RISK AND CAPITAL MANAGEMENT

Basel III, Pillar 3 Disclosures

30th June 2017

EXECUTIVE SUMMARY

This Risk and Capital Management Disclosures encompass the qualitative and quantitative disclosures required by the Central Bank of Bahrain (CBB) in compliance with the Basel III guidelines.

The information presented herein pertains to Securities and Investment Company BSC (c) consolidated with its subsidiaries (together termed as "SICO" or the "Bank").

The report contains a description of the Bank's risk management and capital adequacy practices, including detailed information on the capital adequacy process.

The disclosures have been prepared in accordance with the Public Disclosure Module ("PD") of the CBB Rule Book, Volume I for Conventional Banks. These disclosures should be read in conjunction with the Notes, in particular the Significant Accounting Policies and Financial Risk Management, in the Bank's Consolidated Financial Statements for the same period.

These disclosures have been reviewed by the Bank's external auditors KPMG, based on agreed upon procedures as required under Para PD-A.2.4 of the PD Module.

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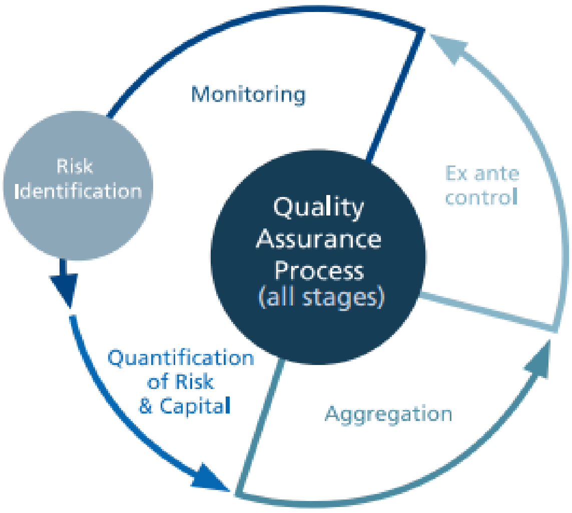
1. OVERVIEW AND STRUCTURE OF RISK MANAGEMENT

Risk management is the systematic process of identifying, assessing and mitigating the principal business risks to which SICO is exposed. Risk management is essential to the Bank's success, as risk is inherent in its activities, and risks are mitigated by establishing appropriate controls; and ensuring that effective monitoring and reporting processes are in place.

The major risks types to which SICO is exposed are:

- Credit risk
- Concentration risk
- Market risk
- Operational risk
- Liquidity risk
- Fiduciary risk
- Legal and Regulatory risk

The Bank maintains a strong focus on its risk management framework, capital management and risk governance structure; and adopts a structured, consistent and disciplined methodology to align business strategy, processes, people, technology and knowledge, in order to evaluate and manage its risks. The stages in the risk management process are as follows:



- **Risk identification:** Identification of the various risks that impact the various business activities of SICO.

- **Quantification of risks and capital coverage:** This step involves quantifying the risks identified in the risk identification process. It creates the objective basis for decision-making, and enables Senior Management to make decisions regarding SICO's risk-bearing capacity within the framework.

- **Aggregation:** Once risks have been identified and quantified, individual risks are aggregated to determine SICO's risk exposure and impact.

- **Ex ante control:** SICO has established various tolerance limits based on the overall risk strategy of the Bank. These limits are revised periodically, taking into account the changing market and economic conditions. SICO has established a comprehensive limit framework to monitor its exposure to all significant risks.

- **Risk monitoring and ex post control:** The risk monitoring process ensures that SICO's risk profile remains in line with its risk tolerance. In this context, there is a standardised procedure for dealing with increasing levels of limit utilisation and limit breaches.

The Bank also applies a rigorous framework of limits to control risk across multiple transactions, products, businesses and markets. This includes setting credit and market risk limits at a variety of levels, and monitoring these limits on a daily basis. Limits are typically set at levels that may be periodically exceeded, rather than at levels which reflect the Bank's maximum risk appetite.

2. RISK GOVERNANCE STRUCTURE

SICO has established a strong organizational structure including disciplined control functions to support the business strategy and risk management of the Bank.

SICO's Board and Senior Management are responsible for understanding the nature and level of risks faced by the Bank, and for ensuring that the risk management process chosen is appropriate, considering the risk profile of SICO. Senior Management are responsible for ensuring that there is a process to relate the business risk to an adequate level of capital; setting the tolerance for various risks, and putting in place the framework and process for measuring and monitoring compliance.

- **Board of Directors (BOD)**: The BOD is primarily responsible for approving the Bank's risk strategy, risk appetite, and risk policies to manage risks arising out of SICO's business activities. These policies are consistent with the Bank's broader business strategies, capital strength, management expertise, and ability to control risk.

