Proposed dividend (note 19)	-	-	-	(22,517)	22,517	-	-	-
Net movement in share of non-controlling shareholders	-	-	-	-	-	-	2,840	2,840
Balance at 31 December 2019	132,519	24,115	324	3,587	22,517	183,062	10,597	193,659

The attached notes 1 to 40 form part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN OFF-BALANCE SHEET EQUITY OF INVESTMENT ACCOUNT HOLDERS

For the year ended 31 December 2020

	Balance at 1 January 2020	**Additional investments**	**Gross income**	**Mudarib share**	**Withdrawals/ distributions**	**Balance at 31 December 2020**
	BD 000	**BD 000**	**BD 000**	**BD 000**	**BD 000**	**BD 000**
Investment in Murabaha	**135,145**	**98,470**	**9,963**	**(1,887)**	**(104,981)**	**136,710**

	Balance at 1 January 2019	Additional investments	Gross income	Mudarib share	Withdrawals / distributions	Balance at 31 December 2019
	BD 000	BD 000	BD 000	BD 000	BD 000	BD 000
Investment in Murabaha	135,110	104,525	9,654	(2,035)	(112,109)	135,145

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

1 CORPORATE INFORMATION AND ACTIVITIES

Kuwait Finance House (Bahrain) B.S.C. (c) (the "Bank") is a closed joint stock company incorporated in the Kingdom of Bahrain on 22 January 2002 under the Bahrain Commercial Companies Law No. 21/2001 and is registered with the Ministry of Industry and Commerce under commercial registration (CR) number 48128. The Bank is regulated and supervised by the Central Bank of Bahrain (the "CBB") and has an Islamic retail banking license. The Bank operates under Islamic principles and in accordance with all the relevant regulatory guidelines for Islamic banks issued by the CBB. The address of the Bank's registered office is World Trade Centre, road number 365, Building number 1B, Block 316, P.O. Box 2066, Manama, Kingdom of Bahrain.

The Bank offers a full range of Islamic banking services and products. The activities of the Bank include accepting Shari'a compliant money placements / deposits, managing Shari'a compliant profit sharing investment accounts, offering Shari'a compliant financing contracts, dealing in Shari'a compliant financial instruments as principal / agent, managing Shari'a compliant financial instruments and other activities permitted under the CBB's Regulated Islamic Banking Services as defined in the licensing framework.

The Bank is a wholly owned subsidiary of Kuwait Finance House K.S.C.P. (the "Ultimate Parent"), a public company incorporated in the State of Kuwait and listed at the Kuwait Stock Exchange. The Ultimate Parent is regulated and supervised by the Central Bank of Kuwait. The Bank's Shari'a Supervisory Board is entrusted to ensure the Group's adherence to Shari'a rules and principles in its transactions and activities.

During the year, the Bank disposed-off its investment in a subsidiary; Energy Central Utilities - Bahrain South Water Company B.S.C.. The income from disposal of the subsidiary is disclosed in note 24.

The Bank and its subsidiaries (together the "Group") operate in the Kingdom of Bahrain and Hashemite Kingdom of Jordan. The activities of the Bank's key subsidiaries are mentioned in note 5.

The Bank has nine branches (2019: nine), all operating in the Kingdom of Bahrain.

Impact of COVID-19

The outbreak of coronavirus ("COVID-19") pandemic across the globe has caused disruption to business and economic activities and uncertainties in the global economic environment. The fiscal and monetary authorities have announced several stimulus packages to the Bank's customers, which are in the process of implementation. The Bank has considered potential impacts of the current market volatility in the determination of the reported amounts of the Bank's financial and non-financial assets and are considered to represent management's best assessment based on current observable information. Markets, however, remain volatile and the recorded amounts remain sensitive to market fluctuations.

The consolidated financial statements were authorised for issue in accordance with a resolution of the Board of Directors passed on 11 February 2021.

2 BASIS OF PREPARATION

2.1 Accounting convention

The consolidated financial statements have been prepared under the historical cost basis, except for managed funds and equity securities that have been measured at fair value. The consolidated financial statements are presented in Bahraini Dinars ("BD") which is the functional and presentation currency of the Bank. All the values are rounded to the nearest BD thousand, unless otherwise indicated.

2.2 Statement of compliance

The consolidated financial statements of the Group have been prepared in accordance with applicable rules and regulations issued by the Central Bank of Bahrain ("CBB") including the recently issued CBB circulars on regulatory concessionary measures in response to COVID-19. These rules and regulations, in particular CBB circular OG/226/2020 dated 21 June 2020 and related CBB communications, require the adoption of all Financial Accounting Standards ("FAS") issued by the Accounting and Auditing Organisation of Islamic Financial Institutions (AAOIFI) with two exceptions which are set out below. In accordance with the AAOIFI framework, for matters not covered by FAS, the Group uses the requirements of the relevant International Financial Reporting Standards ("IFRS") issued by the International Accounting Standards Board ("IASB"). This framework is referred to as "FAS issued by AAOIFI".

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

2 BASIS OF PREPARATION (continued)

2.2 Statement of compliance (continued)

The two exceptions mentioned above are as follows:

(a) recognition of modification losses on financial assets arising from payment holidays provided to customers impacted by COVID-19 without charging additional profit, in equity instead of profit or loss as required by FAS issued by AAOIFI. Any other modification gain or loss on financial assets are recognised in accordance with the requirements of FAS issued by AAOIFI.

(b) recognition of financial assistance received from the government and / or regulators in response to its COVID-19 support measures that meets the government grant requirement, in equity instead of profit or loss. This will only be to the extent of any modification loss recorded in equity as a result of (a) above, and the balance amount to be recognised in profit or loss. Any other financial assistance is recognised in accordance with the relevant requirements of FAS issued by AAOIFI. Please refer note (39) for further details.

The above framework for basis of preparation of the consolidated financial statements is hereinafter referred to as 'FAS issued by AAOIFI as modified by CBB', which has been applied retrospectively and did not result in any change to the financial information reported for the comparative period.

2.3 Basis of consolidation

The consolidated financial statements comprise the financial statements of the Bank and its subsidiaries as at 31 December each year. The financial statements of the subsidiaries are prepared for the same reporting year as the Bank, using consistent accounting policies.

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

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

Share of non-controlling shareholders represents the portion of net income and net assets not held by the Group and are presented separately in the consolidated statement of income and within owners' equity in the consolidated statement of financial position, separately from the equity attributable to shareholders of the Parent. Transactions with the non-controlling interest are handled in the same way as transactions with external parties.

3 SIGNIFICANT ACCOUNTING JUDGMENTS AND ESTIMATES

The preparation of the Group's consolidated financial statements requires management to make judgments, estimates and assumptions that affect the amounts reported in the consolidated financial statements. The most significant uses of judgments and estimates are as follows:

3.1 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 a going concern basis.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

3 SIGNIFICANT ACCOUNTING JUDGMENTS AND ESTIMATES (continued)

3.2 Fair value of unquoted equity securities

Fair value is determined for each investment individually in accordance with the valuation policies set out in note 4.24 and note 32. Where the fair values of the Group's unquoted equity securities cannot be derived from an active market, they are derived using a variety of valuation techniques. Judgment by management is required to establish fair values through the use of appropriate valuation models, consideration of comparable assets, discount rates and the assumptions used to forecast cash flows.

3.3 Impairment provision against financing contracts

In determining impairment on receivables, judgment is required in the estimation of the amount and timing of future cash flows as well as an assessment of whether credit risk on the financial contract has increased significantly since initial recognition or the default has occured and incorporation of forward-looking information in the measurement of expected credit losses ("ECL").

3.4 Impairment of investments at fair value through equity

The Group treats investments carried at fair value through equity as impaired when there is a significant or prolonged decline in the fair value below its cost or where other objective evidence of impairment exists. The determination of what is 'significant' or 'prolonged' requires judgment. The Group evaluates factors, such as the historical share price volatility for comparable quoted equities and future cash flows and the discount factors for comparable unquoted equities.

3.5 Liquidity

The Group manages its liquidity through consideration of the maturity profile of its assets, liabilities and equity of investment account holders which is set out in the maturity profile in note 33 and liquidity risk disclosures in note 34.3. This requires judgment when determining the maturity of assets and liabilities with no specific maturities.

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies adopted in the preparation of the consolidated financial statements are set out below:

4.1 Adoption of new and amended standards and interpretations

FAS 31 Investment Agency (Al-Wakala Bi Al-Istithmar)

This standard defines the accounting principles and reporting requirements for investment agency (Al-Wakala Bi Al-Istithmar) transactions and instruments, in the hands of both the principal and the agent. This standard shall be effective beginning on or after 1 January 2021, with early adoption permitted. The standard requires the principal to evaluate the nature of the investment as either a) a pass-through investment or b) wakala venture.

In case of a pass-through investment approach, the principal shall initially recognize the assets underlying the wakala arrangement in its books of account applying the initial recognition principles as applicable in line with respective FAS. The principal may opt to apply the wakala venture approach if, and only if, the investment agency contract meets any of the conditions described below:

- The instrument is transferable; or
- The investment is made in a single asset (or pool of assets) where such asset(s) are subject to frequent changes throughout the term of the contract i.e. there are routine changes or replacements over the term of arrangement (unless it constitutes a business) at the discretion of the agent; or
- The role of the agent is not limited whereby the agent performs day-to-day asset management function and, where applicable, is also responsible for replacement of assets or recoveries against them.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

4.1 Adoption of new and amended standards and interpretations (continued)

FAS 31 Investment Agency (Al-Wakala Bi Al-Istithmar) (continued)

In case of wakala venture approach, an investment shall be accounted for in the books of the investor applying the "equity method of accounting"; where the investment shall be recognized initially at cost and subsequently shall be measured at the end of the financial period at carrying amount and shall be adjusted to include the investor's share in profit or loss of the wakala venture.

From the agent perspective, the standard requires that at inception of the transaction the agent shall recognize an agency arrangement under off-balance sheet approach since the agent does not control the related assets / business. However, there are exceptions to off-balance sheet approach where by virtue of additional considerations attached to the instrument based on investment agency may mandate the same to be accounted for as on-balance sheet. An agent may maintain multi-level investment arrangements. Under such arrangement, the Group is reinvesting Wakala funds into a secondary contract. Such secondary contracts shall be accounted for in line with the requirements of respective FAS in the books of the agent.

The Board of Directors decided to early adopt the standard with effect from the current year.

From the principal perspective, the Group opted to use Wakala venture approach instead of pass-through approach given the difficulties for the principal to identify in which assets the funds are invested in, and hence, the investment is accounted for applying the equity method of accounting.

The Group provides funds to other financial institutions under this Wakala venture arrangement where the Group is acting as principal. Those Wakala funds are mainly invested in money market placements. Below are the key terms of the WaKala agreements:

- The Muwakkil "Principal / Investor" appointed the Wakil «Agent» to invest its funds in the Wakil's treasury pool.
- The Muwakkil as principal shall bear all the risks associated with the acts of the Wakil as an agent, except those risks resulting from the Wakil's misconduct.
- The Muwakkil will not be entitled to withdraw its funds with the Wakil before the agreed maturity.
- The Wakil agreed to act as an agent of the Muwakkil on restricted limited agency, and the Wakil shall not have any authority to represent or bind the Muwakil, or purport to do so.
- The Wakil shall be entitled to the agency fees specified in the Wakil Offer in respect of each Investment Transaction.
- The Wakil is a trustee to the Wakala investment and shall safeguard and protect the wakala investment.
- The Wakil shall not utilize the Wakala amount for any other purpose, except as permitted by the Muwakkil.
- Upon the completion of the term for each wakala transaction, the Wakil will return the respective amount to the Muwakkil along with the profit.

From agent perspective, a multi-level investment arrangement is maintained, whereby the Group invests funds under the investment agency into unrestricted investment arrangements, under a separate contract and accounted for accordingly based on the relevant accounting standard.

The adoption of the above accounting standard did not have a material impact on the Bank's assets. However, the standard affects the classification of the Bank's Wakala based contracts previously accounted for as part of liabilities. Balances previously classified under liabilities are now been classified under equity of investment account holders as the Bank has invested funds received under wakala in its capacity as a Wakil into unrestricted investment accounts.

As part of the transitional provisions of FAS 31, the Group may choose not to apply this standard on existing transactions executed before 1 January 2020 and have an original contractual maturity before 31 December 2020. However, the Bank has decided to apply the standard on all transactions outstanding as of the year end and the corresponding previous year end. Accordingly, following wakala balances outstanding as at 31 December 2019 have also been reclassified from liabilities to unrestricted investment accounts along with the related profits paid on the wakala balances during the year ended 31 December 2019.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

4.1 Adoption of new and amended standards and interpretations (continued)

FAS 31 Investment Agency (Al-Wakala Bi Al-Istithmar) (continued)

	Audited 31 December 2019 BD 000
Due to banks – wakala based contracts	63,688
Due to non-banks – wakala based contracts	179,410
Subordinated wakala liability	96,011
	339,109

Refer to note 13 for detailed disclosures with relation to Wakala Funds.

FAS 33 Investment in sukuk, shares and similar instruments

This standard aims at setting out principles for the classification, recognition, measurement, presentation, and disclosure of investment in Sukuk, shares and other similar instruments of investments made by Islamic financial institution. The standard defines the key types of instruments of Shari'a compliant investments and the primary accounting treatments commensurate to the characteristic and business model of institution under which the investments are made, managed and held. This standard supersedes FAS 25 "Investment in Sukuk" and is effective beginning or after 1 January 2021 with early adoption permitted. For the purpose of this standard, each investment is to be categorized as one of the below investment categories depending on it nature:

- Monetary Debt-type instrument;
- Non-monetary Debt-type instrument;
- Equity-type instrument; and
- Other investment instruments.

Classification

Unless the irrevocable initial recognition choices provided below are exercised, the Group shall classify investments subject to this standard as subsequently measured at either (i) amortised cost, (ii) fair value through equity or (iii) fair value through income statement, on the basis of both the Group's business model for managing investments and the expected cash flow characteristics of the investment in line with the nature of the underlying Islamic contracts.

