Risk Management Disclosures 31/12/2014

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Risk Management--IBK

Risk Management Disclosures per Basel III Pillar III-31.12.2014

Risk Management Objectives:

The Industrial Bank of Kuwait has clear risk management objectives and a well-established strategy to deliver them, through core risk management processes.

At a strategic level, the Bank's risk management objectives are:

– To identify the Bank's material risks.
– To formulate the Bank's risk appetite and ensure that business profile and plans are consistent with it.
– To optimize risk/return decisions by dialogue with business, while establishing a strong and independent review process and structure.
– To ensure that business growth and strategic plans are properly supported by effective risk assessment.
– To monitor risk profile to ensure that specific financial deliverables remain possible under a range of adverse business conditions.
– To help business and support functions improve the control and co-ordination of risk taking across the Bank.
– To promote risk culture through all areas of the Bank.

Risk Management Structure:

Responsibility for risk management resides at all levels within the Bank, from the Board and the executive level down through the organization to each business manager and risk specialist documented in detail through policies and procedures and available to all staff through an online shared system. In a 3 – Eye approach, the responsibilities for effective review and challenge reside with managers, an independent risk management function and, internal audit. For effective corporate governance, the Chief Risk Officer assists the Board Risk Committee to guide and oversee effective risk management across the Bank. Risk Management also assists the Board of Directors in tasks required by the Board Committees. The Board is responsible for approving risk appetite, which is the level of risk the Bank chooses to take in pursuit of its business objectives. The risk appetite is reviewed annually by the Board Risk Committee so that it is in synchrony with the economic environment.

The Board is also responsible for the internal control and assurance framework. To enhance corporate governance and the management of risk, the following committees have been set up to perform specific roles - the Board Audit Committee, the Board Risk Committee, the Board Nomination and Remuneration Committee and the Board Governance Committee.

Internal Audit is responsible for the independent review of the effectiveness of risk management and the control environment. Its objective is to provide reliable, valued and timely assurance to the Board and Executive Management over the effectiveness of controls, mitigating current and evolving high risks and in so doing enhancing the controls culture within the Bank.

The Board Risk Committee monitors through the risk management function, the Bank's risk profile against the risk appetite documented quantitatively and qualitatively in the risk appetite policy, providing benchmarks for high level oversight and supervision of the management of risks. Where actual performance differs from expectations, the actions being taken by management are reviewed to ensure that the Committee is comfortable with them. The Committee receives regular and comprehensive reports on the Bank's risk profile, an assessment on all risk factors, key issues affecting each business portfolio, risk measurement methodologies and future risk trends. The Board Risk Committee ensures that appropriate policies and procedures exist to manage risks in a professional and pro-active manner, reviewing the independence and integrity of the Bank's risk management function and critically assessing business and strategic risks within established risk management policies and procedures.

The Chief Risk Officer reports directly to the Chairman of the Board. The risk management function is responsible for independently assessing and managing credit, market, liquidity and all types of operational risks. Additionally, the IT security and the IT Risk assessment function (operating independently from the IT department), reports to the CRO. While primary risks are managed by line managers, the risk management function provides a structured and independent assessment of credit, liquidity, market and all types of operational risks by proactively working with line management in identifying, documenting, quantifying, tracking and monitoring Key Risk Indicators and providing solutions whenever KRI's tend to go beyond acceptable levels. It facilitates implementation of risk initiatives and continuously tracks portfolio risks as well as individual credit, investment, new projects and product proposals. It ensures that risks are categorized into groups of low, medium and high risks and that significant risk that are outliers in the boundary provided by the risk appetite policy and those that have potential operational loss impacts, are highlighted, reported and mitigated.

In the collaborative spirit of risk accountability, there are specific committees set up to monitor specific areas of risk. There is an Assets and Liabilities Committee (ALCO) that monitors liquidity risks, investment risks and asset projections, and where the CRO participates as an active member. The Credit Committee and Provisions Committees deal with corporate credit and project finance proposals and impairment and provisions issues. There is a Policies and Procedures Group that reviews and oversees the creation and updating of the Bank's policies and procedures with participation from the business departments. The risk management department has responsibility and voice through membership in the group for policies and procedures. Risk management has implemented an online system for display and control of policies and procedures that is transparent and available to all staff. Risk management is involved in the IT committees including new IT projects as an invitee together with Internal Audit and coordinates the Bank's business continuity plans and off-site disaster recovery activities.

Stress Testing:

A fundamental duty of risk management is to ensure that the Bank does not neglect to prepare for the worst event as they plan for growth. Stress testing helps the Bank understand how its portfolios would react if business conditions became significantly more challenging. Risk Management generates specific forward-looking scenarios and analyses how well liquidity and profitability would hold up, whether the levels of capital would be adequate to meet significant shocks and what managers could do ahead of time to mitigate risk. Stress tests capture a wide range of variables that are relevant to the current environment. The Risk Management function co-ordinates the process of stress testing, using bottom-up analysis on expected and unexpected loss. Projections on credit provisions and investment impairments provided by the Business is taken as expected loss over which risk management assesses through internal modeling, projections of unexpected loss and the capital cover required to tide over periods of stress. The results of the stress tests are presented to the Executive committee, the Board Risk Committee, The Board of Directors and the regulatory authority – The Central Bank of Kuwait for its assessment of the Bank's resilience to stressed credit risk, market risk and economic conditions. The stress scenarios take into account a wide range of factors, including: the

Bank's revenue generation potential, loan loss provisions and the probability of default and possible losses given default within its loan book; and possible declines in the market value of investment assets and effects on capital adequacy.

2014 continued the slow reversal after the great worldwide recession that had started in 2008, though manufacturing business volumes and margins remained flat to declining and the pressures in the system and the Bank's customers continued, though at lower levels that in the previous years since the downturn and larger discretionary provisions were taken. The Bank continued to fine tune the Basel III Pillar II guidelines as adopted by the Central Bank of Kuwait and the Quantitative Impact Analysis for Basel III was completed and submitted to the Central Bank including new guidelines of liquidity under Basel III. A new phase was entered into with active involvement and encouragement of the regulators and continuous interaction with the risk management group. The policies and procedures for the Internal Capital Adequacy Assessment Process (ICAAP) and risk appetite as approved by the Board of Directors was implemented and fine-tuned. Stress tests were periodically conducted internally during the course of the year. External experts assessed the Bank and its mandate, the risk management function of the bank and the Bank's systems, management, plans and strategies and independently conducted stress tests. The Bank did not fail these independent tests in any of the categories and criteria assessed. Following this work and discussion with the expert group, the Bank was able to confirm that its capital position and resources, after exposure to the stress, were expected to continue to meet the CBK's capital requirements.

Risk Management replicates the CAMEL BCOM methodology that is used by the CBK and provided its risk feedback through the ALCO, The Board Risk Committee and the Board and its results are used by the Board committees including the Nomination and Remunerations Committee.

The Bank participated in the proposed formulation of Basel III guidelines and the new Corporate Governance proposals through the industry association of CROs of all Kuwaiti banks and financial institutions.

