

**NATIONAL BANK OF KUWAIT GROUP**  
**CONSOLIDATED FINANCIAL STATEMENTS**  
**31 DECEMBER 2020**

# Consolidated Financial Statements

Page No.

## AUDITORS' REPORT

### CONSOLIDATED FINANCIAL STATEMENTS

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## **INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF NATIONAL BANK OF KUWAIT S.A.K.P.**

### **Report on the Audit of the Consolidated Financial Statements**

#### **Opinion**

We have audited the consolidated financial statements of National Bank of Kuwait S.A.K.P. (the "Bank") and its subsidiaries (together, "the Group"), which comprise the consolidated statement of financial position as at 31 December 2020, and the consolidated statement of income, consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2020, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs), as adopted by Central Bank of Kuwait ("CBK") for use by the State of Kuwait.

#### **Basis for Opinion**

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditors' responsibilities for the Audit of the Consolidated Financial Statements* section of our report. We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants (including International Independence Standards)* (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

#### **Key Audit Matters**

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current year. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. For each key audit matter below, our description of how our audit addressed the matter is provided in that context.

**INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF NATIONAL BANK OF KUWAIT S.A.K.P. (continued)**

**Report on the Audit of the Consolidated Financial Statements (continued)**

**Key Audit Matters (continued)**

We have identified the following key audit matters:

*a) Credit losses on loans, advances and Islamic financing to customers*

The recognition of credit losses on loans, advances and Islamic financing (“credit facilities”) to customers is the higher of Expected Credit Loss (“ECL”) under International Financial Reporting Standard 9: Financial Instruments (“IFRS 9”), determined in accordance with the CBK guidelines, and the provision required by the CBK rules on classification of credit facilities and calculation of their provision (the “CBK rules”) as disclosed in the accounting policies and in Note 13 to the consolidated financial statements.

Recognition of ECL under IFRS 9, determined in accordance with CBK guidelines, is a complex accounting policy, which requires considerable judgement in its implementation. ECL is dependent on management’s judgement in assessing significant increase in credit risk and classification of credit facilities into various stages, determining when a default has occurred, development of models for assessing the probability of default of customers and estimating cash flows from recovery procedures or realization of collateral. As disclosed in Note 33, the COVID-19 global pandemic significantly impacted management’s determination of the ECL and required the application of heightened judgment. As a result, the ECL has a higher than usual degree of uncertainty and the inputs used are inherently subject to change, which may materially change the estimate in future periods.

Recognition of specific provision on impaired facility under the CBK rules is based on the instructions by CBK on the minimum provision to be recognized together with any additional provision to be recognised based on management estimate of expected cash flows related to that credit facility.

Due to the significance of credit facilities and the related estimation uncertainty and judgement in the impairment calculation, this was considered as a key audit matter. This is further heightened by the high degree of estimation uncertainty due to the economic impacts of COVID-19.

Our audit procedures included assessing the design and implementation of controls over the inputs and assumptions used by the Group in developing the models, its governance and review controls performed by the management in determining the adequacy of credit losses. Further, our audit procedures were updated to incorporate consideration of the economic disruption caused by COVID-19, including a focus on rescheduled credit facilities.

**INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF NATIONAL BANK OF KUWAIT S.A.K.P. (continued)**

**Report on the Audit of the Consolidated Financial Statements (continued)**

**Key Audit Matters (continued)**

*a) Credit losses on loans, advances and Islamic financing to customers (continued)*

With respect to the ECL based on IFRS 9, determined in accordance with the CBK guidelines, we have selected a samples of credit facilities outstanding as at the reporting date, which included rescheduled credit facilities, and checked the appropriateness of the Group's determination of significant increase in credit risk and the resultant basis for classification of the credit facilities into various stages. We involved our specialists to review the ECL model in terms of key data, methods and assumptions used to ensure they are in line with IFRS 9 requirements, determined in accordance with CBK guidelines. For a sample of credit facilities, we have checked the appropriateness of the Group's staging criteria, Exposure at Default ("EAD") Probability of Default ("PD") and Loss Given Default ("LGD") including the eligibility and value of collateral considered in the ECL models used by the Group and the overlays considered by the management in view of the ongoing COVID-19 pandemic, in order to determine ECL taking into consideration CBK guidelines. We have also checked the consistency of various inputs and assumptions used by the Group's management to determine ECL.

Further, for the CBK rules provision requirements, we have assessed the criteria for determining whether there is a requirement to calculate any credit loss in accordance with the related regulations and, if required, it has been computed accordingly. For the samples selected, which included rescheduled credit facilities, we have verified whether all impairment events have been identified by the Group's management. For the selected samples which also included impaired credit facilities, we have assessed the valuation of collateral and checked the resultant provision calculations.

*b) Impairment of goodwill and other intangible assets*

The Group has goodwill and other intangible assets with carrying value of KD 581,881 thousand as at 31 December 2020. The impairment tests of goodwill and other intangible assets performed by the management are significant to our audit because the assessment of the recoverable amount of goodwill and other intangible assets under the value-in-use basis is complex and requires considerable judgments on part of management, especially due to the ongoing COVID-19 pandemic. Estimates of future cash flows are based on management's views of variables such as the growth in the banking sector, economic conditions such as the economic growth and expected inflation rates and yield. Therefore, we identified the impairment testing of goodwill and other intangible assets as a key audit matter.

**INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF NATIONAL BANK OF KUWAIT S.A.K.P. (continued)**

**Report on the Audit of the Consolidated Financial Statements (continued)**

**Key Audit Matters (continued)**

*b) Impairment of goodwill and other intangible assets (continued)*

As part of our audit procedures, we have verified prevailing market prices where management has used these as a benchmark to compute the recoverable value. Where “value in use” is the basis to compute the recoverable value we obtained management’s impairment calculations and tested the reasonableness of key assumptions, including profit forecasts and the selection of growth rates and discount rates. We also involved our valuation specialists and challenged the management to substantiate the assumptions, including the comparison of relevant assumptions to industry benchmarks and economic forecasts. We tested the integrity of supporting calculations and corroborated certain information with third party sources. We agreed the underlying cash flows to approved budgets and assessed growth rates and discount rates by comparison with third party information, the Group’s cost of capital and relevant risk factors. Future cash flow assumptions were also assessed through comparison to current trading performance against budget and forecasts, considering the historical accuracy of budgeting and forecasting and the understanding of the reasons for growth profiles used. We further evaluated the management’s sensitivity analysis to ascertain the impact of reasonably possible changes to key assumptions.

We also assessed the adequacy of the Group’s disclosures regarding those assumptions, which are disclosed in Note 16 to the consolidated financial statements.

**Other information included in the Annual Report of the Group for the year ended 31 December 2020**

Management is responsible for the other information. Other information consists of the information included in the Annual Report of the Group for the year ended 31 December 2020, other than the consolidated financial statements and our auditors’ report thereon. We obtained the report of the Bank’s Board of Directors, prior to the date of our auditors’ report, and we expect to obtain the remaining sections of the Group’s Annual Report for the year ended 31 December 2020 after the date of our auditors’ report.

Our opinion on the consolidated financial statements does not cover the other information and we do not and will not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained during the audit, or otherwise appears to be materially misstated. If, based on the work we have performed on the other information that we obtained prior to the date of this auditors’ report, we conclude that there is a material misstatement of other information; we are required to report that fact. We have nothing to report in this regard.

## **INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF NATIONAL BANK OF KUWAIT S.A.K.P. (continued)**

### **Report on the Audit of the Consolidated Financial Statements (continued)**

#### **Responsibilities of Management and Those Charged with Governance for the Consolidated Financial Statements**

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with the IFRSs as adopted for use by the State of Kuwait, and for such internal control as management determines is necessary to enable the preparation of the consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's financial reporting process.

#### **Auditors' Responsibilities for the Audit of the Consolidated Financial Statements**

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- ▶ Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- ▶ Obtain an understanding of internal control relevant to the audit 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 Group's internal control.
- ▶ Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the management.

## **INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF NATIONAL BANK OF KUWAIT S.A.K.P. (continued)**

### **Report on the Audit of the Consolidated Financial Statements (continued)**

#### **Auditors' Responsibilities for the Audit of the Consolidated Financial Statements (continued)**

- ▶ Conclude on the appropriateness of management's use of the going concern basis of accounting and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- ▶ Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- ▶ Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate to those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, actions taken to eliminate threats or safeguards applied.

From the matters communicated to those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current year and are therefore the key audit matters. We describe these matters in our auditors' report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

**INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF NATIONAL BANK OF KUWAIT S.A.K.P. (continued)**

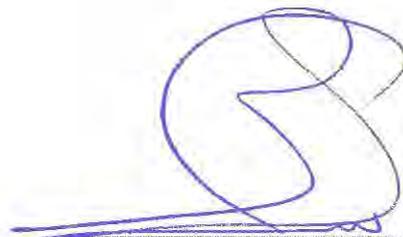
**Report on Other Legal and Regulatory Requirements**

Furthermore, in our opinion proper books of account have been kept by the Bank and the consolidated financial statements, together with the contents of the report of the Bank's Board of Directors relating to these consolidated financial statements, are in accordance therewith. We further report that we obtained all the information and explanations that we required for the purpose of our audit and that the consolidated financial statements incorporate all information that is required by the Capital Adequacy Regulations and Financial Leverage Ratio Regulations issued by the Central Bank of Kuwait ("CBK") as stipulated in CBK Circular Nos. 2/RB, RBA/336/2014 dated 24 June 2014 and its amendments, and 2/BS/342/2014 dated 21 October 2014, and its amendments, respectively, the Companies Law No. 1 of 2016, as amended, and its executive regulations, as amended, or by the Bank's Memorandum of Incorporation and Articles of Association, as amended, that an inventory was duly carried out and that, to the best of our knowledge and belief, no violations of the Capital Adequacy Regulations and Financial Leverage Ratio Regulations issued by the CBK as stipulated in CBK Circular Nos. 2/RB, RBA/336/2014 dated 24 June 2014 and its amendments, and 2/BS/342/2014 dated 21 October 2014, and its amendments, respectively, the Companies Law No. 1 of 2016, as amended, and its executive regulations, as amended, or of the Bank's Memorandum of Incorporation and Articles of Association, as amended, have occurred during the year ended 31 December 2020 that might have had a material effect on the business of the Bank or on its financial position.

We further report that, during the course of our audit, we have not become aware of any violations of the provisions of Law No. 32 of 1968, as amended, concerning currency, the CBK and the organisation of banking business, and its related regulations during the year ended 31 December 2020 that might have had a material effect on the business of the Bank or on its financial position.



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26 January 2021  
Kuwait

National Bank of Kuwait Group

CONSOLIDATED STATEMENT OF INCOME

For the year ended 31 December 2020

|  | Notes | 2020<br>KD 000's | 2019<br>KD 000's |
|--|-------|------------------|------------------|
| Interest income  | 4     | 756,984          | 986,526          |
| Interest expense   | 5     | 266,752          | 421,618          |
| <b>Net interest income</b>   |       | <b>490,232</b>   | <b>564,908</b>   |
| Murabaha and other Islamic financing income                                      |       | 225,137          | 211,317          |
| Finance cost and Distribution to depositors                                      |       | 81,902           | 87,001           |
| <b>Net income from Islamic financing</b>   |       | <b>143,235</b>   | <b>124,316</b>   |
| <b>Net interest income and net income from Islamic financing</b>                 |       | <b>633,467</b>   | <b>689,224</b>   |
| Net fees and commissions   | 6     | 145,981          | 157,152          |
| Net investment income  | 7     | 2,041            | 8,419            |
| Net gains from dealing in foreign currencies                                     |       | 38,159           | 39,343           |
| Other operating income   | 8     | 22,873           | 1,379            |
| <b>Non-interest income</b>   |       | <b>209,054</b>   | <b>206,293</b>   |
| <b>Net operating income</b>  |       | <b>842,521</b>   | <b>895,517</b>   |
| Staff expenses   |       | 174,442          | 175,731          |
| Other administrative expenses  |       | 102,058          | 98,852           |
| Depreciation of premises and equipment   |       | 33,432           | 26,493           |
| Amortisation of intangible assets  | 16    | 1,647            | 3,198            |
| <b>Operating expenses</b>  |       | <b>311,579</b>   | <b>304,274</b>   |
| <b>Operating profit before provision for credit losses and impairment losses</b> |       | <b>530,942</b>   | <b>591,243</b>   |
| <b>Provision charge for credit losses and impairment losses</b>                  | 9     | <b>246,438</b>   | <b>129,715</b>   |
| <b>Operating profit before taxation</b>  |       | <b>284,504</b>   | <b>461,528</b>   |
| Taxation   | 10    | 25,842           | 35,536           |
| <b>Profit for the year</b>   |       | <b>258,662</b>   | <b>425,992</b>   |
| Attributable to:   |       |                  |                  |
| Shareholders of the Bank   |       | 246,341          | 401,291          |
| Non-controlling interests  |       | 12,321           | 24,701           |
|  |       | <b>258,662</b>   | <b>425,992</b>   |
| <b>Basic earnings per share attributable to shareholders of the Bank</b>         | 11    | <b>32 fils</b>   | <b>57 fils</b>   |

The attached notes 1 to 33 form part of these consolidated financial statements.

National Bank of Kuwait Group

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2020

|  | <i>Note</i> | <b>2020</b><br><b>KD 000's</b> | <b>2019</b><br><b>KD 000's</b> |
|--|-------------|--------------------------------|--------------------------------|
| <b>Profit for the year</b>   |             | <b>258,662</b>                 | <b>425,992</b>                 |
| <b>Other comprehensive income:</b>   |             |                                |                                |
| Investment in debt securities measured at FVOCI:   |             |                                |                                |
| Net change in fair value   |             | <b>(36,568)</b>                | 50,791                         |
| Net transfer to consolidated statement of income   |             | <b>12,578</b>                  | 5,440                          |
|  |             | <b>(23,990)</b>                | 56,231                         |
| Share of other comprehensive (loss) income of associates   |             | <b>(291)</b>                   | 158                            |
| Exchange differences on translation of foreign operations  |             | <b>(2,431)</b>                 | 19,066                         |
| <b>Other comprehensive (loss) income for the year reclassifiable to consolidated statement of income in subsequent years</b> |             | <b>(26,712)</b>                | 75,455                         |
| Net loss on investments in equity instruments designated at FVOCI  |             | <b>(7,566)</b>                 | (15,801)                       |
| Actuarial loss in respect of defined benefit plans   | 19          | <b>(7,239)</b>                 | -                              |
| <b>Other comprehensive loss for the year not reclassifiable to consolidated statement of income in subsequent years</b>      |             | <b>(14,805)</b>                | (15,801)                       |
| <b>Other comprehensive (loss) income for the year</b>  |             | <b>(41,517)</b>                | 59,654                         |
| <b>Total comprehensive income for the year</b>   |             | <b>217,145</b>                 | <b>485,646</b>                 |
| <b>Attributable to:</b>  |             |                                |                                |
| Shareholders of the Bank   |             | <b>209,935</b>                 | 462,211                        |
| Non-controlling interests  |             | <b>7,210</b>                   | 23,435                         |
|  |             | <b>217,145</b>                 | <b>485,646</b>                 |

The attached notes 1 to 33 form part of these consolidated financial statements.

# National Bank of Kuwait Group

## CONSOLIDATED STATEMENT OF FINANCIAL POSITION

As at 31 December 2020

|  | Notes | 2020<br>KD 000's  | 2019<br>KD 000's  |
|--|-------|-------------------|-------------------|
| <b>Assets</b>                                      |       |                   |                   |
| Cash and short term funds                          | 12    | 3,903,371         | 3,787,173         |
| Central Bank of Kuwait bonds                       | 14    | 830,233           | 823,229           |
| Kuwait Government treasury bonds                   | 14    | 462,922           | 662,175           |
| Deposits with banks                                |       | 1,027,373         | 1,909,081         |
| Loans, advances and Islamic financing to customers | 13    | 17,504,342        | 16,552,598        |
| Investment securities                              | 14    | 4,728,778         | 4,214,562         |
| Investment in associates                           | 15    | 5,195             | 35,297            |
| Land, premises and equipment                       |       | 426,963           | 433,540           |
| Goodwill and other intangible assets               | 16    | 581,881           | 582,927           |
| Other assets                                       | 17    | 246,333           | 270,171           |
| <b>Total assets</b>                                |       | <b>29,717,391</b> | <b>29,270,753</b> |
| <b>Liabilities</b>                                 |       |                   |                   |
| Due to banks and other financial institutions      |       | 5,981,573         | 7,581,929         |
| Customer deposits                                  |       | 17,104,232        | 15,930,577        |
| Certificates of deposit issued                     |       | 918,862           | 538,611           |
| Other borrowed funds                               | 18    | 808,665           | 351,960           |
| Other liabilities                                  | 19    | 763,004           | 608,516           |
| <b>Total liabilities</b>                           |       | <b>25,576,336</b> | <b>25,011,593</b> |
| <b>Equity</b>                                      |       |                   |                   |
| Share capital                                      | 20    | 685,019           | 652,399           |
| Proposed bonus shares                              | 21    | 34,250            | 32,620            |
| Statutory reserve                                  | 20    | 342,511           | 326,199           |
| Share premium account                              | 20    | 803,028           | 803,028           |
| Treasury shares                                    | 20    | -                 | (39,258)          |
| Treasury share reserve                             | 20    | 34,961            | 25,115            |
| Other reserves                                     | 20    | 1,410,240         | 1,633,641         |
| Equity attributable to shareholders of the Bank    |       | 3,310,009         | 3,433,744         |
| Perpetual Tier 1 Capital Securities                | 22    | 438,438           | 438,438           |
| Non-controlling interests                          | 25    | 392,608           | 386,978           |
| <b>Total equity</b>                                |       | <b>4,141,055</b>  | <b>4,259,160</b>  |
| <b>Total liabilities and equity</b>                |       | <b>29,717,391</b> | <b>29,270,753</b> |

  
Nasser Musaed Abdullah Al-Sayer  
Chairman

  
Isam J. Al Sager  
Group Chief Executive Officer

# National Bank of Kuwait Group

## CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended 31 December 2020

|   | Notes | 2020<br>KD 000's        | 2019<br>KD 000's        |
|---|-------|-------------------------|-------------------------|
| <b>Operating activities</b>   |       |                         |                         |
| Profit for the year   |       | 258,662                 | 425,992                 |
| Adjustments for:  |       |                         |                         |
| Net investment income   | 7     | (2,041)                 | (8,419)                 |
| Depreciation of premises and equipment  |       | 33,432                  | 26,493                  |
| Amortisation of intangible assets   | 16    | 1,647                   | 3,198                   |
| Provision charge for credit losses and impairment losses                                | 9     | 246,438                 | 129,715                 |
| Taxation  | 10    | 25,842                  | 35,536                  |
| Gain on sale of land, premises and equipment  | 8     | (12,715)                | -                       |
| Cash flows from operating activities before changes in operating assets and liabilities |       | <u>551,265</u>          | <u>612,515</u>          |
| Changes in operating assets and liabilities:  |       |                         |                         |
| Central Bank of Kuwait bonds  |       | (7,004)                 | (13,358)                |
| Kuwait Government treasury bonds  |       | 199,253                 | 209,867                 |
| Deposits with banks   |       | 871,020                 | 455,161                 |
| Loans, advances and Islamic financing to customers                                      |       | (675,727)               | (1,172,262)             |
| Other assets  |       | 35,139                  | (12,387)                |
| Due to banks and other financial institutions   |       | (1,688,002)             | (508,555)               |
| Customer deposits   |       | 777,774                 | 1,541,741               |
| Certificates of deposit issued  |       | 380,251                 | 87,483                  |
| Other liabilities   |       | (89,994)                | 133,221                 |
| Tax paid  |       | (36,128)                | (32,702)                |
| Net cash from operating activities  |       | <u>317,847</u>          | <u>1,300,724</u>        |
| <b>Investing activities</b>   |       |                         |                         |
| Purchase of investment securities   |       | (2,020,261)             | (1,577,001)             |
| Proceeds from sale/redemption of investment securities                                  |       | 1,617,668               | 1,079,220               |
| Dividend income   | 7     | 907                     | 2,685                   |
| Proceeds from sale of investment in associate   |       | 694                     | -                       |
| Dividend from associates  |       | 36                      | 153                     |
| Proceeds from sale of land, premises and equipment                                      |       | 34,995                  | 846                     |
| Purchase of land, premises and equipment  |       | (38,848)                | (57,935)                |
| Acquisition of subsidiary net of cash acquired  | 26    | (325)                   | -                       |
| Transaction costs related to acquisition of a subsidiary                                | 26    | (1,815)                 | -                       |
| Increase in holding in subsidiaries   |       | -                       | (1,685)                 |
| Net cash used in investing activities   |       | <u>(406,949)</u>        | <u>(553,717)</u>        |
| <b>Financing activities</b>   |       |                         |                         |
| Net proceeds from issue of Perpetual Tier 1 Capital Securities                          | 22    | -                       | 226,857                 |
| Net proceeds from issue of subordinated Tier 2 bonds                                    | 18    | 116,620                 | -                       |
| Proceeds from issuance of Sukuk by a subsidiary   | 18    | 228,600                 | -                       |
| Other borrowings  | 18    | 75,796                  | -                       |
| Proceeds from sale of treasury shares   |       | 49,104                  | 37,272                  |
| Dividends paid  |       | (226,373)               | (214,344)               |
| Interest paid on Perpetual Tier 1 Capital Securities                                    |       | (22,796)                | (12,258)                |
| Profit distribution on Perpetual Tier 1 Sukuk by a subsidiary                           |       | (5,186)                 | (5,125)                 |
| Capital increase in a subsidiary contributed by non-controlling interest                |       | -                       | 49,615                  |
| Dividends paid by subsidiaries to non-controlling interests                             |       | (10,465)                | (8,558)                 |
| Net cash from financing activities  |       | <u>205,300</u>          | <u>73,459</u>           |
| <b>Increase in cash and short term funds</b>  |       | <b>116,198</b>          | <b>820,466</b>          |
| Cash and short term funds at the beginning of the year                                  |       | <u>3,787,173</u>        | <u>2,966,707</u>        |
| <b>Cash and short term funds at the end of the year</b>                                 | 12    | <u><u>3,903,371</u></u> | <u><u>3,787,173</u></u> |

The attached notes 1 to 33 form part of these consolidated financial statements.