Investment in a monetary debt-type instrument, as it reflects a debt at the back-end, shall be initially classified and measured at cost, till the time the transaction at the back-end is executed, and at amortised cost thereafter.

Investment in a non-monetary debt-type instrument or other investment instrument, may be classified under any of the three categories (i) amortised cost, (ii) fair value through equity or (iii) fair value through income statement) depending on the Group's business model.

Investment in equity-type instrument is carried as investment at fair value through income statement unless the Group make an irrevocable classification choice at initial recognition to classify this as investment at fair value through equity. An investment held for trading purposes shall always fall in fair value through income statement classification.

Recognition and Initial measurement

All investment shall be initially recognized at their value plus transaction costs except for investments at fair value through income statement. Transaction costs relating to investments at fair value through income statement are charged to the consolidated statement of income when incurred. A regular way purchase of investments shall be recognized upon the transfer of control to investor.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

4.1 Adoption of new and amended standards and interpretations (continued)

FAS 33 Investment in sukuk, shares and similar instruments (continued)

Subsequent measurement

a) Investments at amortised cost

Investments carried at amortised cost shall be re-measured as such using the effective profit rate method. All gains or losses arising from the amortization process and those arising from de-recognition or impairment of the investment, are recognized in the consolidated statement of income. Investment carried at amortised cost shall be tested for impairment at each reporting period in accordance with FAS 30 “Impairment, credit losses and onerous commitments”.

b) Investments at fair value through income statement

Investment carried at fair value through income statement shall be re-measured at fair value at end of each reporting period. The resultant remeasurement gain or loss, if any being the difference between the carrying amount and the fair value shall be recognized in the consolidated statement of income.

c) Investments at fair value through equity

Investment carried at fair value through equity shall be re-measured at fair value at the end of each reporting period. The resultant re-measurement gain or loss, if any, being the difference between the carrying amount and the fair value shall be directly recognized in equity under “fair value through equity reserve”. Investment carried at fair value through equity shall be tested for impairment at each reporting period in accordance with FAS 30 “Impairment, credit losses and onerous commitments”.

Reclassification

When, and only when, the Group changes its business model for managing investments, it shall reclassify all affected financial assets prospectively from the reclassification date. In case of reclassification, the Group shall not restate any previously recognized gains, losses (including impairment gains or losses) or returns/ profits.

The Board of Directors decided to early adopt the standard with effect from the current year.

Except for investments in equity instruments and managed funds, all financial assets held by the Group are classified as investments in a monetary debt-type instruments and accordingly classified at amortised cost. With regard to the investments, the Group opted to make an irrevocable classification choice to classify them as investment at fair value through equity. Investment in managed funds is classified as investments at fair value through the statement of income

The adoption of the above accounting standard did not have a material impact on the consolidated financial statements.

FAS 34 Financial Reporting for Sukuk -holders

This standard prescribes the accounting principles and reporting requirements for underlying assets of a sukuk instrument. It requires the originator to prepare or cause to prepare financing reports as needed under this standard. This standard shall be effective from the financial periods beginning on or after 1 January 2021, with early adoption permitted.

The Board of Directors decided to early adopt the standard and concluded that the accounting standard does not have an impact on the Group’s consolidated financial statements as the Group does not have any sukuk issued.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

4.2 Financial contracts and impairment

a) Financial contracts

Financial contracts consist of balances with banks and the Central Bank of Bahrain, Due from banks, Sukuk, Murabaha financing (net of deferred profits), Ijarah Muntahia Bittamleek, Musharaka, other assets, financing commitments and financial guarantee contracts. Balances relating to these contracts are stated net of allowance for credit losses.

b) Impairment assessment

Impairment of financial assets

The Group applies three-stage approach to measure ECL on financial assets carried at amortised cost. Assets migrate through the following three stages based on the change in credit quality since initial recognition.

Stage 1: Twelve months ECL

For exposures where there has not been a Significant Increase in Credit Risk («SICR»), since initial recognition, a portion of the lifetime ECL associated with the probability of default events occurring within next twelve months is recognised.

Twelve-month ECL (Stage 1) is the portion of ECL that results from probable default events on a financial contract within twelve months after the reporting date.

Stage 2: Lifetime ECL – not credit impaired

For credit exposures where there has been a SICR since initial recognition but that are not credit impaired, a lifetime ECL is recognised.

Lifetime ECL (Stage 2) is a probability-weighted estimate of credit losses and is determined based on the difference between the present value of all cash shortfalls. The cash shortfall is the difference between all contractual cash flows that are due to the Group and the present value of the recoverable amount, for financial assets that are not credit-impaired at the reporting date.

Stage 3: Lifetime ECL – credit impaired

Financial contracts are assessed as credit impaired when one or more events that have a detrimental impact on the estimated future cash flows of that asset have occurred.

For Stage 3 financial contracts, the provisions for credit-impairment are determined based on the difference between the net carrying amount and the recoverable amount of the financial contract.

Credit-impaired financial assets

At each reporting date, the Group assesses whether financial assets carried at amortised cost are credit-impaired. Evidence that a financial asset is credit-impaired includes the following observable data:

- significant financial difficulty of the borrower or issuer;
- a breach of contract such as a default or past due event; and
- probability that the borrower will enter bankruptcy or other financial reorganization.

If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows. The carrying amount of the asset is reduced through the use of a provision account and the amount of the loss is recognised in the consolidated statement of income.

Financing contracts together with the associated provisions are written off when there is no realistic prospect of future recovery and collateral has been realised or has been transferred to the Group. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognised, the previously recognised impairment loss is increased or reduced in the consolidated statement of income.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

4.2 Financial contracts and impairment (continued)

b) Impairment assessment (continued)

Stage 3: Lifetime ECL – credit impaired (continued)

The present value of the estimated future cash flows is discounted at the financial asset's original effective profit rate. If a financial asset has a variable profit rate, the discount rate for measuring any impairment loss is the current effective profit rate. The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs of obtaining and selling the collateral, whether or not foreclosure is probable.

Measurement of ECL

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

- Probability of Default (PD);
- Loss Given Default (LGD); and
- Exposure At Default (EAD).

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

Probability of default

Credit risk grades are a primary input into the determination of the term structure of PD for exposures. The Group collects performance and default information about its credit risk exposures. The Group employs statistical models for analysing the data collected and generate estimates of PD of exposures and how these are expected to change as a result of the passage of time. This analysis includes the identification and calibration of relationships between changes in default rates and changes in key macro-economic factors, across various geographies in which the Bank has taken exposures. For most exposures, the key macro-economic indicators include gross domestic product (GDP) growth, real interest rates, oil prices and equity prices.

Incorporation of forward - looking information

The Group employs statistical models to incorporate macro-economic factors on historical default rates. In case none of the macro-economic parameters are statistically significant or the results of forecasted PDs are significantly deviated from the present forecast for the economic conditions, quantitative PD overlay shall be used by the management after analyzing the portfolio.

Incorporating forward-looking information increases the level of judgment as to how changes in these macroeconomic factors will affect the ECL applicable to the stage 1 and stage 2 exposures which are considered as performing (Stage 3 are the exposures under default category). The methodologies and assumptions involved, including any forecasts of future economic conditions, are reviewed periodically.

Loss Given Default

LGD is the magnitude of the likely loss if there is a default. The Group estimates LGD parameters based on the history of recovery rates of claims against defaulted counterparties and collaterals held, based on historical data using both internal and external factors including hair cuts.

Exposure At Default

EAD represents the expected exposure in the event of a default. The Group derives the EAD from the current exposure to the counterparty and potential changes to the current amounts allowed under the contract including amortisation. The EAD of a financial asset is its gross carrying amount. For financing commitments and financial guarantees, the EAD is converted to consolidated statement of financial position equivalents. The EAD is estimated using the outstanding exposure adjusted by CCF times undrawn portion of the facilities. In case of financial guarantee, EAD is estimated as CCF times the committed amount. The outstanding exposure is equivalent to the principal outstanding. The undrawn portion refers to the portion of the unutilized credit limit.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

4.2 Financial contracts and impairment (continued)

b) Impairment assessment (continued)

Significant Increase in Credit Risk

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

The criteria for determining whether credit risk has increased significantly vary on a portfolio level and include quantitative and qualitative factors, including days past due and risk rating.

Renegotiated financial assets

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

The Group considers renegotiated financing to customers due to financial difficulties as one of the reasons for determining the significant increase in credit risk. This may involve extending the payment arrangements and documenting the agreement of new conditions for providing finance. Management continuously reviews renegotiated facilities to ensure that all criteria are met and that future payments are likely to occur.

Backward transition

FAS 30 staging model is of symmetrical nature as exposures may migrate from lifetime ECL measurement (Stage 2 and Stage 3) to 12 month ECL measurement (Stage 1). Once such indicators are no longer triggered, movement back to Stage 1 or Stage 2 are subject to certain criteria such as cooling off period, SICR indicators and payment history, where applicable.

Write-offs

Financing contracts are written-off (either partially or in full) when there is no realistic prospect of recovery. This is generally the case when the Group determines that the borrower does not have assets or sources of income that could generate sufficient cash flows to repay the amounts subject to the write-off. However, financial assets that are written-off could still be subject to enforcement activities in order to comply with the Group's procedures for recovery of amounts due.

Presentation of allowance for credit losses in the consolidated statement of financial position

Allowance for credit losses are presented in the consolidated statement of financial position as follows:
- financial assets measured at amortised cost, as a deduction from the gross carrying amount of the assets; and
- financing commitments and financial guarantee contracts: generally as a provision in other liabilities.

4.3 Foreign currency translation

The consolidated financial statements are presented in Bahraini Dinars, which is the Bank's functional and presentation currency. Each entity in the Group determines its own functional currency and items included in the financial statements of each entity are measured using that functional currency.

(i) Transactions and balances

Transactions in foreign currencies are initially recorded in the functional currency using the rate of exchange prevailing at the date of the transaction.

Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the date of the consolidated statement of financial position. All differences are taken to the consolidated statement of income with the exception of all monetary items that provide an effective protection for a net investment in a foreign operation. These are recognised in other comprehensive income until the disposal of the net investment, at which time they are recognised in the consolidated statement of income.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

4.3 Foreign currency translation (continued)

(i) Transactions and balances (continued)

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial recognition. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value is determined. Exchange gains and losses on non-monetary items classified as «fair value through statement of income» are taken to the consolidated statement of income and for items classified as «fair value through equity» such differences are taken to other comprehensive income. Any goodwill arising on the acquisition of a foreign operation and any fair value adjustments to the carrying amounts of assets and liabilities arising on the acquisition are treated as assets and liabilities of the foreign operations and translated at closing rate.

(ii) Group companies

As at the reporting date, the assets and liabilities of subsidiaries are translated into the Group's presentation currency (Bahraini Dinars) at the rate of exchange prevailing at the date of the consolidated statement of financial position, and their statements of income are translated at the average exchange rates for the year. Exchange differences arising on translation are recognised in other comprehensive income. On disposal of a foreign subsidiary, the cumulative amount recognised in other comprehensive income relating to that particular foreign subsidiary is recognised in the consolidated statement of income.

4.4 Financial instruments - initial recognition and subsequent measurement

Date of recognition

A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity. All financial assets and liabilities are initially recognised on the trade date, i.e. the date that the Group becomes a party to the contractual provisions of the instrument.

Initial and subsequent measurement of financial instruments

The classification of financial instruments at initial recognition depends on the purpose and the management's intention for which the financial instruments were acquired and their characteristics. All financial instruments are measured initially at their fair value plus transaction costs, except in the case of financial assets recorded at fair value through statement of income.

(i) Due from banks

Murabahas are international commodity murabaha transactions. The Bank arranges a murabaha transaction by buying a commodity (which represents the object of the murabaha) and then resells this commodity to the beneficiary murabeh (after computing a profit margin). The sale price (cost plus the profit margin) is paid either lump sum at maturity or in installments by the murabeh over the agreed period.

Murabaha with banks are stated net of deferred profits and provision for impairment, if any. Wakala with banks are stated at cost less provision for impairment, if any.

(ii) Financing contracts

(a) Murabaha

Murabaha represents the sale of goods at cost plus an agreed profit. Murabaha receivables are stated net of deferred profits, any amounts written off and provision for impairment, if any. Promise made in the murabaha to the purchase orderer is not obligatory upon the customer.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

4.4 Financial instruments - initial recognition and subsequent measurement

(ii) Financing contracts (continued)

(b) Ijarah Muntahia Bittamleek

Ijarah Muntahia Bittamleek mainly comprise of land and buildings and certain other assets. Ijarah Muntahia Bittamleek is a lease whereby the legal title of the leased asset passes to the lessee at the end of the ijarah (lease term), provided that all ijarah installments are settled.

Assets under Ijarah Muntahia Bittamleek are initially recognised at cost and subsequently depreciated at rates calculated to write off the cost of each asset over its useful life to its residual value.

(c) Musharaka

Musharaka represents a partnership between the Group and a customer whereby each party contributes to the capital in equal or varying proportions to establish a new project or share in an existing one, and whereby each of the parties becomes an owner of the capital on a permanent or declining basis and shall have a share of profits or losses. These are stated at the fair value of consideration given less any amounts written off and provision for impairment, if any.

(iii) Investments

The Bank accounts for the investments in accordance with the FAS 33 - Investment in sukuk, shares and similar instruments that has been adopted from 1 January 2020. Refer section 4.1 for details.

(iv) Equity of investment account holders

Equity of investment account holders is invested in cash, balances with banks and Central Bank of Bahrain, due from banks, sukuk and financing contracts. No priority is granted to any party for the purpose of distribution of profits. According to the terms of acceptance of the investment account holders funds, 100% of these funds are invested after deductions of mandatory reserve and sufficient operational cash requirements.

Equity of investment account holders is carried at fair value of consideration received less amounts settled. Expenses are allocated to investment accounts in proportion of average equity of investment account holders to average assets, however, investment related expenses and assets are excluded.