Risk Rating by External Rating Agencies:

On December 2014, the international rating agency Fitch reaffirmed the rating of the Industrial Bank of Kuwait as shown below:

Fitch Ratings:

Foreign Currency	
Long Term IDR	A+
Short Term IDR	F1
Viability Rating	bb+ (Upgraded from bb)
Individual Rating	C/D
Support Rating	1
Support Rating Floor	A+
Sovereign Risk	
Foreign Currency Long Term IDR	AA
Local Currency Long Term IDR	AA
Outlooks	
Foreign Currency Long Term IDR	Stable
Sovereign Foreign Currency Long Term IDR	Stable
Sovereign Local Currency Long Term IDR	Stable

Fitch comments that IBK's IDRs and Support rating reflect the extremely high probability of support from the government of Kuwait, in case of need. This is based on the government of Kuwait's 49% direct ownership and 12% indirect ownership of IBK, as well as the long-term government funding provided for the bank's development activities. The ratings also take into account the Kuwaiti authorities' long history of strong support for Kuwaiti banks.

The rating agency ‘Capital Intelligence’ reaffirmed their existing rating of IBK at A for 2014 with a ‘Stable’ outlook. Their summary rating is as follows:

Foreign Currency Long-term	A+
Financial Strength	A
Support	2
Outlook – Foreign Currency	Stable
Outlook – Financial Strength	Stable

Basel III Pillar 3 Consolidated Disclosures:

Overview of Basel III and Pillar 3:

Since December 2005, The Industrial Bank of Kuwait has applied the Basel framework as part of its risk and capital management strategy. The accord is made up of three pillars:

• Pillar 1 covers the calculation of risk-weighted assets for credit risk, market risk and operational risk.

• Pillar 2 allows firms and supervisors to take a view on whether the firm should hold additional capital to cover the three Pillar 1 risk types, or to cover other risks. A firm’s own internal models and assessments support this process which is interactive between the Bank and its regulator, the Central Bank of Kuwait.

Pillar 3 covers external communication of risk and capital information by banks.

The Basel guidelines provide~~s~~ for different approaches to calculating capital requirements.

• The first is the Standardized approach, where risk weights used to assess requirements against credit exposures are consistent across the industry.

• The second approach is the Internal Ratings Based approach (IRB) which relies on the bank’s internal models to derive the risk weights.

• The third approach is the advanced approach suitable for very large and complex structures.

As per the guidelines of the Central Bank of Kuwait, the Bank’s Pillar I capital adequacy calculations are based on the Standardized approach. For stress testing purposes however the Bank uses an internal modeling methodology which is specifically designed for large credit exposures, which constitutes the main business line of the Bank as under its mandate, it cannot have retail or real estate exposures. For stress testing purposes only, the Bank applies its internal approach to calculating probability of default, but uses standard parameters for the LGD (loss given default) and the credit conversion factors. Stress tests are simultaneously carried out as per parameters and scenarios provided by the Central Bank of Kuwait. Stress test submissions are made based on both internal and regulatory methodologies.

Stress tests are conducted twice a year, in accordance with the Bank's Basel ICAAP Policy and as per the guidelines of the Central Bank of Kuwait. Risk Disclosures (qualitative and quantitative) are prepared based on December year-end results and a quantitative-only report is prepared based on June mid-year results.

Capital Risk Management:

Capital adequacy is the degree to which capital resources on the Bank's balance sheet are sufficient to cover the businesses' capital requirements now and in the foreseeable future. The Group's permission to operate as a bank is dependent upon the maintenance of adequate capital resources. Capital risk management is the process for reviewing capital requirements to enable the Bank to:

- Meet minimum regulatory requirements in Kuwait where its business is focused and where it is solely located.
- Support its credit rating and maintain cost of funds;
- Support business growth and the ability to withstand and tide over shocks.

The Bank ensures that it is sufficiently capitalized by continually assessing its capital resources and requirements given current financial projections. This takes into account material risks to the projections as well as strategies employed to manage those risks.

The Bank's capital management considers both economic and regulatory capital. Regulatory capital requirements are calculated on the basis of the Basel framework. Pillar 1 capital covers credit, market and operational risks. The calculation methods and risk weights are specified by Basel III rules. Pillar 2 capital can also be held against the three risk types above, but mainly covers other types of risk. Being an industrial bank with a focused but restricted mandate, a significant weight is given to Concentration Risk. The Bank uses its own internal capital framework and stress testing processes to help determine its economic capital requirements. The Bank ensures that it maintains sufficient buffers above regulatory minima at all times. The adequacy of these buffers is assessed by Risk Management and presented periodically to the Board Audit and Risk Management Committee as part of the Capital Management Policy, the risk governance process, the risk appetite review process and the stress testing process. The Bank's stress testing process forecasts the projected capital requirements and resources in a range of stress scenarios. This enables the Bank to ensure it can meet its minimum regulatory capital requirements in a stressed environment, and to assess that there is adequate buffer above regulatory capital to meet economic capital needs if trigger points are approached. The stress testing process forms a key component of the internal capital adequacy assessment process (ICAAP).

For Pillar I regulatory capital adequacy calculations, the Bank has adopted the Standardized approach of Basel III, as recommended by the Central Bank of Kuwait in determining the capital required for each component of credit, market and operational risk. As the Bank is a specialized development bank which also offers commercial banking facilities to its customers, it has long term support from the Government of Kuwait. This, together with its significant disclosed reserves, makes its available capital substantially in excess of the minimum requirements of Basel III even after taking into account the additional requirements of ICAAP under the new Pillar II and buffers determining economic capital. With the planned expansion of the asset portfolio as per the Bank's three year strategic plan, the capital adequacy ratio is expected to remain substantially above minimum regulatory requirements and economic capital estimates in the foreseeable future. This strong capitalization provides a cushion against low diversification opportunities due to the government mandate to service and develop the industrial sector in Kuwait. Theoretically, even if the Government support were to be completely removed from the capital adequacy equation, the Bank would continue to maintain strong capital adequacy with the ratio exceeding the Basel III norms by a significant margin. In fact the overall capital adequacy ratio based on Basel II was 70.3% as on December 31, 2014. Under Basel II, the long term government loan of KD 300 million had been allowed in Tier 2 capital within the specified limit. However under Basel III, the Central Bank of Kuwait has disallowed inclusion of the government loan in Tier 2 capital. Even with this change under Basel III, the capital adequacy ratio is 47.42% which is substantially above the regulatory requirement.

Capital Resources of the Industrial Bank of Kuwait

In addition to the paid-up capital of KD 20 million and significant disclosed voluntary reserves, the principal corpus of long term funds for the Bank is a renewable long term loan of Kuwaiti Dinars ("KD") 300,000,000 (= USD 1,087,140,000 approx) from the Government of Kuwait first given through an Amiri decree in 1973, from which the Bank's Projects Division provides medium and long term project finance to its industrial borrowers at concessionary pricing. The Government of Kuwait has also provided an additional KD 100 million (=USD 352 M approx) investment mandate for IBK to manage industrial financing portfolios under Islamic principles. The Bank does not have complex or hybrid capital instruments in its capital structure.

