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NBK

NATIONAL BANK OF KUWAIT (INTERNATIONAL) PLC
DIRECTORS' REPORT AND FINANCIAL STATEMENTS 2016

2016

Directors

Chairman
Nasser Musaed Abdullah Al Sayer

Vice Chairman
Isam Jassim Al Sager

Directors
Ghassan Ahmed Saoud Al Khaled
Hamad Abdul Aziz Al Sagar
Shaikha Al Bahar
Georges Richani
Sir Michael Craig-Cooper CBE, TD, DL, FCIArb.
Sir David William Brewer KG CMG CVO
Hamish Cameron Galbraith Marr (appointed 1 October 2016)
Fawzi Dajani

Management

LONDON

Managing Director
Fawzi Dajani

Executive Managers
Paul Kennedy
Sami El Labban
Sally Norman
Nicholas Simmonds

PARIS

General Manager
Sabeur Sassi

Secretaries
Andrew Simon Richardson
Stephen George Byrne (appointed 15 April 2016)

Auditors
Ernst & Young LLP
25 Churchill Place
London E14 5EY

Registered Office
NBK House
13 George Street
London W1U 3QJ

Registered No.
02773743

Strategic Report

31 December 2016

The directors present their strategic report for the year ended 31 December 2016.

Principal activities

The Bank is an authorised bank carrying out international commercial banking, financial and related services from its London headquarters and branch located in Paris.

Key financial highlights

	2016 $000	2015 $000
Operating income	45,102	42,806
Profit before tax	20,286	19,274
Taxation	(3,902)	(3,884)
Profit after tax	16,384	15,390
Total Assets	2,315,302	2,315,313
Dividends – interim	-	1,500
Dividends – proposed	1,500	-
Shareholder's equity	296,805	282,236
Return on shareholder's equity	5.7%	5.6%

Operating income was up on last year by US$ 2.3 million (5.4%). Net interest income at US$ 34.4 million increased year on year by US$ 3.3 million (10.6%), net investment income increased by US$ 1.6 million mainly due to a gain on disposal of the Bank's shares in Visa Europe which was acquired by Visa Inc., partly offset by lower fee income in 2016.

The Bank's cost income ratio at 55.2% remained broadly at same level as 55.6% last year.

Overall the asset base of the Bank remained at the same levels of US$ 2.3 billion compared to last year. Loans to customers also remained at the same level of US$ 1.0 billion compared to last year. Customer deposits dropped by US$ 0.2 billion to US$ 1.1 billion compared to US$ 1.3 billion in last year. Total deposits remained at the same levels.

The Bank's funding and liquidity positions are satisfactory.

Overall shareholder returns are respectable with return on average equity at 5.7%. Average return on assets for the year was 0.7%. The Bank's total capital ratio remains satisfactory at over 21.5% (18.4% in 2015).

Principal risks and uncertainties

Details of the financial risk management objectives and policies of the Bank and exposure of the Bank to market risk, interest rate risk, foreign exchange risk, credit risk and liquidity risk is given in notes to the financial statements.

By order of the Board

A S Richardson
Secretary

21 April 2017

Directors' Report

31 December 2016

The directors have pleasure in submitting their twenty fourth annual report together with the audited financial statements for the year ended 31 December 2016.

Directors

The names of the present directors are listed on page two.

Significant changes during the year and subsequently are as follows:

- Hamish Cameron Galbraith Marr was appointed 1 October 2016.
- Lesley Jane Titcomb was appointed on 1 January 2017.
- Sir Michael Craig-Cooper CBE, TD, DL, FCIArb resigned as a director on 31 January 2017.

According to the register of directors' interests, no director holding office as at 31 December 2016 had any beneficial interest in the shares of the Bank during the year or at year end.

Results and dividends

The Bank has made a profit after tax US$ 16,384 thousand (2015 – profit of US$ 15,390 thousand). The directors proposed a final dividend for the year ending 31 December 2016, amounting to US$ 1,500 thousand, representing a dividend rate of 1%. This was approved by the Board of directors on 31 January 2017.

Future developments

The directors aim to maintain the management policies which have resulted in a successful performance to date. The Bank's presence in two major European financial centres provides strategically important locations both for the optimisation of client service and market participation. In addition, the Bank is well-placed to benefit from the growth in Middle Eastern economies, especially through trade finance business and the structuring and execution of transactions in conjunction with the wider NBK Group.

BREXIT has created uncertainties in the market and the Board of directors is studying the impact of this closely, in particular, the effects on the Paris Branch if passporting rights are lost.

With effect from 30 March 2017 the Bank has successfully launched a certificates of deposit programme with has been successfully received in the market. This programme is designed to further stabilise the Banks sources of funding and optimise cost of funding.

Going concern

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

Charitable donations

The Bank made charitable donations of US$ 1,850 (2015 – US$ 2,240) during the year.

Employees

It is the Bank's policy to attract, retain and develop the best qualified employees to enable it to achieve its overall business objectives. Accordingly, all vacant positions are filled with the best qualified people, preferably internally where that is possible, and before recruiting externally. Equal treatment is afforded to all applicants internally and externally with no discrimination on the grounds of race, colour, sex, nationality, marital status or disability, the criteria for selection being suitability and competence to do the job.

The Bank is committed to providing high quality training to its employees using formal courses in addition to on the job training. This is to ensure that employees have the required knowledge and skills to perform effectively in their present and future positions within the Bank.

Directors' Report

31 December 2016

Supplier's payment policy

It is the Bank's policy in every case to comply with the terms of payment expected by suppliers. In this respect, the Bank's creditor payment practice is to pay within the agreed period from the date of the invoice.

Disclosure of information to the auditors

So far as each person who was a director at the date of approving this report is aware, there is no relevant audit information, being information needed by the auditor in connection with preparing its report, of which the auditor is unaware. Having made enquiries of fellow directors, each director has taken all the steps that he/she is obliged to take as a director in order to make himself/herself aware of any relevant audit information and to establish that the auditor is aware of that information.

Auditors

At the Annual General Meeting on 21 April 2017, a resolution to reappoint Ernst & Young LLP was passed.