Income is allocated proportionately between equity of investment account holders and owners' equity on the basis of the average balances outstanding during the year and share of the funds invested.

4.5 Derecognition of financial assets and financial liabilities

(i) Financial assets

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

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

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

4.5 Derecognition of financial assets and financial liabilities (continued)

(ii) Financial liabilities

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

4.6 Impairment of financial assets

(i) Financial assets carried at amortised cost

The Group applies three-stage approach to measure ECL on financial assets carried at amortised cost as required by FAS 30 with Expected Credit Loss model explained above.

(ii) Investments at fair value through equity

For investments at fair value through equity, the Group assesses at each reporting date whether there is objective evidence that an investment or a group of investments is impaired.

In the case of equity investments classified as «fair value through equity», objective evidence would include a significant or prolonged decline in the fair value of the investment below its cost. Where there is evidence of impairment, the cumulative loss measured as the difference between the acquisition cost and the current fair value less any impairment loss on that investment previously recognised is removed from fair value through equity reserve and recognised in the consolidated statement of income. Impairment losses on equity investments are not reversed through the consolidated statement of income; increases in their fair value subsequent to impairment are recognised directly in equity.

4.7 Offsetting financial instruments

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

4.8 Recognition of income and expense

(i) Income recognition

(a) Murabaha

Where the income is quantifiable and contractually determined at the commencement of the contract, income is recognised on a time-apportioned basis over the period of the contract based on the principal amounts outstanding. Accrual of income is suspended when the Group believes that the recovery of these amounts may be doubtful.

(b) Ijarah Muntahia Bittamleek

Ijarah income is recognised on a time-apportioned basis, net of depreciation, over the lease term. Accrual of income is suspended when the Group believes that the recovery of these amounts may be doubtful.

(c) Musharaka

Income on musharaka contracts is recognised when the right to receive payment is established or on distribution by the musharek.

(d) Dividends

Dividends from investments in equity securities are recognised when the right to receive the payment is established.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

4.8 Recognition of income and expense (continued)

(i) Income recognition (continued)

(e) Fees and commission income

Fees and commission income is recognised when earned.

(f) Revenue from sale of real estate

Revenue on sale of real estate is recognised when all of the following conditions are met:

- A sale is consummated and contracts are signed;
- The buyer's investment, as of the date of financial statements, is adequate (25% and above) to demonstrate a commitment to pay for the property; and
- The Group has transferred to the buyer the risks and rewards of ownership in a transaction that is in substance a sale and does not have a substantial continuing involvement with the property.

Where property is under development and agreement has been reached to sell such property when construction is complete, the Group considers whether the contract comprises:

- contract to construct a property; or
- contract for the sale of a completed property.

Where a contract is determined to be a construction contract, revenue is recognised using the percentage of completion method as construction progresses. The percentage of work complete is measured based on the costs incurred up until the end of the reporting period as a proportion of total costs expected to be incurred.

Where the contract is judged to be for the sale of a completed property, revenue is recognised when the significant risks and rewards of ownership of the property are transferred to the buyer.

(g) Service income

Revenue from rendering of services is recognised when the services are rendered.

(h) Group's share as a mudarib

The Group's share as a mudarib for managing the equity of investment account holders is accrued based on the terms and conditions of the related mudaraba agreements whereas, for off balance sheet equity of investment account holders, mudarib share is recognised when distributed.

(ii) Expense recognition

(a) Profit on due to banks and non-banks

Profit on these is accrued on a time-apportioned basis over the period of the contract based on the principal amounts outstanding.

(b) Return on equity of investment account holders

Return on equity of investment account holders is based on the income generated from jointly financed assets after deducting mudarib share (in case of mudara contracts) and is accrued based on the terms and conditions of the underlying mudaraba or wakala agreement. Investors' share of income represents income generated from assets financed by investment account holders net of allocated operating expenses. The Group's share of profit is deducted from the investors' share of income before distribution to investors.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

4.9 Investment in associates

An associate is an entity in which the Group has significant influence and which is neither a subsidiary nor a joint venture.

Investment in associate is accounted for using the equity method of accounting. Under the equity method, the investment in the associate is carried in the consolidated statement of financial position at cost plus post acquisition changes in the Group's share of net assets of the associate. Goodwill relating to an associate is included in the carrying amount of the investment and is not amortised nor individually tested for impairment.

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

The consolidated statement of income reflects the share of the results of operations of the associate. Where there has been an income or expense recognised in the other comprehensive income of the associate, the Group recognises its share of any such income or expense, when applicable, in other comprehensive income. Gains and losses resulting from transactions between the Group and the associate are eliminated to the extent of stake in the associate.

The reporting dates of the associates and the Group are identical and their accounting policies conform to those used by the Group for like transactions and events in similar circumstances. In case of any difference in the associates' accounting policies, their results are adjusted to bring them in line with the Group accounting policies.

Upon loss of significant influence over the associate, the Group measures and recognises any retaining 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 retaining investment and proceeds from disposal is recognised in the consolidated statement of income.

4.10 Premises and equipment

Premises and equipment are stated at cost excluding the costs of day-to-day servicing, less accumulated depreciation and accumulated impairment in value, if any.

4.11 Depreciation

Depreciation is calculated using the straight-line method to write down the cost of premises and equipment to their residual values over their estimated useful lives. Land is not depreciated. The estimated useful lives are as follows:

	Years
Premises	20
Hardware, software and equipment	3 - 7
Motor vehicles and office furniture	5 - 7

An item of premises and equipment is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is recognised in the consolidated statement of income in the year the asset is derecognised.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

4.12 Impairment of non-financial assets

The Group assesses at each reporting date or more frequently whether there is an indication that a non-financial asset may be impaired. If any such indication exists, or when annual impairment testing for an asset is required, the Group makes an estimate of the asset's recoverable amount. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount.

For assets excluding goodwill, an assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If any such indication exists, the recoverable amount is estimated. A previously recognised impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised. If that is the case, the carrying amount of the asset is increased to its recoverable amount. Impairment losses relating to goodwill cannot be reversed for subsequent increase in its recoverable amount in future periods.

4.13 Financial guarantees

In the ordinary course of business, the Group provides financial guarantees, consisting of letters of credit, guarantees and acceptances. Financial guarantees are initially recorded in the consolidated statement of financial position at fair value in ‹other liabilities' being the premium received. Subsequent to initial recognition, the Group's liability under each guarantee is measured at the higher of the unamortised premium and the best estimate of expenditure required to settle any financial obligation arising as a result of the guarantee.

Any increase in the liability relating to financial guarantees is recognised in the consolidated statement of income under ‹provisions'. The premium received is recognised in the consolidated statement of income on a straight line basis over the life of the guarantee.

4.14 Treasury shares

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

4.15 Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) arising from a past event and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of obligation.

4.16 Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the Chief Operating Decision Maker (CODM). CODM is a person or group that allocates resources to and assesses the performance of the operating segments of the entity. The Group has determined the Managing Director and Chief Executive Officer as its CODM.

4.17 Cash and cash equivalents

Cash and cash equivalents comprise of cash and balances with banks and the Central Bank of Bahrain (excluding mandatory reserve) and due from banks with original maturity of 90 days or less.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

4.18 Employees' end of service benefits

Provision is made for leaving indemnity payable under the Bahraini Labor Law applicable to non-Bahraini employees' accumulated periods of service at the consolidated statement of financial position date.

Bahraini employees of the Group are covered by contributions made to the Social Insurance Organisation ("SIO") as a percentage of the employees' salaries. The Group's obligations are limited to these contributions, which are expensed when due. For Bahrainis with basic salaries above a certain threshold, the Bank recognises leaving indemnity in line with the requirements of Bahrain Labour Law.

4.19 Off-balance sheet equity of investment account holders

Off-balance sheet equity of investment account holders represents funds received by the Bank on the basis of mudaraba to be invested in specified products as directed by the investment account holders. The assets funded by these funds are managed in a fiduciary capacity by the Bank for which the Bank earns mudarib share which is disclosed as part of 'income from financing contracts'. These assets are not included in the consolidated statement of financial position as the Group does not have the right to use or dispose of them except within the conditions laid down in the underlying mudaraba contract. Off-balance sheet equity of investment account holders is included in a seperate statement in the consolidated financial statements of the Bank.

4.20 Earnings prohibited by Shari'a

The Group is committed to avoid recognising any income generated from non-Islamic sources. Accordingly, all non-Islamic income is transferred to charity.

4.21 Inventories

Inventories are carried at the lower of cost and net realisable value. For individually significant amounts this estimation is performed on an individual basis. Amounts which are not individually significant, but which are old or obsolete, are assessed collectively and an allowance applied according to the inventory type and the degree of ageing or obsolescence, based on historical selling prices.

4.22 Assets classified as held for sale

The Group classifies assets as held for sale if their carrying amounts will be recovered principally through a sale rather than through continuing use. Such assets classified as held for sale are measured at the lower of their carrying amount and fair value less costs to sell.

The criteria for held for sale classification is regarded as met only when the sale is highly probable and the asset is available for immediate sale in its present condition. Actions required to complete the sale should indicate that it is unlikely that significant changes to the plan will be made or that the plan will be withdrawn. Management must be committed to the plan, expected within one year from the date of the classification.

Property, plant and equipment and intangible assets are not depreciated or amortised once classified as held for sale.

Assets and liabilities classified as held for sale are presented separately in the consolidated statement of financial position.

Results from discontinued operations are presented as a single amount in the consolidated statement of income.

Assets which ceases to be classified as held for sale are consolidated on a line by line basis. Prior period balances are re-presented.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

4.23 Repossessed assets

Repossessed assets are real estate assets acquired in settlement of financing contracts with customers. These assets are carried at the lower of carrying amount and fair value less costs to sell and reported within "receivables and other assets" in the consolidated statement of financial position.

4.24 Fair value of financial instruments

The Group measures financial instruments and non-financial assets such as investment in real estate, at fair value at the date of statement of financial position. Fair values of financial instruments are disclosed in note 32.

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 the Group. The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

The Group uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs. Observable data used along with the Group's approach to determining fair values of financial instruments and quantitative disclosure are disclosed in note 32.

4.25 Taxation

There is no tax on corporate income in the Kingdom of Bahrain. Taxation on overseas operations is provided for in accordance with the fiscal regulations of the respective countries in which the Group operates and is included in the accompanying consolidated statement of income under "other operating expenses".

4.26 Zakah

In accordance with the instructions of the Shari'a Supervisory Board of the Bank, payment of Zakah is the responsibility of the shareholders of the Bank. Accordingly, no Zakah has been charged to these consolidated financial statements.

4.27 Cross currency swap

Cross currency swap ("Islamic derivative financial instruments") are used to mitigate foreign currency risk. They are initially recognised and subsequently measured in the consolidated statement of financial position at fair value. The fair value of this instrument includes unrealized gain or loss from marking to market the instrument using prevailing market rates or internal pricing models. The instrument with positive market value (unrealised gain) is included in other assets and the instrument with negative market value (unrealised loss) is included in other liabilities in the consolidated statement of financial position. Any gain or loss arising from changes in the fair value of this instrument is taken directly to the consolidated statement of income.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

4.28 Provision for onerous contract or commitment to acquire an asset

The Group will recognize provision when the Group is obligated to acquire an asset under a future commitment or contracts permissible to be entered in the future, and it is expected that the obligation under the contract or commitment is higher than the economic benefits expected to flow through acquisition of such asset. In such situation, the Group will create a provision on this account reflecting the expected losses arising on such transaction.

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

FAS 35 Risk Reserves

This standard defines the accounting and financial reporting principles for risk reserves to be in line with global best practices for accounting and risk management. This standard complements FAS 30 “Impairment, Credit Losses and Onerous Commitments”. Both standards FAS 35 & FAS 30 together supersede the earlier FAS 11 “Provisions and Reserves”. This standard shall be effective beginning or after 1 January 2021, with early adoption is permitted, only if the financial institution decided to early adopt FAS 30.

The Board of Directors expects that the adoption of this standard will have no material impact on the financial statements of the Bank in the year of initial application as the Bank does not maintain risk reserves.

FAS 32 Ijarah

This standard supersedes FAS 8 “Ijarah and Ijarah Muntahia Bittamleek”. The standard aims at setting out principles for the classification, recognition, measurement, presentation and disclosure of Ijarah type transactions including their different forms entered into by an institution, in both the capacities of lessor and lessee. This standard shall be effective beginning or after 1 January 2021, with early adoption permitted.

The Board of Directors is currently assessing the impact of this standard on the consolidated financial statements upon the initial application.

5 LIST OF KEY SUBSIDIARIES

Key subsidiaries, all of which have 31 December as their year end, are listed below.