Subsidiaries**:**

The top corporate entity is The Industrial Bank of Kuwait K.S.C. The Bank has two wholly-owned subsidiaries, Kuwait Industrial Projects Company KSCC (KIPCO), a Kuwaiti closed shareholding company ("KIPCO"), and Senaey Enterprises Ltd, a limited liability company incorporated in George Town, Grand Cayman, the British West Indies (together "the Group"). KIPCO is the Group's vehicle for domestic investments and for holding and managing assets taken over by the Bank as a result of domestic loan defaults; it accounts for some 6% of the total Group assets. Senaey Enterprises is insignificant and not a material element of the Group statement of financial position. Capital adequacy data submitted to the Central Bank of Kuwait includes relevant data from both subsidiaries on a fully consolidated basis.

Capital Structure – 31.12.2014

				KD'000
i)	**Tier I Capital**			220,478
	Permanent Shareholder Equity			20,000
	Reserves:			
		Legal reserves	31,620	
		Voluntary reserves	135,909	
		Fair value reserve	13,280	
		Retained Earnings	19,669	200,478
	Additional Tier I capital			Nil
	Tier 2 Capital			5,508
	General Provision as allowed			5,508
	Total Eligible Capital after deductions			**225,986**

Capital Requirement for Credit Risk Weighted Assets as on 31.12.14.

KD '000

	Asset Categories for Credit Risk (Standard Portfolio)	**Net Credit Exposure** (after CRM)	**Risk Weighted Capital Charge**
1	Cash Items	226	---
2	Claims on Sovereigns	193,189	369
3	Claims on International Organizations.	---	---
4	Claims on PSE	---	---
5	Claims on MDB	---	---
6	Claims on Banks	127,270	25,460
7	Claims on Corporates	314,853	314,853
8	Claims on Securitized Assets	---	---
9	Credit Derivative Claims	---	---
10	Regulatory Retail	---	---
11	Past Due Exposures	4,569	4,329
12	Other Exposures	95,605	95,605
	Total Exposure	735,712	440,616
	Less : Excess general provision		(12,921)
	Total Credit Risk Weighted Exposure		427,695
	Minimum Capital Requirement for Credit Risk		55,600

Capital Requirement for Market Risk

Total Market Risk Weighted Exposure	7,322
Minimum Capital Requirement for Market risk	952

Capital Requirement for Operational Risk

Total Operational Risk Weighted Exposure	41,499
Minimum Capital Requirement for Operational Risk	5,395

Total Risk Weighted Exposure		476,516
Total Minimum Capital Requirement for credit, market and operational risks		61,947
Eligible Capital		225,986
Tier 1	220,478	
Tier 2	5,508	
Unused but Eligible Capital		164,039

Capital Adequacy Ratio

Capital Adequacy Ratio per Basel III / CBK	47.42 %
Capital Adequacy Ratio based on Tier I Capital only.	46.27 %
CET1 Capital Adequacy Ratio	46.27 %.

Credit Risk Management:

Credit risk is the risk of suffering financial loss should any of the Bank's customers or market counterparties fail to fulfill their contractual obligations to the Bank. The granting of credit is one of the Bank's major sources of income and, as the most significant risk; the Bank dedicates considerable resources and energy to control it.

The credit risk that the Bank faces arises mainly from project finance and working capital finance. The Bank is also exposed to other credit risks arising from its treasury activities, including debt securities, settlement balances with market counterparties and available for sale assets.

The role of the risk management function is to provide bank-wide direction, independent risk assessment, oversight and challenge of credit risk-taking. The Bank has dedicated departmental credit policies reviewed by a committee for policies and procedures (where the CRO is a member). The Board of Directors approves the credit risk control framework, which provides a structure within which credit risk is managed together with supporting risk management departmental policies. Loans and advances to customers provide the principal source of credit risk to the Group although the Bank can also be exposed to other forms of credit risk through, for example, loans to banks, loan commitments and debt securities. The Bank's risk management policies and procedures are designed to identify and analyze risk, to set appropriate risk appetite, limits and controls, and to monitor the risks, delinquency, adequacy of follow up and rating assessments. The risk management department independently reviews and rates all individual credit proposals generated by the two credit granting departments, relating to project finance and commercial, working capital and trade finance. It also quantifies, reviews and monitors the quality and movement of the overall credit portfolio of the Bank.

One area of particular review is concentration risk. A concentration of credit risk exists when a number of customers belong to the same group, or are engaged in similar activities and have similar economic characteristics that would cause their ability to meet contractual obligations to be similarly affected by changes in economic and other business conditions. As a result, the Bank constantly reviews its concentration in a number of areas including, for example, geography, maturity, industrial sector and group control. Diversification is achieved through setting maximum exposure guidelines to individual counterparties not exceeding 15% of capital.

The Bank has in place a system for internal credit risk rating of all exposures on a scale of 1 to 10. Risk Management recommends credit ratings for new clients and periodically reviews all existing borrower ratings in the Bank using well defined internal rating parameters. Risk Management tracks the weighted average rating of the credit portfolio and each risk category within the portfolio.

Risk management has implemented an algorithm based system that determines probabilities of default benchmarked to a large external database. This is mapped to the internal credit rating system currently this system is being used to validate the internal ratings of individual credit as also the overall credit portfolio.

In order to mitigate credit risk, exposures are usually secured by acceptable collateral. The existing portfolio of loans and advances reflects the Bank's emphasis on lending inside Kuwait and in particular to industrial units in Kuwait - a country whose dynamics the Bank comprehends well and where the Bank has a better understanding of the inherent risks. The Bank has credit concentration to the industrial sector due to the terms of its constitution. The Bank manages the risk by avoiding concentration by obligor, by a particular industry and, in the case of cross border exposures, by geographical area.

Special attention is paid to overdue accounts by committees especially set up for this purpose. Follow up measures are discussed and remedial action taken. If required, appropriate provisioning levels are determined.

At both the departmental level as well as the overall bank level, disciplined credit processes are in place. The processes are intended to ensure that risks are accurately assessed, properly approved and continuously monitored. The primary tool for managing credit risk is a set of credit policies and procedures that are periodically reviewed and updated. A stringent approval framework exists in the Bank which mandates a rigorous and thorough evaluation of the creditworthiness of every obligor. All credit and investment proposals and their extensions and renewals of existing credits are assessed by Risk Management.

Credit limits are established for all customers after careful assessment of the relevant credit application. As per procedure, the approval of the Board of Directors is necessary for credit limits above a certain level. Management's appetite is conveyed by limits for country, industry, borrower and product. Excesses above approved limits require approval by appropriate credit authorities in the Bank.

Concentrations by size, industry, business and industry sectors are monitored and limited. Central Bank of Kuwait defines concentration as 15 per cent of a bank's total eligible capital base as defined under Basel III/CBK; all concentrations in the portfolio by industry are monitored closely for adverse financial or economic conditions.

