



# **RISK AND CAPITAL MANAGEMENT DISCLOSURES**

*These disclosures have been prepared in accordance with the Public Disclosure Module (“PD”), Section PD-1.3: Disclosures in Annual Reports and PD-3.1.6 Semi-annual Disclosures, CBB Rule Book, Volume II for Islamic Banks. This document should be read in conjunction with the condensed consolidated interim financial information for the six months period ended 30 June 2019 and the qualitative disclosures in the annual report for the year ended 31 December 2018. Information already included in the condensed consolidated financial information are not repeated.*

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## **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. 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 website along with the half yearly financial statements.

GFH Financial Group ("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 condensed consolidated interim financial information for the six months period comprise of financial statements of the Bank and its subsidiaries (together referred to as "the Group") as at 30 June 2019. This document should be read in conjunction with the condensed consolidated interim financial information as at 30 June 2019 as certain disclosures which have made in the condensed consolidated interim financial information as at 30 June 2019 have not been reproduced in this document. The Group's financial statements are prepared and published on a full consolidation basis, with all material subsidiaries being consolidated in accordance with AAOIFI.

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

As at 30 June 2019, the Group's total capital ratio stood at 14.07%.

The Group'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 Group's total risk weighted assets as at 30 June 2019 amounted to USD 7,691,232 thousand. Credit risk accounted for 95 percent, operational risk 4 percent, and market risk 1 percent of the total risk weighted assets respectively. Tier I and total regulatory capital were USD 1,432,374 thousand and USD 1,182,695 thousand respectively, as at 30 June 2019.

At 30 June 2019, Group's CET1 and T1 capital and total capital adequacy ratios were 13.47%, 13.60% and 14.07% respectively.

## 2 Group Structure

The principal material subsidiaries and associates as at 30 June 2019 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
Khaleeji Commercial Bank BSC ('KHCB')	Banking subsidiary	Full consolidation	Full deduction from capital
GFH Capital Limited	Financial entity	Full consolidation	
GFH Sukuk Limited	Financial entity	Full consolidation	No impact as no direct investment by the Bank and the entity is a securitisation vehicle.
Morocco Gateway Investment Company	Commercial entity	Risk weighting of investment exposure	
KHCB Asset Company	Financial entity	Full consolidation	No impact as no direct investment by the Bank and the entity is a securitisation vehicle.
Harbour North 1 Real Estate SPC	Commercial entities	Risk weighting (look through approach) approved by the CBB on 12 June 2019. <sup>[ii]</sup>	
Harbour North 2a Real Estate SPC			
Harbour North 2b Real Estate SPC			
Harbour North 3 Real Estate SPC			
Harbour Row 3 Real Estate SPC			
Harbour Row East 3 Real Estate SPC			
Delmon Lost Paradise Project Company 1 SPC			
Delmon Lost Paradise Project Company 2 SPC			
Tunis Bay Investment Company	Commercial entity	Risk weighting of investment exposure	
Energy City Navi Mumbai Investment Company & Mumbai	Commercial entities	Risk weighting of investment exposure	

IT & Telecom Technology Investment Company (together "India Projects")		
Gulf Holding Company KSC (c)	Commercial entity	Risk weighting of investment exposure
Falcon Cement Company BSC (c)	Commercial entity	Risk weighting of investment exposure
GFH Properties SPC	Commercial entity	Risk weighting of investment exposure
Harbour Row 2 Real Estate SPC	Commercial entity	Risk weighting of investment exposure

	<b>Entity classification as per PCD Module for consolidated capital adequacy</b>	<b>Treatment by the Bank for Consolidated and Solo basis</b>
<b>Associates *</b>		
Bahrain Aluminium Extrusion Company BSC (c)	Commercial entity	Risk weighting of investment exposure
Global Banking Corporation BSC (c) ('GBCorp') <sup>[i]</sup>	Financial entity	Regulatory adjustment (deduction from capital)
Enshaa Development Real Estate BSC (c)	Commercial entity	Risk weighting of investment exposure
Capital Real Estate Projects BSC (c)	Commercial entity	Risk weighting of investment exposure
Al Areen Hotel SPC	Commercial entity	Risk weighting of investment exposure

[i] The Bank's investment in GB Corp does not exceed the threshold for deduction from capital, and hence, the entire investment exposure is risk weighted as per the regulatory adjustment.

[ii] These are pass-through entities and hence the underlying assets are risk weighted.

The investments in subsidiaries and associates are subject to large exposure and connected counterparty limits and guidelines set by the CBB. Significant investment in banking subsidiaries and financial entities that exceed the threshold for deduction from capital, the excess should be deducted from the capital of the Group

The Central Bank of Bahrain, vide its letter dated 30 June 2019, has continued the exemption granted to GFH Financial Group from including the assets acquired via recovery and via the shares swap as part of the Large Exposure and Connected Counterparty limits. The same will be reassessed by Central Bank of Bahrain on an annual basis.

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 2019, which can be accessed directly from investor's relations section in KHCB's website. This document provides the risk and capital

management disclosures of the GFH. The KHCB specific disclosures and requirements that are disclosed in the disclosures of KHCB were not reproduced in this document.

