ALUBAF Arab International Bank B.S.C. (c)

FINANCIAL STATEMENTS,
REPORT OF THE BOARD OF DIRECTORS
AND INDEPENDENT AUDITORS' REPORT

31 DECEMBER 2014

BOARD OF DIRECTORS' REPORT

Members of the General assembly of the Alubaf Arab International Bank, Bahrain:

On behalf of the Board of Directors and for myself, it is my honour to present the Annual report and audited financial statements for the year ended 31 December 2014.

The Middle East and African Region witnessed continued geo- political events in 2014, and the banking industry was not spared from being impacted. However, Alubaf was able to face these continued new challenges and achieved remarkable financial results in 2014.

The Bank posted a strong growth of 11.1% over last year's results and achieved a Net profit of US$ 40.7 million for the year ended 31 December 2014. Overall operating income before provisions stood at US$ 61.9 million, an increase of 20.6% over last year's US$ 51.4 million. However, the Bank increased its provisioning this year to keep pace with the loans portfolio growth and improved its provision coverage ratio to 97% as a prudential measure. After deduction of provisions, the net operating income stood at US$ 54.1 million for the year ended 31 December 2014, as compared to last year's US$ 47.3 million.

Operating expenses increased to 24.9% of the net operating income compared to last year's 22.7%. This is mainly due to increase in staff costs and other operating expenses, to align with increased business activity and to optimize operational efficiency. However, overall cost to income ratio, remained at a reasonable level of 25%. Capital adequacy ratio at 42.19%, reflects its capital strength. Liquidity ratio remained comfortable. Growth in total assets was 8.8% , loans portfolio grew by 33.7% and Non trading investments by 7.8% compared to previous year 2013. Change in product mix was healthy and contributed to a balanced risk-return yield levels.

Alubaf Tower, Al-Seef District,
P.O. Box: 11529, Kingdom of Bahrain
Swift: ALUBBHBM, C.R. 12819
T. +973 17 517722, F. +973 17 540094
Email:info@alubafbank.com, www.alubafbank.com
Authorised capital: US$ 500 million, Paid up capital: US$ 250 Million
Licensed as a Conventional Wholesale Bank by the CBB

برج اليوباف، ضاحية السيف
ص.ب: ١١٥٢٩، مملكة البحرين
س.ت: ١٢٨١٩ ,Swift: ALUBBHBM
تلفون: ٧٢٢ ٥١٧ ١٧ ٩٧٣+
فاكس: ٥٤٠٠٩٤ ١٧ ٩٧٣+

The Board continued with its strategic focus on growth in delivering increasing return to shareholders. The Board and management's adaptation to complex economic scenario has positioned the Bank in strategic growth path. Return on average equity improved to a new level of 13% for the year ended 31 December 2014. The Board seeks to ensure that the Bank's return to shareholders improves over long term.

Looking ahead, we expect to strengthen our competitive position and add value to shareholders, provide state of the art service to our customers, reward management and staff for their valuable contribution and be fully compliant with all regulatory requirements. We are confident that Alubaf is well positioned to seize right growth opportunities and strengthen its drive to increase shareholder value.

Finally, I would like to thank all members of the Board, the shareholders, the Ministry of Industry and Commerce in the Kingdom of Bahrain, the Central Bank of Bahrain and all correspondent banks and our customers for their continued support.

I also extend my appreciation and thanks to all the employees for their dedication and commitment in achieving remarkable results.

Moraja G. Solaiman
Chairman

Alubaf Tower, Al-Seef District,
P.O. Box: 11529, Kingdom of Bahrain
Swift: ALUBBHBM, C.R. 12819
T. +973 17 517722, F. +973 17 540094
Email:info@alubafbank.com, www.alubafbank.com
Authorised capital: US$ 500 million, Paid up capital: US$ 250 Million
Licensed as a Conventional Wholesale Bank by the CBB

برج اليوباف، ضاحية السيف
ص.ب: ١١٥٢٩، مملكة البحرين
Swift: ALUBBHBM، س.ت: ١٢٨١٩
تليفون: ٩٧٣١٧٥١٧٧٢٢+
فاكس: ٩٧٣١٧٥٤٠٠٩٤+

Building a better working world

Ernst & Young
P.O. Box 140
14th Floor, South Tower
Bahrain World Trade Center
Manama
Kingdom of Bahrain

Tel: +973 1753 5455
Fax: +973 1753 5405
manama@bh.ey.com
ey.com/mena
C.R. No. 6700

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF ALUBAF ARAB INTERNATIONAL BANK B.S.C. (c)

Report on the financial statements

We have audited the accompanying financial statements of Alubaf Arab International Bank B.S.C. (c) ('the Bank'), which comprise the statement of financial position as at 31 December 2014 and the statements of profit or loss, comprehensive income, cash flows and changes in equity for the year then ended, and a summary of significant accounting policies and other explanatory information.

Board of Directors' responsibility for the financial statements

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

Auditors' responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the Board of Directors, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Bank as of 31 December 2014, its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Building a better working world

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF ALUBAF ARAB INTERNATIONAL BANK B.S.C. (c) (continued)

Report on other regulatory matters

As required by the Bahrain Commercial Companies Law and the Central Bank of Bahrain (the CBB) Rule Book (Volume 1), we report that:

a) the Bank has maintained proper accounting records and the financial statements are in agreement therewith; and

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

We are not aware of any violations of the Bahrain Commercial Companies Law, the Central Bank of Bahrain and Financial Institutions Law, the CBB Rule Book (Volume 1 and applicable provisions of Volume 6) and CBB directives, or the terms of the Bank's memorandum and articles of association during the year ended 31 December 2014 that might have had a material adverse effect on the business of the Bank or on its financial position. Satisfactory explanations and information have been provided to us by management in response to all our requests.

Ernst + Young

Partner Registration Number: 115
16 February 2015
Manama, Kingdom of Bahrain

STATEMENT OF FINANCIAL POSITION

As at 31 December 2014

	Note	*2014 US$ '000*	*2013 US$ '000*
ASSETS			
Cash and balances with banks	4	22,507	150,345
Deposits with banks and other financial institutions	4,5	523,645	422,005
Investments held for trading	6	3,037	14,626
Non-trading investments	7	147,994	137,282
Loans and advances	8	485,255	362,998
Property, equipment and software	9	12,320	13,366
Interest receivable		8,922	5,916
Other assets		1,277	1,224
TOTAL ASSETS		1,204,957	1,107,762
LIABILITIES AND EQUITY			
Liabilities			
Deposits from banks and other financial institutions	10	616,319	501,186
Due to banks and other financial institutions	10	219,636	268,273
Due to customers	11	25,151	7,714
Interest payable		189	205
Other liabilities	12	11,750	14,283
Total liabilities		873,045	791,661
Equity			
Share capital	13	250,000	250,000
Advance towards capital increase	13	140	-
Statutory reserve	13	17,667	13,597
Retained earnings		65,272	28,642
Fair value reserve		(1,167)	(1,138)
Proposed dividend	14	-	25,000
Total equity		331,912	316,101
TOTAL LIABILITIES AND EQUITY		1,204,957	1,107,762

Hasan Khalifa Abulhasan
Chief Executive Officer

Ali Makhzum Ben Hamza
Director

Suleiman Esa Al Azzabi
Deputy Chairman

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

STATEMENT OF PROFIT OR LOSS

For the year ended 31 December 2014

	Note	*2014* *US$ '000*	*2013* *US$ '000*
Interest and similar income	15	**45,561**	34,627
Interest expense	16	**(1,476)**	(1,860)
Net interest income		**44,085**	32,767
Fee and commission income	17	**16,436**	17,874
Trading income	18	**505**	(1,027)
Gain on non-trading investments - net		**332**	953
Foreign exchange gain		**551**	823
Dividend income		**75**	18
OPERATING INCOME		**61,984**	51,408
Provision for impairment of loans and advances	8	**(7,817)**	(4,017)
NET OPERATING INCOME		**54,167**	47,391
Staff costs		**8,142**	6,253
Depreciation	9	**1,233**	1,078
Other operating expenses	19	**4,092**	3,420
OPERATING EXPENSES		**13,467**	10,751
NET PROFIT FOR THE YEAR		**40,700**	36,640

Hasan Khalifa Abulhasan
Chief Executive Officer

Ali Makhzum Ben Hamza
Director

Suleiman Esa Al Azzabi
Deputy Chairman

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

STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2014

	2014 *US$ '000*	*2013* *US$ '000*
NET PROFIT FOR THE YEAR	**40,700**	36,640
Other comprehensive income		
Other comprehensive income to be reclassified to profit or loss in subsequent periods:		
Unrealised fair value loss on available-for-sale investments - net	**(29)**	(1,138)
Net other comprehensive income to be reclassified to profit or loss in subsequent periods	**(29)**	(1,138)
Other comprehensive income for the year	**(29)**	(1,138)
TOTAL COMPREHENSIVE INCOME FOR THE YEAR	**40,671**	35,502