- **Board Investment Committee (BIC)**: The BIC is the second point where decision making of SICO's investment activities is considered. This committee approves investments within its discretionary powers as delegated by the Board; and in some cases the BIC recommends proposals to the Board for its approval.
- **Audit Committee**: In addition to its overview of Internal Audit, the Audit Committee provides sound support to the compliance framework including regulatory and operational risk.
- **Nominations, Remuneration and Corporate Governance Committee (NRCGC):** The NRCGC contributes to the control framework by nominating qualified Board Members and key management positions. It also approves the remunerations which factor in the risk taken by the business, and oversees corporate governance-related issues.
- **Assets, Liabilities and Investment Committee (ALIC):** ALIC acts as the principal policy-making body responsible for overseeing the Bank's capital and financial resources. It is also responsible for managing the balance sheet and all proprietary investment activities, including investment strategy; and asset, country and industry/sector allocations. The committee is specifically responsible for managing the balance sheet risk; capital and dividend planning; forecasting; and monitoring interest rate risk positions, liquidity and funds management. The committee is also responsible for formulating and reviewing the Bank's investment policies (subject to approval by the Board), strategies, and performance measurement and assessment.
- **Assets Management Committee (AMC):** AMC is a management committee that oversees the fiduciary responsibilities carried out by Asset Management unit in managing clients' discretionary portfolios, as well as the funds operated and managed by SICO. It also reviews the investment strategy of the Bank's funds and portfolios; reviews asset allocations, subscription and redemptions, and adherence to client guidelines.
- **Internal Control Committee (ICC):** The ICC is a management committee that oversees the internal control functions carried out in SICO by various departments. The remit of ICC is to strengthen the internal control culture throughout the company.
- **Risk Management Department (RMD):** RMD is responsible for establishing a sound risk management framework to assist the Bank in the realisation of its business objectives. It also provides oversight of risk management and risk controls across the organisation by coordinating and communicating with each business unit to manage the risks that arise for its business activities; and ensure that the principles and requirements of managing risk are consistently adopted throughout the Bank.
- **Compliance Unit:** This is an independent unit within SICO that is responsible for internal compliance, regulatory compliance, and KYC & AML functions. It ensures compliance with internal and external rules and regulations, and is responsible for implementing the compliance framework across the entire Bank.
- **Internal Control Unit:** The unit is responsible to ensure the adequacy of internal control framework of the various business units of the bank and recommend changes wherever deemed. The unit is also responsible for ensuring that all policies and procedures are followed correctly.
- **Internal Audit:** This is an independent unit that provides an additional line of defence within the Bank's risk management and control framework. Internal Audit is primarily responsible for providing independent and objective assurance that the process for identifying, evaluating and managing significant risks faced by the Bank is appropriate and effectively applied by the business units, control functions and Senior Management.

3. CBB AND BASEL GUIDELINES

CBB Rulebook:

The Central Bank of Bahrain's (CBB) Basel III guidelines prescribe the capital adequacy framework for banks incorporated in the Kingdom of Bahrain. During 2014, the CBB introduced these guidelines and all banks in Bahrain were directed to comply with them.

This disclosure document has been prepared in accordance with the CBB requirements outlined in the Public Disclosure Module ("PD") which comes under Volume 1 (Conventional Banks) of the CBB Rulebook. This quantitative disclosure document follows the requirements of Basel III - Pillar 3.

BASEL III Framework:

Basel III is a comprehensive set of reform measures, developed by the Basel Committee on Banking Supervision, to strengthen the regulation, supervision and risk management of the banking sector.

Basel III measures aim to:

- Improve the banking sector's ability to absorb shocks arising from financial and economic stress, whatever the source
- Improve risk management and governance
- Strengthen banks' transparency and disclosures.

The Basel III Guidelines are based on the same three pillars of Basel II, with the introduction of additional liquidity requirements and capital buffers aimed at improving the ability of banks to withstand periods of economic and financial stress. The Basel III pillars are as follows:

- Pillar 1 - Describes the minimum capital requirements by applying risk-based methodology in the calculation of the risk weighted assets (RWAs) and capital requirement for the major asset classes to derive the capital adequacy ratio (CAR).
- Pillar 2 - Describes the supervisory review processes, which includes the Internal Capital Adequacy Assessment Process (ICAAP)
- Pillar 3 - Describes market discipline, which includes disclosure of the risk management process, and capital adequacy requirements and guidelines.

BASEL III		
Pillar 1	**Pillar 2**	**Pillar 3**
Minimum Capital Requirements	**Supervisory Review Process**	**Market Discipline**
Risk based capital requirements for: - Credit Risk - Market Risk - Operational Risk	**Regulatory Framework for Banks:** Internal Capital Adequacy Assessment Process (ICAAP) **Supervisory Framework:** Supervisory Review & Evaluation Process	**Disclosure requirement for banks:** - Specific quantitative and qualitative disclosures - Transparency for market participants concerning the bank's risk position (scope of application, risk management etc.) - Enhanced comparability of banks

Pillar 1

It lays down the basis for the calculation of the regulatory Capital Adequacy Ratio (CAR). Pillar 1 sets out the definition and calculations of the RWAs, and the derivation of the regulatory capital base. The capital adequacy ratio is calculated by dividing the regulatory capital base by the total RWAs.

Below are the approaches used for deriving the CAR.

Approaches for determining regulatory capital requirements		
Credit Risk	**Market Risk**	**Operational Risk**
Standardized Approach	Standardized Approach	Basic Indicator Approach
Foundation IRB Approach (Internal Ratings Based)	Internal Models Approach (IMA)	Standardized Approach
Advanced IRB Approach (Internal Ratings Based)		Advanced Measurement Approach (AMA)

SICO has adopted the Standardized Approach for Credit Risk and Market Risk, and follows the Basic Indicator Approach for Operational Risk to determine its capital requirements.