This document intends to combine the risk and capital management disclosures of the 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.

**Composition of Capital disclosure - As at 30 June 2019**

**Statement of financial position under the regulatory scope of consolidation and reconciliation of published financial statements to regulatory reporting as at 30 June 2019.**

The table below shows the link between the statement of financial position in the published financial statements (accounting statement of financial position) and the regulatory statement of financial position.

USD'000

<b>As at 30 June 2019</b>	<b>Consolidated Statement of Financial Position as in published financial statements (In USD'000)</b>	<b>Consolidated Statement of Financial Position as per Regulatory Reporting (In USD'000)</b>	<b>Reference</b>
<b>ASSETS</b>			
Cash and bank balance	369,552	364,822	
<i>Of which Expected Credit Losses (ECL) resulting from adoption of FAS 30</i>	<i>(8)</i>	<i>(8)</i>	A
Treasury portfolio	1,682,405	1,682,405	
<i>Of which Expected Credit Losses (ECL) as per FAS 30</i>	<i>(1,808)</i>	<i>(1,808)</i>	A
Financing assets	1,300,231	1,300,231	
<i>Of which Expected Credit Losses (ECL) as per FAS 30</i>	<i>(19,937)</i>	<i>(19,937)</i>	A
Real estate investments	1,821,444	761,316	
Proprietary investments	279,048	800,810	
<i>Of which Expected Credit Losses (ECL) as per FAS 30</i>	<i>(37)</i>	<i>(37)</i>	A
<i>Of which non-significant investments in financial entities</i>	<i>18,000</i>	<i>18,000</i>	B
<i>Of which significant investments in the common stock of financial entity</i>	<i>34,879</i>	<i>34,879</i>	C
Co-investments	77,048	77,048	

As at 30 June 2019	Consolidated Statement of Financial Position as in published financial statements (In USD'000)	Consolidated Statement of Financial Position as per Regulatory Reporting (In USD'000)	Reference
Asset held for sale	101,213	-	
Receivables and prepayments	482,334	420,139	
<i>Of which Expected Credit Losses (ECL) as per FAS 30</i>	<i>(2,597)</i>	<i>(2,597)</i>	A
Property and equipment	24,699	22,546	
<b>Total assets</b>	<b>6,137,974</b>	<b>5,509,318</b>	
<b>LIABILITIES</b>			
Clients' fund	61,097	61,097	
Placements from financial institutions, non-financials and individuals	2,789,757	2,789,757	
Customer current accounts	163,683	163,683	
Term financing	199,960	191,623	
Liabilities directly associated with assets held-for-sale	39,936	-	
Other liabilities	507,933	175,148	
<b>Total liabilities</b>	<b>3,762,366</b>	<b>3,381,308</b>	
<b>Equity of investment account holders</b>	<b>995,837</b>	<b>995,837</b>	
<b>OWNERS' EQUITY</b>			
Share capital	975,638	975,638	D
Treasury shares	(58,890)	(58,890)	E
Statutory reserve	117,301	117,301	F
Fair value reserve	(5,641)	(5,641)	G
Retained earnings	50,298	50,298	H
Foreign currency translation reserve	(43,150)	-	
Share grant reserve	1,198	1,198	I
<b>Total equity attributable to shareholders of the Bank</b>	<b>1,036,754</b>	<b>1,079,904</b>	
Non-controlling interests	317,621	52,269	
Non-controlling interests held-for-sale	25,396	-	
<i>Of which Total minority interest in banking subsidiaries given recognition in CET1 capital</i>	<i>-</i>	<i>52,269</i>	J
<b>Total owners' equity</b>	<b>1,379,771</b>	<b>1,132,173</b>	
<b>Total liabilities, equity of investment account holders and owners' equity</b>	<b>6,137,974</b>	<b>5,509,318</b>	

The table below shows the total assets and shareholders' equity of the Bank's subsidiaries as at 30 June 2019 which are not consolidated for capital adequacy calculation purposes.

Entity name	Principal activities	Total Assets* USD'000	Total Shareholders' equity * USD'000
Morocco Gateway Investment Company	Real estate development	139,936	105,446
India Project	Real estate development	599,478	460,477
Tunis Bay Investment Company	Real estate development	102,605	73,368
Gulf Holding Company	Real estate development	380,099	81,064

