

ITHMAAR BANK B.S.C. (C)

INTERIM CONDENSED CONSOLIDATED FINANCIAL INFORMATION
FOR THE THREE MONTH PERIOD ENDED 31 MARCH 2018

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**AUDITOR'S REVIEW REPORT TO THE SHAREHOLDERS OF
ITHMAAR BANK B.S.C. (C)**

Introduction

We have reviewed the accompanying interim condensed consolidated financial information of Ithmaar Bank B.S.C. (C) (the "Bank") and its subsidiaries (the "Group") which comprises the interim condensed consolidated statement of financial position as at 31 March 2018 and the related interim condensed consolidated statements of income, changes in owners' equity, cash flows, and changes in restricted investment accounts for the three month period then ended, and a summary of significant accounting policies and other explanatory notes. The directors are responsible for the preparation and presentation of this interim condensed consolidated financial information in accordance with basis of preparation stated in Note 2 to this interim condensed consolidated financial information. Our responsibility is to express a conclusion on this interim condensed consolidated financial information based on our review.

Scope of Review

We conducted our review in accordance with International Standard on Review Engagements 2410, "Review of Interim Financial Information Performed by the Independent Auditor of the Entity". A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the accompanying interim condensed consolidated financial information has not been prepared, in all material respects, in accordance with basis of preparation stated in Note 2 to this interim condensed consolidated financial information.

A handwritten signature in blue ink, appearing to read 'PricewaterhouseCoopers', is written over the typed name of the partner.

Partner registration no. 196
14 May 2018
Manama, Kingdom of Bahrain

Ithmaar Bank B.S.C. (C)

Interim condensed consolidated statement of financial position

(Expressed in thousands of Bahraini Dinars unless otherwise stated)

	Notes	At 31 March 2018 (Reviewed)	At 31 December 2017 (Audited)	At 31 March 2017 (Reviewed)
ASSETS				
Cash and balances with banks and central banks	3	218,985	263,819	235,563
Commodity and other placements with banks, financial and other institutions	4	167,600	98,545	27,270
Murabaha and other financings	5	1,789,336	1,808,841	1,771,050
Musharaka financing		147,711	139,252	97,841
Sukuk and investment securities	6	466,630	617,156	671,410
Restricted investment accounts		27,183	27,183	27,231
Assets acquired for leasing		144,989	131,106	105,086
Investment in real estate		3,821	3,994	3,889
Other assets	7	65,756	69,150	80,680
Fixed assets		21,603	22,252	21,435
Intangible assets		60,226	61,121	65,621
Total assets		3,113,840	3,242,419	3,107,076
LIABILITIES, EQUITY OF UNRESTRICTED INVESTMENT ACCOUNTHOLDERS, MINORITY INTEREST AND OWNERS' EQUITY				
Customers' current accounts		654,181	676,888	603,210
Due to banks, financial and other institutions		411,235	434,635	440,124
Due to investors		681,116	719,303	734,521
Other liabilities		158,584	147,551	126,625
Total liabilities		1,905,116	1,978,377	1,904,480
Equity of unrestricted investment accountholders	9	1,063,265	1,064,898	999,507
Minority interest		44,304	44,541	44,489
Total liabilities, equity of unrestricted investment accountholders and minority interest		3,012,685	3,087,816	2,948,476
Share capital	10	100,000	100,000	100,000
Reserves		30,384	31,902	36,181
(Accumulated losses)/ retained earnings		(29,229)	22,701	22,419
Total owners' equity		101,155	154,603	158,600
Total liabilities, equity of unrestricted investment accountholders, minority interest and owners' equity		3,113,840	3,242,419	3,107,076

This interim condensed consolidated financial information was approved by the Board of Directors on 14 May 2018 and signed on their behalf by:



HRH Prince Amr Mohamed Al Faisal
Chairman



Dr. Amani Khaled Bouresli
Director




Ahmed Abdul Rahim
CEO


The notes 1 to 14 on pages 11 to 29 form an integral part of the interim condensed consolidated financial information.


Ithmaar Bank B.S.C. (C)
Interim condensed consolidated income statement
(Expressed in thousands of Bahraini Dinars unless otherwise stated)

	Notes	Three months ended	
		31 March 2018 (Reviewed)	31 March 2017 (Reviewed)
INCOME			
Income from unrestricted investment accounts		16,010	13,926
Less: return to unrestricted investment accounts and impairment provisions		(9,416)	(8,398)
Group's share of income from unrestricted investment accounts as a Mudarib		6,594	5,528
Income from murabaha and other financings		16,076	15,474
Income from sukuk and investment securities		9,268	13,460
Other income		4,157	2,754
Total income		36,095	37,216
Less: profit paid to banks, financial and other institutions – net		(15,526)	(14,496)
Operating income		20,569	22,720
EXPENSES			
Administrative and general expenses		(13,993)	(13,849)
Depreciation and amortization		(2,270)	(2,386)
Total expenses		(16,263)	(16,235)
Net income before provision for impairment and overseas taxation		4,306	6,485
Provision for impairment – net	8	385	409
Net income before overseas taxation		4,691	6,894
Overseas taxation		(2,665)	(3,811)
NET INCOME FOR THE PERIOD		2,026	3,083
Attributable to:			
Equity holders of the Bank		832	1,142
Minority interests		1,194	1,941
		2,026	3,083
Basic and diluted earnings per share	12	Fils 0.83	Fils 1.14

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CEO

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Ithmaar Bank B.S.C. (C)

Interim condensed consolidated statement of changes in owners' equity for the three month period ended 31 March 2018

(Expressed in thousands of Bahraini Dinars unless otherwise stated)

	Reserves						Total reserves	(accumulated losses)/ Retained Earnings	Total owners' equity
	Share capital	Statutory reserve	Investments fair value reserve	Investment in real estate fair value reserve	Foreign currency translation	Other reserves			
At 1 January 2018 (Audited)	100,000	158	3,815	890	(13,241)	40,280	31,902	22,701	154,603
Impact of FAS 30 (note - 2)	-	-	-	-	-	-	-	(52,762)	(52,762)
Adjusted balance at 1 January 2018	100,000	158	3,815	890	(13,241)	40,280	31,902	(30,061)	101,841
Net income for the period	-	-	-	-	-	-	-	832	832
Movement in fair value of sukuk and investment securities	-	-	397	-	-	-	397	-	397
Foreign currency translation adjustments	-	-	(4)	(35)	(1,876)	-	(1,915)	-	(1,915)
At 31 March 2018 (Reviewed)	100,000	158	4,208	855	(15,117)	40,280	30,384	(29,229)	101,155

The notes 1 to 14 on pages 11 to 29 form an integral part of the interim condensed consolidated financial information.