Subsidiary	Year of incorporation	Country of incorporation	Ownership %	
			2020	2019
Kuwait Finance House - Jordan The company and its subsidiaries are engaged in investment advisory and investments in private equities and real estate development.	2007	Hashemite Kingdom of Jordan	**100.00**	100.00
Ishbiliya Village W.L.L. The principal activity of the company is to invest in and develop real estate projects and consequently buying, selling and marketing of such properties.	2005	Kingdom of Bahrain	**100.00**	100.00

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

6 CLASSIFICATION OF FINANCIAL INSTRUMENTS BY MEASUREMENT BASIS

The Group's financial instruments have been classified in accordance with their measurement basis as follows:

At 31 December 2020	Financial assets at fair value through statement of income BD 000	Financial assets at fair value through equity BD 000	Financial assets at amortised cost BD 000	Financial liabilities at amortised cost BD 000	Total BD 000
ASSETS					
Cash and balances with banks and Central Bank of Bahrain	-	-	61,277	-	61,277
Due from banks	-	-	123,590	-	123,590
Financing contracts	-	-	1,005,228	-	1,005,228
Investments	-	6,861	-	-	6,861
Investment in sukuk	-	-	324,739	-	324,739
Receivables and other assets	-	-	160,481	-	160,481
	-	6,861	1,675,315	-	1,682,176
LIABILITIES AND EQUITY OF INVESTMENT ACCOUNT HOLDERS					
Customers' current accounts	-	-	-	133,114	133,114
Due to banks	-	-	-	108,798	108,798
Due to non-banks	-	-	-	364,048	364,048
Other liabilities	-	-	-	14,573	14,573
Equity of investment account holders	-	-	-	966,177	966,177
	-	-	-	1,586,710	1,586,710

At 31 December 2019	Financial assets at fair value through statement of income BD 000	Financial assets at fair value through equity BD 000	Financial assets at amortised cost BD 000	Financial liabilities at amortised cost BD 000	Total BD 000
ASSETS					
Cash and balances with banks and Central Bank of Bahrain	-	-	99,535	-	99,535
Due from banks	-	-	115,216	-	115,216
Financing contracts	-	-	913,907	-	913,907
Investments	1,760	4,396	-	-	6,156
Investment in sukuk	-	-	270,277	-	270,277
Receivables and other assets	-	-	198,684	-	198,684
	1,760	4,396	1,597,619	-	1,603,775
LIABILITIES AND EQUITY OF INVESTMENT ACCOUNT HOLDERS					
Customers' current accounts	-	-	-	128,258	128,258
Due to banks	-	-	-	101,783	101,783
Due to non-banks	-	-	-	222,965	222,965
Other liabilities	-	-	-	13,721	13,721
Equity of investment account holders	-	-	-	1,008,369	1,008,369
	-	-	-	1,475,096	1,475,096

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

7 CASH AND BALANCES WITH BANKS AND CENTRAL BANK OF BAHRAIN

	Note	2020 BD 000	2019 BD 000
Cash		**11,357**	10,816
Balances with banks		**7,939**	17,925
Balance with CBB		**12,888**	38,736
CBB mandatory reserve	7.1	**29,094**	32,060
Less: allowance for credit losses		**(1)**	(2)
	7.2	**61,277**	99,535

7.1 This mandatory reserve is not available for use in the Group's day to day operations.

7.2 This balance includes BD 43,599 thousand (2019: BD 19,915 thousand) financed by investment account holders' funds.

8 DUE FROM BANKS

	2020 BD 000	2019 BD 000
Murabaha	**42,779**	72,765
Wakala	**81,041**	43,135
	123,820	115,900
Less: allowance for credit losses	**(230)**	(684)
	123,590	115,216

8.1 Under the above wakala arrangement, the agent pays the Bank a profit, when realised, equivelent to the expected profit rate stated in the respective wakala offer and anything beyond this rate goes to the agent as an incentive.

8.2 Due from Banks includes BD 100,801 thousand (2019: BD 21,933 thousand) financed by investment account holders' funds. Due from banks carry profit rates ranging from 0.10% to 1.20% per annum (2019: 0.76% to 2.70% per annum).

9 FINANCING CONTRACTS

The table below shows the financing contracts by stage and type of facility:

	31 December 2020		
Self financed	**Murabaha BD 000**	**Ijarah Muntahia Bittamleek BD 000**	**Total BD 000**
Stage 1: 12-month ECL	**166,402**	**202,149**	**368,551**
Stage 2: Lifetime ECL not credit-impaired	**11,011**	**36,782**	**47,793**
Stage 3: Lifetime ECL credit-impaired	**4,684**	**1,670**	**6,354**
Total allowance for credit losses	**(4,034)**	**(3,766)**	**(7,800)**
	178,063	**236,835**	**414,898**
31 December 2019	135,827	207,245	343,072

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

9 FINANCING CONTRACTS (continued)

	31 December 2020		
	Murabaha	Ijarah Muntahia Bittamleek	Total
Financed through investment account holders' funds	BD 000	BD 000	BD 000
Stage 1: 12-month ECL	236,741	287,642	524,383
Stage 2: Lifetime ECL not credit-impaired	15,668	52,337	68,005
Stage 3: Lifetime ECL credit-impaired	6,666	2,376	9,042
Total allowance for credit losses	(5,741)	(5,359)	(11,100)
	253,334	336,996	590,330
31 December 2019	225,910	344,925	570,835

The murabaha balances included above are presented net of deferred profits amounting to BD 38,913 thousand (2019: BD 36,196 thousand).

The table below shows the days past due for the financing contracts. The amounts presented are gross of impairment allowances.

	31 December 2020				31 December 2019
	Stage 1: 12-month ECL	Stage 2: Lifetime ECL not credit-impaired	Stage 3: Lifetime ECL credit-impaired	Total	Total
	BD 000	BD 000	BD 000	BD 000	BD 000
Not past due	877,770	112,356	553	990,679	850,414
1 to 89 days past due	15,164	3,442	-	18,606	43,804
90 days or more past due	-	-	14,843	14,843	38,302
Total allowance for credit losses	(6,799)	(9,957)	(2,144)	(18,900)	(18,613)
	886,135	105,841	13,252	1,005,228	913,907

Movements in allowance for credit losses on financing contracts

	Stage 1: 12-month ECL	Stage 2: Lifetime ECL not credit-impaired	Stage 3: Lifetime ECL credit-impaired	Total
	BD 000	BD 000	BD 000	BD 000
Balance at 1 January 2020	1,655	9,736	7,222	18,613
- transferred to Stage 1: 12-month ECL	141	(73)	(68)	-
- transferred to Stage 2: Lifetime ECL not credit-impaired	(14)	1,071	(1,057)	-
- transferred to Stage 3: Lifetime ECL credit-impaired	(1)	(8)	9	-
Net remeasurement of loss allowance	5,018	(769)	698	4,947
Allowance for credit losses	5,144	221	(418)	4,947
Amounts written off during the year	-	-	(4,660)	(4,660)
Balance at 31 December 2020	6,799	9,957	2,144	18,900

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9 FINANCING CONTRACTS (continued)

Movements in allowance for credit losses on financing contracts (continued)

	Stage 1: 12-month ECL	Stage 2: Lifetime ECL not credit-impaired	Stage 3: Lifetime ECL credit-impaired	Total
	BD 000	BD 000	BD 000	BD 000
Balance at 1 January 2019	2,638	13,337	5,661	21,636
- transferred to Stage 1: 12-month ECL	70	(9)	(61)	-
- transferred to Stage 2: Lifetime ECL not credit-impaired	(27)	529	(502)	-
- transferred to Stage 3: Lifetime ECL credit-impaired	(1)	(1,437)	1,438	-
Net remeasurement of loss allowance	(1,025)	(670)	797	(898)
Allowance for credit losses	(983)	(1,587)	1,672	(898)
Amounts written off during the year	-	(2,014)	(111)	(2,125)
Balance at 31 December 2019	1,655	9,736	7,222	18,613

Movements in deferred profit from murabaha contracts

	2020	2019
	BD 000	**BD 000**
Deferred profit at the beginning of the year	**36,196**	25,892
Murabaha Sales revenue during the year	**744,855**	577,130
Murabaha Cost of Sales	**721,696**	541,332
	23,159	35,798
Deferred profit collected during the year	**(15,779)**	(21,213)
Deferred profit settled during the year	**(4,663)**	(4,281)
Deferred profit at the end of the year	**38,913**	36,196

9.1 Ijarah Muntahia Bittamleek mainly comprise of land and building and are presented net of accumulated depreciation amounting to BD 81,307 thousand (2019: BD 99,123 thousand).

9.2 During the year, the Bank took possession of properties with a carrying value of BD 18,874 thousand (2019: BD 11,659 thousand) as part of financing settlement and were classified as repossessed assets in the receivables and other assets.

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10 INVESTMENTS

The Group's investments are classified as follows:

	Note	2020 BD 000	2019 BD 000
Investment at fair value through statement of income	10.1	-	1,760
Investments at fair value through equity	10.2	**6,861**	4,396
		6,861	6,156

10.1 Carried at fair value through statement of income

	2020 BD 000	2019 BD 000
Designated at fair value through statement of income upon initial recognition - Managed Fund	-	1,760

10.2 Carried at fair value through equity

	2020 BD 000	2019 BD 000
Quoted equity securities - cost	**1,572**	1,572
Unquoted equity securities - cost	**4,271**	2,500
	5,843	4,072
Fair value changes	**1,018**	324
	6,861	4,396

10.2.1 The movement of investments carried at fair value through equity during the year is as follows:

	2020 BD 000	2019 BD 000
At 1 January	**4,396**	4,742
Additions	**3,104**	-
Disposals / redemptions during the year	**(1,333)**	-
Impairment provisions	-	(500)
Fair value changes	**694**	154
At 31 December	**6,861**	4,396

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At 31 December 2020

10 INVESTMENTS (continued)

10.3 Composition of investment portfolio:

The industry and geographic composition of the Group's investment portfolio is as follows. All of these investments are in Middle East.

	2020 BD 000	2019 BD 000
Banking and financial services	**3,746**	6,156
Others	**3,115**	-
	6,861	6,156

11 INVESTMENT IN SUKUK

	Note	2020 BD 000	2019 BD 000
Quoted sukuk			
Government		**199,904**	181,498
Unquoted sukuk			
Government		**103,801**	67,755
Others		**21,039**	21,039
		324,744	270,292
Less: allowance for credit losses		**(5)**	(15)
	11.1	**324,739**	270,277

11.1 Investment in sukuk includes an amount of BD 231,447 thousand (2019: BD 49,461 thousand) financed by investment account holders' funds. Fair value of investment in sukuk as at 31 December 2020 amounted to BD 332,210 thousand (2019: BD 279,901 thousand).

11.2 All sukuk investments are classified as debt-type instruments.

12 INVESTMENT IN ASSOCIATE

The Group has the following associate as at 31 December 2020:

Name of the associate	Nature of business	Country of incorporation	Holding
Deera Investment and Real Estate Development Company	Real estate project development and property management.	Hashemite Kingdom of Jordan	28.00%

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12 INVESTMENT IN ASSOCIATE (continued)

The movement of the Group's investment in an associate is as follows:

	Note	2020 BD 000	2019 BD 000
At 1 January		**8,461**	12,885
Share of loss from associate		**(463)**	(164)
Provision for impairment	26	**(1,109)**	-
Transfer to subsidiaries		**-**	(4,260)
At 31 December		**6,889**	8,461

12.1 The quoted value of the investment in associate for which quoted prices are available is BD 4,944 thousand (2019: BD 4,527 thousand). However, the quoted price does not represent the fair value as the shares are not actively traded. The fair value based on internal models approximates their carrying value.

13 FUNDS UNDER WAKALA ARRANGEMENT

The Group has the below Wakala funds which are received from different fund providers and are reinvested by the Group in it's capacity as Wakeel under multi-level investment arrangements into unrestricted investment accounts with the Group. Under those Wakala agreements, the Group agrees a target rate with the fund providers and any rate beyond that is considered as incentive fee for the Group. Currently, all the below Wakala arrangements are reinvested and maintained under Unrestricted Investment Account. All expenses incurred with relation to Wakala funds are beard by the fund providers. The Group does not charge mudarib fee on these funds.

	2020 BD 000	2019 BD 000
Banks	**87,773**	63,688
Non-banks	**-**	179,410
Parent - subordinated wakala	**95,175**	96,011
Individuals	**473,213**	391,953
	656,161	731,062

Movement of Wakala funds during the year is as follow:

	2020 BD 000	2019 BD 000
At 1 January	**731,062**	601,863
Additions during the year	**309,612**	442,516
Income during the year	**40,509**	36,465
Less: expenses charged during the year	**(10,805)**	(12,222)
Less: incentive fee	**(11,659)**	(2,226)
Distributions to wakala holders	**(18,045)**	(22,017)
Withdrawals	**(366,468)**	(291,300)
At 31 December	**656,161**	731,062

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14 RECEIVABLES AND OTHER ASSETS

	Note	2020 BD 000	2019 BD 000
Land and development cost	14.1	**25,007**	25,047
Fees receivable		**517**	1,528
Project expenses receivable		**83**	308
Inventories		**-**	1,570
Profit receivable		**282**	237
Repossessed assets		**34,974**	18,932
Trade receivables of subsidiaries		**893**	1,524
Prepaid expenses		**1,410**	1,828
Receivables relating to disposal of investments	14.3	**152,579**	187,297
Receivables from corporate customers		**3,269**	6,838
Other assets		**4,767**	2,808
Gross receivables and other assets		**223,781**	247,917
Impairment provisions	14.2	**(404)**	(589)
At 31 December		**223,377**	247,328

14.1 Land and development cost

	2020 BD 000	2019 BD 000
Land	**23,671**	23,690
Development cost	**1,336**	1,357
	25,007	25,047

This development cost represents construction, consultancy and profit paid on financing, capitalised relating to various real estate projects being undertaken by the Group.

14.2 Movement in impairment provisions relating to receivables and other assets.

	Note	2020 BD 000	2019 BD 000
At 1 January		**589**	1,551
Charge / (reversals) for the year	26	**540**	(372)
Settlements / write-offs		**(725)**	(590)
At 31 December		**404**	589

14.3 This includes a receivable of BD 152,579 thousand (2019: BD 187,297 thousand) due from a related party. This receivable is expected to be settled through the realisation of underlying assets and dividend payouts from the Bank. The Ultimate Parent has also provided a letter of guarantee for settlement of the receivable.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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15 DUE TO BANKS

	2020 BD 000	2019 BD 000
Murabaha payables	**108,410**	100,869
Current accounts	**388**	914
	108,798	101,783

16 ASSETS UNDER MANAGEMENT

At 31 December 2020, assets managed in a fiduciary capacity amounted to BD 685,247 thousand (2019: BD 592,074 thousand).