National Bank of Kuwait Group

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2020

KD 000's

|   | <i>Equity attributable to shareholders of the Bank</i> |                              |                          |                              |                        |                               |                                  | <i>Total</i>     | <i>Perpetual Tier 1 Capital Securities</i> | <i>Non - controlling interests</i> | <i>Total equity</i> |
|---|--|------------------------------|--------------------------|------------------------------|------------------------|-------------------------------|----------------------------------|------------------|--|------------------------------------|---------------------|
|   | <i>Share capital</i>                                   | <i>Proposed bonus shares</i> | <i>Statutory reserve</i> | <i>Share premium account</i> | <i>Treasury shares</i> | <i>Treasury share reserve</i> | <i>Other reserves (Note 20e)</i> |                  |  |                                    |                     |
| Balance as at 1 January 2020                                  | 652,399  | 32,620                       | 326,199                  | 803,028                      | (39,258)               | 25,115                        | 1,633,641                        | 3,433,744        | 438,438                                    | 386,978                            | 4,259,160           |
| Profit for the year   | -  | -                            | -                        | -                            | -                      | -                             | 246,341                          | 246,341          | -  | 12,321                             | 258,662             |
| Other comprehensive loss                                      | -  | -                            | -                        | -                            | -                      | -                             | (36,406)                         | (36,406)         | -  | (5,111)                            | (41,517)            |
| <b>Total comprehensive income</b>                             | -  | -                            | -                        | -                            | -                      | -                             | 209,935                          | 209,935          | -  | 7,210                              | 217,145             |
| Transfer to statutory reserve (Note 20b)                      | -  | -                            | 16,312                   | -                            | -                      | -                             | (16,312)                         | -                | -  | -                                  | -                   |
| Issue of bonus shares (Note 20a)                              | 32,620   | (32,620)                     | -                        | -                            | -                      | -                             | -                                | -                | -  | -                                  | -                   |
| Dividends paid  | -  | -                            | -                        | -                            | -                      | -                             | (226,373)                        | (226,373)        | -  | -                                  | (226,373)           |
| Interest paid on perpetual Tier 1 Capital Securities          | -  | -                            | -                        | -                            | -                      | -                             | (22,796)                         | (22,796)         | -  | -                                  | (22,796)            |
| Sale of treasury shares                                       | -  | -                            | -                        | -                            | 39,258                 | 9,846                         | -                                | 49,104           | -  | -                                  | 49,104              |
| Dividend paid by subsidiaries to non-controlling Interests    | -  | -                            | -                        | -                            | -                      | -                             | -                                | -                | -  | (10,465)                           | (10,465)            |
| Profit distribution on Perpetual Tier 1 Sukuk by a subsidiary | -  | -                            | -                        | -                            | -                      | -                             | (3,106)                          | (3,106)          | -  | (2,080)                            | (5,186)             |
| Proposed bonus shares (Note 21)                               | -  | 34,250                       | -                        | -                            | -                      | -                             | (34,250)                         | -                | -  | -                                  | -                   |
| Acquisition of subsidiaries (Note 26)                         | -  | -                            | -                        | -                            | -                      | -                             | -                                | -                | -  | 30,582                             | 30,582              |
| Modification loss on deferral of loans instalments (Note 33)  | -  | -                            | -                        | -                            | -                      | -                             | (130,499)                        | (130,499)        | -  | (19,347)                           | (149,846)           |
| Other movements   | -  | -                            | -                        | -                            | -                      | -                             | -                                | -                | -  | (270)                              | (270)               |
| <b>At 31 December 2020</b>                                    | <b>685,019</b>   | <b>34,250</b>                | <b>342,511</b>           | <b>803,028</b>               | <b>-</b>               | <b>34,961</b>                 | <b>1,410,240</b>                 | <b>3,310,009</b> | <b>438,438</b>                             | <b>392,608</b>                     | <b>4,141,055</b>    |

The attached notes 1 to 33 form part of these consolidated financial statements.

# National Bank of Kuwait Group

## CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2020

KD 000's

|   | <i>Equity attributable to shareholders of the Bank</i> |                              |                          |                              |                        |                               |                                  | <i>Perpetual Tier 1 Capital Securities</i> | <i>Non - controlling interests</i> | <i>Total equity</i> |                  |
|---|--|------------------------------|--------------------------|------------------------------|------------------------|-------------------------------|----------------------------------|--|------------------------------------|---------------------|------------------|
|   | <i>Share capital</i>                                   | <i>Proposed bonus shares</i> | <i>Statutory reserve</i> | <i>Share premium account</i> | <i>Treasury shares</i> | <i>Treasury share reserve</i> | <i>Other reserves (Note 20e)</i> |  |                                    |                     | <i>Total</i>     |
| Balance as at 1 January 2019                                      | 621,332  | 31,067                       | 310,666                  | 803,028                      | (65,425)               | 14,010                        | 1,448,579                        | 3,163,257                                  | 210,700                            | 327,353             | 3,701,310        |
| Profit for the year   | -  | -                            | -                        | -                            | -                      | -                             | 401,291                          | 401,291                                    | -                                  | 24,701              | 425,992          |
| Other comprehensive income (loss)                                 | -  | -                            | -                        | -                            | -                      | -                             | 60,920                           | 60,920                                     | -                                  | (1,266)             | 59,654           |
| <b>Total comprehensive income</b>                                 | -  | -                            | -                        | -                            | -                      | -                             | 462,211                          | 462,211                                    | -                                  | 23,435              | 485,646          |
| Transfer to statutory reserve (Note 20b)                          | -  | -                            | 15,533                   | -                            | -                      | -                             | (15,533)                         | -  | -                                  | -                   | -                |
| Issue of bonus shares (Note 20a)                                  | 31,067   | (31,067)                     | -                        | -                            | -                      | -                             | -                                | -  | -                                  | -                   | -                |
| Sale of treasury shares   | -  | -                            | -                        | -                            | 26,167                 | 11,105                        | -                                | 37,272                                     | -                                  | -                   | 37,272           |
| Dividends paid  | -  | -                            | -                        | -                            | -                      | -                             | (214,344)                        | (214,344)                                  | -                                  | -                   | (214,344)        |
| Issue of Perpetual Tier 1 Capital Securities (Note 22)            | -  | -                            | -                        | -                            | -                      | -                             | -                                | -  | 227,738                            | -                   | 227,738          |
| Transaction costs on issue of Perpetual Tier 1 Capital Securities | -  | -                            | -                        | -                            | -                      | -                             | (881)                            | (881)                                      | -                                  | -                   | (881)            |
| Interest paid on perpetual Tier 1 Capital Securities              | -  | -                            | -                        | -                            | -                      | -                             | (12,258)                         | (12,258)                                   | -                                  | -                   | (12,258)         |
| Dividend paid by subsidiaries to non-controlling Interests        | -  | -                            | -                        | -                            | -                      | -                             | -                                | -  | -                                  | (8,558)             | (8,558)          |
| Profit distribution on Perpetual Tier 1 Sukuk by a subsidiary     | -  | -                            | -                        | -                            | -                      | -                             | (3,069)                          | (3,069)                                    | -                                  | (2,056)             | (5,125)          |
| Proposed bonus shares (Note 21)                                   | -  | 32,620                       | -                        | -                            | -                      | -                             | (32,620)                         | -  | -                                  | -                   | -                |
| Increase in holding in subsidiaries                               | -  | -                            | -                        | -                            | -                      | -                             | 1,702                            | 1,702                                      | -                                  | (7,075)             | (5,373)          |
| Capital increase in a subsidiary                                  | -  | -                            | -                        | -                            | -                      | -                             | -                                | -  | -                                  | 53,303              | 53,303           |
| Other movements   | -  | -                            | -                        | -                            | -                      | -                             | (146)                            | (146)                                      | -                                  | 576                 | 430              |
| <b>At 31 December 2019</b>  | <b>652,399</b>   | <b>32,620</b>                | <b>326,199</b>           | <b>803,028</b>               | <b>(39,258)</b>        | <b>25,115</b>                 | <b>1,633,641</b>                 | <b>3,433,744</b>                           | <b>438,438</b>                     | <b>386,978</b>      | <b>4,259,160</b> |

The attached notes 1 to 33 form part of these consolidated financial statements.

## 1 INCORPORATION AND REGISTRATION

The consolidated financial statements of National Bank of Kuwait S.A.K.P. (the "Bank") and its subsidiaries (collectively the "Group") for the year ended 31 December 2020 were authorised for issue in accordance with a resolution of the directors on 10 January 2021. The Annual General Assembly of the shareholders has the power to amend these consolidated financial statements after issuance. The Bank is a public shareholding company incorporated in Kuwait in 1952 and is registered as a bank (commercial registration number - 8490) with the Central Bank of Kuwait. The Bank's registered office is at Al Shuhada Street, P.O. Box 95, Safat 13001, Kuwait. The principal activities of the Bank are described in Note 3.

## 2 SIGNIFICANT ACCOUNTING POLICIES

### 2.1 Basis of preparation

The consolidated financial statements have been prepared in accordance with the regulations for financial services institutions as issued by the Central Bank of Kuwait (CBK) in the State of Kuwait. These regulations, including the recently issued CBK circulars on regulatory measures in response to COVID-19 and related CBK communications, require banks and other financial institutions regulated by CBK to adopt the International Financial Reporting Standards with the following amendments:

- (a) Expected credit loss ("ECL") on credit facilities to be measured at the higher of ECL computed under IFRS 9 in accordance to the CBK guidelines or the provisions as required by CBK instructions along with its consequent impact on related disclosures; and
- (b) Modification losses on financial assets (consumer and other instalment loans and credit card receivables) arising from payment holidays to customers in response to Covid-19 to be recognized in retained earnings, instead of consolidated statement of income as required by IFRS 9 (note 33).

The above framework is hereinafter referred to as 'IFRS as adopted by CBK for use by the State of Kuwait.

The consolidated financial statements are prepared under the historical cost convention except for the measurement at fair value of derivatives, investment securities measured at fair value and investment properties. In addition and as more fully described below, assets and liabilities that are hedged in fair value hedging relationships are carried at fair value to the extent of the risk being hedged.

### 2.2 Changes in accounting policies

#### New and amended standards and interpretations

The Group applied the following amendments effective from 1 January 2020. The Group has not early adopted any other standard, interpretation or amendment that has been issued but is not yet effective.

#### *Amendments to IFRS 16 Covid-19 Related Rent Concessions*

On 28 May 2020, the IASB issued Covid-19-Related Rent Concessions - amendment to IFRS 16 Leases. The amendments provide relief to lessees from applying IFRS 16 guidance on lease modification accounting for rent concessions arising as a direct consequence of the Covid-19 pandemic. As a practical expedient, a lessee may elect not to assess whether a Covid-19 related rent concession from a lessor is a lease modification. A lessee that makes this election accounts for any change in lease payments resulting from the Covid-19 related rent concession the same way it would account for the change under IFRS 16, if the change were not a lease modification. The amendment applies to annual reporting periods beginning on or after 1 June 2020. Earlier application is permitted. This amendment does not have a material impact on the consolidated financial statements of the Group.

#### *IBOR Transition (Interest Rate Benchmark Reforms):*

The Group adopted Interest Rate Benchmark Reform – Amendments to IFRS 9, IAS 39 and IFRS 7 (IBOR reform Phase 1) with effect from 1 January 2020. IBOR reform Phase 1 provides a number of reliefs, which apply to all hedging relationships that are directly affected by interest rate benchmark reform. Such reliefs permits the Group to assume that hedging relationships are unaffected by the uncertainties caused by IBOR reform. This includes assuming that hedged cash flows are not altered as a result of IBOR reform. Also, the reliefs allow the Group to not discontinue hedging relationships as a result of retrospective or prospective ineffectiveness. IBOR Reform Phase 1 also requires additional disclosures in relation to those hedging relationships to which the reliefs are applied.

Other amendments to IFRSs which are effective for annual accounting period starting from 1 January 2020 did not have any material impact on the accounting policies, financial position or performance of the Group.

**2 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2.2 Changes in accounting policies (continued)**

**Standards issued but not yet effective**

The new and amended standards and interpretations that are issued, but not yet effective, up to the date of issuance of the Group's consolidated financial statements are disclosed below. The Group intends to adopt these standards, if applicable, when they become effective.

*Interest Rate Benchmark Reform - Phase 2 Amendments to IFRS 9, IAS 39 IFRS 7, IFRS 4 and IFRS 16*

In August 2020 the IASB issued Interest Rate Benchmark Reform - Phase 2 Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16, (IBOR reform Phase 2) to address the accounting issues which arise upon the replacement of an IBOR with a risk-free rate ("RFR").

IBOR reform Phase 2 includes a number of reliefs and additional disclosures. The reliefs apply upon the transition of a financial instrument from an IBOR to RFR. As a practical expedient, changes to the basis for determining contractual cash flows as a result of interest rate benchmark reform are required to be treated as changes to a floating interest rate, provided that, for the financial instrument, the transition from the IBOR benchmark rate to RFR takes place on an economically equivalent basis.

IBOR reform Phase 2 provides temporary reliefs that allow the Group's hedging relationships to continue upon the replacement of an existing interest rate benchmark with an RFR. The reliefs require the Group to amend hedge designations and hedge documentation. This includes redefining the hedged risk to reference an RFR, redefining the description of the hedging instrument and / or the hedged item to reference the RFR and amending the method for assessing hedge effectiveness. Updates to the hedging documentation must be made by the end of the reporting period in which a replacement takes place.

The Group is currently assessing the impact of transition and will apply IBOR reform Phase 2 when it becomes applicable. The Group continues to engage with various stakeholders to support an orderly transition. The project is significant in terms of scale and complexity and will impact products, internal systems and processes.

**2.3 Basis of consolidation**

The consolidated financial statements comprise the financial statements of the Bank as at 31 December each year and its subsidiaries as at the same date or a date not earlier than three months from 31 December. The financial statements of subsidiaries and associates are prepared using consistent accounting policies and are adjusted, where necessary, to bring the accounting policies in line with those of the Group. All intercompany balances and transactions, including unrealised profits arising from intra-group transactions have been eliminated on consolidation.

*a. Subsidiaries*

Subsidiaries are all entities over which the Bank has control. The control is achieved when the Bank is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. The Group re-assesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control. Consolidation of a subsidiary begins when the Group obtains control over the subsidiary and ceases when the Group loses control of the subsidiary. Refer Note 25 for the list of major subsidiaries, their principal businesses and the Group's effective holding.

*b. Non-controlling interest*

Interest in the equity of subsidiaries not attributable to the Group is reported as non-controlling interest in the consolidated statement of financial position. Non-controlling interest in the acquiree is measured at the proportionate share in the recognised amounts of the acquiree's identifiable net assets. Losses are allocated to the non-controlling interest even if they exceed the non-controlling interest's share of equity in the subsidiary. Transactions with non-controlling interests are treated as transactions with equity owners of the Group. Gains or losses on changes in non-controlling interests without loss of control are recorded in equity.

**2 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2.3 Basis of consolidation (continued)**

*c. Associates*

Associates are all entities over which the Group has significant influence but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights. Investment in an associate is initially recognised at cost and subsequently accounted for by the equity method of accounting. The Group's investment in associates includes goodwill identified on acquisition. The Group's share of its associates' post-acquisition profits or losses is recognised in the consolidated statement of income, and its share of post-acquisition movements in other comprehensive income is recognised in other comprehensive income. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment.

The Group determines at each reporting date whether there is any objective evidence that the investment in the associate is impaired. If this is the case, the Group calculates the amount of impairment as the difference between the recoverable amount of the associate and its carrying value and recognises the amount in the consolidated statement of income. Upon loss of significant influence over the associate, the Group measures and recognises any retained investment at its fair value. Gain or loss on this transaction is computed by comparing the carrying amount of the associate at the time of loss of significant influence with the aggregate of fair value of the retained investment and proceeds from disposal. This is recognised in the consolidated statement of income.

**2.4 Foreign currencies**

The consolidated financial statements are presented in Kuwaiti Dinars (thousands) which is also the Bank's functional currency.

*a. Translation of foreign currency transactions*

Transactions in foreign currencies are initially recorded in the functional currency rate of exchange ruling at the date of the transaction. Monetary assets and monetary liabilities in foreign currencies (other than monetary items that form part of the net investment in a foreign operation) are translated into functional currency at rates of exchange prevailing at the reporting date. Any gains or losses are taken to the consolidated statement of income. Exchange differences arising on monetary items that form part of the net investment in a foreign operation are determined using closing rates and recognised in other comprehensive income and presented in the foreign currency translation reserve in equity. When a foreign operation is disposed of, the cumulative amount in foreign currency translation reserve relating to that foreign operation is recognised in the consolidated statement of income. Goodwill, intangible assets and any fair value adjustments to the carrying value of assets and liabilities are recorded at the functional currency of the foreign operation and are translated to the presentation currency at the rate of exchange prevailing at the reporting date. All resulting exchange differences are recognised in other comprehensive income and accumulated in foreign currency translation reserve within equity.

Translation gains or losses on non-monetary items are recognised in other comprehensive income when non-monetary items are measured at fair value through other comprehensive income. Translation gains or losses on non-monetary items measured at fair value through profit or loss are recognised in consolidated statement of income.

*b. Translation of financial statements of foreign entities*

The results and financial position of all the Group entities that have a functional currency different from the presentation currency are translated to presentation currency as follows:

The assets and liabilities are translated at rates of exchange ruling at the reporting date. Income and expense items are translated at average exchange rates for the year. All resulting exchange differences are recognised in other comprehensive income and accumulated in foreign currency translation reserve within equity and duly recognised in the consolidated statement of income on disposal of the foreign operation.

**2.5 Interest income and expenses**

Interest income and expense for all interest-bearing financial instruments are recognised within 'interest income' and 'interest expense' in the consolidated statement of income using the effective interest method. The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period.

The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. Fees which are considered as an integral part of the effective yield of a financial asset are recognised using effective yield method. Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

**2 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2.6 Murabaha and other Islamic financing income**

Income from Murabaha, Wakala and Leased assets is recognized on a pattern reflecting a constant periodic return on the outstanding net investment.

**2.7 Fees and commissions income**

Fees and commission income are recognised when the Group satisfies the performance obligation by transferring the promised service to customers. At inception of the contract, the Group determines whether it satisfies the performance obligation over a period of time or at a point in time. Fees income earned from services provided over a period of time is recognised over the period of service. Fees and commissions arising from providing a transaction service are recognised at a point in time on completion of the underlying transaction. Portfolio and other management advisory and service fees are recognised based on the applicable service contracts, usually on a time-apportioned basis. Asset management fees related to investment funds are recognised over the period in which the service is provided. The same principle is applied for wealth management and custody services that are continuously provided over an extended period of time.

**2.8 Dividend income**

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

**2.9 Government grants**

Government grants are recognised where there is reasonable assurance that the grant will be received and all attached conditions will be complied with. When the grant relates to an expense item, it is recognised as income on a systematic basis over the periods that the related costs, for which it is intended to compensate, are expensed. When the grant relates to an asset, it is recognised as income in equal amounts over the expected useful life of the related asset.

**2.10 Impairment of financial assets**

The Group computes Expected Credit Losses (ECL) on the following financial instruments that are not measured at fair value through profit or loss:

- loans and advances, Islamic financing to customers including credit commitments
- letters of credit and financial guarantee contracts including commitments
- investment in debt securities measured at amortised cost or FVOCI
- balances and deposits with banks

Equity investments are not subject to Expected Credit Losses.

**Impairment of credit facilities**

Credit facilities granted by the Group consists of loans and advances, Islamic financing to customers, letters of credit and financial guarantee contracts and commitments to grant credit facilities. Impairment on credit facilities shall be recognised in the consolidated statement of financial position at an amount equal to the higher of ECL under IFRS 9 according to the CBK guidelines, and the provisions required by the CBK instructions.

**Impairment of financial assets other than credit facilities**

The Group recognises ECL on investment in debt securities measured at amortised cost or FVOCI and on balances and deposits with banks.

**Expected Credit Losses**

The Group applies a three stage approach to measure the expected credit loss as follows:

**Stage 1: 12 month ECL**

The Group measures loss allowances at an amount equal to 12 month ECL on financial assets where there has not been significant increase in credit risk since their initial recognition or on exposures that are determined to have a low credit risk at the reporting date. The Group considers a financial asset to have low credit risk when its credit risk rating is equivalent to the globally understood definition of 'investment grade'.

**Stage 2: Lifetime ECL – not credit impaired**

The Group measures loss allowances at an amount equal to lifetime ECL on financial assets where there has been a significant increase in credit risk since initial recognition but are not credit impaired.

**2 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2.10 Impairment of financial assets (continued)**

**Stage 3: Lifetime ECL – credit impaired**

The Group measures loss allowances at an amount equal to lifetime ECL on financial assets that are determined to be credit impaired based on objective evidence of impairment.

Life time ECL is the ECL that result from all possible default events over the expected life of a financial instrument. The 12 month ECL is the portion of life time expected credit loss that result from default events that are possible within the 12 months after the reporting date. Both life time ECLs and 12 month ECLs are calculated either on an individual basis or on a collective basis depending on the nature of the underlying portfolio of financial instruments.

*Determining the stage of Expected Credit Loss*

At each reporting date, the Group assesses whether there has been significant increase in credit risk since initial recognition by comparing the risk of default occurring over the remaining expected life from the reporting date with the risk of default at the date of initial recognition. The quantitative criteria used to determine a significant increase in credit risk is a series of relative and absolute thresholds. All financial assets that are 30 days past due are deemed to have significant increase in credit risk since initial recognition and migrated to stage 2 even if other criteria do not indicate a significant increase in credit risk.

At each reporting date, the Group also assesses whether a financial asset or group of financial assets is credit impaired. The Group considers a financial asset to be credit impaired when one or more events that have a detrimental impact on the estimated future cash flows of the financial asset have occurred or when contractual payments are 90 days past due. All credit impaired financial assets are classified as stage 3 for ECL measurement purposes. Evidence of credit impairment includes observable data about the following:

- Significant financial difficulty of the borrower or issuer
- A breach of contract such as default or past due event
- The lender having granted to the borrower a concession, that the lender would otherwise not consider, for economic or contractual reasons relating to the borrower's financial difficulty
- The disappearance of an active market for a security because of financial difficulties
- Purchase of a financial asset at a deep discount that reflects the incurred credit loss

At the reporting date, if the credit risk of a financial asset or group of financial assets has not increased significantly since initial recognition or not credit impaired, these financial assets are classified as stage 1.

*Measurement of ECLs*

ECL is probability weighted estimates of credit losses and are measured as the present value of all cash shortfalls discounted at the effective interest rate of the financial instrument. Cash shortfall represents the difference between cash flows due to the Group in accordance with the contract and the cash flows that the Group expects to receive. The key elements in the measurement of ECL include probability of default (PD), loss given default (LGD) and exposure at default (EAD). The Group estimates these elements using appropriate credit risk models taking into consideration the internal and external credit ratings of the assets, nature and value of collaterals, forward looking macroeconomic scenarios etc.

*Incorporation of forward looking information*

The Group considers key economic variables that are expected to have an impact on the credit risk and the ECL in order to incorporate forward looking information into the ECL models. These primarily reflect reasonable and supportable forecasts of the future macro-economic conditions. The consideration of such factors increases the degree of judgment in determination of ECL. The management reviews the methodologies and assumptions including any forecasts of future economic conditions on regular basis.

**2 SIGNIFICANT ACCOUNTING POLICIES (continued)****2.10 Impairment of financial assets (continued)***Modification of loans and Islamic financing to customers*

Under certain circumstances, the Group seeks to restructure loans and Islamic financing to customers rather than taking possession of collateral. This may involve extending the payment arrangements, reduction in the amount of principal or interest and the agreement of new loan or financing conditions. If the modifications are substantial, such a facility is derecognised and a new facility is recognised with substantially different terms and conditions. The facility will have a loss allowance measured based on 12 month ECL except in rare occasions where the new facility is considered to be originated and credit impaired. Management continuously reviews modified loans and Islamic financing to customers to ensure that all criteria are met and that future payments are likely to occur. Management also assesses whether there has been significant increase in credit risk or the facility should be classified in stage 3. When loans and Islamic financing to customers have been modified but not derecognised, any impairment is measured using the original effective interest rate as calculated before the modification of terms.

*Write off*

The gross carrying amount of a financial asset is written off (either partially or in full) when the Group determines that the debtor does not have assets or sources of income that could generate sufficient cash flows to repay the amounts. However, financial assets that are written off could still be subject to enforcement activities in order to comply with the Group's procedures for recovery of amounts due.

*Presentation of allowance for ECL in the statement of financial position*

Loss allowances for ECL are presented as a deduction from the gross carrying amount of the financial assets for financial assets carried at amortised cost. In the case of debt instruments measured at FVOCI, the Group recognises the ECL charge in the consolidated statement of income and a corresponding amount is recognised in other comprehensive income with no reduction in the carrying amount of the financial asset in the consolidated statement of financial position. ECL for loan commitments, letters of credit and financial guarantee contracts are recognised in other liabilities. When the Group is unable to identify the ECL on the undrawn portion of credit commitments separately from drawn portion of commitments, the combined amount of ECL is presented as a deduction from the gross carrying amount of the drawn portion.