Ithmaar Bank B.S.C. (C)**Interim condensed consolidated statement of changes in owners' equity for the three month period ended 31 March 2017**

(Expressed in thousands of Bahraini Dinars unless otherwise stated)

	Reserves					Total reserves	Retained Earnings	Total owners' equity
	Share capital	Investments fair value reserve	Investment in real estate value reserve	Foreign currency translation	Other reserves			
Balances transferred as part of reorganization (2 January 2017)	100,000	5,428	797	(8,823)	40,280	37,682	21,277	158,959
Net income for the period	-	-	-	-	-	-	1,142	1,142
Movement in fair value of sukuk and investment securities	-	(1,246)	-	-	-	(1,246)	-	(1,246)
Foreign currency translation adjustments	-	(3)	(2)	(250)	-	(255)	-	(255)
At 31 March 2017 (Reviewed)	100,000	4,179	795	(9,073)	40,280	36,181	22,419	158,600

The notes 1 to 14 on pages 11 to 29 form an integral part of the interim condensed consolidated financial information.

Ithmaar Bank B.S.C. (C)
Interim condensed consolidated statement of cash flows
(Expressed in thousands of Bahraini Dinars unless otherwise stated)

Notes	Three months ended	
	31 March 2018 (Reviewed)	31 March 2017 (Reviewed)
OPERATING ACTIVITIES		
	4,691	6,894
	2,270	2,386
8	(385)	(409)
	16	-
	6,592	8,871
	(4,645)	(424)
	(30,841)	12,025
	(14,996)	(9,696)
	(31,671)	5,924
	(3,762)	8,253
	(17,500)	10,433
	(3,569)	19,351
	19,355	(6,633)
	1,683	(43,033)
	(3,101)	(3,258)
Net cash (used in)/provided by operating activities	(82,455)	1,813
INVESTING ACTIVITIES		
	(13,884)	(8,497)
	124,002	(54,238)
	930	(695)
Net cash provided by/(used in) investing activities	111,048	(63,430)
	(6,086)	2,012
Net increase/(decrease) in cash and cash equivalents	22,507	(59,605)
Cash and cash equivalents at the beginning of the period	297,854	260,993
Cash and cash equivalents at the end of the period	320,361	201,388

The notes 1 to 14 on pages 11 to 29 form an integral part of the interim condensed consolidated financial information.

Ithmaar Bank B.S.C. (C)**Interim condensed consolidated statement of changes in restricted investment accounts
for the three month period ended 31 March 2018**

(Expressed in thousands of Bahraini Dinars unless otherwise stated)

	At 1 January 2018	Income / (Expenses)	Mudarib's Fee	Fair value movements	Net Deposits / (Redemptions)	At 31 March 2018
Dilmunia Development Fund I L.P.*	54,789	(14)	-	-	-	54,775
Shamil Bosphorus Modaraba*	2,356	-	-	-	-	2,356
European Real Estate Placements*	6,184	-	-	167	-	6,351
US Real Estate Placements*	9,514	-	-	-	-	9,514
TOTAL	72,843	(14)	-	167		72,996
Funds managed on agency basis	23,864	(18)	-	-	-	23,846
	96,707	(32)	-	167		96,842

* Income/(loss) will be recognised and distributed at the time of disposal of the underlying investments

The notes 1 to 14 on pages 11 to 29 form an integral part of the interim condensed consolidated financial information.

Ithmaar Bank B.S.C. (C)**Interim condensed consolidated statement of changes in restricted investment accounts
for the three month period ended 31 March 2017**

(Expressed in thousands of Bahraini Dinars unless otherwise stated)

	At 2 January 2017	Income / (Expenses)	Mudarib's Fee	Fair value movements	Net Deposits / (Redemptions)	At 31 March 2017
Dilmunia Development Fund I L.P.*	56,358	39	-	-	-	56,397
Shamil Bosphorus Modaraba*	2,356	-	-	-	-	2,356
European Real Estate Portfolio*	6,000	-	-	-	171	6,171
European Real Estate Placements*	6,085	83	-	64	(1,201)	5,031
US Real Estate Placements*	10,388	-	-	-	-	10,388
TOTAL	81,187	122	-	64	(1,030)	80,343
FUNDS MANAGED ON AGENCY BASIS	24,601	-	-	-	(737)	23,864
	105,788	122	-	64	(1,767)	104,207

* Income/(loss) will be recognised and distributed at the time of disposal of the underlying investments

The notes 1 to 14 on pages 11 to 29 form an integral part of the interim condensed consolidated financial information.

Ithmaar Bank B.S.C. (C)

Notes to interim condensed consolidated financial information for the three month period ended 31 March 2018

1 INCORPORATION AND ACTIVITIES

Ithmaar Bank B.S.C. (C) (the "Bank") was incorporated in the Kingdom of Bahrain on 12 May 2016 as a Closed Joint Stock entity and registered with the Ministry of Industry & Commerce under commercial registration number 99336-1 and was licensed as an Islamic retail bank by the Central Bank of Bahrain (the "CBB") on 14 August 2016.

Ithmaar Holding B.S.C.(formerly Ithmaar Bank B.S.C.) ["Ithmaar"], a Category 1 investment firm licensed and regulated by the Central Bank of Bahrain (CBB) is the ultimate parent company of the Bank.