17 OTHER LIABILITIES

	2020 BD 000	2019 BD 000
Pay orders issued but not presented	**2,967**	2,903
Payable on account of financing contracts	**1,038**	771
Staff related accruals	**3,354**	3,486
Trade payables of subsidiaries	**184**	803
Fixed assets related payables	**1,724**	1,789
Unearned fees	**1,725**	1,678
Accrued expenses and other liabilities	**5,306**	3,969
	16,298	15,399

18 EQUITY OF INVESTMENT ACCOUNT HOLDERS - NON-BANKS AND INDIVIDUALS

The mudarib share on investment accounts ranges from 30% to 85% (2019: 30% to 85%) depending on the investment period and in the case of saving accounts, where there is no restriction on cash withdrawal, the mudarib share ranges from 85% to 95% (2019: 85% to 95%). No mudarib share is charged on the URIA collected as per the wakala arrangement with customers in accordance with the multi-level arrangement. The following table includes the funds received from the Non- Banks and individuals under the wakala arrangement and does not include URIA balances received from Banks under this arrangement. The rate of return to investment account holders, as at 31 December 2020 and 2019, for various types of investment accounts, denominated in BD and USD, is as follows:

Investment accounts (mudaraba and wakala) - denominated in BD	2020 Rate of return %	2019 Rate of return %
Saving accounts	**0.20**	0.19
VIP saving accounts	**0.61**	0.56
Saving call accounts	**2.50**	3.00
One month investment accounts	**1.20 - 1.64**	1.50 - 2.00
Three months investment accounts	**1.90 - 2.04**	1.88 - 2.20
Six months investment accounts	**2.10 - 2.45**	2.25 - 2.50
Nine months investment accounts	**2.20 - 2.50**	2.60 - 2.70
One year investment accounts	**2.50 - 2.86**	2.63 - 3.10
Two year investment accounts	**2.90 - 3.10**	3.60 - 3.80
Three year investment accounts	**3.10 - 3.20**	3.80 - 4.00
Five year investment accounts	**3.20 - 3.30**	4.30 - 4.50

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
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18 EQUITY OF INVESTMENT ACCOUNT HOLDERS - NON-BANKS AND INDIVIDUALS (continued)

Investment accounts (mudaraba and wakala) - denominated in USD	2020 Rate of return %	2019 Rate of return %
Saving accounts	**0.20**	0.19
VIP saving accounts	**0.41**	0.38
Saving call accounts	**1.50**	3.00
One month investment accounts	**0.70 - 1.23**	0.95 - 1.13
Three months investment accounts	**1.00 - 1.64**	1.25 - 1.50
Six months investment accounts	**1.20 - 2.04**	1.55 - 1.88
Nine months investment accounts	**1.30**	1.70
One year investment accounts	**1.50 - 2.45**	1.85 - 2.25

18.1 Investment accounts by type

Investment accounts (mudaraba and wakala) - denominated in BD	2020 Rate of return	2019 Rate of return
Saving accounts	**380,876**	247,152
VIP saving accounts	**16,637**	20,090
One month investment accounts	**42,731**	118,175
Three months investment accounts	**52,024**	93,742
Six months investment accounts	**50,644**	51,559
Nine months investment accounts	**1,378**	1,104
One year investment accounts	**201,262**	285,908
Two year investment accounts	**21,357**	20,392
Three year investment accounts	**11,443**	8,242
Five year investment accounts	**4,877**	2,306
	783,229	848,670

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

19 SHARE CAPITAL AND RESERVES

	2020 BD 000	2019 BD 000
Authorised:		
3,500,000 thousand (2019 : 3,500,000 thousand) ordinary shares of BD 0.1 each	**350,000**	350,000
Issued and fully paid up:		
As at the beginning and end of the year 1,325,187 thousand (2019 : 1,325,187 thousand) ordinary shares of BD 0.1 each	**132,519**	132,519

The Board of Directors of the Bank have proposed a capital reduction of BD 13,721 thousand with a corresponding reduction in the receivable from a related party. This proposal is subject to the approval of the Extra Ordinary General Meeting of the Bank, Ministry of Industry and Commerce, Central Bank of Bahrain and the completion of legal formalities.

Nature and purpose of reserves

Statutory reserve

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

Fair value through equity reserve

Unrealised gains and losses resulting from investments carried at fair value through equity, if not determined to be impaired is recorded in the fair value through equity reserve and is not available for distribution. Upon disposal of related assets, the related cumulative gains or losses are transferred to retained earnings and become available for distribution.

Retained earnings

Retained earnings is the cumulative amount of annual earnings not paid out as dividends. Included in retained earnings is a non-distributable reserve amounting to BD 500 thousand (2019: BD 613 thousand) relating to subsidiaries of the Bank. An amount of BD 16,997 thousand representing modification loss net of government grant is adjusted against the retained earnings. For more details refer to note 39.

Proposed dividend

Proposed dividend is shown seperately within equity till it is approved by the Annual General Meeting. The Board of Directors of the Bank have proposed nil dividend for the year ended 31 December 2020 (2019: BD 22,517 thousand).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

20 TOTAL COMPREHENSIVE INCOME

	2020 BD 000	2019 BD 000
Net income for the year:	**15,237**	25,010
Other comprehensive income		
Fair value adjustments against fair value through equity investments	**694**	154
Total comprehensive income for the year	**15,931**	25,164
Adjustment attributable to non-controlling shareholders	**9**	9
	15,940	25,173

21 CONTINGENT LIABILITIES AND COMMITMENTS

	Note	2020 BD 000	2019 BD 000
Contingent liabilities			
Letters of credit		**5,096**	8,899
Guarantees		**7,754**	6,975
		12,850	15,874
Irrevocable commitments to extend credit (original term to maturity of one year or less)		**62,799**	92,474
Development cost commitment	21.1	**-**	448
		75,649	108,796

21.1 As of 31 December 2019, this represent payments to contractors and consultants for a development project.

21.2 Operating lease commitments

At 31 December 2020, the Group had commitments in respect of non-cancellable operating leases amounting to BD 2,157 thousand (2019: BD 3,088 thousand) relating to leasehold premises. Of the commitments in respect of operating leases, BD 971 thousand (2019: BD 1,107 thousand) are due within one year, BD 917 thousand (2019: BD 1,901 thousand) are due in one to five years and the remaining over five years.

21.3 The Bank is carrying expected credit loss of BD 77 thousand (2019: BD 42 thousand) against the contingent liabilities and commitments which is classified in other liabilities.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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22 CROSS CURRENCY SWAP

During 2019, the Bank entered into cross currency swap with the Parent ("Islamic derivative financial instruments") to mitigate foreign currency risk. Cross currency swap is based on Wa'ad (promise) structure between two parties to buy a specified Shari'a compliant commodity at an agreed price on the relevant date in future. It is a conditional promise to purchase a commodity through unilateral purchase undertaking. For cross currency swaps, fixed or floating payments as well as notional amounts are exchanged in different currencies.

The table below shows the positive and negative fair value of these instruments, which are equivalent to the market value, together with the notional amounts. The notional amount is the amount of currency swap instruments' underlying asset, reference rate or index and is the basis upon which changes in the value of this instrument is measured. The notional amounts indicate the volume of transactions outstanding at the period end and are not indicative of the credit risk.

	Currency Swap		
	Positive fair value BD 000	Negative fair value BD 000	Notional amount BD 000
31 December 2020	**-**	**162**	**195,537**
31 December 2019	-	69	82,940

In respect of cross currency swaps, the notional amount represents the gross cash flows. However, the amounts may be settled net. The following table shows the net cash flows:

	31 December 2020			
	Notional amount BD 000	Within 3 months BD 000	3 to 12 months BD 000	More than 12 months BD 000
Cash inflows	**195,537**	**-**	**195,537**	**-**
Cash outflows	**(195,537)**	**-**	**(195,53 7)**	**-**
	-	**-**	**-**	**-**

	31 December 2020			
	Notional amount BD 000	Within 3 months BD 000	3 to 12 months BD 000	More than 12 months BD 000
Cash inflows	82,940	-	82,940	-
Cash outflows	(82,940)	-	(82,940)	-
	-	-	-	-

23 INCOME FROM FINANCING CONTRACTS

	Note	2020 BD 000	2019 BD 000
Murabaha		**23,585**	22,053
Ijarah Muntahia Bittamleek	23.1	**32,092**	36,185
Due from banks		**1,476**	2,373
	23.2	**57,153**	60,611
Mudarib share from off balance sheet equity of investment account holders		**1,887**	2,035
Fees and commission income		**481**	719
Income from financing contracts		**59,521**	63,365

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23 INCOME FROM FINANCING CONTRACTS (continued)

23.1 This rent revenue is presented net of depreciation on Ijarah Muntahia Bittamleek assets amounting to BD 21,069 thousand (2019: BD 21,761 thousand).

23.2 This is excluding net income of BD 113 thousand (2019: BD 777 thousand) suspended during the year on account of regulatory requirements.

24 INCOME FROM INVESTMENTS

	Note	2020 BD 000	2019 BD 000
Net unrealised gain on investments	24.1	-	198
Net gain on sale of investments	24.2	**359**	-
Fee income		**1,238**	974
Foreign exchange		**413**	839
Loss on sale of development properties		-	(361)
Other income		**55**	70
		2,065	1,720

24.1 This represents fair value changes recognized during the year based on the latest net asset values (NAV's) of the managed funds.

24.2 This amount includes a gain on disposal of a subsidiary during 2020.

25 INCOME AND EXPENSE RELATING TO FINANCING CONTRACTS AND SUKUK

	Note	2020 BD 000	2019 BD 000
Income from financing contracts	23	**57,153**	60,611
Income from sukuk	25.1	**14,855**	20,200
		72,008	80,811
Less: Profit on due to banks and non-banks	28	**15,038**	12,490
Less: Return on equity of investment account holders (wakala)		**18,045**	22,017
Less: Return on equity of investment account holders (mudaraba)		**2,035**	1,883
		35,118	36,390
		36,890	44,421

25.1 This includes an amount of nil (2019: BD 6,316 thousand) on account of gain on sale of sukuk recorded during the year.

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26 PROVISIONS - NET

	Note	2020 BD 000	2019 BD 000
Balances with banks and Central Bank of Bahrain		**(1)**	1
Due from banks		**(454)**	149
Financing contracts	9	**4,947**	(898)
Investments	10.2.1	**-**	500
Investment in sukuk		**(10)**	6
Investment in associates	12	**1,109**	-
Receivables and other assets	14.2	**540**	(372)
Financing commitments and financial guarantees		**35**	(17)
Recoveries from written-off accounts		**(4,533)**	(64)
		1,633	(695)

27 OTHER EXPENSES

	2020 BD 000	2019 BD 000
Business development	**1,932**	1,911
Technology and communication	**3,715**	3,410
Legal, consulting and outsourcing	**795**	514
Premises - rentals and maintenance	**2,021**	1,888
Administration, selling and others	**2,101**	2,166
	10,564	9,889

28 PROFIT ON DUE TO BANKS AND NON-BANKS

	2020 BD 000	2019 BD 000
Due to banks	**4,981**	1,292
Due to non-banks	**10,057**	11,198
	15,038	12,490

29 CASH AND CASH EQUIVALENTS

Cash and cash equivalents for the purpose of the consolidated statement of cash flows comprise of the following amounts:

	2020 BD 000	2019 BD 000
Cash	**11,357**	10,816
Balances with banks	**7,939**	17,925
Balances with CBB excluding mandatory reserve	**12,888**	38,736
Due from banks with original maturity of less than ninety days	**123,590**	115,216
	155,774	182,693

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30 RELATED PARTY TRANSACTIONS AND BALANCES

Related parties represent associated companies, the parent and its major shareholders, directors and key management personnel of the Bank, the Bank's Shari'a Supervisory Board and entities controlled, jointly controlled or significantly influenced by such parties. Transactions with related parties arise from the ordinary course of business. Pricing policies and terms of these transactions are approved by the Group's management. Outstanding balances at the year end, excluding financing contracts, are unsecured.

The balances with related parties included in the consolidated financial statements are as follows:

	Note	Parent BD 000	Directors and key management personnel BD 000	Other related parties BD 000	Total 2020 BD 000	Total 2019 BD 000
Balances with Banks		24	-	20	44	998
Due from banks		66,003	-	-	66,003	3,771
Financing contracts *		-	2,651	20,814	23,465	46,662
Investment in sukuk		-	-	21,039	21,039	21,039
Fees receivable		-	-	517	517	1,528
Receivables and other assets	14.3	-	-	152,579	152,579	187,296
Due to non-banks		-	-	754	754	4,156
Customers' current accounts		249	714	7,176	8,139	2,469
Equity of investment account holders		136,720	2,875	23,582	163,177	340,212
Letters of credit		-	-	2,227	2,227	1,528
Commitments to extend credit		-	-	442	442	442
Off balance sheet equity of investment account holders						
- Funds extended to related parties		-	-	136,710	136,710	135,145
- Funds received from related parties		-	675	3,200	3,875	4,460
Assets under management		-	-	583,615	583,615	592,074

*Includes nil (2019: BD 16,473 thousand) which is past due and impaired

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

	Parent BD 000	Directors and key management personnel BD 000	Other related parties BD 000	Total 2020 BD 000	Total 2019 BD 000
Income from due from banks	30	-	-	30	28
Income from financing contracts	-	64	1,605	1,669	2,281
Income from investment in sukuk	-	-	1,271	1,271	1,271
Fee income	-	-	713	713	729
Allowance for credit losses	-	11	30	41	849
Profit on due to non-banks	-	-	48	48	216
Profit on equity investment account holders	3,775	52	1,622	5,449	10,469
Staff costs	-	4,738	-	4,738	5,353
Other expenses	-	-	1,331	1,331	1,344
Mudarib share of off-balance sheet equity of investment account holders	-	-	1,887	1,887	2,035

Compensation of key management personnel, included in the consolidated statement of income, is as follows:

	2020 BD 000	2019 BD 000
Short term employee benefits	4,517	5,030
Long term employee benefits	221	323

Directors' remuneration and attendance fee for the year ended 31 December 2020 amounted to BD 189 thousand and BD 115 thousand respectively (2019: BD 198 thousand and BD 127 thousand respectively).

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31 SEGMENT INFORMATION

Corporate banking	Principally engaged in Shari'a compliant profit sharing investment arrangements, providing Shari'a compliant financing contracts and other facilities to corporate customers.
Retail and private banking	Principally engaged in Shari'a compliant profit sharing investment arrangements, providing Shari'a compliant financing contracts and other facilities to retail and private banking customers.
Investments	Principally engaged in investment banking activities including private equity, managed funds and other investment management activities.
Treasury	Principally engaged in liquidity management, Shari'a compliant financing contracts to treasury customers, investment in Sukuk, investment accounts from non-bank customers and other international banking relationships.