**Provisions for credit losses in accordance with CBK instructions**

The Group is required to calculate provisions for credit losses on credit facilities in accordance with the instructions of CBK on the classification of credit facilities and calculation of provisions. Credit facilities are classified as past due when a payment has not been received on its contractual payment date or if the facility is in excess of pre-approved limits. A credit facility is classified as past due and impaired when the interest/profit or a principal instalment is past due for more than 90 days and if the carrying amount of the facility is greater than its estimated recoverable value. Past due but not impaired and past due and impaired loans are managed and monitored as irregular facilities and are classified into the following four categories which are then used to determine the provisions.

| Category    | Criteria                                  | Specific provisions |
|-------------|---|---------------------|
| Watch list  | Irregular for a period of up to 90 days   | -                   |
| Substandard | Irregular for a period of 91- 180 days    | 20%                 |
| Doubtful    | Irregular for a period of 181- 365 days   | 50%                 |
| Bad         | Irregular for a period exceeding 365 days | 100%                |

The Group may also include a credit facility in one of the above categories based on management's judgement of a customer's financial and/or non-financial circumstances.

In addition to specific provisions, minimum general provisions of 1% on cash facilities and 0.5% on non-cash facilities are made on all applicable credit facilities (net of certain restricted categories of collateral) which are not subject to specific provisioning.

**2 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2.11 Impairment of non-financial assets**

Goodwill and intangible assets that have an indefinite useful life are not subject to amortisation and are tested annually for impairment. Other non-financial assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised in the consolidated statement of income for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. If previously recognised impairment losses have decreased, such excess impairment provision is reversed in the consolidated statement of income for non-financial assets other than goodwill.

**2.12 Share based compensation**

*Equity settled share based compensation*

The fair value of the employee services received in exchange for the grant of options or shares is recognised as an expense, together with a corresponding increase in equity. The total amount to be expensed over the vesting period is determined by reference to the fair value of the options or shares on the date of grant using the Black Scholes model. At each reporting date, the Group revises its estimates of the number of options that are expected to become exercisable. It recognises the impact of the revision of original estimates, if any, in the consolidated statement of income, with a corresponding adjustment to equity.

*Cash settled share based compensation*

The fair value of the employee services received in exchange for the cash settled share based payment is recognised as an expense, together with a corresponding increase in liability. The total amount to be expensed over the vesting period is determined by reference to the fair value of the options determined using the Black Scholes model. The liability is remeasured to fair value at each reporting date up to and including the settlement date, with changes in fair value recognised in the consolidated statement of income.

**2.13 Post-employment benefits**

The Group is liable to make defined contributions to State plans and lump sum payments under defined benefit plans to employees at cessation of employment, in accordance with the laws of the place they are employed. The defined benefit plans are unfunded. The present value of the defined benefit obligation is determined annually by actuarial valuations using the projected unit credit method. An actuarial valuation involves making various assumptions such as determination of the discount rate, future salary increases and mortality rates. These assumptions are reviewed at each reporting date. Current service cost, past service cost and net interest expense on the defined benefit plans are recognized in consolidated statement of income and is included in staff expenses. Any gains or losses on re-measurement of defined benefit plans attributable to changes in actuarial assumptions are recognized in other comprehensive income and is included in Actuarial Valuation reserve.

**2.14 Taxation**

Income tax payable on taxable profit ('current tax') is recognised as an expense in the period in which the profits arise in accordance with the fiscal regulations of the respective countries in which the Group operates. Deferred tax assets are recognised for deductible temporary differences, carry forward of unused tax credits and unused tax losses, to the extent it is probable that taxable profit will be available to utilise these. Deferred tax liabilities are recognised for taxable temporary differences. Deferred tax assets and liabilities are measured using tax rates and applicable legislation enacted at the reporting date.

**2.15 Recognition of financial assets and financial liabilities**

Financial assets and financial liabilities are recognised when the Group becomes party to contractual provisions of the instrument and are initially measured at fair value. Transaction costs are included only for those financial instruments that are not measured at fair value through statement of income.

**2.16 Classification and measurement of financial assets**

The Group determines the classification of financial assets based on the business model it uses to manage the financial assets and the contractual cash flow characteristics of the financial assets.

*Business model assessment*

The Group determines its business model at the level that best reflects how it manages groups of financial assets to achieve its business objective. The Group's business model is not assessed on an instrument by instrument basis but at a higher level of aggregated portfolios and is based on a number of observable factors. The information considered includes:

**2 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2.16 Classification and measurement of financial assets (continued)**

- The stated policies and objectives for the portfolio and the operation of those policies in practice
- The risks that affect the performance of the business model (and the financial assets held within that business model) and how those risks are managed;
- The frequency, volume and timing of sales in prior periods, the reasons for such sales and its expectations about future sales activity.

The business model assessment is based on reasonably expected scenarios without taking 'worst case' or 'stress case' scenarios into account. If cash flows after initial recognition are realised in a way that is different from the Group's original expectations, the Group does not change the classification of the remaining financial assets held in that business model, but incorporates such information when assessing newly originated or newly purchased financial assets going forward.

*Assessment of whether contractual cash flows are solely payments of principal and interest (SPPI test)*

The Group assesses the contractual terms of financial assets to identify whether they meet the SPPI test. 'Principal' for the purpose of this test is defined as the fair value of the financial asset at initial recognition and may change over the life of the financial asset. Interest is defined as consideration for time value of money and for the credit risk associated with the principal and for other basic lending risks and costs as well as a profit margin. In assessing whether the contractual cash flows are solely payments of principal and interest, the Group considers whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. The Group considers:

- Contingent events that would change the amount and timing of cash flows;
- Leverage features;
- Prepayment and extension terms;
- Terms that limit the Group's claim to cash flows from specified assets (e.g. non-recourse asset arrangements); and
- Features that modify consideration of the time value of money – e.g. periodical reset of interest rates.

Contractual terms that introduce a more than de minimus exposure to risks or volatility in the contractual cash flows that are unrelated to a basic lending arrangement do not give rise to contractual cash flows that are solely payment of principal and interest. In such cases, the financial asset is measured at fair value through profit or loss.

The Group classifies its financial assets upon initial recognition into the following categories:

- Financial assets carried at amortised cost
- Financial assets carried at fair value through other comprehensive income (FVOCI)
- Financial assets carried at fair value through profit or loss (FVTPL)

*Financial assets carried at Amortised cost:*

A financial asset is carried at amortised cost if it meets both of the following conditions:

- it is held within a business model whose objective is to hold assets to collect contractual cash flows ; and
- its contractual terms give rise, on specified dates, to cash flows that are solely payments of principal and interest on the principal amount outstanding

**2 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2.16 Classification and measurement of financial assets (continued)**

Financial assets carried at amortised cost are subsequently measured at amortised cost using the effective interest method. Interest income, foreign exchange gains and losses and charge for expected credit losses are recognised in the consolidated statement of income. Any gain or loss on de-recognition is recognised in the consolidated statement of income.

*Financial assets carried at fair value through other comprehensive income (FVOCI):*

**(i) Debt Securities at FVOCI**

A debt security is carried at FVOCI if it meets both of the following conditions:

- it is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
- its contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding

Debt Securities at FVOCI are subsequently measured at fair value. Interest income calculated using the effective interest method, foreign exchange gains and losses and impairment losses are recognised in the consolidated statement of income. Fair value changes which are not part of an effective hedging relationship are recognised in other comprehensive income and presented in the cumulative changes in fair values as part of equity until the asset is derecognised or reclassified. When the financial asset is derecognised, the cumulative gain or loss previously recognised in other comprehensive income is reclassified from equity to the consolidated statement of income.

**(ii) Equity investments at FVOCI**

Upon initial recognition, the Group makes an irrevocable election to classify some of its equity investments as equity investments at FVOCI if they meet the definition of Equity under IAS 32 Financial Instruments: Presentation and are not held for trading. Such classification is determined on an instrument by instrument basis. Equity investments at FVOCI are subsequently measured at fair value. Changes in fair values including foreign exchange component are recognised in other comprehensive income and presented in the cumulative changes in fair values as part of equity. Cumulative gains and losses previously recognised in other comprehensive income are transferred to retained earnings on de-recognition and are not recognised in the consolidated statement of income. Dividend income on equity investments at FVOCI are recognised in the consolidated statement of income unless they clearly represent a recovery of part of the cost of the investment. Equity investments at FVOCI are not subject to impairment assessment.

*Financial assets carried at fair value through profit or loss:*

Financial assets in this category are those assets which have been either designated by management upon initial recognition or are mandatorily required to be measured at fair value under IFRS 9. Management designates an instrument as FVTPL that otherwise meet the requirements to be measured at amortised cost or at FVOCI only if it eliminates, or significantly reduces, an accounting mismatch that would otherwise arise. Financial assets with contractual cash flows not representing solely payment of principal and interest are mandatorily required to be measured at FVTPL.

Financial assets at FVTPL are subsequently measured at fair value. Changes in fair value are recognised in the consolidated statement of income. Interest income is recognised using the effective interest method. Dividend income from equity investments measured at FVTPL is recognised in the consolidated statement of income when the right to the payment has been established.

The Group's financial assets are classified and measured as follows:

**Cash and short term funds**

Cash and short term funds consist of cash in hand, current account and money at call with other banks and deposits with banks maturing within seven days. Cash and short term funds are classified and carried at amortised cost using effective interest rate.

**Deposits with banks**

Deposits with banks are classified and carried at amortised cost using the effective interest method. The carrying values of such assets which are being effectively hedged for changes in fair value are adjusted to the extent of the changes in fair value attributable to the risk being hedged.

**2 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2.16 Classification and measurement of financial assets (continued)**

**Loans and advances to customers**

Loans and advances are stated at amortised cost using the effective interest method. The carrying values of such assets which are being effectively hedged for changes in fair value are adjusted to the extent of the changes in fair value attributable to the risk being hedged.

**Islamic financing to customers**

Islamic financing to customers are financial assets with fixed or determinable payments that are not quoted in an active market. Major islamic financing products are:

*a. Murabaha*

Murabaha is an agreement relating to the sale of commodities at cost plus an agreed upon profit margin, whereby the seller informs the buyer of the price at which the deal will be completed and also the amount of profit to be recognized. Murabaha is a financial asset originated by the Group and is stated at amortised cost.

*b. Wakala*

Wakala is an agreement involving Al-Muwakkil (the Principal) who wishes to appoint Al-Wakil (the Agent) to be his agent with respect to the investment of Al-Muwakkil's fund, in accordance with regulations of the Islamic Sharia'a. Wakala is a financial asset originated by the Group and stated at amortised cost.

*c. Leased assets - the Group as a lessor*

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating lease. Leased assets are stated at amortised cost using effective profit rate.

**Financial investments**

Group's financial investments consist of debt securities, equity investments and other investments.

Debt securities are classified as either at amortised cost or at fair value through other comprehensive income based on the business model in which these securities are managed.

Equity investments are generally carried at fair value through profit or loss except for those specific investments for which the Group has made an election to classify at fair value through other comprehensive income.

Other investments are carried at fair value through profit or loss.

**2.17 Fair value measurement**

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 in the principal or, in its absence, in the most advantageous market to which the Group has access at that date under current market conditions regardless of whether that price is directly observable or estimated using another valuation technique.

When available, the Group measures the fair value of an instrument using the quoted price in an active market for that instrument. A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

If there is no quoted price in an active market, then the Group uses valuation techniques that include the use of valuation models that maximise the use of relevant observable inputs and minimise the use of unobservable inputs. The chosen valuation technique incorporates all of the factors that market participants would take into account in pricing a transaction. The inputs to these models are taken from observable markets where possible, but where this is not feasible, estimation is required in establishing fair values. Judgements and estimates include considerations of liquidity and model inputs related to items such as credit risk (both own and counterparty), funding value adjustments, correlation and volatility.

If an asset or liability measured at fair value has a bid price and an ask price, then the Group measures assets at a bid price and liabilities at an ask price.

Fair values of investment properties are determined by appraisers having an appropriate recognised professional qualification and recent experience in the location and category of the property being valued and also considering the ability to generate economic benefits by using the property in its highest and best use.

**2 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2.18 Repurchase and resale agreements**

Assets sold with a simultaneous commitment to repurchase at a specified future date at an agreed price (repos) are not derecognised in the consolidated statement of financial position. Amounts received under these agreements are treated as interest bearing liabilities and the difference between the sale and repurchase price treated as interest expense using the effective yield method. Assets purchased with a corresponding commitment to resell at a specified future date at an agreed price (reverse repos) are not recognised in the consolidated statement of financial position. Amounts paid under these agreements are treated as interest earning assets and the difference between the purchase and resale price treated as interest income using the effective yield method.

**2.19 Offsetting of financial assets and liabilities**

Financial assets and financial liabilities are only offset and the net amount reported in the consolidated statement of financial position when there is a legally enforceable right to set off the recognised amounts and the Group intends to either settle on a net basis, or to realise the asset and settle the liability simultaneously.

**2.20 De-recognition of financial assets and financial liabilities**

**Financial assets**

A financial asset (or where applicable, a part of a financial asset or part of a group of similar financial assets) is derecognised where:

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

When the Group has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Group's continuing involvement in the asset. 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 Group could be required to repay.

**Financial liabilities**

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expired.

Where 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 a de-recognition of the original liability and the recognition of a new liability.

**2.21 Derivative financial instruments and hedge accounting**

The Group deals in interest rate swaps to manage its interest rate risk on interest bearing assets and liabilities. Similarly the Group deals in forward foreign exchange contracts for customers and to manage its foreign currency positions and cash flows. All derivative financial instruments of the Group are recorded in the consolidated statement of financial position at fair value. The fair value of a derivative is the equivalent of the unrealised gain or loss from marking to market the derivative using prevailing market rates or internal pricing models. Positive and negative fair values are reported as assets and liabilities respectively and are offset when there is both an intention to settle net and a legal right to offset exists.

For the purposes of hedge accounting, hedges are classified into two categories: (a) fair value hedges which hedge the exposure to changes in the fair value of a recognised asset or liability and (b) cash flow hedges which hedge exposure to variability in cash flows that is either attributable to a particular risk associated with a recognised financial asset or liability or a highly probable forecast transaction.

In relation to fair value hedges which meet the conditions for hedge accounting, any gain or loss from remeasuring the hedging instrument is recognised immediately in the consolidated statement of income. The carrying amounts of hedged items are adjusted for fair value changes attributable to the risk being hedged and the difference is recognised in the consolidated statement of income.

**2 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2.21 Derivative financial instruments and hedge accounting (continued)**

In relation to cash flow hedges which meet the conditions for hedge accounting, the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised initially in equity and any ineffective portion is recognised in the consolidated statement of income. The gains or losses on cash flow hedges recognised initially in equity are transferred to the consolidated statement of income in the period in which the hedged transaction impacts the consolidated statement of income. Where the hedged transaction results in the recognition of an asset or liability, the associated gains or losses that had initially been recognised in equity are included in the initial measurement of the cost of the related asset or liability. For hedges that do not qualify for hedge accounting, any gains or losses arising from changes in fair value of the hedging instrument are taken directly to the consolidated statement of income.

Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated or exercised, no longer qualifies for hedge accounting or is revoked by the Group. For cash flow hedges, any cumulative gain or loss on the hedging instrument recognised in equity remains in equity until the forecast transaction occurs. In the case of fair value hedges of interest bearing financial instruments, any adjustment relating to the hedge is amortised over the remaining term to maturity. Where the hedged transaction is no longer expected to occur, the net cumulative gain or loss recognised in equity is transferred to the consolidated statement of income.

**2.22 Trade and settlement date accounting**

All "regular way" purchase and sale of financial assets other than investments in equity instruments are recognised on the settlement date, i.e. the date the asset is delivered to the Group. Investments in equity instruments are recognised on the trade date, i.e. the date that the Group commits to purchase or sell the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame generally established by the regulation or convention in the market place.

**2.23 Investment properties**

Investment properties are properties held either to earn rental income or for capital appreciation or for both, but not for sale in the ordinary course of business, use in the production or supply of goods or services or for administrative purposes. Investment property is measured at cost on initial recognition and subsequently at fair value with any change therein recognised in consolidated statement of income. Cost includes expenditure that is directly attributable to the acquisition of the investment property. Fair values of investment properties are determined by appraisers having an appropriate recognised professional qualification and recent experience in the location and category of the property being valued. Any gain or loss on disposal of an investment property (calculated as the difference between the net proceeds from disposal and the carrying amount of the item) is recognised in consolidated statement of income. When the use of a property changes such that it is reclassified as Land, premises and equipment, its fair value at the date of reclassification becomes its cost for subsequent accounting.

**2.24 Land, premises and equipment**

Land and premises comprise mainly branches and offices. All premises and equipment are stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Projects and work in progress are stated at cost less impairment if any. Costs are those expenses incurred by the Group that are directly attributable to the creation of the asset. When the asset is ready for use, capital work in progress is transferred to the appropriate category and depreciated in accordance with the Group's policies.

Subsequent costs are included in the asset's carrying amount or are recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the consolidated statement of income during the period in which they are incurred.

Land is not depreciated. Depreciation is provided on the depreciable amount of other items of premises and equipment on a straight line basis over their estimated useful life. The depreciable amount is the gross carrying value, less the estimated residual value at the end of its useful life. The estimated useful life of premises and equipment are as follows:

|                            |                                  |
|----------------------------|----------------------------------|
| Building on leasehold land | term of lease (maximum 20 years) |
| Building on freehold land  | 50 years                         |
| IT systems and equipment   | 3-10 years                       |

**2 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2.24 Land, premises and equipment (continued)**

Residual values and useful lives of assets are reviewed, and adjusted if appropriate, at each reporting date. The carrying values of land, premises and equipment are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable. Gains and losses on disposals are determined by comparing proceeds with the carrying amount. These are included in the consolidated statement of income.

**2.25 Leases**

At inception of a contract, the Group assesses whether the contract is a lease. A contract is a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for a consideration. If the contract is identified as a lease, the Group recognises a right-of-use asset and a lease liability at the lease commencement date. The Group elected to use the recognition exemptions for lease contracts that, at the commencement date, have a lease term of 12 months or less and lease contracts for which the underlying asset is of low value.

*Right-of-use assets*

The right-of-use asset is initially measured at cost, which comprises the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date, plus any initial direct costs incurred. The right-of-use asset is subsequently depreciated using the straight-line method over the lease term. In addition, the right-of-use asset is periodically reduced by impairment losses, if any. The Group presents right-of-use assets in 'land, premises and equipment' in the consolidated statement of financial position.

*Lease Liabilities*

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the Group's incremental borrowing rate. The lease liability is subsequently measured at amortised cost using the effective interest method. In addition, the carrying amount of lease liabilities is remeasured if there is a modification, a change in the lease term, or a change in the lease payments. The Group presents lease liabilities in 'other liabilities' in the consolidated statement of financial position.

**2.26 Business combinations**

Business combinations are accounted for using the acquisition method of accounting. The cost of an acquisition is measured as the aggregate of the consideration transferred, measured at acquisition date fair value and the amount of any non-controlling interest in the acquiree. Non-controlling interest in the acquiree is measured at the proportionate share in the recognised amounts of the acquiree's identifiable net assets. Other acquisition related costs incurred are expensed and included in other administrative expenses.

If the business combination is achieved in stages, the acquirer's previously held equity interest in the acquiree is remeasured to fair value at the acquisition date and included in cost of acquisition. Any resulting gain or loss is recognised in consolidated statement of income. Identifiable assets acquired and liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. The excess of the cost of acquisition over the fair value of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the consolidated statement of income.

**2.27 Goodwill and intangible assets**

*a. Goodwill*

Goodwill acquired in a business combination is initially measured at cost, being the excess of the cost of the acquisition over the net fair value of the identifiable assets and liabilities acquired. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill is reviewed for impairment, annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired. Goodwill is recorded in the functional currency of the foreign operation and is translated to the presentation currency at the rate of exchange prevailing at the reporting date. When subsidiaries are sold, the difference between the selling price and the net assets plus cumulative translation differences and goodwill is recognised in the consolidated statement of income.

**2 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2.27 Goodwill and intangible assets (continued)**

*b. Intangible assets*

Intangible assets comprise separately identifiable intangible items arising from business combinations. An intangible asset is recognised only when its cost can be measured reliably and it is probable that the expected future economic benefit will flow to the Group. Intangible assets are initially measured at cost. The cost of intangible assets acquired in a business combination is their fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. The useful lives of the intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortised on a straight line basis over the useful economic life of 5 to 15 years and tested for impairment whenever there is an indication that the intangible asset may be impaired. Intangible assets with indefinite useful lives are not amortised but tested for impairment annually or whenever there is an indication that the intangible asset may be impaired. If the carrying value of the intangible asset is more than the recoverable amount, the intangible asset is considered impaired and is written down to its recoverable amount. The excess of carrying value over the recoverable amount is recognised in the consolidated statement of income. Impairment losses on intangible assets recognised in the consolidated statement of income in previous periods are reversed when there is an increase in the recoverable amount.

**2.28 Property acquired on settlement of debt**

Property acquired on settlement of debt is stated at the lower of the related loans and advances and the current fair value of such assets. Gains or losses on disposal and revaluation losses are recognised in the consolidated statement of income.

**2.29 Due to Banks and Financial Institutions, Customer deposits & Certificates of deposit issued**

Due to Banks and Financial Institutions, Customer Deposits & Certificates of deposit issued are stated at amortised cost using effective interest method. The carrying values of such liabilities which are being effectively hedged for changes in fair value are adjusted to the extent of the changes in fair value being hedged.

**2.30 Islamic customer deposits**

Islamic customer deposits comprise of Investment accounts and Non-investment accounts.

*Investment accounts*

Investment accounts may take the form of investment deposits, which are valid for specified periods of time, and are automatically renewable on maturity for the same period, unless the concerned depositors give written notice to the contrary, or take the form of investment saving accounts for unspecified periods. In all cases, investment accounts receive a proportion of the profit, bear a share of loss and are carried at cost plus profit payable.

*Non-investment accounts*

Non-investment accounts represent, in accordance with Islamic Sharia'a, Qard Hasan from depositors to the Group. These accounts are neither entitled to profit nor do they bear any risk of loss, as the Group guarantees to pay the related balance. Investing Qard Hasan is made at the discretion of the Group and the results of such investments are attributable to the shareholders of the Group. Non-investment accounts are carried at cost.

**2.31 Other borrowed funds**

Other borrowed funds includes Tier 2 bonds, Global Medium Term Notes, Global Medium Term Sukuk and Medium term borrowings. These are financial liabilities and are initially recognised at their fair value being the issue proceeds net of transaction costs and are subsequently measured at their amortised cost using the effective interest rate method. The carrying values of such liabilities which are being effectively hedged for changes in fair value are adjusted to the extent of the changes in fair value being hedged.

**2.32 Financial guarantees**

In the ordinary course of business, the Group gives financial guarantees, consisting of letters of credit, guarantees and acceptances. Financial guarantees are initially recognised in the consolidated financial statements at fair value, being the premium received, in other liabilities. The premium received is recognised in the consolidated statement of income in 'net fees and commissions' on a straight line basis over the life of the guarantee. The guarantee liability is subsequently carried at initial measurement less amortisation. When a payment under the guarantee is likely to become payable, the present value of the expected net payments less the unamortised premium is charged to the consolidated statement of income.

**2 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2.33 Treasury shares**

The Bank's holding of its own shares are accounted for as treasury shares and are stated at purchase consideration including directly attributable costs. When the treasury shares are sold, gains are credited to a separate account in equity (treasury share reserve) which is non distributable. Any realised losses are charged to the same account to the extent of the credit balance on that account. Any excess losses are charged to retained earnings then to reserves. Gains realised subsequently on the sale of treasury shares are first used to offset any previously recorded losses in the order of reserves, retained earnings and the treasury share reserve amount. No cash dividends are distributed on these shares. The issue of bonus shares increases the number of shares proportionately and reduces the average cost per share without affecting the total cost of treasury shares.

