BURGAN BANK GROUP

CONSOLIDATED FINANCIAL STATEMENTS

31 DECEMBER 2017

Consolidated Statement of Financial Position
As at 31 December 2017

	Notes	***2017*** ***KD 000's***	*2016* *KD 000's*
ASSETS			
Cash and cash equivalents	3	937,174	896,005
Treasury bills and bonds with CBK and others		489,809	479,996
Due from banks and other financial institutions	4	632,010	803,412
Loans and advances to customers	5	4,407,568	4,224,086
Investment securities	6	622,765	554,335
Other assets	7	187,535	180,411
Property and equipment		101,756	89,497
Intangible assets	8	36,595	41,134
TOTAL ASSETS		7,415,212	7,268,876
LIABILITIES AND EQUITY			
LIABILITIES			
Due to banks		883,724	824,676
Due to other financial institutions		975,164	1,208,419
Deposits from customers		4,154,408	3,737,259
Other borrowed funds	10	322,494	437,994
Other liabilities	11	211,762	214,972
TOTAL LIABILITIES		6,547,552	6,423,320
EQUITY			
Share capital	12	215,183	204,936
Share premium	12	210,559	210,559
Treasury shares	12	(2,817)	(12,582)
Statutory reserve	12	81,815	74,997
Voluntary reserve	12	82,193	75,375
Treasury shares reserve	12	43,309	45,082
Investment revaluation reserve		(12,446)	2,732
Share based compensation reserve		564	564
Foreign currency translation reserve		(97,203)	(83,782)
Other reserves		1,503	2,670
Retained earnings		149,752	129,556
Total equity attributable to the equity holders of the Bank		672,412	650,107
Perpetual Tier 1 capital securities	12	144,025	144,025
Non-controlling interests		51,223	51,424
TOTAL EQUITY		867,660	845,556
TOTAL LIABILITIES AND EQUITY		7,415,212	7,268,876

Khalid Al Zouman
Group Chief Financial Officer

Eduardo Eguren Linsen
Group Chief Executive Officer

Majed Essa Al Ajeel
Chairman of the Board

The attached notes 1 to 25 form an integral part of these consolidated financial statements.

Consolidated Statement of Income
For the year ended 31 December 2017

	Notes	***2017*** ***KD 000's***	*2016* *KD 000's*
Interest income	13	337,037	312,215
Interest expense	14	(166,117)	(156,474)
Net interest income		170,920	155,741
Fee and commission income		43,753	41,363
Fee and commission expense		(7,131)	(6,189)
Net fee and commission income		36,622	35,174
Net gain from foreign currencies		9,655	15,552
Net investment income	15	10,019	12,632
Dividend income		3,042	2,843
Other income	5	9,168	12,732
Operating income		239,426	234,674
Staff expenses		(50,825)	(52,674)
Other expenses		(58,366)	(61,084)
Operating profit before provision		130,235	120,916
Provision for loans and advances	5	(41,538)	(41,509)
Provision for investment securities		(8,770)	(3,205)
Profit for the year before taxation and board of directors' remuneration		79,927	76,202
Taxation	16	(10,767)	(9,367)
Board of directors' remuneration		(90)	(90)
Profit for the year		69,070	66,745
Attributable to:			
Equity holders of the Bank		65,223	68,178
Non-controlling interests		3,847	(1,433)
		69,070	66,745
Basic and diluted earnings per share attributable to the equity holders of the Bank (Fils)	17	25.4	27.0

The attached notes 1 to 25 form an integral part of these consolidated financial statements.

Consolidated Statement of Comprehensive Income
For the year ended 31 December 2017

	2017	*2016*
	KD 000's	*KD 000's*
Profit for the year	69,070	66,745
Other comprehensive income (loss)		
Items that are or may be reclassified to consolidated statement of income in subsequent periods:		
Financial assets available for sale:		
Change in fair value, net of provisions	(11,429)	2,717
Net transfer to consolidated statement of income	(3,626)	2,688
Foreign currency translation adjustment	(15,166)	(25,145)
Changes in fair value of cash flow hedges	1,592	1,303
Net (loss) profit on hedge of a net investment	(2,747)	8,472
Other comprehensive loss for the year	(31,376)	(9,965)
Total comprehensive income for the year	37,694	56,780
Attributable to:		
Equity holders of the Bank	35,457	60,759
Non-controlling interests	2,237	(3,979)
	37,694	56,780

The attached notes 1 to 25 form an integral part of these consolidated financial statements.

BURGAN BANK GROUP

Consolidated Statement of Changes in Shareholders' Equity
For the year ended 31 December 2017

	Attributable to equity holders of the Bank												*Perpetual Tier 1 capital securities*	*Non-controlling interests*	*Total equity*
	Share capital	*Share premium*	*Treasury shares*	*Statutory reserve*	*Voluntary reserve*	*Treasury shares reserve*	*Investment revaluation reserve*	*Share based compensation reserve*	*Foreign currency translation reserve*	*Other reserves**	*Retained earnings*	*Total*			
	KD 000's	*KD 000's*	*KD 000's*	*KD 000's*	*KD 000's*	*KD 000's*	*KD 000's*	*KD 000's*	*KD 000's*	*KD 000's*	*KD 000's*	*KD 000's*	*KD 000's*	*KD 000's*	*KD 000's*
Balance at 1 January 2017	204,936	210,559	(12,582)	74,997	75,375	45,082	2,732	564	(83,782)	2,670	129,556	650,107	144,025	51,424	845,556
Profit for the year	-	-	-	-	-	-	-	-	-	-	65,223	65,223	-	3,847	69,070
Other comprehensive loss	-	-	-	-	-	-	(15,178)	-	(13,421)	(1,167)	-	(29,766)	-	(1,610)	(31,376)
Total comprehensive (loss) income	-	-	-	-	-	-	(15,178)	-	(13,421)	(1,167)	65,223	35,457	-	2,237	37,694
Transfer to reserves	-	-	-	6,818	6,818	-	-	-	-	-	(13,636)	-	-	-	-
Bonus shares issued (note 6)	10,247	-	-	-	-	-	-	-	-	-	(10,247)	-	-	-	-
Cash dividend paid (note 12)	-	-	-	-	-	-	-	-	-	-	(10,141)	(10,141)	-	(2,438)	(12,579)
Sale of treasury shares	-	-	9,765	-	-	(1,773)	-	-	-	-	-	7,992	-	-	7,992
Interest payment on Tier 1 capital securities (note 12)	-	-	-	-	-	-	-	-	-	-	(11,003)	(11,003)	-	-	(11,003)
Balance at 31 December 2017	215,183	210,559	(2,817)	81,815	82,193	43,309	(12,446)	564	(97,203)	1,503	149,752	672,412	144,025	51,223	867,660

**Refer note 12 for further break up of other reserves.*

The attached notes 1 to 25 form an integral part of these consolidated financial statements.

BURGAN BANK GROUP

Consolidated Statement of Changes in Shareholders' Equity (continued)
For the year ended 31 December 2017

	Attributable to equity holders of the Bank														
	Share capital KD 000's	*Share premium KD 000's*	*Treasury shares KD 000's*	*Statutory reserve KD 000's*	*Voluntary reserve KD 000's*	*Treasury shares reserve KD 000's*	*Investment revaluation reserve KD 000's*	*Share based compensati on reserve KD 000's*	*Foreign currency translation reserve KD 000's*	*Other reserves* KD 000's*	*Retained earnings KD 000's*	*Total KD 000's*	*Perpetual Tier 1 capital securities KD 000's*	*Non-controlling interests KD 000's*	*Total equity KD 000's*
Balance at 1 January 2016	204,936	210,559	(12,582)	67,859	68,237	45,082	(2,292)	564	(61,557)	(7,112)	122,981	636,675	144,025	55,623	836,323
Profit (loss) for the year	-	-	-	-	-	-	-	-	-	-	68,178	68,178	-	(1,433)	66,745
Other comprehensive Income (loss)	-	-	-	-	-	-	5,024	-	(22,225)	9,782	-	(7,419)	-	(2,546)	(9,965)
Total comprehensive income	-	-	-	-	-	-	5,024	-	(22,225)	9,782	68,178	60,759	-	(3,979)	56,780
Transfer to reserves	-	-	-	7,138	7,138	-	-	-	-	-	(14,276)	-	-	-	-
Cash dividend paid (note 12)	-	-	-	-	-	-	-	-	-	-	(36,375)	(36,375)	-	(220)	(36,595)
Interest payment on Tier 1 capital securities (note 12)	-	-	-	-	-	-	-	-	-	-	(10,952)	(10,952)	-	-	(10,952)
Balance at 31 December 2016	204,936	210,559	(12,582)	74,997	75,375	45,082	2,732	564	(83,782)	2,670	129,556	650,107	144,025	51,424	845,556

**Refer note 12 for further break up of other reserves.*

The attached notes 1 to 25 form an integral part of these consolidated financial statements.

Consolidated Statement of Cash Flows
Year ended 31 December 2017

	Notes	***2017*** ***KD 000's***	*2016* *KD 000's*
Operating activities			
Profit for the year before taxation		79,927	76,202
Adjustments:			
Net investment income	15	(10,019)	(12,632)
Provision for impairment of loans and advances		41,538	41,509
Provision for impairment of investment securities		8,770	3,205
Dividend income		(3,042)	(2,843)
Depreciation and amortisation		12,160	12,410
Other income	22	(6,260)	-
Operating profit before changes in operating assets and liabilities		123,074	117,851
Changes in operating assets and liabilities:			
Treasury bills and bonds with CBK and others		(9,813)	(8,196)
Due from banks and other financial institutions		171,695	(174,625)
Loans and advances to customers		(225,313)	(307,867)
Other assets		(7,124)	(14,878)
Due to banks		59,048	(61,426)
Due to other financial institutions		(233,255)	391,578
Deposits from customers		417,149	(137,085)
Other liabilities		(4,274)	21,091
Taxation paid		(9,793)	(8,668)
Net cash from (used in) operating activities		281,394	(182,225)
Investing activities			
Purchase of investment securities		(1,019,340)	(418,548)
Proceeds from sale of investment securities		942,209	458,945
Purchase of property and equipment		(20,474)	(16,799)
Dividends received		3,042	2,843
Net cash (used in) from investing activities		(94,563)	26,441
Financing activities			
Other borrowed funds	10	(115,500)	219,991
Sale of treasury shares		7,992	-
Cash dividend paid to equity holders of the Bank	12	(10,141)	(36,375)
Cash dividend paid to non-controlling interests		(2,438)	(220)
Interest payment on Tier 1 capital securities		(11,003)	(10,952)
Net cash (used in) from financing activities		(131,090)	172,444
Net increase in cash and cash equivalents		55,741	16,660
Effect of foreign currency translation		(14,572)	(24,064)
Cash and cash equivalents at 1 January		896,005	903,409
Cash and cash equivalents at 31 December	3	937,174	896,005
Additional cash flow information :			
Interest received		318,527	292,989
Interest paid		165,710	130,355

The attached notes 1 to 25 form an integral part of these consolidated financial statements.

1. INCORPORATION AND PRINCIPAL ACTIVITIES

Burgan Bank K.P.S.C. (the "Bank") is a public shareholding company incorporated in the State of Kuwait by Amiri Decree dated 27 December 1975 listed on the Kuwait Stock Exchange and is registered as a bank with the Central Bank of Kuwait ("CBK"). The Bank's registered address is P.O. Box 5389, Safat 12170, State of Kuwait.

The consolidated financial statements of the Bank and its subsidiaries (collectively the "Group") for the year ended 31 December 2017 were authorised for issue in accordance with a resolution of the Board of Directors on _______ 2017 and are issued subject to the approval of the Annual General Assembly of the shareholders of the Bank. The Annual General Assembly of the Shareholders has the power to amend these consolidated financial statements after issuance.

The principal activities of the Group are explained in note 18.

The Bank is a subsidiary of Kuwait Projects Company Holding K.S.C.P ("the Parent Company").

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of preparation
The consolidated financial statements are prepared under the historical cost convention, except for financial assets classified as fair value through profit or loss, certain financial assets classified as available for sale and derivative financial instruments that are measured at fair value.

The consolidated financial statements are presented in Kuwaiti Dinars ("KD"), which is the Bank's functional currency, rounded to the nearest thousand except when otherwise stated.

Statement of compliance
The consolidated financial statements of the Group have been prepared in accordance with the regulations of the State of Kuwait for financial services institutions regulated by the CBK. These regulations require adoption of all International Financial Reporting Standards ("IFRS") as issued by International Accounting Standards Board ("IASB") except for International Accounting Standards ("IAS") 39: Financial Instruments: Recognition and Measurement requirement for collective provision, which has been replaced by the CBK's requirement for a minimum general provision as described under the accounting policies for impairment of financial assets.

Changes in accounting policies and disclosures
The accounting policies used in the preparation of these consolidated financial statements are consistent with those used in the previous financial year, except for the adoption of the amendments to the existing standards relevant to the Group, effective as of 1 January 2017. The nature and the impact of each amendment is described below:

Amendments to IAS 7 Statement of Cash Flows: Disclosure Initiative
The amendments require entities to provide disclosure of changes in their liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes (such as foreign exchange gains or losses). The Group has provided the information for both the current and the comparative period in Note 10.

Amendments to IAS 12 Income Taxes: Recognition of Deferred Tax Assets for Unrealised Losses
The amendments clarify that an entity needs to consider whether tax law restricts the sources of taxable profits against which it may make deductions on the reversal of deductible temporary difference related to unrealised losses. Furthermore, the amendments provide guidance on how an entity should determine future taxable profits and explain the circumstances in which taxable profit may include the recovery of some assets for more than their carrying amount. The Group applied amendments retrospectively. However, their application has no material effect on the Group's financial position and performance as the Group.