Documentation and perfection of the collateral position is ensured before credit is granted; care is taken to ensure that collateral documentation is sufficient and adequately protective. In case of industrial loans the customer provides a first mortgage on the project's fixed and moveable assets; a minimum collateral coverage of 1.5 times the loan is normally maintained. In case of marketable equity, evaluations are carried out on a quarterly basis and collateral coverage is monitored by the Follow Up department. The borrower arranges for comprehensive insurance of the assets covered under the industrial loan, with the Bank as first beneficiary.

Risk Management tracks delinquencies at the company and portfolio level and is in constant dialogue with the Business departments so that action on irregularities can be taken in time and slippage down the past-due time buckets are controlled as far as possible. The classification on irregularities and approach to provisioning is explained below. A loan is placed on non-accrual when interest or principal has not been paid for 90 days. Nonaccrual status is considered confidential information and is not disclosed to any party outside the Bank**.** Additionally, loans are placed on non-accrual status whenever there is reasonable probability that 100 percent of future interest will not be collected. Loans are not placed back on accrual status unless all back interest and principal payments are made. Loans that are well secured and are in the process of collection are placed on accrual status. The Bank also makes additional provisions on a case by case basis based on the recommendations of the Provisions Committee using management's discretionary provisioning authority.

Information related to credit exposures:

Past Due / Impaired Assets and Provisioning:

IBK follows the Central Bank of Kuwait definitions of irregular assets and guidelines for impairment provision. Classification of credit exposures and computation of provisions are as below:

A. Credit Facilities to Customers (Resident & Non-Resident):

(i) Exposure is classified as Irregular if:

- the debit balance in the current account has been constantly showing an excess of over 10% of the approved Overdraft limit;
- the current account is in debit, without an approved Overdraft limit;

- credit facilities have expired, outstanding's have not been settled and the Bank has decided not to renew the facilities on credit grounds;
- loan installments are defaulted;
- interest is in arrears.

(ii) Irregular exposures are classified as below:

- Sub-Standard: Where any of the irregularities as above has been existing for a period exceeding 90 days but less than 180 days, or if, in the Bank's judgment, there is noticeable deterioration in the customer's financial condition.
- Doubtful Debts: Where any of the irregularities as above has been existing for a period exceeding 180 days but less than 365 days, or if, in the Bank's judgment, there is noticeable deterioration in the customer's financial condition.
- Bad Debts: Where any of the irregularities as above has existed for a period exceeding 365 days, or if, in the Bank's judgment, there is noticeable deterioration in the customer's financial condition. (iii) Provision requirements:

Specific provisions are made as below:

- Sub-Standard exposures : 20%
- Doubtful Debts : 50%
- Bad Debts : 100%

1% General Provisions are made on all exposures not subject to a specific provision after deducting certain allowed collaterals as per the guidelines of The Central Bank of Kuwait.

This section discusses the part of the credit portfolio where customers have been delinquent in their repayments. The actual cash overdue amount (excluding interest) was 4.30% of credit exposure.

	2014	
Past Due Period Category (days)	**Delinquent Amount (KD 000)**	**% Of Total Past Due**
0<30	4,063	33.54
31<90	6,077	50.17
91<180	1,164	9.61
181<364	225	1.85
1 year (365) <3 year	585	4.83
Doubtful Debt (3-5years)	-	-
Bad debt (over 5 years)	-	-
Total Past Due	**12,114**	
Total Credit Exposure	**282,003**	
Past Due exposure as % of total credit exposure	**4.30%**	

The ratio of Non-Performing Loans (NPL) to credit exposure stood at 1.37% as on 31.12.2014. The CBK definition of nonperforming loans has been applied which considers of all credit exposures that are past due with 90 days or greater, and also considers the customer's total exposure if it's NPL exposure for a particular facility exceeds 50% of its total exposure. This NPL figure includes customers with more than one facility, where past due exceeds 50% of his total exposure.

B. Sovereign Exposures:

Impairment classification and provisioning is made on the credit scoring method as per Bank of England Matrix.

C. Credit Rating:

The Bank follows an internal credit rating system based on a rating scale of 1 – 10. Ratings between 1-4 are considered Prime Credit. Those that fall in the categories 5A, 5B and 5C are Performing Credits and those between 6–10 belong to the Non-Performing credit or Watch List.

Information on Credit Exposures:

Gross Credit Exposures before CRM as on 31.12.14 **KD '000**

	Asset Categories (standard portfolios)	On Balance Sheet	Off Balance Sheet ****
1	Cash Items	226	---
2	Claims on Sovereigns	193,189	---
3	Claims on Internatio0nal Organizations.	---	---
4	Claims on PSE	---	---
5	Claims on MDB	---	---
6	Claims on Banks	122,845	4,293
7	Claims on Corporates	278,383	55,877
8	Claims on Securitized Assets	---	---
9	Credit Derivative Claims	---	---
10	Regulatory Retail	---	---
11	Qualifying Residential Housing Loans	---	---
12	Past Due Exposures	4,556	13
13	Other Exposures	87,222	8,383
	Total	686,421	68,566

**** Note: All unfunded corporate credit exposures are located in Kuwait.

Daily Average Gross Credit Loans and Advances:

31 DEC 2014

	Year, 2013		Year, 2014	
	Daily Average Balance	%	Daily Average Balance	%
Grand Total Loans and Advances	319,082,702.03	100.00	299,231,723.28	100.00
Loans & Advances - Industrial Loan I	157,478,737.96	49.35	151,861,313.66	50.75
Total Loans and Advances - Commercial	161,603,964.07	50.65	147,370,409.62	49.25
Industrial Loans - Commercial	125,496,999.90	39.33	115,733,261.62	38.68
Other Loans	1,224,357.86	0.38	1,175,947.24	0.39
OverDrafts & Overdrawn A/cs	34,732,996.48	10.89	30,129,681.72	10.07
Suspense L/Cs & Doc Rec.	81,143.26	0.03	69,422.23	0.02
Acceptance Bills	68,466.57	0.02	262,096.81	0.09

Geographical Distribution of Exposures:

31 DEC 2014

	Total Loans and Advances				Loans & Advances- Industrial Loan-I				Loans & Advances-Commercial Facilities			
	December, 2014		December, 2013		December, 2014		December, 2013		December, 2014		December, 2013	
Kuwait	280,839	99.59%	305,438	99.61%	148,174	100%	153,620	100%	132,665	99.13%	151,818	99.22%
Europe	441	0.16%	438	0.14%	0		0		441	0.33%	438	0.29%
Asia & Pacific	723	0.26%	760	0.25%	0		0		723	0.54%	760	0.50%
Grand Total	282,003	100.0%	306,636	100.0%	148,174		153,620		133,829	100.0%	153,016	100.0%

Residual Maturity of the Loans and Advances Portfolio:

31 DEC 2014

	Total Portfolio		Industrial Loan at encourged rates		Loans & Advances at Commercial rate	
	December, 2013	December, 2014	December, 2013	December, 2014	December, 2013	December, 2014
Upto 1 Month	*50,570*	*39,861*	*9,239*	*7,278*	*41,331*	*32,583*
1 to 3 Month	*61,090*	*46,812*	*4,904*	*9,902*	*56,186*	*36,910*
3 to 12 Month	*48,943*	*51,683*	*27,654*	*25,014*	*21,288*	*26,669*
1 to 3 Years	*81,942*	*87,161*	*63,988*	*65,386*	*17,953*	*21,775*
3 to 5 Years	*48,229*	*46,155*	*44,072*	*41,725*	*4,157*	*4,430*
Over 5 Years	*15,863*	*10,331*	*3,763*	*(1,132)*	*12,100*	*11,463*
Balance at Year end	*306,636*	*282,003*	*153,620*	*148,174*	*153,016*	*133,829*

Loans and Advances Portfolio by Sector

31 DEC 2014

	Regular & Iregular Loans and Advances of the Bank							
	Outstanding Balance 2013		Outstanding Balance 2014		Total Provision 2013		Total Provision 2014	
Chemicals	17,130,058.11	5.59%	16,291,182.15	5.78%	171,303.55	4.52%	162,234.79	4.33%
Food & Beverages	15,440,313.93	5.04%	15,109,457.26	5.36%	152,858.34	4.04%	138,800.68	3.71%
Metal Products & Engineering	96,448,598.44	31.47%	91,267,159.23	32.36%	1,153,272.88	30.45%	1,161,719.38	31.03%
Construction & Bulding Material	69,848,119.92	22.79%	68,799,627.47	24.40%	1,215,606.07	32.09%	1,217,807.17	32.53%
Trading and Commerce	85,000.00	0.03%	160,225.00	0.06%	850.00	0.02%	1,602.25	0.04%
Furniture	2,049,277.60	0.67%	2,670,424.39	0.95%	20,497.73	0.54%	26,709.19	0.71%
Textile	83,916.27	0.03%	102,689.86	0.04%	839.16	0.02%	1,026.90	0.03%
Marine	1.00	0.00%	1.00	0.00%	1.00	0.00%	1.00	0.00%
Paper & Printing	13,383,372.27	4.37%	7,803,223.20	2.77%	133,834.71	3.53%	78,033.22	2.08%
Government	759,730.95	0.25%	722,503.65	0.26%	7,597.31	0.20%	7,225.04	0.19%
Oil and Gas	35,749,624.25	11.66%	43,117,345.86	15.29%	357,496.24	9.44%	431,173.46	11.52%
Agriculture and Fishing	516,102.18	0.17%	430,000.00	0.15%	5,161.02	0.14%	4,300.00	0.11%
Others(Non Financial)	36,540,665.44	11.92%	35,088,117.59	12.44%	384,193.21	10.14%	369,031.69	9.86%
Non Financial Sectors	288,034,780.36	93.98%	281,561,956.66	99.84%	3,603,511.23	95.13%	3,599,664.77	96.14%
Financial Sectors	18,437,506.84	6.02%	440,932.78	0.16%	184,380.02	4.87%	144,414.28	3.86%
Total Sectors	**306,472,287.20**	**100.00%**	**282,002,889.44**	**100.00%**	**3,787,891.25**	**100.00%**	**3,744,079.05**	**100.00%**
	General Provision & management decision				23,783,879.00		15,523,293.00	
	Total Provision				**27,571,770.25**		**19,267,372.05**	

Impaired Loans – Geographical Distribution

31 DEC 2014

	Outstanding loans		Provision provided for impaired loans	
	2013	**2014**	2013	**2014**
Kuwait	2,727	1,693	800	839
Other GCC countries				
Grand total	**2,727**	**1,693**	**800**	**839**
Impaired loans as a percentage of outstanding loans portfolio	0.89%	0.57%		
Coverage percentage			29.34%	49.50%

1)For purposes of this table, Impaired loans is defined as those for which specific provision have been provided for.

Credit risk mitigation

Netting: In cases where the Bank's claims against customers are not settled, the Bank exercises set-off rights and pursues its claim on a net basis. During the course of any legal action, the Bank preserves its claim at the original net level, disregarding any partial payment(s) in order to avoid inadvertently triggering any legal issues that could otherwise arise.

Collateral Valuation and Management: In cases where collateral is to be taken, the Bank accepts standard collateral types such as cash, chattel mortgage over movable assets, mortgage over fixed assets, personal / corporate/ bank guarantees etc. In the case of mortgages, the Bank insists on being named the loss-payee in the related insurance policy. Where guarantees are taken, the Bank satisfies itself of the creditworthiness of the guarantor by obtaining full financial information about the guarantor, on the rationale that the Bank views the guarantor as though he were himself the primary obligor who would himself have to be eligible for the size of the commitment. In respect of bank guarantees, a formal guarantor line for the bank concerned is a pre-requisite.

Given its status as a specialized industrial finance institution, the Bank has sufficient skills and means in-house to evaluate projects, factories and other types of fixed assets under mortgage to the Bank.

Credit Risk Concentration: The Bank's charter limits its customer-base to manufacturing industries specifically to entities holding industrial license. Accordingly, there is a credit concentration in the industrial sector. Within that class, the Bank's portfolio is composed of customers spanning a wide variety of activity. Additionally, the Bank participates in syndicated loans to non-resident banks. The Bank's customer-base is not subject to any significant degree of cyclicality.

Credit Exposure after risk mitigation and credit conversion factor. 31.12.2014

	KD '000	Credit Exposure before CRM	Net Credit Exposure after CRM	Credit Risk Weighted Asset
	Asset Categories (standard portfolios)			
1	Cash Items	226	226	0
2	Claims on Sovereigns	193,189	193,189	369
3	Claims on International Organizations.	0	0	0
4	Claims on PSE	0	0	0
5	Claims on MDB	0	0	0
6	Claims on Banks	127,270	127,270	25,460
7	Claims on Corporates*	334,260	314,853	314,853
8	Regulatory Retail	0	0	0
9	Qualifying Residential Housing Loans	0	0	0
10	Past Due Exposures	4,569	4,569	4,329
11	Other Exposures	95,605	95,605	95,605
	Total	755,119	735,712	440,616
	* Includes Contingencies and Commitments		Excess General Provision	(12,921)
			Total	***427,695***

Market Risk Management:

Market Risk is the risk that the Bank's earnings or capital, or its ability to meet business objectives, will be adversely affected by changes in the level or volatility of market rates or prices such as interest rates, credit spreads, commodity prices, equity prices and foreign exchange rates. This risk is inherent in the financial instruments associated with our operations and/or activities including loans granted at commercial rates, deposits, securities and trading account assets, and derivatives. The majority of market risk exposure resides in the Bank's treasury and investment functions and market risk through the local equity holdings of the Bank's subsidiary KIPCO. IBK Risk Management's market risk objectives are to:

- Understand and control market risk by robust measurement and the setting of limits and monitoring of the same.
- Ensuring accuracy in the deal/settlement process
- Facilitate business growth within a controlled and transparent risk management framework.
- Measure and report non-traded market risk.

Market risk for the Bank is relatively limited as**,** except for managing an FX book for its own account and its local industrial customers, and in rare cases using derivatives for hedging purposes, the Bank does not expose itself significantly to market risks. Appropriate limits have been established and treasury and investment activities are constantly monitored.