By order of the Board

A S Richardson
Secretary

21 April 2017

Statement of Directors' Responsibilities

The directors are responsible for preparing the Directors' report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with UK Financial Reporting Standard 101. Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Bank and of the profit or loss of the Bank for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and estimates that are reasonable and prudent;
- state whether applicable UK Financial Reporting Standards have been followed, subject to any material departures disclosed and explained in the financial statements;
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Bank will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Bank's transactions and disclose with reasonable accuracy at any time the financial position of the Bank and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Bank and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Independent Auditors' Report

To the members of National Bank of Kuwait (International) PLC

We have audited the financial statements of National Bank of Kuwait (International) PLC for the year ended 31 December 2016 which comprise the Statement of Income, the Statement of Comprehensive Income, the Statement of Financial Position, the Statement of Changes in Equity and the related notes 1 to 24. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice), including FRS 101 "Reduced Disclosure Framework".

This report is made solely to the Bank's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Bank's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Bank and the Bank's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditor

As explained more fully in the Directors' Responsibilities Statement set out on page 6, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Bank's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the Strategic report and Directors' Report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the Bank's affairs as at 31 December 2016 and of its profit for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice, including FRS 101 "Reduced Disclosure Framework"; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matter prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements;
- the Strategic Report and the Directors' Report have been prepared in accordance with applicable legal requirements.

Independent Auditors' Report

To the members of National Bank of Kuwait (International) PLC

Matters on which we are required to report by exception

In light of the knowledge and understanding of the Bank and its environment obtained in the course of the audit, we have identified no material misstatements in the Strategic Report or Directors' Report.

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

For and on behalf of Ernst & Young LLP
London

21 April 2017

Statement of Income

For the year ended 31 December 2016

	Notes	2016 $000	2015 $000
			(Restated)
Interest and similar income	3	43,845	39,592
Interest and similar expense	4	(9,444)	(8,492)
Net interest and similar income		34,401	31,100
Net fees and commissions income	5	7,393	10,519
Net gains from dealing in foreign currencies	6	1,482	1,182
Net investment income	14	1,597	-
Other operating income		229	5
Total operating income		45,102	42,806
Administrative expenses	7	(24,470)	(23,374)
Depreciation		(438)	(409)
Operating expenses		(24,908)	(23,783)
Operating profit before impairment provision		20,194	19,023
Net release of provision related to credit facilities	13	92	251
Profit for the year before taxation	8	20,286	19,274
Taxation	9	(3,902)	(3,884)
Profit for the year		16,384	15,390

Notes 1 to 24 are an integral part of the financial statement.

Statement of Comprehensive Income

For the year ended 31 December 2016

	2016 $000	2015 $000
		(Restated)
Profit for the Year	16,384	15,390
Other comprehensive income:		
Change in fair value of investments available-for-sale (net of tax)	(1,815)	254
Other comprehensive (loss)/income for the year reclassifiable to statement of income	(1,815)	254
Total comprehensive income for the year	14,569	15,644

Notes 1 to 24 are an integral part of the financial statement.

Statement of Financial Position

31 December 2016

	Notes	2016 $000	2015 $000
			(Restated)
Assets			
Cash and cash equivalents	11	118,825	4,953
Deposits with banks		803,221	795,923
Loans and advances to banks	12	20,000	84,652
Loans and advances to customers	13	953,390	1,007,099
Investment securities	14	383,596	398,706
Fixed assets		1,628	1,975
Other assets	15	34,642	22,005
Total assets		2,315,302	2,315,313
Liabilities			
Due to banks and other financial institutions		847,345	720,339
Customer deposits		1,134,454	1,271,477
Other liabilities	16	36,698	41,261
Total liabilities		2,018,497	2,033,077
Equity			
Share capital	17	150,083	150,083
Retained earnings		144,195	127,811
Cumulative changes in fair values		2,527	4,342
Total equity		296,805	282,236
Total equity and liabilities		2,315,302	2,315,313

The financial statements were approved by the board of directors and authorised for issue on 21 April 2017.

Nasser Al Sayer
Director
21 April 2017

Notes 1 to 24 are an integral part of the financial statement.

Statement of Changes in Equity

31 December 2016

	Share capital $000	Retained earnings $000	Cumulative changes in fair values $000	Total $000
Balances as at 31 December 2014	150,083	113,921	4,088	268,092
Profit for the year	-	15,390	-	15,390
Other comprehensive income for the year	-	-	254	254
Total comprehensive income for the year	-	15,390	254	15,644
Dividend paid	-	(1,500)	-	(1,500)
Balances as at 31 December 2015	150,083	127,811	4,342	282,236
Profit for the year	-	16,384	-	16,384
Other comprehensive loss for the year	-	-	(1,815)	(1,815)
Total comprehensive income (loss) for the year	-	16,384	(1,815)	14,569
Balances as at 31 December 2016	150,083	144,195	2,527	296,805

Notes 1 to 24 are an integral part of the financial statement.

Notes to the Financial Statements

31 December 2016

1. INCORPORATION AND REGISTRATION

The financial statements of National Bank of Kuwait (International) PLC (the "Bank") were approved by the Board of Directors on 21 April 2017. The Bank is incorporated in United Kingdom and is principally engaged in banking activities, primarily in United Kingdom and France. The address of registered office is NBK House, 13 George Street, London W1U 3QJ.

The Bank is a wholly-owned subsidiary of National Bank of Kuwait SAKP, Kuwait. Copies of the Group financial statements of National Bank of Kuwait SAKP may be obtained from: NBK House, 13 George Street, London, W1U 3QJ. National Bank of Kuwait SAKP is the ultimate parent company.