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

STATEMENT OF CASH FLOWS

For the year ended 31 December 2014

	Note	*2014* *US$ '000*	*2013* *US$ '000*
OPERATING ACTIVITIES			
Net profit for the year		**40,700**	36,640
Adjustments for:			
Provision for loan losses	8	**7,817**	4,017
Depreciation	9	**1,233**	1,078
Changes in fair value of investments held for trading	18	**(17)**	540
Net gain on non-trading investments		**(332)**	(953)
Amortisation of non-trading investments		**767**	542
Amortisation of assets reclassified as "loans and advances" from trading investments		**(603)**	(554)
Operating profit before changes in operating assets and liabilities		**49,565**	41,310
Changes in operating assets and liabilities:			
Deposits with banks and other financial institutions		**41,015**	(188,910)
Loans and advances		**(129,471)**	12,223
Investments held for trading		**11,606**	(16,095)
Interest receivable		**(3,006)**	2,118
Other assets		**(53)**	(729)
Deposits from banks and other financial institutions		**115,133**	(17,831)
Due to banks and other financial institutions		**(48,637)**	1,210
Due to customers		**17,437**	(13,369)
Interest payable		**(16)**	36
Other liabilities		**(2,533)**	10,115
Net cash from (used in) operating activities		**51,040**	(169,922)
INVESTING ACTIVITIES			
Purchase of non-trading investments		**(28,943)**	(109,112)
Proceeds from disposal of non-trading investments		**17,767**	10,946
Purchase of property, equipment and software	9	**(187)**	(478)
Net cash used in investing activities		**(11,363)**	(98,644)
FINANCING ACTIVITIES			
Advance towards capital increase	13	**140**	-
Dividends paid	14	**(25,000)**	(20,000)
Net cash used in financing activities		**(24,860)**	(20,000)
INCREASE / (DECREASE) IN CASH AND CASH EQUIVALENTS		**14,817**	(288,566)
Cash and cash equivalents at 1 January		**373,440**	662,006
CASH AND CASH EQUIVALENTS AT 31 DECEMBER	4	**388,257**	373,440

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

STATEMENT OF CHANGES IN EQUITY
For the year ended 31 December 2014

	Note	Share capital US$ '000	Advance towards capital increase US$ '000	Statutory reserve US$ '000	Retained earnings US$ '000	Fair value reserve US$'000	Proposed dividend US$ '000	Total US$ '000
Balance as of 1 January 2014		250,000	-	13,597	28,642	(1,138)	25,000	316,101
Advance towards capital increase	13	-	140	-	-	-	-	140
Net profit for the year		-	-	-	40,700	-	-	40,700
Other comprehensive income		-	-	-	-	(29)	-	(29)
Total comprehensive income for the year		-	-	-	40,700	(29)	-	40,671
Dividends paid for 2013	14	-	-	-	-	-	(25,000)	(25,000)
Transfer to statutory reserve	13	-	-	4,070	(4,070)	-	-	-
Balance as of 31 December 2014		**250,000**	**140**	**17,667**	**65,272**	**(1,167)**	**-**	**331,912**
Balance as of 1 January 2013		250,000	-	9,933	20,666	-	20,000	300,599
Net profit for the year		-	-	-	36,640	-	-	36,640
Other comprehensive income		-	-	-	-	(1,138)	-	(1,138)
Total comprehensive income for the year		-	-	-	36,640	(1,138)	-	35,502
Dividends paid for 2012	14	-	-	-	-	-	(20,000)	(20,000)
Transfer to statutory reserve	13	-	-	3,664	(3,664)	-	-	-
Proposed dividend	14	-	-	-	(25,000)	-	25,000	-
Balance as of 31 December 2013		250,000	-	13,597	28,642	(1,138)	25,000	316,101

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

1 ACTIVITIES

ALUBAF Arab International Bank B.S.C. (c) (the "Bank") is a closed Bahraini joint stock company incorporated in the Kingdom of Bahrain and registered with the Ministry of Industry and Commerce under Commercial Registration (CR) number 12819. The Bank operates under a wholesale banking license issued by the Central Bank of Bahrain (the "CBB") under the new integrated licensing framework. The Bank's registered office is at Building 854, Road 3618, Avenue 436, Alubaf Tower, Al-Seef District, PO Box 11529, Manama, Kingdom of Bahrain.

The Bank is majority owned by Libyan Foreign Bank, a bank registered in Libya (refer note 13 for more details).

The financial statements of the Bank for the year ended 31 December 2014 were authorised for issue in accordance with a resolution of the Board of Directors on 16 February 2015.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES

2.1 Basis of preparation

The financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") and are in conformity with the Bahrain Commercial Companies Law ("BCCL") the Central Bank of Bahrain ("CBB") and Financial Institutions Law, the CBB Rule Book (Volume 1 and applicable provisions of Volume 6) and the relevant CBB directives.

Basis of measurement

The financial statements have been prepared on a historical cost basis, except for derivative financial instruments, trading investments and available-for-sale (AFS) financial assets that have been measured at fair value.

Functional and presentation currency

The financial statements are presented in United States Dollars (US$), being the Bank's functional currency, and all value are rounded to the nearest thousand (US$ '000), except when otherwise indicated.

The financial statements provide comparative information in respect of the previous period.

2.2 Summary of significant accounting policies

Financial instruments – initial recognition and subsequent measurement

A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity.

Financial assets and financial liabilities

Financial assets of the Bank comprise cash and balances with banks, deposits with banks and other financial institutions, investments held for trading, non-trading investments, loans and advances, interest receivable and other assets. Financial liabilities of the Bank comprise deposits from banks and other financial institutions, due to banks and other financial institutions, due to customers, interest payable and other liabilities.

The specific accounting policies relating to various financial assets and liabilities are set out below:

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

2.2 Summary of significant accounting policies (continued)

Financial assets and financial liabilities (continued)

i) Financial assets

Initial recognition and measurement
Financial assets are classified, at initial recognition, as financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, available for sale financial assets, or as derivative instruments, as appropriate. All financial assets are recognised initially at fair value plus, in the case of financial assets not recorded at fair value through profit or loss, transaction costs that are attributable to the acquisition of the financial asset.

Purchases or sales of financial assets that require delivery of assets within a time frame established by regulation or convention in the market place (regular way trades) are recognised on the trade date, i.e., the date that the Bank commits to purchase or sell the asset.

Subsequent measurement
For purposes of subsequent measurement financial assets are classified in four categories:

- At fair value through profit or loss
- Loans and receivables
- Held-to-maturity
- Available for sale

a) Financial assets at fair value through profit or loss
Financial assets at fair value through profit or loss include financial assets held for trading. Financial assets are classified as held for trading if they are acquired for the purpose of selling or repurchasing in the near term. These are subsequently measured at fair value with any realised and unrealised gains and losses arising from changes in fair values being included in the statement of profit or loss in the period in which they arise. Interest earned and dividends received in respect of financial assets at fair value through profit or loss are included in 'interest and similar income' and 'dividend income' respectively.

b) Loans and receivables
Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement, such financial assets are subsequently measured at amortised cost using the effective interest rate (EIR) method, less impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the EIR. The EIR amortisation is included in 'interest and similar income' in the statement of profit or loss. The losses arising from impairment of loans and receivables are recognised in the statement of profit or loss.

c) Held-to-maturity
Non-derivative financial assets with fixed or determinable payments and fixed maturities are classified as held-to-maturity when the Bank has the positive intention and ability to hold them to maturity. After initial measurement, held-to-maturity financial assets are measured at amortised cost using the EIR, less impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the EIR. The EIR amortisation is included as 'interest and similar income' in the statement of profit or loss. The losses arising from impairment are recognised in the statement of profit or loss.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

2.2 Summary of significant accounting policies (continued)

Financial assets and financial liabilities (continued)

i) Financial assets (continued)

d) Available-for-sale
Available-for-sale financial assets include equity investments and debt securities. Equity investments classified as available-for-sale are those that are neither classified as held for trading nor designated at fair value through profit or loss. Debt securities in this category are those that are intended to be held for an indefinite period of time and that may be sold in response to needs for liquidity or in response to changes in the market conditions.

After initial measurement, available-for-sale financial assets are subsequently measured at fair value with unrealised gains or losses recognised in other comprehensive income and credited in the fair value reserve until the investment is derecognised, at which time the cumulative gain or loss is recognised in other operating income, or the investment is determined to be impaired, when the cumulative loss is reclassified from the fair value reserve to the statement of profit or loss.

The Bank evaluates whether the ability and intention to sell its available-for-sale financial assets in the near term is still appropriate. When, in rare circumstances, the Bank is unable to trade these financial assets due to inactive markets, the Bank may elect to reclassify these financial assets if the management has the ability and intention to hold the assets for foreseeable future or until maturity.

For a financial asset reclassified from the available-for-sale category, the carrying amount at the date of reclassification becomes its new amortised cost and any previous gain or loss on the asset that has been recognised in equity is amortised to profit or loss over the remaining life of the investment using the EIR. Any difference between the new amortised cost and the maturity amount is also amortised over the remaining life of the asset using the EIR. If the asset is subsequently determined to be impaired, then the amount recorded in equity is reclassified to the statement of profit or loss.