*\*The numbers disclosed are before considering intercompany eliminations.*

### Composition of Regulatory Capital as at 30 June 2019

Composition of Capital as at 30 June 2019			USD'000
			Source based on reference letters of the statement of financial position under the regulatory scope of consolidation
<b>Common Equity Tier 1 capital: instruments and reserves</b>			
1.	Directly issued qualifying common share capital plus related stock surplus	975,638	D
2.	Retained earnings	50,298	H
3.	Accumulated other comprehensive income (and other reserves)	112,858	F+G+I
4.	<i>Not applicable</i>		
5.	Common share capital issued by subsidiaries and held by third parties (amount allowed in group CET1)	52,269	J
6.	<b>Common Equity Tier 1 capital before regulatory adjustments</b>	1,091,063	
<b>Common Equity Tier 1 capital: regulatory adjustments</b>			
7.	Prudential valuation adjustments	-	
8.	Goodwill (net of related tax liability)	-	
9.	Other intangibles other than mortgage-servicing rights (net of related tax liability)	-	
10.	Deferred tax assets that rely on future profitability excluding those arising from temporary differences (net of related tax liability)	-	
11.	Cash-flow hedge reserve	-	
12.	Shortfall of provisions to expected losses	-	
13.	Securitisation gain on sale (as set out in paragraph 562 of Basel II framework)	-	
14.	<i>Not applicable</i>		
15.	Defined-benefit pension fund net assets	-	
16.	Investments in own shares	(58,890)	E
17.	Reciprocal cross-holdings in common equity	-	
18.	Investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions, where the bank does not own more than 10% of the issued share capital (amount above 10% threshold)	-	
19.	Significant investments in the common stock of banking, financial and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions (amount above 10% threshold)	-	
20.	Mortgage servicing rights (amount above 10% threshold)	-	
21.	Deferred tax assets arising from temporary differences (amount above 10% threshold, net of related tax liability)	-	
22.	Amount exceeding the 15% threshold	-	



23.	of which: significant investments in the common stock of financials	-	
24.	of which: mortgage servicing rights	-	
25.	of which: deferred tax assets arising from temporary differences	-	
26.	CBB specific regulatory adjustments	-	
27.	Regulatory adjustments applied to Common Equity Tier 1 due to insufficient Additional Tier 1 and Tier 2 to cover deductions	-	
28.	<b>Total regulatory adjustments to Common equity Tier 1</b>	-	
29.	<b>Common Equity Tier 1 capital (CET1)</b>	1,132,173	
<b>Additional Tier 1 capital: instruments</b>			
30.	Directly issued qualifying Additional Tier 1 instruments plus related stock surplus	-	
31.	of which: classified as equity under applicable accounting standards	-	
32.	of which: classified as liabilities under applicable accounting standards	-	
33.	<i>Directly issued capital instruments subject to phase out from Additional Tier 1</i>	-	
34.	Additional Tier 1 instruments (and CET1 instruments not included in row 5) issued by subsidiaries and held by third parties (amount allowed in group AT1)	11,201	
35.	<i>of which: instruments issued by subsidiaries subject to phase out</i>	-	
36.	<b>Additional Tier 1 capital before regulatory adjustments</b>	-	
<b>Additional Tier 1 capital: regulatory adjustments</b>			
37.	Investments in own Additional Tier 1 instruments	-	
38.	Reciprocal cross-holdings in Additional Tier 1 instruments	-	
39.	Investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions, where the bank does not own more than 10% of the issued common share capital of the entity (amount above 10% threshold)	-	
40.	Significant investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation (net of eligible short positions)	-	
41.	CBB specific regulatory adjustments	-	
42.	Regulatory adjustments applied to Additional Tier 1 due to insufficient Tier 2 to cover deductions	-	
43.	<b>Total regulatory adjustments to Additional Tier 1 capital</b>	-	
44.	<b>Additional Tier 1 capital (AT1)</b>	-	
45.	<b>Tier 1 capital (T1 = CET1 + AT1)</b>	1,143,374	
<b>Tier 2 capital: instruments and provisions</b>			
46.	Directly issued qualifying Tier 2 instruments plus related stock surplus	-	
47.	<i>Directly issued capital instruments subject to phase out from Tier 2</i>	-	
48.	Tier 2 instruments (and CET1 and AT1 instruments not included in rows 5 or 34) issued by subsidiaries and held by third parties (amount allowed in group Tier 2)	14,934	
49.	<i>of which: instruments issued by subsidiaries subject to phase out</i>	-	
50.	Provisions	24,387	A
51.	<b>Tier 2 capital before regulatory adjustments</b>	39,321	
<b>Tier 2 capital: regulatory adjustments</b>			
52.	Investments in own Tier 2 instruments	-	
53.	Reciprocal cross-holdings in Tier 2 instruments	-	
54.	Investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions, where the bank does not own more than 10% of the issued common share capital of the entity (amount above the 10% threshold)	-	
55.	Significant investments in the capital banking, financial and insurance entities that are outside the scope of regulatory consolidation (net of eligible short positions)	-	
56.	National specific regulatory adjustments	-	
57.	<b>Total regulatory adjustments to Tier 2 capital</b>	-	
58.	<b>Tier 2 capital (T2)</b>	39,321	
59.	<b>Total capital (TC = T1 + T2)</b>	1,182,695	
60.	<b>Total risk weighted assets</b>		
<b>Capital ratios and buffers</b>			
61.	Common Equity Tier 1 (as a percentage of risk weighted assets)	13.47%	
62.	Tier 1 (as a percentage of risk weighted assets)	13.60%	
63.	Total capital (as a percentage of risk weighted assets)	14.07%	