Other amendments to IFRSs which are effective for annual accounting period starting from 1 January 2017 did not have any material impact on the accounting policies, financial position or performance of the Group.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

New and revised IASB Standards issued, but not yet effective
Standards and amendments to standards issued but not yet effective up to the date of issuance of the Group's consolidated financial statements which are relevent to the Group are listed below. The Group intends to adopt those standards when they become effective.

IFRS 9: Financial Instruments
The IASB issued the final version of IFRS 9 'Financial Instruments' in July 2014, effective for annual periods beginning on or after 1 January 2018. IFRS 9 sets out the requirements for recognizing and measuring financial assets and financial liabilities, impairment of financial assets and hedge accounting. This standard replaces IAS 39 Financial Instruments: Recognition and Measurement.

The Group has determined 1 January 2018 as the date of application of IFRS 9. The classification, measurement and impairment requirements are applied retrospectively by adjusting the opening consolidated statement of financial position as at the date of application. The Group will not restate the comparatives as permitted by IFRS 9.

Classification and measurement
The classification and measurement of all financial assets except equity instruments and derivatives will depend on the combination of entity's business model for managing the assets and the contractual cash flow characteristics of the instrument. These factors will determine whether the financial assets are measured at amortised cost (AC), fair value through other comprehensive income (FVOCI) or fair value through profit or loss (FVTPL).

Equity instruments are measured at FVTPL. However, the Group may, at initial recognition of the equity instrument, irrevocably elect to designate the instrument as FVOCI, with no subsequent recycling to consolidated statement of income. IFRS 9 will also allow entities to continue or irrevocable designate instruments that qualify to be classified as FVOCI or AC as FVTPL, if this results in elimination or reduction in any mismatch in measurement or recognition. Derivatives are measured at fair value.

The classification and measurement of financial liabilities will remain similar to IAS 39 except for the treatment of gains and losses on own credit risk arising from liabilities designated at FVTPL which will be taken through other comprehensive income (OCI) with no subsequent recycling to consolidated statement of income.

Based on the assessment done by the Group, the adoption of this standard will result in reclassification of financial assets held to maturity to financial assets carried at FVOCI and financial assets carried at AC based on business model being used by the Group to manage those assets. Further, certain equity instruments and managed funds carried as financial assets available for sale will be reclassified to financial assets carried at FVTPL. The adoption of this standard is not expected to have any impact on its financial liabilities.

Hedge accounting
The Group determined that all existing hedge relationships that are currently designated in effective hedging relationships will continue to qualify for hedge accounting under IFRS 9. As IFRS 9 does not change the general principles of how an entity accounts for effective hedges, applying the hedging requirements of IFRS 9 will not have a significant impact on Group's consolidated financial statements.

Impairment of financial assets
The impairment requirement applies to financial assets measured at AC, debt instrument classified as FVOCI, lease receivables, loan commitments and financial guarantee contracts. The impairment under IFRS 9 fundamentally changes the methodology of identification of credit loss from the current "incurred loss" model of IAS 39 to a forward looking expected credit loss (ECL) model.

At initial recognition and reporting date if there has not been a significant increase in credit risk since initial recognition and credit loss allowance is required for ECL resulting from default events that are possible within the next 12 months ("12 months ECL"). If there has been a significant increase in credit risk since initial recognition then credit loss allowance is required for ECL resulting from all possible default events over the expected life of the financial instrument ("Life time ECL").

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

New and revised IASB Standards issued, but not yet effective (continued)

IFRS 9: Financial Instruments (continued)

The assessment of credit risk and the estimation of ECL are based on models, methodologies and assumptions incorporating all available relevant information including past events, current conditions and reasonable forecasts of future economic conditions as at the reporting date, taking into account the time value of money.

The bank will determine the potential impact of the expected credit losses provision stipulated within IFRS (9) in the Financial Statements as at 31/3/2018. The bank will adhere to the instructions that will be issued by CBK in this regard.

IFRS 15 – Revenue from Contracts with customers
In May 2014, the IASB issued IFRS 15 Revenue from Contracts with Customers, effective for periods beginning on 1 January 2018 with early adoption permitted. IFRS 15 defines principles for recognising revenue and will be applicable to all contracts with customers. However, interest and fee income integral to financial instruments and leases will continue to fall outside the scope of IFRS 15 and will be regulated by the other applicable standards (e.g., IFRS 9, and IFRS 16 Leases).

Revenue under IFRS 15 will need to be recognised as goods and services are transferred, to the extent that the transferor anticipates entitlement to goods and services. The standard will also specify a comprehensive set of disclosure requirements regarding the nature, extent and timing as well as any uncertainty of revenue and corresponding cash flows with customers.

The Group did not early adopt IFRS 15 and has evaluated that the adoption of the standard will not have significant impact on the Group’s consolidated financial statements.

IFRS 2 Classification and Measurement of Share-based Payment Transactions — Amendments to IFRS 2
The IASB issued amendments to IFRS 2 Share-based Payment that address three main areas: the effects of vesting conditions on the measurement of a cash-settled share-based payment transaction; the classification of a share based payment transaction with net settlement features for withholding tax obligations; and accounting where a modification to the terms and conditions of a share-based payment transaction changes its classification from cash settled to equity settled.

On adoption, entities are required to apply the amendments without restating prior periods, but retrospective application is permitted if elected for all three amendments and other criteria are met. The amendments are effective for annual periods beginning on or after 1 January 2018, with early application permitted. The Group is assessing the potential effect of the amendments on its consolidated financial statements and do not expect significant impact on adoption of this standard.

IFRS 16 Leases
The IASB issued the new standard for accounting for leases - IFRS 16 Leases in January 2016. The new standard does not significantly change the accounting for leases for lessors. However, it does require lessees to recognise most leases on their balance sheets as lease liabilities, with the corresponding right- of-use assets. Lessees must apply a single model for all recognised leases, but will have the option not to recognise ‘short-term’ leases and leases of ‘low-value’ assets. Generally, the profit or loss recognition pattern for recognised leases will be similar to today’s finance lease accounting, with interest and depreciation expense recognised separately in the consolidated statement of income. IFRS 16 is effective for annual periods beginning on or after 1 January 2019. Early application is permitted provided the new revenue standard, IFRS 15, is applied on the same date. Lessees must adopt IFRS 16 using either a full retrospective or a modified retrospective approach. The Group does not anticipate early adopting IFRS 16 and is in the process of evaluating the effect of IFRS 16 on the Group and do not expect any significant impact on adoption of this standard.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Basis of consolidation

The consolidated financial statements comprise the financial statements of the Bank and its subsidiaries (investees which are controlled by the Bank). Control is achieved when the Group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Specifically, the Group controls an investee if and only if the Group has:

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

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

- The contractual arrangement with the other vote holders of the investee
- Rights arising from other contractual arrangements
- The Group's voting rights and potential voting rights

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

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

A change in the ownership interest of a subsidiary, without a loss of control, is accounted for as an equity transaction.

If the Group loses control over a subsidiary, it derecognises the related assets (including goodwill), liabilities, non-controlling interest and other components of equity while any resultant gain or loss is recognised in profit or loss. Any investment retained is recognised at fair valueat the date of loss of control.

The principal operating subsidiaries of the Group are as follows:

Name of company	*Principal activities*	*Country of incorporation*	***Effective interest as at 31 December 2017***	*Effective interest as at 31 December 2016*
Algeria Gulf Bank S.P.A. ("AGB")	Banking	Algeria	86.01%	86.01%
Bank of Baghdad P.J.S.C. ("BoB")	Banking	Iraq	51.79%	51.79%
Tunis International Bank S.A ("TIB")	Banking	Tunisia	86.70%	86.70%
Burgan Bank A.S. ("BBT")	Banking	Turkey	99.26%	99.26%
Burgan Bank Financial Services Limited("BBFS")	Financial Advisory Services	Dubai	100.00%	100.00%
Held through BoB				
Baghdad Brokerage Company	Brokerage	Iraq	51.79%	51.79%
Al Amin Insurance Brokerage Co.	Brokerage	Iraq	26.29%	26.29%

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Basis of consolidation (continued)

Held through BBT

Burgan Finansal Kiralama A.S	Leasing	Turkey	99.26%	99.26%
Burgan Yatirim Menkul Degerler A.S.	Brokerage	Turkey	99.26%	99.26%
Burgan Portfoy Yonetimi A.S.	Asset Management	Turkey	99.26%	99.26%
Burgan Wealth Limited	Wealth Management Services	Dubai	99.26%	99.26%

Name of company	***Principal activities***	***Country of incorporation***	***Effective interest as at 31 December 2017***	*Effective interest as at 31 December 2016*
Structuredentity ("SPVs") treated as a subsidiary				
Burgan Tier 1 Financing Limited	Special purpose entity	Dubai	100%	100%
Burgan Senior SPC Limited	Special purpose entity	Dubai	100%	100%

Financial instruments

Classification of financial instruments

The Group classifies financial instrumentsas at "fair value through profit or loss", "loans and receivables", "available for sale", "held to maturity" and "financial liabilities at amortised cost". Management determines the appropriate classification of each instrument at initial recognition.

Recognition/de-recognition

A financial asset or a financial liability is recognised when the Group becomes a party to the contractual provisions of the instrument. All regular way purchase and sale of financial assets are recognised using settlement date accounting. Changes in fair value between the trade date and settlement date are recognised in the consolidated statement of income or in OCI in accordance with the policy applicable to the related instrument. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame generally established by regulations or conventions in the market place.

A financial asset (in whole or in part) is derecognised either when: the contractual rights to receive cash flows from the asset have expired; or the Group has transferred its rights to receive cash flows from the assets or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass through' arrangement; and either (a) the Group has transferred substantially all the risks and rewards of the asset, or (b) the Group has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset. Where the Group has transferred its right 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.

A financial liability is derecognised when the obligation specified in the contract is discharged, cancelled or expired. When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as the derecognition of the original liability and the recognition of a new liability. The difference in the respective carrying amounts is recognised in the consolidated statement of income.

Measurement

All financial assets or financial liabilities are initially measured at fair value. Transaction costs are added only for those financial instruments not measured at fair value through profit or loss. Transaction costs on financial assets at fair value through profit or loss are recognised in the consolidated statement of income.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial instruments (continued)

Measurement (continued)

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss includes financial assets held for trading and financial assets designated upon initial recognition as at fair value through profit or loss. Financial assets are classified as held for trading if they are acquired for the purpose of selling or buying in the near term. Changes in fair value are recognised in net investment income. Interest earned is accrued in interest income, using the effective interest rate (EIR), while dividend income is recorded under operating income, in the consolidated statement of income, when the right to receive the payment has been established.

Financial assets are designated as at fair value through profit or loss, if they are managed and their performance is evaluated on reliable fair value basis in accordance with documented investment strategy.

After initial recognition financial assets at fair value through profit or loss are remeasured at fair value with all changes in fair value recognised in the consolidated statement of income.

Derivative instruments are categorised as held for trading unless they are designated as hedging instruments.

Financial assets held to maturity

Non-derivative financial assets with fixed or determinable payments and fixed maturities are classified as held to maturity when the Group has the positive intention and ability to hold to maturity.

After initial recognition, held to maturity financial assets are carried at amortised cost using the EIR method, less impairment losses, if any. The calculation takes into account any premium or discount on acquisition and includes transaction costs and fees that are an integral part of the effective interest rate.

Loans and receivables

These are non-derivative financial assets having fixed or determinable payments that are not quoted in an active market. These are subsequently measured at amortised cost using the effective yield method adjusted for impairment losses, if any.

Treasury bills and bonds with CBK and others, due from banks and OFIs, and loans and advances to customers are classified as “loans and receivables”.

Financial assets available for sale

Financial assets available for sale include equity and debt securities. Equity investments classified as available for sale are those that do not qualify to be classified as loans and receivables, held to maturity or at fair value through profit or loss. Debt securities in this category are those which are intended to be held for an indefinite period of time that may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices.

These are subsequently measured at fair value with gains and losses being recognised as other comprehensive income in the equity as "investment revaluation reserve" until the financial assets are derecognised or until the financial assets are determined to be impaired at which time the cumulative gains and losses previously reported as OCI in equity are transferred to the consolidated statement of income. Financial assets whose fair value cannot be reliably measured are carried at cost less impairment losses, if any.

Financial liabilities at amortised cost

These financial liabilities are subsequently measured at amortised cost using the EIR. “Due to banks”, “due to other financial institutions (“OFI”)”, “deposit from customers”, “other borrowed funds”, and “other liabilities” are classified as “financial liabilities at amortised cost”.

Financial guarantees

In the ordinary course of business, the Group gives financial guarantees, consisting of letters of credit, guarantees and acceptances. Financial guarantees are initially recognised in the consolidated financial statements at fair value, being the premium received. The premium received is amortised in the consolidated statement of income in 'fee and commission income' on a straight line basis over the life of the guarantee. The guarantee liability is subsequently measured as higher of the amount initially recognised less amortisation or the value of any financial obligation that may arise as a result of financial guarantee. Any increase in the liability relating to financial guarantees is recorded in the consolidated statement of income.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Derivative financial instruments
The Group makes use of derivative instruments to manage exposures to interest rate, foreign currency and credit risks.

Where derivative contracts are entered into by specifically designating such contracts as a fair value hedge or a cash flow hedge of a recognised asset or liability, the Group accounts for them using hedge accounting principles, provided certain criteria are met. Derivatives are carried as financial assets when the fair value is positive and as financial liabilities when the fair value is negative.

For derivative contracts that do not qualify for hedge accounting, any gains or losses arising from changes in fair value of the derivative contract are taken directly to the consolidated statement of income.

Hedge accounting
For the purposes of hedge accounting, hedges are classified into two categories: (a) fair value hedges when hedging the exposure to changes in the fair value of a recognised asset or liability or an unrecognised firm commitment; and (b) cash flow hedges, when hedging exposure to variability in cash flows that is either attributable to a particular risk associated with a recognised asset or liability or a highly probable forecast transaction or a foreign currency risk in an unrecognised firm commitment.