Derecognition
A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is primarily derecognised (i.e., removed from the Bank's statement of financial position) when:

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

When the Bank has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, it evaluates if and to what extent it has retained the risks and rewards of ownership. When it has neither transferred nor retained substantially all of the risks and rewards of the asset, nor transferred control of the asset, the Bank continues to recognise the transferred asset to the extent of the Bank's continuing involvement. In that case, the Bank also recognises an associated liability. The transferred asset and the associated liability are measured on a basis that reflects the rights and obligations that the Bank has retained.

Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Bank could be required to repay.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

2.2 Summary of significant accounting policies (continued)

i) Financial assets (continued)

Impairment of financial assets
The Bank assesses, at each reporting date, whether there is objective evidence that a financial asset or a group of financial assets is impaired. An impairment exists if one or more events that has occurred since the initial recognition of the asset (an incurred 'loss event'), has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that the debtors or a group of debtors is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganisation and observable data indicating that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

The impairement assessment of different categories of financial assets are discussed below:

a) Financial assets carried at amortised cost
For financial assets carried at amortised cost, the Bank first assesses individually whether objective evidence of impairment exists for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If the Bank determines that no objective evidence of impairment exists for an individually assessed financial asset, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognised are not included in a collective assessment of impairment.

The amount of any impairment loss identified is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not yet been incurred). The present value of the estimated future cash flows is discounted at the financial asset's original effective interest rate.

The carrying amount of the asset is reduced through the use of an allowance account and the loss is recognised in the statement of profit or loss. Interest income continues to be accrued on the reduced carrying amount and is accrued using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. Financial assets carried at amortised cost, together with the associated allowance are written off when there is no realistic prospect of future recovery and all collateral has been realised or has been transferred to the Bank. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognised, the previously recognised impairment loss is increased or reduced by adjusting the allowance account. If a write-off is later recovered, the recovery is credited in the statement of profit or loss.

b) Available-for-sale
For available-for-sale financial assets, the Bank assesses at each reporting date whether there is objective evidence that an investment or a group of investments is impaired.

In the case of equity investments classified as available-for-sale, objective evidence would include a significant or prolonged decline in the fair value of the investment below its cost. 'Significant' is evaluated against the original cost of the investment and 'prolonged' against the period in which the fair value has been below its original cost. When there is evidence of impairment, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognised in the statement of profit or loss – is removed from other comprehensive income and recognised in the statement of profit or loss. Impairment losses on equity investments are not reversed through profit or loss; increases in their fair value after impairment are recognised in other comprehensive income.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

2.2 Summary of significant accounting policies (continued)

i) Financial assets (continued)

Impairment of financial assets (continued)

b) Available-for-sale (continued)
The determination of what is 'significant' or 'prolonged' requires judgement. In making this judgement, the Bank evaluates, among other factors, the duration or extent to which the fair value of an investment is less than its cost.

In the case of debt instruments classified as available-for-sale, the impairment is assessed based on the same criteria as financial assets carried at amortised cost. However, the amount recorded for impairment is the cumulative loss measured as the difference between the amortised cost and the current fair value, less any impairment loss on that investment previously recognised in the statement of profit or loss.

Future interest income continues to be accrued based on the reduced carrying amount of the asset, using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. If, in a subsequent year, the fair value of a debt instrument increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in the statement of profit or loss, the impairment loss is reversed through the statement of profit or loss.

ii) Financial liabilities
All financial liabilities are recognised initially at fair value.

Subsequent measurement
After initial recognition, are subsequently measured at amortised cost using the EIR method.

Amortised cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the EIR. The EIR amortisation is included as finance costs in the statement of profit or loss.

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

iii) Offsetting of financial instruments
Financial assets and financial liabilities are offset and the net amount is reported in the statement of financial position if there is a currently enforceable legal right to offset the recognised amounts and there is an intention to settle on a net basis, to realise the assets and settle the liabilities simultaneously.

Derivative financial instruments
The Bank makes use of derivative instruments, such as forward foreign exchange contracts.

Derivatives are initially recognised, and subsequently measured at fair value with transaction costs taken directly to the statement of profit or loss. The fair value of a derivative is the equivalent of the unrealised gain or loss from marking to market the derivative. Derivatives with positive fair values (unrealised gains) are included in other assets and derivatives with negative fair values (unrealised losses) are included in other liabilities in the statement of financial position.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

2.2 Summary of significant accounting policies (continued)

Cash and cash equivalents
For the purpose of the statement of cash flows, cash and cash equivalents comprise cash and balances with banks and deposits with banks and other financial institutions with original maturities of 90 days or less.

Property, equipment and software
Property, equipment and software are stated at cost, net of accumulated depreciation and accumulated impairment losses, if any. Expenditure incurred to replace a component of an item of property, equipment and software that is accounted for separately is capitalised and the carrying amount of the component that is replaced is written off. When significant parts of property, equipment and software are required to be replaced at intervals, the Bank depreciates them separately based on their specific useful lives. Land is not depreciated. Repair and maintenance costs are recognised in profit or loss as incurred.

Depreciation is calculated on a straight-line basis over the estimated useful lives of the assets, as follows:

Assets	*Estimated useful life in years*
Building	15
Furniture, equipment and vehicles	3 to 5
Software	3 to 5

An item of property and equipment and any significant part initially recognised is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the statement of profit or loss when the asset is derecognised.

The residual values, useful lives and methods of depreciation of property, equipment and software are reviewed at each financial year end and adjusted prospectively, if appropriate.

Impairment of non-financial assets
The Bank assesses at each reporting date whether there is an indication that an asset may be impaired. If any indication exists, or when annual impairment testing for an asset is required, the Bank estimates the asset's recoverable amount. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount, with the difference being recognised as an impairment in the statement of profit or loss.

Renegotiated loans
In the ordinary course of its business, the Bank seeks to restructure loans. This may involve extending the payment arrangements and the agreement of new loan conditions. Once the terms have been renegotiated, any impairment is measured using the original effective interest rate as calculated before the modification of terms and the loan is no longer considered past due. Management continually reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur. The loans continue to be subject to an individual or collective impairment assessment, calculated using the loan's original effective interest rate.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

2.2 Summary of significant accounting policies (continued)

Financial guarantees
In the ordinary course of business, the Bank gives financial guarantees, consisting of letters of credit and guarantees.

Financial guarantees are initially recognised in the financial statements at fair value, being the commission received. Subsequent to initial recognition, the Bank's liability under each guarantee is measured at the higher of the un-amortised commission and the best estimate of expenditure required to settle any financial obligation arising as a result of the guarantee.

Provisions
Provisions are recognised when the Bank has a present obligation (legal or constructive) as a result of a past event and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. The expense relating to a provision is presented in the statement of profit or loss net of any reimbursement.

If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects, when appropriate, the risks specific to the liability. When discounting is used, the increase in the provision due to the passage of time is recognised in the statement of profit or loss.

Employees' end of service benefits
Costs relating to employees' end of service benefits are accrued in accordance with actuarial and other valuations as required by regulations applicable in the Kingdom of Bahrain. The Bank makes contributions to Social Insurance Organisation calculated as a percentage of employees' salaries. The Bank's obligations are limited to these contributions, which are expensed when due.

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

Share capital and statutory reserve

Share capital
Ordinary shares issued by the Bank are classified as equity. The Bank classifies capital instruments as financial liabilities or equity instruments in accordance with the substance of the contractual terms of the instruments. Incremental costs directly attributable to the issue of an equity instrument are deducted from the initial measurement of the equity instruments.

Statutory reserve
The Bahrain Commercial Companies Law 2001 requires that 10% of the annual profit be appropriated to a statutory reserve which is normally distributable only on dissolution. Appropriations may cease when the reserve reaches 50% of the paid up share capital.

Dividend
The Bank recognises a liability to make cash or non-cash distributions to equity holders when the distribution is authorised and the distribution is no longer at the discretion of the Bank. As per the corporate laws in the Kingdom of Bahrain, a distribution is authorised when it is approved by the shareholders. A corresponding amount is recognised directly in equity.

Fair value measurement
The Bank measures financial instruments, such as investments and derivatives at fair value at each balance sheet date. Fair value related disclosures for financial instruments and non-financial assets that are measured at fair value or where fair values are disclosed, are disclosed in note 21.5.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

2.2 Summary of significant accounting policies (continued)

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

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

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

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

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

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

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

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

For the purpose of fair value disclosures, the Bank has determined classes of assets and liabilities on the basis of the nature, characteristics and risks of the asset or liability and the level of the fair value hierarchy as explained above.

Revenue recognition
Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Bank and the revenue can be reliably measured, regardless of when the payment is being made. Revenue is measured at the fair value of the consideration received or receivable, taking into account contractually defined terms of payment. The following specific recognition criteria must also be met before revenue is recognised:

Interest income
For all financial instruments measured at amortised cost and interest-bearing financial assets classified as available-for-sale, interest income is recorded using the effective interest rate (EIR). EIR is the rate that exactly discounts the estimated future cash payments or receipts over the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or liability. The recognition of interest income is suspended when the loans become impaired, such as when overdue by more than 90 days.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

2.2 Summary of significant accounting policies (continued)

Revenue recognition (continued)

Fee and commission income
Fee and commission income are recognised when earned.