2. SIGNIFICANT ACCOUNTING POLICIES

2.1 Basis of preparation

The financial statements have been prepared in accordance with the provisions of the Companies Act 2006 relating to banking companies and UK Financial Reporting Standard 101 'Reduced Disclosure Framework' for qualifying entities applying EU-adopted IFRS. The Bank has taken advantage of the following exemptions under FRS 101:

a) IAS 1 Presentation of Financial Statements, paragraph 38, to present comparative information in respect of IAS 16 Property, Plant and Equipment, paragraph 73(e).

b) IAS 1, paragraphs 10(d), 10(f), 16, 38A, 38B, 38C, 38D and 111.

c) The requirements of IAS 7 Statement of Cash Flows.

d) IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors, paragraphs 30 and 31.

e) IAS 24 Related Party Disclosures, paragraph 17.

f) The requirements in IAS 24 Related Party Disclosures to disclose related party transactions entered into between two or more members of a group, provided that any subsidiary which is a party to the transaction is wholly owned by such a member.

The financial statements are prepared under the historical cost convention except for the measurement at fair value of derivatives and investments available-for-sale. 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.

The comparative financial statements for the year ended 31 December 2015 have been reclassified to conform to classification in the current year. This reclassification does not have any effect on the results of the Bank. Such reclassification has been made to the financial statements of the Bank to improve the quality of information presented. Interest and similar income and Interest and similar expense has been reclassified by US$ 7,379 thousand, previously interest income and interest expenses on derivatives was disclosed on a gross basis and now is shown net to improve presentation of interest yield and cost of funds. Deferred tax assets and deferred tax liabilities has been netted in other liabilities, previously this was presented on a gross basis. Investment securities and cumulative changes in fair values have been restated to reflect re-measurement of valuation of equity amounting to US$ 1,373 thousand as at 31 December 2015.

The Bank has one wholly-owned subsidiary: Fitzrovia Solutions Limited (formerly known "NBK (Loans) Limited"), registered in England. It has not traded during the year, has no assets and is not consolidated, on the grounds of materiality. The Company was dissolved on 17 January 2017.

The financial statements have been prepared on a going concern basis in accordance with UK Financial Reporting Standard 101.

Notes to the Financial Statements

31 December 2016

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

2.2 Change in accounting policies

The accounting policies applied are consistent with those used in the previous year. Amendments to IFRSs which are effective for annual accounting period starting from 1 January 2016 did not have any material impact on the accounting policies, financial position or performance of the Bank.

2.3 Foreign currencies

The Bank has a multi-currency share capital comprising two classes of ordinary shares: GB pounds sterling and US dollars. The functional and presentation currency of the Bank is US dollars and reserves are also held in US dollars. The exchange rate used to convert GB pounds sterling to US dollars is 1.23 per GB pounds sterling for the statement of financial position.

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 are translated into functional currency at rates of exchange prevailing at the reporting date. Any gains or losses are taken to the statement of income. Non-monetary items in foreign currencies that are measured in terms of historical cost are translated using the rate of exchange at the date of the transaction.

2.4 Interest income and expenses

Interest income and expense for all interest-bearing financial instruments are recognised within 'interest income' and 'interest expense' in the 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 an integral part of the effective yield of a financial asset are recognised using the effective interest 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.

The interest differential between the currencies involved in forward exchange contracts is included in the interest income and expenses.

2.5 Fees and commissions income

Fees that are an integral part of the effective interest rate of loans are treated as an adjustment to the effective interest rate of the loans. 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 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.

2.6 Dividend income

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

2.7 Impairment of financial assets

The Bank assesses at each reporting date whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if and only if there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred 'loss event') and that loss event has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Objective evidence includes observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of financial assets since their initial recognition although the decrease cannot be identified with the individual financial assets in the group.

Notes to the Financial Statements

31 December 2016

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

2.7 Impairment of financial assets (continued)

If such evidence exists, any impairment loss is recognised in the statement of income.

a. Assets carried at amortised cost

The amount of impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the statement of income. If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognised in the statement of income.

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

b. Assets classified as available-for-sale

The amount of impairment loss is measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in the statement of income. This amount is recognised in the statement of income. If, in a subsequent period, the amount of the impairment loss decreases for an equity instrument, the previously recognised losses are not reversed through the statement of income, instead, they are recorded as increases in the cumulative changes in fair value reserve. If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in statement of income, the impairment loss is reversed through the statement of income.

2.8 Impairment of non-financial assets

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 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 for non-financial assets.

2.9 Leases

Operating leases are leases that do not transfer substantially all the risks and rewards incidental to ownership to the lessee. The Bank has entered into operating leases where rentals payable are charged to the statement of income on a straight-line basis over the lease term.

2.10 Pensions

The Bank operates defined contribution pension schemes for employees in the UK and France. The costs of providing retirement benefits are charged to the statement of income in the period in which they are incurred.

2.11 Taxation

Current income tax assets and liabilities for the current year are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amounts are those that are enacted or substantively enacted, at the reporting date in the countries where the Bank operates and generates taxable income. 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.

Notes to the Financial Statements

31 December 2016

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

2.12 Recognition of financial assets and financial liabilities

Financial assets and financial liabilities are recognised when the Bank 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 the income statement.

2.13 Cash and cash equivalents

Cash and cash equivalents consist of cash in hand and current account balances with central banks.

2.14 Deposits with banks

Deposits with banks are stated at amortised cost using the effective interest method less any amounts written off and provision for impairment.

2.15 Loans and advances to Banks and Loans and advances to customers

Loans and advances are financial assets with fixed or determinable payments that are not quoted in an active market.

Carrying value

Loans and advances are stated at amortised cost using the effective interest method less any amounts written off and provision for impairment. 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 being hedged.

Renegotiated loans

In the event of a default, the Bank seeks to restructure loans rather than take possession of collateral. This may involve extending the payment arrangements and the agreement of new loan conditions. When the terms and conditions of these loans are renegotiated, the terms and conditions of the new contractual arrangement apply in determining whether these loans remain past due. Management continually reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur. The loan continues to be subject to an individual or collective impairment assessment.