When a financial instrument is designated as a hedge, the Group formally documents the relationship between the hedging instrument and hedged item as well as its risk management objectives and its strategy for undertaking the various hedging transactions. The Group also document its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows attributable to the hedge risk.

The Group discontinues hedge accounting when the following criteria are met:

a) it is determined that the hedging instrument is not, or has ceased to be, highly effective as a hedge;
b) the hedging instrument expires, or is sold, terminated, or exercised;
c) the hedged item matures or is sold or repaid; or
d) a forecast transaction is no longer deemed highly probable.

Fair value hedges
The changes in fair value of the hedging instrument that qualify and is designated as fair value hedge is recorded in the consolidated statement of income, together with changes in the fair value of the hedged asset or liability that are attributable to the hedged risk.

If the hedge accounting is discontinued, the fair value adjustment to the hedged item is amortised to the consolidated statement of income over the period to maturity of the previously designated hedge relationship using the EIR.

If the hedged item is derecognised, the unamortised fair value is recognised immediately in the consolidated statement of income.

When an unrecognised firm commitment is designated as a hedged item, the subsequent cumulative change in the fair value of the firm commitment attributable to the hedged risk is recognised as an asset or liability with a corresponding gain or loss recognised in consolidated statement of income.

Cash flow hedges
For qualifying cash flow hedges, the fair value gain or loss associated with the effective portion of the cash flow hedge is recognised initially in OCI, and transferred to the consolidated statement of income in the periods when the hedged transaction affects consolidated statement of income. Any ineffective portion of the gain or loss on the hedging instrument is recognised immediately in the consolidated statement of income.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in other comprehensive income at that time remains in other comprehensive income and is recognised when the hedged forecast transaction is ulimately recognised in the consolidated statement of income. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was recognised in other comprehensive income is immediately transferred to the consolidated statement of income.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Derivative financial instruments (continued)

Hedge accounting (continued)

Hedge of net investment in a foreing operation

Hedges of net investments in a foreign operation, including a hedge of a monetary item that is accounted for aspart of the net investment, are accounted for in a way similar to cash flow hedges. Gains or losses on the hedging instrument relating to the effective portion of the hedge are recognised in other comprehensive income while any gains or losses relating to the ineffective portion are recognised in the consolidated statement of income. On disposal of the foreign operation, the cumulative value of any such gains or losses recognised in other comprehensive income is transferred to the consolidated statement of income.

Fair value measurement

The Group measures financial instruments, such as, derivatives, investment securities etc., at each balance sheet date. Also, fair values of financial instruments measured atamortised cost are disclosed in note 22.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderlytransaction between market participants at the measurement date. The fair value measurement is based on thepresumption that the transaction to sell the asset or transfer the liability takes place either:

- In the principal market for the asset or liability, or
- In the absence of a principal market, in the most advantageous market for the asset or liability

The principal or the most advantageous market must be accessible to by the Group.

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

A fair value measurement of a non-financial asset takes into account a market participant's ability to generateeconomic benefits by using the asset in its highest and best use or by selling it to another market participantthat would use the asset in its highest and best use.

The Group uses valuation techniques that are appropriate in the circumstances and for which sufficient data areavailable to measure fair value, maximising the use of relevant observable inputs and minimising the use ofunobservable inputs.

All assets and liabilities for which fair value is measured or disclosed in the consolidated financial statements are categorisedwithin the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fairvalue measurement as a whole:

- Level 1 — Quoted (unadjusted) market prices in active markets for identical assets or liabilities
- Level 2 — Valuation techniques for which the lowest level input that is significant to the fair valuemeasurement is directly or indirectly observable
- Level 3 — Valuation techniques for which the lowest level input that is significant to the fair valuemeasurement is unobservable

For financial instruments quoted in an active market, fair value is determined by reference to quoted market prices. Bid prices are used for assets and offer prices are used for liabilities. The fair value of investments in mutual funds, unit trusts or similar investment vehicles are based on the last published net assets value.

For unquoted financial instruments fair value is determined by reference to the market value of a similar investment, discounted cash flows, other appropriate valuation models or brokers’ quotes.

For financial instruments carried at amortised cost, the fair value is estimated by discounting future cash flows at the current market rate of return for similar financial instruments.

For investments in equity instruments, where a reasonable estimate of fair value cannot be determined, the investment is carried at cost.

For assets and liabilities that are recognised in the consolidated financial statements on a recurring basis, the Groupdetermines whether transfers have occurred between Levels in the hierarchy by re-assessing categorisation(based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Fair value measurement (continued)

For the purpose of fair value disclosures, the Group has determined classes of assets and liabilities on the basisof the nature, characteristics and risks of the asset or liability and the level of the fair value hierarchy asexplained above.

Amortised cost

This is computed using the effective interest method less any allowance for impairment. The calculation takes into account any premium or discount on acquisition and includes transaction costs and fees that are an integral part of the effective interest rate.

Offsetting of financial instruments

Financial assets and financial liabilities are offset and the net amount reported in the consolidated statement of financial position, if there is a currently enforceable legal right to offset and intends to settle on a net basis, to realise the asset and settle the liability simultaneously.

Assets pending sale

The Group occasionally acquires non-monetary assets in settlement of certain loans and advances. Such assets are stated at the lower of the carrying value of the related loans and advances and the current fair value. Gains or losses on disposal, and revaluation losses, are recognised in the consolidated statement of income.

Impairment of financial assets

The Group assesses at each reporting date whether there is an objective evidence that a specific financial asset or a group of financial assets are impaired. A financial asset or a group of financial assets is deemed to be impaired, if and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

Objective evidence that a specific financial asset or a group of financial assets classified as loans and receivables are impaired includes whether any payment of principal or interest is overdue by more than 90 days or there are any known difficulties in the cash flows including the sustainability of the counterparty's business plan, credit rating downgrades, breach of original terms of the contract, its ability to improve performance once a financial difficulty has arisen, deterioration in the value of collateral etc. The Group assess whether objective evidence of impairment exists on an individual basis for each individually significant asset and collectively for others not deemed individually significant except for financial assets classified as due from banks and financial institutions and loans and receivables where minimum general provision as per CBK's instructions is followed.

The impairment loss for financial assets classified as loans and receivables is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows including amounts recoverable from collateral and guarantees, discounted at the financial asset's original effective interest rate. If the financial asset has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the consolidated statement of income.

For debt instruments classified as available-for-sale, the Group assesses individually whether there is objective evidence of impairment based on the same criteria as financial assets classified as loans and receivables. However, the amount recorded for impairment is the cumulative loss measured as the difference between the amortised cost and the current fair value, less any impairment loss on that investment previously recognised in the consolidated statement of income. If, in a subsequent period, the fair value of a debt instrument increases and the increase can be objectively related to a credit event occurring after the impairment loss was recognised in the consolidated statement of income, the impairment loss is reversed through the consolidated statement of income.

In the case of equity instruments classified as 'available for sale', a significant or prolonged decline in the fair value of the security below its cost is considered in determining whether the assets are impaired. If any evidence of impairment exists, the cumulative loss measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in the consolidated statement of income, is recognised in the consolidated statement of income. Subsequent increases in fair value of such available for sale equity instruments are not reversed through the consolidated statement of income.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Impairment of financial assets (continued)
For non-equity financial assets, the carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the consolidated statement of income. If, in a subsequent period, 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 by adjusting the allowance account.

In addition, in accordance with CBK instructions, a minimum general provision is made on all applicable credit facilities (net of certain categories of collateral) that are not provided for specifically.

Financial assets are written off when there is no realistic prospect of recovery.

Renegotiated loans
In the event of a default, the Group seeks to restructure loans rather than take possession of collateral. This may involve extending the payment arrangements and the agreement of new loan conditions. When the terms and conditions of these loans are renegotiated, the terms and conditions of the new contractual arrangement apply in determining whether these loans remain past due. Management continually reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur.

Repurchase and reverse repurchase agreements
Assets sold with a simultaneous commitment to repurchase at a specified future date at an agreed price (repos) are not derecognised in the consolidated statement of financial position as the Group retains substaintially all the risks and rewards of ownership. The corresponding cash received is recognised in the consolidated statement of financial position as an asset with a corresponding obligation to return it, including the accrued interest as a liability, reflecting the transaction's economic substance as loan to the Group. The difference between the sale and repurchase price is treated as interest expense using the effective interest rate method.

Conversely, assets purchased with a corresponding commitment to resell at a specified future date at an agreed price (reverse repos) are not recognised in the consolidated statement of financial position. Amounts paid under these agreements are treated as interest earning assets and the difference between the purchase and resale price treated as interest income using the effective interest rate method.

Cash and cash equivalents
Cash and cash equivalents comprises of cash in hand and in current account with banks and OFIs and balances with CBK and due from banks and OFIs with original maturities not exceeding thirty days from acquisition date.

Investment in associate
The Group's investment in its associate is accounted for using the equity method. An associate is an entity in which the Group has significant influence. Significant influence is the power to participate in the financial and operating policy decisions of the investee, but is not control or joint control over those policies.

Under the equity method, the investment in associate is carried in the consolidated statement of financial position at cost plus post acquisition changes in the Group's share of net assets of the associate. Goodwill relating to the associate is included in the carrying amount of the investment and is neither amortised nor individually tested for impairment.

The consolidated statement of income reflects the share of the results of operations of the associate. Where there has been a change recognised directly in the other comprehensive income of the associate, the Group recognises its share of any changes and discloses this, when applicable, in the statement of changes in equity. Unrealised gains and losses resulting from transactions between the Group and the associate are eliminated to the extent of the interest in the associate.

The Group's share of profit of an associate is shown on the face of the consolidated statement of income. This is the profit attributable to equity holders of the associate and therefore is profit after tax and non-controlling interest in the subsidiaries of the associate.

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

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Investment in associate (continued)
After application of the equity method, the Group determines whether it is necessary to recognise an additional impairment loss on the Group's investment in its 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.

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

Property and equipment
Property and equipment are stated at cost less accumulated depreciation and impairment losses. Depreciation is provided on all premises and equipment, other than freehold land, at rates calculated to write off the cost of each asset on a straight line basis to their residual values over its estimated useful life. Freehold land is stated at cost less impairment losses.

The estimated useful lives of the assets for the calculation of depreciation are as follows:

Buildings	20 to 35 years
Furniture and equipment	4 to 11 years
Motor vehicles	3 to 7 years
Computers	5 years

When assets are sold or retired, their cost and accumulated depreciation are eliminated from the accounts and any gain or loss resulting from their disposal is recognised in the consolidated statement of income.

The carrying amounts of property and equipment are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, the assets are written down to their recoverable amounts and the impairment loss is recognised in the consolidated statement of income.

Expenditure incurred to replace a component of an item of property and equipment that is accounted for separately is capitalised and the carrying amount of the component that is replaced is written off. Other subsequent expenditure is capitalised only when it increases future economic benefits of the related item of property and equipment. All other expenditure is recognised in the consolidated statement of income as the expense is incurred.

Intangible assets
Intangible assets represent separately identifiable non-monetary assets without physical substance arising from business combinations. Intangible assets are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is the fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses.

The useful lives of intangible assets are assessed as finite.

Intangible assets with finite lives are amortised over the useful economic life, as mentioned below, and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset with a finite useful economic life is reviewed at least at each financial position date. Changes in the expected useful economic life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortisation period or method, as appropriate, and are treated as changes in accounting estimates. The amortisation expense on intangible assets with finite lives is recognised in the consolidated statement of income under "other expenses" consistent with the function of the intangible asset.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Intangible assets (continued)
Amortisation is calculated using the straight-line method to write down the cost of intangible assets over their estimated useful economic lives as follows:

Banking license	10 to 30 years
Customer relationships and core deposits	5 to 10 years

Gains or losses arising from derecognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognised in the consolidated statement of income when the asset is derecognised. A previously recognisedimpairment loss is reversed only if there has been achange in the assumptions used to determine the asset'srecoverable amount since the last impairment loss was recognised.

Leases
The determination of whether an arrangement is, or contains, a lease is based on the substance of the arrangement at inception date: whether fulfillment of the arrangement is dependent on the use of a specific asset or assets or the arrangement conveys a right to use the asset.

Group as a lessee
Leases that do not transfer to the Group substantially all the risks and benefits incidental to ownership of the leased items are operating leases. Operating lease payments are recognised as an expense in the consolidated statement of income on a straight-line basis over the lease term. Contingent rental payable is recognised as an expense in the period in which they are incurred.

Group as a lessor
Leases where the Group does not transfer substantially all of the risk and benefits of ownership of the asset are classified as operating leases. Initial direct costs incurred in negotiating operating leases are added to the carrying amount of the leased asset and recognised over the lease term on the same basis as rental income. Contingent rents are recognised as revenue in the period in which they are earned.

Business combinations and goodwill
A business combination is the bringing together of separate entities or businesses into one reporting entity as a result of one entity, the acquirer, obtaining control of one or more other businesses. The acquisition method of accounting is used to account for business combinations. Under this method, the acquirer recognises, separately from goodwill, identifiable assets acquired, liabilities assumed and any non-controlling interests in the acquiree at the acquisition date.

The identifiable assets acquired and the liabilities assumed at the acquisition date are measured at fair values. For each business combination, the Group elects whether to measure the non-controlling interests in the acquiree at fair value or at the proportionate share of the acquiree's identifiable net assets. Acquisition costs incurred are expensed in the period in which they are incurred.

If the business combination is achieved in stages, the acquisition date fair value of the acquirer's previously held equity interest in the acquiree is remeasured to fair value at the acquisition date through the consolidated statement of income. It is then considered in the determination of goodwill.

Goodwill arising in a business combination is recognised as of the acquisition date as the excess of :

a) the aggregate of the consideration transferred, the amount of any non-controlling interests in the acquiree measured at fair value or at the non-controlling interest's proportionate share of the acquiree's
b) identifiable net assets and the acquisition-date fair value of the acquirer's previously held equity interest in the acquiree; over
c) the net of the acquisition-date amounts of the identifiable assets acquired and the liabilities assumed measured at their fair values.

