



**RISK AND CAPITAL MANAGEMENT
DISCLOSURES**

Table of Contents

1 Executive summary	3
2 Group Structure	4
3 Capital structure and capital adequacy ratio	5
4 Credit risk	7
4.1 Capital requirements for credit risk	7
4.2 Quantitative information on credit risk	10
4.2.1 Gross and average credit exposure	10
4.2.2 Credit exposure by geography	11
4.2.3 Credit exposure by sector	12
4.2.4 Exposure by maturity	13
4.2.5 Exposures in excess of regulatory limits	14
4.2.6 Impaired facilities and past due exposures	14
4.2.7 Credit risk mitigation	16
4.2.8 Related party and intra-group transactions	17
4.2.9 Exposure to highly leveraged and other high risk counterparties	18
4.2.10 Renegotiated facilities	18
4.2.11 Equity investments held in banking book	18
5 Market risk	20
6 Operational risk	20
7 Other types of risk	21
7.1 Liquidity risk	21
7.2 Management of profit rate risk in the banking book	22
7.3 Concentration risk	23
7.4 Counterparty credit risk	23
7.5 Reputational risk (non-performance risk)	23
7.6 Displaced commercial risk	24
7.7 Other risks	24
8 Product disclosures	24
8.1 Equity of Investment Account Holders (EIAH)	24
8.2 Restricted investment accounts	27
9 Financial performance and position	30

1 Executive summary

The Central Bank of Bahrain's ("CBB") Basel 3 guidelines outlining the capital adequacy framework for banks incorporated in the Kingdom of Bahrain became effective from 1 January 2015. The banks are required to maintain minimum capital adequacy ratio of 12.5% on a consolidated basis [i.e. CET1 – 6.5%, AT1-1.5%, Tier 2 – 2% and CCB – 2.5%] and a capital adequacy ratio of 8% on a solo basis [i.e. CET1 – 4.5%, AT1 – 1.5% and Tier 2 – 2%]. These disclosures have been prepared in accordance with the CBB requirements outlined in the Public Disclosure Module ("PD"), Section PD-1.3: Disclosures in Annual Reports of the CBB Rule Book, Volume II for Islamic Banks and Section PD-3.1.6: Publication of reviewed (Unaudited) quarterly financial statements for locally incorporated banks. Section PD-1.3 reflect the requirements of Basel 2 - Pillar 3 and the Islamic Financial Services Board's ("IFSB") recommended disclosures for Islamic banks and PD 3.1.6 highlights the requirement to make quantitative disclosures described in PD-1.3 on their web site along with the half yearly financial statements.

GFH Financial Group (formerly Gulf Finance House BSC) ["GFH/ the Bank"] was incorporated in 1999 in the Kingdom of Bahrain under Commercial Registration No. 44136. The Bank operates as an Islamic Wholesale Investment Bank under a license granted by the Central Bank of Bahrain ("CBB"). The Bank's activities are regulated by the CBB and supervised by a Shari'a Supervisory Board whose role is defined in the Bank's Memorandum and Articles of Association. The principal activities of the Bank include investment advisory services and investment transactions which comply with Islamic rules and principles.

This report contains a description of the Bank's risk and capital management practices and processes, including detailed information on the capital management process.

As at 30 June 2015 the Group's total capital ratio stood at a healthy 21.72%.

The Bank's Tier I and total capital adequacy ratios comply with the minimum capital requirements under the CBB's Basel 3 / IFSB for Islamic financial institutions framework.

The Banks total risk weighted assets as at 30 June 2015 amounted to USD 3,940,071 thousand. Credit risk accounted for 92 percent, operational risk 4 percent, and market risk 4 percent of the total risk weighted assets respectively. Tier I and total regulatory capital were USD 841,534 thousand and USD 855,750 thousand respectively, as at 30 June 2015.

At 30 June 2015, Group's CET1 and T1 capital and total capital adequacy ratios were 21.29% and 21.36%, respectively.

2 Group Structure

The Bank along with its subsidiaries is together referred to as the “Group”. The principal material subsidiaries and associates as at 30 June 2015 and their treatment for consolidated capital adequacy purposes are as follows:

Subsidiaries	Entity classification as per PCD module for consolidated capital adequacy	Treatment by the Bank	
		Consolidated	Solo Basis
Cemena Investment Company	Significant commercial entity	Risk weighting of investment exposure	
Khaleeji Commercial Bank (KHCB)	Banking subsidiary	Full consolidation	Full deduction from capital
GFH Sukuk Limited	Financial entity	Full consolidation	No impact as no direct investment by the Bank and the entity is a securitization vehicle
Morocco Holding Company (“MGIC”)	Commercial entity	Risk weighting in investment exposure	
GFH Capital Limited	Financial entity	Full consolidation	Full deduction from capital
Associates			
Injazat Technology Fund BSC (c)	Financial entity	Risk weighting of investment exposure	

Leeds United Football Company	Commercial entity	Risk weighting of investment exposure
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The investments in subsidiaries and associates are subject to large exposure and connected counterparty limits and guidelines set by the CBB. These guidelines are considered for transfer of funds or regulatory capital within the Group. The investment in subsidiaries should be generally deducted from the capital of the Bank. In the opinion of the Bank, certain investments / asset holding vehicles are pass-through entities and hence the underlying investments are risk weighted.

During the period, the Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI) issued amendments to FAS 23 which are effective from 1 January 2015. These amendments provide clarification and expand the scenarios for assessing control when an entity holds less than majority voting rights in an investee. In particular, the concept of de-facto control has been introduced.

In accordance with the transitional provisions of the amended FAS 23, the Group reassessed its control conclusions for its investees as of 1 January 2015, being the date of initial application of these amendments. The exercise has resulted in change in control conclusion in respect of three entities namely; Khaleeji Commercial Bank, Morocco Gateway Investment Company and Capital Real Estate BSC (c) (“CRE”). Accordingly, the Bank has consolidated these entities for the preparation of its condensed consolidated interim financial information for the six months period ended 30 June 2015 and these entities are also considered as subsidiaries for capital adequacy computation.