The focus at IBK is on industrial lending and on corporate banking. The Bank has a long term investment in its wholly owned subsidiary (KIPCO) which invests in the local market and has a non-traded Kuwaiti equity portfolio. There is also an international component in the Bank's equity book which is invested in start-up ventures through reputed international managers. These investments are of long term nature and are exposed to the downside risk of direct equity investments. These investments are diversified and individual investments are capped within limits. The Bank is not actively involved in equity or bond trading, trading in derivative products, options, commodities or most of the other market risk generating activities that commercial/investment banks usually engage in.

Market risk is monitored taking into consideration market analysis, market liquidity, business strategy and dealer experience. The Bank has limits on investment size, country, and counterparty exposure as well as on open positions by dealers and for the Bank as a whole. These limits help to reduce the absolute amounts of market risk. In addition, the Bank has established stop-loss limits for certain activities involving market risk.

Market risk for trading portfolio and foreign exchange exposures**:** The Bank currently does not have a proprietary trading portfolio of any significance in foreign exchange or money market instruments. It does not have derivative trading exposures or exposures in commodities. However, all forward foreign exchange swap positions have been considered as part of derivative exposures amounting to KD 4.2 million.

Market Risk

	Capital Requirement under Standardized Approach.	
	Risk Category	**Capital Charge**
1	Interest Rate Risk	0
2	Equity Position Risk	0
3	Foreign Exchange Risk	585.76
4	Commodities Risk	0
	Minimum Capital Requirement for Market Risk	585.76
	Total Market Risk Weighted Assets	7,322

Equity position in the banking book :

Given the specialized nature of the Bank and under its constitution, the Bank invests in equity of companies both for strategic and relationship reasons as well as to generate capital gains. The Direct Investments and Promotions department manages the equities portfolio which has local and international dimensions. It makes investments in new ventures and funds with the objective of making capital gains in the international private equity markets. The equities portfolio for investments within Kuwait is managed by "Kuwait Industrial Projects Company KSCC"(KIPCO), a wholly owned subsidiary of the Industrial Bank of Kuwait, whose financial statements are consolidated with those of the Bank.

Strategic investments are those that fit in with the Bank's objectives of long term industrial development and expected to benefit the Bank in terms of reach and network presence. Strategic investments in equities may be made to ensure growth and development of existing companies, investment in new ventures as well as to exercise control over companies which have turned severely delinquent and are underperforming and thus have to be taken over. Equity investments may be made by KIPCO as pre-IPO placements or may be made directly through the stock exchange for listed companies. Since these are long term investments, this is a passive investment portfolio with valuations subject to the movements of the market. Following world and regional trends, the Kuwait Stock Exchange index continues to witness high volatility.

Impaired investments form a small component of the equities portfolio. This is retained to exercise remedial control over companies which have turned severely delinquent, are underperforming and thus have to be taken over. These are under management of KIPCO and relate to domestic exposures only.

Differentiation is made between the component of the portfolio which has been made with the objective of making capital gains and those that have been made for strategic reasons mentioned above. It is recognized that equity investments carry considerable downside risk as well as expectation of high returns. As per Basel III guidelines, 100% capital is set aside to cater to risks of all investments in equities in the books of the Bank. Risk Management rates all investments made by the Direct Investments and Promotions department using a rating methodology for private equity developed internally by the risk management department.

Interest Rate Risk Management:

The overall goal is to manage interest rate sensitivity so that movements in interest rates do not adversely affect net Interest Income. Interest rate risk is measured as the potential volatility in Net Interest Income caused by changes in market interest rates. The Bank uses interest rate gap analysis to measure the interest rate sensitivity of its earnings caused by re-pricing mismatches between rate sensitive assets, liabilities and off balance sheet positions.

The Bank has received a 20 year loan from the Government of Kuwait (initiated in 1975) which is partly priced at the fixed rate of 1/2 % per annum to the extent of the total industrial loans and commitments made by the Bank. In 2007, this was extended by another KD 100 million by the Government. This low-cost source is a very important component of the Bank's total cost base. The Bank engages in subsidized fixed rate lending to the industrial sector. To that extent, fixed cost sources and applications of funds are outside the framework of interest rate risk calculations.

Substantially all remaining KD loans are floating and priced at the Central Bank discount rate plus margin and are re-priced when the Central Bank changes the discount rate.

Around 90% of the Bank's assets are denominated in Kuwaiti Dinars. Among other currencies, the US Dollar is significant. As to all other currencies, the exposure, though not significant, is nonetheless generally matched in each of the maturity buckets.

From time to time, stress tests are conducted to gauge the impact on income under stress conditions e.g. sensitivity to a 1% reduction in the discount rate of the Central Bank.

Interest rate risk in the banking book

Interest rate risk in the banking book arises from the mismatches between assets and liabilities, in the various maturity buckets. These are however kept within prescribed limits set for each maturity bucket. There is a downside risk in providing hedging as the Kuwaiti Dinar market lacks depth, with limited number of players in the interbank Kuwaiti Dinar market. Interbank activity is sporadic beyond short maturities. Central Bank of Kuwait intervention bonds, direct one month intervention and treasury bonds are the only available instruments for deploying excess liquidity. As a result, CBK interventions can have a major impact on KIBOR rates. The lack of interest rate hedging instruments in the KD market is a concern. However, the Bank's overall exposure to interest rate risk is mitigated by the following factors: (i) active and effective management of the Treasury investments portfolio; (ii) commercial loans are priced on floating rate basis; and (iii) project loans are funded by the Government loan and are thus market-independent.

December, 2014	Interest Rate Sensitivity KD (000)		
Kuwaiti Dinar			
	up to 1 year	1-5 years	Over 5 Years
Interest earning Assets	405,574	150,623	15,562
Interest bearing Liabilities	318,105	0	0
GAP	87,469	150,623	15,562
Cumulative GAP	87,469	238,092	253,654

Sensitivity to 1% rate change **2,536.54**

December, 2014	Interest Rate Sensitivity USD in KD (000)		
US DOLLAR			
	up to 1 year	1-5 years	Over 5 Years
Interest earning Assets	43,864	0	0
Interest bearing Liabilities	73,863	0	0
GAP	(29,999)	0	0
Cumulative GAP	(29,999)	(29,999)	(29,999)

Sensitivity to 1% rate change **(299.99)**

Overall sensitivity in KD to 1% rate change **2,236.55**

Liquidity Risk Management:

Liquidity risk is the risk that the Bank is unable to meet its obligations when they fall due as a result of a sudden, and potentially protracted, increase in net cash outflows. Such outflows would deplete available cash resources for client lending, trading activities, investments and deposits. In extreme circumstances lack of liquidity could result in reductions in balance sheet and sales of assets, or potentially an inability to fulfil lending commitments. The risk that it will be unable to do so is inherent in all banking operations and can be affected by a range of institution-specific and market-wide events.