If the aggregate consideration transferred is lower than the fair value of the net assets of the subsidiary acquired, the difference is recognised in consolidated statement of income.
Goodwill is allocated to each of the Group's cash-generating units or for groups of cash-generating units and is tested annually for impairment and is assesssed regularly whether there is any indication of impairment. Goodwill impairment is determined by assessing the recoverable amount of cash-generating unit to which goodwill relates.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Business combinations and goodwill (continued)
The recoverable value is the higher of the fair value less costs to sell and its value in use of the cash-generating unit, which is the net present value of estimated future cash flows expected from such cash-generating unit. If the recoverable amount of cash-generating unit is less than the carrying amount of the unit, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets of the unit prorated on the basis of the carrying amount of each asset in the unit. Any impairment loss recognised for goodwill is not reversed in the subsequent period.

Where goodwill forms part of a cash-generating unit (group of cash-generating units) and part of the operations within that unit is disposed off, the goodwill associated with the operation disposed off is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation.

End of service indemnity
Provision is made under the Kuwait Labour Law, employee contracts and respective applicable laws in the countries where the subsidiaries operate. This liability, which is unfunded, represents the amount payable to each employee and is a reliable approximation of the present value of the final obligation.

Treasury shares
The Bank's holding in its own shares is stated at acquisition cost and is recognised in shareholders' equity. Treasury shares are accounted for using the cost method. Under this method, the weighted average cost of the shares reacquired is charged to a contra account in the equity. When the treasury shares are reissued, gains are credited to a separate account in equity, "treasury shares reserve", which is not distributable.

Any realised losses are charged to the same account to the extent of the credit balance on that account. Any excess losses are charged to retained earnings then to the voluntary reserve and statutory reserve. Gains realised subsequently on the sale of treasury shares are first used to offset any previously recorded losses in the order of reserves, retained earnings and the treasury shares reserve account. These shares are not entitled to any cash dividend that the Bank may propose. The issue of bonus shares increases the number of shares proportionately and reduces the average cost per share without affecting the total cost of treasury shares.

Share based compensation
The Group operates an equity settled share based compensation plan. The cost of share based compensation transactions with employees is measured by reference to the fair value at the date on which they are granted. The total amount to be expensed over the vesting period is determined by reference to the fair value of the options or shares on the date of grant using the Black Scholes model. Measurement inputs include share price on grant date, exercise price, volatility, risk free interest rate and expected dividend yield. At each reporting date, the Group revises its estimates of the number of options that are expected to become exercisable. It recognises the impact of the revision of original estimates, if any, in the consolidated statement of income, with a corresponding adjustment to equity.

Other reserve
Other reserve is used to record the effect of changes in ownership interest in subsidiaries, without loss of control, changes in fair value of cash flow hedges and hedge of net investments in foreign operations.

Revenue recognition
Interest and similar income and expense
Interest income and expense are recognised in the consolidated statement of income for all financial instruments measured at amortised cost, interest bearing assets classified as available-for-sale and financial instruments designated at fair value through profit or loss using effective interest rate method. The effective interest rate is the rate that exactly discounts estimated future cash flows through the expected life of the financial instrument or, a shorter period, when appropriate, to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, all fees and points paid or received between parties to the contract, transaction costs and all other premiums or discounts are considered, but not future credit losses.

Once a financial instrument is impaired, interest is thereafter recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Revenue recognition (continued)

Interest and similar income and expense (continued)

When the Group enters into an interest rate swap to change interest from fixed to floating (or vice versa) the amount of interest income or expense is adjusted by the net interest on the effective portion of the swap. All fees paid or recieved are treated as an integral part of the effective interest rate of financial instruments and are recognised over their lives, except when the underlying risk is sold to a third party, at which time it is recognised immediately.

Fee and commission income

Fee and commission earned for the provision of services over a period of time are accrued over that period. These fee include credit related fee and other management fees. Loan commitment fee and originating fee that are an integral part of the effective interest rate of a loan are recognised (together with any incremental cost) as an adjustment to the effective interest rate on loan.

Dividend income

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

Foreign 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.

Transactions in foreign currencies are initially recorded at the spot rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the spot rate of exchange ruling at the reporting date. Any resultant gains or losses are recognised in the consolidated statement of income.

Non-monetary assets and liabilities in foreign currencies that are stated at fair value are translated to respective entity's functional currency at the foreign exchange rates ruling on the dates that the values were determined. In case of non-monetary assets whose change in fair values are recognised directly in OCI, foreign exchange differences are recognised directly in OCI and for non-monetary assets whose change in fair value are recognised directly in the consolidated statement of income, foreign exchange differences are recognised in the consolidated statement of income.

As at the reporting date, the assets and liabilities of subsidiaries are translated into the Bank's presentation currency (KD) at the rate of exchange ruling on the reporting date, and their statement of incomes are translated at the average exchange rates for the year. Exchange differences arising on translation are taken directly to OCI. On disposal of a foreign subsidiary, the deferred cumulative amount recognised in OCI relating to that particular subsidiary is recognised in the consolidated statement of income.

Any goodwill or fair value adjustments to the carrying amounts of assets and liabilities arising on acquisition are treated as assets and liabilities of the respective subsidiaries and translated at the rate of exchange ruling on the reporting date.

Taxation

National Labour Support Tax (NLST)

The Bank calculates the NLST in accordance with Law No. 19 of 2000 and the Ministry of Finance Resolutions No. 24 of 2006 at 2.5% of taxable profit for the year. As per law, cash dividends from listed companies which are subjected to NLST have been deducted from the profit for the year.

Kuwait Foundation for the Advancement of Sciences (KFAS)

The Bank calculates the contribution to KFAS at 1% in accordance with the calculation based on the Foundation's Board of Directors resolution.

Zakat

Contribution to Zakat is calculated at 1% of the profit of the Bank in accordance with Law No. 46 of 2006 and the Ministry of Finance resolution No. 58/2007 effective from 10 December 2007.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Taxation (continued)

Taxation on overseas subsidiaries

Taxation on overseas subsidiaries is calculated on the basis of the tax rates applicable and prescribed according to the prevailing laws, regulations and instructions of the countries where these subsidiaries operate. Income tax payable on taxable profit ('current tax') is recognised as an expense in the period in which the profits arise in accordance with the fiscal regulations of the respective countries in which the Group operates.

Deferred tax is provided using the liability method on temporary differences between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes at the reporting date.

Deferred tax assets are recognised for all deductible temporary differences, the carry forward of unused tax credits and any unused tax losses. Deferred tax assets are recognised to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry forward of unused tax credits and unused tax losses can be utilised, except when the deferred tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Unrecognised deferred tax assets are re-assessed at each reporting date and are recognised to the extent that it has become probable that future taxable profits will allow the deferred tax asset to be recovered.

Deferred tax assets and deferred tax liabilities are offset if a legally enforceable right exists to set off current tax assets against current income tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

Deferred tax assets and liabilities are measured using tax rates and applicable legislation at the reporting date.

Segment information

A segment is a distinguishable component of the Group that engages in business activities from which it earns revenue and incurs costs. The operating segments are used by the management of the Bank to allocate resources and assess performance. Operating segments exhibiting similar economic characteristics, product and services, class of customers where appropriate are aggregated and reported as reportable segments.

Contingencies

Contingent assets are not recognised in the consolidated financial statements, but are disclosed when an inflow of economic benefit is probable.

Contingent liabilities are not recognised in the consolidated financial statements, but are disclosed unless the possibility of an outflow of resources embodying economic benefit is remote.

Fiduciary assets

Assets and related deposits held in trust or in a fiduciary capacity are not treated as assets or liabilities of the Group and accordingly are not included in the consolidated statement of financial position.

Significant accounting judgments, estimates and assumptions

The preparation of the Group's consolidated financial statements requires management to make judgements, estimates and assumptions that affect the reported amount of revenues, expenses, assets and liabilities, and the accompanying disclosures, as well as the disclosure of contingent liabilities. Uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of assets or liabilities affected in future periods.

Judgments

In the process of applying the Group's accounting policies, management has made the following judgements, apart from those involving estimations, which have the most significant effect on the amounts recognised in the consolidated financial statements:

Classification of financial assets

On acquisition of financial assets, management decides whether it should be classified as investments at fair value through profit or loss or investments available for sale or loans and receivables or held to maturity.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Significant accounting judgments, estimates and assumptions (continued)

Judgments (continued)

Impairment of financial assets available for sale

The Group treats available for sale equity investments as impaired when there has been a significant or prolonged decline in the fair value below its cost or where other objective evidence of impairment exists. The determination of what is "significant" or "prolonged" requires considerable judgement. In making this judgement, the Group evaluates, among other factors, historical share price movements and duration and extent to which the fair value of an investment is less than its cost.

Deferred tax assets

Deferred tax assets are recognised in respect of tax losses to the extent that it is probable that future taxable profits will be available against which the losses can be utilised. Judgment is required to determine the amount of deferred tax assets that can be recognised, based upon the likely timing and level of future taxable profits, together with future tax planning strategies.

Estimation uncertainty and assumptions

The key assumptions concerning the future and other key sources of estimation uncertainty at the reporting date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below. The Group based its assumptions and estimates on parameters available when the consolidated financial statements were prepared. Existing circumstances and assumptions about future developments, however, may change due to market changes or circumstances beyond the control of the Group. Such changes are reflected in the assumptions when they occur.

Impairment of goodwill

The Group determines whether goodwill is impaired at least on an annual basis. This requires an estimation of the value in use or fair value less cost to sell of the cash-generating units to which the goodwill is allocated. Estimating the value in use requires the Group to make an estimate of the expected future cash flows from the cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows.

Fair values of assets and liabilities including intangible assets

Considerable judgement by management is required in the estimation of the fair value of the assets including intangible assets with finite useful life, liabilities and contingent liabilities acquired.

Impairment losses on loans and advances

The Group reviews its loans and advances on a quarterly basis to assess whether a provision for impairment should be recorded in the consolidated statement of income. In particular, considerable judgement by management is required in the estimation of the amount and timing of future cash flows when determining the level of provisions required. Such estimates are necessarily based on assumptions about several factors involving varying degrees of judgment and uncertainty, and actual results may differ resulting in future changes to such provisions.

Fair value measurement of financial instruments

When the fair values of financial assets and financial liabilities recorded in the statement of financial position cannot be measured based on quoted prices in active markets, their fair value is measured using valuation techniques including the DCF model. The inputs to these models are taken from observable markets where possible, but where this is not feasible, a degree of judgement is required in establishing fair values. Judgements include considerations of inputs such as liquidity risk, credit risk and volatility. Any changes in these estimates and assumptions as well as the use of different, but equally reasonable estimates and assumptions may have an impact on carrying amounts of loans and receivables and investments available for sale.

3. CASH AND CASH EQUIVALENTS

	2017 ***KD 000's***	*2016* *KD 000's*
Cash on hand and in current account with banks and OFIs	567,094	551,173
Balances with the CBK	132,494	127,913
Due from banks and OFIs maturing within thirty days	237,586	216,919
	937,174	896,005

4. DUE FROM BANKS AND OTHER FINANCIAL INSTITUTIONS

	2017 ***KD 000's***	*2016* *KD 000's*
Loans and advances		
- Banks	101,417	233,099
- OFIs	184,348	114,627
	285,765	347,726
Deposits with banks	372,574	482,308
Gross due from banks and OFIs	658,339	830,034
Provision (note 5) *	(26,329)	(26,622)
	632,010	803,412

*Provision includes precautionary provisions amounting to KD 20,265 (31 December 2016: KD 20,265) judgmentally allocated previously for other financial institutions.

5. LOANS AND ADVANCES TO CUSTOMERS

a) Balances

	2017 ***KD 000's***	*2016* *KD 000's*
Corporate	4,127,073	3,961,829
Retail	460,555	471,380
Gross loans and advances to customers	4,587,628	4,433,209
Provision	(180,060)	(209,123)
	4,407,568	4,224,086

b) Provisions

	Banks and OFIs *KD 000's*	*Corporate* *KD 000's*	*Retail* *KD 000's*	*Total* *KD 000's*
At 1 January 2017	26,967	196,160	30,024	253,151
Exchange adjustment	(7)	(2,498)	(271)	(2,776)
Amounts written off	-	(56,471)	(12,999)	(69,470)
Charged to consolidated statement of income	(410)	38,483	3,465	41,538
At 31 December 2017	**26,550**	**175,674**	**20,219**	**222,443**
At 1 January 2016	28,539	195,509	31,145	255,193
Exchange adjustment	32	(5,939)	60	(5,847)
Amounts written off	(1,043)	(30,703)	(5,958)	(37,704)
Charged to consolidated statement of income	(561)	37,293	4,777	41,509
At 31 December 2016	26,967	196,160	30,024	253,151

The provision includes KD 16,054 thousand (31 December 2016: KD 17,406 thousand), being provision for non-cash facilities reported under other liabilities (note 11), of which KD 221 thousand (31 December 2016: KD 345 thousand) relates to Due from Banks and Other Financial Institutions. Provision for Corporate and Retail includes precautionary provisions amounting to KD 102,365 (31 December 2016: KD 111,365).

5. LOANS AND ADVANCES TO CUSTOMERS (continued)

The impairment provision for credit facilities complies in all material respects with the specific provision requirements of the CBK and IFRS. In March 2007, the CBK issued a circular amending the basis of making minimum general provisions on facilities changing the rate from 2% to 1% for cash facilities and 0.5% for non cash facilities. The revised rates are applied effective from 1 January 2007 on the net increase in facilities, net of certain restricted categories of collateral during the reporting period. The general provision as of 31 December 2006 in excess of the present 1% for cash facilities and 0.5% for non cash facilities amounts to KD 16,154 thousand and is retained as a general provision until further directive from the CBK. Interest income on impaired loans and advances is immaterial.