Pillar 2

It sets out the supervisory review and evaluation process of an institution's risk management framework, and accordingly its capital adequacy through ICAAP.

The supervisory review and evaluation process represents the CBB's review of the Bank's capital management, and an assessment of internal controls and corporate governance. The process is designed to ensure that institutions identify their material risks and allocate adequate capital, and employ sufficient management processes to support such risks. The process also encourages institutions to develop and apply enhanced risk management techniques for the measurement and monitoring of risks, in addition to the credit, market and operational risks addressed in the core Pillar 1 framework.

Other risk types which are not covered by the minimum capital requirements in Pillar 1 include liquidity risk, interest rate risk in the banking book, business risk and concentration risk. These are covered either by risk management processes under Pillar 2.

Pillar 2 also comprises an Internal Capital Adequacy Assessment Process (ICAAP). ICAAP incorporates a review and evaluation of risk management and capital relative to the risks to which the Bank is exposed. The ICAAP addresses all components of the Bank's risk management, from the daily management of more material risks to the strategic capital management of the Bank. The ICAAP is based on the Bank's economic capital framework, which is designed to ensure that SICO has sufficient capital resources available to meet regulatory and internal capital requirements, even during periods of economic or financial stress.

Pillar 3

It describes the level of qualitative and quantitative information that should be disclosed about an institution's risk management and capital adequacy practices.

Scope of Application

SICO is a conventional wholesale bank incorporated in Bahrain and regulated by the CBB. SICO provides financial services with a principal focus on the GCC. There is a regulatory requirement to calculate and maintain minimum regulatory capital ratios on both solo as well as consolidated basis.

The principal subsidiaries that are fully consolidated in the financial statements of SICO are SICO Funds Services Company BSC (c) ("SFS"), incorporated in Bahrain, and providing custody and fund administration services; and SICO UAE LLC (acquired September 2011), incorporated in Abu Dhabi and providing brokerage services in the UAE.

The adoption of IFRS 10 resulted in the Group also consolidating SICO Kingdom Equity Fund ("SKEF") and SICO Fixed Income Fund ("SFIF").

During 2016, SICO early adopted IFRS 9 accounting standards, which resulted in a change in the classification and measurement of eligible financial instruments as required under the standards.

4. CAPITAL STRUCTURE AND CAPITAL ADEQUACY

For the purpose of computing the regulatory capital adequacy ratio, the Bank applies the methodology and rules as defined in the CA Module of the CBB's Rule Book. The following also need to be considered:

a) The Bank's paid up capital consists only of ordinary shares which have proportionate voting rights, and the Bank does not have any other type of capital instruments.

b) The Bank's Tier 1 capital, which consists of Common Equity Tier 1, comprises share capital, share premium, reserves, retained earnings, unrealised losses arising from fair valuing equity securities classified as fair value through other comprehensive income and eligible reserves.

c) The Bank does not maintain any AT1 and Tier 2 capital components.

d) The Bank has prepared its capital structure in accordance with the CBB's Basel III capital adequacy framework

e) The Bank has no subsidiaries and/or investments that are required to be deducted from capital.

f) The Bank has no restrictions on the transfer of funds or regulatory capital within the Group, other than restrictions over transfers to ensure minimum regulatory capital requirements are met for subsidiary companies.

4.1 CAPITAL STRUCTURE

Common Equity Tier 1 (CET1)	
Issued and fully paid ordinary shares	42,849
Less: Employee stock incentive program funded by the bank (outstanding)	-1,599
General Reserve	3,217
Legal / Statutory reserves	5,969
Share Premium	692
Retained Earnings Brought forward	5,111
Current interim cumulative net income / losses	2,086
Securitization exposures subject to deduction	-
Accumulated other comprehensive income and losses	63
Total Common Equity Tier 1 Capital (A)	**58,388**
Other Capital (AT1 & Tier 2)	
Instruments issued by parent company	-
Instruments issued by banking subsidiaries to third parties	-
Share premium	-
Assets revaluation reserve - property, plant, and equipment	-
General loan loss provisions	-
Total AT1 & Tier 2 (B)	**-**
Total Available Capital (C) = (A) + (B)	**58,388**
Credit risk weighted exposures	62,074
Market risk weighted exposures	29,525
Operational risk weighted exposures	15,288
Total Risk weighted exposures (D)	**106,887**
CET1 Capital Ratio (A) / (D)	**54.63%**
Total Capital Adequacy Ratio (C) / (D)	**54.63%**

4.2 CAPITAL ADEQUACY RATIO
Consolidated & Subsidiaries above 5% of Group capital:

Subsidiaries	30 June 2017	
	Total Capital Adequacy Ratio	Tier 1 Capital Ratio
SICO Consolidated (Group)	54.63%	54.63%
SICO UAE*	5.60	2.06

** SICO UAE CAR has been computed using the capital charges as outlined in Emirates Securities and Commodities Authority (ESCA) regulations, wherein the minimum required ratio* is 1 with anything above 1.25 considered healthy.

4.3 REGULATORY CAPITAL DISCLOSURES

The capital reconciliation approach shows the link between the balance sheet in the published financial statements and the numbers that are used in the composition of capital disclosure.