Dividend income
Dividend income is recognised when the Bank's right to receive the payment is established, which is generally when shareholders approve the dividend.

Foreign currencies
The Bank's financial statements are presented in United States Dollars (US$), which is the Bank's functional currency.

Transactions in foreign currencies are initially recorded at the rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated at the functional currency spot rates of exchange at the reporting date. Differences arising on settlement or translation of monetary items are recognised in profit or loss.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value is determined. The gain or loss arising on translation of non-monetary items measured at fair value is treated in line with the recognition of the gain or loss on the change in fair value of the item (i.e., translation differences on items whose fair value gain or loss is recognised in other comprehensive income (OCI) or profit or loss are recognised in OCI or profit or loss, respectively).

2.3 Changes in accounting policies and disclosures

i) New and amended standards and interpretations
The below new standards and amendments apply for the first time for annual periods beginning on or after 1 January 2014. However, they did not impact the annual financial statements of the Bank.

Investment Entities (Amendments to IFRS 10, IFRS 12 and IAS 27)
These amendments provide an exception to the consolidation requirement for entities that meet the definition of an investment entity under IFRS 10 Consolidated Financial Statements and must be applied retrospectively, subject to certain transition relief. The exception to consolidation requires investment entities to account for subsidiaries at fair value through profit or loss.

Offsetting Financial Assets and Financial Liabilities - Amendments to IAS 32
These amendments clarify the meaning of 'currently has a legally enforceable right to set-off' and the criteria for non-simultaneous settlement mechanisms of clearing houses to qualify for offsetting and is applied retrospectively.

Novation of Derivatives and Continuation of Hedge Accounting – Amendments to IAS 39
These amendments provide relief from discontinuing hedge accounting when novation of a derivative designated as a hedging instrument meets certain criteria and retrospective application is required. These amendments have no impact on the Bank as the Bank does not have any derivatives.

Annual Improvements 2010-2012 Cycle
In the 2010-2012 annual improvements cycle, the IASB issued seven amendments to six standards, none of which had an impact on the Bank's financial statements.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

2.3 Changes in accounting policies and disclosures (continued)

i) New and amended standards and interpretations (continued)
Annual Improvements 2011-2013 Cycle
In the 2011-2013 annual improvements cycle, the IASB issued four amendments to four standards, none of which had an impact on the Bank's financial statements.

ii) Standards issued but not yet effective
The standards and interpretations that are issued, but not yet effective, up to the date of issuance of the Bank's financial statements are disclosed below. This listing is of standards and interpretations issued, which the Bank reasonably expect to be applicable at a future date. The Bank intends to adopt these standards, if applicable, when they become effective.

IFRS 9 Financial Instruments
In July 2014, the IASB issued the final version of IFRS 9 Financial Instruments which reflects all phases of the financial instruments project and replaces IAS 39 Financial Instruments: Recognition and Measurement and all previous versions of IFRS 9. The standard introduces new requirements for classification and measurement, impairment, and hedge accounting. IFRS 9 is effective for annual periods beginning on or after 1 January 2018, with early application permitted. Retrospective application is required, but comparative information is not compulsory. Early application of previous versions of IFRS 9 (2009, 2010 and 2013) is permitted if the date of initial application is before 1 February 2015. Management is currently assessing the impact of adopting IFRS 9 when it becomes effective.

Amendments to IAS 19 Defined Benefit Plans: Employee Contributions
IAS 19 requires an entity to consider contributions from employees or third parties when accounting for defined benefit plans. Where the contributions are linked to service, they should be attributed to periods of service as a negative benefit. These amendments clarify that, if the amount of the contributions is independent of the number of years of service, an entity is permitted to recognise such contributions as a reduction in the service cost in the period in which the service is rendered, instead of allocating the contributions to the periods of service. This amendment is effective for annual periods beginning on or after 1 July 2014. It is not expected that this amendment would be relevant to the Bank, since the Bank has no defined benefit plans with contributions from employees or third parties.

Annual improvements 2010-2012 Cycle
These improvements are effective from 1 July 2014 and are not expected to have a material impact on the Bank. They include:

a) IFRS 2 Share-based Payment
This improvement is applied prospectively and clarifies various issues relating to the definitions of performance and service conditions which are vesting conditions, including:

► A performance condition must contain a service condition;
► A performance target must be met while the counterparty is rendering service;
► A performance target may relate to the operations or activities of an entity, or to those of another entity in the same Bank;
► A performance condition may be a market or non-market condition; and
► If the counterparty, regardless of the reason, ceases to provide service during the vesting period, the service condition is not satisfied.

This improvement has no impact on the Bank as it does not have any share based payments.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

2.3 Changes in accounting policies and disclosures (continued)

ii) Standards issued but not yet effective (continued)

b) IFRS 3 Business Combinations
The amendment is applied prospectively and clarifies that all contingent consideration arrangements classified as liabilities (or assets) arising from a business combination should be subsequently measured at fair value through profit or loss whether or not they fall within the scope of IFRS 9 (or IAS 39, as applicable).

c) IFRS 8 Operating Segments
The amendments are applied retrospectively and clarifies that:

► An entity must disclose the judgements made by management in applying the aggregation criteria in paragraph 12 of IFRS 8, including a brief description of operating segments that have been aggregated and the economic characteristics (e.g., sales and gross margins) used to assess whether the segments are 'similar'.

► The reconciliation of segment assets to total assets is only required to be disclosed if the reconciliation is reported to the chief operating decision maker, similar to the required disclosure for segment liabilities.

As the Bank is not a listed entity, it is not required to make segment disclosures. Accordingly, these improvements have no impact on the Bank.

d) IAS 16 Property, Plant and Equipment and IAS 38 Intangible Assets
The amendment is applied retrospectively and clarifies in IAS 16 and IAS 38 that the asset may be revalued by reference to observable data on either the gross or the net carrying amount. In addition, the accumulated depreciation or amortisation is the difference between the gross and carrying amounts of the asset.

e) IAS 24 Related Party Disclosures
The amendment is applied retrospectively and clarifies that a management entity (an entity that provides key management personnel services) is a related party subject to the related party disclosures. In addition, an entity that uses a management entity is required to disclose the expenses incurred for management services.

Annual improvements 2011-2013 Cycle
These improvements are effective from 1 July 2014 and are not expected to have a material impact on the Bank. They include:

f) IFRS 13 Fair Value Measurement
The amendment is applied prospectively and clarifies that the portfolio exception in IFRS 13 can be applied not only to financial assets and financial liabilities, but also to other contracts within the scope of IAS 39.

IFRS 15 Revenue from Contracts with Customers
IFRS 15 was issued in May 2014 and establishes a new five-step model that will apply to revenue arising from contracts with customers. Under IFRS 15 revenue is recognised at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer. The principles in IFRS 15 provide a more structured approach to measuring and recognising revenue.

The new revenue standard is applicable to all entities and will supersede all current revenue recognition requirements under IFRS. Either a full or modified retrospective application is required for annual periods beginning on or after 1 January 2017 with early adoption permitted. The Bank is currently assessing the impact of IFRS 15 and plans to adopt the new standard on the it's effective date.

3 SIGNIFICANT ACCOUNTING JUDGEMENTS, ESTIMATES AND ASSUMPTIONS

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

In the process of applying the Bank's accounting policies, management has made the following judgements, estimates and assumptions which have the most significant effect on the amounts recognised in the financial statements.

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

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

Impairment and uncollectability of financial assets
Financial assets not carried at fair value are reviewed at each statement of financial position date to determine whether there is objective evidence that a specific financial asset may be impaired. If such evidence exists, any impairment loss is recognised in the statement of profit or loss. For assets carried at amortised cost, impairment is based on estimated future cash flows discounted at the original effective interest rate.

Classification of investments
Management decides on acquisition of a financial asset whether it should be classified as "fair value through profit or loss", "available-for-sale" or held to maturity. The classification of each investment reflects the management's intention in relation to each investment and is subject to different accounting treatments based on such classification.

4 CASH AND BALANCES WITH BANKS

	2014 *US$ '000*	*2013* *US$ '000*
Cash	**18**	4
Money at call and short notice	**22,489**	150,341
Cash and balances with banks	**22,507**	150,345
Deposits with banks and other financial institutions with original maturities of 90 days or less (note 5)	**365,750**	223,095
Cash and cash equivalents	**388,257**	373,440

5 DEPOSITS WITH BANKS AND OTHER FINANCIAL INSTITUTIONS

Deposits with banks and other financial institutions represent interest bearing money market deposits held with banks and other financial institutions as at the statement of financial position date as follows:

	2014 *US$ '000*	*2013* *US$ '000*
Deposits with original maturities of 90 days or less (note 4)	**365,750**	223,095
Deposits with original maturities of over 90 days	**157,895**	198,910
	523,645	422,005

6 INVESTMENTS HELD FOR TRADING

	2014 *US$ '000*	*2013* *US$ '000*
Quoted:		
- Debt securities	**3,000**	11,715
- Equity	**37**	2,911
	3,037	14,626

7 NON-TRADING INVESTMENTS

	2014 *US$ '000*	*2013* *US$ '000*
Held-to-maturity:		
Debt securities:		
- Sovereign	**53,122**	47,446
- Banks and corporates	**74,150**	71,553
Wakala units	**3,000**	3,000
Total held-to-maturity	**130,272**	121,999
Available-for-sale:		
Debt securities:		
- Sovereign	**4,549**	7,194
- Banks and corporates	**13,173**	8,089
Total available-for-sale	**17,722**	15,283
Total non-trading investments	**147,994**	137,282

8 LOANS AND ADVANCES

Loans and advances are stated net of provision for loan losses. The below gross loans and provisions for loan losses exclude interest in suspense amounting to US$ 304 thousand as of 31 December 2014 (2013: US$ 252 thousand).