**2.34 Fiduciary assets**

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

**2.35 Significant accounting judgements and estimates**

In the process of applying the Group's accounting policies, management has used judgements and made estimates in determining the amounts recognised in the consolidated financial statements. The most significant use of judgements and estimates are as follows:

*Accounting Judgements*

*Classification of financial assets*

The Group determines the classification of financial assets based on the assessment of the business model within which the assets are held and assessment of whether the contractual terms of the financial asset are solely payments of principal and interest on the principal amount outstanding. Judgments are required in determining the business model at an appropriate level that best reflects an aggregated group or portfolio of assets which are managed together to achieve a particular business objective. The Group also applies judgment to assess if there is a change in business model in circumstances when the assets with in that business model are realised differently than the original expectations. Refer Note 2.16 classification of financial assets for more information.

*Estimation uncertainty and assumptions*

The key assumptions concerning the future and other key sources of estimation uncertainty at the reporting date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below:

*Expected Credit Losses on financial assets*

The Group estimates Expected Credit Loss (ECL) for all financial assets carried at amortised cost or fair value through other comprehensive income except for equity instruments.

Significant judgements are required in applying the accounting requirements for measuring ECL, such as:

- Determining criteria for significant increase in credit risk
- Choosing appropriate models and assumptions for 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 group of similar financial assets for the purpose of measuring ECL.

Information about significant judgements and estimates made by the Group in the above areas is set out in Note 30.1.1.

*Provision for credit losses*

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

*Impairment of goodwill*

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

**2 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2.35 Significant accounting judgements and estimates (continued)**

*Impairment of investment in associates*

The Group calculates the amount of impairment as the difference between the recoverable amount and its carrying value if there is any objective evidence that the investment in associates are impaired. The estimation of recoverable amount requires the Group to make an estimate of the expected future cash flows and selection of appropriate inputs for valuation.

*Fair values of assets and liabilities including intangibles*

Considerable judgment by management is required in the estimation of the fair value of the assets including intangibles with definite and indefinite useful life, liabilities and contingent liabilities acquired as a result of business combination.

*Share based payments*

The Group measures the share based payments to employees by reference to the fair value of the relevant equity instruments. Estimating fair value for share based payment transactions requires determination of the most appropriate valuation model. This estimate also requires determination of the most appropriate inputs to the valuation model including the expected life of the share option, volatility and dividend yield and making assumptions about them. The assumptions and models used for estimating fair value for share based payment transactions are disclosed in Note 23.

*Valuation of unquoted financial assets*

Fair value of unquoted financial assets is determined using valuation techniques including the discounted cash flow model. The inputs to these models are taken from observable markets where possible, but where this is not feasible, a degree of judgment is required in establishing fair values. The judgments include considerations of inputs such as liquidity risk, credit risk and volatility. Changes in assumptions about these factors could affect the reported fair value of financial instruments. The determination of the cash flows and discount factors requires significant estimation.

**3 SEGMENTAL ANALYSIS**

The Group organises and manages its operations by geographic territory in the first instance, primarily Domestic and International. Within its Domestic operations, the Group segments its business into Consumer and Private Banking, Corporate Banking, Investment Banking and Asset Management, Islamic Banking and Group Centre. All operations outside Kuwait are classified as International. Management treats the operations of these segments separately for the purposes of decision making, resource allocation and performance assessment.

**Consumer and Private Banking**

Consumer Banking provides a diversified range of products and services to individuals. The range includes consumer loans, credit cards, deposits, foreign exchange and other branch related services. Private Banking provides a comprehensive range of customised and innovative banking services to high net worth individuals and to institutional clients.

**Corporate Banking**

Corporate Banking provides a comprehensive product and service offering to business and corporate customers, including lending, deposits, trade finance, foreign exchange and advisory services.

**Investment Banking and Asset Management**

Investment Banking provides a full range of capital market advisory and execution services. The activities of Asset Management include wealth management, asset management, custody, brokerage and research.

**Islamic Banking**

Islamic banking represents the financial results of Boubyan Bank K.S.C.P., and its subsidiaries.

**Group Centre**

Group Centre includes treasury, investments, and other defined Group activities. Treasury provides a comprehensive range of treasury services and products to its clients, and is also responsible for the Bank's liquidity and market risk management. Group Centre includes any residual in respect of transfer pricing and inter segment allocations.

**International**

International includes all branches, subsidiaries and associates outside the State of Kuwait.

# National Bank of Kuwait Group

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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### 3 SEGMENTAL ANALYSIS (continued)

The following table shows net interest income and net income from Islamic financing, net operating income, profit for the year, total assets and total liabilities information in respect of the Group's business segments:

2020

|   | <i>Consumer<br/>and Private<br/>Banking<br/>KD 000's</i> | <i>Corporate<br/>Banking<br/>KD 000's</i> | <i>Investment<br/>Banking<br/>and Asset<br/>Management<br/>KD 000's</i> | <i>Islamic<br/>Banking<br/>KD 000's</i> | <i>Group<br/>Centre<br/>KD 000's</i> | <i>International<br/>KD 000's</i> | <i>Total<br/>KD 000's</i> |
|---|--|---|---|---|--------------------------------------|-----------------------------------|---------------------------|
| Net interest income and net income from Islamic financing | 219,879  | 80,297                                    | 746   | 143,235                                 | 26,642                               | 162,668                           | 633,467                   |
| Net operating income                                      | 278,702  | 127,070                                   | 24,134  | 171,656                                 | 34,860                               | 206,099                           | 842,521                   |
| Profit (loss) for the year                                | 151,832  | 64,378                                    | 12,387  | 33,547                                  | (53,419)                             | 49,937                            | 258,662                   |
| Total assets  | 4,753,571  | 4,978,948                                 | 67,145  | 6,437,149                               | 3,331,686                            | 10,148,892                        | 29,717,391                |
| Total liabilities   | 6,474,936  | 2,350,988                                 | 11,071  | 5,810,419                               | 237,618                              | 10,691,304                        | 25,576,336                |

2019

|   | <i>Consumer<br/>and Private<br/>Banking<br/>KD 000's</i> | <i>Corporate<br/>Banking<br/>KD 000's</i> | <i>Investment<br/>Banking<br/>and Asset<br/>Management<br/>KD 000's</i> | <i>Islamic<br/>Banking<br/>KD 000's</i> | <i>Group<br/>Centre<br/>KD 000's</i> | <i>International<br/>KD 000's</i> | <i>Total<br/>KD 000's</i> |
|---|--|---|---|---|--------------------------------------|-----------------------------------|---------------------------|
| Net interest income and net income from Islamic financing | 215,757  | 109,643                                   | 875   | 124,316                                 | 57,199                               | 181,434                           | 689,224                   |
| Net operating income                                      | 291,554  | 157,114                                   | 28,574  | 151,184                                 | 46,423                               | 220,668                           | 895,517                   |
| Profit (loss) for the year                                | 178,266  | 60,305                                    | 15,690  | 62,677                                  | (3,126)                              | 112,180                           | 425,992                   |
| Total assets  | 4,651,598  | 4,930,920                                 | 79,344  | 5,300,548                               | 3,208,951                            | 11,099,392                        | 29,270,753                |
| Total liabilities   | 5,447,815  | 2,294,546                                 | 22,447  | 4,647,367                               | 795,608                              | 11,803,810                        | 25,011,593                |

#### Geographic information:

The following table shows the geographic distribution of the Group's operating income based on the location of the operating entities.

| Net operating income               | 2020<br>KD 000's | 2019<br>KD 000's |
|------------------------------------|------------------|------------------|
| Kuwait                             | 636,422          | 674,849          |
| Other Middle East and North Africa | 146,741          | 160,536          |
| Europe                             | 32,918           | 35,901           |
| Others                             | 26,440           | 24,231           |
|                                    | 842,521          | 895,517          |

# National Bank of Kuwait Group

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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### 3 SEGMENTAL ANALYSIS (continued)

The following table shows the geographic distribution of the Group's non-current assets based on the location of the operating entities.

| Non-current assets                 | 2020<br>KD 000's | 2019<br>KD 000's |
|------------------------------------|------------------|------------------|
| Kuwait                             | 1,007,509        | 1,018,524        |
| Other Middle East and North Africa | 46,302           | 41,237           |
| Europe                             | 10,428           | 10,900           |
| Others                             | 4,459            | 5,151            |
|                                    | <u>1,068,698</u> | <u>1,075,812</u> |

Non-current assets consist of land, premises and equipment, goodwill and other intangible assets, investment properties and property acquired on settlement of debts.

### 4 INTEREST INCOME

|  | 2020<br>KD 000's | 2019<br>KD 000's |
|--|------------------|------------------|
| Deposits with banks                            | 44,467           | 94,607           |
| Loans and advances to customers                | 533,226          | 655,226          |
| Debt investment securities                     | 151,496          | 188,635          |
| Kuwait Government treasury bonds and CBK bonds | 27,795           | 48,058           |
|  | <u>756,984</u>   | <u>986,526</u>   |

### 5 INTEREST EXPENSE

|   | 2020<br>KD 000's | 2019<br>KD 000's |
|---|------------------|------------------|
| Due to banks and other financial institutions | 81,736           | 161,415          |
| Customer deposits                             | 167,281          | 228,711          |
| Certificates of deposit issued                | 6,879            | 17,063           |
| Other borrowed funds                          | 10,856           | 14,429           |
|   | <u>266,752</u>   | <u>421,618</u>   |

### 6 NET FEES AND COMMISSIONS

|                                       | 2020<br>KD 000's | 2019<br>KD 000's |
|---------------------------------------|------------------|------------------|
| Fees and commissions income           | 185,440          | 196,438          |
| Fees and commissions related expenses | (39,459)         | (39,286)         |
| Net fees and commissions              | <u>145,981</u>   | <u>157,152</u>   |

Fees and commissions income includes asset management fees of KD 36,519 thousand (2019: KD 38,712 thousand) earned on trust and fiduciary activities where the Group holds or invests assets on behalf of its customers.

# National Bank of Kuwait Group

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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### 7 NET INVESTMENT INCOME

|   | <i>2020</i><br><i>KD 000's</i> | <i>2019</i><br><i>KD 000's</i> |
|---|--------------------------------|--------------------------------|
| Net realised gain (loss) on sale of investments                                     | 445                            | (377)                          |
| Net (loss) gains from investments carried at fair value through statement of income | (2,776)                        | 3,579                          |
| Dividend income   | 907                            | 2,685                          |
| Share of results of associates  | 276                            | 2,163                          |
| Net gain on business combination (Note 26)  | 2,726                          | -                              |
| Other investment income   | 463                            | 369                            |
|   | <u>2,041</u>                   | <u>8,419</u>                   |

### 8 OTHER OPERATING INCOME

Other operating income includes gain on sale of properties amounting to KD 12,715 thousand. Further, it includes Covid-19 related Government support towards staff expenses received by the Group amounting to KD 11,788 thousand (refer to Note 33).

### 9 PROVISION CHARGE FOR CREDIT LOSSES AND IMPAIRMENT LOSSES

|  | <i>2020</i><br><i>KD 000's</i> | <i>2019</i><br><i>KD 000's</i> |
|--|--------------------------------|--------------------------------|
| Provision charge for credit losses (Note 13)           | 217,723                        | 122,585                        |
| ECL charge for investment in debt securities (Note 14) | 13,752                         | 3,506                          |
| ECL charge for other financial assets                  | 13,719                         | 763                            |
| Other impairment losses                                | 1,244                          | 2,861                          |
|  | <u>246,438</u>                 | <u>129,715</u>                 |

### 10 TAXATION

|   | <i>2020</i><br><i>KD 000's</i> | <i>2019</i><br><i>KD 000's</i> |
|---|--------------------------------|--------------------------------|
| National Labour Support Tax                                       | 6,366                          | 10,252                         |
| Zakat   | 2,814                          | 4,540                          |
| Contribution to Kuwait Foundation for the Advancement of Sciences | 2,178                          | 3,759                          |
| Overseas tax  | 14,484                         | 16,985                         |
|   | <u>25,842</u>                  | <u>35,536</u>                  |

# National Bank of Kuwait Group

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### 11 EARNINGS PER SHARE

Basic earnings per share is calculated by dividing the profit for the year attributable to shareholders of the Bank (adjusted for interest and profit paid on Perpetual Tier 1 Capital Securities and Sukuk) by the weighted average number of shares outstanding during the year net of treasury shares. There are no dilutive potential shares that are convertible into shares.

|  | 2020<br>KD 000's | 2019<br>KD 000's |
|--|------------------|------------------|
| Profit for the year attributable to shareholders of the Bank   | 246,341          | 401,291          |
| Less: Interest paid on Perpetual Tier 1 Capital Securities   | (22,796)         | (12,258)         |
| Less: Profit distribution on Perpetual Tier 1 Sukuk by a subsidiary attributable to shareholders of the Bank | (3,106)          | (3,069)          |
|  | <u>220,439</u>   | <u>385,964</u>   |
| Weighted average number of shares outstanding during the year net of treasury shares (thousand)              | <u>6,797,099</u> | <u>6,768,372</u> |
| Basic earnings per share   | <u>32 fils</u>   | <u>57 fils</u>   |

Earnings per share calculations for 2019 have been adjusted to take account of the bonus shares issued in 2020.

### 12 CASH AND SHORT TERM FUNDS

|   | 2020<br>KD 000's | 2019<br>KD 000's |
|---|------------------|------------------|
| Cash on hand  | 228,294          | 235,524          |
| Current account with other banks                            | 738,927          | 961,974          |
| Money at call   | 874,975          | 361,590          |
| Balances with the Central Bank of Kuwait                    | 684,611          | 298,046          |
| Deposits and Murabaha with banks maturing within seven days | 1,389,558        | 1,930,843        |
|   | <u>3,916,365</u> | <u>3,787,977</u> |
| Expected credit losses                                      | (12,994)         | (804)            |
|   | <u>3,903,371</u> | <u>3,787,173</u> |

### 13 LOANS, ADVANCES AND ISLAMIC FINANCING TO CUSTOMERS

|  | <i>Middle<br/>East and North<br/>Africa</i><br>KD 000's | <i>North<br/>America</i><br>KD 000's | <i>Europe</i><br>KD 000's | <i>Asia</i><br>KD 000's | <i>Others</i><br>KD 000's | <i>Total</i><br>KD 000's |
|--|---|--------------------------------------|---------------------------|-------------------------|---------------------------|--------------------------|
| 2020   |   |                                      |                           |                         |                           |                          |
| Corporate  | 9,903,392   | 409,519                              | 1,228,407                 | 367,708                 | 197,326                   | 12,106,352               |
| Retail   | 6,083,546   | -                                    | 1,668                     | -                       | -                         | 6,085,214                |
| Loans, advances and Islamic financing to customers | <u>15,986,938</u>                                       | <u>409,519</u>                       | <u>1,230,075</u>          | <u>367,708</u>          | <u>197,326</u>            | <u>18,191,566</u>        |
| Provision for credit losses                        |   |                                      |                           |                         |                           | (687,224)                |
|  |   |                                      |                           |                         |                           | <u>17,504,342</u>        |

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13 LOANS, ADVANCES AND ISLAMIC FINANCING TO CUSTOMERS (continued)

|  | <i>Middle<br/>East and<br/>North<br/>Africa</i><br>KD 000's | <i>North<br/>America</i><br>KD 000's | <i>Europe</i><br>KD 000's | <i>Asia</i><br>KD 000's | <i>Others</i><br>KD 000's | <i>Total</i><br>KD 000's |
|--|---|--------------------------------------|---------------------------|-------------------------|---------------------------|--------------------------|
| 2019   |   |                                      |                           |                         |                           |                          |
| Corporate  | 9,672,508   | 387,169                              | 725,840                   | 379,836                 | 258,412                   | 11,423,765               |
| Retail   | 5,634,078   | -                                    | 3,491                     | -                       | -                         | 5,637,569                |
| Loans, advances and Islamic financing to customers | 15,306,586  | 387,169                              | 729,331                   | 379,836                 | 258,412                   | 17,061,334               |
| Provision for credit losses                        |   |                                      |                           |                         |                           | (508,736)                |
|  |   |                                      |                           |                         |                           | <u>16,552,598</u>        |

In March 2007, the Central Bank of Kuwait issued a circular amending the basis of making general provisions on facilities changing the minimum rate from 2% to 1% for cash facilities and 0.5% for non-cash facilities. The required rates were effective from 1 January 2007 on the net increase in facilities, net of certain restricted categories of collateral, during the reporting period. Pending further directive from the Central Bank of Kuwait, the general provision in excess of 1% for cash facilities and 0.5% for non-cash facilities was retained as general provision.

The Expected Credit Losses on credit facilities determined under IFRS 9 in accordance to the CBK guidelines amounted to KD 604,962 thousand as at 31 December 2020 (2019: KD 394,935 thousand).

Provisions for credit losses on cash facilities are as follows:

|   | <i>Specific</i>         |                         | <i>General</i>          |                         | <i>Total</i>            |                         |
|---|-------------------------|-------------------------|-------------------------|-------------------------|-------------------------|-------------------------|
|   | <i>2020</i><br>KD 000's | <i>2019</i><br>KD 000's | <i>2020</i><br>KD 000's | <i>2019</i><br>KD 000's | <i>2020</i><br>KD 000's | <i>2019</i><br>KD 000's |
| Balance at beginning of the year              | 111,666                 | 120,740                 | 397,070                 | 384,968                 | 508,736                 | 505,708                 |
| Provided during the year                      | 105,101                 | 112,943                 | 107,851                 | 10,122                  | 212,952                 | 123,065                 |
| Provisions at acquired subsidiary             | 5,100                   | -                       | 6,372                   | -                       | 11,472                  | -                       |
| Amounts written off net of exchange movements | (50,814)                | (122,017)               | 4,878                   | 1,980                   | (45,936)                | (120,037)               |
| Balance at end of the year                    | <u>171,053</u>          | <u>111,666</u>          | <u>516,171</u>          | <u>397,070</u>          | <u>687,224</u>          | <u>508,736</u>          |

Further analysis of specific provision based on class of financial asset is given below:

|   | <i>Corporate</i>        |                         | <i>Retail</i>           |                         | <i>Total</i>            |                         |
|---|-------------------------|-------------------------|-------------------------|-------------------------|-------------------------|-------------------------|
|   | <i>2020</i><br>KD 000's | <i>2019</i><br>KD 000's | <i>2020</i><br>KD 000's | <i>2019</i><br>KD 000's | <i>2020</i><br>KD 000's | <i>2019</i><br>KD 000's |
| Balance at beginning of the year              | 43,415                  | 50,875                  | 68,251                  | 69,865                  | 111,666                 | 120,740                 |
| Provided during the year                      | 64,078                  | 84,832                  | 41,023                  | 28,111                  | 105,101                 | 112,943                 |
| Provisions at acquired subsidiary             | 5,100                   | -                       | -                       | -                       | 5,100                   | -                       |
| Amounts written off net of exchange movements | (41,713)                | (92,292)                | (9,101)                 | (29,725)                | (50,814)                | (122,017)               |
| Balance at end of the year                    | <u>70,880</u>           | <u>43,415</u>           | <u>100,173</u>          | <u>68,251</u>           | <u>171,053</u>          | <u>111,666</u>          |

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### 13 LOANS, ADVANCES AND ISLAMIC FINANCING TO CUSTOMERS (continued)

Analysis of total provision charge for credit losses is given below:

|                                    | <i>Specific</i>                |                                | <i>General</i>                 |                                | <i>Total</i>                   |                                |
|------------------------------------|--------------------------------|--------------------------------|--------------------------------|--------------------------------|--------------------------------|--------------------------------|
|                                    | <i>2020</i><br><i>KD 000's</i> | <i>2019</i><br><i>KD 000's</i> | <i>2020</i><br><i>KD 000's</i> | <i>2019</i><br><i>KD 000's</i> | <i>2020</i><br><i>KD 000's</i> | <i>2019</i><br><i>KD 000's</i> |
| Cash facilities                    | <b>105,101</b>                 | 112,943                        | <b>107,851</b>                 | 10,122                         | <b>212,952</b>                 | 123,065                        |
| Non cash facilities                | <b>5,417</b>                   | (1,704)                        | <b>(646)</b>                   | 1,224                          | <b>4,771</b>                   | (480)                          |
| Provision charge for credit losses | <b>110,518</b>                 | 111,239                        | <b>107,205</b>                 | 11,346                         | <b>217,723</b>                 | 122,585                        |

The available provision on non-cash facilities of KD 36,768 thousand (2019: KD 31,997 thousand) is included under other liabilities (Note 19).

Non-performing loans, advances and Islamic financing to customers and related provisions are as follows:

|  | <i>2020</i><br><i>KD 000's</i> | <i>2019</i><br><i>KD 000's</i> |
|--|--------------------------------|--------------------------------|
| Loans, advances and Islamic financing to customers | <b>312,381</b>                 | 186,903                        |
| Provisions   | <b>149,152</b>                 | 100,818                        |

The fair value of collateral that the Group holds relating to loans, advances and Islamic financing to customers individually determined to be non-performing at 31 December 2020 amounts to KD 179,969 thousand (2019: KD 75,756 thousand). The collateral consists of cash, securities, bank guarantees and properties.