Pursuant to the reorganisation of Ithmaar at its Extraordinary General Meeting (EGM) held on 28 March 2016 where shareholders approved to restructure Ithmaar Bank B.S.C. into a holding company and two subsidiaries to segregate core and non-core assets, all the assets and liabilities of Ithmaar were transferred to the Bank on 2 January 2017. Since Ithmaar remained the ultimate parent before and after this reorganization, this transaction has been accounted as a business combination under common control and the assets and liabilities have been transferred at their book values.

The principal activities of the Bank and its subsidiaries (collectively the "Group") are a wide range of financial services, including retail, commercial and private banking services.

The Bank's activities are supervised by the CBB and are subject to the supervision of Shari'a Supervisory Board.

The Group's activities also include acting as a Mudarib (manager, on a trustee basis), of funds deposited for investment in accordance with Islamic laws and principles particularly with regard to the prohibition of receiving or paying interest. These funds are included in the interim condensed consolidated financial information as equity of unrestricted investment accountholders and restricted investment accounts. In respect of equity of unrestricted investment accountholders, the investment accountholder authorises the Group to invest the accountholders' funds in a manner which the Group deems appropriate without laying down any restrictions as to where, how and for what purpose the funds should be invested. In respect of restricted investment accounts, the investment accountholders impose certain restrictions as to where, how and for what purpose the funds are to be invested. Further, the Group may be restricted from commingling its own funds with the funds of restricted investment accounts.

The Group carries out its business activities through the Bank's head office, 16 commercial branches in Bahrain and its following principal subsidiary companies:

	<u>% owned</u>		Country of Incorporation	Principal business activity
	Voting	Economic		
Faysal Bank Limited	67	67	Pakistan	Banking
Sakana Holistic Housing Solutions B.S.C. (C) (Sakana) [under Voluntary Liquidation]	63	50	Kingdom of Bahrain	Mortgage finance

2 SIGNIFICANT GROUP ACCOUNTING POLICIES

Except for the adoption of FAS 30 impairment and credit loss, the interim condensed consolidated financial information has been prepared using accounting policies consistent with those adopted by the Group in its consolidated financial statements for the year ended 31 December 2017, which were prepared in accordance with the Financial Accounting Standards issued by the Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI), the Shari'a rules and principles as determined by the Shari'a Supervisory Board of Ithmaar, the Bahrain Commercial Companies Law, Central Bank of Bahrain (CBB) and the Financial Institutional Law. In accordance with the requirement of AAOIFI, for matters where no AAOIFI standards exist, the Group uses the relevant International Financial Reporting Standards (IFRS).

The Group has certain assets, liabilities and related income and expenses which are not Sharia compliant as these existed before Ithmaar (the ultimate parent) converted to an Islamic retail bank in April 2010. These are currently presented in accordance with AAOIFI standards in the interim condensed consolidated financial information as appropriate.

The Sharia Supervisory Board has approved the Sharia Compliance Plan ("Plan") for assets and liabilities which are not Sharia Compliant. The Sharia Supervisory Board is monitoring the implementation of this Plan.

The interim condensed consolidated financial information have been prepared in accordance with the guidance given by the International Accounting Standard 34 – "Interim Financial Reporting". The interim condensed consolidated financial information do not contain all information and disclosures required in the annual consolidated financial statements, and should be read in conjunction with the annual consolidated financial statements as at 31 December 2017. In addition, results for the three months ended 31 March 2018 are not necessarily indicative of the results that may be expected for the financial year ending 31 December 2018.

New accounting standard: Issued and effective

Adoption of Financial Accounting Standard no. 30 – Impairment and Credit Losses

The Bank has adopted Financial Accounting Standard (FAS) 30 – Impairment and Credit Losses issued in November 2017 with a date of initial application of 1 January 2018. The requirements of FAS 30 represent a significant change in accounting for impairment and credit losses.

The key changes to the Bank's accounting policies resulting from its adoption of FAS 30 are summarized below.

FAS 30 replaces the 'incurred loss' model with an 'expected credit loss' model ("ECL"). The new impairment model also applies to certain financing commitments and financial guarantees. The allowance is based on the ECLs associated with the probability of default in the next twelve months unless there has been a significant increase in credit risk since origination in which case the allowance is based on the change in the ECLs over the life of the asset. Under FAS 30, credit losses are recognized earlier than under the previous standard.

Basis of Preparation - Measurement of the expected credit loss allowance

The measurement of the expected credit loss allowance of a receivable or exposure measured with the use of complex models and significant assumptions about future economic conditions and credit behaviour (e.g. the likelihood of customers defaulting and the resulting losses).

A number of significant judgements are also required in applying the accounting requirements for measuring ECL, such as:

- Determining the criteria for significant increase in credit risk;
- Determining the criteria for definition of default;
- Choosing appropriate models and assumptions for the measurement of ECL;
- Establishing the number and relative weightings of forward-looking scenarios for each type of product/market and the associated ECL and
- Establishing groups of similar receivables for the purpose of measuring ECL

Transition

Changes in accounting policies resulting from the adoption of FAS 30 have been applied retrospectively, except as described below.

Comparative periods have not been restated. Relevant difference in the carrying amounts of financial assets and financial liabilities resulting from the adoption of FAS 30 are recognized in retained earnings and minority interest as at 1 January 2018. Accordingly, the information presented for 2017 is not directly comparable to the information presented for 2018 under FAS 30.

Ithmaar Bank B.S.C. (C)**Notes to interim condensed consolidated financial information
for the three month period ended 31 March 2018**

(Expressed in thousands of Bahraini Dinars unless otherwise stated)

2 SIGNIFICANT GROUP ACCOUNTING POLICIES (continued)**Adoption of Financial Accounting Standard no. 30 – Impairment and Credit Losses (continued)****Reconciliation of carrying amounts as at 31 December 2017 & carrying amount as at 1st January 2018**

The following table reconciles the carrying amounts as of 31 December 2017 to the carrying amounts under FAS 30 on transition to FAS 30 on 1 January 2018.