	2014 *US$ 000*	*2013* *US$ 000*
Sovereign loans	**53,826**	61,536
Commercial loans	**166,441**	106,212
Letters of credit - financing	**283,870**	206,334
	504,137	374,082
Provision for loan losses	**(18,882)**	(11,084)
	485,255	362,998

8 LOANS AND ADVANCES (continued)

Movements in provision for loan losses were as follows:

	2014 *US$ '000*	*2013* *US$ '000*
At 1 January	**11,084**	7,067
Provided during the year	**7,817**	4,017
Exchange difference	**(19)**	-
At 31 December	**18,882**	11,084

The provision for loan losses comprise of the following:

	2014 *US$ '000*	*2013* *US$ '000*
Specific provision	**7,236**	5,384
Collective provision	**11,646**	5,700
At 31 December	**18,882**	11,084
Gross amount of loans, individually determined to be impaired, before deducting any individually assessed impairment allowance	**7,472**	12,595

Renegotiated facilities

	2014 *US$ '000*	*2013* *US$ '000*
Loans and advances		
Commercial loans	**8,412**	8,828

Reclassification of financial assets

In October 2008, the IASB issued amendments to IAS 39 "Financial Instruments: Recognition and Measurement" and IFRS 7 "Financial Instruments: Disclosures" titled "Reclassification of Financial Assets". The amendments to IAS 39 permit reclassification of financial assets from the "trading investment" category to "loans and advances" category in certain circumstances.

The amendments to IFRS 7 introduce additional disclosure requirements if an entity has reclassified financial assets in accordance with the IAS 39 amendments. The amendments are effective retrospectively from 1 July 2008.

In accordance with the amendments to IAS 39 and IFRS 7, "Reclassification of Financial Assets" the Bank reclassified investments in Iraq Notes with a carrying value of US $ 40.2 million, effective 1 July 2008 from 'trading investment' to 'loans and advances' pursuant to the amendment to IAS 39 and IFRS 7 issued by IASB in October 2008 and considering the global financial crisis as a rare circumstance in the financial sector.

The carrying values and fair values of the assets reclassified are as follows:

	2014 *US$ '000*	*2013* *US$ '000*
Carrying value	**43,242**	42,639
Fair value	**46,361**	46,687

8 LOANS AND ADVANCES (continued)

Reclassification of financial assets (continued)
Additional fair value loss that would have been recognised in the statement of profit or loss for the year ended 31 December 2014 had the trading investment not been reclassified amounts to US$ 277 thousand (2013: US$ 5,076 thousand).

The Bank earns an effective interest rate of 8.89% (2013: 8.89%) and expects to recover US $43,242 thousand (2013: US $ 42,639 thousand) on this reclassified financial asset.

9 PROPERTY, EQUIPMENT AND SOFTWARE

	Land and Building US$ '000	*Furniture, equipment and motor vehicles US$ '000*	*Software US$ '000*	*Total US$ '000*
Cost:				
At 1 January 2014	11,854	2,902	791	15,547
Additions during the year	31	154	2	187
Disposal during the year	-	(1)	-	(1)
At 31 December 2014	11,885	3,055	793	15,733
Depreciation:				
At 1 January 2014	465	1,159	557	2,181
Charge for the year	512	555	166	1,233
Relating to disposal	-	(1)	-	(1)
At 31 December 2014	977	1,713	723	3,413
Net book value:				
At 31 December 2014	**10,908**	**1,342**	**70**	**12,320**
At 31 December 2013	11,389	1,743	234	13,366

10 DEPOSITS FROM AND DUE TO BANKS AND OTHER FINANCIAL INSTITUTIONS

Deposits from banks and other financial institutions represent interest bearing money market deposits held with the Bank as at the statement of financial position date.

Due to banks and other financial institutions represent current account balances and cash collateral held with the Bank in relation to the letters of credit and guarantee as at the statement of financial position date.

11 DUE TO CUSTOMERS

Due to customers represent current account balances and cash collateral of corporate customers held with the Bank in relation to the letters of credit and letters of guarantee as at the statement of financial position date.

12 OTHER LIABILITIES

	***2014* US$ '000**	*2013 US$ '000*
Accrued expenses	**4,358**	2,204
Unearned fee income	**4,908**	9,865
Retention money	-	130
Other	**2,484**	2,084
	11,750	14,283

13 SHARE CAPITAL

	2014	*2013*
	US$ '000	*US$ '000*
Authorised:		
10,000,000 (2013: 10,000,000) ordinary shares of US$ 50 each	**500,000**	500,000

	2014	*2013*
	US$ '000	*US$ '000*
Issued and fully paid up :		
5,000,000 (2013: 5,000,000) ordinary shares of US$ 50 each	**250,000**	250,000

Shareholders

	2014		*2013*	
	Percentage holding (%)	*US$ '000*	*Percentage holding (%)*	*US$ '000*
Libyan Foreign Bank	**99.50**	**248,750**	99.50	248,750
National Bank of Yemen	**0.28**	**689**	0.28	689
Yemen Bank for Reconstruction and Development	**0.22**	**561**	0.22	561
	100.00	**250,000**	**100.00**	**250,000**

Advance towards capital increase
At the Extra Ordinary General Meeting held on 28 April 2014, the shareholders approved the increase of the Bank's share capital from US$ 250 million to US$ 300 million. During the year, US$ 140 thousand was received by the Bank towards capital increase from one of the minority shareholders. On receipt of the remaining amounts, the capital increase will be registered with the Ministry of Industry and Commerce.

Statutory reserve
As required by the Bahrain Commercial Companies Law (BCCL) and the Bank's articles of association, a statutory reserve has been created by transfer of 10% of its annual profit. The Bank may resolve to discontinue such transfers when the reserve totals 50% of the paid up capital. The reserve is not distributable except in such circumstances as stipulated in the BCCL and following approval of the Central Bank of Bahrain.

14 DIVIDENDS PAID AND PROPOSED

The Bank has not proposed a dividend for the year ended 31 December 2014 (2013: US$ 25million; US$ 5 per share).

During the year, the dividend for the year ended 31 December 2013 amounting to US$ 25 million (US$ 5 per share) was paid following regulatory approvals and the approval of the shareholders in the Annual General Meeting held on 28 April 2014.

15 INTEREST INCOME

	2014 US$ '000	2013 US$ '000
Loans and advances	**34,587**	23,967
Deposits with banks and other financial institutions	**3,302**	3,676
Investments held for trading	**375**	737
Non-trading investments	**7,297**	6,247
	45,561	34,627

16 INTEREST EXPENSE

	2014 US$ '000	2013 US$ '000
Deposits from and due to banks and other financial institutions	**1,475**	1,845
Due to customers	**1**	15
	1,476	1,860

17 FEE AND COMMISSION INCOME

	2014 US$ '000	2013 US$ '000
Commission income on letters of credit	**15,211**	17,257
Commission income on letters of guarantee	**304**	160
Other	**921**	457
	16,436	17,874

18 TRADING INCOME

	2014 US$ '000	2013 US$ '000
Changes in fair value of investments held for trading	**17**	(540)
Trading gains / (losses) - net	**488**	(487)
	505	(1,027)

19 OTHER OPERATING EXPNESES

	2014 US$ '000	2013 US$ '000
Administrative and marketing expenses	**2,213**	1,777
Board of Directors' expenses	**846**	921
Professional services	**178**	406
Fees and other charges	**855**	316
	4,092	3,420

20 COMMITMENTS AND CONTINGENT LIABILITIES

	2014	*2013*
	US$ '000	*US$ '000*
Letters of credit	**260,062**	163,393
Letters of guarantee	**8,394**	6,347
Foreign exchange contracts	**340**	2,521
Undrawn loan commitments	**18,409**	1,102
	287,205	173,363

Legal claim contingency
The Bank is defendant in a legal proceeding that has arisen in the ordinary course of business. A counterparty is pursuing a claim of approximately US$ 8 million including opportunity loss for future periods. The counterparty's claim is based on a document, which management believes does not commit the Bank. The Directors of the Bank, on reviewing the advice of professional legal advisers, are satisfied that the claim is not legally tenable and the outcome will not have any material effect on the financial position of the Bank.

21 RISK MANAGEMENT

21.1 Introduction
Risk is inherent in the Bank's activities and is managed through a process of ongoing identification, measurement and monitoring, subject to risk limits and other controls. This process of risk management is critical to the Bank's continuing profitability and each individual within the Bank is accountable for the risk exposures relating to his or her responsibilities. The main risks to which the Bank is exposed are credit risk, liquidity risk, market risk and operational risk.

a) Risk management structure

Board of Directors
The Board of Directors is responsible for the overall risk management approach and for approving the risk strategies and principles.