### 14 FINANCIAL INVESTMENTS

The table below provides the details of the categorisation of financial investments:

| <i>2020</i>                               | <i>Amortised cost</i><br><i>KD 000's</i> | <i>Fair value through other comprehensive income</i><br><i>KD 000's</i> | <i>Fair value through statement of income</i><br><i>KD 000's</i> | <i>Total</i><br><i>KD 000's</i> |
|---|--|---|--|---------------------------------|
| <b>Investment securities</b>              |  |   |  |                                 |
| Debt securities - Government (Non Kuwait) | 857,932                                  | 1,813,428   | -  | 2,671,360                       |
| Debt securities - Non Government          | -  | 1,787,677   | 18,828   | 1,806,505                       |
| Equities                                  | -  | 37,531  | 25,811   | 63,342                          |
| Other investments                         | -  | -   | 212,315  | 212,315                         |
|   | <b>857,932</b>                           | <b>3,638,636</b>  | <b>256,954</b>   | <b>4,753,522</b>                |
| Expected credit losses                    | (24,744)                                 | -   | -  | (24,744)                        |
|   | <b>833,188</b>                           | <b>3,638,636</b>  | <b>256,954</b>   | <b>4,728,778</b>                |
| <b>Central Bank of Kuwait bonds</b>       | 830,233                                  | -   | -  | 830,233                         |
| <b>Kuwait Government treasury bonds</b>   | 462,922                                  | -   | -  | 462,922                         |
|   | <b>2,126,343</b>                         | <b>3,638,636</b>  | <b>256,954</b>   | <b>6,021,933</b>                |

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14 FINANCIAL INVESTMENTS (continued)

| 2019                                      | Amortised cost<br>KD 000's | Fair value<br>through other<br>comprehensive<br>income<br>KD 000's | Fair value<br>through<br>statement of<br>income<br>KD 000's | Total<br>KD 000's |
|---|----------------------------|--|---|-------------------|
| Investment securities                     |                            |  |   |                   |
| Debt securities - Government (Non Kuwait) | 834,170                    | 1,661,773  | -   | 2,495,943         |
| Debt securities - Non Government          | -                          | 1,510,270  | -   | 1,510,270         |
| Equities                                  | -                          | 43,125   | 26,935  | 70,060            |
| Other investments                         | -                          | -  | 162,303   | 162,303           |
|   | 834,170                    | 3,215,168  | 189,238   | 4,238,576         |
| Expected credit losses                    | (24,014)                   | -  | -   | (24,014)          |
|   | 810,156                    | 3,215,168  | 189,238   | 4,214,562         |
| Central Bank of Kuwait bonds              | 823,229                    | -  | -   | 823,229           |
| Kuwait Government treasury bonds          | 662,175                    | -  | -   | 662,175           |
|   | 2,295,560                  | 3,215,168  | 189,238   | 5,699,966         |

Investments in debt securities are subject to Expected Credit Losses. Central Bank of Kuwait bonds and Kuwait Government treasury bonds are not subject to Expected Credit Losses. An analysis of changes in the gross carrying amount and the corresponding Expected Credit Losses in relation to Investment in debt securities are as follows:

| 2020   | Stage 1<br>KD 000's | Stage 2<br>KD 000's | Stage 3<br>KD 000's | Total<br>KD 000's |
|--|---------------------|---------------------|---------------------|-------------------|
| Gross carrying amount as at 1 January 2020         | 3,466,874           | 539,339             | -                   | 4,006,213         |
| Assets purchased/derecognised during the year -Net | 464,597             | (117,628)           | -                   | 346,969           |
| Transfer between stages                            | 14,613              | (19,166)            | 4,553               | -                 |
| Fair value and exchange movements                  | 109,518             | (246)               | (3,417)             | 105,855           |
| At 31 December 2020                                | 4,055,602           | 402,299             | 1,136               | 4,459,037         |
| 2019   | Stage 1<br>KD 000's | Stage 2<br>KD 000's | Stage 3<br>KD 000's | Total<br>KD 000's |
| Gross carrying amount as at 1 January 2019         | 2,867,755           | 649,651             | -                   | 3,517,406         |
| Assets purchased/derecognised during the year -Net | 511,674             | (148,740)           | -                   | 362,934           |
| Transfer between stages                            | (39,296)            | 39,296              | -                   | -                 |
| Fair value and exchange movements                  | 126,741             | (868)               | -                   | 125,873           |
| At 31 December 2019                                | 3,466,874           | 539,339             | -                   | 4,006,213         |

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### 14 FINANCIAL INVESTMENTS (continued)

| 2020   | Stage 1<br>KD 000's | Stage 2<br>KD 000's | Stage 3<br>KD 000's | Total<br>KD 000's |
|--|---------------------|---------------------|---------------------|-------------------|
| ECL allowance as at 1 January 2020                       | 11,528              | 25,207              | -                   | 36,735            |
| Impact due to purchase/de-recognition                    | 3,350               | (786)               | -                   | 2,564             |
| Impact due to transfer between stages                    | 84                  | (3,860)             | 5,050               | 1,274             |
| Re-measurement of ECL                                    | 8,245               | 1,669               | -                   | 9,914             |
| Net charge (release) to consolidated statement of income | 11,679              | (2,977)             | 5,050               | 13,752            |
| At 31 December 2020                                      | 23,207              | 22,230              | 5,050               | 50,487            |
| 2019   | Stage 1<br>KD 000's | Stage 2<br>KD 000's | Stage 3<br>KD 000's | Total<br>KD 000's |
| ECL allowance as at 1 January 2019                       | 6,606               | 26,623              | -                   | 33,229            |
| Impact due to purchase/de-recognition                    | 3,465               | (924)               | -                   | 2,541             |
| Impact due to transfer between stages                    | (117)               | 352                 | -                   | 235               |
| Re-measurement of ECL                                    | 1,574               | (844)               | -                   | 730               |
| Net charge (release) to consolidated statement of income | 4,922               | (1,416)             | -                   | 3,506             |
| At 31 December 2019                                      | 11,528              | 25,207              | -                   | 36,735            |

ECL allowance for investments in debt securities as at 31 December 2020 consists of KD 24,744 thousand (2019: KD 24,014 thousand) in respect of debt securities carried at amortised cost and KD 25,743 thousand (2019: KD 12,721 thousand) in respect of debt securities carried at fair value through other comprehensive income.

The Group has classified certain unquoted equity investments at fair value through other comprehensive income on the basis that these are not held for trading. The dividend received on such investments during 2020 was KD 346 thousand (2019: KD 1,898 thousand). During the year, the Group sold FVOCI equity investments with a carrying value of KD 2 thousand (2019: KD 3,320 thousand) and the realised loss on sale amounted to KD 61 thousand (2019: realised gain of KD 2,399 thousand).

### 15 INVESTMENT IN ASSOCIATES

Associates of the Group:

|  | Carrying value   |                  |
|--|------------------|------------------|
|  | 2020<br>KD 000's | 2019<br>KD 000's |
| Bank of London and the Middle East (Note 26) | -                | 29,595           |
| Others                                       | 5,195            | 5,702            |
|  | 5,195            | 35,297           |

During the year the Group provided KD 408 thousand (2019: KD 200 thousand) by way of impairment in respect of its associates. The impairment in respect of associates is calculated as the difference between fair value less cost of disposal and the carrying value. Fair value less cost of disposal is determined using market multiples.

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## 16 GOODWILL AND OTHER INTANGIBLE ASSETS

|  | <i>Goodwill</i><br><i>KD 000's</i> | <i>Intangible</i><br><i>Assets</i><br><i>KD 000's</i> | <i>Total</i><br><i>KD 000's</i> |
|--|------------------------------------|---|---------------------------------|
| <b>Cost</b>                                      |                                    |   |                                 |
| At 1 January 2020                                | 405,104                            | 220,548   | 625,652                         |
| Exchange rate adjustments                        | 600                                | 340   | 940                             |
| At 31 December 2020                              | <u>405,704</u>                     | <u>220,888</u>  | <u>626,592</u>                  |
| <b>Accumulated amortisation &amp; impairment</b> |                                    |   |                                 |
| At 1 January 2020                                | -                                  | 42,725  | 42,725                          |
| Amortisation charge for the year                 | -                                  | 1,647   | 1,647                           |
| Exchange rate adjustments                        | -                                  | 339   | 339                             |
| At 31 December 2020                              | <u>-</u>                           | <u>44,711</u>   | <u>44,711</u>                   |
| <b>Net book value</b>                            |                                    |   |                                 |
| At 31 December 2020                              | <u>405,704</u>                     | <u>176,177</u>  | <u>581,881</u>                  |
|  |                                    |   |                                 |
|  | <i>Goodwill</i><br><i>KD 000's</i> | <i>Intangible</i><br><i>Assets</i><br><i>KD 000's</i> | <i>Total</i><br><i>KD 000's</i> |
| <b>Cost</b>                                      |                                    |   |                                 |
| At 1 January 2019                                | 398,056                            | 218,466   | 616,522                         |
| Exchange rate adjustments                        | 7,048                              | 2,082   | 9,130                           |
| At 31 December 2019                              | <u>405,104</u>                     | <u>220,548</u>  | <u>625,652</u>                  |
| <b>Accumulated amortisation &amp; impairment</b> |                                    |   |                                 |
| At 1 January 2019                                | -                                  | 37,549  | 37,549                          |
| Amortisation charge for the year                 | -                                  | 3,198   | 3,198                           |
| Exchange rate adjustments                        | -                                  | 1,978   | 1,978                           |
| At 31 December 2019                              | <u>-</u>                           | <u>42,725</u>   | <u>42,725</u>                   |
| <b>Net book value</b>                            |                                    |   |                                 |
| At 31 December 2019                              | <u>405,104</u>                     | <u>177,823</u>  | <u>582,927</u>                  |

Net book value of goodwill as at 31 December 2020 includes KD 334,531 thousand (2019: KD 334,531 thousand) in respect of Boubyan Bank K.S.C.P., KD 68,823 thousand (2019: KD 67,672 thousand) in respect of National Bank of Kuwait - Egypt S.A.E. and KD 2,350 thousand (2019: KD 2,901 thousand) in respect of Credit Bank of Iraq S.A.

Net book value of intangible assets as at 31 December 2020 includes banking licences and brand amounting to KD 158,623 thousand (2019: KD 158,623 thousand), customer relationships and core deposits amounting to KD 10,844 thousand (2019: KD 12,490 thousand) and brokerage licences amounting to KD 6,710 thousand (2019: KD 6,710 thousand). Intangible assets with indefinite useful life amounts to KD 165,333 thousand (2019: KD 165,333 thousand). Intangible assets with definite useful life amounting to KD 10,844 thousand (2019: KD 12,490 thousand) are amortised over a period of 5 to 15 years.

**16 GOODWILL AND OTHER INTANGIBLE ASSETS (continued)****Impairment testing for goodwill and intangible assets with indefinite useful life**

The carrying value of goodwill and intangible assets with indefinite useful life are tested for impairment on an annual basis (or more frequently if evidence exists that goodwill or intangible assets might be impaired) by estimating the recoverable amount of the cash generating unit (CGU) to which these items are allocated using value-in-use calculations unless fair value based on an active market price is higher than the carrying value of the CGU. The value in use calculations use pre-tax cash flow projections based on financial budgets approved by management over a five years period and a relevant terminal growth rate. These cash flows are then discounted to derive a net present value which is compared to the carrying value. The discount rate used is pre-tax and reflects specific risks relating to the relevant cash generating unit.

Since the fair value less cost of disposal of the Group's holding in Boubyan Bank K.S.C.P. is higher than its carrying value, there is no indication that the associated goodwill or intangible assets with indefinite useful life is impaired. Recoverable amount of other goodwill and other intangible assets with indefinite useful life is calculated using value-in-use method based on following inputs. The goodwill in respect of National Bank of Kuwait - Egypt S.A.E. is allocated to a single CGU which consists of identifiable net assets including intangible assets of National Bank of Kuwait - Egypt S.A.E. A discount rate of 16% (2019: 17%) and a terminal growth rate of 5% (2019: 5%) are used to estimate the recoverable amount of this cash generating unit. A discount rate of 9% (2019: 10%) and terminal growth rate of 3% (2019: 3%) are used to estimate the recoverable amount of the brokerage licence in Kuwait. The Group has also performed a sensitivity analysis by varying these input factors by a reasonable margin. Based on such analysis, there are no indications that goodwill or intangible assets with indefinite useful life are impaired.

**17 OTHER ASSETS**

|  | <i>2020</i><br><i>KD 000's</i> | <i>2019</i><br><i>KD 000's</i> |
|--|--------------------------------|--------------------------------|
| Interest receivable                          | 84,979                         | 104,293                        |
| Positive fair value of derivatives (Note 28) | 22,840                         | 33,609                         |
| Sundry debtors and prepayments               | 34,477                         | 42,153                         |
| Investment properties                        | 47,133                         | 46,555                         |
| Properties acquired on settlement of debts   | 12,721                         | 12,790                         |
| Others                                       | 44,183                         | 30,771                         |
|  | <u>246,333</u>                 | <u>270,171</u>                 |

**18 OTHER BORROWED FUNDS**

|   | <i>2020</i><br><i>KD 000's</i> | <i>2019</i><br><i>KD 000's</i> |
|---|--------------------------------|--------------------------------|
| Global Medium Term Notes - USD 750,000 thousand             | 232,239                        | 227,159                        |
| Global Medium Term Sukuk - USD 750,000 thousand             | 229,713                        | -                              |
| Subordinated Tier 2 bonds - KD 150,000 thousand             | 149,388                        | -                              |
| Subordinated Tier 2 bonds - USD 300,000 thousand            | 90,750                         | -                              |
| Subordinated Tier 2 bonds - KD 125,000 thousand             | -                              | 124,801                        |
| Medium term borrowing from banks and financial institutions | 106,575                        | -                              |
|   | <u>808,665</u>                 | <u>351,960</u>                 |

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### 18 OTHER BORROWED FUNDS (continued)

Global Medium Term senior unsecured notes of USD 750,000 thousand were issued in May 2017, with a tenor of 5 years, issued at 99.491 per cent of nominal value and carry a fixed interest rate of 2.75% per annum, payable semi-annually in arrears.

Global Medium Term senior unsecured Sukuk of USD 750,000 thousand were issued by Boubyan Bank K.S.C.P, a subsidiary of the Group in February 2020, with a tenor of 5 years, issued at par and carry at a fixed profit rate of 2.593% per annum, payable semi-annually in arrears.

Subordinated Tier 2 bonds of KD 150,000 thousand were issued in November 2020 with a tenor of up to 10 years, comprising equal tranches of fixed rate bonds and floating rate bonds. Fixed rate bonds carry an interest rate of 4.75% per annum for the first five years and will be reset on the fifth year anniversary of date of issuance. Floating rate bonds carry an interest rate of 3% per annum over the CBK discount rate, reset semi-annually, subject to a maximum of 1% over the prevailing rate for the fixed rate bonds. These bonds are unsecured and callable in whole or in part at the option of the Bank after 5 years from the date of issuance, subject to certain conditions and regulatory approvals.

Subordinated Tier 2 bonds of USD 300,000 thousand were issued in November 2020 with a tenor of up to 10 years, carry a fixed rate of 2.5% per annum for the first five years and will be reset on the fifth year anniversary of date of issuance. These bonds are unsecured and callable in whole or in part at the option of the Bank after 5 years from the date of issuance, subject to certain conditions and regulatory approvals.

Subordinated Tier 2 bonds of KD 125,000 thousand were issued in November 2015 with a tenor of up to 10 years, comprising equal tranches of fixed rate bonds and floating rate bonds. Fixed rate bonds carry an interest rate of 4.75% per annum for the first five years and reset on the fifth year anniversary of date of issuance. Floating rate bonds carry an interest rate of 2.5% per annum over the CBK discount rate, reset semi-annually, subject to a maximum of 1% over the prevailing rate for the fixed rate bonds. These bonds were unsecured and callable in whole or in part at the option of the Bank after 5 years from the date of issuance, subject to certain conditions and regulatory approvals. During the year, the Bank exercised the call option to redeem these bonds.

### 19 OTHER LIABILITIES

|  | <i>2020</i><br><i>KD 000's</i> | <i>2019</i><br><i>KD 000's</i> |
|--|--------------------------------|--------------------------------|
| Interest payable                             | 90,716                         | 132,431                        |
| Income received in advance                   | 39,052                         | 35,954                         |
| Taxation                                     | 22,240                         | 29,431                         |
| Provision on non-cash facilities (Note 13)   | 36,768                         | 31,997                         |
| Accrued expenses                             | 56,771                         | 46,607                         |
| Negative fair value of derivatives (Note 28) | 238,061                        | 101,781                        |
| Post-employment benefit                      | 51,711                         | 39,951                         |
| Lease liabilities                            | 27,007                         | 27,345                         |
| Others                                       | 200,678                        | 163,019                        |
|  | <u>763,004</u>                 | <u>608,516</u>                 |

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**19 OTHER LIABILITIES (continued)****Post-Employment Benefit**

The present value of defined benefit obligations and the related current and past service cost was determined by actuarial valuations using the projected unit credit method. The significant inputs used in the actuarial valuation are a discount rate of 4% (2019: 5%), future salary increases in line with expected consumer price inflation and demographic assumptions of mortality, withdrawal, retirement and disability rates.

The movement in the post-employment benefit was as follows:

|  | <i>2020</i><br><i>KD 000's</i> | <i>2019</i><br><i>KD 000's</i> |
|--|--------------------------------|--------------------------------|
| Balance at 1 January                               | 39,951                         | 37,802                         |
| Net charge during the year                         | 9,386                          | 7,979                          |
| Paid during the year                               | (4,865)                        | (5,830)                        |
| Actuarial loss in respect of defined benefit plans | 7,239                          | -                              |
| Balance at 31 December                             | <u>51,711</u>                  | <u>39,951</u>                  |

**20 SHARE CAPITAL AND RESERVES****a) Share capital**

The authorised share capital of the Bank comprises of 7,500,000,000 (2019: 7,500,000,000) shares of 100 fils each.

|  | <i>2020</i><br><i>KD 000's</i> | <i>2019</i><br><i>KD 000's</i> |
|--|--------------------------------|--------------------------------|
| Issued and fully paid in cash:                               |                                |                                |
| 6,850,185,181 (2019 : 6,523,985,887) shares of 100 fils each | <u>685,019</u>                 | <u>652,399</u>                 |

Annual General Assembly meeting of the shareholders held on 7 March 2020 approved an increase of KD 32,620 thousand (2019: KD 31,067 thousand) in the issued and fully paid share capital of the Bank by issuing 326,199,294 (2019: 310,665,994) bonus shares representing 5% of the share capital. The issued and fully paid up share capital increased from KD 652,398,588.700 to KD 685,018,518.100 and the change in share capital was recorded in the commercial register on 15 March 2020.

The movement in ordinary shares in issue during the year was as follows:

|   | <i>2020</i>          | <i>2019</i>          |
|---|----------------------|----------------------|
| Number of shares in issue as at 1 January   | 6,523,985,887        | 6,213,319,893        |
| Bonus issue                                 | <u>326,199,294</u>   | <u>310,665,994</u>   |
| Number of shares in issue as at 31 December | <u>6,850,185,181</u> | <u>6,523,985,887</u> |

**b) Statutory reserve**

The Board of Directors recommended a transfer of KD 16,312 thousand (2019: KD 15,533 thousand) to the statutory reserve. This is in compliance with the Bank's Articles of Association and the Companies Law, as amended, which require a minimum of 10% of profit for the year attributable to the shareholders of the Bank before KFAS, NLST and Zakat to be transferred to a non-distributable statutory reserve until such time as this reserve exceeds 50% of the Bank's issued capital. Accordingly, the transfer to statutory reserve, which is less than 10% of the profit for the year, is that amount required to make the statutory reserve in excess of 50% of the Bank's issued capital.

Distribution of this reserve is limited to the amount required to enable payment of a dividend of 5% of share capital in years when accumulated profits are not sufficient for the payment of a dividend of that amount.

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**20 SHARE CAPITAL AND RESERVES (continued)**

c) Share premium account

The balance in the share premium account is not available for distribution.

d) Treasury shares and Treasury share reserve

The Bank held the following treasury shares at the year end:

|  | <i>2020</i> | <i>2019</i> |
|--|-------------|-------------|
| Number of treasury shares                                | -           | 56,200,000  |
| Treasury shares as a percentage of total shares in issue | -           | 0.9%        |
| Cost of treasury shares (KD thousand)                    | -           | 39,258      |
| Market value of treasury shares (KD thousand)            | -           | 60,134      |
| Weighted average market value per treasury share (fils)  | -           | 947         |

Movement in treasury shares was as follows:

|                           | <i>No. of shares</i> |                   |
|---------------------------|----------------------|-------------------|
|                           | <i>2020</i>          | <i>2019</i>       |
| Balance as at 1 January   | <b>56,200,000</b>    | 89,200,000        |
| Bonus issue               | <b>2,810,000</b>     | 4,460,000         |
| Sales                     | <b>(59,010,000)</b>  | (37,460,000)      |
| Balance as at 31 December | <u>-</u>             | <u>56,200,000</u> |

The balance in the treasury share reserve account is not available for distribution. Further, an amount equal to the cost of treasury shares is not available for distribution from general reserve throughout the holding period of these treasury shares.

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20 SHARE CAPITAL AND RESERVES (continued)

e) Other reserves

|   | <i>KD 000's</i>        |                          |   |  |                                    |                                    |                               |                             |
|---|------------------------|--------------------------|---|--|------------------------------------|------------------------------------|-------------------------------|-----------------------------|
|   | <i>General reserve</i> | <i>Retained earnings</i> | <i>Foreign currency translation reserve</i> | <i>Cumulative changes in fair values</i> | <i>Share based payment reserve</i> | <i>Actuarial valuation reserve</i> | <i>Proposed cash dividend</i> | <i>Total other reserves</i> |
| Balance as at 1 January 2020                                  | 117,058                | 1,429,694                | (207,046)                                   | 53,153                                   | 14,409                             | -                                  | 226,373                       | 1,633,641                   |
| Profit for the year   | -                      | 246,341                  | -   | -  | -                                  | -                                  | -                             | 246,341                     |
| Other comprehensive loss                                      | -                      | -                        | (2,450)                                     | (27,957)                                 | -                                  | (5,999)                            | -                             | (36,406)                    |
| <b>Total comprehensive income (loss)</b>                      | <b>-</b>               | <b>246,341</b>           | <b>(2,450)</b>                              | <b>(27,957)</b>                          | <b>-</b>                           | <b>(5,999)</b>                     | <b>-</b>                      | <b>209,935</b>              |
| Transfer to statutory reserve (Note 20b)                      | -                      | (16,312)                 | -   | -  | -                                  | -                                  | -                             | (16,312)                    |
| Dividends paid  | -                      | -                        | -   | -  | -                                  | -                                  | (226,373)                     | (226,373)                   |
| Interest paid on perpetual Tier 1 Capital Securities          | -                      | (22,796)                 | -   | -  | -                                  | -                                  | -                             | (22,796)                    |
| Realised loss on equity investments at FVOCI                  | -                      | (61)                     | -   | 61                                       | -                                  | -                                  | -                             | -                           |
| Profit distribution on perpetual Tier 1 Sukuk by a subsidiary | -                      | (3,106)                  | -   | -  | -                                  | -                                  | -                             | (3,106)                     |
| Proposed bonus shares (Note 21)                               | -                      | (34,250)                 | -   | -  | -                                  | -                                  | -                             | (34,250)                    |
| Proposed cash dividend 20 fils per share (Note 21)            | -                      | (137,004)                | -   | -  | -                                  | -                                  | 137,004                       | -                           |
| Modification loss on deferral of loans instalments (Note 33)  | -                      | (130,499)                | -   | -  | -                                  | -                                  | -                             | (130,499)                   |
| <b>At 31 December 2020</b>                                    | <b>117,058</b>         | <b>1,332,007</b>         | <b>(209,496)</b>                            | <b>25,257</b>                            | <b>14,409</b>                      | <b>(5,999)</b>                     | <b>137,004</b>                | <b>1,410,240</b>            |

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20 SHARE CAPITAL AND RESERVES (continued)

|   | <i>General<br/>reserve</i> | <i>Retained<br/>earnings</i> | <i>Foreign<br/>currency<br/>translation<br/>reserve</i> | <i>Cumulative<br/>changes in<br/>fair values</i> | <i>Share based<br/>payment<br/>reserve</i> | <i>Proposed<br/>cash<br/>dividend</i> | <i>Total<br/>other<br/>reserves</i> |
|---|----------------------------|------------------------------|---|--|--|---------------------------------------|-------------------------------------|
| Balance as at 1 January 2019                                      | 117,058                    | 1,315,182                    | (225,725)   | 13,311   | 14,409                                     | 214,344                               | 1,448,579                           |
| Profit for the year   | -                          | 401,291                      | -   | -  | -  | -                                     | 401,291                             |
| Other comprehensive income  | -                          | -                            | 18,679  | 42,241   | -  | -                                     | 60,920                              |
| <b>Total comprehensive income</b>                                 | <b>-</b>                   | <b>401,291</b>               | <b>18,679</b>   | <b>42,241</b>                                    | <b>-</b>                                   | <b>-</b>                              | <b>462,211</b>                      |
| Transfer to statutory reserve (Note 20b)                          | -                          | (15,533)                     | -   | -  | -  | -                                     | (15,533)                            |
| Dividends paid  | -                          | -                            | -   | -  | -  | (214,344)                             | (214,344)                           |
| Interest paid on perpetual Tier 1 Capital Securities              | -                          | (12,258)                     | -   | -  | -  | -                                     | (12,258)                            |
| Realised gain on equity investments at FVOCI                      | -                          | 2,399                        | -   | (2,399)  | -  | -                                     | -                                   |
| Transaction costs on issue of Perpetual Tier 1 Capital Securities | -                          | (881)                        | -   | -  | -  | -                                     | (881)                               |
| Profit distribution on perpetual Tier 1 Sukuk by a subsidiary     | -                          | (3,069)                      | -   | -  | -  | -                                     | (3,069)                             |
| Proposed bonus shares (Note 21)                                   | -                          | (32,620)                     | -   | -  | -  | -                                     | (32,620)                            |
| Proposed cash dividend 35 fils per share (Note 21)                | -                          | (226,373)                    | -   | -  | -  | 226,373                               | -                                   |
| Increase in holding in subsidiaries                               | -                          | 1,702                        | -   | -  | -  | -                                     | 1,702                               |
| Other movements   | -                          | (146)                        | -   | -  | -  | -                                     | (146)                               |
| <b>At 31 December 2019</b>  | <b>117,058</b>             | <b>1,429,694</b>             | <b>(207,046)</b>  | <b>53,153</b>                                    | <b>14,409</b>                              | <b>226,373</b>                        | <b>1,633,641</b>                    |

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**20 SHARE CAPITAL AND RESERVES (continued)****e) Other reserves (continued)**

The general reserve was created in accordance with Bank's Articles of Association and is freely distributable, except for the amount equivalent to the cost of treasury shares.