	Carrying amount as at 31 December 2017	Re-measurement	FAS 30 carrying amount as at 1 January 2018
Financial assets - amortized cost			
Cash, Commodity and other placements with banks, financial and other institutions	362,364	(54)	362,310
Financing assets (funded & unfunded)	3,050,607	(54,193)	2,996,414
Sukuk and investment securities	483,426	(44)	483,382
Other receivables	64,185	(6,450)	57,735
Total Financial assets - amortized cost	3,960,582	(60,741)	3,899,841

*Impairment allowance is increased due to change from incurred to expected credit loss (ECL).

Impact on retained earnings and other reserves

	Retained earnings
Opening balance as at 1 January 2018	154,603
Recognition of expected credit losses under FAS 30	(52,762)
Adjusted opening balance as at 1 January 2018	101,841

Relevant differences in the carrying amounts of financial assets and financial liabilities resulting from the adoption of FAS 30 and attributable to unrestricted investment account holders amounted to BD26.5 million as of 1 January 2018. This amount has been adjusted against the balance of Investment Risk Reserve (IRR) of BD6.8 million which was attributable to unrestricted investment holders and the balance amount of BD19.7 million has been adjusted against the retained earnings attributable to shareholders based on appropriate approvals as per Bank/ Company's policy. The FAS 30 impact attributable to unrestricted investment account holders for the three month period ended 31 March 2018 was also absorbed by shareholders.

Ithmaar Bank B.S.C. (C)**Notes to interim condensed consolidated financial information
for the three month period ended 31 March 2018**

(Expressed in thousands of Bahraini Dinars unless otherwise stated)

2 SIGNIFICANT GROUP ACCOUNTING POLICIES (continued)**Adoption of Financial Accounting Standard no. 30 – Impairment and Credit Losses (continued)**

The following table reconciles the provision recorded as at 31 December 2017 to that of FAS 30 as at 1 January 2018:

	31 December		FAS 30
	2017	Re-measurement	1 January 2018
Financial assets			
Cash, Commodity and other placements with banks, financial and other institutions	-	(54)	(54)
Financing assets (funded & unfunded)	(114,796)	(54,193)	(168,989)
Sukuk and investment securities	(7,233)	(44)	(7,277)
Other receivables	(12,507)	(6,450)	(18,957)
	(134,536)	(60,741)	(195,277)

ECL – Significant increase in credit risk (SICR)

To determine whether credit risk has significantly increased since initial recognition, the Bank will compare the risk of default at the assessment date with the risk of default at initial recognition. This assessment is to be carried out at each assessment date.

For the Corporate portfolio, the Bank assess for significant increase in credit risk (SICR) at a counterparty level as the internal rating is currently carried out at a counterparty level and rating is not assigned at facility level. The Bank maintains a facility level rating being the counterparty's internal rating at date of facility origination and date of assessment.

For the Retail portfolio, the Bank currently manages its retail portfolio at a facility level, therefore assessment for SICR on the retail portfolio is done on a facility level. Days past due (DPD) of individual facilities will reflect on the counterparty SICR assessment.

Determining whether credit risk has increased significantly

In determining whether credit risk has increased significantly since initial recognition, the Bank uses its internal credit risk grading system, external risk ratings, delinquency status of accounts, restructuring, expert credit judgement and, where possible, relevant historical experience.

Using its expert credit judgment and, where possible, relevant historical experience, the Bank may determine that an exposure has undergone a significant increase in credit risk based on particular qualitative indicators that it considers are indicative of such and whose effect may not otherwise be fully reflected in its quantitative analysis on a timely basis.

The Bank considers that a significant increase in credit risk occurs no later than when an asset is more than 30 days past due. Days past due are determined by counting the number of days since the earliest elapsed due date in respect of which full payment has not been received. Due dates are determined without considering any grace period that might be available to the borrower.

The Bank monitors the effectiveness of the criteria used to identify significant increases in credit risk by regular reviews and validations.

The Bank classifies its financial instruments into stage 1, stage 2 and stage 3, based on the applied impairment methodology, as described below: -

- Stage 1: for financial instruments where there has not been a significant increase in credit risk since initial recognition and that are not credit-impaired on origination, the Bank recognises an allowance based on the 12-month ECL.
- Stage 2: for financial instruments where there has been a significant increase in credit risk since initial recognition but they are not credit-impaired, the Bank recognises an allowance for the lifetime ECL for all financings categorized in this stage based on the actual / expected maturity profile including restructuring or rescheduling of facilities.
- Stage 3: for credit-impaired financial instruments, the Bank recognises the lifetime ECL. Default identification process i.e. DPD of 90 more is used as stage 3.

Ithmaar Bank B.S.C. (C)**Notes to interim condensed consolidated financial information
for the three month period ended 31 March 2018**

(Expressed in thousands of Bahraini Dinars unless otherwise stated)

2 SIGNIFICANT GROUP ACCOUNTING POLICIES (continued)**Adoption of Financial Accounting Standard no. 30 – Impairment and Credit Losses (continued)****Default**

FAS 30 seeks to align accounting for impairment of financial instruments with the manner in which credit risk is internally managed within the banks. In this context, the 'risk of default' of a financial instrument is a key component of the expected loss model under FAS 30.

In general, counterparties with facilities exceeding 90 days past dues are considered in default.

Non-Retail:

The Bank has set out the following definition of default (as provided by the Basel document and FAS 30 guidelines):

Non-retail customers with the following characteristics:

- Rating of 8 or above from the internal rating system
- All or any of the facility/ies in which any instalment or part thereof is outstanding for a period of 90 days or more
- All or any of the facility/ies put on non-accrual status (i.e. profit suspended)
- All or any of the facility/ies wherein 'specific provision' is set aside individually
- Event driven defaults such as declaration of bankruptcy, death of borrower (in absence of succession plan or professional management), and other specific events which would significantly impact the borrower's ability the Bank.

The Bank will not consider the 90 days past due criteria in cases of technical defaults (e.g. facilities marked as 90+DPD due to administrative reasons and not credit related concerns and there is no dispute regarding repayment).