For the three-step approach for reconciliation of regulatory capital, please refer to the relevant appendix as follows:

Appendix 1	Step 1: Balance sheet under the regulatory scope of consolidation
Appendix 2	Step 2: Reconciliation of published financial balance sheet to regulatory reporting
Appendix 3	Step 3: Composition of Capital Common Template (transition)
Appendix 4	Disclosure template for main features of regulatory capital instruments

5. CREDIT RISK

Credit risk is the potential for financial loss resulting from the failure of a borrower or counterparty to honour its financial or contractual obligations. The Bank's exposure to credit risk comes mostly from:

- Cash placed with banks and financial institutions
- Investment in Fixed Income instruments
- Overdrafts (brokerage clients)
- Receivables from brokers
- Securities financing transactions (i.e. REPO and Reverse REPO)
- Margin Trading Facilities

Risk Management works in coordination with the business units in identifying and aggregating credit exposures. Credit risk also encompasses the following risks to which SICO is exposed, and are being effectively managed as a part of the Credit Risk Management strategy:

Counterparty Risk: SICO deals with different counterparties for its money market placements, brokerage and REPO activities. To measure counterparty risk, SICO employs an internal rating model to assign ratings to each of its counterparty by applying qualitative and quantitative factors and has a limits framework to manage counterparty risk.

Settlement Risk: SICO is exposed to settlement risk through its brokerage services on unfunded deals where exposure remains until settlement. SICO applies several assessments against its clients during the screening and on a subsequent basis to minimize settlement risk. SICO manages settlement risk through setting settlement limits to counterparties based their credit profile and by monitoring settlement exposures.

Default Risk: As part of SICO's Margin Trading facilities and Reverse REPO, it is exposed to the risk of default wherein individuals and corporates may be unable to make the required payments on their obligations. SICO accepts only liquid securities as collateral, and also apply haircuts on the collateral value, which acts as a margin of safety in case it is to offset the collateral against the outstanding obligations. Moreover, SICO employs margin calls to ensure collateral coverage does not drop below the agreed parameters.

For the measurement of the above credit risk components, SICO employs several methodologies for mitigating the credit risk. SICO also uses ratings issued by external credit assessment institutions (ECAIs) such as Standard & Poor's, Moody's and Fitch, to derive the risk weightings under the CBB's Basel III capital adequacy framework and as part of its internal rating model. These ratings are used mainly for banks and financial institutions, but also where applicable, for other exposures such as debt instruments. Where ratings vary between rating agencies, the more conservative rating is adopted.

Credit risk is monitored and controlled by policies and procedures that are put in place by RMD, and that have been approved by the Management and the Board where required. The policy framework establishes approval authorities, concentration limits, risk-rating methodologies, and guidelines for management of exposures. For lending exposures such as Margin Trading and Reverse REPO, financial securities that are obtained as collateral are liquid in nature, and appropriate haircuts are also applied on them. The lending exposures are closely monitored along with their collaterals, which are marked to market on a daily basis and margin calls are enforced where collateral coverage drops below the required level. The Bank also adheres strictly to the large exposure norms as prescribed by the Central Bank of Bahrain under the Credit Risk Management Module.

5.1 Gross credit exposures

As at 30th June 2017	Gross credit exposure			Credit Risk Weighted Assets	Capital requirement @ 12%
	On-balance sheet (Funded)	Off-balance sheet (Unfunded)	TOTAL		
Claims on sovereigns	22,495	-	22,495	-	-
Claims on Bahraini PSE	500	-	500	-	-
Claims on banks	65,892	-	65,892	33,483	4,018
Claims on corporates	15,025	-	15,025	8,154	978
Regulatory retail portfolios	6,132	-	6,132	1,820	218
Investments in securities	8,231	-	8,231	10,801	1,296
Holdings in real estate	2,261	-	2,261	4,522	543
Other assets	3,294	-	3,294	3,294	395
TOTAL	**123,830**	**-**	**123,830**	**62,074**	**7,448**

The on-balance sheet and off-balance sheet gross exposures have been risk weighted using the applicable risk weights and CCF's (credit conversion factors) as per CBB guidelines.

The balances above are representative of the position during the period; hence the average balances for the year are not separately disclosed.

5.2 Maturity Profile

As at 30th June 2017	Less than 1 year	Over 1 year to 5 years	Above 5 Years	Total
Cash and Bank balances	24,275	-	-	**24,275**
Call deposits	1,008	-	-	**1,008**
Placements with banks	61,518	-	-	**61,518**
Treasury bills	4,420	-	-	**4,420**
FVTPL investments	-	6,577	18,197	**24,774**
FVOCI investments	113	-	5,534	**5,647**
Investments at amortized cost	-	-	8,875	**8,875**
Fees receivable	767	-	-	**767**
Other assets	10,127	-	-	**10,127**
Total assets	**102,228**	**6,577**	**32,606**	**141,411**
Commitments	**3,270**	**-**	**-**	**3,270**
Contingencies	**5,133**	**-**	**-**	**5,133**

Note: *Commitments and contingencies mentioned above do not have a defined maturity and hence conservatively considered less than 1 year.*