The foreign currency translation reserve includes the exchange differences on conversion of results and financial position of all group entities including goodwill, intangible assets and any fair value adjustments to the carrying value of assets and liabilities from their functional currency to the presentation currency.

Actuarial valuation reserve represents the loss resulting from increase in the present value of defined benefit plans due to changes in actuarial assumptions.

**21 PROPOSED DIVIDEND**

The Board of Directors recommended distribution of a cash dividend of 20 fils (2019: 35 fils per share) and bonus shares of 5% (2019: 5%) on outstanding shares as at 31 December 2020. The cash dividend and bonus shares, if approved by the shareholders' general assembly, shall be payable to the shareholders after obtaining the necessary regulatory approvals.

**22 PERPETUAL TIER 1 CAPITAL SECURITIES**

The Bank issued the following Perpetual Tier 1 Capital Securities (the "Capital Securities"), through wholly owned special purpose vehicles:

|  | <i>2020</i><br><i>KD 000's</i> | <i>2019</i><br><i>KD 000's</i> |
|--|--------------------------------|--------------------------------|
| USD 700,000 thousand (issued in April 2015 at an interest rate of 5.75% per annum, semi-annually in arrears, until the first call date in April 2021)      | <b>210,700</b>                 | 210,700                        |
| USD 750,000 thousand (issued in November 2019 at an interest rate of 4.5% per annum, semi-annually in arrears, until the first call date in November 2025) | <b>227,738</b>                 | 227,738                        |
| Balance at 31 December   | <b>438,438</b>                 | 438,438                        |

The above mentioned Capital securities are subordinated, unsecured and are eligible to be classified under equity in accordance with IAS 32: Financial Instruments – Presentation. Payments of interest in respect of the Capital Securities may be cancelled (in whole or in part) at the sole discretion of the Bank on a non-cumulative basis. Any such cancellation is not considered an event of default. Payments of interest are treated as a deduction from equity. The Capital Securities have no maturity date and are callable (in whole but not in part) at par at the option of the Bank on the first call date and on every interest payment date thereafter, subject to certain conditions.

**23 SHARE BASED PAYMENT**

The Bank operates a cash settled share based compensation plan and granted options to its senior executives. These options vest if the employees remain in service for a period of three years and will be settled by cash payment determined based on the market value of the Bank's equity shares on vesting date.

The fair value of options granted during the year as determined using the Black-Scholes valuation model was KD 0.785 (2019: KD 0.975) as at the end of the year. The significant inputs into the model were a share price of KD 0.840 (2019: KD 1.070) at the measurement date, a standard deviation of expected share price returns of 20.7% (2019: 25%), option life disclosed above and annual risk free interest rate of 1.5% (2019: 2.75%). The volatility measured at the standard deviation of expected share price returns is based on statistical analysis of daily share prices over the last three years.

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### 23 SHARE BASED PAYMENT (continued)

The following table shows the movement in number of share options during the year:

|                            | <u>2020</u>                 | <u>2019</u>                 |
|----------------------------|-----------------------------|-----------------------------|
|                            | <i>No. of share options</i> | <i>No. of share options</i> |
| Outstanding at 1 January   | 8,444,607                   | 7,928,367                   |
| Granted during the year    | 2,543,895                   | 2,829,298                   |
| Exercised during the year  | (2,885,594)                 | (2,061,303)                 |
| Lapsed during the year     | (1,195,622)                 | (251,755)                   |
| Outstanding at 31 December | <u>6,907,286</u>            | <u>8,444,607</u>            |

The expense accrued on account of share based compensation plans for the year amounts to KD 1,281 thousand (2019: KD 3,454 thousand) and is included under staff expenses.

### 24 FAIR VALUE OF FINANCIAL INSTRUMENTS

The fair value of financial assets and financial liabilities that are traded in active markets are based on quoted market prices or dealer price quotations. For all other financial instruments the Group determines fair values using valuation techniques.

The Group measures fair values using the following fair value hierarchy, which reflects the significance of the inputs used in making the measurements:

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

Level 2: inputs other than quoted prices included within Level 1 that are observable either directly (i.e. as prices) or indirectly (i.e. derived from prices). This category includes instruments valued using quoted prices for identical or similar instruments in market that are considered less than active or other valuation techniques in which all significant inputs are observable from market data. Debt securities under this category mainly include sovereign debt instruments in the Middle East & North Africa (MENA) region.

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

Valuation techniques include discounted cash flow models, comparison with similar instruments for which market observable prices exist, recent transaction information and net asset values. Assumptions and inputs used in valuation techniques include risk-free and benchmark interest rates, credit spreads and other premium used in estimating discount rates, bond and equity prices, foreign currency exchange rates and expected price volatilities and correlations. The objective of valuation techniques is to arrive at a fair value measurement that reflects the price that would be received to sell the asset or paid to transfer the liability in an orderly transaction between market participants at the measurement date.

The Group determines whether transfers have occurred between levels in the hierarchy by reassessing 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.

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24 FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

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

| 2020                                       | Level 1<br>KD 000's | Level 2<br>KD 000's | Level 3<br>KD 000's | Total<br>KD 000's |
|--|---------------------|---------------------|---------------------|-------------------|
| Debt securities                            | 3,216,740           | 389,193             | 14,000              | 3,619,933         |
| Equities and other investments             | 46,497              | 173,876             | 55,284              | 275,657           |
|  | <u>3,263,237</u>    | <u>563,069</u>      | <u>69,284</u>       | <u>3,895,590</u>  |
| Derivative financial instruments (Note 28) | -                   | (215,221)           | -                   | (215,221)         |
| 2019                                       | Level 1<br>KD 000's | Level 2<br>KD 000's | Level 3<br>KD 000's | Total<br>KD 000's |
| Debt securities                            | 2,645,665           | 512,378             | 14,000              | 3,172,043         |
| Equities and other investments             | 47,480              | 119,941             | 64,942              | 232,363           |
|  | <u>2,693,145</u>    | <u>632,319</u>      | <u>78,942</u>       | <u>3,404,406</u>  |
| Derivative financial instruments (Note 28) | -                   | (68,172)            | -                   | (68,172)          |

The table below analyses the movement in level 3 and the income (interest, dividend and realised gain) generated during the year.

|                                   | At 1<br>January 2020<br>KD 000's | Change in<br>fair value<br>KD 000's | Additions<br>KD 000's | Sale/<br>redemption<br>KD 000's | Exchange<br>rate<br>movements<br>KD 000's | At 31<br>December<br>2020<br>KD 000's | Net gains<br>(losses)<br>in the<br>consolidated<br>statement of<br>income<br>KD 000's |
|-----------------------------------|----------------------------------|-------------------------------------|-----------------------|---------------------------------|---|---------------------------------------|---|
| Debt securities                   | 14,000                           | -                                   | -                     | -                               | -   | 14,000                                | 873   |
| Equities and<br>other investments | 64,942                           | (10,620)                            | 2,336                 | (1,372)                         | (2)                                       | 55,284                                | (1,600)   |
|                                   | <u>78,942</u>                    | <u>(10,620)</u>                     | <u>2,336</u>          | <u>(1,372)</u>                  | <u>(2)</u>                                | <u>69,284</u>                         | <u>(727)</u>  |
|                                   | At 1<br>January 2019<br>KD 000's | Change in<br>fair value<br>KD 000's | Additions<br>KD 000's | Sale/<br>redemption<br>KD 000's | Exchange<br>rate<br>movements<br>KD 000's | At 31<br>December<br>2019<br>KD 000's | Net gains<br>(losses)<br>in the<br>consolidated<br>statement of<br>income<br>KD 000's |
| Debt securities                   | 14,000                           | -                                   | -                     | -                               | -   | 14,000                                | 973   |
| Equities and<br>other investments | 83,787                           | (20,520)                            | 6,208                 | (5,280)                         | 747                                       | 64,942                                | (1,310)   |
|                                   | <u>97,787</u>                    | <u>(20,520)</u>                     | <u>6,208</u>          | <u>(5,280)</u>                  | <u>747</u>                                | <u>78,942</u>                         | <u>(337)</u>  |

**24 FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)**

Debt securities included in this category consists of unquoted corporate bonds issued by banks and financial institutions. The fair values of these bonds are estimated using discounted cash flow method using credit spread of 4% (2019: 4%). Equities and other securities included in this category mainly include strategic equity investments and private equity funds which are not traded in an active market. The fair values of these investments are estimated by using valuation techniques that are appropriate in the circumstances. Valuation techniques include discounted cash flow models, observable market information of comparable companies, recent transaction information and net asset values. Significant unobservable inputs used in valuation techniques mainly include discount rate, terminal growth rate, revenue, profit estimates and market multiples such as price to book and price to earnings. Given the diverse nature of these investments, it is not practical to disclose a range of significant unobservable inputs.

Other financial assets and liabilities are carried at amortised cost and the carrying values are not materially different from their fair values as most of these assets and liabilities are of short term maturities or are repriced immediately based on market movement in interest rates. Fair values of remaining financial assets and liabilities carried at amortised cost are estimated mainly using discounted cash flow models incorporating certain assumptions such as credit spreads that are appropriate in the circumstances.

Sensitivity analysis on fair value estimations, by varying input assumptions by a reasonable margin, did not indicate any material impacts on consolidated statement of financial position or consolidated statement of income.

**25 SUBSIDIARIES**

Principal operating subsidiaries:

| <i>Name of entities</i>  | <i>Country of incorporation</i> | <i>Principal business</i> | <i>Percentage ownership</i> |             |
|--|---------------------------------|---------------------------|-----------------------------|-------------|
|  |                                 |                           | <i>2020</i>                 | <i>2019</i> |
| Boubyan Bank K.S.C.P.  | Kuwait                          | Islamic Banking           | <b>59.9</b>                 | 59.9        |
| National Bank of Kuwait - Egypt S.A.E.   | Egypt                           | Banking                   | <b>98.5</b>                 | 98.5        |
| Watani Investment Company K.S.C.(Closed)   | Kuwait                          | Investment Company        | <b>99.9</b>                 | 99.9        |
| National Bank of Kuwait (International) PLC                                      | United Kingdom                  | Banking                   | <b>100.0</b>                | 100.0       |
| National Bank of Kuwait France SA  | France                          | Banking                   | <b>100.0</b>                | 100.0       |
| NBK Banque Privée (Suisse) S.A.  | Switzerland                     | Investment Management     | <b>100.0</b>                | 100.0       |
| National Bank of Kuwait (Lebanon) S.A.L.   | Lebanon                         | Banking                   | <b>85.5</b>                 | 85.5        |
| Credit Bank of Iraq S.A.   | Iraq                            | Banking                   | <b>91.0</b>                 | 91.0        |
| National Investors Group Holdings Limited  | Cayman Islands                  | Investment Company        | <b>100.0</b>                | 100.0       |
| Watani Wealth Management Company   | Saudi Arabia                    | Investment Management     | <b>100.0</b>                | 100.0       |
| Watani Financial Brokerage Company K.S.C. (Closed)                               | Kuwait                          | Brokerage                 | <b>93.3</b>                 | 93.3        |
| Bank of London and the Middle East (held through Boubyan Bank K.S.C.P. (Note 26) | United Kingdom                  | Islamic Banking           | <b>71.1</b>                 | 27.9        |

At 31 December 2020, 38.1% (2019: 38.1%) of the Group's interest in National Bank of Kuwait (Lebanon) S.A.L. was held by an intermediate holding company, NBK Holding (Liban) S.A.L.

The Bank also holds voting capital in certain special purpose entities which have been established to manage funds and fiduciary assets on behalf of the Bank's customers. The Bank does not have a beneficial interest in the underlying assets of these companies. Information about the Group's fund management activities is set out in Note 32.

# National Bank of Kuwait Group

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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### 25 SUBSIDIARIES (continued)

Significant non-controlling interest exists in Boubyan Bank K.S.C.P. as follows:

|  | 2020<br>KD 000's | 2019<br>KD 000's |
|--|------------------|------------------|
| Accumulated balances of non-controlling interest | 381,928          | 374,719          |
| Profit attributable to non-controlling interest  | 12,248           | 24,560           |

Summarised financial information of Boubyan Bank K.S.C.P. is as follows:

| <i>Summarised financial information</i> | 2020<br>KD 000's | 2019<br>KD 000's |
|---|------------------|------------------|
| Assets                                  | 6,437,149        | 5,300,548        |
| Liabilities                             | 5,810,419        | 4,647,367        |
| Net operating income                    | 167,482          | 145,769          |
| Results for the year                    | 33,547           | 62,677           |
| Other comprehensive loss for the year   | (10,935)         | (2,943)          |
|   | 2020<br>KD 000's | 2019<br>KD 000's |
| <i>Summarised cash flow information</i> |                  |                  |
| Operating cash flow                     | (7,564)          | 328,237          |
| Investing cash flow                     | (194,104)        | (90,754)         |
| Financing cash flow                     | 273,526          | 107,487          |

During 2016, Boubyan Bank issued "Tier 1 Sukuk", through a Sharia's compliant Sukuk arrangement amounting to USD 250,000 thousand. Tier 1 Sukuk is a perpetual security in respect of which there is no fixed redemption date and constitutes direct, unsecured, subordinated obligations (senior only to share capital) of the Boubyan Bank subject to the terms and conditions of the Mudaraba Agreement. The Tier 1 Sukuk is listed on the Irish Stock Exchange and NASDAQ Dubai and callable by the Boubyan Bank after five-year period ending May 2021 (the "First Call Date") or any profit payment date thereafter subject to certain redemption conditions. Tier 1 Sukuk bears an expected profit rate of 6.75% per annum to be paid semi-annually in arrears until the First Call Date. After that, the expected profit rate will be reset based on then prevailing 5 years U.S Dollar Mid Swap Rate plus initial margin of 5.588% per annum. At the issuer's sole discretion, it may elect not to make any Mudaraba distributions expected and in such event, the Mudaraba profit will not be accumulated and the event is not considered an event of default. The Group did not subscribe to the Tier 1 Sukuk issue and the total amount is included in non-controlling interest in the consolidated statement of financial position.

### 26 BUSINESS COMBINATION

During the year, the Group, through its subsidiary Boubyan Bank K.S.C.P, acquired an additional equity interest in Bank of London and Middle East plc ("BLME") (previously classified as "investment in associate"), resulting in an increase in its effective ownership from 27.91% to 71.08%. The acquisition will enable the Group to provide its existing and future clients with additional Sharia compliant UK service offerings, particularly wealth management opportunities and to deploy its digital capabilities in BLME's business. Having obtained control, the Group reclassified its investment in BLME from associate to subsidiary and consolidated the financial statements of BLME from 27 January 2020 ("date of acquisition").

As the business combination was achieved in stages, in accordance with IFRS 3: Business Combination, the Group re-measured its previously held equity interest in BLME at the acquisition date fair value.

In compliance with IFRS 3, "Business Combination", the Group has carried out one time 'Purchase Price Allocation (PPA)' exercise.

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#### 26 BUSINESS COMBINATION (continued)

The fair values of assets acquired and liabilities assumed, as well as the non-controlling interests at the proportionate share of BLME's identifiable net assets, are summarized as follows:

|  |                 |
|--|-----------------|
| <b>ASSETS</b>                                    | <b>KD 000's</b> |
| Cash and short term funds                        | 28,602          |
| Deposits with banks                              | 3,031           |
| Islamic financing to customers                   | 538,037         |
| Investment securities                            | 34,294          |
| Investments in associates                        | 484             |
| Other assets                                     | 11,838          |
|  | <u>616,286</u>  |
| <b>LIABILITIES</b>                               |                 |
| Due to banks and other financial institutions    | 149,422         |
| Customer deposits                                | 364,884         |
| Other liabilities                                | 10,483          |
|  | <u>524,789</u>  |
| Net assets                                       | 91,497          |
| Non-controlling interests                        | (3,274)         |
| Fair value of net assets acquired by the Group   | <u>88,223</u>   |
|  | <b>KD 000's</b> |
| Cash and cash equivalents in subsidiary acquired | 28,602          |
| Less: Consideration paid                         | (28,927)        |
| Cash outflow on acquisition                      | <u>(325)</u>    |

The consideration paid, non-controlling interest and fair value of previous held equity interest relating to the above business combination amounted to KD 28,927 thousand, KD 25,516 thousand and KD 16,735 thousand respectively.

The net gain on acquisition amounted to KD 2,726 thousand after adjusting for loss of KD 12,504 thousand on re-measurement of previously held equity interest and transaction cost of KD 1,815 thousand. The net gain is included under "Net investment income" in the consolidated statement of income.

The consolidated statement of income of the Group for the year ended 31 December 2020, includes operating income of KD 13,710 thousand and profit attributable to the equity holders of the Bank of KD 697 thousand in respect of BLME.

Had the business combination taken place at the beginning of the year, operating income of the Group and profit attributable to equity holders of the Bank, would not have been materially different.

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**27 COMMITMENTS AND CONTINGENT LIABILITIES**

|  | 2020<br>KD 000's | 2019<br>KD 000's |
|--|------------------|------------------|
| Commitments on behalf of customers for which there are corresponding liabilities by the customers concerned: |                  |                  |
| Acceptances  | 204,623          | 237,145          |
| Letters of credit  | 432,378          | 459,233          |
| Guarantees   | 3,856,034        | 3,891,746        |
|  | <u>4,493,035</u> | <u>4,588,124</u> |

Irrevocable commitments to extend credit amount to KD 1,210,802 thousand (31 December 2019: KD 701,471 thousand). This includes commitments to extend credit which are irrevocable over the life of the facility or are revocable only in response to a material adverse change.

In the normal course of business, the Group has exposure to various indirect credit commitments which, though not reflected in the consolidated statement of financial position, are subject to normal credit standards, financial controls and monitoring procedures.

These credit commitments do not necessarily represent future cash requirements, since many of these commitments will expire or terminate without being funded. Credit losses, if any, which may result from exposure to such commitments are not expected to be significant.

The Group has commitments in respect of capital expenditure amounting to KD 62,319 thousand (31 December 2019: KD 57,299 thousand).

**28 DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGE ACCOUNTING**

Derivative financial instruments are financial instruments that derive their value by referring to interest rates, foreign exchange rates, index of prices or rates and credit rating or credit index. Notional principal amounts merely represent amounts to which a rate or price is applied to determine the amounts of cash flows to be exchanged and do not represent the potential gain or loss associated with the market or credit risk of such instruments.

Derivative financial instruments are carried at fair value in the consolidated statement of financial position. Positive fair value represents the cost of replacing all transactions with a fair value in the Group's favour had the rights and obligations arising from that instrument been closed in an orderly market transaction at the reporting date. Credit risk in respect of derivative financial instruments is limited to the positive fair value of the instruments. Negative fair value represents the cost to the Group's counter parties of replacing all their transactions with the Group.

The Group deals in interest rate swaps to manage its interest rate risk on interest bearing assets and liabilities and to provide interest rate risk management solutions to customers. Similarly the Group deals in forward foreign exchange contracts for customers and to manage its foreign currency positions and cash flows.

Interest rate swaps used to hedge the change in fair value of the Group's financial assets and liabilities and which qualifies as effective hedging instruments are disclosed as 'held as fair value hedges'. Other interest rate swaps and forward foreign exchange contracts are carried out for customers or used for hedging purpose but do not meet the qualifying criteria for hedge accounting. The risk exposures on account of derivative financial instruments for customers are covered by entering into opposite transactions (back to back) with counter parties or by other risk mitigating transactions.

**Interest rate swaps**

Interest rate swaps are contractual agreements between two counter-parties to exchange interest payments on a defined principal amount for a fixed period of time. In cross currency interest rate swaps, the Group exchanges interest payment in two different currencies on a defined principal amount for a fixed period of time and also exchanges defined principal amounts in two different currencies at inception of the contract and re-exchanges principal amounts on maturity. Profit rate swaps are also included in this category.

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**28 DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGE ACCOUNTING (continued)****Forward foreign exchange**

Forward foreign exchange contracts are agreements to buy or sell currencies at a specified rate and at a future date.

The fair value of derivative financial instruments included in the financial records, together with their notional amounts is summarised as follows:

|   | 2020  |   |                              | 2019  |   |                              |
|---|---|---|------------------------------|---|---|------------------------------|
|   | <i>Positive<br/>fair value<br/>KD 000's</i> | <i>Negative<br/>fair value<br/>KD 000's</i> | <i>Notional<br/>KD 000's</i> | <i>Positive<br/>fair value<br/>KD 000's</i> | <i>Negative<br/>fair value<br/>KD 000's</i> | <i>Notional<br/>KD 000's</i> |
| Interest rate swaps (held as fair value hedges) | 9,447                                       | 219,553                                     | 3,482,334                    | 15,990                                      | 86,968                                      | 3,064,122                    |
| Interest rate swaps (others)                    | 94  | 75  | 50,036                       | 263   | 255   | 90,364                       |
| Forward foreign exchange contracts              | 13,299                                      | 18,433                                      | 2,736,116                    | 17,356                                      | 14,558                                      | 3,599,153                    |
|   | <b>22,840</b>                               | <b>238,061</b>                              | <b>6,268,486</b>             | <b>33,609</b>                               | <b>101,781</b>                              | <b>6,753,639</b>             |

Positive fair value is included in other assets (Note 17) and negative fair value is included in other liabilities (Note 19)

The Group's strategy is not to carry interest rate risk for long duration assets. The Group uses interest rate swaps to hedge its exposure to changes in the fair values due to interest rate risk on certain investments in fixed rate debt securities, fixed-rate corporate loans and fixed rate liabilities issued. Hedge accounting is applied where economic hedge relationships meet the hedge accounting criteria. In fair value hedge relationships, the Group assesses whether the interest rate swaps designated in each hedging relationship is expected to be highly effective in offsetting changes in fair value of the hedged item attributable to interest rate risk using appropriate qualitative and quantitative methods. The Group generally seeks to fully match the critical terms (tenor, notionals, interest rate exposure, currency, interest payments frequency and payment periods) of the hedged item and hedging instrument. The Group minimises counterparty credit risk in derivative instruments by entering into transactions with high-quality counterparties.

Interest rate swaps held as fair value hedges are predominantly based on USD LIBOR and are subject to Interest rate benchmark reforms. The Group has applied the hedging relief available under the amendments to IFRS 9 Financial Instruments relating to interest rate benchmark reforms such as relief on assessment of economic relationship between hedged items and hedging instruments.

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**29 RELATED PARTY TRANSACTIONS**

Related parties comprise board members and executive officers of the Bank, their close family members, companies controlled by them or close family members and associates of the Group. Certain related parties were customers of the Group in the ordinary course of business. Transactions with related parties were made on substantially the same terms, including interest rates and collateral, as those prevailing at the same time for comparable transactions with unrelated parties and did not involve more than a normal amount of risk. Lending to Board Members and their related parties is secured by tangible collateral in accordance with regulations of Central Bank of Kuwait.