KHCB, a banking subsidiary of the Bank, is a locally incorporated commercial bank and the specific quantitative and qualitative disclosures pertaining to all the risks of KHCB have been disclosed in the Risk Management Disclosures of KHCB as at 30 June 2015, which can be accessed through the following link. [<http://www.khcbonline.com/main/Investor-Relations/Financial-Reports/>]. This documents intends to combine the risk and capital management disclosures of the parent bank and its involvement with its subsidiaries and associates. The quantitative disclosures in these documents provide further details of the exposures used for capital calculation purposes (where some entities are consolidated and some may be risk weighted) and accordingly will not match with the consolidated financial statements of the Group.

There are no restrictions for transfer of capital other than those applicable to licensed financial entities and process of commercial companies law of respective jurisdictions.

3 Capital structure and capital adequacy ratio

The Bank’s regulator CBB sets and monitors capital requirements for the Bank as a whole (i.e. at a consolidated level). The banks are required to maintain minimum capital adequacy ratio of 12.5% on a consolidated basis [i.e. CET1 – 6.5%, AT1-1.5%, Tier 2 – 2% and CCB – 2.5%] and a capital adequacy ratio of 8% on a solo basis [i.e. CET1 – 4.5%, AT1 – 1.5% and Tier 2

– 2%]. Banking operations are categorised as either trading book or banking book, and risk-weighted assets are determined according to specified requirements that seek to reflect the varying levels of risk attached to assets and off-balance sheet exposures.

The Bank's policy is to maintain strong capital base so as to maintain investor, creditor and market confidence and to sustain the future development of the business.

The Bank has adopted the standardised approach to credit and market risk and basic indicator approach for operational risk management under the revised framework.

The Bank's regulatory capital position at 30 June 2015 was as follows:

USD'000

Eligible Capital	30 June 2015
<u>Common Equity Tier 1 (CET 1)</u>	
Issue and fully paid ordinary shares	597,995
Statutory reserve	70,060
Retained earnings	13,719
Current interim cumulative net profit	3,320
Accumulated other comprehensive income and losses (and other reserves)	23,266
Total CET1 capital before minority interest	708,360
Total minority interest in banking subsidiaries given recognition in CET1 capital	131,560
Total CET 1 capital prior to regulatory adjustments	839,920
Less: Investment in own shares	(948)
Total Common Equity Tier 1 capital after to the regulatory adjustments	838,972
Other capital (AT1 & T2)	
Instruments issued by banking subsidiaries to third parties	
- AT2	2,562



Total Tier 1 Capital	841,534
Instruments issued by banking subsidiaries to third parties	
- T2	3,415
- General financing loss provisions	10,801
Total Capital	855,750

USD 000's

Risk weighted exposures	30 June 2015
Credit risk	3,652,959
Market risk	130,043
Operational risk	157,069
Total capital base	3,940,071
CET1	21.29%
T1	21.36%
Total Capital Adequacy ratio (Total Capital)	21.72%

The Bank's paid up capital consists only of ordinary shares which have proportionate voting rights.

4 Credit risk

4.1 Capital requirements for credit risk

To assess its capital adequacy requirements for credit risk in accordance with the CBB requirements, the Bank adopts the standardized approach. According to the standardized approach, on and off balance sheet credit exposures are assigned to various defined categories based on the type of counterparty or underlying exposure. The main relevant categories are claims on banks, claims on investment firms, past due facilities, investment in equities, holdings of real estate, claims on corporate portfolio and other assets. Risk Weighted Assets (RWAs) are calculated based on prescribed risk weights by CBB relevant to the standard categories and counterparty's external credit ratings, where available.



Rating of exposures and risk weighting

As the Bank is not engaged in granting credit facilities in its normal course of business, it does not use a detailed internal credit “grading” model. The use of external rating agencies is limited to assigning of risk weights for placements with financial institutions. The Bank uses ratings by Standard & Poors, Fitch and Capital Intelligence to derive risk weights for the purpose of capital adequacy computations. However, preferential risk weight of 20% is used which is applicable to short term claims on locally incorporated banks where the original maturity of these claims are three months or less and these claims are in Bahraini Dinar or US Dollar. The other exposures are primarily classified as ‘unrated exposure’ for the purposes of capital adequacy computations.

As per CBB guidelines, 100% of the RWA’s financed by owners’ equity (i.e. self financed) are included for the purpose of capital adequacy computations whereas only 30% of the RWA’s financed by equity of investment account holders [EIAH] are required to be included.

Following is the analysis for credit risk as computed for regulatory capital adequacy purposes:

USD 000's

Asset categories for credit risk	Gross credit exposures	Average risk weights	Total credit risk weighted exposure
Self financed assets			
Cash items	13,253	0%	-
Total claims on sovereigns	44,706	0%	-
Standard Risk Weights for Claims on Banks	48,212	30%	14,674
Preferential Risk Weight for Claims on Locally Incorporated Banks	16,300	20%	3,260
Short-term Claims on Banks	1,368	20%	275
Claims on Corporates including Takaful Companies and Category 3 Investment Firms	560,313	89%	499,210
Past Due Facilities	136,705	141%	192,714
Investments in Securities and Sukuk	237,128	357%	846,610
Holding of Real Estate	631,772	287%	1,810,834
Others Assets	15,829	100%	15,829
Total self financed assets (A)	1,705,586	198%	3,383,406
Total regulatory capital required (A x 12.5%)		12.5%	422,926
Financed by EIAH			
Cash items	-	0%	-
Total claims on sovereigns	163,326	0%	-
Total Claims on PSEs	6,934	0%	-
Standard Risk Weights for Claims on Banks	62,046	48%	29,536
Preferential Risk Weight for Claims on Locally Incorporated Banks	104,151	20%	20,830
Claims on Corporates including Takaful Companies and Category 3 Investment Firms	618,146	72%	443,287
Other assets and specialized financing	57,822	700%	404,855
Total financed by EIAH (B)	1,012,425	89%	898,508
Considered for credit risk (C) = (B x 30%)		30%	269,553
Total regulatory capital required (C x 12.5%)		12.5%	33,694
TOTAL GROSS CREDIT EXPOSURES	2,718,011	-	-
TOTAL RISK WEIGHTED EXPOSURE			3,652,959
TOTAL REGULATORY CAPITAL REQUIRED			456,620