5.3 Sectoral distribution

As at 30th June 2017	Financial	Sovereign	Diversified Funds	Real Estate	Others	Total
Cash and Bank balances	75,632	8,616	-	-	2,553	**86,801**
Treasury bills	-	4,420	-	-	-	**4,420**
FVTPL investments	7,967	898	6,167	6,062	3,680	**24,774**
FVOCI investments	4,715	-	-	656	276	**5,647**
Investments at amortized cost	-	8,875	-	-	-	**8,875**
Fees receivables	-	-	-	-	767	**767**
Other assets	-	-	-	-	10,127	**10,127**
Total assets	**88,314**	**22,809**	**6,167**	**6,718**	**17,403**	**141,411**

5.4 Geographical distribution

As at 30th June 2017	Middle East and Asia	North America	Europe	Total
Cash and Bank balances	81,074	-	5,727	86,801
Treasury bills	4,420	-	-	4,420
FVTPL investments	19,944	4,830	-	24,774
FVOCI investments	5,647	-	-	5,647
Investments at amortized cost	8,875	-	-	8,875
Fees receivables	767	-	-	767
Other assets	10,127	-	-	10,127
Total assets	**130,854**	**4,830**	**5,727**	**141,411**

5.5 Large exposure limits

As at **30th June 2017**, the below exposures were in excess of the 15% large exposure limit as defined in the CM Module of the CBB's rule book.

Counterparty	Country	Amount	Exposure as a % to eligible capital base
Central Bank Of Bahrain	Bahrain	12,483	21.38%
Ahli United Bank	Bahrain	10,906	18.68%
Al Salam Bank	Bahrain	9,461	16.20%
Bahrain Islamic Bank	Bahrain	9,151	15.67%

6. MARKET RISK

Market risk is the risk of loss in the value of any financial instrument due to an adverse fluctuation in equity prices, interest rates and foreign exchange rates, whether arising out of factors affecting specific instruments or the market in general.

The Bank's exposure to market risk primarily comes from its investment and trading activities that are conducted by its Investment unit. The Bank invests and trades across different products, such as equities and fixed income, and through different types of funds in regional and international markets.

Market risk is controlled and mitigated primarily through a series of different layers of limits and maintaining a dynamic investment allocation. These limits reflect the Bank's risk appetite in the context of the market environment and business strategy. In setting limits, the Bank takes into consideration many factors, including market volatility, product liquidity and risk appetite.

These limits adhered to by the Investments team and are also monitored independently by RMD. Market risk is monitored and also controlled by policies and procedures that are put in place and practiced across the Bank. The policy framework establishes and clearly defines the approval authorities and portfolio review parameters.

Market risk encompasses the following risks to which SICO is exposed, and are being effectively managed as a part of the Market Risk Management strategy:

- **Equity Price Risk**
- **Interest Rate Risk**
- **Currency Risk**

The market risk weighted assets and the capital requirement is computed as follows:

	Market Risk Weighted Assets			Capital Requirement @ 12%
	During the Year to date period		As at	
	Minimum	Maximum	30-Jun-17	
Interest Rate Position Risk	1,088	1,273	1,273	153
Equities Position Risk	952	1,052	952	114
Foreign Exchange Risk	125	137	137	16
Total min capital required for market risk			**2,362**	**283**
Multiplier			12.5	12.5
TOTAL			**29,525**	**3,543**

6.1 Equity Price Risk

A significant portion of the Bank's proprietary portfolio comprises equity instruments which are affected by equity price risk. Uncertain conditions in the equity markets are carefully considered by rebalancing asset allocations to minimise risk exposures. This risk is also mitigated by managing the portfolio within duly approved investment guidelines and other investment limits. These are closely monitored by RMD, and regularly reviewed by ALIC.

SICO's risk management approach continues to be forward-looking, proactive, and highly effective in rebalancing its investment portfolio in line with the Bank's investment strategy, to ensure capital preservation, quality and liquidity.

Equity Positions in the Banking Book

	Gross Exposure	Risk Weighted Assets	Capital requirement @ 12%
Equity investments			
- Listed	3,054	3,054	366
- Unlisted	-	-	-
Investment in rated funds	-	-	-
Investment in unrated funds - Listed/Unlisted	6,167	8,737	1,048
TOTAL	**9,221**	**11,791**	**1,414**

6.2 Interest Rate Risk

Interest rate risk is the risk where changes in market interest rates might adversely affect the Bank's financial condition. Investments in debt instruments, placements, deposits and borrowings give rise to interest rate risk. The Investments and Treasury team monitors and manages these exposures in order to mitigate this risk.
A reasonable spread is maintained between money market placements and deposit interest rates. Treasury assets and liabilities are maintained in closely matching maturity buckets in highly liquid short-term money market vehicles to avoid any material mismatch. Moreover, SICO does not trade speculatively in derivatives.

Bank placements are mostly short term (less than 3 months) with a fixed interest rate and are subject to re-pricing risk at rollover. Investments in bonds are subject to interest rate risk and the Bank controls the same by managing the portfolio duration by combining floaters and short duration bonds along with longer duration ones.