Details of the interests of related parties are as follows:

|  | <i>Number of<br/>Board Members<br/>or Executive<br/>Officers</i> |             | <i>Number of<br/>related parties</i> |             | <i>2020<br/>KD 000's</i> | <i>2019<br/>KD 000's</i> |
|--|--|-------------|--------------------------------------|-------------|--------------------------|--------------------------|
|  | <i>2020</i>  | <i>2019</i> | <i>2020</i>                          | <i>2019</i> |                          |                          |
| <b>Board Members</b>                     |  |             |                                      |             |                          |                          |
| Loans (secured)                          | 3  | 3           | 15                                   | 16          | 72,909                   | 78,779                   |
| Contingent liabilities                   | -  | -           | 8                                    | 9           | 23,109                   | 30,671                   |
| Credit cards                             | 4  | 7           | 24                                   | 10          | 90                       | 46                       |
| Deposits                                 | 9  | 9           | 54                                   | 54          | 43,041                   | 30,627                   |
| Collateral against credit facilities     | 3  | 3           | 12                                   | 13          | 253,188                  | 335,201                  |
| Interest and fee income                  |  |             |                                      |             | 3,194                    | 3,624                    |
| Interest expense                         |  |             |                                      |             | 121                      | 315                      |
| Purchase of equipment and other expenses |  |             |                                      |             | 55                       | 30                       |
| <b>Executive Officers</b>                |  |             |                                      |             |                          |                          |
| Loans                                    | 1  | 2           | 5                                    | 7           | 3,257                    | 3,422                    |
| Contingent liabilities                   | 3  | 3           | -                                    | -           | 2                        | 2                        |
| Credit cards                             | 5  | 13          | 10                                   | 7           | 45                       | 108                      |
| Deposits                                 | 12   | 13          | 33                                   | 39          | 8,874                    | 7,101                    |
| Interest and fee income                  |  |             |                                      |             | 479                      | 121                      |
| Interest expense                         |  |             |                                      |             | 90                       | 115                      |
|  |  |             |                                      |             | <i>2020<br/>KD 000's</i> | <i>2019<br/>KD 000's</i> |
| <b>Associates</b>                        |  |             |                                      |             |                          |                          |
| Placements                               |  |             |                                      |             | -                        | 52,280                   |
| Acceptances                              |  |             |                                      |             | -                        | 17,297                   |
|  |  |             |                                      |             | <i>2020<br/>KD 000's</i> | <i>2019<br/>KD 000's</i> |
| Salaries and other short term benefits   |  |             |                                      |             | 7,473                    | 11,502                   |
| Post-employment benefits                 |  |             |                                      |             | 230                      | 418                      |
| Share based compensation                 |  |             |                                      |             | 565                      | 1,539                    |
|  |  |             |                                      |             | <b>8,268</b>             | <b>13,459</b>            |

Board members do not receive any emoluments in the form of fees, salaries or bonuses for their services rendered to the Bank.

### 30 RISK MANAGEMENT

Risk is inherent in the Group's activities but is managed in a structured, systematic manner through a global risk policy which embeds comprehensive risk management into organisational structure, risk measurement and monitoring processes. The overall risk management direction and oversight are provided by the Board of Directors with the support of the Board Risk Committee and the Board Audit Committee. The Group's Risk Management and Internal Audit functions assist Executive Management in controlling and actively managing the Group's overall risk profile.

The Group is exposed to credit risk, liquidity risk, market risk and operational risk.

In accordance with the Central Bank of Kuwait's directives, the Group has implemented a comprehensive system for the measurement and management of risk. This methodology helps in reflecting both the expected loss likely to arise in normal circumstances and unexpected losses, which are an estimate of the ultimate actual loss based on statistical models. Information compiled from all internal business groups are closely examined and analysed to identify and control risks.

Transactions and outstanding risk exposures are quantified and compared against authorised limits, whereas non-quantifiable risks are monitored against policy guidelines and key risk and control indicators. Any discrepancies, excesses or deviation are escalated to management for appropriate action.

As part of its overall risk management, the Group uses interest rate swaps, forward foreign exchange contracts and other instruments to manage exposures resulting from changes in interest rates, foreign exchange, equity risks, credit risks and exposures arising from forecast transactions. Collaterals are used to reduce the Group's credit risks.

The Group's comprehensive risk management framework has specific guidelines that focus on maintaining a diversified portfolio to avoid excessive concentration of risk.

#### 30.1 CREDIT RISK

Credit risk is the risk that counterparty will cause a financial loss to the Group by failing to discharge an obligation. Credit risk arises in the Group's normal course of business.

All significant policies relating to credit risks are reviewed and approved by the Board of Directors.

Credit limits are established for all customers after a careful assessment of their creditworthiness. Standing procedures, outlined in the Group's Credit Policy Manual, require that all credit proposals be subjected to detailed screening by the domestic or international credit control divisions pending submission to the appropriate credit committee. Whenever necessary, all loans are secured by acceptable forms of collateral to mitigate the related credit risks.

In accordance with the instructions of the Central Bank of Kuwait dated 18 December 1996, setting out the rules and regulations regarding the classification of credit facilities, the Group has formed an internal committee comprising competent professional staff and having as its purpose the study and evaluation of the existing credit facilities of each customer of the Group. This committee is required to identify any abnormal situations and difficulties associated with a customer's position which might cause the debt to be classified as irregular, and to determine an appropriate provisioning level. The committee, which meets regularly throughout the year, also studies the positions of those customers whose irregular balances exceed 25% of their total debt, in order to determine whether further provisions are required.

The Group further limits risk through diversification of its assets by geography and industry sector. In addition, all credit facilities are continually monitored based on a periodical review of the credit performance and account rating.

**30 RISK MANAGEMENT (continued)**

**30.1 CREDIT RISK (continued)**

**30.1.1 ASSESSMENT OF EXPECTED CREDIT LOSSES**

**Definition of default**

The Group considers a financial asset to be in default and therefore Stage 3 (credit impaired) for ECL calculations when:

- the borrower is unlikely to pay its credit obligations to the Group in full, without recourse by the Group to actions such as realising security (if any is held);
- the borrower is past due more than 90 days on any material credit obligation to the Group; or
- borrower is considered as credit impaired based on qualitative assessment for internal credit risk Management purposes
- retail facilities from commencement of legal recourse

Any credit impaired or stressed facility that has been restructured would also be considered as in default.

The Group considers investments and interbank balances as in default when the coupon or principal payment is past due for 1 day. The Group considers externally-rated portfolio with ratings 'D' for S&P and Fitch, and 'C' for Moody's as defaulted.

The Group considers a variety of indicators that may indicate unlikelihood to pay as part of a qualitative assessment of whether a customer is in default. Such indicators include:

- breaches of covenants
- borrower having past due liabilities to public creditors or employees
- borrower is deceased

The Group considers a financial asset as 'cured' (i.e. no longer be in default) and therefore reclassified out of stage 3 when it no longer meets any of the default criteria. In respect of restructured facilities which are classified in stage 3, these would be required to complete the moratorium period (if any) and meet the scheduled payments (all on current basis) for at least 1 year (except for retail facilities), or as determined by the Group for consideration for classifying the facility in stage 2/stage 1.

**Significant increase in credit risk**

The Group continuously monitors all assets subject to ECLs. In order to determine whether an instrument or a portfolio of instruments is subject to 12 months ECL or life time ECL, the Group assess as whether there has been a significant increase in credit risk since initial recognition. The quantitative criteria used to determine a significant increase in credit risk is a series of relative and absolute thresholds. Financial assets that are 30 days past due are deemed to have significant increase in credit risk since initial recognition and migrated to stage 2 even if other criteria do not indicate a significant increase in credit risk.

The Group considers a financial instrument with an external rating of "investment grade" as at the reporting date to have low credit risk. In addition to the above quantitative criteria, the Group applies qualitative criteria for the assessment of significant increase in credit risk based on monitoring of certain early warning signals.

**Measurement of ECLs**

ECLs are probability-weighted estimates of credit losses and are measured as the present value of all cash shortfalls discounted at the effective interest rate of the financial instrument. Cash shortfall represents the difference between cash flows due to the Group in accordance with the contract and the cash flows that the Group expects to receive. The key elements in the measurement of ECL include probability of default (PD), loss given default (LGD) and exposure at default (EAD). The Group estimates these elements using appropriate credit risk models taking into consideration the internal and external credit ratings of the assets, nature and value of collaterals, forward-looking macro-economic scenarios, etc.

The Group calculates ECL on credit facilities classified in stage 3 at 100% of the defaulted exposure net of value of eligible collaterals after applying applicable haircuts.

**30 RISK MANAGEMENT (continued)**

**30.1 CREDIT RISK (continued)**

**30.1.1 ASSESSMENT OF EXPECTED CREDIT LOSSES (continued)**

**Measurement of ECLs (continued)**

The Group in estimating ECL for credit facilities has taken into consideration the following key parameters based on inputs from CBK:

- Floor for estimating PDs for specific portfolios
- Eligible collateral with haircuts for determining LGD
- Deemed maturity for exposures in Stage 2
- Credit Conversion Factor on utilized and un-utilized portions for cash and non-cash facilities

**Internal rating and PD estimation process**

In managing its portfolio, the Group utilises ratings and other measures and techniques which seek to take account of all aspects of perceived risk. The Group uses industry-standard rating tools for assessing ratings/scores that are then leveraged for PD estimation process. The tool provides the ability to analyse a business and produces risk ratings at both the obligor and facility levels. The analysis supports the usage of financial factors as well as non-financial subjective factors. The Group also uses external ratings by recognised rating agencies for externally-rated portfolios.

The Probability of Default (PD) is the likelihood that an obligor will default on its obligations in the future. IFRS 9 requires the use of separate PD for a 12-month duration and lifetime duration depending on the stage allocation of the obligor. A PD used for IFRS 9 should reflect the Group's estimate of the future asset quality. The through-the-cycle (TTC) PDs are generated from the rating tool based on the internal/external credit ratings. The Group converts the TTC PDs to point-in-time (PIT) PD term structures using appropriate models and techniques.

The Group assesses the PD for its retail portfolio through behavioural scorecards. The Consumer portfolio is further segmented statistically and risk pools with shared risk characteristics are addressed with different scorecards relevant for each of the risk pool. The segmentation is based on demographic, behavioural and financial variables which distinctly rank order risk. The scorecards were developed using statistical techniques. Executing the scorecard will return an associated PD value for each of the facility. The term structure PDs are then derived using a base PD.

**Exposure at default**

Exposure at default (EAD) represents the amount which the obligor will owe to the Group at the time of default. The Group considers variable exposures that may increase the EAD in addition to the drawn credit line. These exposures arise from undrawn limits and contingent liabilities. Therefore, the exposure will contain both on and off balance sheet values. EAD is estimated taking into consideration the contractual terms such as coupon rates, frequency, reference curves, maturity, pre-payment options, amortization schedule, credit conversion factors, etc. EAD for retail loans incorporate prepayment assumptions whereas for credit cards portfolio, credit conversion factors are applied to estimate the future drawdowns.

**Loss given default**

Loss given default (LGD) is the magnitude of the likely loss if there is a default. The Group estimates LGD parameters based on the history of recovery rates of claims against defaulted counterparties. The LGD models consider the structure, collateral, seniority of the claim, counterparty industry and recovery costs of any collateral that is integral to the financial asset.

**Incorporation of forward-looking information**

The Group considers key economic variables that are expected to have an impact on the credit risk and the ECL in order to incorporate forward-looking information into the ECL models. Key economic variables include, but not limited to, Gross Domestic Product, Equity price index, Oil prices, and Government expenditure. These primarily reflect reasonable and supportable forecasts of the future macro-economic conditions. The consideration of such factors increases the degree of judgment in determination of ECL. The Group employs statistical models to incorporate macro-economic factors on historical default rates. The Group considers 3 scenarios (baseline, upside and downside) of forecasts of macro-economic data separately for designated geographical segments and appropriate probability weights are applied to these scenarios to derive a probability-weighted outcome of expected credit loss. The ECL estimates have been assessed for sensitivity to changes to forecasts of macro-variables and also together with changes to the weights assigned to the scenarios. The impact on ECL is not material. The management reviews the methodologies and assumptions including any forecasts of future economic conditions on a regular basis.

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**30 RISK MANAGEMENT (continued)****30.1 CREDIT RISK (continued)****30.1.2 MAXIMUM EXPOSURE TO CREDIT RISK**

An analysis of loans, advances and Islamic facilities to customers and contingent liabilities before and after taking account of collateral held or other credit enhancements, is as follows:

|  | 2020                               |                                  | 2019                               |                                  |
|--|------------------------------------|----------------------------------|------------------------------------|----------------------------------|
|  | <i>Gross exposure<br/>KD 000's</i> | <i>Net exposure<br/>KD 000's</i> | <i>Gross exposure<br/>KD 000's</i> | <i>Net exposure<br/>KD 000's</i> |
| Loans, advances and Islamic financing to customers | 17,504,342                         | 12,418,411                       | 16,552,598                         | 11,328,972                       |
| Contingent liabilities                             | 4,493,035                          | 4,334,856                        | 4,588,124                          | 4,400,491                        |

**Collateral and other credit enhancements**

The amount, type and valuation of collateral are based on guidelines specified in the risk management framework. The main types of collateral accepted includes real estate, quoted shares, cash collateral and bank guarantees. The revaluation and custody of collaterals are performed independent of the business units.

**30.1.3 RISK CONCENTRATION OF THE MAXIMUM EXPOSURE TO CREDIT RISK**

Concentrations of credit risk arise from exposure to customers having similar characteristics in terms of the geographic location in which they operate or the industry sector in which they are engaged, such that their ability to discharge contractual obligations may be similarly affected by changes in political, economic or other conditions.

Credit risk can also arise due to a significant concentration of Group's assets to any single counterparty. This risk is managed by diversification of the portfolio. The 20 largest loans, advances and Islamic financing to customers outstanding as a percentage of gross loans, advances and Islamic financing to customers as at 31 December 2020 is 15% (2019: 16%).

The Group's financial assets and off-balance sheet items, before taking into account any collateral held or credit enhancements can be analysed by the following geographic regions:

| 2020   | <i>Middle East and North Africa</i> |                  |                  |                  |                 | <i>North America</i> | <i>Europe</i> | <i>Asia</i> | <i>Others</i> | <i>Total</i>      |
|--|-------------------------------------|------------------|------------------|------------------|-----------------|----------------------|---------------|-------------|---------------|-------------------|
|  | <i>KD 000's</i>                     | <i>KD 000's</i>  | <i>KD 000's</i>  | <i>KD 000's</i>  | <i>KD 000's</i> |                      |               |             |               |                   |
| Balances and deposits with banks                   | 3,489,487                           | 401,963          | 713,193          | 97,807           | -               | -                    | -             | -           | -             | 4,702,450         |
| Central Bank of Kuwait bonds                       | 830,233                             | -                | -                | -                | -               | -                    | -             | -           | -             | 830,233           |
| Kuwait Government treasury Bonds                   | 462,922                             | -                | -                | -                | -               | -                    | -             | -           | -             | 462,922           |
| Loans, advances and Islamic financing to customers | 15,325,904                          | 397,034          | 1,125,330        | 364,412          | 291,662         | -                    | -             | -           | -             | 17,504,342        |
| Investment securities                              | 3,666,033                           | 22,618           | 29,212           | 721,435          | 13,823          | -                    | -             | -           | -             | 4,453,121         |
| Other assets                                       | 155,805                             | 2,733            | 22,543           | 2,390            | 3,008           | -                    | -             | -           | -             | 186,479           |
|  | <u>23,930,384</u>                   | <u>824,348</u>   | <u>1,890,278</u> | <u>1,186,044</u> | <u>308,493</u>  | -                    | -             | -           | -             | <u>28,139,547</u> |
| Commitments and contingent liabilities (Note 27)   | 3,127,945                           | 339,984          | 1,347,854        | 884,069          | 3,985           | -                    | -             | -           | -             | 5,703,837         |
|  | <u>27,058,329</u>                   | <u>1,164,332</u> | <u>3,238,132</u> | <u>2,070,113</u> | <u>312,478</u>  | -                    | -             | -           | -             | <u>33,843,384</u> |

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**30 RISK MANAGEMENT (continued)****30.1 CREDIT RISK (continued)****30.1.3 RISK CONCENTRATION OF THE MAXIMUM EXPOSURE TO CREDIT RISK (continued)**

| <b>2019</b>  | <i>Middle<br/>East and<br/>North<br/>Africa<br/>KD 000's</i> | <i>North<br/>America<br/>KD 000's</i> | <i>Europe<br/>KD 000's</i> | <i>Asia<br/>KD 000's</i> | <i>Others<br/>KD 000's</i> | <i>Total<br/>KD 000's</i> |
|--|--|---------------------------------------|----------------------------|--------------------------|----------------------------|---------------------------|
| Balances and deposits with banks                   | 3,494,891  | 705,067                               | 906,852                    | 353,920                  | -                          | 5,460,730                 |
| Central Bank of Kuwait bonds                       | 823,229  | -                                     | -                          | -                        | -                          | 823,229                   |
| Kuwait Government treasury bonds                   | 662,175  | -                                     | -                          | -                        | -                          | 662,175                   |
| Loans, advances and Islamic financing to customers | 14,818,076   | 382,951                               | 719,862                    | 375,937                  | 255,772                    | 16,552,598                |
| Investment securities                              | 3,296,624  | 22,206                                | 70,104                     | 573,527                  | 19,738                     | 3,982,199                 |
| Other assets                                       | 176,211  | 4,177                                 | 23,352                     | 4,849                    | 2,237                      | 210,826                   |
|  | <u>23,271,206</u>  | <u>1,114,401</u>                      | <u>1,720,170</u>           | <u>1,308,233</u>         | <u>277,747</u>             | <u>27,691,757</u>         |
| Commitments and contingent liabilities (Note 27)   | 2,775,531  | 315,361                               | 1,328,457                  | 863,948                  | 6,298                      | 5,289,595                 |
|  | <u>26,046,737</u>  | <u>1,429,762</u>                      | <u>3,048,627</u>           | <u>2,172,181</u>         | <u>284,045</u>             | <u>32,981,352</u>         |

The Group's financial assets and off-balance sheet items, before taking into account any collateral held or credit enhancements, can be analysed by the following industry sectors:

|  | <b>2020<br/>KD 000's</b> | <b>2019<br/>KD 000's</b> |
|--|--------------------------|--------------------------|
| <b>Industry sector</b>                 |                          |                          |
| Trading                                | 2,123,271                | 2,106,532                |
| Manufacturing                          | 3,144,536                | 2,797,628                |
| Banks and other financial institutions | 9,936,940                | 10,541,633               |
| Construction                           | 1,599,860                | 1,455,836                |
| Real Estate                            | 3,842,488                | 3,463,146                |
| Retail                                 | 5,841,638                | 5,506,856                |
| Government                             | 3,558,422                | 3,571,248                |
| Others                                 | 3,796,229                | 3,538,473                |
|  | <u>33,843,384</u>        | <u>32,981,352</u>        |

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**30 RISK MANAGEMENT (continued)****30.1 CREDIT RISK (continued)****30.1.4 CREDIT QUALITY PER CLASS OF FINANCIAL ASSETS**

In managing its portfolio, the Group utilises ratings and other measures and techniques which seek to take account of all aspects of perceived risk. Credit exposures classified as 'High' quality are those where the ultimate risk of financial loss from the obligor's failure to discharge its obligation is assessed to be low. These include facilities to corporate entities with financial condition, risk indicators and capacity to repay which are considered to be good to excellent. Credit exposures classified as 'Standard' quality comprise all other facilities whose payment performance is fully compliant with contractual conditions and which are not 'impaired'. The ultimate risk of possible financial loss on 'Standard' quality is assessed to be higher than that for the exposures classified within the 'High' quality range.

The table below shows the credit quality by class of financial assets for statement of financial position lines, based on the Group's credit rating system.

|  | <i>Neither past due nor impaired</i> |                                    | <i>Past due</i>                       | <i>Total</i><br><i>KD 000's</i> |
|--|--------------------------------------|------------------------------------|---------------------------------------|---------------------------------|
|  | <i>High</i><br><i>KD 000's</i>       | <i>Standard</i><br><i>KD 000's</i> | <i>or impaired</i><br><i>KD 000's</i> |                                 |
| <b>2020</b>  |                                      |                                    |                                       |                                 |
| Balances and short term deposits with banks        | 3,660,103                            | -                                  | 27,968                                | 3,688,071                       |
| Central Bank of Kuwait bonds                       | 830,233                              | -                                  | -                                     | 830,233                         |
| Kuwait Government treasury bonds                   | 462,922                              | -                                  | -                                     | 462,922                         |
| Deposits with banks                                | 785,529                              | 241,618                            | 3,017                                 | 1,030,164                       |
| Loans, advances and Islamic financing to customers | 15,837,486                           | 1,861,450                          | 492,630                               | 18,191,566                      |
| Investments in debt securities – Amortised cost    | 71,688                               | 786,244                            | -                                     | 857,932                         |
| Investments in debt securities – FVOCI             | 2,969,885                            | 630,084                            | 1,136                                 | 3,601,105                       |
| Investments in debt securities – FVPL              | 18,828                               | -                                  | -                                     | 18,828                          |
|  | <u>24,636,674</u>                    | <u>3,519,396</u>                   | <u>524,751</u>                        | <u>28,680,821</u>               |
| <b>2019</b>  |                                      |                                    |                                       |                                 |
| Balances and short term deposits with banks        | 3,552,453                            | -                                  | -                                     | 3,552,453                       |
| Central Bank of Kuwait bonds                       | 823,229                              | -                                  | -                                     | 823,229                         |
| Kuwait Government treasury bonds                   | 662,175                              | -                                  | -                                     | 662,175                         |
| Deposits with banks                                | 1,584,829                            | 325,513                            | -                                     | 1,910,342                       |
| Loans, advances and Islamic financing to customers | 15,529,923                           | 1,219,147                          | 312,264                               | 17,061,334                      |
| Investments in debt securities – Amortised cost    | 26,677                               | 807,493                            | -                                     | 834,170                         |
| Investments in debt securities – FVOCI             | 2,477,622                            | 694,421                            | -                                     | 3,172,043                       |
|  | <u>24,656,908</u>                    | <u>3,046,574</u>                   | <u>312,264</u>                        | <u>28,015,746</u>               |

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## 30 RISK MANAGEMENT (continued)

## 30.1 CREDIT RISK (continued)

## 30.1.5 AGEING ANALYSIS OF PAST DUE OR IMPAIRED LOANS, ADVANCES AND ISLAMIC FINANCING TO CUSTOMERS

|                    | <i>Corporate</i>                              |   | <i>Retail</i>                                 |   | <i>Total</i>                                  |   |
|--------------------|---|---|---|---|---|---|
|                    | <i>Past due and not impaired<br/>KD 000's</i> | <i>Past due and impaired<br/>KD 000's</i> | <i>Past due and not impaired<br/>KD 000's</i> | <i>Past due and impaired<br/>KD 000's</i> | <i>Past due and not impaired<br/>KD 000's</i> | <i>Past due and impaired<br/>KD 000's</i> |
| <b>2020</b>        |   |   |   |   |   |   |
| Up to 30 days      | 76,833  | 282                                       | 36,969  | 538                                       | 113,802                                       | 820                                       |
| 31 - 60 days       | 20,695  | -   | 30,361  | 43  | 51,056  | 43  |
| 61 - 90 days       | 8,952   | 79  | 6,439   | 24  | 15,391  | 103                                       |
| 91-180 days        | -   | 32,451                                    | -   | 5,455                                     | -   | 37,906                                    |
| More than 180 days | -   | 175,510                                   | -   | 97,999                                    | -   | 273,509                                   |
|                    | <u>106,480</u>                                | <u>208,322</u>                            | <u>73,769</u>                                 | <u>104,059</u>                            | <u>180,249</u>                                | <u>312,381</u>                            |
| <b>2019</b>        |   |   |   |   |   |   |
| Up to 30 days      | 31,800  | 22,809                                    | 42,782  | 13  | 74,582  | 22,822                                    |
| 31 - 60 days       | 21,309  | -   | 18,727  | -   | 40,036  | -   |
| 61 - 90 days       | 6,611   | -   | 4,132   | 2   | 10,743  | 2   |
| 91-180 days        | -   | 1,858                                     | -   | 24,572                                    | -   | 26,430                                    |
| More than 180 days | -   | 60,056                                    | -   | 77,593                                    | -   | 137,649                                   |
|                    | <u>59,720</u>                                 | <u>84,723</u>                             | <u>65,641</u>                                 | <u>102,180</u>                            | <u>125,361</u>                                | <u>186,903</u>                            |

Of the aggregate amount of gross past due or impaired loans, advances and Islamic financing to customers, the fair value of collateral that the Group held as at 31 December 2020 was KD 200,737 thousand (2019: KD 92,129 thousand).