4.2 Quantitative information on credit risk

4.2.1 Gross and average credit exposure

The following are gross credit risk exposures considered for Capital Adequacy Ratio calculations of the Bank classified as per disclosure in the condensed consolidated interim financial information:

USD 000's

Balance sheet items	Self Finance exposure	Financed by EIAH	Total Funded exposure	Unfunded exposure	Total gross credit exposure	Average gross credit exposure*
Bank balances	70,839	79,173	150,012	-	150,012	130,498
Placements with financial institutions	36,012	140,146	176,158	-	176,158	201,015
Financing receivables	193,012	612,836	805,848	64,263	870,111	818,134
Investment securities	490,031	181,321	671,352	-	671,352	647,398
Assets acquired for leasing	141,082	-	141,082	-	141,082	136,017
Investment properties	309,767	-	309,767	-	309,767	309,767
Development properties	62,371	-	62,371	-	62,371	64,404
Equity-accounted investees	6,907	-	6,907	-	6,907	6,907
Property, plant and equipment	22,764	-	22,764	-	22,764	22,764
Other assets	285,946	-	285,946	21,541	307,487	262,751
Total credit exposure	1,618,731	1,013,476	2,632,207	85,804	2,718,011	2,599,655

* Average gross credit exposures have been calculated based on the average of balances outstanding on a quarterly basis for six months period ended 30 June 2015. Assets funded by EIAH are geographically classified in GCC countries, and are placed with Banks and financial institutions having maturity profile of up to 3 months.

4.2.2 Credit exposure by geography

The classification of credit exposure by geography, based on the location of the counterparty, was as follows:

USD 000's

	GCC countries	MENA	Asia	UK	Europe (excluding UK)	USA	Total
Assets							
Bank balances	132,387	4,427	291	4,939	338	7,630	150,012
Placements with financial institutions	176,158	-	-	-	-	-	176,158
Financing receivables	748,809	35,721	-	21,318	-	-	805,848
Investment securities	436,001	51,965	73,655	87,703	20,428	1,600	671,352
Assets acquired for leasing	141,082	-	-	-	-	-	141,082
Investment properties	309,767	-	-	-	-	-	309,767
Development properties	62,371	-	-	-	-	-	62,371
Equity-accounted investees	6,907	-	-	-	-	-	6,907
Property, plant and equipment	22,764	-	-	-	-	-	22,764
Other assets	179,144	81,704	5,599	19,499	-	-	285,946
Total	2,215,390	173,817	79,545	133,459	20,766	9,230	2,632,207
Off-Balance sheet							
Restricted investment accounts	48,700	52	-	-	-	-	48,752
Financial guarantees	53,066	-	-	-	-	-	53,066
Undrawn financing facilities	169,714	1,382	-	-	-	-	171,096

*The geographical exposures of total assets are reconciled to the gross credit exposures considered for risk weighting for capital adequacy computation purposes.

4.2.3 Credit exposure by sector

The classification of credit exposure by industry was as follows:

USD 000's

	Trading and manufacturing	Banks and financial institutions	Development Infrastructure	Technology	Others	Total
Assets						
Bank balances	-	150,012	-	-	-	150,012
Placements with financial institutions	-	176,158	-	-	-	176,158
Financing receivables	-	75,212	222,477	-	508,159	805,848
Investment securities	76,051	69,221	292,548	3,679	229,853	671,352
Assets acquired for leasing	-	-	141,082	-	-	141,082
Investment properties	-	-	309,767	-	-	309,767
Development properties	-	-	62,371	-	-	62,371
Equity-accounted investees	-	-	6,907	-	-	6,907
Property, plant and equipment	-	-	18,494	-	4,270	22,764
Other assets	297	31,398	191,498	-	62,753	285,946
Total	76,348	502,001	1,245,144	3,679	805,035	2,632,207
Off-Balance sheet items						
Restricted investment accounts	-	-	48,752	-	-	48,752
Financial guarantees	-	-	6,953	46,113	-	53,066
Undrawn financing facilities	-	-	31,368	139,728	-	171,096

*The sector exposures of total assets are reconciled to the gross credit exposures considered for risk weighting for capital adequacy computation purposes.

4.2.4 Exposure by maturity

The maturity profile of exposures based on maturity was as follows:

USD 000's

	Up to 3 months	3 to 6 months	6 months- 1 year	1 to 3 years	Over 3 years	Maturity not stated	Total
Assets							
Bank balances	149,959	-	-	-	-	53	150,012
Placements with financial institutions	176,158	-	-	-	-	-	176,158
Financing receivables	127,024	59,300	52,143	162,610	404,771	-	805,848
Investment securities	4,509	-	35,169	451,041	180,633	-	671,352
Assets acquired for leasing	-	695	700	1,379	138,308	-	141,082
Investment properties	-	-	-	259,404	50,363	-	309,767
Development properties	-	-	-	45,501	16,870	-	62,371
Equity-accounted investees	-	-	-	2,488	4,419	-	6,907
Property, plant and equipment	-	-	-	-	21,764	1,000	22,764
Other assets	21,212	16,373	99,674	113,687	-	35,000	285,946
Total assets	478,862	76,368	187,686	1,036,110	817,128	36,053	2,632,207
Off-Balance sheet items							
Restricted investment accounts	10,769	-	12,507	25,476	-	-	48,752
Commitments	64,743	46,546	81,111	25,260	6,502	-	224,162

The table above shows the maturity profile of the Group's assets and unrecognized commitments on the basis of their contractual maturity, here available. For other items, (including past due receivables), the maturity profile is on the basis of their expected realization. The total assets are reconciled to the gross credit exposures considered for capital adequacy computation purposes.