Audit Risk and Compliance Committee
The Audit Risk and Compliance Committee (ARCC) of the Board is responsible for assessing the quality and integrity of financial reporting, effectiveness of systems monitoring financial and disclosure compliance with legal and regulatory requirements, supervision of compliance function and soundness of internal controls. The ARCC also obtains regular updates from management and the Bank's compliance officer regarding compliance matters, which may have a material impact on the Bank's financial statements and reviews the findings of any examinations by regulatory agencies.

Management Risk Committee
The Management Risk Committee has the overall responsibility for establishing the risk strategy and implementing principles, frameworks, policies and limits. It is responsible for the fundamental risk issues and manages and monitors relevant risk decisions.

Asset Liability Management Committee
The Asset Liability Management Committee's (ALCO) objective is to prudently direct and manage asset and liability allocation to achieve the Bank's strategic goals. The ALCO monitors the Bank's liquidity risks by ensuring that the Bank's activities are in line with the risk/reward guidelines approved by the Board.

Internal Audit
Internal control processes throughout the Bank are audited at least annually by the Internal Audit Department, based on the risk-based audit plan approved by the ARCC. Audit staff examine both the adequacy of the procedures and the Bank's compliance with the procedures. Internal Audit discusses the results of all assessments with management and reports its findings and recommendations to the ARCC.

21 RISK MANAGEMENT (continued)

21.1 Introduction (continued)

b) Risk measurement and reporting systems
Monitoring and controlling risks is primarily performed based on limits approved by the Board. These limits reflect the business strategy and market environment of the Bank as well as the level of risk that it is willing to accept, with additional emphasis on selected industries. The Bank also monitors and measures the overall risk-bearing capacity in relation to the aggregate risk exposure across all risk types and activities.

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

In order to manage credit concentration risk, the Bank's policies and procedures include guidelines to maintain a diversified portfolio. Identified concentrations of credit risks are controlled and managed accordingly.

21.2 Credit risk
Credit risk is the risk that a customer or counterparty will fail to meet a commitment, resulting in financial loss to the Bank. Such risk arises from lending, treasury and other activities undertaken by the Bank. Credit risk is actively monitored in accordance with the credit policies which clearly define delegated lending authorities, and procedures. The Bank manages its credit risk by monitoring concentration of exposures by geographic location and adhering to approved limits formulated. The Bank limits its risk on off balance sheet items with adequate collateral.

a. Maximum exposure to credit risk without taking account of any collateral and other credit enhancements
The table below shows the maximum exposure to credit risk for the components of the statement of financial position. The maximum exposure is shown gross, before the effect of mitigation through the use of master netting and collateral agreements. The net exposure represents gross exposure net of cash collateral against LC's.

	Gross maximum exposure 2014 US$ '000	***Net maximum exposure 2014 US$ '000***	*Gross maximum exposure 2013 US$ '000*	*Net maximum exposure 2013 US$ '000*
Balances with banks	**22,489**	**22,489**	150,341	150,341
Deposits with banks and other financial institutions	**523,645**	**523,645**	422,005	422,005
Investments held for trading	**3,000**	**3,000**	11,715	11,715
Non-trading investments	**147,994**	**147,994**	137,282	137,282
Loans and advances	**485,255**	**439,643**	362,998	341,937
Interest receivable	**8,922**	**8,922**	5,916	5,916
Other assets	**921**	**921**	928	928
Total funded credit risk exposure	**1,192,226**	**1,146,614**	1,091,185	1,070,124
Unfunded exposure on credit related contingencies	**286,865**	**179,254**	170,842	48,681
Total funded and unfunded credit risk exposures	**1,479,091**	**1,325,868**	1,262,027	1,118,805

The amount, type and valuation of collateral are based on guidelines specified in the risk management framework. The main types of collaterals accepted include cash collateral, residential and commercial real estate and securities.

21 RISK MANAGEMENT (continued)

21.2 Credit risk (continued)

b. Credit quality per class of financial assets

The table below presents an analysis of the financial assets exposed to credit risk and external rating designation at 31 December 2014 and 2013. The credit quality is graded based on external credit rating agencies - Standard & Poor, Fitch and Moody's and internal ratings are categorised as follows:

(i) High standard - Where external credit rating agency ratings are A and above.
(ii) Standard - Where external credit rating agency ratings are below A.
(iii) Watch list - Where the facility is not past due but recoverability is being monitored.
(iv) Past due and impaired - Where interest or principal sum of loan is due for more than 90 days.

	Neither past due nor impaired					
	High standard grade US$ '000	*Standard grade US$ '000*	*Watch list US$ '000*	*Past due and individually impaired US$ '000*	*Provision for loan losses US$ '000*	*Total US$ '000*
At 31 December 2014						
Balances with banks	1,883	20,606	-	-	-	22,489
Deposits with banks and other financial institutions	16,931	506,714	-	-	-	523,645
Investments held for trading	-	3,000	-	-	-	3,000
Non-trading investments	28,209	119,785	-	-	-	147,994
Loans and advances	-	496,665	-	7,472	(18,882)	485,255
Interest receivable	293	8,629	-	-	-	8,922
Other assets	-	921	-	-	-	921
Funded exposures	47,316	1,156,320	-	7,472	(18,882)	1,192,226
Credit related contingencies	-	286,865	-	-	-	286,865
Gross unfunded exposures	-	286,865	-	-	-	286,865
Net funded and unfunded exposures	47,316	1,443,185	-	7,472	(18,882)	1,479,091

21 RISK MANAGEMENT (continued)

21.2 Credit risk (continued)

b. Credit quality per class of financial assets (continued)

	Neither past due nor impaired					
	High standard grade US$ '000	*Standard grade US$ '000*	*Watch list US$ '000*	*Past due and individually impaired US$ '000*	*Provision for loan losses US$ '000*	*Total US$ '000*
At 31 December 2013						
Balances with banks	131,250	19,091	-	-	-	150,341
Deposits with banks and other financial institutions	-	422,005	-	-	-	422,005
Investments held for trading	497	11,218	-			11,715
Non-trading investments	13,019	124,263	-	-	-	137,282
Loans and advances	-	370,315	-	3,767	(11,084)	362,998
Interest receivable	185	5,731	-	-	-	5,916
Other assets	-	928	-	-	-	928
Funded exposure	144,951	953,551	-	3,767	(11,084)	1,091,185
Credit related contingencies	-	170,842	-	-	-	170,842
Gross unfunded exposures	-	170,842	-	-	-	170,842
Net funded and unfunded exposures	144,951	1,124,393	-	3,767	(11,084)	1,262,027

Excludes loans of US$ 8,828 thousand which have been restructured and therefore classified under "Standard grade".

c. Concentration of maximum exposure to credit risk

The geographical distribution of gross credit exposures (net of provision for impairment) is presented below:

At 31 December 2014

	Bahrain US$ '000	***Other GCC countries US$ '000***	***Middle-east and African countries US$ '000***	***Europe US$ '000***	***Rest of the world US$ '000***	***Total US$ '000***
Balances with banks	**5,936**	**1,346**	**54**	**15,051**	**102**	**22,489**
Deposits with banks and other financial institutions	**189,157**	**137,566**	**70,000**	**126,922**	**-**	**523,645**
Investments held for trading	**-**	**-**	**-**	**3,000**	**-**	**3,000**
Non-trading investments	**29,916**	**52,763**	**11,891**	**48,647**	**4,777**	**147,994**
Loans and advances	**-**	**5,225**	**377,663**	**88,239**	**14,128**	**485,255**
Interest receivable	**485**	**620**	**6,512**	**1,146**	**159**	**8,922**
Other assets	**882**	**-**	**39**	**-**	**-**	**921**
Gross funded exposures	**226,376**	**197,520**	**466,159**	**283,005**	**19,166**	**1,192,226**
Credit related contingencies	**-**	**510**	**264,757**	**11,839**	**9,759**	**286,865**
Gross unfunded exposures	**-**	**510**	**264,757**	**11,839**	**9,759**	**286,865**
Gross funded and unfunded exposures	**226,376**	**198,030**	**730,916**	**294,844**	**28,925**	**1,479,091**

21 RISK MANAGEMENT (continued)

21.2 Credit risk (continued)

c. Concentration of maximum exposure to credit risk (continued)

At 31 December 2013

	Bahrain *US$ '000*	*Other GCC countries* *US$ '000*	*Other Middle- east and African countries* *US$ '000*	*Europe* *US$ '000*	*Rest of the world* *US$ '000*	*Total* *US$ '000*
Balances with banks	2,597	14,030	167	14,706	118,841	150,341
Deposits with banks and other financial institutions	166,052	80,000	70,000	75,953	30,000	422,005
Investments held for trading	623	-	958	5,892	4,242	11,715
Non-trading investments	29,430	37,928	14,127	51,026	4,771	137,282
Loans and advances	-	3,914	288,073	52,113	18,898	362,998
Interest receivable	548	526	3,784	810	248	5,916
Other assets	928	-	-	-	-	928
Gross funded exposures	200,178	136,398	377,109	200,500	177,000	1,091,185
Credit related contingencies	-	11,536	157,162	110	2,034	170,842
Gross unfunded exposures	-	11,536	157,162	110	2,034	170,842
Gross funded and unfunded exposures	200,178	147,934	534,271	200,610	179,034	1,262,027