Liquidity risks are managed by monitoring asset liability maturity mismatch gaps and target liquidity ratios. The Bank's liquidity, both in local and foreign currency remained comfortable in 2014. The Bank continued to build relationships with Kuwaiti institutions who are in a position to lend in foreign currency. Thus a diversified fund sourcing base is available. Contingency plans are in place to manage short term liquidity shocks. These risks are monitored by Risk Management and collectively assessed through the Assets and Liabilities and Investments Committee (ALCO). The Bank adheres to the guidelines of the Central Bank of Kuwait with regard to liquidity management and has always adhered to the regulatory gap limits.

Accounting policies: Financial assets which are intended to be held for an indefinite period of time and which are not classified as at fair value through statement of income, loans and receivables and Held to Maturity assets are classified as Available for Sale investments. Such investments are reported at fair value, determined on a quarterly basis and marked to market where market valuations are available. Unlisted equity participations or private investments in Funds whose fair value cannot be reliably determined are carried at cost less impairment. Other Available-for-Sale investments are initially recognized at cost and subsequently re-measured at fair value with unrealized gains or losses recognized directly in Other Comprehensive Income.

The fair value investments listed on the stock exchange are based on their quoted market price (bid price) at the balance sheet date without any deduction for transaction cost.

All classifications of investments are based on International Financial Reporting Standards.

Note: Quantitative information relating to investments is available in the financial statements.

Operational Risk Management:

Operational risk is the risk of direct or indirect losses resulting from human factors, external events, and inadequate or failed internal processes and systems. Operational risks are inherent in the Bank's operations. Major sources of operational risk include: operational process reliability, IT security, outsourcing of operations, dependence on key suppliers, implementation of strategic change, integration of acquisitions, fraud, human error, customer service quality, regulatory compliance, recruitment, training and retention of staff, and social and environmental impacts. The Bank is committed to the identification, measurement and management of operational risks. Such risks are managed through bank-wide or line of business specific policies and procedures, controls, and monitoring tools. A critical element is the identification of business specific Key Risk Indicators (KRIs) and their monitoring across business lines. In particular, Risk Management has worked closely with business units and implemented improved management approaches for operational risk, including self-assessment formats and surveys, to focus on critical risk areas, to strengthen control, and minimise operating losses.

The Bank's operational risk management framework aims to:

- Understand and report the operational risks being taken by the Bank.
- Capture and report KRIs and operational errors made.
- Understand and minimize the frequency and impact, on a cost benefit basis, of operational risk events.
- Manage residual exposures using insurance.

The primary responsibility for managing operational risk rests with the departmental managers who are responsible for maintaining the internal control procedures that are appropriate to their particular operating environment. An operational risk self-assessment process is in place with focus on Key Risk Indicators that are specific to the operational area. Risk Management and Internal Audit functions play a vital role in reviewing and maintaining the integrity of the control environment. Additionally, the Bank has covered certain specific areas of operational risk that cannot be controlled internally, through insurance policies. A high proportion of the Bank's operational risk events have a low financial cost associated with them and a very small proportion of operational risk events have a material impact and this remained true for the year 2014.

Procedures are in place to safeguard the confidentiality and integrity of stored data and information. These include:

- The installation of firewall systems to protect the network from external interference
- Access controls over application systems
- Compliance with the principle of dual control in operating procedures
- Various monitoring and internal control processes.
- Online data replication process on independent servers.
- Onsite contingency planning.
- Offsite business continuity and disaster recovery programs.

The IT Security function reports to the Chief Risk Officer and independently monitors the security environment and security incidents and violations. In 2014, as a new core banking system is in the process of implementation, the external vulnerability assessment has been planned in stages.

As a result of risk and system analysis the Bank is in the process of substantially upgrading the IT infrastructure including transactional, data warehousing and risk management solutions in order to form the base for future growth opportunities.

Capital allocation for Operational Risk:

For the purpose of capital adequacy under Basel III, the Bank presently follows the Standardized Approach of measurement for calculating its operational risk capital charge based on three years' gross income. This is calculated as per Beta factors provided under Basel III guidelines which serve as a proxy for the relationship between operational loss for a business line and the gross income for that business line. The total operational risk charge has been calculated as the three year average of the summation of the regulatory capital charges across the business lines namely 'Commercial Banking' including project lending and working capital lending, and 'Trading & Sales' under which direct equity fund investments are classified. As the constitution of the Bank and its specialized nature restrict it from operating in certain areas, it is being specifically stated that it does ***not*** operate in the areas of retail banking, in raising corporate finance through the equity markets, in third party payment services, in agency services, in asset management, brokerage and third party custodial services. The Bank maintains a database of its operational losses and classifies it as per Basel standards.

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Operational Risk

KD'000

Business Line (per Basel III Classification)	Gross Income* 2012	2013	2014	3 year average Gross Income	Capital Charge
Commercial Banking	17,240	15,032	18,225	16,832	2,524.85
Other	4,299	5,054	3,898	4,417	795.06
Total	21,539	20,086	22,123	21,249	3,319.91
Total Operational Risk Weighted Exposure					41,499

* 'Gross Income' excludes gains from disposal of 'Available for Sale' investments as per Basel III / Central Bank of Kuwait guidelines relating to calculation of Operational Risk Charge

Anti-Money Laundering Policies

The Bank is subject to the rules and regulations of its regulator, the CBK, in the conduct of banking business. The Bank is bound by CBK Instruction No. (2/BS/BSa/308/2013) and Law No. 106 of 2013 and subsequent amendments which have been designed to combat money laundering.

The Bank has internal written policies and procedures authorized by its Board of Directors, designed to prevent, detect and combat money laundering. Its anti-money laundering systems include processes, policies, personnel and training, documentation, reporting, and control systems. In 2013, based on new guidelines of the Central Bank of Kuwait the AML policy and procedure was updated to cover the latest developments.

The Bank is required to obtain from its customers, copies of the licence and registration at the time of opening customer accounts. The Bank follows Know Your Customer ("KYC") processes, and the identity of the Bank's customers is established *ab initio* through official documents as above. Customer records are preserved for a period of 5 years after the termination of the banking relationship. Suspicious transactions are tracked. Awareness programs are conducted continuously. The Bank has implemented a state of the art automated anti-money laundering system to track and analyze suspicious transactions. The Bank has initiated the process of becoming FATCA compliant.

In 2014, the new guidelines of the Central Bank of Kuwait requires all customers of the Bank to be rated for money laundering and terrorist financing risks. An internal methodology has been developed by risk management and has been incorporated in Board approved policies of AML-TF. Implementation across the customer base will take place in 2015.

Information related to the Bank's remuneration policy:

Overview of the key features and objectives of the remuneration policy

The Bank's Remuneration Policy is designed to attract and retain highly qualified, skilled, and knowledgeable professionals and incorporates all the requirements of the CBK as mentioned within its corporate governance instructions. The Policy includes all necessary aspects and components of financial remuneration taking into account reinforcing the Bank's performance objectives and effective risk management. The Bank's Remuneration Policy incorporates all the requirements of the CBK as mentioned within its corporate governance instructions,

The Bank's Board, based on the Board Nominations and Remuneration Committee (NRC) recommendations, approves and modifies the Bank's remuneration policy and its design, and reviews the process of its implementation to ensure that it is operating as intended.