Retail:

The Bank has set out the following definition of default:

- All facilities in which any instalment or part thereof is outstanding for a period of 90 days or more

The Bank will not consider the 90 days past due criteria in cases of technical defaults (e.g. facilities marked as 90+DPD due to administrative reasons and not credit related concerns and there is no dispute regarding repayment).

Measurement of ECL

ECL is a probability-weighted estimate of credit losses. It is measured as follows:

- financial assets that are not credit-impaired at the reporting date: as the value of all cash shortfalls (i.e. the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Bank expects to receive);
- financial assets that are credit-impaired at the reporting date: as the difference between the gross carrying amount and the present value of estimated future cash flows;
- financial guarantee contracts: the expected payments to reimburse the holder less any amounts that the Bank expects to recover.

The Bank measures an ECL at an individual instrument level taking into account the projected cash flows, PD, LGD, Credit Conversion Factor (CCF) and discount rate. For portfolios wherein instrument level information is not available, the Bank carries out ECL estimation on a collective basis.

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

- i Probability of default (PD);
- ii Loss given default (LGD);
- iii Exposure at default (EAD).

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

Ithmaar Bank B.S.C. (C)

**Notes to interim condensed consolidated financial information
for the three month period ended 31 March 2018**

(Expressed in thousands of Bahraini Dinars unless otherwise stated)

2 SIGNIFICANT GROUP ACCOUNTING POLICIES (continued)

Adoption of Financial Accounting Standard no. 30 – Impairment and Credit Losses (continued)

Measurement of ECL (continued)

PD estimates are estimates at a certain date, which are calculated based on statistical rating models, and assessed using rating tools tailored to the various categories of counterparties and exposures. These statistical models are based on internally compiled data comprising both quantitative and qualitative factors. If a counterparty or exposure migrates between ratings classes, then this will lead to a change in the estimate of the associated PD.

LGD is the magnitude of the likely loss if there is a default. The Bank has internally estimated the LGD. The LGD in further will be computed based on the history of recovery rates of claims against defaulted counterparties

EAD represents the expected exposure in the event of a default. The Bank derives the EAD from the current exposure to the counterparty and potential changes to the current amount allowed under the contract including amortization. The EAD of a financial asset is its gross carrying amount. For lending commitments and financial guarantees, the EAD includes the amount currently outstanding.

The period of exposure limits the period over which possible defaults are considered and thus affects the determination of PDs and measurement of ECLs (especially for Stage 2 accounts with lifetime ECL).

Subject to using a maximum of a 12-month PD for financial assets for which credit risk has not significantly increased, the Bank measures ECL considering the risk of default over the maximum contractual period over which it is exposed to credit risk, even if, for risk management purposes, the Bank considers a longer period. The maximum contractual period extends to the date at which the Bank has the right to require repayment of an advance or terminate a loan commitment or guarantee.

Incorporation of forward looking information

The Bank incorporates forward-looking information into both its assessment of whether the credit risk of an instrument has increased significantly since its initial recognition and its measurement of ECL. The Bank annually source macro-economic forecast data from the International Monetary Fund (IMF) database for the relevant exposure country.

Macro-economic variables checked for correlation with the probability of default for the past five years and only those variables for which the movement can be explained are used. Management judgement is exercised when assessing the macroeconomic variables.

Generating the term structure of PD

Credit risk grades and days past due (DPD) are primary inputs into the determination of the term structure of PD for exposures. The Bank collects performance and default information about its credit risk exposures analyzed by type of borrower, days past due and as well as by credit risk grading.

The Bank employs statistical models to analyze the data collected and generate estimates of the remaining lifetime PD of exposures and how these are expected to change as a result of the passage of time.

This analysis includes the identification and calibration of relationships between changes in default rates and macro-economic factors as well as in-depth analysis of the impact of certain other factors (e.g. forbearance experience) on the risk of default. For most exposures, key macro-economic indicators include: GDP, Net Lending and Population.

Based on consideration of a variety of external actual and forecast information, the Bank formulates a 'base case' view of the future direction of relevant economic variables as well as a representative range of other possible forecast scenarios (i.e. on incorporation of forward-looking information). The Bank then uses these forecasts to adjust its estimates of PDs.

For Corporate portfolio, through the yearly review of the corporate portfolio, the Bank observes yearly performances to compute a count based PD over the one-year horizon for the past 5 years. These PDs are grouped as per internal risk ratings (i.e. from 1 to 7). An average default rate of the 5 yearly observed default provides the through the cycle PDs.

Ithmaar Bank B.S.C. (C)

**Notes to interim condensed consolidated financial information
for the three month period ended 31 March 2018**

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2 SIGNIFICANT GROUP ACCOUNTING POLICIES (continued)

Adoption of Financial Accounting Standard no. 30 – Impairment and Credit Losses (continued)

Generating the term structure of PD (continued)

The retail portfolio is segmented based on products that exhibit distinguished behavior into the following categories:

- Auto finance;
- Mortgage finance;
- Personal Finance and;
- Credit cards.

PDs for each segment are measured using Observed Default Estimation and thus PD is calculated based on DPD bucket level for each segment separately. Under this analysis, the delinquency status of accounts is tracked at an interval of one year with a moving month cycle. A minimum of 5 year DPD data is considered.

The PD's derived are adjusted with forward looking information based on macro-economic variables and calibrated to derive the final PD's separately for Corporate and Retail portfolio.

Impairment

The Bank recognizes loss allowances for ECL on the following type financial instruments:

- All Islamic financing and certain other assets (including Commodity and Murabaha receivables)
- Debt instruments that are measured at amortised cost or at fair value
- Financing commitments that are not measured at fair value through profit and loss (FVTPL)
- Financial guarantee contracts that are not measured at fair value through profit and loss (FVTPL)
- Lease receivables and contract assets
- Balances with banks
- Related party balances

The Bank measures loss allowances at an amount equal to lifetime ECL, except for the other financial instruments on which credit risk has not increased significantly since their initial recognition, for which ECL is measured as 12-month ECL.