64.	Institution specific buffer requirement (minimum CET1 requirement plus capital conservation buffer plus countercyclical buffer requirements plus D-SIB buffer requirement, expressed as a percentage of risk weighted assets)	N/A	
65.	of which: capital conservation buffer requirement	N/A	
66.	of which: bank specific countercyclical buffer requirement	N/A	
67.	of which: D-SIB buffer requirement	N/A	
68.	Common Equity Tier 1 available to meet buffers (as a percentage of risk weighted assets)	13.47%	
<b>National minima including CCB (where different from Basel III)</b>			
69.	CBB Common Equity Tier 1 minimum ratio	9.0%	
70.	CBB Tier 1 minimum ratio	10.5%	
71.	CBB total capital minimum ratio	12.5%	
<b>Amounts below the thresholds for deduction (before risk weighting)</b>			
72.	Non-significant investments in the capital of other financials	18,000	B
73.	Significant investments in the common stock of financials	34,879	C
74.	Mortgage servicing rights (net of related tax liability)	-	
75.	Deferred tax assets arising from temporary differences (net of related tax liability)	-	
76.	Provisions eligible for inclusion in Tier 2 in respect of exposures subject to 10 standardized approach (prior to application of cap)	24,387	A
77.	Cap on inclusion of provisions in Tier 2 under 10 standardized approach	-	
78.	N/A	-	
79.	N/A	-	
<b>Capital instruments subject to phase-out arrangements (only applicable between 1 Jan 2019 and 1 Jan 2023)</b>			
80.	Current cap on CET1 instruments subject to phase out arrangements	NA	
81.	Amount excluded from CET1 due to cap (excess over cap after redemptions and maturities)	NA	
82.	Current cap on AT1 instruments subject to phase out arrangements	NA	
83.	Amount excluded from AT1 due to cap (excess over cap after redemptions and maturities)	NA	
84.	Current cap on T2 instruments subject to phase out arrangements	NA	
85.	Amount excluded from T2 due to cap (excess over cap after redemptions and maturities)	NA	

Disclosure template for main features of regulatory capital instruments		
1	Issuer	GFH Financial Group B.S.C
2	Unique identifier (e.g. CUSIP, ISIN or Bloomberg identifier for private placement)	GFH ( <i>DFM</i> ) GFH ( <i>BHB</i> ) GFH ( <i>KSE</i> )
3	Governing law(s) of the instrument Regulatory treatment	All applicable laws and regulations in the Kingdom of Bahrain.
	<b>Regulatory treatment</b>	
4	Transitional CBB rules	Common Equity Tier 1
5	Post-transitional CBB rules	Common Equity Tier 1
6	Eligible at solo/group/group & solo	Group and solo
7	Instrument type (types to be specified by each jurisdiction)	Common equity shares
8	Amount recognized in regulatory capital (Currency in mil, as of most recent reporting date)	USD 976 million
9	Par value of instrument	USD 0.265
10	Accounting classification	Shareholders' equity
11	Original date of issuance	1999
12	Perpetual or dated	<i>Not applicable</i>
13	Original maturity date	<i>Not applicable</i>
14	Issuer call subject to prior supervisory approval	<i>Not applicable</i>
15	Optional call date, contingent call dates and redemption amount	<i>Not applicable</i>
16	Subsequent call dates, if applicable Coupons / dividends	<i>Not applicable</i>
17	Dividends	Dividends as decided by the shareholders
18	Coupon rate and any related index	<i>Not applicable</i>
19	Existence of a dividend stopper	<i>Not applicable</i>
20	Fully discretionary, partially discretionary or mandatory	Fully discretionary
21	Existence of step up or other incentive to redeem	<i>Not applicable</i>
22	Noncumulative or cumulative	<i>Not applicable</i>
23	Convertible or non-convertible	<i>Not applicable</i>
24	If convertible, conversion trigger (s)	<i>Not applicable</i>
25	If convertible, fully or partially	<i>Not applicable</i>
26	If convertible, conversion rate	<i>Not applicable</i>
27	If convertible, mandatory or optional conversion	<i>Not applicable</i>
28	If convertible, specify instrument type convertible into	<i>Not applicable</i>
29	If convertible, specify issuer of instrument it converts into	<i>Not applicable</i>
30	Write-down feature	<i>Not applicable</i>
31	If write-down, write-down trigger(s)	<i>Not applicable</i>
32	If write-down, full or partial	<i>Not applicable</i>
33	If write-down, permanent or temporary	<i>Not applicable</i>
34	If temporary write-down, description of write-up mechanism	<i>Not applicable</i>
35	Position in subordination hierarchy in liquidation (specify instrument type immediately senior to instrument)	<i>Not applicable</i>
36	Non-compliant transitioned features	<i>Not applicable</i>
37	If yes, specify non-compliant features	<i>Not applicable</i>

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### **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 2019 was as follows:

USD'000	
<b>Total Regulatory Capital</b>	<b>30 June 2019</b>
<b>Common Equity Tier 1 (CET 1)</b>	
Issue and fully paid ordinary shares	975,638
Statutory reserve	117,301
Retained earnings	1,164
Current interim cumulative net profit	49,134
Accumulated other comprehensive income and losses (and other reserves)	(4,443)
<b>Total CET1 capital before minority interest</b>	<b>1,138,794</b>
Total minority interest in banking subsidiaries given recognition in CET1 capital	52,269
<b>Total CET 1 capital prior to regulatory adjustments</b>	<b>1,191,063</b>
Less: Investment in own shares	(58,890)
<b>Total Common Equity Tier 1 (CET1) capital after to the regulatory adjustments</b>	<b>1,132,173</b>
<b>Additional Tier 1 Capital (AT1)</b>	
Instruments issued by banking subsidiaries to third parties	11,201
<b>Total Tier 1 (T1) Capital</b>	<b>1,143,374</b>
Instruments issued by banking subsidiaries to third parties	14,934
Expected Credit Losses (ECL) Stages 1 & 2	24,387
<b>Total Capital (T1 &amp; T2)</b>	<b>1,182,695</b>



USD 000's

<b>Risk weighted exposures</b>	<b>30 June 2019</b>
Credit risk:	
- Self-financed assets	7,821,213
- Assets financed by EIAH (30%)	140,018
Market risk	50,293
Operational risk	392,710
<b>Total Risk weighted exposures</b>	<b>8,404,234</b>
<b>Common Equity Tier 1 (CET1)</b>	<b>13.47%</b>
<b>Tier 1 capital (T1)</b>	<b>13.60%</b>
<b>Total Capital Adequacy ratio (Total Capital)</b>	<b>14.07%</b>

The Bank's paid up capital consists only of one class of shares with 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.



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*Rating of exposures and risk weighting*

The use of external rating by External Credit Assessment Institutions (ECAI) is generally limited to the Bank's exposure to financial institutions and investments in sukuks. For externally rated facilities the Bank uses ratings by Standards & Poor, Moody's, Fitch and Capital Intelligence to derive risk weights for the purpose of capital adequacy computations. For financial institutions, domestic currency ratings are used to assess claims on domestic currency while foreign currency rating is used for foreign currency exposures. A 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.

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

<b>Asset categories for credit risk</b>	<b>Gross credit exposures</b>	<b>Average risk weights</b>	<b>Total credit risk weighted exposure</b>
<b>Self-financed assets</b>			
Cash items	15,479	0%	-
Total claims on sovereigns	205,664	0%	-
Total Claims on PSEs	1,132	0%	-
Standard Risk Weights for Claims on Banks	310,133	20%-100%	240,163
Short-term Claims on locally incorporated Banks – BHD and USD	330,302	20%	66,060
Preferential Risk Weight for Claims on Banks	108,724	20%	21,745
Claims on Corporates including Takaful Companies and Category 3 Investment Firms (Unsecured portion after Credit Risk Mitigant)	828,973	100%-150%	829,448
Past Due Facilities	159,553	100% - 150%	218,165
Investments in Equity Securities	561,877	100% - 800%	1,782,906
Holdings of Real Estate	1,584,873	100% - 400%	4,639,984
Others Assets	22,176	100%	22,176
<b>Total self-financed assets (A)</b>	<b>4,128,886</b>	<b>53%</b>	<b>7,821,213</b>
<b>Total regulatory capital required (A x 12.5%)</b>		<b>12.5%</b>	<b>977,652</b>
<b>Financed by EIAH</b>			
Total claims on sovereigns	439,048	0%	-
Total Claims on PSEs	113,966	20%-100%	34,042
Standard Risk Weights for Claims on Banks	98,931	20% - 100%	44,512
Short-term Claims on locally incorporated Banks – BHD and USD	202,238	20%	40,448
Claims on Corporates including Takaful Companies and Category 3 Investment Firms (Unsecured portion after Credit Risk Mitigant)	347,727	100%	347,727
<b>Total financed by EIAH (B)</b>	<b>1,201,910</b>	<b>38%</b>	<b>466,729</b>
<b>Considered for credit risk (C) = (B x 30%)</b>		<b>30%</b>	<b>140,019</b>
<b>TOTAL REGULATORY CAPITAL REQUIRED (C x 12.5%)</b>		<b>12.5%</b>	<b>17,502</b>
<b>TOTAL GROSS CREDIT EXPOSURES</b>	<b>5,330,796</b>		
<b>TOTAL RISK WEIGHTED EXPOSURE</b>			<b>7,961,232</b>
<b>TOTAL REGULATORY CAPITAL REQUIRED</b>			<b>996,595</b>



## 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*

	Average <sup>[1]</sup> Exposure	Gross Exposure		
		Self – Financed	Financed by EIAH	Total
Cash and bank balances	455,701	163,860	205,691	369,552
Treasury portfolio	1,579,815	192,550	1,489,855	1,682,405
Financing assets	1,286,396	348,701	951,530	1,300,231
Real estate investments	1,823,161	1,821,444	-	1,821,444
Proprietary investments	275,192	279,048	-	279,048
Co-Investments	77,304	77,048	-	77,048
Assets held-for-sale	124,177	101,213	-	101,213
Receivables and prepayments	375,895	482,334	-	482,334
Property, plant and equipment	24,411	24,699	-	24,699
<b>Total funded Credit Exposure</b>	<b>6,022,052</b>	<b>3,490,897</b>	<b>2,647,076</b>	<b>6,137,974</b>
Restricted investment accounts	28,619	28,486	-	28,486
Commitments	60,518	60,518	-	60,518
Financial guarantees	29,258	28,061	-	28,061
Undrawn commitments to extend finance	64,e262	60,518	-	60,518
<b>Total unfunded Credit Exposure</b>	<b>296,931</b>	<b>296,261</b>	<b>-</b>	<b>296,261</b>