Management monitors the operating results of its segments separately for the purpose of making decisions about resource allocation and performance assessment. Segment performance is evaluated based on segment profit (as reported in internal management reports) which is measured using the same measurement principles as are used in the preparation of these interim condensed consolidated financial statements.

The following table presents segment wise operating income, net income, total assets and total liabilities and equity of investment account holders of the Group for the year ended and as at 31 December 2020:

	Corporate banking	Retail & Private Banking	Investment	Treasury	Total
	BD 000	BD 000	BD 000	BD 000	BD 000
Operating income	28,239	23,482	3,215	21,042	75,978
Net income for the year	7,164	1,445	2,141	4,487	15,237
Segment assets	443,043	473,656	235,496	603,469	1,755,664
Segment liabilities and equity of investment account holders	26,129	1,067,705	359	494,242	1,588,435

The following table shows the distribution of the Group's operating income and total assets by geographical segments, based on the location in which the transactions and assets are recorded, for the year ended and as at 31 December 2020:

	Kingdom of Bahrain	Other countries	Total
	BD 000	BD 000	BD 000
Operating income	73,920	2,058	75,978
Segment assets	1,457,100	298,564	1,755,664

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31 SEGMENT INFORMATION (continued)

The following table presents segment wise operating income, net income, total assets and total liabilities and equity of investment account holders of the Group for the year ended and as at 31 December 2019:

	Corporate banking BD 000	Retail & Private Banking BD 000	Investment BD 000	Treasury BD 000	Total BD 000
Operating income	28,573	24,591	3,608	28,349	85,121
Net income for the year	8,496	9,284	255	6,975	25,010
Segment assets	423,790	417,320	274,282	555,041	1,670,433
Segment liabilities and equity of investment account holders	44,562	941,627	978	489,607	1,476,774

The following table shows the distribution of the Group's operating income and total assets by geographical segments, based on the location in which the transactions and assets are recorded, for the year ended and as at 31 December 2019:

	Kingdom of Bahrain	Other countries	Total
Operating income	82,602	2,519	85,121
Segment assets	1,373,395	297,038	1,670,433

32 FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair value is the value representing the estimate of the amount of cash or cash equivalents that would be received for an asset sold or the amount of cash or cash equivalents paid for a liability extinguished or transferred in an orderly transaction between a willing buyer and a willing seller at the measurement date.

At 31 December 2020 and 2019, the fair value of financial instruments carried at amortised cost approximate their carrying values except for the investment in sukuk.

Financial instruments recorded at fair value

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

- Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities;
- Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly; and
- Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

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32 FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

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

	Level 1 2020 BD 000	**Level 2 2020 BD 000**	**Level 3 2020 BD 000**	**Total 2020 BD 000**
Investments at fair value through equity				
Quoted equity securities	**1,390**	**-**	**-**	**1,390**
Unquoted equity securities	**-**	**-**	**5,471**	**5,471**
	1,390	**-**	**5,471**	**6,861**

	Level 1 2019 BD 000	Level 2 2019 BD 000	Level 3 2019 BD 000	Total 2019 BD 000
Investments at fair value through statement of income				
Managed funds	-	1,760	-	1,760
Investments at fair value through equity				
Quoted equity securities	706	-	-	706
Unquoted equity securities	-	-	3,690	3,690
	706	1,760	3,690	6,156

During the year ended 31 December 2020, there were no transfers between Level 1 and Level 2 fair value measurements, and no transfers into and out of Level 3 fair value measurements.

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

	Unquoted equity securities 2020 BD 000	Unquoted equity securities 2019 BD 000
Balance at 1 January	**3,690**	4,190
Impairment	**-**	(500)
Additions	**3,104**	-
Disposals / redemptions during the year	**(1,333)**	-
Fair value changes	**10**	-
Balance at 31 December	**5,471**	3,690

Impact on fair value of Level 3 financial instruments measured at fair value of changes to key assumptions

	Carrying amount 2020 BD 000	**Effect of reasonably possible alternative assumption 2020 BD 000**	Carrying amount 2019 BD 000	Effect of reasonably possible alternative assumption 2019 BD 000
Investments at fair value through equity Unquoted equity securities	**5,471**	**547**	3,690	369
	5,471	**547**	3,690	369

In order to determine reasonably possible alternative assumptions the Group adjusted key unobservable models inputs as follows:

For equities, the Group adjusted the price earning ratio by increasing and decreasing the price earning ratio by ten percent, which is considered by the Group to be within a range of reasonably possible alternatives based on the price earning ratios of companies with similar industry and risk profiles.

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33 MATURITY ANALYSIS OF ASSETS, LIABILITIES AND EQUITY OF INVESTMENT ACCOUNT HOLDERS

The table below shows an analysis of assets, liabilities and equity of investment account holders analysed according to when they are expected to be recovered or settled. Group's contractual undiscounted repayment obligations are disclosed in note 34.3 'Risk Management - Liquidity Risk and Funding Management'.

	Up to one year			Over one year				
	Up to 3 months 2020 BD 000	3 to 12 months 2020 BD 000	Subtotal upto 12 months 2020 BD 000	1 to 5 years 2020 BD 000	5 to 10 years 2020 BD 000	Over 10 years 2020 BD 000	Subtotal Over 1 year 2020 BD 000	Total 2020 BD 000
Assets								
Cash and balances with banks and Central Bank of Bahrain	17,064	765	**17,829**	12,112	7,622	23,714	**43,448**	**61,277**
Due from banks	123,590	-	**123,590**	-	-	-	**-**	**123,590**
Financing contracts	204,907	141,964	**346,871**	324,449	166,584	167,324	**658,357**	**1,005,228**
Investments	-	-	**-**	6,861	-	-	**6,861**	**6,861**
Investment in sukuk	28,322	61,260	**89,582**	205,536	29,621	-	**235,157**	**324,739**
Investment in associate	-	-	**-**	6,889	-	-	**6,889**	**6,889**
Receivables and other assets	38,631	695	**39,326**	184,051	-	-	**184,051**	**223,377**
Premises and equipment	-	-	**-**	-	3,703	-	**3,703**	**3,703**
Total	**412,514**	**204,684**	**617,198**	**739,898**	**207,530**	**191,038**	**1,138,466**	**1,755,664**
Liabilities and equity of investment account holders								
Customers' current accounts	7,162	-	**7,162**	41,984	41,984	41,984	**125,952**	**133,114**
Due to banks	108,798	-	**108,798**	-	-	-	**-**	**108,798**
Due to non-banks	8,785	754	**9,539**	251,515	51,498	51,496	**354,509**	**364,048**
Other liabilities	9,374	4,080	**13,454**	2,844	-	-	**2,844**	**16,298**
Equity of investment account holders	64,026	150,357	**214,383**	250,600	250,597	250,597	**751,794**	**966,177**
Total	**198,145**	**155,191**	**353,336**	**546,943**	**344,079**	**344,077**	**1,235,099**	**1,588,435**
Net	**214,369**	**49,493**	**263,862**	**192,955**	**(136,549)**	**(153,039)**	**(96,633)**	**167,229**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

33 MATURITY ANALYSIS OF ASSETS, LIABILITIES AND EQUITY OF INVESTMENT ACCOUNT HOLDERS (continued)

	Up to one year			Over one year				
	Up to 3 months	3 to 12 months	Subtotal upto 12 months	1 to 5 years	5 to 10 years	Over 10 years	Subtotal Over 1 year	Total
	2019	2019	2019	2019	2019	2019	2019	2019
	BD 000	BD 000	BD 000	BD 000	BD 000	BD 000	BD 000	BD 000
Assets								
Cash and balances with banks and Central Bank of Bahrain	34,852	6,706	41,558	8,153	8,043	41,781	57,977	99,535
Due from banks	115,216	-	115,216	-	-	-	-	115,216
Financing contracts	176,064	158,753	334,817	308,775	155,380	114,935	579,090	913,907
Investments	1,760	-	1,760	4,396	-	-	4,396	6,156
Investment in sukuk	16,525	22,609	39,134	112,388	118,755	-	231,143	270,277
Investment in associate	-	-	-	8,461	-	-	8,461	8,461
Receivables and other assets	48,255	68	48,323	199,005	-	-	199,005	247,328
Premises and equipment	-	-	-	-	9,553	-	9,553	9,553
Total	392,672	188,136	580,808	641,178	291,731	156,716	1,089,625	1,670,433
Liabilities and equity of investment account holders								
Customers' current accounts	6,899	-	6,899	40,453	40,453	40,453	121,359	128,258
Due to banks	914	-	914	100,869	-	-	100,869	101,783
Due to non-banks	9,466	42,881	52,347	59,643	55,488	55,487	170,618	222,965
Other liabilities	7,789	4,388	12,177	3,222	-	-	3,222	15,399
Equity of investment account holders	46,383	193,070	239,453	341,438	213,739	213,739	768,916	1,008,369
Total	71,451	240,339	311,790	545,625	309,680	309,679	1,164,984	1,476,774
Net	321,221	(52,203)	269,018	95,553	(17,949)	(152,963)	(75,359)	193,659

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At 31 December 2020

34 RISK MANAGEMENT

34.1 Introduction

Risk is inherent in the Group's activities but it is managed through a process of ongoing identification, measurement and monitoring of material risks. The Group manages its exposure to risks within the approved risk limits. The process of risk management is critical to the Group's continuing profitability and each business unit within the Group is accountable for the risk exposures relating to its responsibilities. The Group is mainly exposed to credit risk, liquidity risk, profit rate risk and market risk, the latter being subdivided into trading and non-trading risks. The Group is also subject to prepayment risk and operating risk.

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

Risk management structure

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

Board of Directors

The Board of Directors is responsible for the overall risk management approach and for approving the risk strategies, policies and risk appetite of the Bank.

Audit & Compliance Committee (ACC)

The ACC is a Board appointed committee which is comprised of two independent directors and an executive director. The Chairman of the Committee is also an independent director. For audit related matters, the committee assists the Board of Directors in carrying out its responsibilities with respect to assessing the quality and integrity of financial reporting, the audit thereof and the soundness of the internal controls of the Bank. For compliance related matters, the committee assists the Board of Directors in the assessment of compliance with law, regulations and other requirements imposed on the Bank from time to time. The committee also overseas and manages the compliance and anti financial crime requirements of the Bank and legal related matters.

Board Risk Committee (BRC)

The Board Risk Committee is a Board appointed committee which is comprised of two independent directors and one executive director. The Chairman of the Committee is also an independent director. The committee is a reviewing and recommending body appointed by the Board of Directors to assist the Board in discharging its oversight duties relating to:

- Recommendation of the risk charter of the Bank to the Board, highlighting the key risks from identified business strategies, the risk appetite, the risk governance models including strategies, policies, processes, roles and responsibilities relating to various departments and various levels of risk management within the Bank; and
- Establishing appropriate policies and procedures to mitigate the applicable risks on the overall operations of the Bank.

Corporate Governance Committee

The Corporate Governance Committee is a Board appointed committee which is comprised of three independent directors including the Chairman. The committee is a reviewing and recommending body appointed by the Board of Directors to assist the Board in discharging its oversight duties relating to:

- Establishing appropriate Corporate Governance structures, delegation of authority and reporting protocols; and
- Ensure potential measure and improvements in corporate governance are implemented.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

34 RISK MANAGEMENT (continued)

34.1 Introduction (continued)

Internal Control Systems

The Board is responsible for approving and reviewing the effectiveness of the Bank's system of internal control, for the purpose of ensuring effective and efficient operations, quality of internal and external reporting, internal control, and compliance with laws and regulations. Senior Management is responsible for establishing and maintaining the system of internal control designed to manage the risk of failure to achieve the Bank's objectives. The system of internal control can only provide reasonable but not absolute assurance against the risk of material loss.

The effectiveness of the internal control system is reviewed by the Board and the Audit & Compliance Committee, which also receives review reports undertaken by the Bank's Internal Audit, Compliance and Anti Financial Crime departments. The Audit & Compliance Committee reviews the management letters issued by the external auditors and holds periodic meetings with them to discuss various matters including existing and potential internal control issues.

The regulatory non-compliances, if any, resulting in financial penalties are disclosed in the Annual Public Disclosures of the Bank. The Bank always enhances its internal control environment to avoid recurrence of similar penalties.

Asset and Liability Committee (ALCO) / Risk Management Committee (RMC)

ALCO / RMC is a senior management committee responsible for maintaining oversight of the Bank's risk profile and governance aspects. It helps the Board Risk Committee in establishing the risk policies and strategies and monitors the risk appetite in terms of risk limits and reports. It also controls the risks by appropriate actions. ALCO / RMC establishes policy and objectives for the asset and liability management of the Bank in terms of structure, distribution, risk and return and its impact on profitability. It also monitors the cash flow, cost and yield profiles and tenor of assets and liabilities and evaluates both from profit rate sensitivity and liquidity points of view, makes corrective adjustments based upon perceived trends and market conditions and monitors liquidity, foreign exchange exposures and positions.

Shari'a Supervisory Board

The Bank's Shari'a Supervisory Board is entrusted with the responsibility of ensuring the Bank's adherence to Shari'a rules and principles in its transactions and activities.

Provisioning Committee (PC)

The PC is a senior management committee responsible for ensuring adequate provisions and profit suspensions against all the past due and impaired exposures of the Bank. It reviews past due details and approve the resulting provisioning and profit suspension amounts submitted by the respective departments in line with the approved Provisions & Impairment Policy of the Bank. The PC also reviews credit classification and reclassification requests submitted by Business Units and recommends the provisions and profit suspensions to the Audit & Compliance Committee and Board of Directors for final approval.

Risk management department

The Risk Management Department is responsible for implementing and maintaining risk related procedures to ensure an independent control process. It also helps the ALCO / RMC in establishing risk strategies, policies and limits, across the Bank. The department is also responsible for the independent control of risks, including monitoring the risk of exposures against limits and the assessment of risks of new products and structured transactions. This department also ensures the complete capture of the risks in risk measurement and reporting systems and performs stress tests on the various portfolios of the Bank.