12-month ECL are the portion of ECL that result from default events on a financial instrument that are possible within the 12 months after the reporting date.

Restructured financial assets

If the terms of a financial asset are renegotiated or modified or an existing financial asset is replaced with a new one due to financial difficulties of the borrower, then an assessment is made of whether the financial asset should be derecognized and ECL are measured as follows:

- If the expected restructuring will not result in derecognition of the existing asset, then the expected cash flows arising from the modified financial asset are included in calculating the cash shortfalls from the existing asset.
- If the expected restructuring will result in derecognition of the existing asset, then the expected fair value of the new asset is treated as the final cash flow from the existing financial asset at the time of its derecognition. This amount is included in calculating the cash shortfalls from the existing financial asset that are discounted from the expected date of derecognition to the reporting date using the original effective profit rate of the existing financial asset.

Ithmaar Bank B.S.C. (C)

**Notes to interim condensed consolidated financial information
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2 SIGNIFICANT GROUP ACCOUNTING POLICIES (continued)

Adoption of Financial Accounting Standard no. 30 – Impairment and Credit Losses (continued)

Credit-impaired financial assets

At each reporting date, the Bank assesses whether financial assets carried at amortized cost are credit-impaired. A financial asset is 'credit-impaired' when one or more events that have detrimental impact on the estimated future cash flows of the financial asset have occurred.

Evidence that a financial asset is credit-impaired includes the following observable events:

- significant financial difficulty of the borrower or issuer;
- a breach of contract such as a default or past due event;
- the restructuring of a loan or advance by the Bank on terms that the Bank would not consider otherwise;
- it is becoming probable that the borrower will enter bankruptcy or other financial reorganization;

Presentation of allowance for ECL in the statement of financial position

Loss allowances for ECL in case of financial assets measured at amortized cost: as a deduction from the gross carrying amount of the assets.

Write-off

The Bank's existing policy remains the same under FAS 30. Financial assets are written off either partially or in their entirety only when the Bank has stopped pursuing the recovery. If the amount to be written off is greater than the accumulated loss allowance, the difference is first treated as an addition to the allowance that is then applied against the gross carrying amount. Any subsequent recoveries are credited to credit loss expense.

The Bank writes off financial assets, in a whole or in part, when it has exhausted all practical recovery efforts and has concluded there is no reasonable expectation of recovery. Indicators that there is no reasonable expectation of recovery (i) ceasing enforcement activity and (ii) where the Bank's recovery method is foreclosing on a collateral and the value of the collateral is such that there is no reasonable expectation of recovering in full. The Bank may however write-off financial assets that are still subject to enforcement activity.

Risk Management in the Bank

The Bank's activities expose it to a variety of financial risks and those activities involve the analysis, evaluation, acceptance and management of some degree of risk or combination of risks. Taking risk is core to the banking business, and these risks are an inevitable consequence of participating in financial markets. The Bank's aim is therefore to achieve an appropriate balance between risk and return and minimize potential adverse effects on the Bank's financial performance.

The Bank's risk management policies, procedures and systems are designed to identify and analyze these risks and to set appropriate risk mitigants and controls. The Bank reviews its risk management policies and systems on an ongoing basis to reflect changes in markets, products and emerging best practices.

Risk management is performed by the Risk Management Department under policies approved by the Board of Directors. The Risk Management Department identifies and evaluates financial risks in close co-operation with the Bank's operating units. The most important types of risks identified by the Bank are credit risk, liquidity risk, market risk, reputational risk, operational risk and information security risk. Market risk includes currency risk, profit rate risk, and price risk.

Credit Risk

Credit risk is considered to be the most significant and pervasive risk for the Bank. The Bank takes on exposure to credit risk, which is the risk that the counter-party to a financial transaction will fail to discharge an obligation causing the Bank to incur a financial loss. Credit risk arises principally from financing (credit facilities provided to customers) and from cash and deposits held with other banks and financial institutions. Further, there is credit risk in certain off-balance sheet financial instruments, including guarantees, letters of credit, acceptances and commitments to extend credit. Credit risk monitoring and control is performed by the Risk Management Department which sets parameters and thresholds for the Bank's financing and off-balance sheet financial instruments.

Ithmaar Bank B.S.C. (C)**Notes to interim condensed consolidated financial information
for the three month period ended 31 March 2018**

(Expressed in thousands of Bahraini Dinars unless otherwise stated)

2 SIGNIFICANT GROUP ACCOUNTING POLICIES (continued)**Adoption of Financial Accounting Standard no. 30 – Impairment and Credit Losses (continued)****Loss allowance**

The following table sets out information about the credit quality of financial assets measured at amortized cost. Unless specifically indicated, for financial assets, the amounts in the table represent gross carrying amounts.

	Stage 1	Stage 2	Stage 3	Total
Financial assets - amortized cost				
Cash, Commodity and other placements with banks, financial and other institutions	386,639	-	-	386,639
Financings (Funded and unfunded exposure) Corporate				
Low risks (1-3)	259,611	95,786	-	355,397
Acceptable risks (4-6)	1,107,215	118,058	-	1,225,273
Watch list (7)	11,338	28,823	-	40,161
Non performing (8-10)	-	-	160,297	160,297
Carrying amount - Corporate	1,378,164	242,667	160,297	1,781,128
Retail (un-rated)	1,430,307	32,045	12,577	1,474,929
Carrying amount including unfunded	2,808,471	274,712	172,874	3,256,057
Sukuk and investment securities	426,180	-	6,918	433,098
Other receivables	67,242	3,755	6,548	77,545
Loss allowance	(45,862)	(16,443)	(130,597)	(192,902)
Total Financial assets carrying amount	3,642,670	262,024	55,743	3,960,437

Ithmaar Bank B.S.C. (C)**Notes to interim condensed consolidated financial information
for the three month period ended 31 March 2018**

(Expressed in thousands of Bahraini Dinars unless otherwise stated)