During the year the Group recovered KD 7,736 thousand (2016: KD 10,763 thousand) from customers whose balances were written off and recorded the same under other income in the consolidated statement of income.

The breakup of specific and general provision is as follows:

	2017 ***KD 000's***	*2016* *KD 000's*
General provision	202,846	207,989
Specific provision	19,597	45,162
	222,443	253,151

6. INVESTMENT SECURITIES

	2017 ***KD 000's***	*2016* *KD 000's*
Financial assets at fair value through profit or loss		
Investments held for trading		
Debt securities		
- Quoted	872	2,739
Equity securities		
- Quoted	550	571
Investments designated at fair value through profit or loss		
Equity securities		
- Quoted	317	320
- Unquoted	33,645	35,173
Managed funds	53,472	62,639
Total financial assetsat fair value through profit or loss	88,856	101,442

6. INVESTMENT SECURITIES (continued)

Financial assets available for sale		
Debt securities		
- Quoted	217,947	117,172
- Unquoted	47,000	49,903
	264,947	167,075
Equity securities		
- Quoted	40,912	57,984
- Unquoted	134,329	142,306
	175,241	200,290
Total financial assets available for sale	440,188	367,365
Financial assets held to maturity		
Debt securities		
- Quoted	78,334	70,880
Total financial assets held to maturity	78,334	70,880
Investment in associates	15,387	14,648
Total investment securities	622,765	554,335

Associates of the Group:

Name of company	***Principal activities***	***Country of incorporation***	***Effective interest as at 31 December 2017***	*Effective interest as at 31 December 2016*
FIMBank P.L.C. ("FIMBank")	International Trade Finance	Malta	19.7%	19.7%
Middle East Payment Services Co. ("MEPS")	Credit Card & ATM Services	Jordan	19.5%	19.5%
First Real Estate Investment Company K.S.C. (Closed) ("FREICO")	Investing in Real Estate	Kuwait	19.8%	19.8%

Carrying value of associates is as follows:

	2017 KD000's	*2016 KD000's*
FIMBank	9,631	8,937
MEPS	1,404	1,378
FREICO	4,352	4,333

Summarised financial information of associates is as follows:

	2017 KD000's	*2016 KD000's*
Net result	3,346	2,417
Other comprehensive income (loss)	1,349	(1,086)

7. OTHER ASSETS

	2017 ***KD 000's***	*2016* *KD 000's*
Accrued interest receivable	92,465	73,955
Prepaid expenses	7,067	7,400
Assets pending sale *	22,547	29,371
Deferred tax assets	2,164	2,877
Taxation paid in advance	3,328	3,805
Sundry debtors	15,462	22,293
Other balances	44,502	40,710
	187,535	180,411

* The fair value of real estate assets included in assets pending for sale are based on valuations performed by accredited independent valuers by using market comparable method. As the significant valuation inputs used are based on unobservable market data these are classified under level 3 fair value hierarchy. However, the impact on the consolidated statement of income would be immaterial if the relevant risk variables used to fair value were altered by 5%.

8. INTANGIBLE ASSETS

	Goodwill ***KD 000's***	***Other intangible assets*** ***KD 000's***	***Total*** ***KD 000's***
Cost			
At 1 January 2017	15,651	51,479	67,130
Exchange adjustment	(425)	(169)	(594)
At 31 December 2017	15,226	51,310	66,536
Amortisation			
At 1 January 2017	-	25,996	25,996
Charge for the year	-	3,945	3,945
At 31 December 2017	-	29,941	29,941
Net book value			
At 31 December 2017	15,226	21,369	36,595
At 31 December 2016	15,651	25,483	41,134

The carrying amounts of goodwill and other intangible assets allocated to each CGU are as follows:

		Other intangible assets KD000's				
	Goodwill ***KD 000's***	***Banking license***	***Customer relationship***	***Core customer deposits***	***Total***	***Total*** ***KD 000's***
AGB	3,419	8,465	195	22	8,682	12,101
BoB	6,618	2,463	-	-	2,463	9,081
TIB	5,189	7,452	-	-	7,452	12,641
BBT	-	-	2,461	311	2,772	2,772
At 31 December 2017	15,226	18,380	2,656	333	21,369	36,595

8. INTANGIBLE ASSETS (continued)

		Other intangible assets KD000's				
	Goodwill KD 000's	*Banking license*	*Customer relationship*	*Core customer deposits*	*Total*	*Total KD 000's*
AGB	3,611	9,486	362	43	9,891	13,502
BoB	6,777	3,785	-	-	3,785	10,562
TIB	5,263	8,162	-	-	8,162	13,425
BBT	-	-	3,235	410	3,645	3,645
At 31 December 2016	15,651	21,433	3,597	453	25,483	41,134

Impairment testing of goodwill

The carrying value of goodwill is tested for impairment on an annual basis (or more frequently if evidence exists that goodwill might be impaired) by estimating the recoverable amount of the cash-generating unit ("CGU") to which these items are allocated using value-in-use calculations unless fair value based on active market price is higher than the carrying value of the CGU. The value in use calculations use pre-tax cash flow projections based on financial budgets approved by management over a five years period and a relevant terminal growth rate of 4% to 5% (31 December 2016: 4% to 7%). These cash flows were then discounted using a pre-tax discount rate of 18% to 25% (31 December 2016: 15% to 30%) to derive a net present value which is compared to the carrying value. The discount rate used is pre-tax and reflects specific risks relating to the relevant CGU. The recoverable amounts are either higher or approximates the carrying value of goodwill. The Group has also performed a sensitivity analysis by varying these input factors by a reasonable possible margin. Based on such analysis, there are no indications that goodwill is impaired considering the level of judgments and estimations used.

9. MATERIAL PARTLY-OWNED SUBSIDIARIES

The management of the Bank has concluded that BoBis the only subsidiary which has non-controlling interests that is material to the Group.

The information relating to non-controlling interests to BB Group is as follows:

	BoB	
	2017 KD 000's	*2016 KD 000's*
Accumulated balances	35,550	36,212
Profit (loss) attributable	2,388	(2,463)
Dividends	2,008	-

The summarised financial information of this subsidiary as of 31 December is provided below. This information is based on amounts before inter-company eliminations.

Summaried statement of income:

	BoB	
	2017 KD 000's	*2016 KD 000's*
Operating income	16,262	17,268
Operating expense	(11,299)	(13,380)
Operating profit before provision	4,963	3,888
Profit for the year	3,754	771
Total comprehensive income	3,840	1,586

9. MATERIAL PARTLY-OWNED SUBSIDIARIES (continued)

Summarised statement of financial position:

	BoB	
	2017 KD 000's	*2016 KD 000's*
Loans and advances to customers	42,252	45,299
Customer deposits	191,432	292,478
Total assets	270,998	372,110
Total liabilities	197,475	296,118
Total equity	73,523	75,992
Net cash flows (used) from	(118,722)	
- operating activities		(11,817)
- investment activities	(6,422)	1,002
- financing activities	(3,791)	-
Net decrease in cash and cash equivalents during the year	(128,935)	(10,815)

10. OTHER BORROWED FUNDS

	Effective interest rate	***2017 KD 000's***	*2016 KD 000's*
Subordinated bonds – KWD 2026 (Fixed tranche)*	**6.00%**	29,805	29,769
Subordinated bonds – KWD 2026 (Floating tranche capped at 7%)*	**CBK+3.95%**	69,215	69,131
Subordinated bonds -KWD 2022 (Fixed tranche)	**5.650%**	35,210	35,167
Subordinated bonds – KWD 2022(Floating tranche capped at 6.650%)	**CBK + 3.9%**	37,199	37,154
Medium term borrowing	**3M Libor +1 .05%**	-	106,850
Euro Medium Term Note	**3.125%**	149,842	151,709
Other borrowings – subsidiaries	**11.85% - 13.04%**	-	4,260
Other borrowings – subsidiaries	**1.00%-3.17%**	1,223	3,954
		322,494	437,994

*During the previous year, the Bank issued KD 100 million bonds due in 2026 (the "KWD 2026 bonds") at the principal amount. The effective interest rate of floating rate tranche is capped at 7% up to the reset date and following the reset date the effective interest rate will be capped at the sum of the interest rate applicable at that time to the Fixed rate bond and 1%. The reset date is defined as the fifth anniversary from the issuance date. The KWD 2026 bonds are callable in full but not in part, at the option of the Bank, after 5 years from the date of issuance (subject to certain conditions being satisfied and prior approval of the CBK). These bonds are eligible as Tier II capital under the Kuwait Basel III regulations.

Movement in other borrowed funds included in consolidated statements of cash flows under financing activities includes KD 3,289 thousand (2016: KD 401 thousand) arising from foreign currency translation gain.

11. OTHER LIABILITIES

	2017	*2016*
	KD 000's	*KD 000's*
Accrued interest payable	61,411	61,004
Staff benefits	13,213	12,101
Provision for non-cash credit facilities (note 5)	16,054	17,406
Clearing cheques and balances	41,238	37,147
Income received in advance	14,453	11,885
Other payable and accruals	34,045	29,602
Deferred tax liabilities	53	35
Taxation payable	13,112	11,632
Other balances	18,183	34,160
	211,762	214,972

12. EQUITY AND RESERVES

a) Authorised, issued and fully paid up capital of the Bank

	2017	*2016*
Authorised share capital (shares of 100 fils each)	2,500,000,000	2,500,000,000
Issued and fully paid up capital (shares of 100 fils each)	2,151,827,115	2,049,359,158

b) On 29 March 2017, the annual general assembly approved the distribution of cash dividend of 5 fils per share (2015: 18 fils) and bonus shares of 5% (2015: Nil) for the year ended 31 December 2016.

c) The share premium and treasury shares reserve are not available for distribution. The Companies Law and the Bank's articles of association require that 10% of the profit for the year attributable to equity holders of the Bank before Board of Directors remuneration, NLST, KFAS and Zakat be transferred annually to statutory reserve. The Bank may resolve to discontinue such annual transfers when the reserve equals 50% of paid up share capital. Distribution of statutory reserve is limited to the amount required to enable the payment of dividend of 5% of share capital in years when accumulated profits are not sufficient for the payment of a dividend of that amount.

d) The articles of association of the Bank requires an amount of not less than 10% of the profit for the year attributable to equity holders of the Bank before Board of Directors remuneration, NLST, KFAS and Zakat be transferred annually to the voluntary reserve. There is no restriction on distribution of this reserve, except as noted in note 12 (e).

12. EQUITY AND RESERVES (continued)

e) Treasury shares

	2017	*2016*
Number of shares held	6,700,953	28,496,685
Percentage of shares held	0.31%	1.39%
Cost KD 000's	2,817	12,582
Market value KD 000's	2,004	8,692
Weighted average market value per share (fils)	335	321

The balance in the treasury share reserve account is not available for distribution. An amount equal to the cost of treasury shares is not available for distribution from share premium, statutory reserve, voluntary reserve and retained earnings throughout the holding period of these treasury shares.

f) Other reserves

	2017			
	Hedge of net investment in foreign operations KD 000's	*Cash flow hedge reserve KD 000's*	*Changes in ownership in subsidiaries KD 000's*	***Total KD 000's***
Balance at 1 January	1,762	2,461	(1,553)	2,670
Changes in fair value of cash flow hedge reserve	-	1,580	-	1,580
Loss on hedge of a net investment	(2,747)	-	-	(2,747)
Total comprehensive (loss) income	(2,747)	1,580	-	(1,167)
Balance at the end of the year	(985)	4,041	(1,553)	1,503

	2016			
	Hedge of net investment in foreign operations KD 000's	*Cash flow hedge reserve KD 000's*	*Changes in ownership in subsidiaries KD 000's*	*Total KD 000's*
Balance at 1 January	(6,710)	1,151	(1,553)	(7,112)
Changes in fair value of cash flow hedge reserve	-	1,310	-	1,310
Gain on hedge of a net investment	8,472	-	-	8,472
Total comprehensive income	8,472	1,310	-	9,782
Balance at the end of the year	1,762	2,461	(1,553)	2,670

g) Proposed dividends

The Board of Directors has recommended distributing cash dividend of ___ fils per share (2016: 5 fils) and ___% bonus shares (2016: 5) for the financial year ended 31 December 2017. Subject to being approved at the annual general assembly ("AGM") of the shareholders, the cash dividend and bonus shares shall be payable to shareholders registered in the Bank's records as of the AGM date.

12. EQUITY AND RESERVES (continued)

h) Perpetual Tier 1 Capital Securities

On 30 September, 2014, the Bank through Burgan Tier 1 Financing Limited (a newly incorporated special purpose company with limited liability in the Dubai International Financial Centre) ("Issuer") issued Perpetual Tier 1 Capital Securities (the "Tier 1 securities"), amounting to USD 500,000 thousand.

The Tier 1 securities are unconditionally and irrevocably guaranteed by the Bank and constitute direct, unconditional, subordinated and unsecured obligations of the Issuer and are classified as equity in accordance with IAS 32: Financial Instruments – Classification. The Tier 1 securities do not have a maturity date. They are redeemable by the Bank at its discretion after 30 September 2019 (the "First Call Date") or on any interest payment date thereafter subject to the prior consent of the regulatory authority.

The Tier 1 securities bear interest on their nominal amount from the issue date to the first call date at a fixed annual rate of 7.25%. Thereafter the interest rate will be reset at five year intervals. Interest will be payable semi-annually in arrears and treated as a deduction from equity.

The Bank at its sole discretion may elect not to distribute interest and this is not considered an event of default.If the Bank does not pay interest on the Tier 1 securities, on a scheduled interest payement date (for whatever reason), then the Bank must not make any other distribution or payment on or with respect to its other shares that rank equally with or junior to the Tier 1 securities (other than pro-rata distributions or payments on shares that rank equally with Tier 1 securities) unless and until it has paid two consecutive interest payments in full on the Tier 1 securities.

The semi-annual interest payments were paid during the year.