4.2.5 Exposures in excess of regulatory limits

The CBB has set single exposure limit of 15 % of the Bank's capital base on exposures to individual or a group of closely related counterparties and as per the prudential rules prior approval of the CBB is required for assuming such exposures, except in cases of certain categories of exposure which are exempted by CBB. In case of non-exempt exposures, a deduction from capital is required for the amount in excess of the single exposure limits.

There were no exposures in excess of 15% of capital base as at 30 June 2015.

4.2.6 Impaired facilities and past due exposures

The commercial and credit granting is done by KHCB and for the specific qualitative disclosures pertaining to KHCB please refer Risk Management Disclosures of KHCB [*Refer section 2 of this document*].

As the Bank is not engaged in granting credit facilities in its normal course of business, it does not use a detailed internal credit "grading" model. The current risk assessment process classifies credit exposures into two broad categories "Unimpaired" and "Impaired", reflecting risk of default and the availability of collateral or other credit risk mitigation. The Bank does not perform a collective assessment of impairment for its credit exposures as the credit characteristics of each exposure is considered to be different. The collective assessment of impairment in the disclosure is from KHCB. Credit and investment exposures are subject to regular reviews by the Investment units and Risk Management Department. Quarterly updates on the investments / facilities are prepared by the investment unit reviewed by the management and sent to the Board for review. The

All impaired and past due credit exposures at 30 June 2015 mainly relate to the development infrastructure sectors.

Movement in impairment provisions during the period:

US\$ 000's

30 June 2015	Financing receivables	Financing to projects	Receivable from investment banking services	Other receivables
At 1 January	97,184	85,588	153,630	79,759
Charge for the period	1,525	-	-	-
Write back during the year	(129)	-	-	-
Write off during the year	(1,658)	-	-	-
At 30 June	96,922	85,588	153,630	79,759

Analysis of past due and impaired and past due but not impaired receivables:

US\$ 000's

As at 30 June 2015	Past due but not impaired amounts *	Gross impaired amounts
Up to 3 months	100,653	-
Over 3 months to 1 year	21,769	24,281
1 to 3 years	1,371	32,360
Over 3 years	50,838	411,037
Total	174,631	467,678

* The Bank believes that the past due exposures are not further impaired on the basis of the assessment of the level of future expected cash flows from the counterparty and / or the stage of collection of amounts owed to the Bank.

Geographical concentration of impaired and past due receivables:

As at 30 June 2015	Gross impaired amounts	Specific impairment allowance	Net exposure				Collective impairment
			Net impaired	Past due but not impaired	Neither past due nor impaired	Total	
GCC	249,182	192,196	56,986	65,171	190,239	312,396	10,637
Countries							
Other	64,826	64,826	-	21,482	24,842	46,324	-
MENA							
Other Asia	80,000	80,000	-	29,117	3,000	32,117	-
Europe	73,670	73,670	-	1,875	-	1,875	164
UK	-	-	-	-	17,980	17,980	-
Total	467,678	410,692	56,986	117,645	236,061	410,692	10,801

Industry/sector wise breakdown of impaired and past due receivables:

As at 30 June 2015	Gross impaired amounts	Specific impairment allowance	Net exposure				Collective impairment
			Net impaired	Past due but not impaired	Neither past due nor impaired	Total	
Development							
Infrastructure	415,756	378,653	37,103	59,754	55,593	152,450	4,016
Banks and financial institution	16,781	15,423	1,358	21,416	103,194	125,968	1,987
Others	35,141	16,616	18,525	36,475	77,274	132,274	4,798
Total	467,678	410,692	56,986	117,645	236,061	410,692	10,801

4.2.7 Credit risk mitigation

The credit risk exposures faced by the Bank are primarily in respect of its own short term liquidity related to placements with other financial institutions, and in respect of investment related funding made to its project vehicles. The funding made to the project vehicles are based on the assessment of the underlying value of the assets and the expected streams of cash flows. Since these exposures arise in the ordinary course of the Bank's investment banking activities and are with the project vehicles promoted by the Bank, they are generally transacted without any collateral or other credit risk mitigants.

4.2.8 Related party and intra-group transactions

Related counterparties are those entities which are connected to the Bank through significant shareholding or control or both. The Bank has entered into business transactions with such counterparties in the normal course of its business. For the purpose of identification of related parties the Bank follows the guidelines issued by Central Bank of Bahrain and definitions as per FAS issued by AAOIFI. Detailed break up of related parties transactions and exposures as at and for the six months period ended 30 June 2015 are as follows:

US\$'000's

	Associates	Key management personnel	Significant shareholders / entities in which directors are interested	Assets under management including special purpose entities	Total
30 June 2015					
Assets					
Financing assets	886	-	-	10,217	11,103
Equity-accounted investees	6,907	-	-	-	6,907
Investment securities	21,782	-	22,680	127,746	176,528
Other assets	16,218	-	-	88,341	104,559
Property, plant and equipment	197	-	-	-	197
Liabilities					
Investors' funds	-	-	-	5,271	5,271
Customer current accounts	310	-	730	3,488	4,528
Other liabilities	-	-	-	52,826	52,826
Equity of investment holders	289	-	3,493	22,220	26,002
Income					
Income from financing assets and assets acquired for leasing	72	-	-	268	340
Income from investment banking services	-	-	-	21,022	21,022
Management and other fees	88	-	-	-	88
Income from investment securities	(507)	-	-	-	(507)
Share of profit of equity-accounted investees	1,838	-	-	-	1,838

US\$ 000's

30 June 2015	Associates	Key management personnel	Significant shareholders / entities in which directors are interested	Assets under management including special purpose entities	Total
Expenses					
Return to investment account holders	3	-	3	156	162
Staff cost	-	2,354	-	-	2,354
Other expenses	-	185	-	45	230

4.2.9 Exposure to highly leveraged and other high risk counterparties

The Bank has no exposure to highly leveraged and other high risk counterparties as per definition provided in the CBB rule book PD 1.3.24.