2.16 Investments available-for-sale

Investments available-for-sale are those investments which are designated as available-for-sale or investments that do not qualify to be classified as fair value through the statement of income, held to maturity, or loans and advances. After initial recognition, investments which are classified as available-for-sale are normally remeasured at fair value, unless fair value cannot be reliably determined in which case they are measured at cost less impairment. 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 in equity until the investment is derecognised or the investment is determined to be impaired. On derecognition or impairment the cumulative gain or loss previously reported as "cumulative changes in fair values" within equity, is included in the statement of income for the period. In case of a reversal of previously recognised impairment losses for equity investments, such changes will not be recognised in the current statement of income but will be recorded as an increase in the reserve for cumulative changes in fair values. If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised, the impairment loss is reversed through the statement of income. The portion of any fair value changes relating to an effective hedging relationship is recognised directly in the statement of income. The interest income from debt securities classified as available-for-sale is recorded in interest income and the dividend income from equities are recorded in dividend income.

Notes to the Financial Statements

31 December 2016

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

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 Bank has access at that date.

When available, the Bank 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 Bank uses valuation techniques that maximize the use of relevant observable inputs and minimize 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.

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

The Bank 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.

2.18 Offsetting of financial assets and liabilities

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

2.19 Derecognition 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 Bank 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 Bank 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 Bank 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 Bank'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 Bank 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 derecognition of the original liability and the recognition of a new liability.

Notes to the Financial Statements

31 December 2016

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

2.20 Derivative financial instruments

The Bank deals in interest rate swaps to manage its interest rate risk on interest bearing assets and liabilities. Similarly the Bank deals in forward foreign exchange contracts for customers and to manage its foreign currency positions and cash flows. All derivative financial instruments of the Bank are recorded in the 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 statement of income. The hedged items are adjusted for fair value changes relating to the risk being hedged and the difference is recognised in the statement of income.

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 statement of income. The gains or losses on cash flow hedges recognised initially in equity are transferred to the statement of income in the period in which the hedged transaction impacts the 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 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 Bank. 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 statement of income.

2.21 Trade and settlement date accounting

All "regular way" purchases and sales of financial assets are recognised on the trade date, i.e. the date that the Bank 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 regulation or convention in the market place.

Notes to the Financial Statements

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2. SIGNIFICANT ACCOUNTING POLICIES (continued)

2.22 Fixed assets

Fixed assets are stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

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 Bank and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the statement of income during the period in which they are incurred.

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:

Leasehold improvements	: term of lease
Other tangible fixed assets	: 3-5 years

Residual values and useful lives of assets are reviewed, and adjusted if appropriate, at each reporting date. The carrying values of tangible fixed assets 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 statement of income.

2.23 Due to Banks and Financial Institutions and Customer deposits

Due to Banks and Financial Institutions and Customer Deposits are stated at amortised cost using the effective interest method.

2.24 Financial guarantees

In the ordinary course of business, the Bank gives financial guarantees, consisting of letters of credit, guarantees and acceptances. Financial guarantees are initially recognised in the financial statements at fair value, being the premium received, in other liabilities. The premium received is recognised in the 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 statement of income.

2.25 Significant accounting judgements and estimates

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

Accounting Judgements

Classification of investments

Financial assets within the scope of IAS 39 are classified as financial assets at fair value through profit or loss, loans and receivables, held to maturity investments, available-for-sale financial assets, or as derivatives designated as hedging instruments in an effective hedge, as appropriate. The Bank determines the classification of its financial assets at initial recognition.

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2. SIGNIFICANT ACCOUNTING POLICIES (continued)

2.25 Significant accounting judgements and estimates (continued)

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:

Provision for credit losses

The Bank reviews its loans, advances to banks and customers on a quarterly basis to assess whether a provision for credit losses should be recorded in the statement of income. In particular, considerable judgement 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.

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 judgement is required in establishing fair values. The judgements 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. INTEREST AND SIMILAR INCOME

	2016 $000	2015 $000
Deposits with banks	11,342	5,412
Loans and advances	30,512	31,948
Debt investment securities	1,944	2,155
Other	47	77
	43,845	39,592

4. INTEREST AND SIMILAR EXPENSES

	2016 $000	2015 $000
Due to banks and other financial institutions	6,667	4,707
Customer deposits	2,660	3,635
Other	117	150
	9,444	8,492

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5. NET FEES AND COMMISSIONS INCOME

	2016 $000	2015 $000
Fees and commission income:		
Lending related fees	1,216	4,369
Retail banking customer fees	1,853	1,546
Financial guarantee contract & letter of credit fees	3,885	4,043
Other	707	848
	7,661	10,806
Fees and commission related expenses	(268)	(287)
Net fees and commissions income	7,393	10,519

6. NET GAINS FROM DEALING IN FOREIGN CURRENCIES

Net gains from dealing in foreign currencies mainly consist of dealing profits generated from foreign currency related transactions.

7. ADMINISTRATIVE EXPENSES

	2016 $000	2015 $000
Staff costs:		
Wages and salaries	9,806	9,260
Social security costs	2,073	1,977
Pension costs	915	866
	12,794	12,103
Other administrative expenses	11,676	11,271
	24,470	23,374

The average number of employees, all engaged in banking activities during the year was 132 (2015 – 109).

The Bank operates two defined contribution pension schemes. The UK scheme assets are in the form of units in a life fund. Employees in France are members of a scheme operated on behalf of all French banks.

8. PROFIT FOR THE YEAR BEFORE TAX

		2016 $000	2015 $000
This is stated after charging:			
Auditors' remuneration	- audit service	381	385
	- non-audit service	60	201
Operating lease rentals	- land and buildings	1,804	1,877

Notes to the Financial Statements

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9. TAXATION

(a) Tax on profit on ordinary activities

The tax charge is made up as follows:

	2016 $000	2015 $000
Current tax:		
UK corporation tax on the profit for the year	3,986	2,886
UK double tax relief	(271)	(286)
Foreign tax	508	491
Amounts overprovided in previous years	(225)	(172)
Total current tax	3,998	2,919
Deferred tax (income)/charge (Note c)	(96)	965
Total taxation (Note b)	3,902	3,884