3 CASH AND BALANCES WITH BANKS AND CENTRAL BANKS

	31 March 2018			31 December 2017		
	Relating to owners	Relating to unrestricted investment accounts	Total	Relating to owners	Relating to unrestricted investment accounts	Total
Cash reserve with central banks	65,354	870	66,224	63,686	824	64,510
Cash and balances with banks and central banks	122,591	30,170	152,761	173,386	25,923	199,309
	187,945	31,040	218,985	237,072	26,747	263,819

4 COMMODITY AND OTHER PLACEMENTS WITH BANKS, FINANCIAL AND OTHER INSTITUTIONS

	31 March 2018			31 December 2017		
	Relating to owners	Relating to unrestricted investment accounts	Total	Relating to owners	Relating to unrestricted investment accounts	Total
Commodity placements	167,654	-	167,654	98,545	-	98,545
Less: Provisions	(54)	-	(54)	-	-	-
	167,600	-	167,600	98,545	-	98,545

Cash and cash equivalents for the purpose of cash flow statement are as under:

	31 March 2018			31 March 2017		
	Relating to owners	Relating to unrestricted investment accounts	Total	Relating to owners	Relating to unrestricted investment accounts	Total
Cash and balances with banks and central banks	187,945	31,040	218,985	234,703	860	235,563
Commodity and other placements with banks, financial and other institutions - net	167,600	-	167,600	27,270	-	27,270
Less: Placement maturing after ninety days	-	-	-	-	-	-
Less: Balances with central banks relating to minimum reserve requirement	(65,354)	(870)	(66,224)	(61,445)	-	(61,445)
	290,191	30,170	320,361	200,528	860	201,388

Ithmaar Bank B.S.C. (C)**Notes to interim condensed consolidated financial information
for the three month period ended 31 March 2018**

(Expressed in thousands of Bahraini Dinars unless otherwise stated)

5 MURABAHA AND OTHER FINANCINGS

	31 March 2018			31 December 2017		
	Relating to owners	Relating to unrestricted investment accounts	Total	Relating to owners	Relating to unrestricted investment accounts	Total
Murabaha and other financings	1,392,757	560,430	1,953,187	1,361,141	562,496	1,923,637
Less: Provisions	(150,624)	(13,227)	(163,851)	(108,323)	(6,473)	(114,796)
	1,242,133	547,203	1,789,336	1,252,818	556,023	1,808,841

The movement in provisions is as follows:

	31 March 2018		
	Relating to owners	Relating to unrestricted investment accounts	Total
At 1 January	(108,323)	(6,473)	(114,796)
Impact of FAS 30	(47,425)	(6,767)	(54,192)
Charge for the period	(1,601)	-	(1,601)
Write back during the period	2,040	-	2,040
Utilised during the period	21	47	68
Reclassification	1,061	(34)	1,027
Exchange differences and other movements	3,603	-	3,603
	(150,624)	(13,227)	(163,851)

Ithmaar Bank B.S.C. (C)

**Notes to interim condensed consolidated financial information
for the three month period ended 31 March 2018**

(Expressed in thousands of Bahraini Dinars unless otherwise stated)

6 SUKUK AND INVESTMENT SECURITIES

	31 March 2018			31 December 2017		
	Relating to owners	Relating to unrestricted investment accounts	Total	Relating to owners	Relating to unrestricted investment accounts	Total
Investment securities at fair value through income statement						
<i>Held for trading</i>						
Debt-type instruments – unlisted	28,942	-	28,942	114,945	-	114,945
Equity-type securities – listed	401	-	401	-	-	-
	29,343	-	29,343	114,945	-	114,945
Investment securities at fair value through equity						
Equity-type securities – listed	13,072	-	13,072	20,837	-	20,837
Equity-type securities – unlisted	2,223	-	2,223	2,323	-	2,323
	15,295	-	15,295	23,160	-	23,160
Provision for impairment	(4,144)	-	(4,144)	(4,375)	-	(4,375)
	11,151	-	11,151	18,785	-	18,785
Investment securities carried at amortised cost						
Sukuk – unlisted	6,356	86,200	92,556	6,570	87,798	94,368
Other debt-type instruments – listed	2,003	-	2,003	2,098	-	2,098
Other debt-type instruments – unlisted	338,539	-	338,539	394,193	-	394,193
	346,898	86,200	433,098	402,861	87,798	490,659
Provision for impairment	(6,962)	-	(6,962)	(7,233)	-	(7,233)
	339,936	86,200	426,136	395,628	87,798	483,426
	380,430	86,200	466,630	529,358	87,798	617,156

FAS 25 specifies a hierarchy of valuation techniques based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources; unobservable inputs reflect the Group's market assumptions. These two types of inputs have created the following fair value hierarchy:

Level 1 – Quoted prices (unadjusted) in active markets for identical investments.

Level 2 – Inputs other than quoted prices included within Level 1 that are observable for the investments, either directly (that is, as prices) or indirectly (that is, derived from prices).

Level 3 – Inputs for the investments that are not based on observable market data (unobservable inputs).

This hierarchy requires the use of observable market data when available. The Group considers relevant and observable market prices in its valuations where possible.

Ithmaar Bank B.S.C. (C)

**Notes to interim condensed consolidated financial information
for the three month period ended 31 March 2018**

(Expressed in thousands of Bahraini Dinars unless otherwise stated)

6 SUKUK AND INVESTMENT SECURITIES (continued)

Investments measured at fair value

At 31 March 2018

**Investment securities at fair value
through income statement**

	Level 1	Level 2	Level 3	Total
Debt-type instruments	-	28,942	-	28,942
Equity securities	401	-	-	401

**Investment securities at fair value
through equity**

Equity securities	10,880	271	-	11,151
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11,281	29,213	-	40,494
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Investments measured at fair value

At 31 December 2017

**Investment securities at fair value
through income statement**

Debt-type instruments	-	114,945	-	114,945
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**Investment securities at fair value
through equity**

Equity securities	18,511	274	-	18,785
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18,511	115,219	-	133,730
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Total income for the three month period included in the
interim condensed consolidated income statement