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**30 RISK MANAGEMENT (continued)****30.2 LIQUIDITY RISK**

Liquidity risk is the risk that the Group will be unable to meet its financial liabilities when they fall due. To limit this risk, management has arranged diversified funding sources, manages assets with liquidity in mind and monitors liquidity on a daily basis.

The table below summarises the maturity profile of Group's assets, liabilities and equity based on contractual cash flows and maturity dates. This does not necessarily take account of the effective maturities.

|   | <i>Up to 3<br/>months<br/>KD 000's</i> | <i>3 to 12<br/>months<br/>KD 000's</i> | <i>Over 1<br/>year<br/>KD 000's</i> | <i>Total<br/>KD 000's</i> |
|---|--|--|-------------------------------------|---------------------------|
| <b>2020</b>   |  |  |                                     |                           |
| <b>Assets</b>   |  |  |                                     |                           |
| Cash and deposits with banks                          | 4,735,951                              | 165,864                                | 28,929                              | 4,930,744                 |
| Central Bank of Kuwait bonds                          | 518,803                                | 311,430                                | -                                   | 830,233                   |
| Kuwait Government treasury bonds                      | -                                      | 35,500                                 | 427,422                             | 462,922                   |
| Loans, advances and Islamic financing to<br>Customers | 5,094,225                              | 2,021,684                              | 10,388,433                          | 17,504,342                |
| Investment securities                                 | 517,128                                | 752,978                                | 3,458,672                           | 4,728,778                 |
| Investment in associates                              | -                                      | -                                      | 5,195                               | 5,195                     |
| Land, premises and equipment                          | -                                      | -                                      | 426,963                             | 426,963                   |
| Goodwill and other intangible assets                  | -                                      | -                                      | 581,881                             | 581,881                   |
| Other assets  | 157,800                                | 23,223                                 | 65,310                              | 246,333                   |
|   | <u>11,023,907</u>                      | <u>3,310,679</u>                       | <u>15,382,805</u>                   | <u>29,717,391</u>         |
| <b>Liabilities and equity</b>                         |  |  |                                     |                           |
| Due to banks and other financial institutions         | 4,878,897                              | 1,091,685                              | 10,991                              | 5,981,573                 |
| Customer deposits                                     | 14,636,146                             | 1,811,947                              | 656,139                             | 17,104,232                |
| Certificates of deposit issued                        | 633,231                                | 285,631                                | -                                   | 918,862                   |
| Other borrowed funds                                  | -                                      | -                                      | 808,665                             | 808,665                   |
| Other liabilities                                     | 429,421                                | 16,101                                 | 317,482                             | 763,004                   |
| Share capital and reserves                            | -                                      | -                                      | 3,173,005                           | 3,173,005                 |
| Proposed cash dividend                                | 137,004                                | -                                      | -                                   | 137,004                   |
| Perpetual Tier 1 Capital Securities                   | -                                      | -                                      | 438,438                             | 438,438                   |
| Non-controlling interests                             | -                                      | -                                      | 392,608                             | 392,608                   |
|   | <u>20,714,699</u>                      | <u>3,205,364</u>                       | <u>5,797,328</u>                    | <u>29,717,391</u>         |

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**30 RISK MANAGEMENT (continued)**

**30.2 LIQUIDITY RISK (continued)**

|  | <i>Up to 3<br/>months<br/>KD 000's</i> | <i>3 to 12<br/>months<br/>KD 000's</i> | <i>Over 1<br/>year<br/>KD 000's</i> | <i>Total<br/>KD 000's</i> |
|--|--|--|-------------------------------------|---------------------------|
| <b>2019</b>  |  |  |                                     |                           |
| <b>Assets</b>                                      |  |  |                                     |                           |
| Cash and deposits with banks                       | 5,281,618                              | 411,747                                | 2,889                               | 5,696,254                 |
| Central Bank of Kuwait bonds                       | 515,775                                | 307,454                                |                                     | 823,229                   |
| Kuwait Government treasury bonds                   | 77,000                                 | 144,000                                | 441,175                             | 662,175                   |
| Loans, advances and Islamic financing to customers | 4,082,071                              | 2,653,219                              | 9,817,308                           | 16,552,598                |
| Investment securities                              | 462,839                                | 467,986                                | 3,283,737                           | 4,214,562                 |
| Investment in associates                           |  |  | 35,297                              | 35,297                    |
| Land, premises and equipment                       |  |  | 433,540                             | 433,540                   |
| Goodwill and other intangible assets               |  |  | 582,927                             | 582,927                   |
| Other assets                                       | 168,883                                | 33,695                                 | 67,593                              | 270,171                   |
|  | <u>10,588,186</u>                      | <u>4,018,101</u>                       | <u>14,664,466</u>                   | <u>29,270,753</u>         |
| <b>Liabilities and equity</b>                      |  |  |                                     |                           |
| Due to banks and other financial institutions      | 5,717,489                              | 1,736,642                              | 127,798                             | 7,581,929                 |
| Customer deposits                                  | 12,359,638                             | 2,953,053                              | 617,886                             | 15,930,577                |
| Certificates of deposit issued                     | 327,415                                | 211,196                                |                                     | 538,611                   |
| Other borrowed funds                               |  |  | 351,960                             | 351,960                   |
| Other liabilities                                  | 423,853                                | 9,063                                  | 175,600                             | 608,516                   |
| Share capital and reserves                         |  |  | 3,207,371                           | 3,207,371                 |
| Proposed cash dividend                             | 226,373                                |  |                                     | 226,373                   |
| Perpetual Tier 1 Capital Securities                |  |  | 438,438                             | 438,438                   |
| Non-controlling interests                          |  |  | 386,978                             | 386,978                   |
|  | <u>19,054,768</u>                      | <u>4,909,954</u>                       | <u>5,306,031</u>                    | <u>29,270,753</u>         |

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30 RISK MANAGEMENT (continued)

30.2 LIQUIDITY RISK (continued)

The liquidity profile of financial liabilities of the Group summarised below reflects the cash flows including future interest payments over the life of these financial liabilities based on contractual repayment arrangements.

|  | <i>Up to 3<br/>months<br/>KD 000's</i> | <i>3 to 12<br/>months<br/>KD 000's</i> | <i>Over 1<br/>year<br/>KD 000's</i> | <i>Total<br/>KD 000's</i> |
|--|--|--|-------------------------------------|---------------------------|
| <b>2020</b>  |  |  |                                     |                           |
| <b>Financial Liabilities</b>   |  |  |                                     |                           |
| Due to banks and other financial institutions                        | 4,883,508                              | 1,098,156                              | 12,281                              | 5,993,945                 |
| Customer deposits  | 14,730,515                             | 1,852,136                              | 716,370                             | 17,299,021                |
| Certificates of deposit issued                                       | 633,421                                | 286,136                                | -                                   | 919,557                   |
| Other borrowed funds   | 3,519                                  | 19,518                                 | 912,558                             | 935,595                   |
|  | <u>20,250,963</u>                      | <u>3,255,946</u>                       | <u>1,641,209</u>                    | <u>25,148,118</u>         |
| <b>Contingent liabilities and commitments</b>                        |  |  |                                     |                           |
| Contingent liabilities   | 1,152,531                              | 1,474,293                              | 1,866,211                           | 4,493,035                 |
| Irrevocable commitments  | 91,853                                 | 154,876                                | 964,073                             | 1,210,802                 |
|  | <u>1,244,384</u>                       | <u>1,629,169</u>                       | <u>2,830,284</u>                    | <u>5,703,837</u>          |
| <b>Derivative financial instruments<br/>settled on a gross basis</b> |  |  |                                     |                           |
| Contractual amounts payable  | 2,147,085                              | 629,467                                | 89,207                              | 2,865,759                 |
| Contractual amounts receivable                                       | 2,146,919                              | 624,465                                | 82,730                              | 2,854,114                 |
|  | <u>2,146,919</u>                       | <u>624,465</u>                         | <u>82,730</u>                       | <u>2,854,114</u>          |
|  | <i>Up to 3<br/>months<br/>KD 000's</i> | <i>3 to 12<br/>months<br/>KD 000's</i> | <i>Over 1<br/>year<br/>KD 000's</i> | <i>Total<br/>KD 000's</i> |
| <b>2019</b>  |  |  |                                     |                           |
| <b>Financial Liabilities</b>   |  |  |                                     |                           |
| Due to banks and other financial institutions                        | 5,729,714                              | 1,763,398                              | 133,267                             | 7,626,379                 |
| Customer deposits  | 12,381,043                             | 3,026,956                              | 691,187                             | 16,099,186                |
| Certificates of deposit issued                                       | 328,343                                | 212,896                                | -                                   | 541,239                   |
| Other borrowed funds   | -                                      | 12,509                                 | 391,881                             | 404,390                   |
|  | <u>18,439,100</u>                      | <u>5,015,759</u>                       | <u>1,216,335</u>                    | <u>24,671,194</u>         |
| <b>Contingent liabilities and commitments</b>                        |  |  |                                     |                           |
| Contingent liabilities   | 1,029,923                              | 1,392,635                              | 2,165,566                           | 4,588,124                 |
| Irrevocable commitments  | 72,132                                 | 149,425                                | 479,914                             | 701,471                   |
|  | <u>1,102,055</u>                       | <u>1,542,060</u>                       | <u>2,645,480</u>                    | <u>5,289,595</u>          |
| <b>Derivative financial instruments<br/>settled on a gross basis</b> |  |  |                                     |                           |
| Contractual amounts payable  | 2,201,357                              | 1,293,436                              | 246,059                             | 3,740,852                 |
| Contractual amounts receivable                                       | 2,203,782                              | 1,290,473                              | 248,708                             | 3,742,963                 |
|  | <u>2,203,782</u>                       | <u>1,290,473</u>                       | <u>248,708</u>                      | <u>3,742,963</u>          |

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**30 RISK MANAGEMENT (continued)****30.3 MARKET RISK**

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to changes in market prices. Market risks arise from open positions in interest rate, currency and equity products, all of which are exposed to general and specific market movements and changes in the level of volatility of market rates or prices such as interest rates, foreign exchange rates and equity prices.

**30.3.1 INTEREST RATE RISK**

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

The Group is not excessively exposed to interest rate risk as its assets and liabilities are repriced regularly and most exposures arising on medium term fixed rate lending or fixed rate borrowing are covered by interest rate swaps. Furthermore, the re-pricing gaps of its assets and liabilities are carefully monitored and controlled through limits pre-established by the Board of Directors and adjusted where necessary, to reflect the changing market conditions.

**Interest rate sensitivity**

Interest rate sensitivity of profit measures the effect of the assumed changes in interest rates on the net interest income for one year, based on the interest bearing financial assets and financial liabilities held at the year end. This includes the effect of hedging instruments but excludes loan commitments. The sensitivity on equity is the impact arising from changes in interest rate on fair value of investments in debt securities classified as FVOCI. Sensitivity to interest rate movements will be on a symmetric basis as financial instruments giving rise to non-symmetric movements are not significant.

Based on the Group's financial assets and financial liabilities held at the year end, an assumed 25 basis points increase in interest rate, with all other variables held constant, would impact the Group's profit and equity as follows:

| Currency | Movement in Basis points | 2020                         |                              | 2019                         |                              |
|----------|--------------------------|------------------------------|------------------------------|------------------------------|------------------------------|
|          |                          | Effect on profit<br>KD 000's | Effect on equity<br>KD 000's | Effect on profit<br>KD 000's | Effect on equity<br>KD 000's |
| KWD      | +25                      | 8,761                        | -                            | 7,588                        | -                            |
| USD      | +25                      | 1,412                        | (2)                          | 2,174                        | (3)                          |
| EUR      | +25                      | 493                          | -                            | 573                          | -                            |
| GBP      | +25                      | 716                          | -                            | 550                          | -                            |
| EGP      | +25                      | 80                           | (372)                        | 23                           | (37)                         |

**30.3.2 FOREIGN EXCHANGE RISK**

Foreign exchange risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates.

Foreign exchange risks are controlled through limits pre-established by the Board of Directors on currency position exposures. In general assets are typically funded in the same currency as that of the business being transacted to eliminate exchange exposures. Appropriate segregation of duties exists between the treasury front and back office functions, while compliance with position limits is independently monitored on an ongoing basis.

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**30 RISK MANAGEMENT (continued)****30.3 MARKET RISK (continued)****30.3.2 FOREIGN EXCHANGE RISK (continued)**

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

| <i>Currency</i> | <i>% Change in<br/>currency rate</i> | <i>2020</i>                          | <i>2019</i>                          |
|-----------------|--------------------------------------|--------------------------------------|--------------------------------------|
|                 |                                      | <i>Effect on profit<br/>KD 000's</i> | <i>Effect on profit<br/>KD 000's</i> |
| USD             | +5                                   | 2,252                                | 3,071                                |
| GBP             | +5                                   | 149                                  | 156                                  |
| EUR             | +5                                   | (240)                                | (8)                                  |
| Other           | +5                                   | (142)                                | (219)                                |

**30.3.3 EQUITY PRICE RISK**

Equity price risk is the risk that the fair values of equities will fluctuate as a result of changes in the level of equity indices or the value of individual share prices. Equity price risk arises from the change in fair values of equity investments. The Group manages the risk through diversification of investments in terms of geographic distribution and industry concentration. The table below analyses the effect of equity price risk on profit (as a result of change in the fair value of equity investments held as fair value through profit or loss) and on equity (as a result of change in the fair value of equity investments classified as FVOCI) at the year end due to an assumed 5% change in market indices, with all other variables held constant.

| <i>Market indices</i> | <i>% Change in<br/>equity price</i> | <i>2020</i>                              |  | <i>2019</i>                              |  |
|-----------------------|-------------------------------------|--|--|--|--|
|                       |                                     | <i>Effect on<br/>profit<br/>KD 000's</i> | <i>Effect on<br/>equity<br/>KD 000's</i> | <i>Effect on<br/>profit<br/>KD 000's</i> | <i>Effect on<br/>equity<br/>KD 000's</i> |
| Kuwait stock exchange | +5                                  | 70                                       | 15                                       | 128                                      | 10                                       |
| Qatar stock market    | +5                                  | 182                                      | -  | 172                                      | -  |
| UAE stock indices     | +5                                  | 159                                      | 3  | 230                                      | 1  |
| Saudi stock exchange  | +5                                  | 592                                      | -  | 600                                      | -  |

**30.4 OPERATIONAL RISK**

Operational risk is the risk of loss arising from inadequate or failed internal processes, human error, systems failure or from external events. The Group has a set of policies and procedures, which are approved by the Board of Directors and are applied to identify, assess and supervise operational risk in addition to other types of risks relating to the banking and financial activities of the Group. Operational risk is managed by the operational risk function, which ensures compliance with policies and procedures and monitors operational risk as part of overall global risk management.

The Operational Risk function of the Group is in line with the Central Bank of Kuwait instructions dated 14 November 1996, concerning the general guidelines for internal controls and the instructions dated 13 October 2003, regarding the sound practices for managing and supervising operational risks in banks.

# National Bank of Kuwait Group

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

31 December 2020

### 31 CAPITAL

A key objective of the Group is to maximise shareholders' value with optimal levels of risk, whilst maintaining a strong capital base to support the development of its business and comply with the externally-imposed capital requirements.

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

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

The Group's regulatory capital and capital adequacy ratios (Basel III) are shown below:

|   | <b>2020</b><br><i>KD 000's</i> | <b>2019</b><br><i>KD 000's</i> |
|---|--------------------------------|--------------------------------|
| Risk Weighted Assets                        | <b>21,052,128</b>              | 20,428,019                     |
| Capital required at 15%                     | <b>3,157,819</b>               | 3,064,203                      |
| Capital available                           |                                |                                |
| Common Equity Tier 1 capital                | <b>2,869,437</b>               | 2,754,674                      |
| Additional Tier 1 capital                   | <b>493,786</b>                 | 486,245                        |
| Tier 1 capital                              | <b>3,363,223</b>               | 3,240,919                      |
| Tier 2 capital                              | <b>517,546</b>                 | 386,983                        |
| Total capital                               | <b>3,880,769</b>               | 3,627,902                      |
| Common Equity Tier 1 capital adequacy ratio | <b>13.6%</b>                   | 13.5%                          |
| Tier 1 capital adequacy ratio               | <b>16.0%</b>                   | 15.9%                          |
| Total capital adequacy ratio                | <b>18.4%</b>                   | 17.8%                          |

The calculations include Boubyan Bank K.S.C.P., an Islamic Banking subsidiary. For purposes of determining risk-weighted assets and capital required, exposures and assets at Boubyan Bank K.S.C.P. are risk weighted, and capital charge calculated, in accordance with Central Bank of Kuwait regulations applicable to banks providing banking services compliant with Codes of Islamic Sharia'a. Those figures are then added to corresponding figures pertaining to all the rest of the Group, identical with the treatment in relevant reports submitted to the Central Bank of Kuwait.

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

|                 | <b>2020</b><br><i>KD 000's</i> | <b>2019</b><br><i>KD 000's</i> |
|-----------------|--------------------------------|--------------------------------|
| Tier 1 capital  | <b>3,363,223</b>               | 3,240,919                      |
| Total exposures | <b>32,504,240</b>              | 31,865,265                     |
| Leverage ratio  | <b>10.3%</b>                   | 10.2%                          |

### 32 FUNDS UNDER MANAGEMENT

The Group manages a number of funds, some of which are managed in association with other professional fund managers. The funds have no recourse to the general assets of the Group and the Group has no recourse to the assets of the funds. Accordingly, the assets of these funds are not included in the consolidated statement of financial position. As at 31 December 2020, funds under management were KD 4,745 million (2019: KD 4,469 million).

### 33 IMPACT OF COVID-19

The COVID-19 pandemic spread rapidly across global geographies causing massive disruption to business and economic activities and bringing unprecedented uncertainties to the global economic environment. Fiscal and monetary authorities worldwide launched extensive responses designed to mitigate the severe consequences of the pandemic.

#### Covid-19 support measures

In response to the crisis the Central Bank of Kuwait (CBK) implemented various measures targeted at reinforcing the banking sectors ability to play a vital role in the economy, including but not limited to the expansion of lending capacity, strengthening financing capabilities, providing direction in lending to productive economic sectors and in the provision of liquidity to impacted customers. Some of the important measures are given below:

- Decreased the Liquidity Coverage Ratio (LCR) from 100% to 80%
- Decreased the Net Stable Financing Ratio (NSFR) from 100% to 80%
- Decreased the regulatory Liquidity Ratio from 18% to 15%
- Increased the limit for maximum negative cumulative gap for liquidity
- Released Capital conservation buffer of 2.5% of risk-weighted assets in the form of CET1
- Decreased the risk weights for lending to SMEs from 75% to 25% to be applied in the calculation of risk-weighted assets
- Increased the limit for maximum permissible financing (Loans to Deposits Ratio) from 90% to 100% of deposits
- Increased loan-to-value limits for loans granted to individuals for the purpose of purchasing and/or developing properties
- Provision of loans by banks at concessional interest rates to SMEs and other companies impacted by the Covid-19 (Emergency Line of Credit programme)

Further, during the year, the Group received an aggregate amount of KD 11,788 thousand as Covid-19 support towards staff expenses from the Government in some of the jurisdictions where the Group operates. This is included in other operating income in the consolidated statement of income (refer to Note 8).

Kuwait banks announced postponement of payment of instalments of consumer and other instalment loans and credit card instalments for all customers for a period of six months effective from April 2020 with cancellation of interest and profits resulting from this deferral. This deferral scheme also applies to loans and financing facilities to SMEs. The instalment deferrals are considered as short-term liquidity support to address borrower's potential cash-flow issues. The customers have the option not to participate in this scheme. Additionally recoveries of instalments and interest on loans to corporate customers impacted by Covid-19 are postponed for a period of six months effective from March 2020. Similar measures were announced in many of the jurisdictions where the Group has operations.

#### Consumer and other instalment loans deferral

The Group implemented the consumer and other instalment loans deferral by postponing the instalments falling due within the six months period from 1 April 2020 to 30 September 2020 with a corresponding extension of the facility tenure. The instalment deferral resulted in a loss of KD 149,846 thousand to the Group arising from the modification of contractual cash-flows. The loss attributable to Bank's equity shareholders amounting to KD 130,499 thousand is charged to retained earnings and the remaining loss to the non-controlling interest, in accordance with the Group's accounting policy as stated in Note 2.

#### Expected Credit Loss (ECL) estimates

The Group considered the potential impact of the uncertainties caused by the Covid-19 pandemic together with the associated economic support and relief measures of governments and central banks in its estimation of ECL requirements for the year ended 31 December 2020.

**33 IMPACT OF COVID-19 (continued)**

**Expected Credit Loss (ECL) estimates (continued)**

*Significant increase in credit risk*

The Group considered the following aspects to assess if there was significant increase in credit risk or objective evidence of impairment in the light of Covid-19 situation.

- Temporary financial difficulties of the borrowers are distinguished from longer-term or permanent impact
- Borrowers operating in certain sectors or industries are likely to be more severely impacted
- Deferral of instalments or interest payments on loans or financing facilities will not automatically trigger significant increase in credit risk
- Retail loans to certain customer segment are more likely to have significant increase in credit risk arising from job losses and pay cuts
- Significant corporate exposures are individually assessed to identify significant increase in credit risk as and when reliable data is available

The above assessment has resulted in staging downgrade of certain exposures and corresponding increase in ECL.

*Macro-economic factors*

The Group considered the effects of volatility witnessed in the range of macroeconomic factors and in the scenarios used for determination of ECL. In particular, given the continuing uncertainties and impact stemming from Covid-19, and considering that the situation is fast-evolving, the Group revised certain assumptions reflected through constructing a plausible forward-looking view of the macroeconomic factors. The Group applies appropriate probability weightages on the 3 scenarios (Baseline, Benign, Severe) and, combined with the revised forecasts of macro-economic factors into all 3 scenarios are significantly conservative when compared to year ended 31 December 2019. The Group also applied management overlay in assessing the ECL for the retail segment given that employees of specific industries in the private sector are expected to be most impacted due to Covid-19. These adjustments and management overlays resulted in significant increase in the amount of ECL requirements for the year ended 31 December 2020.

Notwithstanding the above, ECL requirement for credit facilities estimated as at 31 December 2020 continues to be lower than the provisions required as per CBK instructions. In accordance with Group accounting policy, the higher amount, being the provision required as per CBK instructions, is therefore recognized as the provision requirement for credit losses on credit facilities.

**Other impacts**

The Group considered the potential impact of the current economic volatility on the reported amounts of the Group's financial and non-financial assets. The reported amounts best represent management's assessment based on observable information. Markets, however, remain volatile and asset carrying values remain sensitive to market fluctuations. The impact of the highly uncertain economic environment remains judgmental and the Group will accordingly continue to reassess its position and the related impact on a regular basis.