13. INTEREST INCOME

	2017 *KD 000's*	*2016* *KD 000's*
Loans and advances to customers	263,540	241,449
Due from banks and other financial institutuions	53,616	54,604
Treasury bills and bonds	11,954	11,016
Investment securities	7,927	5,146
	337,037	312,215

14. INTEREST EXPENSE

	2017 *KD 000's*	*2016* *KD 000's*
Deposits from customers	86,975	77,599
Due to banks	23,968	29,767
Due to other financial institutuions	24,150	25,039
Other borrowed funds	31,024	24,069
	166,117	156,474

15. NET INVESTMENT INCOME

	2017 *KD 000's*	*2016* *KD 000's*
Financial assets at fair value through profit or loss:		
– net gain on investments held for trading	198	13
– net gain on investments designated at fair value through profit or loss	5,987	12,870
	6,185	12,883
Net gain (loss) from financial assets available for sale	3,166	(694)
Share of result from associates	668	443
	10,019	12,632

16. TAXATION

	2017 *KD 000's*	*2016* *KD 000's*
NLST	1,279	1,600
KFAS	614	574
Zakat	672	633
Taxation arising from overseas subidiaries	8,202	6,560
	10,767	9,367

Components of taxation arising from overseas subsidiaries are as follows:

	2017 *KD 000's*	*2016* *KD 000's*
Current tax	8,521	6,002
Deferred tax	(319)	558
	8,202	6,560

16. TAXATION (continued)

The tax rate applicable to the taxable subsidiary companies is in the range of 10% to 25% (2016: 10% to 25%) whereas the effective income tax rate for the year ended 31 December 2017 is in the range of 10% to 40% (2016: 10% to 30%). For the purpose of determining the taxable results for the year, the accounting profit of the overseas subsidiary companies were adjusted for tax purposes. Adjustments for tax purposes include items relating to both income and expense. The adjustments are based on the current understanding of the existing laws, regulations and practices of each overseas subsidiary companies jurisdiction.

17. EARNINGS PER SHARE

Basic and diluted earnings per share is computed by dividing the profit for the year attributable to equity holders of the Bank after interest payment of Tier 1 capital securities by the weighted average number of shares outstanding during the year less treasury shares.

The computation of basic and diluted earnings per share is as follows:

	2017 ***KD 000's***	*2016* *KD 000's*
Profit for the year attribuitable to equity holders of the Bank	65,223	68,178
Less: Interest payments on Tier 1 capital securities	(11,003)	(10,952)
Profit for the year attributable toequity holders of the Bank after interest payment on Tier1 capital securities	54,220	57,226
	Shares	*Shares*
Weighted average number of outstanding shares, net of treasury shares	2,133,594,718	2,122,273,443
Basic and diluted earnings per share (fils)	25.4	27.0

The basic and diluted earnings per share for the comparative year presented have been restated for the effect of bonus shares issued on 29 March 2017 (note 12).

18. SEGMENT INFORMATION

For management purposes, the Group organises its operations by geographic territory in the first instance, primarily Domestic and International. All operations outside Kuwait are classified as International. Within its domestic operations, the Group is organised into the following business segments.

- Corporate banking: provides comprehensive product and services to corporate customers and financial institutions including lending, deposits, trade services, foreign exchange, advisory services and others.

- Private and retail banking: provides wide range of products and services to retail and private bank customers including loans, deposits, credit and debit cards, foreign exchange, and others.

- Treasury, investment banking and others: includes treasury asset liability and liquidity management, investment services and management, fund management and any residual of transfer pricing. It also provides products and services to banks including money markets, lending, deposits, foreign exchange and others.

Executive Management monitors the operating results of its business units separately for the purpose of making decisions about resource allocation and performance assessment. Segment performance is evaluated based on segment result after provisions which in certain respects are measured differently from operating profit or loss in the consolidated financial statements.

18. SEGMENT INFORMATION (continued)

The table below presents income and results and certain assets and liabilities information regarding the Group's operating segments.

	Kuwait Operations				*International Operations*	*Unallocated Intragroup Transactions*	*Group*
	Corporate banking KD 000's	*Retail and Private banking KD 000's*	*Treasury investment banking and others KD 000's*	*Total KD 000's*	*KD 000's*	*KD 000's*	*Total KD 000's*
31 December 2017							
Net interest income	45,209	33,237	29,209	107,655	74,294	(11,029)	170,920
Segment operating income	65,684	39,738	46,216	151,638	107,510	(19,722)	239,426
Depreciation and amortisation	(865)	(1,711)	(535)	(3,111)	(5,104)	(3,945)	(12,160)
Segment result before provisions	55,815	20,229	40,119	116,163	47,470	(20,256)	143,377
Provision for loans and advances	(1,662)	(3,850)	(629)	(6,141)	(14,021)	624	(19,538)
Provision for investment securities	-	-	(8,706)	(8,706)	(64)	-	(8,770)
Segment result after provisions	54,153	16,379	30,784	101,316	33,385	(19,632)	115,069
Unallocated expenses				(10,142)	-	(3,000)	(13,142)
Unallocated provisions				(22,000)	-	-	(22,000)
Profit for the year before taxationand board of directors' renumeration				69,174	33,385	(22,632)	79,927
Total assets	1,934,272	1,163,502	2,355,218	5,452,992	2,594,655	(632,435)	7,415,212
Total liabilities	948,525	795,149	2,864,589	4,608,263	2,314,006	(374,717)	6,547,552

18. SEGMENT INFORMATION (continued)

	Kuwait Operations				*International Operations*	*Unallocated Intragroup Transactions*	*Group*
	Corporate banking KD 000's	*Retail and Private banking KD 000's*	*Treasury investment banking and others KD 000's*	*Total KD 000's*	*KD 000's*	*KD 000's*	*Total KD 000's*
31 December 2016							
Net interest income	41,084	35,227	19,763	96,074	69,663	(9,996)	155,741
Segment operating income	67,081	39,858	38,369	145,308	101,338	(11,972)	234,674
Depreciation and amortisation	(745)	(1,611)	(531)	(2,887)	(5,578)	(3,945)	(12,410)
Segment result before provisions	58,598	21,382	32,325	112,305	35,965	(14,418)	133,852
Provision for loans and advances	(5,369)	(5,025)	1,376	(9,018)	(11,987)	3,496	(17,509)
Provision for investment securities	-	-	(2,472)	(2,472)	(733)	-	(3,205)
Segment result after provisions	53,229	16,357	31,229	100,815	23,245	(10,922)	113,138
Unallocated expenses				(9,852)	-	(3,084)	(12,936)
Unallocated provisions				(24,000)	-	-	(24,000)
Profit for the year before taxationand board of directors' renumeration				66,963	23,245	(14,006)	76,202
Total assets	2,068,362	1,220,105	2,141,708	5,430,175	2,365,998	(527,297)	7,268,876
Total liabilities	732,642	789,762	3,082,389	4,604,793	2,089,316	(270,789)	6,423,320

19. TRANSACTIONS WITH RELATED PARTIES

The Group has entered into transactions with certain related parties (Parent Company, directors and key management personnel of the Group and entities controlled, jointly controlled or significantly influenced by such parties) who were customers of the Group during the year.The "Others" column in the table below mainly represent transactions with other related parties that are either controlled or significantly influenced by the parent company.The terms of these transactions are substantially on the same commercial basis as approved by the Group's management, including collateral.Lending to Board Members and their related parties is secured by tangible collateral in accordance with regulations of Central Bank of Kuwait.The outstanding balances and transactions are as follows:

	Parent company KD 000's	***Associate KD 000's***	***Others KD 000's***	***2017 KD 000s***	*2016 KD 000s*
Consolidated Statement of Financial Position					
Due from banks and OFIs*	-	46,168	263,883	310,051	270,085
Loans and advances to customers*	-	-	960,658	960,658	983,563
Investment securities	25,532	-	136,798	162,330	179,607
Investment securities managed by a related party	-	-	52,455	52,455	58,106
Due to banks	-	4	22,225	22,229	7,718
Due to other financial institutions	-	-	70,378	70,378	44,354
Deposits from customers	118,263	-	55,404	173,667	57,598
Commitments, contingent liabilities and derivatives					
Letters of credit	-	-	5,841	5,841	6,010
Letters of guarantee	-	-	60,514	60,514	58,233
Derivative financial instruments	-	-	42,450	42,450	39,880
Transactions					
Interest income	35	2,058	47,150	49,243	41,912
Interest expense	(304)	-	(1,052)	(1,356)	(1,263)
Fee and commission income	2	-	1,843	1,845	1,106
Dividend income	1,837	-	148	1,985	1,984
Other expense	-	-	(2,409)	(2,409)	(2,074)

* As of 31 December 2017, the fair value of the total eligible collateral to the extent of the outstanding balances amounting to KD 590,373 thousand (2016: KD 644,653 thousand).

19. TRANSACTIONS WITH RELATED PARTIES (continued)

	No. of Board members or executive staff	*2017 KD 000's*	*2016 KD 000's*
Board members			
Loans and advances to customers	2	3,604	3,926
Deposits from customers	8	590	1,390
Executive staff			
Loans and advances to customers	21	267	174
Deposits from customers	34	2,626	2,154
Letters of guarantee	2	1	2

Key management compensation
Remuneration paid or payable in relation to "key management" (deemed for this purpose to comprise Directors in relation to their committee service, the Chief Executive Officer and other Senior Officers), was as follows:

	2017 KD 000's	*2016 KD 000's*
Short term employee benefits – including salary and bonus	5,070	5,483
Accrual for end of service indemnity	568	455
Accrual for cost of long term incentive rights	766	996
Accrual for committee services	300	300
	6,704	7,234

20. COMMITMENTS AND CONTINGENT LIABILITIES

	2017 KD 000's	*2016 KD 000's*
Acceptances	39,863	43,837
Letters of credit	288,681	216,091
Letters of guarantee	862,297	918,874
Undrawn lines of credit	688,916	632,928
Other commitments	56,351	52,482
	1,936,108	1,864,212

The primary purpose of these instruments is to ensure that funds are available to customers as required. Acceptances, standby letters of credit and guarantees, which represent irrevocable assurances that the Group will make payments in the event that the customer cannot meet its obligations to third parties, carry the same credit risk as loans. Documentary and commercial letters of credit, which are undertaken by the Group on behalf of the customer authorising a third party to draw drafts on the Group up to a stipulated amount under specific terms and conditions, are collateralised by the underlying shipments of goods to which they relate and therefore carry less risk than a direct borrowing.

Undrawn lines of credit represent unused portions of authorisations to extend cash credit. With respect to credit risk on undrawn lines of credit, the Group is potentially exposed to loss in an amount equal to the total unused lines. However, the likely amount of loss is less than the total unused lines since most of these lines will expire or terminate without being funded.

The Group makes available to its customers guarantees which may require that the Group makes payments on their behalf and enters into commitments to extend credit lines to secure their liquidity needs. Such payments are collected from customers based on the terms of the letter of credit. They expose the Group to similar risks to loans and these are mitigated by the same control processes and policies.

21. DERIVATIVE FINANCIAL INSTRUMENTS

In the ordinary course of business the Group enters into various types of transactions that involve derivative financial instruments. The Group offers it's clients derivatives products that are traded in the financial markets in order to service their risk management needs to hedge currency and interest rate exposures. The Group also uses derivatives for economic hedging purpose to manage its own assets and liabilities as well as to hedge certain risk exposures such as variation in future cash flows attributable to a recognised asset or liability (cash flow hedge), or hedges of net investment in foreign operation. For those derivative conttracts that are designated as a hedging instrument, hedge accounting is used provided certain criteria are met.

Derivatives are initially recognised and are subsequently measured at fair value. Fair values are obtained from quoted market prices in active markets, and valuation techniques (such as discounted cash flow models and option pricing models), as appropriate. All derivatives are carried as assets when their fair value is positive and as liabilities when fair values are negative.

The method of recognising the resulting fair value gain or loss depends on whether the derivative is designated as a hedging instrument and, if so, the nature of the item being hedged.

At the inception of the transactions the Group documents the relationship between the hedging instruments and the hedged items, its risk management objective, together with the methods selected to assess hedge effectiveness. The Group also documents its assessment both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in cash flows of the hedged items.

Derivative instruments that are used by the Group as part of its risk management strategies, but which do not qualify for hedge accounting under the bank's hedge accounting policies, are presented as Derivatives held for trading (non-qualifying hedges).

Derivatives held for hedging

Hedge of net investment in foreign operations
The Bank entered into forward foreign exchange contracts between TRY and USD, rolled over on a monthly basis, which has been designated as a hedge of the Bank's net investment in it's Turkish subsidiary. This transaction has created a net long position in USD. Gains or losses on the retranslation of the aforesaid contracts are transferred to equity to offset any gains or losses on translation of the net investments in the Turkish subsidiary. No ineffectiveness from hedges of net investments in foreign operations was recognised in the consolidated statement of income during the year.

Cash flow hedges
One of the subsidiary of the Group applies cash flow hedge accounting using interest rate swaps to hedge its foreign currency deposits with an average maturity upto 3 months against interest rate fluctuations. The subsidiary implements effectiveness tests at balance sheet dates for hedge accounting; the effective portions are accounted as part of changes in fair value of derivatives under other reserves, whereas the ineffective portion is recognised in the consolidated statement of income.

No ineffectiveness from hedges was recognised in the consolidated statement of income during the year.

Derivatives held for trading
Derivative contracts that are entered into for the purpose of servicing customers in their risk management needs as well as derivatives used by the Group for economic hedging purpose but which do not meet the qualifying criteria for hedge accounting are classified as 'Derivatives held for trading'. The risk exposures on account of derivative contracts for customers are covered by entering into positions with an opposite risk profile with other counter parties or by other risk mitigating transactions.

Types of derivative contracts
Forward foreign exchange contracts
Forward foreign exchange contracts are contractual agreements to either buy or sell a specified currency, at a specific price and date in the future, and are customised contracts transacted in the over-the-counter market.