Remuneration components: The various remuneration components are combined to ensure an appropriate and balanced remuneration package that reflects the characteristics of the business unit, the employee's grade in the Bank and the job function as well as market practice concerning the prevailing remunerations level. The employee remuneration components are:

1. Fixed remuneration,
2. Performance based Annual Incentives for all staff (STI),
3. Risk and Return Based Long Term Incentives for Senior Staff (LTI),
4. Other benefits, and
5. End of service payments.

The fixed remuneration is determined on the basis of the role of the individual employee, including job responsibility, job complexity, grade, performance and local market conditions and the applicable laws.

The performance-based incentives (STI and LTI) are designed to motivate and reward the employees to achieve the goals and objectives of the Bank as per the strategy and annual plans of the Bank. Performance based incentives are disbursed as an annual cash bonus for all staff (STI) and deferred cash bonus for the senior staff (LTI). The incentive schemes are linked with a balanced mix of performance indicators at the corporate level, department / unit level and the employee level. The primary goal of the STI is to align the incentive with the Bank's annual performance and individual contributions. The LTI for the senior staff is designed to encourage sustainable and risk adjusted long term performance of the Bank. The LTI scheme is applicable from 2015 onwards.

The Bank has introduced a formal performance management process for evaluating and measuring staff performance at all levels. In the beginning of the year, the staff and their performance managers plan and document the annual performance goals (KPIs), required competencies and personal development plans for the staff. At the annual performance appraisal interview, the performance managers and the reviewers evaluate and document performance against the documented goals. Decisions on adjustment of the employee's fixed salary and on performance based incentives are made on the basis of the annual performance review.

Other benefits like annual leave, medical leave and other leaves, medical insurance, annual tickets, and allowances are provided on the basis of individual employment contracts, local market practice subject to the applicable laws. End of service payments are payable in accordance with the employment contract subject to the applicable laws.

The CEO oversees the implementation of the remuneration system of the employees as per the approved policy, including the design and related procedures. The Board NRC periodically evaluates the sufficiency and effectiveness of the Remuneration Policy to ensure its alignment with the Bank's objectives. The NRC assists the Board to conduct an independent annual review of the Bank's compliance with the Remuneration Policy.

Nomination and Remuneration Committee: The role of the Nomination and Remuneration Committee is to assist the Board of Directors in fulfilling its oversight on the identification of persons eligible for membership of the Board of Directors; the Committee will submit its recommendations to the Board regarding candidates to the different committees. The committee is also responsible for the draft, review and update of the Remuneration policy, and assist the board in evaluating the effectiveness and fairness of the policy, and to ensure that the policy is appropriate with the strategic objectives of the Bank. The NRC conducts regular revision of Remuneration Policy and makes recommendations on any updates to the Board. It carries out regular evaluation of the sufficiency and effectiveness of Remuneration Policy to ensure alignment with Bank's objectives. It makes recommendations to the Board regarding the level and components of the remuneration of the CEO and his direct reports as well as the Bank's executive staff. It works closely with the Bank's Risk Committee and the CRO in order to evaluate the incentives proposed by the remuneration system

Meetings: 7 meetings were held in 2014.

Members of the NRC:

Mr. Salah M. Al-Kulaib (full year),

Mr. Ahmed T. Al-Tahous (full year),

Mr. Adel F. Al-Humaidhi (full year)

Mr. Khalid J. Al Rubaian (from 25.6.2014)

Mr. Khalid S Al Ali (from 25.6.2014)

Mr. Khaled N. Al-Fouzan (till 25.6.2014),

External Consultants to the design of the remuneration structure and advisor to the Committee: Ernst & Young Consultancy Co. WLL. Under the recommendations of the consultants, a new incentive policy was structured in 2014, the components and description of which has been given above. A completely revised performance management system for all employees became effective in 2014.

Risk Assessment: The main business of the Bank is in the nature of a combination of development and commercial banking supplemented by an investments portfolio. It also manages two government funded portfolios related to small scale industry and handicrafts and agricultural financing. It is risk management department's assessment that the remuneration policy of the bank evenly weights the long and the medium term results and this is well documented and recorded in the new performance appraisal system (PMS) through a SMART process (Specific, Measurable, Achievable, Relevant and Time based) through detailed and quantified KPIs (Key performance indicators), continuous performance monitoring and coaching, periodic reviews and final performance based on financial results as well as defined qualitative objectives. Senior management is judged by the Remuneration Committee on a distribution and combination of return on investment, defined risk measures including CAMEL-BCOM components, and business elements. In 2014, risk management confirms that no material risk taker or the senior management approached areas for short term gains such as financial market trading or areas subject to high risk and potential reward or indulged in excessive risk taking. All proposals of the Bank and the overall portfolio of the Bank was assessed independently by risk management and reported to the Board Risk Committee.

With respect to the determination of relationship between performance and levels of remuneration, the Bank has established adequate links and weights for individual performance, business unit performance and corporate performance according to the different levels of bank staff with assistance of the external consultants. Corporate performance in turn, takes measures relating to ROE, assets portfolio and defined risk measures.

Variable remuneration for senior staff has short term and long term components. The long term component is vested after 3 years from the date of granting. The vesting amount may increase or decrease according to the 3 year average performance in terms of EPS and risk measures. The Bank has only cash based variable remuneration and does not provide stock options or shares. Corporate performance targets have a ROE weight of 40%, asset portfolio performance of 30% and risk rating measure of 30%, as designed by E & Y consultants. All staff of the Bank is eligible for performance based variable incentives. Only senior management and staff, who are 20 in number, are eligible for long term variable incentives. There were no sign-on awards provided to any staff.

Senior Management is defined as the CEO and his executive team of three DCEOs. Reporting to the CEO, is the DCEO – Finance and Operations, the DCEO – Projects and Portfolios and DCEO – Finance and Investments. Material risk takers include the heads of revenue generating business departments which are Project Finance and Follow Up, Corporate Finance, Direct Investments, Treasury, Small Enterprise Finance and Agriculture finance. Included under the control functions is the Chief Risk Officer, Head of Internal Audit, Financial Control, Head of AML and the Compliance officer.

<u>Remuneration paid in 2014 (in KD)</u>

Category 1: 4 employees

Fixed

Unrestricted Cash-based	Deferred Cash-based	Unrestricted Other
462300	3892	6610

Variable

Unrestricted Cash-based	Deferred Cash-based	Unrestricted Other
	143180	

Category 2: 7 employees

Fixed

Unrestricted Cash-based	Deferred Cash-based	Unrestricted Other
369274	8127	7846

Variable

Unrestricted Cash-based	Deferred Cash-based	Unrestricted Other
	90333	

Category 3: 5 employees

Fixed

Unrestricted Cash-based	Deferred Cash-based	Unrestricted Other
199355	6197	4179

Variable

Unrestricted Cash-based	Deferred Cash-based	Unrestricted Other
	33795	