6.2(a) Interest Rate Risk Sensitive Assets and Liabilities:

As at 30th June 2017	Effective Interest rate% p.a.	Within 1 year	Over 1 year	Non-interest sensitive	Total
Cash and Bank balances	-	-	-	24,274	24,274
Call deposits	-	1,008	-	-	1,008
Placements with banks	1.95%	61,519	-	-	61,519
Treasury bills	2.10%	4,420	-	-	4,420
FVTPL investments	6.62%	-	11,756	13,018	24,774
FVTOCI investments	4.09%	113	2,109	3,425	5,647
Investments at amortized cost	6.23%		8,875	-	8,875
Furniture, equipment and intangibles	-	-	-	1,510	1,510
Fees receivable	-	-	-	767	767
Other assets	-	-	-	8,617	8,617
Total Assets		**67,060**	**22,740**	**51,611**	**141,411**
Short term borrowings*	1.16%	38,059	-	-	38,059
Customer accounts	-	-	-	39,173	39,173
Other liabilities	-	-	-	3,099	3,099
Payables to unit holders	-	-	-	2,692	2,692
Total Liabilities	-	***38,059***	-	***44,964***	***83,023***
Total Equity	-	-	-	***58,388***	***58,388***
Total Liability and Equity		**38,059**	**-**	**103,352**	**141,411**
Interest rate sensitivity Gap		*29,001*	*22,740*	*-51,741*	
Cumulative Interest rate sensitivity gap		**29,001**	**22,740**	**-**	

**Short term borrowings have fixed interest rate for the tenor and are subject to interest rate risk only at rollover.*

6.2(b) Interest Rate Risk in the Banking Book

A 100 bps and 50 bps increase in market interest rates would affect the value of the fixed rate debt instruments in the FVOCI book as follows:

100 bps increase	50 bps increase
614.4	**307.2**

The interest rate risk on the Bank's placements and short-term borrowings is considered minimal, and hence no sensitivity analysis has been presented.

6.3 Currency Risk

A substantial portion of SICO's business is transacted in Bahraini Dinar, GCC currencies and United States Dollar. The Bank's exposure to other foreign currencies is insignificant and hence the foreign exchange risk is low. Foreign exchange rate risk is managed by applying appropriate limits that are set in accordance with the Bank's strategic plans and risk tolerance, determined by ALIC and approved by the Board of Directors. Treasury manages these positions on an ongoing basis, hedging such exposures as appropriate, while RMD along with ALIC regularly reviews such positions.

7. OPERATIONAL RISK

Operational risk is the risk of loss resulting from inadequate or failed internal processes, systems or human factors, or from external events. Unlike market or credit risks which are systemic in nature, operational risk is institution-specific and is inherent in the day-to-day operations of the Bank. This risk could arise from a broad spectrum of causes such as deficient transaction processing, business practices, workplace practices, system failures, human errors, business interruptions and damage to physical assets. Operational risk also includes internal and external fraud.

Operational risk also encompasses other risks and areas like:
- **Reputational Risk**
- **Legal Risk**

The Bank has in place sound internal control measures, consisting of operating policies and procedures framework, compliance initiatives, and adequate and skilled personnel, which are the key to successful operational risk management. The Bank has a very conservative control philosophy, and adopts a number of mechanisms to manage this risk. These include a well-defined organisational structure, approved policies and procedures guidelines, segregation of duties, approval authorities, periodical reconciliations, and various limits. Internal Control, Compliance and Internal Audit functions support this activity.

The operational risk weighted assets are computed as per the guidelines of the CBB, which are as follows:

Average gross income for the past 3 years (excluding extraordinary and exceptional income)

	2014	2015	2016
Gross income	10,284	6,495	7,673
Average gross income (A)			8,151
Alpha (B)			15%
(C) = (A) * (B)			1,223
Risk weighted exposures (D) = (C) * 12.5			**15,283**
Capital requirement @ 12% of (D)			**1,834**

8. OTHER RISKS

8.1 Concentration Risk

Concentration risk arises when the Bank's exposure is concentrated with one or more related counterparties, assets classes, sectors, or geographies. Weakness in the counterparty or assets, sector, or country may place SICO under considerable risk and potential loss.

The Bank complies strictly with the large exposure norms prescribed by the CBB in the CM Module of the CBB's rule book.

The Bank continues its effort to maintain an acceptable level of concentration by adhering to the limits set as per the Investment guidelines.

8.2 Liquidity Risk

Liquidity risk is the inability to meet contractual and contingent financial obligations, on- or off-balance sheet, as they come due, as a result of the potential inability to liquidate financial assets at the required time and price, in order to cope with a pay out of liabilities or investment obligations in assets. Such risks may arise from a depletion of cash and cash equivalents, investments turning illiquid, and mismatches in the maturity pattern of assets and liabilities. Measuring and managing liquidity needs are vital for the effective operation of investment banks.

The Bank's Treasury unit manages this risk by monitoring settlement obligations and maintaining sufficient liquid assets, including call deposits and short-term placements. The Bank's liquidity position is monitored on a daily basis, and maturity mismatches of Bank's maturity profile are also monitored and reported to the Board periodically. Moreover, SICO's liquidity risk is low as its assets are very liquid and also has a high proportion of its assets in cash equivalents.

8.3 Fiduciary Risks

Fiduciary risk is defined as the risk that monies entrusted to a financial institution through funds or trusts or agency accounts are (i) not properly managed, (ii) not used for the intended purposes; (iii) not properly recorded and accounted for; and (iv) do not achieve the value-for-money objectives.