[1] 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 2019. 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

	<b>GCC countries</b>	<b>MENA</b>	<b>Asia</b>	<b>Others</b>	<b>Total</b>
<b>Assets</b>					
Cash and bank balances	353,019	616	34	15,883	369,552
Treasury portfolio	1,503,417	-	-	178,988	1,682,405
Financing assets	1,249,857	-	111	50,263	1,300,231
Real estate investments	989,567	462,893	368,984	-	1,821,444
Proprietary investments	278,307	-	-	741	279,048
Co-Investments	1,620	-	57,573	17,855	77,049
Assets held-for-sale	101,213	-	-	-	101,213
Receivables and prepayments	352,566	6,902	22,070	100,796	482,334
Property, plant and equipment	22,570	2,129	-	-	24,699
<b>Total</b>	<b>4,852,136</b>	<b>472,540</b>	<b>448,772</b>	<b>364,526</b>	<b>6,137,974</b>
<b>Off-Balance sheet</b>					
Restricted investment accounts	25,825	-	2,634	-	28,459
Commitments	60,518	-	-	-	60,518
Financial guarantees	20,681	-	-	-	20,681
Undrawn financing facilities	179,196	-	-	-	179,196

\*The geographical exposures of total assets are based on the condensed consolidated interim financial information as at 30 June 2019.

#### 4.2.3 Credit exposure by sector

The classification of credit exposure by industry was as follows:

USD 000's

	<b>Banks and financial institutions</b>	<b>Development Infrastructure</b>	<b>Others</b>	<b>Total</b>
<b>Assets</b>				
Cash and bank balances	260,049	109,284	219	369,552
Treasury portfolio	1,231,644	19,981	430,780	1,682,405
Financing assets	22,798	660,240	617,193	1,300,231
Real estate investments	-	1,821,444	-	1,821,444
Proprietary investments	115,904	97,197	65,947	279,048
Co-Investments	-	77,048	-	77,048
Assets held-for-sale	101,213	-	-	101,213
Receivables and prepayments	16,634	233,482	232,218	482,334
Property, plant and equipment	-	20,007	4,692	24,699
<b>Total</b>	<b>1,748,242</b>	<b>3,038,683</b>	<b>1,351,049</b>	<b>6,137,974</b>
<b>Off-Balance sheet items</b>				
Restricted investment accounts	103	25,722	2,634	28,459
Commitments	-	42,518	18,000	60,518
Financial guarantees	-	7,650	20,411	28,061
Undrawn financing facilities	-	127,082	52,114	179,196

\*The sector exposures of total assets are based on the condensed consolidated interim financial information as at 30 June 2019.

#### 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
<b>Assets</b>							
Bank balances	329,830	8,440	23,963	7,255	-	64	369,552
Treasury portfolio	503,602	183,743	116,090	246,523	632,447	-	1,682,405
Financing assets	187,235	67,151	195,625	487,875	362,345	-	1,300,231
Real estate investments	-	-	-	889,674	931,770	-	1,821,444
Proprietary investments	2,451	-	81,024	112,205	83,368	-	279,048
Co-Investments	2,320	-	-	74,728	-	-	77,048
Assets held-for-sale	-	-	101,213	-	-	-	101,213
Receivables and prepayments	176,724	52,255	66,245	185,899	1,211	-	482,334
Property, plant and equipment	-	-	-	-	24,699	-	24,699
<b>Total assets</b>	<b>1,202,162</b>	<b>311,589</b>	<b>584,160</b>	<b>2,004,159</b>	<b>2,035,840</b>	<b>64</b>	<b>6,137,974</b>
<b>Off-Balance sheet items</b>							
Restricted investment accounts	153	-	-	28,306	-	-	28,459
Commitments	-	2,000	4,000	46,518	8,000	-	60,518
Financial guarantees	28,061	-	-	-	-	-	28,061
Undrawn financing facilities	33,517	23,419	89,934	32,310	16	-	179,196

The table above shows the maturity profile of the Group's assets and unrecognized commitments on the basis of their contractual maturity, where available. For other items, (including past due receivables), the maturity profile is on the basis of their expected realization. The total assets are as per the assets of the condensed consolidated interim financial information.

#### **4.2.5 Exposures in excess of regulatory limits**

The CBB has set single exposure limit of 15% of the Bank’s total capital base on exposures to individual and a combined exposure limit of 25% of total capital base of closely connected counterparties. The excess amount of any exposure above the mentioned thresholds must be risk weighted at 800%, unless it is an exempt exposure in accordance with the requirements of CBB rulebook. With this exemption from Central Bank of Bahrain, there are no combined exposure in excess of the limit of 25% of total capital base of closely connected counterparties.