4.2.10 Renegotiated facilities

As at 30 June 2015, other assets which are neither past due nor impaired include certain short-term financing to projects which were renegotiated. In certain cases, on a need basis, the Bank supports its project vehicles by providing short-term liquidity facilities. These facilities are provided based on assessment of cash flow requirements of the projects and the projects ability to repay the financing amounts based on its operating cash flows. The assessment is independently reviewed by the management of the Bank. Although no specific collateral is provided, such exposures are usually adequately covered by the value of the underlying project asset cash flows. The terms of the renegotiation primarily include extension of the repayment period. The facilities are provided for as viewed necessary based on periodic impairment assessments.

4.2.11 Equity investments held in banking book

For qualitative disclosures pertaining to KHCB, kindly refer the Risk Management Disclosures for KHCB for the six months period ended 30 June 2015 [*Refer section 2 of this document*].

The Bank does not have a trading book and hence all of its equity investments are classified in the banking book and are subject to credit risk weighting under the capital adequacy framework. For regulatory capital computation purposes, the Bank's equity investments in the banking book include available-for-sale investments, significant investments in commercial entities and associate investments in nonfinancial commercial entities (i.e. significant financial entities which qualify as associates are treated separately for regulatory purposes).

The RMD provides an independent review of all transactions. A fair evaluation and impairment assessment of investments takes place every quarter with inputs from the Investment department and RMD. Investment updates are periodically reviewed by the Board of Directors. Regular audits of business units and processes are undertaken by Internal Audit.

The Bank's equity investments are predominantly in its own projects, which include venture capital, private equity and development infrastructure investment products. The intent of such investments is a later stage exit along with the investors principally by means of sell outs at the project level or through initial public offerings. The Bank also has a strategic financial institutions investment portfolio which is aligned with the long term investment objectives of the Bank.

Information on equity investments (including significant commercial entities)	US\$ 000's
Privately held	504,390
Quoted in an active market	8,432
Managed funds	10,035
Realised gain/ (loss) during the period	2,936
Unrealised gain recognized in the balance sheet not through income statement	1,781

The following are the categories under which equity investments are included in the capital adequacy computations as per the requirements of the CBB rules:

US\$ 000's

	Gross exposure*	Risk weight	Risk weighted exposure	Capital charge @ 12.5%
Listed equity investments	8,432	100%	8,432	1,054
Unlisted equity investments	136,790	150%	205,185	25,648
Significant investment in the common shares of financial entities >10%	5,820	250%	14,550	1,819
Significant investment in the common shares of commercial entities	76,051	800%	608,408	76,051
Investment in listed unrated funds	10,035	100%	10,035	1,254
All other holdings of real estate	327,549	200%	655,098	81,887
Investments in listed real estate companies	5,675	300%	17,025	2,128
Investment in unlisted real estate companies	280,054	400%	1,120,216	140,027
Total	850,406		2,638,949	329,869

*Includes amounts of risk weighted assets arising from full consolidation of certain investments.

5 Market risk

To assess its capital adequacy requirements for market risk in accordance with the CBB capital adequacy module for Islamic Banks, the Bank adopts the standardised approach. Foreign exchange risk charge is computed based on 8% of overall net open foreign currency position of the Bank.

US\$ 000's

	30 June 2015	Maximum during the period	Minimum during the period
Foreign exchange risk - A	10,374	10,579	10,374
Risk weighted assets - B= (A*12.5)	129,675	133,238	129,675
Capital requirement – (B*12.5%)	16,209	16,655	16,209

	30 June 2015	Maximum during the period	Minimum during the period
Sukuk risk Equity of investment account holders - A	98	2,215	98
Risk weighted assets - B= (A*12.5*30%)	368	8,306	368
Capital requirement – (B*12.5%)	46	997	44

The Sukuk risk is arising on full consolidation of KHCB for capital adequacy purposes.

6 Operational risk

The Bank adopts the Basic Indicator Approach to evaluate operational risk charge in accordance with the approach agreed with the CBB. The bank's average gross income for the last two financial years is multiplied by a fixed coefficient alpha of 15% set by CBB and a multiple of 12.5x is used to arrive at the risk weighted assets that are subject to capital charge.

US\$ 000's

	Average gross income	Risk weighted assets	Capital charge at 12.5%
Operational risk	83,770	157,069	19,633

Litigations and claims

The Group has a number of claims and litigations filed against it in connection with projects promoted by the Bank in the past and with certain transactions. Further, claims against the Bank also have been filed by former employees. Based on the advice of the Bank's external legal counsel who confirmed that the Bank has strong grounds to successfully defend itself against these claims. Accordingly, no provision for these claims has been made in the condensed consolidated interim financial information. No further disclosures regarding contingent liabilities arising from any of such claims are being made by the Bank as the directors of the Bank believe that such disclosures may be prejudicial to the Bank's legal position.

7 Other types of risk

For qualitative disclosures of the below mentioned risks for KHCB kindly refer Risk Management Disclosure of KHCB for the six months period ended 30 June 2015 [*Refer section 2 of this document*].

7.1 Liquidity risk

Liquidity risk is the risk that the Bank will encounter difficulty in meeting its financial obligations on account of a maturity mismatch between assets and liabilities. The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation. Whilst this is the policy, the Group's current position is under severe stress with contractual liabilities exceeding liquid assets. Focus has therefore been on extending the maturity of liabilities and raising capital in the form of debt or equity.

The following are the key liquidity ratios which reflect the liquidity position of the Bank.

Liquidity ratios	30 June 2015	Maximum	Minimum
Liquid assets : Total assets	12.84%	14.36%	12.84%
Liquid assets : Total deposits	66.84%	72.08%	66.84%
Short term assets : Short term liabilities*	53.50%	66.29%	53.50%
Illiquid assets : Total assets	87.16%	87.16%	85.64%

* Based on maturity profile of assets and liabilities of one year or less of GFH and KHCB.