21. DERIVATIVE FINANCIAL INSTRUMENTS (continued)

Swaps

Swaps are contractual agreements between two parties to exchange streams of payments over time based on specified notional amounts, in relation to movements in a specified underlying index such as an interest rate, foreign currency rate or equity index.

Interest rate swaps relate to contracts taken out by the Bank with OFIs in which the Group either receives or pays a floating rate of interest, respectively, in return for paying or receiving a fixed rate of interest. The payment flows are usually netted against each other, with the difference being paid by one party to the other.In a currency swap, the Group pays a specified amount in one currency and receives a specified amount in another currency. Currency swaps are mostly gross–settled.

Options

Options are contractual agreements that convey the right, but not the obligation, for the purchaser either to buy or sell a specified amount of a financial instrument at a fixed price, either at a fixed future date or at any time within a specified period.

The Group purchases and sells options through regulated exchanges and in the over–the–counter markets. Options purchased by the Group provide the Group with the opportunity to purchase (call options) or sell (put options) the underlying asset at an agreed–upon value either on or before the expiration of the option. The Group is exposed to credit risk on purchased options only to the extent of their carrying amount, which is their fair value.

Options written by the Group provide the purchaser the opportunity to purchase from or sell to the Group the underlying asset at an agreed–upon value either on or before the expiration of the option.

The table below shows the fair value of derivative financial instruments, recorded as assets or liabilities, together with their notional amounts analysed by the terms of maturity. The notional amount, recorded gross, is the amount of a derivative's underlying asset, reference rate or index and is the basis upon which changes in the value of derivatives are measured. The notional amounts indicate the volume of transactions outstanding at the year end and are indicative of neither the market risk nor the credit risk.Credit risk in respect of derivative financial instruments is limited to the positive fair value of instruments. The credit risk exposure is managed as part of the overall borrowers lending limits, together with potential exposures from market movements.

			Notional amount		
31 December 2017	***Positive fair value KD 000's***	***Negative fair value KD 000's***	***Within 1 year KD 000's***	***Over 1 year KD 000's***	***Total KD 000's***
Derivatives held for trading: (non-qualifying hedges)					
Forward swaps/ foreign exchange contracts	8,245	(8,019)	1,181,338	219	1,181,557
Interest rate swaps	5,390	(2,205)	39,703	290,082	329,785
Options	2,383	(2,142)	339,068	42,450	381,518
	16,018	(12,366)	1,560,109	332,751	1,892,860
Derivatives held for hedging:					
Forward swaps/ foreign exchange contracts	198	(2,375)	84,897	-	84,897
Interest rate swaps	21,390	(5,101)	24,170	166,132	190,302
	21,588	(7,476)	109,067	166,132	275,199

21. DERIVATIVE FINANCIAL INSTRUMENTS (continued)

31 December 2016	*Positive fair value KD 000's*	*Negative fair value KD 000's*	*Notional amount* *Within 1 year KD 000's*	*Over 1 year KD 000's*	*Total KD 000's*
Derivatives held for trading: (non-qualifying hedges)					
Forward swaps/ foreign exchange contracts	9,085	(22,698)	955,026	7,256	962,282
Interest rate swaps	2,745	(1,091)	49,322	223,041	272,363
Options	1,759	(1,646)	250,451	39,880	290,331
	13,589	(25,435)	1,254,799	270,177	1,524,976
Derivatives held for hedging:					
Forward swaps/ foreign exchange contracts	2,035	(101)	88,559	-	88,559
Interest rate swaps	15,983	(2,561)	7,634	116,358	123,992
	18,018	(2,662)	96,193	116,358	212,551

22. FAIR VALUE MEASUREMENT

Fair value of all financial instruments is not materially different from their carrying values. For financial assets and financial liabilities that are liquid or having a short-term maturity (less than three months) it is assumed that the carrying amounts approximate to their fair value. This assumption is also applied to demand deposits, savings accounts without a specific maturity.

The fair value of investment securities is categorised as per the policy on fair value measurement in Note 2. Movement in level 3 is mainly on account of purchase, sale and change in fair value and on account of investment security acquired against recovery of debt previously written off, recorded as other income and change in fair value. During the year, a decrease of KD 12,728 thousand (2016: increase KD 9,423 thousand) was recorded in the other comprehensive income representing change in fair value. There were no material transfers between the levels during the year. The impact on the consolidated statement of financial position or the consolidated statment of shareholders' equity would be immaterial if the relevant risk variables used to fair value the unquoted securities were altered by 5%.

Debt securities included under level 3 consists of unquoted corporate bonds. The fair values of these bonds are estimated using discounted cash flow method using credit spread (ranging from 1% to 3%) (2016: 1% to 3%). Equities and other securities included in this category mainly include strategic equity investments and managed funds which are not traded in an active market. The fair values of these investments are estimated by using valuation techniques that are appropriate in the circumstances. Valuation techniques include discounted cash flow models, observable market information of comparable companies, recent transaction information and net asset values. Significant unobservable inputs used in valuation techniques mainly include discount rate, terminal growth rate, revenue, profit estimates and market multiples such as price to book and price to earnings. Given the diverse nature of these investments, it is not practical to disclose a range of significant unobservable inputs.

Other financial assets and liabilitiesare carried at amortised cost and their carrying values are not materially different from their fair values. Fair values of remaining financial assets and liabilities carried at amortised cost are estimated using valuation techniques incorporating certain assumptions such as future cashflows and credit spreads that are appropriate in the circumstances.

The impact on the consolidated statement of financial position or the consolidated statement of income or the consolidated statment of shareholders' equity would be immaterial if the relevant risk variables used for fair value estimations to fair value the unquoted securities were altered by 5%.

22. FAIR VALUE MEASUREMENT (continued)

Fair value measurement hierarchy for financial assets and financial liabilities that are carried at fair value is as follows:

	31December 2017				*31 December 2016*			
	Level 1	***Level 2***	***Level 3***	***Total***	*Level 1*	*Level 2*	*Level 3*	*Total*
	KD 000's	***KD 000's***	***KD 000's***	***KD 000's***	*KD 000's*	*KD 000's*	*KD 000's*	*KD 000's*
Financial assets								
***Financial assets at fair value through profit or loss*:**								
Financial assets held for trading:								
Equity securities	550		-	550	571	-	-	571
Debt securities	872			872	2,739	-	-	2,739
Derivative financial instruments:								
- Forward swaps/foreign exchange contracts	-	8,443	-	8,443	-	11,120	-	11,120
- Interest rate swaps	-	26,780	-	26,780	-	18,728	-	18,728
- Options	-	2,383	-	2,383	-	1,759	-	1,759
Financial assets designated at fair value through profit or loss:								
Equity securities	317		33,645	33,962	320	-	35,173	35,493
Managed funds			53,472	53,472	-	-	62,639	62,639
***Financial assets available for sale*:**								
Equity securities	40,912		134,329	175,241	57,984	-	142,306	200,290
Debt securities	217,947		47,000	264,947	117,172	-	49,903	167,075
Financial liabilities								
***Financial liabilities at fair value through profit or loss*:**								
Derivative financial instruments:								
Forward swaps/foreign exchange contracts	-	10,394	-	10,394	-	22,799	-	22,799
Interest rate swaps	-	7,306	-	7,306	-	3,652	-	3,652
Options	-	2,142	-	2,142	-	1,646	-	1,646

23. RISK MANAGEMENT

INTRODUCTION
Monitoring and controlling risks is primarily performed based on limits established by the Group. These limits reflect the business strategy and market environment of the Group as well as the level of risk that the Group is willing to accept, with additional emphasis on selected geographic and industrial sectors. In addition, the Group monitors and measures the overall risk bearing capacity in relation to the aggregate risk exposure across all risk types and activities.

The operations of certain subsidiaries are also subject to regulatory requirements within the jurisdictions where it operates. Such regulations not only prescribe approval and monitoring of activities, but also impose certain restrictive provisions (e.g. capital adequacy) to minimise the risk of default and insolvency on the part of the banking and insurance companies to meet unforeseen liabilities as these arise.

As part of its overall risk management, the Group uses derivatives and other instruments to manage exposures resulting from changes in interest rates and foreign currency transactions.

The risk profile is assessed before entering into hedge transactions, which are authorised by the appropriate level of seniority within the Group.

The Group classifies the risks faced as part of its day to day activities into certain categories of risks and accordingly specific responsibilities have been given to various officers for the identification, measurement, control and reporting of these identified families of risks. The categories of risks are:

A. Risks arising from financial instruments:
   i. Credit risk which includes default risk of clients and counterparties
   ii. Market risk which includes interest rate, foreign exchange and equity price risks and
   iii. Liquidity risk

B. Other risks
   i. Operational risk which includes risks due to operational failures

A. CREDIT RISK

Credit risk is the risk that a counterparty will be unable to pay amounts in full when due. The Group structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or group of borrowers, and to geographical and industry segments. Such risks are monitored on a regular basis and are subject to regular review. Limits on the level of credit risk by product, industry sector and by country are approved by the Board or each subsidiary board.

The exposure to any one borrower, including Banks and OFIs is further restricted by sub limits covering items on statement of financial position and commitments and contingent liabilities exposures and daily delivery risk limits in relation to trading items such as forward foreign exchange contracts. Actual exposures against limits are monitored daily. The Group has a well-documented credit policy that complies with CBK regulations and defines the appetite of the Group for assumption of risks in its various business groups.

Exposure to credit risk is managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by changing lending limits where appropriate. Exposure to credit risk is also managed in part by obtaining collateral and corporate and personal guarantees.

Credit risk arising from derivative financial instruments is limited to those with positive fair values, recorded in the consolidated statement of financial position.

23. RISK MANAGEMENT (continued)

A. CREDIT RISK (continued)

Maximum exposure to credit risk:
The table below shows the maximum exposure to credit risk across financial assets before taking into consideration the effect of any collateral and other credit enhancements i.e. credit risk mitigation.

	2017 ***KD 000's***	*2016* *KD 000's*
Cash and cash equivalents	849,238	817,324
Treasury bills and bonds with CBK and others	489,809	479,996
Due from banks and other financial institutions	632,010	803,412
Loans and advances to customers	4,407,568	4,224,086
Investments securities	344,153	240,694
Other assets*	152,429	136,958
Total	6,875,207	6,702,470
Commitments and contingent liabilities	1,936,108	1,864,212
Maximum credit risk exposure before consideration of credit risk mitigation	8,811,315	8,566,682

* Other assets include accrued interest receivable, sundry debtors and other balances as shown in note 7.

The exposures set above, are based on net carrying amounts as reported in the consolidated statement of financial position, except for commitments and contingent liabilities.

Collateral and Credit risk mitigation techniques
The amount, type and valuation of collateral are based on guidelines specified in the risk management framework. The main types of collaterals accepted include real estate and marketable securities. The revaluation and custody of collaterals are performed independent of the business units.

The main credit risk mitigation techniques applied by the Group are based on eligible collaterals. The Group's management monitors the market value of collateral, requests additional collateral in accordance with the underlying agreement, and monitors the market value of the collateral at regular intervals in line with regulatory guidelines.

For further details regarding the Group's use of credit risk mitigation techniques, and collateral policy, refer to Basel III – Pillar 3 Disclosures under the risk management section of the annual report.

Credit risk concentration
The top 10 largest exposures outstanding as a percentage of gross loans and advances to customers at 31 December 2017 is 23 % (31 December 2016: 23%).

The concentration across classes within loans and advances to customers, which form part of the significant portion of assets subject to credit risk, is given in note 5.

23. RISK MANAGEMENT (continued)

A. CREDIT RISK (continued)

The Group's financial assets and commitments and contingent liabilities, before taking into account any collateral held or credit enhancements can be analysed by the following geographic regions:

	2017			*2016*		
	Assets KD 000s	***Commitments and contingent liabilities KD 000s***	***Total KD 000s***	*Assets KD 000s*	*Commitments and contingent liabilities KD 000s*	*Total KD 000s*
Kuwait	3,583,518	1,239,658	4,823,176	3,579,622	1,301,247	4,880,869
Jordan	88,123	7,185	95,308	78,990	5,973	84,963
Algeria	590,121	266,327	856,448	451,636	194,721	646,357
Iraq	174,598	19,515	194,113	251,243	26,899	278,142
Tunisia	58,110	1,580	59,690	43,661	4,205	47,866
Turkey	1,444,979	255,576	1,700,555	1,343,543	245,767	1,589,310
Other middle east	542,623	81,182	623,805	597,602	24,200	621,802
Europe	130,575	19,189	149,764	115,281	24,807	140,088
Rest of the world	262,560	45,896	308,456	240,892	36,393	277,285
	6,875,207	1,936,108	8,811,315	6,702,470	1,864,212	8,566,682

The Group's financial assets and commitments and contingent liabilities, before taking into account any collateral held or credit enhancements can be analysed by the following industry sectors:

	2017 KD 000's	*2016 KD 000's*
Industry sector		
Sovereign	1,470,281	1,099,508
Banking	825,824	1,498,306
Investment	275,404	197,955
Trade and commerce	777,798	711,538
Real estate	1,197,690	991,619
Personal	1,286,424	1,362,556
Manufacturing	735,358	626,797
Construction	948,658	852,475
Other Services	1,293,878	1,225,928
	8,811,315	8,566,682

Credit quality per class of financial assets

The credit quality of financial assets are summarised by reference to public ratings given to the clients/counterparties by recognised and approved External Credit Assessment Institutions (ECAIs) namely Moody's, Standard and Poor's and Fitch. Based on the rating systems as declared by the ECAIs, the ratings are classified into Investment Grade and Non-Investment Grade ratings. Those who are not rated by any of these three ECAIs are considered to be unrated. In order to ensure that the ratings are not considered selectively, if a current rating from one of these ECAIs available in respect of any client/counterparty, it is always taken into account and in such cases, the client/counterparty is not considered as unrated.

For further details regarding the Group's credit risk management policy please refer to Basel III – Pillar 3 Disclosures under the risk management section of the annual report.