The Bank's exposure in excess of 15% of the obligor limit to individual counterparties based on regulatory “total available capital” at 30 June 2019 is shown below:

	<b>CAR limits 15% (US\$ 000's)</b>	<b>Exposure (US\$ 000's)</b>	<b>Excess over permissible limit (US\$ 000's)</b>
30 June 2019			
Counterparty A	177,404	318,344	140,940

#### **4.2.6 Impaired facilities and past due exposures**

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. Credit and investment exposures are subject to regular reviews by the Investment units and Risk Management Department. Regular updates on the investments / facilities are prepared by the investment unit reviewed by the management and sent to the Board for review.

*Movement in impairment provisions during the period of Islamic Financing Contracts:*

*USD'000*

<b>30 June 2019</b>	<b>Total</b>	<b>Stage 3</b>	<b>Stage 1 and 2</b>
At 1 January	4,184	4,139	45
Charge for the period	170	-	170
<b>At 30 June</b>	<b>4,354</b>	<b>4,139</b>	<b>215</b>

*Analysis of past due and impaired and past due but not impaired receivables of aging of Islamic Financing Contracts:*

*USD'000*

<b>30 June 2019</b>	<b>Past due but not impaired</b>	<b>Past due and impaired</b>
1 to 3 years	-	9,186

\* 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:*

USD'000

30 June 2019	Gross impaired receivables	Specific Impairment allowance	Net receivables
United Kingdom (UK)	9,186	(4,184)	5,002

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

USD'000

30 June 2019	Gross impaired receivables	Specific Impairment allowance	Net receivables
Other sector	9,186	(4,184)	5,002

#### 4.2.6.1 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 mitigates.

#### 4.2.7 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 2019 were disclosed in note 18 of the condensed consolidated interim financial information.

#### 4.2.8 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.

#### 4.2.9 Restructured facilities

As at 30 June 2019, the Bank does not have any restructured facilities. For the disclosures pertaining to restructured facilities of KHC B, please refer the disclosures of KHC B.

#### 4.2.10 Equity investments held in banking book

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 structured notes, quoted and unquoted equity securities and significant investments in commercial entities.

The Risk Management Department 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 Risk Management Department. 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.

<b>Information on equity investments (including significant commercial entities)</b>	USD 000's
Privately held	776,714
Quoted in an active market	26,511
Managed funds	-
Dividend income	3,858
Realised gain/ (loss) during the period	494
Unrealised gain recognized in the balance sheet not through income statement	-



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

USD 000's

	Gross exposure*	Risk weight	Risk weighted exposure	Capital charge @12.5%
Listed equity investments	26,407	100%	26,407	3,301
Unlisted equity investments	344,065	150%	516,098	64,512
Significant investment in the common shares of financial entities >10%	52,879	250%	132,198	16,525
Other investment with excess amount over 15% of total capital	138,525	800%	1,108,204	138,525
All other holdings of real estate	822,985	200%	1,645,969	205,746
Investments in listed real estate companies	103	300%	309	39
Investment in unlisted real estate companies	743,973	400%	2,975,894	371,987
<b>Total</b>	<b>2,128,937</b>		<b>6,405,891</b>	<b>800,635</b>

\*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.

USD 000's

	30 June 2019	Maximum during the period	Minimum during the period
Foreign exchange risk – A	4,023	4,023	2,814
Risk weighted assets – B (A*12.5)	50,293	50,293	35,173
Capital requirement – (B*12.5%)	6,287	6,287	4,397

## 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 three 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.

USD 000's

	<b>Average gross income</b>	<b>Risk weighted assets</b>	<b>Capital charge at 12%</b>
Operational risk	209,445	392,710	49,089

### **Litigations, claims and contingencies**

The Group has certain claims and litigations filed against it in connection with projects promoted by the Bank in the past and with certain transactions. Based on the advice of the Bank's external legal counsel, the management is of the opinion that the Bank has strong grounds to successfully defend itself against these claims. Appropriate provision have been made in the books of accounts. No further disclosures regarding contingent liabilities arising from any 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

### 7.1 Liquidity risk

Liquidity risk is the inability of the Bank to fund increases in assets and meet obligations as they come due, without incurring unacceptable losses. This also includes the inability of the Bank to liquidate its assets at their expected prices in a reasonable period. The Group's approach to managing liquidity is to ensure that it should 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.

The Bank has a liquidity risk policy in place, which describes the roles and responsibilities of various committees, Treasury and other concerned departments in management of liquidity. It also stipulates various liquidity ratios to be maintained by the Bank, as well as gap limits for time bucket of the maturity ladder.

The liquidity position is closely monitored and stressed to cover both normal and more severe market conditions. Daily reports cover the liquidity position of the Bank. Moreover, periodic reports are submitted to the Asset and Liability Management Committee of the Bank (ALCO) Audit & Risk Committee (ARC) and to the Board of Directors for review and strategic direction.