The maturity profile of the Bank's financial liabilities including KHCB are as follows based on contractual cash flows are as follows:

USD'000's

	Up to 3 months	3 to 6 months	6 months-1 year	1 to 3 years	Over 3 years	Total
Investors' funds	9,634	-	-	-	-	9,634
Placements from financial and other institutions	167,897	17,297	15,268	126,625	2,188	329,275
Customer current accounts	117,763	14,912	6,194	10,204	-	149,073
Financing liabilities	31,701	-	41,752	82,261	12,785	168,499
Other liabilities	14,023	-	70,755	51,292	-	136,070
Total liabilities	341,018	32,209	133,969	270,382	14,973	792,551
Unrestricted investment accounts	387,899	188,984	92,567	294,019	-	963,469

7.2 Management of profit rate risk in the banking book

Profit rate risk is the potential impact of the mismatch between the rate of return on assets and the expected rate of return of the sources of funding. Majority of the Bank's profit based asset and liabilities are short-term in nature, except for certain long term liabilities which have been utilised to fund the Bank's strategic investments in its associates. The following disclosures are of the Bank and KHCB.

US\$'000's

	Up to 3 months	3 to 6 months	6 months - 1 year	1 to 3 years	Over 3 years	Total
30 June 2015						
Assets						
Placement with financial institutions	176,158	-	-	-	-	176,158
Financing assets	127,024	59,300	51,905	162,610	405,009	805,848
Asset acquired for leasing (including lease rental)	-	695	700	1,377	138,310	141,082
Investment securities	4,509	-	4,987	5,340	166,485	181,321
Total assets	307,691	59,995	57,592	169,327	709,804	1,304,409
Liabilities						
Investors' funds	9,634	-	-	-	-	9,634
Placements from financial and other institutions	167,897	17,297	15,268	126,625	2,188	329,275
Customer current accounts	3,313	-	-	-	-	3,313
Financing liabilities	31,701	-	41,752	82,261	12,785	168,499
Total liabilities	212,545	17,297	57,020	208,886	14,973	510,721
Equity of investment account holders	387,899	188,984	92,567	294,019	-	963,469
Profit rate sensitivity gap	(292,753)	(146,286)	(91,995)	(333,578)	694,831	(169,781)

The management of profit rate risk against profit rate gap limits is supplemented by monitoring the sensitivity of the Bank's financial assets and liabilities to various standard and non-standard profit rate scenarios. Standard scenarios that are considered on a monthly basis include a 100 basis point (bp) parallel fall or rise in all yield curves. An analysis of the Group's sensitivity to an increase or decrease in market profit rates for a 200bps increase / (decrease) is as below: (assuming no asymmetrical movement in yield curves and a constant balance sheet position)

US\$ 000's

200 bps parallel increase / (decrease)

At 30 June 2015
 Average for the period
 Maximum for the period
 Minimum for the period

2014
3,396
± 4,189
± 4,085
± 3,396

7.3 Concentration risk

This risk arises from exposure to a common set of factors that can produce losses large enough to threaten the Bank's health or ability to maintain its core business. Concentration risk can arise from exposure to specific classes of assets, sector, country, revenue streams, counterparty, a group of counterparties, etc. Concentration risk is mitigated by limits, diversification by assets, geography counterparty quality etc. As part of ICAAP, thresholds for exposure concentrations will be set up which will trigger additional capital requirements. The geographical and sector concentration of credit exposures has been disclosed in paragraphs 4.2.2 and 4.2.3.

7.4 Counterparty credit risk

Counterparty credit risk is the risk that a counterparty to a contract in the profit rate, foreign exchange, equity and credit markets defaults prior to maturity of the contract. In addition to the identified credit risk exposures the Bank's counterparty credit risk from markets as such is limited to the fair value of contracts of foreign exchange risk management instruments the overall exposure to which is usually not significant. For other credit market transactions (primarily inter-bank placements), the Bank has established a limit structure based on the credit quality (assessed based on external rating) of each counter party bank to avoid concentration of risks for counterparty, sector and geography. The Bank is constantly reviewing and monitoring the position to ensure proper adherence to the limits and defined policies of the Bank. As at 30 June 2015, the Bank did not have any open positions on foreign exchange contracts.

7.5 Reputational risk (non-performance risk)

Reputation risk is the risk that negative perception regarding the Bank's business practices or internal controls, whether true or not, will cause a decline in the Bank's investor base, lead to costly litigation that could have an adverse impact on liquidity or capital of the Bank. Being an Islamic Investment Bank, reputation is an important asset and among the issues that could affect the Bank's reputation is the inability to exit from investments, lower than expected returns on investments and poor communication to investors. A well developed and coherently implemented

communication strategy helps the Bank to mitigate reputational risks. Additionally, the RMD has recently put together an Internal Capital Adequacy Assessment Process (ICAAP) Policy to effectively assess and measure all non Pillar 1 risks.

7.6 Displaced commercial risk

Displaced Commercial Risk (DCR) refers to the market pressure to pay returns that exceeds the rate that has been earned on the assets financed by the liabilities, when the return on assets is under performing as compared with competitor's rates. The Bank's DCR primarily arises from the funds accepted in the form of Investment Account Holders (IAH) which is currently not very significant in terms of its size and in comparison to the overall activities of the Bank. The returns to investors on the funds are based on returns earned from short-term placements and hence the Bank is not exposed to a significant repricing risk or maturity mismatch risk in relation to these accounts. In relation to the DCR that may arise from its investment banking and restricted investment account products, the risk is considered limited as the Bank does not have any obligation to provide fixed or determinable returns to its investors. The Bank constantly monitors all potential risks that may arise from all such activities as part of its reputational risk management.

7.7 Other risks

Other risks include strategic, fiduciary risks, regulation risks etc. which are inherent in all business activities and are not easily measurable or quantifiable. However, the Bank has proper policies and procedure to mitigate and monitor these risks. The Bank's Board is overall responsible for approving and reviewing the risk strategies and significant amendments to the risk policies. The Bank senior management is responsible for implementing the risk strategy approved by the Board to identify, measure, monitor and control the risks faced by the Bank. The Bank as a matter of policy regularly reviews and monitors financial and marketing strategies, business performance, new legal and regulatory developments and its potential impact on the Bank's business activities and practices.