Treasury department

The treasury department is responsible for managing the Bank's assets and liabilities and the overall financial structure. It is also primarily responsible for the funding and liquidity risks of the Bank.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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34 RISK MANAGEMENT (continued)

34.1 Introduction (continued)

Internal audit

Independent, objective activity that reviews the effectiveness of risk management, internal control environment and governance processes. Internal Audit discusses the results of all assessments with the management, and reports its findings and recommendations to the Audit & Compliance Committee.

Compliance department

The compliance department is responsible for managing all the compliance related issues with the external parties and regulators.

Risk measurement and reporting systems

The Group identifies, measures, controls and monitors its material risks on a periodic basis. The Bank has established relevant risk limit structures to quantify its risk appetite. The Bank conducts stress testing under various scenarios for its material portfolios using statistical methods to assess the impact of such scenarios on its portfolio and regulatory capital.

Established risk limits reflect the business strategy and market environment in which the Bank operates as well as the level of risk that the Bank is willing to accept. In addition, the Bank monitors and measures the overall risk bearing capacity in relation to the aggregate risk exposures across its material risk types and activities.

Information compiled from all the businesses is examined and processed in order to analyse, control and identify risks at an early stage. This information is presented and explained to the Board of Directors, the Board Risk Committee and senior management. The report includes aggregate credit exposures, concentration limits, investment limits, foreign exchange exposures, profit rate limits, liquidity gaps and ratios and changes in Group's risk profile. On a periodic basis, detailed reporting of industry, customer and geographic risks takes place. Senior management assesses the appropriateness of the general allowance for credit losses on a quarterly basis. The Board of Directors receives the risk management report once in a quarter or when needed which is designed to provide all the necessary information to assess and conclude on the risks of the Group.

As part of the Risk Management's reporting framework, tailored risk reports are prepared and distributed in order to ensure that all business divisions have access to extensive, necessary and up-to-date information. Periodic briefing is given to the Managing Director and Chief Executive Officer and all other relevant members of the Bank on the utilisation of market limits, proprietary investments and liquidity and any other risk developments.

34.2 Credit risk

Credit risk is the risk that the Group will incur a loss because its customers, clients or counterparties fail to discharge their contractual obligations. The Bank manages and controls its credit risk by setting limits on the amount of risk it is willing to accept for individual counterparties and for geographical and industry concentrations, and by monitoring exposures in relation to such limits.

The Bank has established a credit quality review process to provide early identification of possible changes in the creditworthiness of counterparties, including regular collateral revisions. Counterparty limits are established with the use of a credit risk classification system, which assigns each counterparty a risk rating. Risk ratings for corporate customers are subject to revision at the time of renewal of the corporate facility. The credit quality review process allows the Bank to assess the potential loss as a result of the risks to which it is exposed and take corrective action.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

34 RISK MANAGEMENT (continued)

34.2 Credit risk (continued)

The Bank has adopted FAS 30 starting January 2018 where impairment is based on a forward-looking Expected Credit Loss (ECL) model. ECL would be measured taking into account the projected cash flows, Probability of Default (PD), Loss Given Default (LGD) and Exposure At Default (EAD). The amount of ECLs recognised as a loss allowance or provision depends on the extent of credit deterioration since initial recognition.

Credit-related commitments risk

The Bank makes available to its customers guarantees which may require that the Bank makes payments on their behalf. Such payments are collected from customers based on the terms of the letter of credit. They expose the Bank to risks similar to financing contracts and these are mitigated by the same control processes and policies.

Risk concentrations of the maximum exposure to credit risk without taking collateral

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

The maximum credit exposure to any client or counterparty as of 31 December 2020 was BD 290,045 thousand (2019: BD 276,740 thousand).

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

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

	Gross maximum exposure 2020 BD 000	Gross maximum exposure 2019 BD 000
Balances with banks and Central Bank of Bahrain	**49,920**	88,719
Due from banks	**123,590**	115,216
Financing contracts	**1,005,228**	913,907
Investment in sukuk	**324,739**	270,277
Receivables and other assets	**160,481**	199,554
Total	**1,663,958**	1,587,673
Contingent liabilities and commitments	**75,649**	108,796
Total credit risk exposure	**1,739,607**	1,696,469

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

34 RISK MANAGEMENT (continued)

34.2 Credit risk (continued)

Risk concentrations of the maximum exposure to credit risk

The Group financial assets having credit risk, before taking into account any collateral held can be analysed by the following geographical regions:

	Bahrain 2020 BD 000	Other GCC 2020 BD 000	North America 2020 BD 000	Other 2020 BD 000	Total 2020 BD 000
Balances with banks and Central Bank of Bahrain	41,993	1,469	5,236	1,222	49,920
Due from banks	22,813	98,506	2,271	-	123,590
Financing contracts	980,871	24,357	-	-	1,005,228
Investment in sukuk	324,739	-	-	-	324,739
Receivables and other assets	6,369	154,112	-	-	160,481
Contingent liabilities and commitments	75,649	-	-	-	75,649
Total	1,452,434	278,444	7,507	1,222	1,739,607

	Bahrain 2019 BD 000	Other GCC 2019 BD 000	North America 2019 BD 000	Other 2019 BD 000	Total 2019 BD 000
Balances with banks and Central Bank of Bahrain	70,806	1,829	14,361	1,723	88,719
Due from banks	64,036	46,987	4,193	-	115,216
Financing contracts	884,253	29,654	-	-	913,907
Investment in sukuk	270,277	-	-	-	270,277
Receivables and other assets	9,710	189,844	-	-	199,554
Contingent liabilities and commitments	108,796	-	-	-	108,796
Total	1,407,878	268,314	18,554	1,723	1,696,469

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

34 RISK MANAGEMENT (continued)

34.2 Credit risk (continued)

Risk concentrations of the maximum exposure to credit risk (continued)

An industry sector analysis of the Group's financial assets having credit risk, before taking into account collateral held or other credit enhancements, is as follows:

	Trading and manufacturing 2020 BD 000	Banking and financial institutions 2020 BD 000	Construction and real estate 2020 BD 000	Other 2020 BD 000	Total 2020 BD 000
Balances with banks and Central Bank of Bahrain	-	49,920	-	-	49,920
Due from banks	-	123,590	-	-	123,590
Financing contracts	117,428	1,119	465,689	420,992	1,005,228
Investment in sukuk	-	303,705	21,034	-	324,739
Receivables and other assets	-	156,024	4,457	-	160,481
Contingent liabilities and commitments	5,022	2,227	10,951	57,449	75,649
Total	**122,450**	**636,585**	**502,131**	**478,441**	**1,739,607**

	Trading and manufacturing 2019 BD 000	Banking and financial institutions 2019 BD 000	Construction and real estate 2019 BD 000	Other 2019 BD 000	Total 2019 BD 000
Balances with banks and Central Bank of Bahrain	-	88,719	-	-	88,719
Due from banks	-	115,216	-	-	115,216
Financing contracts	101,765	6,976	489,663	315,503	913,907
Investment in sukuk	-	249,240	21,037	-	270,277
Receivables and other assets	-	188,623	5,301	5,630	199,554
Contingent liabilities and commitments	40,036	4,053	36,603	28,104	108,796
Total	141,801	652,827	552,604	349,237	1,696,469

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34 RISK MANAGEMENT (continued)

34.2 Credit risk (continued)

Collateral and other credit enhancements

The amount and type of collateral required depends on an assessment of the credit risk of the counterparty. Guidelines are implemented regarding the acceptability of types of collateral and valuation parameters.

The main types of collateral obtained by the Bank are as follows:

- For commercial financing, lien over investment accounts, charges over real estate properties, inventory, trade receivables and unlisted equities; and
- For retail and consumer financing, lien over investment accounts, and mortgages over the related assets.

The Bank also obtains personal guarantees from company owners for commercial financing obtained. Management monitors the market value of collateral, requests additional collateral in accordance with the underlying agreement, and monitors the market value of collateral obtained periodically during its review of the Expected credit losses.

The Bank closely monitors collateral held for financial assets considered to be credit-impaired, as it becomes more likely that the Bank will take possession of the collateral to mitigate potential credit losses. Financial assets that are credit-impaired and related collateral held in order to mitigate potential losses are shown below:

	Gross Exposures 2020	Expected Credit Loss 2020	Carrying Amount 2020	Fair Value of Collateral Held 2020
Murabaha	**11,350**	**1,355**	**9,995**	**52,965**
Ijarah Muntahia Bittamleek	**4,046**	**789**	**3,257**	**9,059**
Total	**15,396**	**2,144**	**13,252**	**62,024**

	Gross Exposures 2019 BD 000	Impairment Allowance 2019 BD 000	Carrying Amount 2019 BD 000	Fair Value of Collateral Held 2019 BD 000
Murabaha	33,002	4,896	28,106	162,649
Ijarah Muntahia Bittamleek	30,680	2,326	28,354	117,360
Total	63,682	7,222	56,460	280,009

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

34 RISK MANAGEMENT (continued)

34.2 Credit risk (continued)

Individually assessed provisions

The Group performs assessment of Expected Credit Loss (ECL) and Significant Increase in Credit Risk (SICR) using qualitative and quantitative information appropriate for each individually significant financing contract on an individual basis. Individual assessment is important for large material exposures, as these are managed individually and incorporate obligor and facility specific information. Items considered when determining provision amounts include the sustainability of the counterparty's business plan, its ability to improve performance once a financial difficulty has arisen, projected receipts and the expected dividend payout should bankruptcy ensue, the availability of other financial support, the realisable value of collateral, and the timing of the expected cash flows. The ECL is evaluated at each reporting date, unless unforeseen circumstances require more careful attention.

Collectively assessed provisions

ECLs are assessed collectively for financing contracts in case of small, very immaterial portfolios. Provisions are evaluated on each reporting date with each portfolio subjected to a separate review. Collective assessment would enable application of standardized rules to specific portfolios for assessing SICR.

The collective assessment takes account of impairment that is likely to be present in the portfolio even though there is not yet objective evidence of the impairment in an individual assessment. Impairment losses are estimated by taking into consideration of the following information: historical losses on the portfolio, current economic conditions, the approximate delay between the time a loss is likely to have been incurred and the time it will be identified as requiring an individually assessed impairment provision, and expected receipts and recoveries once impaired. Management is responsible for deciding the length of this period which can extend for as long as one year. The impairment provision is then reviewed as a part of the credit management framework to ensure alignment with the Group's overall policy.

Financial guarantees and letters of credit are assessed and provision made in a similar manner as for financing contracts.

34.3 Liquidity risk and funding management

Liquidity risk is the risk that the Group will be unable to meet its payment obligations when they fall due under normal and stress circumstances. To limit this risk, management arranges diversified funding sources in addition to its core deposit base, manages assets with liquidity in mind, and monitors future cash flows and liquidity on a daily basis. This incorporates an assessment of expected cash flows and the availability of high grade collateral which could be used to secure additional funding if required.

The Group maintains a portfolio of highly marketable and diverse assets that can be easily liquidated in the event of an unforeseen interruption of cash flow. The Group also has committed lines of credit that it can access to meet liquidity needs. In addition, the Bank maintains a mandatory reserve with the Central Bank of Bahrain equal to 3% of customer deposits denominated in Bahrain Dinars, excluding deposits from resident subsidiaries. The liquidity position is assessed and managed under a variety of scenarios, giving due consideration to stress factors relating to both the market in general and specifically to the Bank. The most important of these is to maintain limits on the ratio of high quality liquid assets ("HQLA") to customer deposits. HQLA comprise of cash, balances with Central Bank of Bahrain, investment in quoted securities and liquid sukuk in line with the Liquidity Risk Module of the CBB. Customer deposits comprise of customers' current accounts, unrestricted investment accounts and murabaha due to non-banks. The ratios during the year were as follows:

HQLA to Customer Deposits Ratio	2020 %	2019 %
31 December	**28.48%**	28.02%
During the year:		
Average	**31.41%**	26.87%
Highest	**34.16%**	31.27%
Lowest	**28.48%**	25.27%

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34 RISK MANAGEMENT (continued)

34.3 Liquidity risk and funding management (continued)

Analysis of financial liabilities and equity of investment account holders by remaining contractual maturities

The table below summarises the maturity profile of the Group's financial liabilities and equity of investment account holders at 31 December 2020 and 2019 based on contractual undiscounted repayment obligations. Maturity analysis of assets, liabilities and equity of investment account holders by expected maturities is disclosed in Note 33. Repayments which are subject to notice are treated as if notice were to be given immediately. However, the Group expects that many customers will not request repayment on the earliest date the Group could be required to pay and the table does not reflect the expected cash flows indicated by the Group's deposit retention history.

	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
At 31 December 2020					
Due to banks	388	108,829	-	-	109,217
Due to non-banks	-	75,401	198,827	96,456	370,684
Customers' current accounts	133,114	-	-	-	133,114
Other liabilities	-	9,369	4,081	2,848	16,298
Equity of investment account holders	397,512	353,571	190,587	31,327	972,997
Total undiscounted financial liabilities 2020	531,014	547,170	393,495	130,631	1,602,310

	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
At 31 December 2019					
Due to banks	914	-	-	106,217	107,131
Due to non-banks	-	148,945	76,966	1,260	227,171
Customers' current accounts	128,258	-	-	-	128,258
Other liabilities	-	7,788	4,389	3,222	15,399
Equity of investment account holders	266,082	325,772	269,995	166,595	1,028,444
Total undiscounted financial liabilities 2019	395,254	482,505	351,350	277,294	1,506,403

Contingent liabilities and commitments

These include commitments to enter into contracts which are designed to meet the requirements of the Group's customers. Commitments represent contractual commitments under murabaha, musharaka and ijarah muntahia bittamleek contracts. Commitments generally have fixed expiration dates, or other termination clauses. Since commitments may expire without being exercised, the total contract amounts do not necessarily represent future cash flow requirements.