23. RISK MANAGEMENT (continued)

A. CREDIT RISK (continued)

a) Financial assets neither past due nor impaired

	2017			
	Rated		***Unrated***	***Total***
	Investment grade KD 000's	***Non investment grade KD 000's***	***KD 000's***	***KD 000's***
Sovereigns	759,320	-	309,213	1,068,533
Banks and OFIs	259,574	77,761	565,189	902,524
Corporates	-	-	3,649,273	3,649,273
Retail	-	-	400,272	400,272
Other credit exposures	266,556	14,368	215,658	496,582
	1,285,450	92,129	5,139,605	6,517,184

	2016			
	Rated		*Unrated*	*Total*
	Investment grade KD 000's	*Non investment grade KD 000's*	*KD 000's*	*KD 000's*
Sovereigns	681,131	-	293,907	975,038
Banks and OFIs	453,372	102,813	569,509	1,125,694
Corporates	-	-	3,591,464	3,591,464
Retail	-	-	317,686	317,686
Other credit exposures	93,751	16,323	267,578	377,652
	1,228,254	119,136	5,040,144	6,387,534

b) Financial assets past due but not impaired

For credit risk related exposures, a past due exposure is considered to be one where the client or counterparty has failed to meet his contractual obligation to the Group towards payment of the interest or the principal or a part thereof on the date on which such payment is due.

	2017			*2016*		
	1 to 45 days KD000's	***45 to 90 days KD 000's***	***Total KD 000's***	*1 to 45 days KD 000's*	*45 to 90 days KD 000's*	*Total KD 000's*
Banks and OFIs	-	-	-	-	-	-
Corporates	142,649	79,477	222,126	96,213	40,364	136,577
Retail	20,691	4,239	24,930	22,248	4,970	27,218
	163,340	83,716	247,056	118,461	45,334	163,795
Fair value of collateral held*	30,414	76,137	106,551	25,626	213	25,839

***Fair value of collateral stated above is to the extent of the outstanding exposure.*

23. RISK MANAGEMENT (continued)

A. CREDIT RISK (continued)

c) Impaired financial assets

The Group considers an asset to be impaired if the realisable value of the asset is less than the value at which it is carried in the books of the Group before it considers the necessity of making a specific provision for the same.

	2017			*2016*		
	Total KD 000's	***Provision KD 000's***	***Fair value of collateral held* KD 000's***	*Total KD 000's*	*Provision KD 000's*	*Fair value of collateral held* KD 000's*
Corporates	100,558	5,851	90,815	155,643	22,364	129,683
Retail	24,623	8,363	11,072	34,314	16,452	11,326
	125,181	14,214	101,887	189,957	38,816	141,009

****Fair value of collateral stated above is to the extent of the outstanding exposure.***

The ratio of gross impaired financial assets over gross loans and advances to banks, OFIs and customers as at 31 December 2017 was 2.6% (2016: 4.0%) and the ratio of impaired financial assets, net of provisions over loans and advances to banks, OFIs and customers as at 31 December 2017 was 2.3% (2016: 3.2%).

B. MARKET RISK

Market risk is the risk that the value of an asset will fluctuate as a result of changes in market variables such as interest rates, foreign exchange rates, and equity prices, whether those changes are caused by factors specific to the individual investment or its issuer or factors affecting all financial assets traded in the market.

Market risk is managed on the basis of pre-determined asset allocations across various asset categories, diversification of assets in terms of geographical distribution and industry concentration, a continuous appraisal of market conditions and trends and management's estimate of long and short term changes in fair value.

Interest rate risk

Interest rate risk arises from the possibility that changes in interest rates will affect the fair value or cash flows of the financial instruments. The Group takes on exposure to the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows. This arises as a result of mismatches or gaps in the amounts of assets and liabilities and off balance sheet instruments that mature or reprice in a given period. The Group manages this risk by matching the repricing of assets and liabilities through risk management strategies.

The Group is exposed to interest rate risk on its interest bearing assets and liabilities (treasury bills and bonds with CBK and others, due from banks and OFIs, loans and advances to customers, due to banks, due to OFIs, deposits from customers and other borrowed funds).

The table below summarises the effect on net interest income as a result of the changes in interest rate:

	2017	*2016*
	KD 000's	*KD 000's*
Increase in interest rate "Basis Points"		
50	6,560	6,738
100	13,335	13,883
Decrease in interest rate "Basis Points"		
50	(6,214)	(6,634)
100	(12,423)	(13,267)

Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Group takes on exposure to effects of fluctuations in the prevailing currency exchange rates on its financial position and cash flows. The Board of Directors sets limits on the level of exposure by currency and in total for both overnight and intra-day positions, which are monitored daily.

23. RISK MANAGEMENT (continued)

B. MARKET RISK (continued)

Currency risk (continued)

The table below analyses the effect on profit and equity of an assumed 5% strengthening in value of the currency rate against the Kuwaiti Dinar from levels applicable at the year end, with all other variables held constant. A negative amount in the table reflects a potential net reduction in profit or equity, where as a positive amount reflects a net potential increase.

		2017		*2016*	
Currency	***% Change in currency rate***	***Effect on profit KD 000's***	***Effect on equity KD 000's***	*Effect on profit KD 000's*	*Effect on equity KD 000's*
Algerian Dinar	**+5**	499	3,666	364	3,741
Iraqi Dinar	**+5**	189	3,942	39	4,289
Turkish Lira	**+5**	409	-	344	-
US Dollar	**+5**	198	2,596	652	2,558
Others	**+5**	109	-	(161)	-

Equity price risk

Equity price risk is the risk that the fair values of equities will fluctuate as a result of changes in the level of equity indices or the value of individual share prices. Equity price risk arises from the change in fair values of equity investments. The Group manages this risk through diversification of investments in terms of geographical distribution and industry concentration. The majority of the Group's quoted investments are listed on the regional Stock Exchanges.

The Group conducts sensitivity analysis on regular intervals in order to assess the potential impact of any major changes in fair value of equity instruments. Based on the results of the analysis conducted there are no material implication over the Group's profit or other comprehensive income for a 5% fluctuation in major stock exchanges.

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, such as fixed rate mortgages when interest rate fall. The fixed rate assets of the Group are not significant compared to the total assets. Moreover, other market conditions causing prepayment is not significant in the markets in which the Group operates. Therefore, the Group considers the effect of prepayment on net interest income is not material after taking in to account the effect of any prepayment penalties.

23. RISK MANAGEMENT (continued)

C. LIQUIDITY RISK

Liquidity risk is the risk that the Group will be unable to meet its liabilities when they fall due. The Group is exposed to daily calls on its available cash resources from overnight deposits, current accounts, maturing deposits, loan draw downs, guarantees. To limit this risk, the Group manages assets with liquidity in mind and monitors liquidity on a daily basis.

The table below shows an analysis of financial liabilities and contingent liabilities and commitments based on the remaining undiscounted contractual maturities:

31 December 2017	***Up to 3 months KD 000's***	***3 – 6 months KD 000's***	***6 – 12 months KD 000's***	***More than 12 months KD 000's***	***Total KD 000's***
Financial liabilities					
Due to banks	590,966	82,679	149,286	83,379	906,310
Due to other financial institutions	357,641	132,243	152,768	350,091	992,743
Deposits from customers	3,325,532	464,372	299,151	86,014	4,175,069
Other borrowed funds	1,226	2,583	5,905	406,825	416,539
Other liabilities	189,750	5,234	6,759	10,019	211,762
	4,465,115	687,111	613,869	936,328	6,702,423
Contingent liabilities and commitments	854,168	265,810	254,633	561,497	1,936,108

31 December 2016	*Up to 3 months KD 000's*	*3 – 6 months KD 000's*	*6 – 12 months KD 000's*	*More than 12 months KD 000's*	*Total KD 000's*
Financial liabilities					
Due to banks	663,595	35,165	68,139	65,044	831,943
Due to other financial institutions	381,623	183,602	380,783	280,578	1,226,586
Deposits from customers	2,672,685	385,932	341,393	348,402	3,748,412
Other borrowed funds	4,339	4,363	110,514	426,348	545,564
Other liabilities	174,428	3,496	7,237	29,811	214,972
	3,896,670	612,558	908,066	1,150,183	6,567,477
Contingent liabilities and commitments	534,774	249,921	437,148	642,369	1,864,212

The table below summarises the maturity profile of the Group's assets and liabilities. The maturities of assets and liabilities have been determined according to when they are expected to be recovered or settled. The maturity profile for financial assets at fair value through profit or loss and financial assets available for sale is determined based on management's estimate of liquidation of those financial assets. The actual maturities may differ from the maturities shown below since borrowers may have the right to prepay obligations with or without prepayment penalties.

23. RISK MANAGEMENT (continued)

C. LIQUIDITY RISK (continued)

	Up to 3 months KD 000s	***3 – 6 months KD 000s***	***6 – 12 months KD 000s***	***More than 12 months KD 000s***	***Total KD 000s***
31 December 2017					
ASSETS					
Cash and cash equivalents	937,174	-	-	-	937,174
Treasury bills and bonds with CBK and others	153,870	94,924	28,077	212,938	489,809
Due from banks and other financial institutions	409,371	70,472	67,821	84,346	632,010
Loans and advances to customers	1,234,295	684,370	647,987	1,840,916	4,407,568
Investment securities	12,249	12,001	4,576	593,939	622,765
Other assets	70,212	3,458	4,367	109,498	187,535
Property and equipment	-	-	-	101,756	101,756
Intangible assets	-	-	-	36,595	36,595
Total assets	2,817,171	865,225	752,828	2,979,988	7,415,212
LIABILITIES AND EQUITY					
Due to banks	578,598	77,730	145,447	81,949	883,724
Due to other financial institutions	356,780	131,037	150,321	337,026	975,164
Deposits from customers	3,322,550	454,601	294,513	82,744	4,154,408
Other borrowed funds	-	293	293	321,908	322,494
Other liabilities	189,750	5,234	6,759	10,019	211,762
Equity	-	-	-	867,660	867,660
Total liabilities and equity	4,447,678	668,895	597,333	1,701,306	7,415,212

	Up to 3 months KD 000s	*3 – 6 months KD 000s*	*6 – 12 months KD 000s*	*More than 12 months KD 000s*	*Total KD 000s*
31 December 2016					
ASSETS					
Cash and cash equivalents	896,005	-	-	-	896,005
Treasury bills and bonds with CBK and others	221,307	55,866	35,693	167,130	479,996
Due from banks and other financial institutions	420,413	183,697	129,612	69,690	803,412
Loans and advances to customers	1,190,157	540,346	786,987	1,706,596	4,224,086
Investment securities	29,667	8,780	10,349	505,539	554,335
Other assets	51,695	2,704	4,344	121,668	180,411
Property and equipment	-	-	-	89,497	89,497
Intangible assets	-	-	-	41,134	41,134
Total assets	2,809,244	791,393	966,985	2,701,254	7,268,876
LIABILITIES AND EQUITY					
Due to banks	661,913	33,412	66,482	62,869	824,676
Due to other financial institutions	380,711	182,162	373,970	271,576	1,208,419
Deposits from customers	2,671,586	381,249	336,520	347,904	3,737,259
Other borrowed funds	4,338	2,095	108,338	323,223	437,994
Other liabilities	174,428	3,496	7,237	29,811	214,972
Equity	-	-	-	845,556	845,556
Total liabilities and equity	3,892,976	602,414	892,547	1,880,939	7,268,876

23. RISK MANAGEMENT (continued)

D. OPERATIONAL RISK

Operational risk is the risk of loss arising from the failures in operational process, people and system that supports operational processes. The Group has a set of policies and procedures, which are approved by the Board of Directors and are applied to identify, assess and supervise operational risk in addition to other types of risks relating to the banking and financial activities of the Group. Operational risk is managed by Risk management. Risk management ensures compliance with policies and procedures to identify, assess, supervise and monitor operational risk as part of overall Global risk management.

24. CAPITAL MANAGEMENT

The primary objectives of the Group's capital management policy are to ensure that the group complies with regulatory capital requirements and that the group maintains strong credit ratings and health capital ratios in order to support its business and maximize shareholder value.

Capital adequacy, financial leverage and the use of various levels of regulatory capital are monitored regularly by the Group's management and are governed by guidelines of Basel Committee on Banking Supervision as adopted by the CBK.

The disclosures relating to the capital adequacy regulations issued by Central Bank of Kuwait (CBK) as stipulated in CBK Circular number 2/RB, RBA/A336/2014 dated 24 June 2014 (Basel III) and the Leverage regulations as stipulated in CBK Circular number 2/BS/ 342/2014 dated 21 October 2014 under the Basel Committee framework are included under the 'Basel III qualitative and quantitative disclosures' section of the Annual Report.

The Group's risk weighted assets (after regulatory phase out of haircut on real estate collaterals of 90% (2016:80%), regulatory capital and capital adequacy ratios (Basel III), are shown below:

	2017 ***KD 000s***	*2016* *KD 000s*
Risk weighted assets	5,716,085	5,434,896
Total capital required	800,253	760,885
Common Equity Tier 1 (CET1) capital	624,124	609,506
Additional Tier 1 (AT1) capital	145,389	146,055
Tier 2 capital	154,196	150,967
Total eligible capital	923,709	906,528
CET1 capital adequacy ratio	10.9%	11.2%
Tier 1 capital adequacy ratio	13.5%	13.9%
Total capital adequacy ratio	16.2%	16.7%

The Group's financial leverage ratio,calculated in accordance with CBK circular number 2/BS/ 342/2014 dated 21 October 2014, is shown below:

	2017 ***KD 000s***	*2016* *KD 000s*
Tier 1 capital	**769,513**	755,561
Total exposure	7,943,450	7,793,599
Leverage ratio	9.7%	9.7%

25. COMPARATIVE INFORMATION

Certain corresponding figures for 2016 have been reclassified in order to conform to the presentation of financial statements for the current year. Such reclassifications do not affect previously reported net profit or shareholders' equity.