8 Product disclosures

8.1 Equity of Investment Account Holders (EIAH)

The Bank does not have significant amount under EIAH and does not use EIAH as a main source of its funding. The Bank does not, as a focused product proposition, offer EIAH products to its clients. The current EIAH deposits have been accepted on a case-by-case basis considering the Bank's relationship with its customers. The EIAH holder authorises the Bank to invest the funds in any investments approved by the Bank's Sharia'a Board without any preconditions. All EIAH accounts are on profit sharing basis, but the Bank does not guarantee any particular level of return. In accordance with the principles of Sharia'a, the entire investment risk is on the investor. Any loss arising from the investment will be borne by the customer except in the case of the Bank's negligence. The Bank charges a Mudarib fee as its share of profit. Early withdrawal is at the discretion of the Bank and is subject to the customer giving reasonable notice for such withdrawal and agreeing to forfeit a share of the profit earned on such account.

Currently, the Bank comingles the EIAH funds with its funds for investments only into interbank placements and hence is not subject to any significant profit re-pricing or maturity mismatch risks. The Bank has an element of displaced commercial risk on EIAH which is mitigated by setting up and maintaining an appropriate level of Profit Equalisation Reserve (PER) and Investment Risk Reserve (IRR) to smoothen return to EIAH holders.

Profit Equalisation reserve (PER) is created by allocations from gross income of the Mudarabah before adjusting the Mudarib (Bank) share. Investment Risk Reserves (IRR) comprises amounts appropriated out of the income of investment account holders after deduction of the Mudarib share of income. Administrative expenses incurred for management of the funds are borne directly by the Bank and are not charged separately to investment accounts. All terms of the EIAH are agreed upfront with the customers and form part of the agreement with the customer. Till date, the Bank has not made any withdrawals on PER or IRR. Any movements on these accounts are therefore only on account of additional reserves added. The historical returns data on EIAH of the Bank is as follows:

	US\$ 000's	
	30 June 2015	31 December 2014
Total EIAH as at 30 June / 31 December	1,661	1,655
Average EIAH balance	1,658	1,657
Average rate of return earned (%)	0.44%	0.88%
Total profits on EIAH assets earned	8	16
Distributed to investor	7	14.60
Allocated to IRR	0.2	0.3
Allocated to PER	0.3	0.5
Bank's share of profits	0.5	0.6
Average declared rate of return (%)	0.44%	0.88%

The information disclosed above pertains to EIAH directly promoted by the Bank.

The disclosures below are pertaining to the EIAH from KHCB.

The details of income distribution to IAH holders for the last five years are given below:

	USD 000's				
	June 2015	2014	2013	2012	2011
Allocated income to IAH	21,655	34,066	35,318	26,321	23,931
Distributed profit *	9,862	23,451	23,127	16,703	17,584
Mudarib fees	11,793	10,615	12,191	9,618	6,347
As at 30 June					
IAH ^[1]	980,653	891,273	691,271	512,586	487,838
Profit Equalisation Reserve (PER)	-	-	-	-	-
Investment Risk Reserve (IRR)	-	-	-	-	-
Profit Equalisation Reserve-to-IAH (%)	-	-	-	-	-
Investment Risk Reserve-to-IAH (%)	-	-	-	-	-

^[1] Represents average balance

* Includes contribution towards deposit protection scheme

Ratio of profit distributed to PSIA by type of IAH (based on tenor):

USD 000's

Mudaraba Tenor	Profit distribution amount in USD					Ratio of profit paid as a percentage of total				
	June 2015	2014	2013	2012	2011	June 2015	2014	2013	2012	2011
1 Month ^[2]	1,618	3,459	3,947	4,321	4,838	16.4	14.7	17.1	25.9	27.5
3 Months	422	1,008	1,804	1,737	3,950	4.3	4.3	7.8	10.4	22.5
6 Months	1,761	3,859	2,918	1,257	2,027	17.9	16.5	12.6	7.5	11.5
12 Months	4,875	11,085	9,565	7,952	5,342	49.4	47.3	41.4	47.6	30.4
18 Months	3	3	-	-	-	0.0	0.0	-	-	-
24 Month	8	199	605	80	-	0.1	0.8	2.6	0.5	-
VIP Mudaraba PER and IRR expenses	1,175	3,838	4,289	1,355	1,875	11.9	16.4	18.5	8.1	10.7
	-	-	-	-	(448)	-	-	-	-	(2.6)
Total	9,862	23,451	23,128	16,702	17,584	100.0	100.0	100.0	100.0	100.0

^[2] Includes saving account and call mudaraba

Distribution of profits by type of IAH products:

(Annualised rates)

Year	Avg. profit earned from IAH assets (%age of asset)	PER set aside as a %age of IAH assets	IRR set aside as a %age of IAH assets	Mudharib fees as a %age of IAH assets	Profit paid as a %age of IAH assets
June 2015	2.21	-	-	1.20	1.01
2014	3.82	-	-	1.19	2.63
2013	5.11	-	-	1.76	3.35
2012	5.13	-	-	1.88	3.26
2011	4.99	-	-	1.22	3.69

Following are the average profit rates declared and distributed to the investors by the Bank:

(Annualised rates)

Type of deposit	June 2015	2014	2013	2012	2011
1 month Mudharaba ^[3]	0.91%	1.15%	1.12%	2.25%	2.51%
3 months Mudharaba	1.77%	2.19%	2.98%	3.08%	4.25%
6 months Mudharaba	2.72%	3.08%	3.64%	3.55%	4.52%
12 months Mudharaba	2.83%	3.39%	4.27%	4.46%	5.01%
18 months Mudharaba	3.13%	3.30%	-	-	-
24 months Mudharaba	3.39%	4.92%	5.07%	5.07%	-
VIP Mudharaba	2.24%	3.49%	4.09%	2.79%	3.67%

^[3] Includes saving account and call mudaraba

Market benchmark rates:

The Bank refers to the group of commercial Islamic banks incorporated in the Kingdom of Bahrain so as to benchmark the rate of return on IAH.