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

34 RISK MANAGEMENT (continued)

34.3 Liquidity risk and funding management (continued)

Contingent liabilities and commitments (continued)

The table below shows the contractual expiry by maturity of the Group's credit commitments and contingent items.

	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
At 31 December 2020					
Letters of credit	**7,872**	**271**	**4,746**	**(7,793)**	**5,096**
Guarantees	**7,754**	**114**	**1,885**	**(1,999)**	**7,754**
Irrevocable commitments to extend credit	**-**	**1,421**	**33,315**	**28,063**	**62,799**
Development commitment	**-**	**-**	**-**	**-**	**-**
Total	**15,626**	**1,806**	**39,946**	**18,271**	**75,649**

	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
At 31 December 2019					
Letters of credit	6,630	164	1,528	577	8,899
Guarantees	6,975	-	-	-	6,975
Irrevocable commitments to extend credit	-	4,651	87,823	-	92,474
Development commitment	-	-	448	-	448
Total	13,605	4,815	89,799	577	108,796

34.4 Market risk

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to changes in market variables such as profit rates, foreign exchange rates, and equity prices. The Group manages and monitors the positions using sensitivity analysis.

Profit rate risk

Profit rate risk arises from the possibility that changes in profit rates will affect future profitability or the fair values of financial instruments. The Bank measures the profit rate risk by measuring and managing the repricing gaps. It also performs sensitivity analysis.

The following table demonstrates the sensitivity to reasonably possible change in profit rates, with all other variables held constant of the Group's consolidated statement of income. The sensitivity of the consolidated statement of income is the effect of the assumed changes in profit rates on the consolidated net income for the year, based on the non-trading financial assets and financial liabilities held as at the date of statement of financial position.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

34 RISK MANAGEMENT (continued)

34.4 Market risk (continued)

Profit rate risk (continued)

The effect of decrease in basis points is expected to be equal and opposite to the effect of the increase shown.

	2020 BD 000	Change in basis points BD 000	Effect on net income for the year BD 000
ASSETS			
Due from banks	123,590	+25	309
Financing contracts	836,291	+25	2,091
Investment in sukuk	324,739	+25	812
LIABILITIES AND EQUITY OF INVESTMENT ACCOUNT HOLDERS			
Due to banks	108,798	+25	(272)
Due to non-banks	364,048	+25	(910)
Equity of investment account holders	966,177	+25	(2,415)
Total			(385)

	2019 BD 000	Change in basis points BD 000	Effect on net income for the year BD 000
ASSETS			
Due from banks	115,216	+25	288
Financing contracts	770,671	+25	1,927
Investment in sukuk	270,277	+25	676
LIABILITIES AND EQUITY OF INVESTMENT ACCOUNT HOLDERS			
Due to banks	101,783	+25	(255)
Due to non-banks	222,965	+25	(557)
Equity of investment account holders	1,008,369	+25	(2,521)
Total			(442)

Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Bank has established Value at Risk limit for foreign currency exposures. This limit is monitored on a regular basis by the risk management department and reported to the ALCO / RMC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
At 31 December 2020

34 RISK MANAGEMENT (continued)

34.4 Market risk (continued)

Currency risk (continued)

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

	Equivalent long (short) 2020	Equivalent long (short) 2019
	BD 000	BD 000
Currency		
GBP	(1,012)	12
KWD	2,533	122
EUR	(997)	(711)

The table below indicates the currencies to which the Group had significant exposure at 31 December on all its monetary assets and liabilities. The analysis calculates the effect of a reasonably possible movement of the currency rate against the Bahraini Dinar, with all other variables held constant, on the consolidated statement of income.

The effect of decreases in currency rate is expected to be equal and opposite to the effect of the increases shown.

	Change in currency rate	Effect on profit 2020	Change in currency rate	Effect on profit 2019
	%	BD 000	%	BD 000
GBP	+20	(202)	+20	2
KWD	+20	507	+20	24
EUR	+20	(199)	+20	(142)
Total		106		(116)

Equity price risk

Equity price risk is the risk that the fair values of equities decrease as a result of changes in the levels of equity indices and the value of individual stocks. The equity price risk exposure arises from the Group's investment portfolio.

The effect on income and equity (as a result of a change in the fair value of equity instruments) due to a reasonably possible change (i.e. +10%) in the value of individual investments, with all other variables held constant, is nil and BD 686 thousand (2019: nil and BD 440 thousand) respectively, except in cases where impairment loss occured which will result in decrease being taken to the consolidated statement of income.

The effect of decrease in the value of individual investments is expected to be equal and opposite to the effect of the increase shown.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

34 RISK MANAGEMENT (continued)

34.5 Prepayment risk

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

34.6 Operational risk

Operational risk is the risk of loss arising from systems failure, human error, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to financial loss. The Group cannot expect to eliminate all operational risks, but through a control framework and by monitoring and responding to potential risks. The Bank has implemented Risks Controls and Self Assessment process (RCSA) whereby each of the units identifies risks in processes, key risk indicators and implemented controls. The key risk indicators values and actual incidents to the operational risk unit are reported to senior management for action. Controls include effective segregation of duties, access, authorisation and reconciliation procedures, staff education and assessment processes, including the use of internal audit.

35 CAPITAL MANAGEMENT

The Group maintains an actively managed capital base to cover risks inherent in the business. The adequacy of the Group's capital is monitored using, among other measures, the rules and ratios established by the Basel Committee on Banking Supervision ("BIS rules/ratios") and adopted by the Central Bank of Bahrain in supervising the Group. The Bank has also implemented the Internal Capital Adequacy and Assessment Plan (ICAAP) as per the CBB guidelines based on Pillar II recommendations of the Basel Committee. The Bank had identified the capital requirement for future three years based on the Bank's projected financials and the risk charges required for its significant risks including credit risk, market risk, profit rate risk, liquidity risk, investments risks and operational risks. The Board of Directors, on an annual basis, review and approve the ICAAP plan for both normal and stress conditions.

The primary objectives of the Group's capital management are to ensure that the Group complies with externally imposed capital requirements and that the Group maintains healthy capital ratios in order to support its business and to maximise shareholders' value.

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

35 CAPITAL MANAGEMENT (continued)

Regulatory capital and risk-weighted assets

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

	Note	2020 BD 000	2019 BD 000
Common equity Tier 1 capital	35.1	**175,631**	182,079
Tier 2 capital	35.2	**38,567**	59,015
Total capital		**214,198**	241,094
Credit risk-weighted assets		**823,366**	951,189
Market risk-weighted assets		**23,580**	25,320
Operational risk-weighted assets		**136,539**	171,366
Total risk weighted assets		**983,485**	1,147,875
Capital adequacy ratio		**21.8%**	21.0%
Minimum requirement		**12.5%**	12.5%

35.1 Common equity Tier 1 capital comprises of share capital, share premium, general reserve, statutory reserve and retained earnings, less unrealised loss arising from fair valuing equities.

35.2 Tier 2 capital comprises of subordinated wakala payable under unrestricted investment account holder, provisions against stage 1 and stage 2 exposures and asset revaluation reserves. Certain adjustments are made to AAOIFI-based results and reserves, as prescribed by the Central Bank of Bahrain.

36 EARNINGS AND EXPENSES PROHIBITED BY SHARI'A

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

37 SOCIAL RESPONSIBILITY

The Bank discharges its social responsibilities through donations to charitable causes and organisations approved by Shari'a Supervisory Board.

38 COMPARATIVE FIGURES

Certain of the prior year figures have been reclassified to conform to the presentation adopted in the current year. Such reclassification does not affect previously reported net income or owners' equity.

39 MODIFICATION LOSS, GOVERNMENT ASSISTANCE & OTHER MEASURES BY THE CBB TO HELP BANKS COMBAT THE EFFECTS OF COVID-19 PANDEMIC

During the year, based on a regulatory directive issued by the CBB (refer note 2) as concessionary measures to mitigate the impact of COVID-19, the one-off modification losses amounting to BD 18,457 thousand arising from the 6-month payment holidays provided to financing customers without charging additional profits has been recognized directly in equity. The modification loss has been calculated as the difference between the net present value of the modified cash flows calculated using the original effective profit rate and the current carrying value of the financial assets on the date of modification. The Bank provided payment holidays on financing exposures amounting to BD 699,288 thousand as part of its support to impacted customers.

Further, as per the regulatory directive, financial assistance amounting to BD 1,460 thousand (representing specified reimbursement of a portion of staff costs and waiver of fees, levies and utility charges) received from the government and/or regulators, in response to its COVID-19 support measures, have been recognized directly in equity.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

39 MODIFICATION LOSS, GOVERNMENT ASSISTANCE & OTHER MEASURES BY THE CBB TO HELP BANKS COMBAT THE EFFECTS OF COVID-19 PANDEMIC (continued)

The CBB has issued various other measures to help banks combat the effect of COVID-19 and ease liquidity conditions as well as to assist in complying with the regulatory requirements which are as follows:

- Concessionary repo to eligible banks at zero percent profit rate;
- Reduction in cash reserve ratio requirement with CBB from 5% to 3%.
- Reduction in liquidity coverage ratio ("LCR") and net stable funding ratio ("NSFR") from 100% to 80%;
- Aggregate of modification loss and incremental ECL for stage 1 and stage 2 (recorded post March 2020) to be added back to the Tier 1 Capital for the two years ending 31 December 2020 and 31 December 2021. Subsequently from the year ending 31 December 2022, these to be deducted from Tier 1 capital on a straight line basis over the three year period ending 31 December 2024.
- Bank's to be more prudent in determining additional provisions for the period from 1st April to 31 December 2020 considering the economic and financial impact of COVID-19 on its customers.

The aforementioned measures have resulted in the following effects to the Group:

- Since the Group is maintaining adequate liquidity (LCR of 604.90% and NSFR of 112.38%), it was not eligible for the concessionary repo from the CBB and therefore the Group has not applied for this facility.
- The reduction in cash reserve requirement with the CBB has resulted in an average positive impact of BD 18,440 thousand on the Bank's liquidity position.
- The Bank is maintaining adequate liquidity ratios i.e. LCR of 604.90% and NSFR of 112.38% as at 31 December 2020. Although the relaxation is provided by the CBB, the Bank on a prudent basis continues to target 100% as the internal limit for the LCR and the NSFR ratios.
- Based on the above relaxation regarding the adding back of aggregate of modification loss and incremental ECL for Stage 1 and Stage 2 to the Tier 1 Capital, the capital adequacy ratio of the Bank stands at 21.78% as at 31 December 2020.
- Bank has performed a detailed assessment of its financing portfolio and concluded that the current provision levels are suffiiceint. The Bank on a regular basis assesses its financing portfolio for any credit deterioration due to COVID -19 and its resulting impact on the additional ECL requirements.

	Net Impact on the Group's consolidated income statement	Net Impact on the Group's consolidated net assets	Net Impact on the Group's consolidated total equity
	BD 000	BD 000	BD 000
Modification loss	-	(18,457)	(18,457)
Amortisation related to the modification loss	18,457	18,457	18,457
Government assistance	-	1,460	1,460
Total	18,457	1,460	1,460

In addition to the above, reduction in CBB cash reserve ratio has also improved the Group's liquidity by BD 19.8 million. However, there will not be a net increase in the Group's consolidated net assets as the reduction in CBB cash reserve is offset by increase in the other yielding financing assets of the Group.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2020

40 NSFR REQUIREMENTS AND CALCULATION METHODOLOGY

The Net Stable Funding Ratio ('NSFR') is calculated in accordance with the Liquidity Risk Management Module guidelines, issued by the CBB and is effective from 2019. The minimum NSFR ratio as per CBB is 100%. However, based on the regulatory directive issued by the CBB in response to its COVID-19 measures, the minimum NSFR reduced to 80%. The Group's consolidated NSFR ratio as of 31 December 2020 is 112.38%.

The NSFR (as a percentage) is calculated as follows:

	Unweighted Values (i.e. before applying relevant factors)				Reviewed 31 December 2020 BD 000s	Audited 31 December 2019 BD 000s
Item	No specified maturity	Less than 9 months	More than 9 months and less than one year	Over one year	Total weighted value	Total weighted value
Available Stable Funding (ASF):						
Capital:						
Regulatory Capital	176,485	-	-	37,904	**214,390**	242,192
Other Capital Instruments	-	-	-	65,975	**65,975**	47,125
Retail deposits and deposits from small business customers:						
Stable deposits						
Less stable deposits	-	562,058	69,788	37,208	**605,870**	520,031
Wholesale funding:						
Other wholesale funding	-	556,049	160,886	81,282	**280,927**	385,177
Other liabilities:						
All other liabilities not included in the above categories	-	26,836	-	7,741	**7,741**	10,597
Total ASF	176,485	1,144,944	230,674	230,111	**1,174,902**	1,205,122
Required Stable Funding (RSF):						
Total NSFR high-quality liquid assets (HQLA)	351,762	12,888	-	-	**15,566**	12,733
Performing financing and sukuk/securities:						
Performing financing to financial institutions secured by non-level 1 HQLA and unsecured performing financing to financial institutions	-	131,760	-	-	**19,764**	19,950
Performing financing to non-financial corporate clients, financing to retail and small business customers, and financing to sovereigns, central banks and PSEs, of which:	-	-	46,229	536,339	**519,165**	635,867
With a risk weight of less than or equal to 35% as per the CBB Capital Adequacy Ratio guidelines	-	-	-	161,636	**105,064**	-
Performing residential mortgages, of which:						
With a risk weight of less than or equal to 35% under the CBB Capital Adequacy Ratio Guidelines	-	-	-	184,613	**119,998**	97,222
Securities/sukuk that are not in default and do not qualify as HQLA, including exchange- traded equities	-	-	-	20,886	**17,753**	17,753
Other assets:						
All other assets not included in the above categories	246,463	-	-	-	**246,463**	332,290
OBS items	33,590	-	-	-	**1,680**	2,148
Total RSF	631,815	144,648	46,229	903,474	**1,045,451**	1,117,963
NSFR (%)					**112.38%**	107.80%