(b) Factors affecting tax charge for the year

	2016 $000	2015 $000
Profit on ordinary activities before tax	20,286	19,274
Profit taxed at UK corporation tax		
Average standard rate of 20% (2015 – 20.25%)	4,057	3,903
Effects of:		
Disallowed expenses	8	16
Foreign tax net of double tax relief	237	205
Depreciation net of capital allowances	(77)	28
UK corporation tax over provided	(225)	(172)
Others	(98)	(96)
Total tax charge	3,902	3,884

(c) Deferred tax

Disclosed in statement of financial position	2016 $000	2015 $000
Deferred tax liabilities		
Capital allowances and depreciation	111	203
Revaluation of available-for-sale securities net of FRS 101 transition adjustments	3,239	4,092
	3,350	4,295
Deferred tax assets		
Disallowed provisions	21	21
Revaluation of fair value hedges (interest rate swaps) net of FRS 101 transition adjustments	2,574	3,172
	2,595	3,193
Deferred tax liabilities – Net (Note 16)	755	1,102

Notes to the Financial Statements

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9. TAXATION (continued)

(c) Deferred tax (continued)

Reconciliation of deferred tax liabilities - Net

	2016 $000	2015 $000
As at 1 January	1,102	137
Charged to statement of income:		
Accelerated capital allowances and depreciation	(92)	122
Disallowed provision	-	44
FRS 101 transition adjustments	-	799
Revaluation of loan hedges taxed during the year	(4)	-
Charged to statement of comprehensive income		
Deferred tax movement arising from movement in net revaluation of available-for-sale securities and associated hedges	(251)	-
	755	1,102

Deferred tax is computed at the rate expected to apply when the underlying temporary differences eventually reverse. Based on the announced changes in the corporation tax rates coming into effect in future years, the corporation tax rate of 20% will reduce to 19% with effect from 1 April 2017 and 17% with effect from 1 April 2020.

Paris branch deferred tax assets totalling US$ 140 thousand (2015: US$ 132 thousand) in respect of UK taxation timing differences have not been recognised or UK capital allowances claimed on the basis that it is unlikely there will be any UK tax payable on the branch profits in the foreseeable future.

10. EMOLUMENTS OF DIRECTORS

	2016 $000	2015 $000
Fees and other emoluments	429	467
Pension contributions in respect of defined contribution schemes	37	33
Highest paid director	368	394

11. CASH AND CASH EQUIVALENTS

	2016 $000	2015 $000
Cash on hand	2,306	3,567
Balances with central banks	116,519	1,386
	118,825	4,953

Notes to the Financial Statements

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12. LOANS AND ADVANCES TO BANKS

	2016 $000	2015 $000
Loans and advances to banks	20,000	84,652
Less: provision for credit losses	-	-
	20,000	84,652

13. LOANS AND ADVANCES TO CUSTOMERS

	2016 $000	2015 $000
Loans and advances to customers	953,776	1,007,576
Less: provision for credit losses	(386)	(477)
	953,390	1,007,099
These amounts include:		
Due from group undertakings	9,854	11,854

	Specific provision		Collective provision		Total	
	2016 $000	2015 $000	2016 $000	2015 $000	2016 $000	2015 $000
Balance at beginning of the year	63	106	414	622	477	728
Amounts written off net of exchange movement	1	-	-	-	1	-
Release during the year	(48)	(43)	(44)	(208)	(92)	(251)
Balance at end of the year	16	63	370	414	386	477

Non-performing loans and advances to customers and the related specific provisions are as follows:

	2016 $000	2015 $000
Loans and advances to customers	17	63
Specific provisions	17	63

14. INVESTMENT SECURITIES

	2016 $000	2015 $000
Investments available-for-sale	397	1,375
Equities	383,199	397,331
Debt securities	383,596	398,706

Debt securities are held on a yield-to-maturity basis, for portfolio management purposes. See Note 22 for details on valuation of investment securities.

Debt securities with a book value of US$ 368 thousand (2015 – US$ 716 thousand) are pledged as security for outstanding cross-currency interest rate swaps.

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14. INVESTMENT SECURITIES (continued)

The Bank held Visa Europe shares as at 31 December 2015. During the year, Visa Europe was acquired by Visa Inc. The acquisition process was initiated by the end of 2015 and was completed in June 2016. The Bank received cash consideration amounting to US$1,114 thousand, deferred cash payment amounting to US$ 118 thousand (which will be paid on completion of third anniversary) and also 725 Series B Visa Inc. preferred stock. During the year, the Bank has accounted for the gain on disposal of Visa Europe shares amounting to US$ 1,597 thousand which comprised of cash consideration and a day one fair value gain on the preferred stock.

15. OTHER ASSETS

	2016 $000	2015 $000
Accrued interest receivable	6,164	7,427
Sundry debtors and prepayments	2,404	1,392
Derivative assets (Note 20)	25,315	10,858
Others	759	2,328
	34,642	22,005

16. OTHER LIABILITIES

	2016 $000	2015 $000
Interest payable	4,931	4,619
Deferred income	4,617	4,798
Derivative liabilities (Note 20)	17,627	25,101
Tax payable	3,023	1,906
Deferred tax liabilities (Note 9)	755	1,102
Others	5,745	3,735
	36,698	41,261

17. SHARE CAPITAL

There are two classes of ordinary share capital issued, being in pounds sterling and US dollars:

Authorised at 31 December 2015 and 2016	Ordinary share capital	
Nominal value	£1 each	$1 each
Number of shares	50,000	182,910,000

Allotted, called up and fully paid at 31 December 2015 and 2016:

	£000	$000	Total $000
Currency amounts at 31 December 2015 and 2016	50	150,000	
US dollar equivalent at 31 December 2015 and 2016	83	150,000	150,083

18. ORDINARY DIVIDENDS

For the year ended 31 December 2016, the Board of Directors proposed a cash dividend on US Dollar denominated shares only at the rate of US$ .01 per share amounting to US$ 1,500 thousand, which was paid in March 2017. During the year 2015, the Board of Directors has paid interim dividend on US dollar denominated shares only at the rate of US$ .01 per share amounting to US$ 1,500 thousand.

Notes to the Financial Statements

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19. RELATED PARTY TRANSACTIONS

Related parties comprise board members and senior officers of the Bank, their close family members and companies controlled by them or close family members. Certain related parties were customers of the Bank 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. There are no provisions for credit losses against loans and advances to related parties as at 31 December 2016 and 31 December 2015.