The RMD carries out risk assessment on the various fiduciary activities of the Bank by working alongside with the Bank's relevant lines of business and committees, to ensure that SICO fulfills its fiduciary duties against the asset management, fund administration and custody clients, wherein it adopts the appropriate standards relative to the fiduciary relationship with clients. Below are the various activities carried out by SICO and the Bank's subsidiary, SICO Funds Services Company (SFS), which can give rise to the following fiduciary risks:

Asset Management: The Bank has a range of controls to support the quality of the investment process, supervised by the Asset Management Committee (AMC). There are operating policies and procedures, and Investment Guidelines, coupled with dedicated buy-side research and other guidelines, to support this activity. There are also strict operational controls to protect clients' assets, staff code of conduct policy and 'Chinese Walls' to avoid any conflicts of interest.

RMD and Compliance regularly monitor the activities of the Asset Management division, and report their findings and observations to the AMC, and in the periodic compliance reports sent to clients.

Custody and Fund Administration: The Bank's custody and fund administration activities are handled by SICO Funds Services Company (SFS), which operates as a standalone subsidiary. SFS has put in place a number of operating controls, including the monitoring and reporting of securities position reconciliations.

Corporate Finance: This activity is subject to legal and reputation risk. Such risks are mitigated by obtaining the necessary legal and regulatory approvals. Advisory and underwriting matters are monitored and controlled by Senior Management.

8.4 Business Continuity

SICO has in place business continuity plans (BCPs) to ensure the Bank's business operations and functions are carried out in case of any disturbance or unexpected events affecting business operations. The BCP provides each business line with the necessary guidelines and procedures in case of an emergency or disaster. The Bank has established a business continuity centre at a different location within the Kingdom of Bahrain, which maintains a full operational status and is capable of carrying out majority of the Bank's operational activities. The effectiveness of the business continuity centre has been tested by conducting actual business from the BCP site as required.

8.5 Compliance Risk

Compliance risk is risk of current and prospective risk to earnings or capital arising from violation of, or non-compliance with, laws, regulations, rules, prescribed practices, contractual agreements or ethical standards. Compliance risk can lead to diminished reputation, limited business opportunities, reduced expansion potential, and even to cessation of operations. The Bank ensures adherence to all applicable regulations provided by various regulatory authorities, including regulations by CBB and Bahrain Bourse. In addition, the Bank's internal policies ensure that its practices are in line with best market practices, which helps in managing Compliance risks.

APPENDIX 1

Step 1: Balance sheet under the regulatory scope of consolidation.

This step in not applicable to the Bank since there is no difference between the regulatory consolidation and the accounting consolidation, as they are identical.

APPENDIX 2

Step 2: Reconciliation of published financial balance sheet to regulatory reporting.

	Published financial statements	Consolidated PIR data
	30-Jun-17	30-Jun-17
Assets	BD '000	BD '000
Cash and cash equivalents	86,801	
of which Cash and balances at central banks		29,703
of which Placements with banks and financial institutions		57,098
Treasury bills	4,420	
of which other assets		4,420
Investments at fair value through profit and loss	24,774	24,774
Investments at fair value through other comprehensive income	5,647	5,647
Furniture, equipment and intangibles	1,510	
of which intangibles (computer software)		953
of which furniture and equipment		557
Fees receivable	767	
of which other assets		767
Other assets	17,492	
of which loans and advances (margin receivables)		6,132
of which interest receivable		483
of which other assets		10,877
Total assets	**141,411**	**141,411**
Liabilities		
Short-term bank borrowings	38,059	
of which amounts relating to repo transactions		33,474
of which other short-term borrowings		4,585
Customer liabilities	39,173	
of which other liabilities		39,173
Other liabilities	3,099	
of which Interest payable		22
of which other liabilities		3,077
Payable to other unit holders (Other liabilities)	2,692	2,692
Total liabilities	**83,023**	**83,023**
Shareholders' Equity		
Share Capital - eligible for CET1	42,849	42,849
Shares under employee share incentive scheme	(1,599)	(1,599)
Statutory reserve	6,661	
of which share premium		692
of which legal reserve		5,969
General reserve	3,217	3,217
Investments fair value reserve	63	
of which unrealized gains from fair valuing equities		19
of which unrealized gains from other financial instruments		44
Retained earnings	7,197	
of which retained earnings brought forward from previous year		5,111
of which net profits for the current period		2,086
Total shareholder' equity	**58,388**	**58,388**
Total liabilities and equity	**141,411**	**141,411**

APPENDIX 3

Step 3: Composition of Capital Common Template (transition)