Sectoral classification of gross credit exposures is presented below:

At 31 December 2014

	Sovereign ***US$ '000***	***Banks and financial institutions*** ***US$ '000***	***Commercial, business and others*** ***US$ '000***	***Total*** ***US$ '000***
Balances with banks	-	22,489	-	22,489
Deposits with banks and other financial institutions	-	523,645	-	523,645
Investments held for trading	-	3,000	-	3,000
Non-trading investments	57,670	49,704	40,620	147,994
Loans and advances	53,826	342,674	88,755	485,255
Interest receivable	2,149	5,644	1,129	8,922
Other assets	-	39	882	921
Gross funded exposures	113,645	947,195	131,386	1,192,226
Credit related contingencies	4,872	258,295	23,698	286,865
Gross unfunded exposures	4,872	258,295	23,698	286,865
Gross funded and unfunded exposures	118,517	1,205,490	155,084	1,479,091

21 RISK MANAGEMENT (continued)

21.2 Credit risk (continued)

c. Concentration of maximum exposure to credit risk (continued)

At 31 December 2013

	Sovereign US$ '000	Banks and financial institutions US$ '000	Commercial, business and others US$ '000	Total US$ '000
Balances with banks	-	150,341	-	150,341
Deposits with banks and other financial institutions	-	422,005	-	422,005
Investments held for trading	1,581	5,395	4,739	11,715
Non-trading investments	54,640	41,936	40,706	137,282
Loans and advances	61,537	286,170	15,291	362,998
Interest receivable	2,102	3,111	703	5,916
Other assets	-	7	921	928
Gross funded exposures	119,860	908,965	62,360	1,091,185
Credit related contingencies	1,102	156,911	12,829	170,842
Gross unfunded exposures	1,102	156,911	12,829	170,842
Gross of funded and unfunded exposures	120,962	1,065,876	75,189	1,262,027

21.3 Market risk

Market risk is the risk of potential financial loss that may arise from adverse changes in the value of a financial instrument or portfolio of financial instruments due to movements in interest rates, foreign exchange rates and equity. This risk arises from asset - liability mismatches, changes that occur in the yield curve and foreign exchange rates. Given the Bank's low risk strategy, aggregate market risk levels are considered very low.

21.3.1 Interest rate risk

Interest rate risk arises from the possibility that changes in interest rates will affect the value of financial instruments. The Bank is exposed to interest rate risk as a result of mismatches or gaps in the amounts of assets and liabilities that mature or reprise in a given period. The Bank manages this risk by matching the repricing of assets and liabilities through a number of means. The Bank's interest rate sensitivity position as of 31 December, is as follows:

Sensitivity analysis - interest rate risk

	Impact on statement of profit or loss	
	2014	2013
	US$ '000	US$ '000
25 bps increase/decrease		
US Dollar	**± 524**	± 291
Euro	**± 1**	± 5

21 RISK MANAGEMENT (continued)

21.3 Market risk (continued)

21.3.2 Currency risk

Currency risk arise from the movement of the rate of exchange over a period of time. The Bank's currency risk is limited to assets and liabilities denominated in GBP and Euro. The following table demonstrates the sensitivity to a reasonable possible change in foreign exchange rates, with all other variables held constant, on the Bank's statement of comprehensive income:

	Change in rate	*Effect on net income for the year*	
		2014	*2013*
		US$ '000	*US$ '000*
Euro	± 5%	± 13	± 94
GBP	± 5%	-	± 4

As other currencies exposure is insignificant and GCC currencies to which the Bank is exposed are pegged to the US Dollar, their balances are not considered to represent significant currency risk.

21.3.3 Equity price risk

Equity price risk is the risk that the fair value of equities decreases as a result of changes in the value of individual companies' shares. The effect on profit and equity, as a result of a change in fair value of trading equity instruments, due to a reasonably possible change in equity prices, with all other variables held constant, is as follows:

	Change in equity prices	*Effect on net income and equity for the year*	
		2014	*2013*
		US$ '000	*US$ '000*
Investments held for trading	± 10%	± 4	± 291

21.4 Liquidity risk

Liquidity risk is the risk that the Bank will be unable to meet its funding requirements. Liquidity risk can be caused by market disruptions or a credit downgrade which may cause certain sources of funding to dry up immediately. To limit this risk, management has arranged diversified funding sources, manages assets with liquidity in mind, and monitors liquidity on a daily basis. This incorporates an assessment of expected cash flow and the availability of high grade collateral which would be used to secure additional funding if required.

21 RISK MANAGEMENT (continued)

21.4 Liquidity risk (continued)

The maturity profile of the assets and liabilities at **31 December 2014** given below reflects the management's best estimates of the maturities of assets and liabilities that have been determined on the basis of the remaining period at the balance sheet date.

At 31 December 2014	*Up to 1 year*						
	Up to 1 month US$ '000	*1 to 3 months US$ '000*	*3 to 12 months US$ '000*	*Total US$ '000*	*More than 1 year US$ '000*	*No specific maturity US$ '000*	*Total US$ '000*
ASSETS							
Cash and balances with banks	22,507	-	-	22,507	-	-	22,507
Deposits with banks and other financial institutions	337,267	186,378	-	523,645	-	-	523,645
Investments held for trading	3,037	-	-	3,037	-	-	3,037
Non-trading investments	-	3,813	5,067	8,880	139,114	-	147,994
Loans and advances	120,685	88,223	208,000	416,908	68,347	-	485,255
Property, equipment and software	-	-	-	-	-	12,320	12,320
Interest receivable	3,305	2,355	3,262	8,922	-	-	8,922
Other assets	48	288	69	405	872	-	1,277
Total assets	486,849	281,057	216,398	984,304	208,333	12,320	1,204,957
LIABILITIES							
Deposits from banks and other financial institutions	502,144	110,175	4,000	616,319	-	-	616,319
Due to banks and other financial institutions	80,091	104,650	34,114	218,855	781	-	219,636
Due to customers	18,668	4,023	95	22,786	2,365	-	25,151
Interest payable	95	87	7	189	-	-	189
Other liabilities	135	6,550	4,264	10,949	128	673	11,750
Total liabilities	601,133	225,485	42,480	869,098	3,274	673	873,045
Net liquidity gap	(114,284)	55,572	173,918	115,206	205,059	11,647	331,912
Cumulative liquidity gap	(114,284)	(58,712)	115,206	-	320,265	331,912	-

21 RISK MANAGEMENT (continued)

21.4 Liquidity risk (continued)

At 31 December 2013	*Up to 1 year*						
	Up to 1 month US$ '000	*1 to 3 months US$ '000*	*3 to 12 months US$ '000*	*Total US$ '000*	*More than 1 year US$ '000*	*No specific maturity US$ '000*	*Total US$ '000*
ASSETS							
Cash and balances with banks	150,345	-	-	150,345	-	-	150,345
Deposits with banks and other financial institutions	159,595	262,410	-	422,005	-	-	422,005
Investments held for trading	14,626	-	-	14,626	-	-	14,626
Non-trading investments	-	2,220	4,315	6,535	130,747	-	137,282
Loans and advances	37,209	29,218	194,547	260,974	102,024	-	362,998
Property, equipment and software	-	-	-	-	-	13,366	13,366
Interest receivable	2,359	1,582	1,975	5,916	-	-	5,916
Other assets	2	311	28	341	883	-	1,224
Total assets	364,136	295,741	200,865	860,742	233,654	13,366	1,107,762
LIABILITIES							
Deposits from banks and other financial institutions	257,736	243,450	-	501,186	-	-	501,186
Due to banks and other financial institutions	137,368	36,315	87,465	261,148	7,125	-	268,273
Due to customers	7,714	-	-	7,714	-	-	7,714
Interest payable	67	138	-	205	-	-	205
Other liabilities	593	142	11,439	12,174	1,678	431	14,283
Total liabilities	403,478	280,045	98,904	782,427	8,803	431	791,661
Net liquidity gap	(39,342)	15,696	101,961	78,315	224,851	12,935	316,101
Cumulative liquidity gap	(39,342)	(23,646)	78,315	-	303,166	316,101	-

21 RISK MANAGEMENT (continued)

21.4 Liquidity risk (continued)

The maturity profile of the financial and contingent liabilities as at **31 December 2014** based on contractual undiscounted repayment amounts is as follows:

At 31 December 2014	*Up to 1 year*						
	Up to 1 month US$ '000	*1 to 3 months US$ '000*	*3 to 12 months US$ '000*	*Total US$ '000*	*More than 1 year US$ '000*	*No specific maturity US$ '000*	*Total US$ '000*
Liabilities							
Deposits from banks and financial institutions	502,261	110,252	4,006	616,519	-	-	616,519
Due to banks and other financial institutions	80,096	104,668	34,126	218,890	782	-	219,672
Due to customers	18,669	4,023	95	22,787	2,367	-	25,154
Interest payable	95	87	-	182	-	-	182
Other liabilities	135	6,550	4,264	10,949	128	673	11,750
Total undiscounted liabilities	601,256	225,580	42,491	869,327	3,277	673	873,277
Derivatives:							
Foreign exchange contracts	340	-	-	340	-	-	340
Commitments and contingent liabilities							
Letters of credit	34,335	73,141	143,212	250,688	9,374	-	260,062
Letters of guarantee	3	1,053	1,122	2,178	6,216	-	8,394
Undrawn loan commitments	18,409	-	-	18,409	-	-	18,409
	52,747	74,194	144,334	271,275	15,590	-	286,865

21 RISK MANAGEMENT (continued)

21.4 Liquidity risk (continued)

At 31 December 2013	*Up to 1 year*						
	Up to 1 month US$ '000	*1 to 3 months US$ '000*	*3 to 12 months US$ '000*	*Total US$ '000*	*More than 1 year US$ '000*	*No specific maturity US$ '000*	*Total US$ '000*
Liabilities							
Deposits from banks and financial institutions	257,775	243,568	-	501,343	-	-	501,343
Due to banks and other financial institutions	137,389	36,331	87,544	261,264	7,138	-	268,402
Due to customers	7,715	-	-	7,715	-	-	7,715
Interest payable	67	138	-	205	-	-	205
Other liabilities	593	142	11,439	12,174	1,678	431	14,283
Total undiscounted liabilities	403,539	280,179	98,983	782,701	8,816	431	791,948
Derivatives:							
Foreign exchange contracts	2,521	-	-	2,521	-	-	2,521
Commitments and contingent liabilities							
Letters of credit	32,487	36,317	87,464	156,268	7,125	-	163,393
Letters of guarantee	-	1,355	4,973	6,328	19	-	6,347
Undrawn loan commitments	1,102	-	-	1,102	-	-	1,102
	33,589	37,672	92,437	163,698	7,144	-	170,842

21 RISK MANAGEMENT (continued)

21.5 Fair value of financial instruments

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

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

Fair value hierarchy

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

Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities;

Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly; and

Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

Fair value hierarchy - financial instruments measured at fair value

The following table provides the fair value measurement hierarchy of the Bank's financial instruments measured at fair value:

At 31 December 2014

	Level 1	***Level 2***	***Total***
	US$ '000	***US$ '000***	***US$ '000***
Investments held for trading	**3,037**	**-**	**3,037**
Available-for-sale investments	**17,722**	**-**	**17,722**
Derivative financial instruments	**-**	**(57)**	**(57)**
	20,759	**(57)**	**20,702**

At 31 December 2013

	Level 1	*Level 2*	*Total*
	US$ '000	*US$ '000*	*US$ '000*
Investments held for trading	14,626	-	14,626
Available-for-sale investments	15,283	-	15,283
Derivative financial instruments	-	7	7
	29,909	7	29,916

The Bank had no investments measured at fair value qualifying for level 3 of fair value heirarchy as at 31 December 2014 and as at 31 December 2013.

Transfers between level 1, level 2 and level 3

During the year ended 31 December 2014, there were no transfers between level 1 and level 2 fair value measurements, and no transfers into or out of level 3 fair value measurement (2013: nil).

21 RISK MANAGEMENT (continued)

21.5 Fair value of financial instruments (continued)

Fair value hierarchy - financial instruments not measured at fair value

The following table provides the fair value measurement hierarchy of the Bank's financial instruments not measured at fair value:

At 31 December 2014

	Level 1 US$ '000	Level 2 US$ '000	Level 3 US$ '000	Total fair value US$ '000	Carrying value US$ '000
Held-to-maturity investments	**121,988**	**-**	**7,815**	**129,803**	**130,272**
Loans and advances	**46,361**	**-**	**-**	**46,361**	**43,242**
	168,349	**-**	**7,815**	**176,164**	**173,514**

At 31 December 2013

	Level 1 US$ '000	Level 2 US$ '000	Level 3 US$ '000	Total fair value US$ '000	Carrying value US$ '000
Held-to-maturity investments	106,012	-	9,630	115,642	121,999
Loans and advances	46,687	-	-	46,687	42,639
	152,699	-	9,630	162,329	164,638

- Fair values of held-to-maturity investments are determined based on quoted prices in the active markets.
- Fair values of certain loans and advances falling under Level 1 are determined based on quoted prices in active markets.

Balances with banks, deposits with banks and other financial institutions, loans and advances (other than those disclosed in the table above), interest receivable, other assets, deposits from banks and other financial institutions, due to banks and other financial institutions, due to customers, interest payable and other liabilities are generally short term in nature. Management has assessed that the fair values of these approximate their carrying values as of 31 December 2014 and 31 December 2013.

22 DERIVATIVE FINANCIAL INSTRUMENTS

In the ordinary course of business, the Bank enters into various types of transactions that involve derivative financial instruments. A derivative financial instrument is a financial contract between two parties where payments are dependent upon movements in price in one or more underlying financial instruments, reference rates or indices.

These include forward exchange contracts which create rights and obligation that have the effect of transferring between the parties of the instrument one or more of the financial risks inherent in an underlying primary financial instrument. On inception, a derivative financial instrument gives one party a contractual right to exchange financial assets or financial liabilities with another party under conditions that are potentially favourable, or a contractual obligation to exchange financial assets or financial liabilities with another party under conditions that are potentially unfavourable. However, they generally do not result in a transfer of the underlying primary financial instrument on inception of the contract, nor does such a transfer necessarily take place on maturity of the contract. Some instruments embody both a right and an obligation to make an exchange. Because the terms of the exchange are determined on inception of the derivative instruments, as prices in financial markets change those terms may become either favourable or unfavourable.

22 DERIVATIVE FINANCIAL INSTRUMENTS (continued)

The table below shows the net fair values of derivative financial instruments together with the notional amount. These contracts are settled on a net basis. Depending on currency movements, the contracts may result in either a net asset or a net liability. The following table shows the material outstanding contracts as at 31 December:

	2014		*2013*	
	Notional amount US$ '000	***Gain / (loss) US$ '000***	*Notional amount US$ '000*	*Gain / (loss) US$ '000*
Forward exchange contracts	**340**	**(57)**	2,521	7

23 TRANSACTIONS WITH RELATED PARTIES

Related parties represent associated companies, shareholders, directors and key management personnel of the Bank, and entities controlled, jointly controlled or significantly influenced by such parties. Pricing policies and terms of these transactions are approved by the Bank's management.

Transactions with related parties included in the statement of profit or loss and statement of financial position are as follows:

	2014 US$ '000	*2013 US$ '000*
Statement of profit or loss		
Interest income	**756**	278
Interest expense	**841**	921
Fee and commission income	**1,077**	615

	2014 US$ '000	*2013 US$ '000*
Statement of financial position		
Assets		
Cash and balances with banks	**1,595**	10,772
Deposit with banks and financial institutions	**88,541**	77,500
Loans and advances	**7,511**	7,874
Interest receivable	**199**	119
Other assets	**220**	38
Liabilities		
Deposits from banks and other financial institutions	**400,376**	243,935
Due to banks and other financial institutions	**16,249**	15,536
Interest payable	**154**	128
Other liabilities	**2,221**	3,014
Assets under management (note 24)	**23,376**	26,517
Contingent liabilities- Letters of credit (fully secured by deposits)	**17,549**	21,542

23 TRANSACTIONS WITH RELATED PARTIES (continued)

Compensation paid to the Board of Directors and key management personnel:

	2014 *US$ 000*	*2013* *US$ 000*
Short term benefits*	**4,330**	3,469
End of term benefits	**189**	132
Total compensation	**4,519**	3,601

* Includes accrual for sitting fee and bonus of US$ 662 thousand (2013: US$ 680 thousand) and the reimbursement of travel, accommodation and other expenses paid to Board of Directors amounting to US$ 184 thousand (2013: US$ 197 thousand). The accrual is subject to approval by the Bank's shareholders in the next Annual General Meeting.

Short term benefits also includes compensation paid to key management personnel as salary, allowances and bonus.

24 ASSETS UNDER MANAGEMENT

The Bank provides trade finance services to certain customers on behalf of its Parent, which involve the Bank acting as the custodian of the assets in a fiduciary capacity. Assets that are held in financing capacity are not included in these financial statements. At 31 December 2014, the Bank had fiduciary assets under management of US$ 23,376 thousand (2013:US$ 26,517 thousand).

25 CAPITAL ADEQUACY

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

In order to maintain or adjust the capital structure, the Bank may adjust the amount of dividend payment to shareholders, return capital to shareholders or issue capital securities.

The risk asset ratio, calculated in accordance with the capital adequacy guidelines, under Basel II, approved by the Central Bank of Bahrain.

	2014 *US$ 000*	*2013* *US$ 000*
Capital base:		
Tier 1 capital	**331,912**	311,206
Tier 2 capital	**9,134**	805
Total capital base (a)	**341,046**	312,011
Risk weighted assets (b)	**808,372**	712,166
Capital adequacy (a/b * 100)	**42.19%**	43.81%
Minimum requirement	**12.00%**	12.00%