	2016 $000	2015 $000
Board members & senior officers of the Banks		
Customer deposits	7,692	9,015
Interest expense	15	14
Parent Company		
Deposits with banks	6,012	4,529
Other assets	540	181
Due to banks and other financial institutions	83,771	44,713
Other liabilities	13,932	15,888
Contingent liabilities	43,140	41,853
Fully owned subsidiaries of the Parent Company		
Loans and advances to customers	9,854	11,854
Other assets	1	1
Due to banks and other financial institutions	477	267
Customer deposits	13,770	15,599
Contingent liabilities	158	162
Partly owned subsidiaries of the Parent Company		
Due to banks and other financial institutions	3,152	35,582
Other liabilities	-	1
Contingent liabilities	27,752	38,272
Interest income	-	49
Interest expenses	28	25
Fee income	336	524

20. DERIVATIVES FINANCIAL INSTRUMENTS

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.

Notes to the Financial Statements

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20. DERIVATIVES FINANCIAL INSTRUMENTS (continued)

Derivative financial instruments are carried at fair value in the statement of financial position. Positive fair value represents the cost of replacing all transactions with a fair value in the Bank'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 Bank's counterparties of replacing all their transactions with the Bank.

The Bank deals in interest rate swaps to manage its interest rate risk on interest bearing assets and liabilities. Similarly the Bank 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 Bank's financial assets and liabilities and which qualifies as effective hedging instruments are disclosed as 'held as fair value hedges'. 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 foreign currency risk exposures on account of derivative financial instruments for customers are covered by entering into opposite transactions (back to back) with counterparties or by other risk mitigating transactions.

Interest rate swaps

Interest rate swaps are contractual agreements between two counterparties to exchange interest payments on a defined principal amount for a fixed period of time. In cross currency interest rate swaps, the Bank 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.

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 statements, together with their notional amounts is summarised as follows:

	2016			2015		
	Positive fair value $000	Negative fair value $000	Notional $000	Positive fair value $000	Negative fair value $000	Notional $000
Interest rate swaps (held as fair value hedges)	333	14,660	165,640	57	17,809	157,836
Forward foreign exchange contracts	24,982	2,967	1,288,003	10,801	7,292	1,021,050
	25,315	17,627	1,453,643	10,858	25,101	1,178,886

Gain on hedged fixed income financial assets amounted to US$ 17,244 thousand (2015: US$ 19,515 thousand).

Notes to the Financial Statements

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21. COMMITMENTS AND CONTINGENT LIABILITIES

Set out below are the notional principal amounts of off-balance sheet transactions. The notional principal amounts indicate the volume of business outstanding at the balance sheet date and do not represent amounts at risk. These credit commitments do not necessarily represent future cash requirements, since many of these commitments will expire or terminate without being funded.

	2016 $000	2015 $000
Contingent liabilities:		
Acceptances and endorsements	-	10,000
Guarantees	380,314	470,965
Irrevocable letters of credit	40,987	48,753
At 31 December	421,301	529,718
Commitments:		
Undrawn, formal standby facilities, credit lines and other commitments to lend	76,119	111,723

Operating lease commitments – Bank as a lessee

The Bank has entered into commercial leases on land and building and computer and other equipment. The leases include a renewal option at the end of their term. There is no restriction placed upon the lessee by entering into the lease.

	2016 $000	2015 $000
At the year-end, annual commitments under non-cancellable operating leases were:		
Expiring:		
Within one year	1,707	1,955
In one to five years	6,336	7,670
More than 5 years	6,506	9,180
	14,549	18,805

22. 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 Bank determines fair values using valuation techniques.

The Bank 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.

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.

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22. FAIR VALUE OF FINANCIAL INSTRUMENTS

Valuation techniques include discounted cash flow models, comparison with similar instruments for which market observable prices exist and recent transaction information. 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 following table provides the fair value measurement hierarchy of the Bank's financial instruments recorded at fair value:

2016	Level 1 $000	Level 2 $000	Level 3 $000	Total $000
Equities	1	-	396	397
Debt securities	372,931	10,267	1	383,199
	372,932	10,267	397	383,596
Derivative financial instruments (Note 20)	-	7,688	-	7,688

2015	Level 1 $000	Level 2 $000	Level 3 $000	Total $000
Equities	2	-	1,373	1,375
Debt securities	380,723	10,014	6,594	397,331
	380,725	10,014	7,967	398,706
Derivative financial instruments (Note 20)	-	(14,243)	-	(14,243)

Debt securities included in level 2 consists of unquoted corporate bonds issued by banks. The fair values of these securities are estimated using valuation techniques with observable inputs. Derivatives are valued using valuation techniques which include forward pricing and swap models using present value calculations. The models incorporate various inputs such as foreign exchange spot and forward rates and interest yield curves. The impact of non-performance risk is not considered in the valuation as it is not significant.

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

	At 1 January 2016 $000	Additions $000	Change in fair value $000	Sale $000	Exchange rate movements $000	At 31 December 2016 $000	Net gains in the statement of income $000
Equity	1,373	363	33	(1,373)	-	396	1,597
Debt securities	6,594	-	-	(6,593)	-	1	13
	7,967	363	33	(7,966)	-	397	1,610

Notes to the Financial Statements

31 December 2016

22. FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

	At 1 January 2015 $000	Additions $000	Change in fair value $000	Sale $000	Exchange rate movements $000	At 31 December 2015 $000	Net gains in the statement of income $000
Equity	-	-	1,373	-	-	1,373	-
Debt securities	22,943	-	-	(15,740)	(609)	6,594	335
	22,943	-	1,373	(15,740)	(609)	7,967	335

Equity included in this category is a strategic equity investment which is not traded in an active market. The fair value of this equity investment is estimated using an internal valuation technique, which includes taking observable market information and applying an appropriate discount rate. Sensitivity analysis for fair value estimations on equity investments, by varying input assumptions in the range from 5% to 10% (2015: range from 5% to 10%), did not indicate any material impacts. The impacts on statement of financial position or statement of income, ranged from US$ 18 thousand to US$ 36 thousand (2015: US$ 16 thousand to US$ 32 thousand). Debt securities included in this category for year ended 31 December 2015 consists of unquoted corporate bonds issued by banks and financial institutions. The fair values of these bonds were estimated using a discounted cash flow method with a credit spread of 2%.