IAH account by type of assets:

The following table summarises the movement in type of assets in which the IAH funds are invested and allocated among various type of assets for the year ended 30 June 2015:

Particular	Allocation at 1 January 2015	Movement	Allocation at 30 June 2015	Proportion of total assets (%)
Cash and bank balances	78,711	(1,186)	77,525	57.5%
Placements with financial institutions	201,607	(61,462)	140,146	100.0%
Financing assets ^[4]	523,279	89,557	612,836	75.0%
Investment securities - Sukuk	95,432	85,889	181,321	100.0%
Total	899,029	112,798	1,011,828	

^[4] Includes Murabaha, Wakala, and Istisna contracts.

8.2 Restricted investment accounts

The Bank offers Restricted Investment Accounts (“RIAs”) to both financial institutions and high net worth individuals in the GCC. All RIA product offering documents (“Offering Document”) are drafted and issued with input from the Bank’s Investment Banking, Shari’a, Financial Control, Legal and Risk Management Departments to ensure that the Investors have sufficient information to make an informed decision after considering all relevant risk factors. The Bank has guidelines for the development, management and risk mitigation of its’ RIA investments and for establishment of sound management and internal control systems to ensure that the interests of the investment account holders are protected at all times. Wherever it is necessary for the Bank establishes Special Purpose Vehicles (SPVs) for management of the investment. The Bank has a Board approved SPV Governance framework in place to equip the Board in ensuring that the management of such SPVs are conducted in a professional and transparent manner.

The Bank is aware of its fiduciary responsibilities in management of the RIA investments and has clear policies on discharge of these responsibilities. The Bank considers the following in discharge of its fiduciary responsibilities:

- Ensuring that the investment structure, Offering Documents and the investment itself are fully compliant with Islamic Shari’a principles and the CBB regulations;
- Appropriately highlighting to the Investors, as part of the RIA Offering Document, of all the relevant and known risk factors and making it clear that the investment risk is to be borne by the Investor before accepting the investment funds;
- Completing all necessary legal and financial due diligence on investments undertaken on behalf of the Investors with the same level of rigor as the Bank requires for its’ own investments;
- Ensuring that the funds are invested strictly in accordance with the provisions outlined in the Offering Documents;



- Preparing and disseminating periodical investment updates to Investors on a regular basis during the tenor of the investment;
- Distributing the capital and profits to the Investor in accordance with the terms of the offering document; and
- In all matters related to the RIA, RIA SPV(s) and the investment, act with the same level of care, good faith and diligence as the Bank would apply in managing its own investments.

Within the Bank, the abovementioned responsibilities and functions are provided, managed and monitored by qualified and experienced professionals from the Investment Banking, Shari'a, Financial Control, Legal, Investment Administration and the Risk Management Departments.

The restricted investment accounts primarily represents the investments in the projects promoted by the Bank and managed on a portfolio basis on behalf of investors.

The RIA products offered by the Bank had no distributions made in the past five years. The disclosures pertaining to RIA of KHCB are as under.

RIA name	Details	Launch date	Projected returns	Return frequency	Return annualized (%)				
					June 2015	2014	2013	2012	2011
RIA 1 - Safana	An investment structure designed to participate in the equity interest of Safana Investment WLL. A company established for the purpose of acquiring reclaimed land to subdivide and sell, the Bank made an offer to buy back < USD 53,050 of each investors funds in RIA 1 at par. This offer was formalized in a letter to investors dated 25 May 2011. A total of 74 of the 95 RIA 1 investors accepted the offer at a cost of USD 3,236,074 to the Bank and resulting in a total of 39 investors being fully exited from the RIA. As a result, total investors funds have reduced to USD 22.1 million.	2007	61.78% over product tenor	Bullet payment on maturity	-	-	-	-	-

RIA name	Details	Launch date	Projected returns	Return frequency	Return annualized (%)				
					June 2015	2014	2013	2012	2011
RIA 4 – Janayen	A restricted investment product designed to invest in growth and income generating real estate assets in the GCC and MENA regions. To date, RIA 4 has made distributions and redemptions to investors amounting to approximately 33.66% of investors' initial capital. These distributed funds were in the form of yields amounting to \approx 21.17% in addition to 12.49% redemption of capital.	2007	44.33%	Quarterly	-	-	-	-	-
RIA 5 - North Gate	A restricted investment product which owns a 6.0% stake in Shaden Real Estate Investment WLL which in turn (through its subsidiaries), holds a parcel of reclaimed land measuring approximately 3.875 million Sq. Meters (located in Al-Hidd, Muharraq). The mixed-use plot will be sold to end users subsequent to the completion of infrastructure works. During the period, the Bank has bought back 4,040,000 shares (50%) from its investors at USD 11,251,989 at a profit of 5%.	2008	90.66% over product tenor	Bullet return at maturity	-	-	-	-	-
RIA 6 - Locata	A Restricted Mudaraba product which entitles the investors beneficial ownership of 25% equity share capital of Locata Corporation Pty Ltd., a company incorporated in Australia. The Company has invented a new and patented wireless radiolocation technology and shall use this funding to scale up its production capacity, sales/marketing channels and further product enhancement	2009	110.54% over product tenor	Bullet return at maturity	-	-	-	-	-



RIA name	Details	Launch date	Projected returns	Return frequency	Return annualized (%)				
					June 2015	2014	2013	2012	2011
	capabilities. During 2014, 479 shares were bought back from its investors.								

9 Financial performance and position

Following are basic quantitative indicators of the financial performance:

	2015 (6 months)	2014 (6 months)	2013 (12 months)	2012 (12 months)	2011 (12 months)	2010 (12 months)
Return on average equity	1.93%	3.55%	-9.84%	2.19%	0.16%	-127.15%
Return on average assets	0.47%	0.92%	-3.05%	1.17%	0.04%	-25.62%
Cost-to-Income-Ratio*	71.29%	81.59%	113.73%	53.90%	79.20%	-

* Cost has been considered excluding impairment allowances. Income is net of finance expense.