	31 March 2018	31 March 2017
	528	2,925

Ithmaar Bank B.S.C. (C)**Notes to interim condensed consolidated financial information
for the three month period ended 31 March 2018**

(Expressed in thousands of Bahraini Dinars unless otherwise stated)

7 OTHER ASSETS

	31 March 2018			31 December 2017		
	Relating to owners	Relating to unrestricted investment accounts	Total	Relating to owners	Relating to unrestricted investment accounts	Total
Accounts receivable	40,138	15,899	56,037	37,311	15,102	52,413
Due from related parties	2,923	-	2,923	3,916	-	3,916
Taxes – deferred	8,529	-	8,529	8,476	-	8,476
Taxes – current	9,492	17	9,509	10,338	-	10,338
Assets acquired against claims	6,231	1,044	7,275	6,514	-	6,514
	67,313	16,960	84,273	66,555	15,102	81,657
Provision for impairment	(13,932)	(4,585)	(18,517)	(7,887)	(4,620)	(12,507)
	53,381	12,375	65,756	58,668	10,482	69,150

8 PROVISIONS

	31 March 2018		
	Relating to owners	Relating to unrestricted investment accounts	Total
At 1 January	(141,004)	(11,094)	(152,098)
Impact of FAS 30	(53,974)	(6,767)	(60,741)
Charge for the period	(1,697)	-	(1,697)
Write back during the period	2,082	-	2,082
Utilised during the period	21	48	69
Exchange differences	4,163	-	4,163
	(190,409)	(17,813)	(208,222)

Ithmaar Bank B.S.C. (C)**Notes to interim condensed consolidated financial information
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(Expressed in thousands of Bahraini Dinars unless otherwise stated)

9 EQUITY OF UNRESTRICTED INVESTMENT ACCOUNTHOLDERS

The funds received from Unrestricted Investment Accountholders (URIA) are invested on their behalf without recourse to the Group as follows:

	31 March 2018	31 December 2017
Cash and balances with banks and central banks	31,040	26,747
Murabaha and other financings	547,203	556,023
Musharaka financing	147,384	135,374
Sukuk and investment securities	86,200	87,798
Restricted investment accounts	2,828	2,828
Assets acquired for leasing	142,532	128,642
Other assets	12,375	10,482
Due from the Bank	235,116	280,093
	1,204,678	1,227,987
Customers' current accounts	(91,031)	(107,720)
Due to banks, financial and other institutions	(17,005)	(15,220)
Other liabilities	(33,377)	(40,149)
Equity of unrestricted investment accountholders	1,063,265	1,064,898

10 SHARE CAPITAL

	Number of shares (thousands)	Share capital
Authorised	7,540,000	754,000
Issued and fully paid		
Total outstanding as at 1 January 2018	1,000,000	100,000
At 31 March 2018 (Reviewed)	1,000,000	100,000
Issued and fully paid		
Total outstanding as at 1 January 2017	1,000,000	100,000
At 31 December 2017 (Audited)	1,000,000	100,000

The Bank's total issued and fully paid share capital at 31 March 2018 comprises 1,000,000,000 shares at 100 fils per share amounting to BD100,000,000.

Ithmaar Bank B.S.C. (C)**Notes to interim condensed consolidated financial information
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11 RELATED PARTY TRANSACTIONS AND BALANCES

Parties are considered to be related if one party has the ability to control the other party or to exercise significant influence or joint control over the other party in making financial and operating decisions.

- (a) Directors and companies in which they have an ownership interest.
- (b) Major shareholders of the Bank, Ultimate Parent and companies in which Ultimate Parent has ownership interest and subsidiaries of such companies (affiliates).
- (c) Associated companies of the Bank.
- (d) Senior management.

A related party transaction is a transfer of resources, services, or obligations between related parties, regardless of whether a price is charged.

Significant balances with related parties comprise:

	31 March 2018				
	Shareholders & Affiliates	Associates and joint ventures	Directors and related entities	Senior management	Total
Assets					
Murabaha and other financings	621,710	-	4,828	-	626,538
Investment in associates	-	178	-	-	178
Other assets	2,769	-	-	154	2,923
Liabilities					
Customers' current accounts	-	7,824	-	331	8,155
Due to banks, financial and other institutions	47,599	-	-	-	47,599
Equity of unrestricted investment accounts	9,456	9,651	-	799	19,906
Other liabilities	22,514	-	-	-	22,514
Commitments	3,929	-	-	-	3,929
					31 March 2018
	Shareholders & Affiliates	Associates and joint ventures	Directors and related entities	Senior management	Total
Income					
Return to unrestricted investment accounts	80	80	1	-	161
Income from murabaha and other financings	3,489	-	-	-	3,489
Other income - Management fees	170	-	-	-	170
Profit paid to banks, financial and other institutions – net	336	282	-	-	618
Expenses					
Administrative and general expenses	54	-	-	-	54

Ithmaar Bank B.S.C. (C)**Notes to interim condensed consolidated financial information
for the three month period ended 31 March 2018**

(Expressed in thousands of Bahraini Dinars unless otherwise stated)

12 EARNINGS PER SHARE (BASIC & DILUTED)

Earnings per share (Basic & Diluted) are calculated by dividing the net income/(loss) attributable to shareholders by the weighted average number of issued and fully paid up ordinary shares during the period.

	Three month period ended	
	31 March 2018	31 March 2017
Net income attributable to shareholders (BD'000)	832	1,142
Weighted average number of issued and fully paid up ordinary shares ('000)	1,000,000	1,000,000
Earnings per share (Basic & Diluted) – Fils	0.83	1.14

13 CONTINGENT LIABILITIES AND COMMITMENTS**Contingent liabilities**

	31 December	
	31 March 2018	2017
Acceptances and endorsements	30,951	23,685
Guarantees and irrevocable letters of credit	287,498	261,777
Customer and other claims	114,190	117,547
	432,639	403,009

Commitments

	31 December	
	31 March 2018	2017
Undrawn facilities, financing lines and other commitments to finance	681,477	680,981