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 (Level 3) 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 statement of financial position or statement of income.

23. RISK MANAGEMENT

Risk is inherent in the Bank's activities but is managed in a structured, systematic manner through risk management policies which embed 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 Audit and Risk Committee. The Bank's Risk Management and Internal Audit functions assist Executive Management in controlling and actively managing the Bank's overall risk profile.

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

In accordance with regulatory requirements, the Bank has implemented a comprehensive system for the measurement and management of risk commensurate with the Bank's size and business model.

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

The Bank uses interest rate swaps, forward foreign exchange contracts and other instruments to manage the financial risks resulting from changes in interest rates, foreign exchange, equity valuation and credit exposures where possible collateral is used to reduce the Bank's exposure to credit risk.

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

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31 December 2016

23. RISK MANAGEMENT (continued)

23.1 CREDIT RISK

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

All policies relating to credit risk are reviewed and approved by the Board of Directors. The Board Audit and Risk Committee and the Board oversee credit risk on a quarterly basis.

Credit limits are established for all customers after a careful assessment of their creditworthiness. Procedures outlined in the Bank's Credit Policies require that all credit proposals be subjected to detailed screening by the Credit Risk Department before submission to the Credit Approval Committee. Whenever necessary, all loans are secured by acceptable forms of collateral to mitigate the related credit risks.

The Bank has an internal Credit Risk Committee ("CRC") that monitors both individual facilities and stresses emerging at a portfolio level, where for the latter CRC may take early preventative actions including making adjustments to credit policy. It is planned that CRC's governance responsibilities will be expanded to include the approval of provisions, both collective and on individual impaired facilities, in line with changes to accounting treatments. CRC meets regularly throughout the year.

The Bank further limits credit 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.

23.1. 1 MAXIMUM EXPOSURE TO CREDIT RISK

The following disclosures highlight the diversity of exposures.

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

	2016		2015	
	Gross Exposure $000	Net Exposure $000	Gross Exposure $000	Net Exposure $000
Loans and advances to banks	20,000	20,000	84,652	84,652
Loans and advances to customers	953,390	112,600	1,007,099	70,235
Contingent liabilities	421,301	419,868	529,718	528,223

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 collateral are performed independent of the business units.

23.1. 2 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.

Notes to the Financial Statements

31 December 2016

23. RISK MANAGEMENT (continued)

23.1 CREDIT RISK (continued)

23.1. 2 RISK CONCENTRATION OF THE MAXIMUM EXPOSURE TO CREDIT RISK (continued)

Credit risk can also arise due to a significant concentration of Bank's assets to any single counterparty. This risk is managed by diversification of the portfolio. The Bank's maximum limit is 25% of capital to any single obligor group. The ten largest loans and advances to customers outstanding as a percentage of gross loans and advances to customers as at 31 December 2016 is 37% (2015: 34%).

The Bank'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:

2016 Geograpic Region	Middle East and North Africa $000	North America $000	Europe $000	Asia $000	Others $000	Total $000
Balances with central banks	-	-	116,519	-	-	116,519
Deposits with banks	369,165	5,639	415,602	12,815	-	803,221
Loans and advances to banks	-	-	-	-	20,000	20,000
Loans and advances to customers	205,731	-	443,531	-	304,128	953,390
Investments available-for-sale	50,828	68,770	263,601	-	-	383,199
Other assets	406	1,602	27,806	2,424	-	32,238
	626,130	76,011	1,267,059	15,239	324,128	2,308,567
Commitments and contingent liabilities (Note 21)	75,204	-	410,898	-	11,318	497,420
	701,334	76,011	1,677,957	15,239	335,446	2,805,987

2015 Geograpic Region	Middle East and North Africa $000	North America $000	Europe $000	Asia $000	Others $000	Total $000
Balances with central banks	-	-	1,386	-	-	1,386
Deposits with banks	455,917	58,986	280,832	96	92	795,923
Loans and advances to banks	10,887	-	16,265	-	57,500	84,652
Loans and advances to customers	217,750	-	446,967	-	342,382	1,007,099
Investments available-for-sale	16,607	71,400	309,324	-	-	397,331
Other assets	360	-	18,750	1,503	-	20,613
	701,521	130,386	1,073,524	1,599	399,974	2,307,004
Commitments and contingent liabilities (Note 21)	155,412	-	481,381	-	4,648	641,441
	856,933	130,386	1,554,905	1,599	404,622	2,948,445

Notes to the Financial Statements

31 December 2016

23. RISK MANAGEMENT (continued)

23.1 CREDIT RISK (continued)

23.1. 2 RISK CONCENTRATION OF THE MAXIMUM EXPOSURE TO CREDIT RISK (continued)

The Bank'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:

Industry sector	2016 $000	2015 $000
Trading	-	117
Manufacturing	250,453	311,805
Banks and other financial institutions	1,109,826	1,086,006
Construction	55,368	79,787
Real Estate	854,108	996,820
Retail	21,739	15,171
Government	396,608	362,079
Others	117,885	96,660
	2,805,987	2,948,445

23.1. 3 CREDIT QUALITY PER CLASS OF FINANCIAL ASSETS

In managing its portfolio, the Bank 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 customers and banks 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 Bank's credit rating system.