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

Liquidity ratios	30 June 2019	Maximum	Minimum
Liquid assets : Total assets	30.94%	30.94%	25.67%
Liquid assets : Total deposits	47.36%	47.36%	30.81%
Short term assets : Short term liabilities*	38.58%	59.04%	38.58%
Illiquid assets : Total assets	69.06%	74.33%	69.06%

\* Based on maturity profile of assets and liabilities of one year or less of the Group.

The maturity profile of the Group's financial liabilities based on contractual cash flows are as follows:  
 USD 000's

	<b>Up to 3 months</b>	<b>3 to 6 months</b>	<b>6 months-1 year</b>	<b>1 to 3 years</b>	<b>Over 3 years</b>	<b>Total</b>
<b>30 June 2019</b>						
Clients' funds	46,421	-	-	14,676	-	61,097
Placements from financial, non-financial and other individual Customer current accounts	1,264,836	619,865	653,768	240,095	11,193	2,789,757
Term financing	43,646	16,867	18,318	20,934	63,918	163,683
Liabilities directly related to assets held-for-sales	128,784	17,435	10,208	31,226	12,307	199,960
Other liabilities	-	-	39,936	-	-	39,936
	34,421	19,500	47,408	406,604	-	507,933
<b>Total liabilities</b>	<b>1,518,108</b>	<b>673,667</b>	<b>769,638</b>	<b>713,535</b>	<b>87,418</b>	<b>3,762,366</b>
<b>Equity of investment account holders</b>	<b>60,276</b>	<b>188,369</b>	<b>305,560</b>	<b>211,523</b>	<b>230,109</b>	<b>995,837</b>

## 7.2 Management of profit rate risk in the banking book

Profit rate risk is the potential impact of the mismatch between the reset of rate of return on assets and the rate of return of the sources of funding. The Board of Directors is responsible for the overall management of the profit rate risk. The ALCO helps the Board in determining the borrowing and funding strategy of the Bank in order to optimize risk return trade off. It supports the Board in managing profit rate risk by recommending policies, setting limits and guidelines and monitoring the risk on a regular basis.

The following disclosures are of the Group.

	US\$ 000's					
	Up to 3 months	3 to 6 months	6 months - 1 year	1 to 3 years	Over 3 years	Total
<b>30 June 2019</b>						
<b>Assets</b>						
Treasury portfolio	419,484	177,340	104,669	169,477	632,447	1,503,416
Financing assets	187,235	67,151	195,625	487,875	362,345	1,300,231
<b>Total assets</b>	<b>606,719</b>	<b>244,491</b>	<b>300,294</b>	<b>657,352</b>	<b>994,792</b>	<b>2,803,648</b>
<b>Liabilities</b>						
Clients' funds	46,421	-	-	14,676	-	61,097
Placements from financial, non-financial and other individual	1,264,836	619,865	653,768	240,095	11,193	2,789,757
Customer current accounts	43,646	16,867	18,318	20,934	63,918	163,683
Term financing	128,784	17,435	10,208	31,226	12,307	199,960
<b>Total liabilities</b>	<b>1,483,687</b>	<b>654,167</b>	<b>682,294</b>	<b>306,931</b>	<b>87,418</b>	<b>1,885,768</b>
<b>Equity of investment account holders</b>	<b>60,276</b>	<b>188,369</b>	<b>305,560</b>	<b>211,523</b>	<b>230,109</b>	<b>995,837</b>
<b>Profit rate sensitivity gap</b>	<b>(937,244)</b>	<b>(598,045)</b>	<b>(687,560)</b>	<b>138,898</b>	<b>677,265</b>	<b>(1,406,686)</b>

The management of profit rate risk against profit rate gap limits is supplemented by monitoring the sensitivity of the Group's financial assets and liabilities to various standard and non-standard profit rate scenarios. Standard scenarios that are considered 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)

	USD'000
<b>200 bps parallel increase / (decrease)</b>	<b>2019</b>
At 30 June 2019	± 14,067
Average for the period	± 13,564
Maximum for the period	± 14,067
Minimum for the period	± 13,564

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### **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. 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 2019, 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.

### **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

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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.

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:

	<i>USD 000's</i>	
	<b>30 June 2019</b>	<b>31 Dec 2018</b>
Total EIAH as at 30 June / 31 December	591	590
Average EIAH balance	591	924
Average rate of return earned (%)	0.24%	1.10%
Total profits on EIAH assets earned	1	10
Distributed to investor	1	10
Allocated to IRR	0.1	0.2
Allocated to PER	0.1	0.3
Bank's share of profits	0.1	0.5
Average declared rate of return (%)	0.24%	1.10%

*The information disclosed above pertains to EIAH directly promoted by the Bank. For the qualitative disclosures pertaining to EIAH of KHCB, please refer the disclosures of KHCB.*

## **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;



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- 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 Bank do not have significant exposures through restricted investment accounts on solo basis and there were no annual distributions made by the Bank for RIA for the past five years.

For the qualitative and quantitative disclosures pertaining to RIA's of KHCB, please refer the financial disclosures of KHCB.

## **9 Penalties**

During the period, financial penalties amounting Bahraini Dinar ("BHD") 1,600 was imposed by the Central Bank of Bahrain, due to delay in submission of invitation to CBB for the Bank's ordinary general assembly meeting.