	Neither past due nor impaired		Past due and	Past due and	
	High	Standard	not impaired	impaired	Total
2016	$000	$000	$000	$000	$000
Balances with central banks	116,519	-	-	-	116,519
Deposits with banks	637,750	165,471	-	-	803,221
Loans and advances to banks	-	20,000	-	-	20,000
Loans and advances to customers	729,743	218,852	5,164	17	953,776
Debt securities	372,931	10,268	-	-	383,199
Derivative assets	24,450	865	-	-	25,315
	1,881,393	415,456	5,164	17	2,302,030
2015					
Balances with central banks	1,386	-	-	-	1,386
Deposits with banks	771,638	24,285	-	-	795,923
Loans and advances to banks	64,652	20,000	-	-	84,652
Loans and advances to customers	870,515	136,998	-	63	1,007,576
Debt securities	387,317	10,014	-	-	397,331
Derivative assets	24,450	865	-	-	25,315
	2,119,958	192,162	-	63	2,312,183

Notes to the Financial Statements

31 December 2016

23. RISK MANAGEMENT (continued)

23.2 LIQUIDITY RISK

Liquidity risk is the risk that the Bank will be unable to meet its financial liabilities when they fall due. To limit this risk, management has arranged diversified funding sources and manages its assets with liquidity in mind. The Bank ensures that it has sufficient liquidity even in stress scenarios, and liquidity adequacy is monitored daily

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

2016 Assets	Up to 3 Months $000	3 to 12 Months $000	Over 1 Year $000	Total $000
Cash and cash equivalents	118,825	-	-	118,825
Deposits with banks	746,635	56,586	-	803,221
Loans and advances to banks	-	20,000	-	20,000
Loans and advances to customers	49,969	134,017	769,404	953,390
Investment securities	136,519	137,348	109,729	383,596
Fixed assets	-	-	1,628	1,628
Other assets	30,748	3,561	333	34,642
	1,082,696	351,512	881,094	2,315,302
Liabilities and equity				
Due to banks and other financial institutions	302,449	544,896	-	847,345
Customer deposits	985,307	149,147	-	1,134,454
Other liabilities	7,427	10,846	18,425	36,698
Share capital and reserves	1,500	-	295,305	296,805
	1,296,683	704,889	313,730	2,315,302

2015 Assets	Up to 3 Months $000	3 to 12 Months $000	Over 1 Year $000	Total $000
Cash and cash equivalents	4,953	-	-	4,953
Deposits with banks	718,668	77,255	-	795,923
Loans and advances to banks	37,500	27,152	20,000	84,652
Loans and advances to customers	59,541	126,934	820,624	1,007,099
Investment securities	157,167	142,731	98,808	398,706
Fixed assets	-	-	1,975	1,975
Other assets	14,459	3,639	3,907	22,005
	992,288	377,711	945,314	2,315,313
Liabilities and equity				
Due to banks and other financial institutions	238,134	482,205	-	720,339
Customer deposits	1,192,353	79,116	8	1,271,477
Other liabilities	11,707	2,179	27,375	41,261
Share capital and reserves	-	-	282,236	282,236
	1,442,194	563,500	309,619	2,315,313

Notes to the Financial Statements

31 December 2016

23. RISK MANAGEMENT (continued)

23.2 LIQUIDITY RISK (continued)

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

2016	Up to 3 Months $000	3 to 12 Months $000	Over 1 Year $000	Total $000
Financial Liabilities				
Due to banks and other financial institutions	302,594	550,335	-	852,929
Customer deposits	985,440	149,896	-	1,135,336
	1,288,034	700,231	-	1,988,265
Contingent liabilities and commitments				
Contingent liabilities	99,556	162,756	158,989	421,301
Irrevocable commitments	1,216	6,621	68,282	76,119
	100,772	169,377	227,271	497,420
Derivatives				
Interest rate swaps (net interest)	399	3,319	20,160	23,878
	399	3,319	20,160	23,878

2015	Up to 3 Months $000	3 to 12 Months $000	Over 1 Year $000	Total $000
Financial Liabilities				
Due to banks and other financial institutions	238,154	485,440	-	723,594
Customer deposits	1,192,586	79,481	8	1,272,075
	1,430,740	564,921	8	1,995,669
Contingent liabilities and commitments				
Contingent liabilities	79,902	232,273	217,543	529,718
Irrevocable commitments	5,778	600	105,345	111,723
	85,680	232,873	322,888	641,441
Derivatives				
Interest rate swaps (net interest)	383	3,296	25,066	28,745
	383	3,296	25,066	28,745

Notes to the Financial Statements

31 December 2016

23. RISK MANAGEMENT (continued)

23.3 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.

23.3.1 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 Bank is not excessively exposed to interest rate risk. 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 undrawn loan commitments. The sensitivity on equity is the impact arising from changes in interest rate on fair value of available-for-sale investments. 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 Bank'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 Bank's profit and equity as follows:

		2016		2015	
Currency	Movement in basis points	Effect on Profit $000	Effect on Equity $000	Effect on Profit $000	Effect on Equity $000
GBP	+25	1,102	-	1,076	-
USD	+25	(656)	-	87	-
EUR	+25	1,289	-	860	-

23.3.2 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 monitoring against 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 or are covered by forward foreign exchange contracts. 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.

The Bank does not have significant net open positions in any foreign currencies and accordingly there is no significant impact on the income statement or equity as a result of foreign exchange rate fluctuations.

Notes to the Financial Statements

31 December 2016

23. RISK MANAGEMENT (continued)

23.4 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 Bank 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 Bank. Operational risk management is overseen by the Risk Management Department, which ensures compliance with policies and procedures and monitors operational risk as part of overall Bank risk management.

24. CAPITAL MANAGEMENT

A key objective of the Bank 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.

Capital adequacy is monitored on a regular basis against both regulatory and internal capital requirements. The Bank ensures that it has adequate capital even in stress scenarios through the Individual Capital Adequacy Assessment Process.

The Bank's regulatory capital and capital adequacy ratios as reported to the Prudential Regulatory Authority are shown below:

	2016 $000	2015 $000
Risk Weighted Assets	1,303,500	1,514,057
Capital available		
Common Equity Tier 1 capital	279,845	277,894
Tier 1 capital	279,845	277,894
Tier 2 capital	-	-
Total capital	279,845	277,894
Common Equity Tier 1 capital adequacy ratio	21.5%	18.4%
Tier 1 capital adequacy ratio	21.5%	18.4%
Total capital adequacy ratio	21.5%	18.4%

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