	Composition of Capital and mapping to regulatory reports	Component of regulatory capital (BD '000s)	Amounts subject to pre-2015 treatment	Source based on reference no. of the balance sheet under the regulatory scope of consolidation from step 2
	Common Equity Tier 1 capital: instruments and reserves			
1	Directly issued qualifying common share capital (and equivalent for non-joint stock companies) plus related stock surplus	42,849		
2	Retained earnings	5,111		
3	Accumulated other comprehensive income (and other reserves)	10,428		
4	Not Applicable	-		
5	Common share capital issued by subsidiaries and held by third parties (amount allowed in group CET1)	-		
6	**Common Equity Tier 1 capital before regulatory adjustments**	**58,388**		
	Common Equity Tier 1 capital: regulatory adjustments			
7	Prudential valuation adjustments	-		
8	Goodwill (net of related tax liability)	-		
9	Other intangibles other than mortgage-servicing rights (net of related tax liability)	-		
10	Deferred tax assets that rely on future profitability excluding those arising from temporary differences (net of related tax liability)	-		
11	Cash-flow hedge reserve	-		
12	Shortfall of provisions to expected losses	-		
13	Securitization gain on sale (as set out in paragraph 562 of Basel II framework)	-		
14	Not applicable.	-		
15	Defined-benefit pension fund net assets	-		
16	Investments in own shares (if not already netted off paid-in capital on reported balance sheet)	-		
17	Reciprocal cross-holdings in common equity	-		
18	Investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions, where the bank does not own more than 10% of the issued share capital (amount above 10% threshold)	-		
19	Significant investments in the common stock of banking, financial and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions (amount above 10% threshold)	-		
20	Mortgage servicing rights (amount above 10% threshold)	-		
21	Deferred tax assets arising from temporary differences (amount above 10% threshold, net of related tax liability)	-		
22	Amount exceeding the 15% threshold	-		
23	of which: significant investments in the common stock of financials	-		
24	of which: mortgage servicing rights	-		
25	of which: deferred tax assets arising from temporary differences	-		
26	National specific regulatory adjustments	-		
	REGULATORY ADJUSTMENTS APPLIED TO COMMON EQUITY TIER 1 IN RESPECT OF AMOUNTS SUBJECT TO PRE-2015 TREATMENT	-		
27	Regulatory adjustments applied to Common Equity Tier 1 due to insufficient Additional Tier 1 and Tier 2 to cover deductions	-		
28	**Total regulatory adjustments to Common equity Tier 1**	-		
29	**Common Equity Tier 1 capital (CET1)**	**58,388**		
	Additional Tier 1 capital: instruments			
30	Directly issued qualifying Additional Tier 1 instruments plus related stock surplus	-		

31	of which: classified as equity under applicable accounting standards	-
32	of which: classified as liabilities under applicable accounting standards	-
33	Directly issued capital instruments subject to phase out from Additional Tier 1	-
34	Additional Tier 1 instruments (and CET1 instruments not included in row 5) issued by subsidiaries and held by third parties (amount allowed in group AT1)	-
35	of which: instruments issued by subsidiaries subject to phase out	-
36	Additional Tier 1 capital before regulatory adjustments	-
	Additional Tier 1 capital: regulatory adjustments	
37	Investments in own Additional Tier 1 instruments	-
38	Reciprocal cross-holdings in Additional Tier 1 instruments	-
39	Investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions, where the bank does not own more than 10% of the issued common share capital of the entity (amount above 10% threshold)	-
40	Significant investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation (net of eligible short positions)	-
41	National specific regulatory adjustments	-
	REGULATORY ADJUSTMENTS APPLIED TO ADDITIONAL TIER 1 IN RESPECT OF AMOUNTS SUBJECT TO PRE-2015 TREATMENT	-
	OF WHICH: [INSERT NAME OF ADJUSTMENT]	-
	OF WHICH: …	-
42	Regulatory adjustments applied to Additional Tier 1 due to insufficient Tier 2 to cover deductions	-
43	Total regulatory adjustments to Additional Tier 1 capital	-
44	**Additional Tier 1 capital (AT1)**	**-**
45	**Tier 1 capital (T1 = CET1 + AT1)**	**58,388**
	Tier 2 capital: instruments and provisions	
46	Directly issued qualifying Tier 2 instruments plus related stock surplus	-
47	Directly issued capital instruments subject to phase out from Tier 2	-
48	Tier 2 instruments (and CET1 and AT1 instruments not included in rows 5 or 34) issued by subsidiaries and held by third parties (amount allowed in group Tier 2)	-
49	of which: instruments issued by subsidiaries subject to phase out	-
50	Provisions	-
51	Tier 2 capital before regulatory adjustments	-
	Tier 2 capital: regulatory adjustments	
52	Investments in own Tier 2 instruments	-
53	Reciprocal cross-holdings in Tier 2 instruments	-
54	Investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions, where the bank does not own more than 10% of the issued common share capital of the entity (amount above the 10% threshold)	-
55	Significant investments in the capital banking, financial and insurance entities that are outside the scope of regulatory consolidation (net of eligible short positions)	-
56	National specific regulatory adjustments	-
57	**Total regulatory adjustments to Tier 2 capital**	**-**
58	**Tier 2 capital (T2)**	**-**
59	**Total capital (TC = T1 + T2)**	**58,388**
	RISK WEIGHTED ASSETS IN RESPECT OF AMOUNTS SUBJECT TO PRE-2015 TREATMENT	-
	OF WHICH: Significant investments in the common stock of banking, financial and insurance entities that are outside the scope of regulatory consolidation, net of eligible	-
60	**Total risk weighted assets**	**106,887**

	Capital ratios	
61	**Common Equity Tier 1 (as a percentage of risk weighted assets)**	**54.63%**
62	**Tier 1 (as a percentage of risk weighted assets)**	**54.63%**
63	**Total capital (as a percentage of risk weighted assets)**	**54.63%**
64	Institution specific buffer requirement (minimum CET1 requirement plus capital conservation buffer plus countercyclical buffer requirements plus D-SIB buffer requirement expressed as a percentage of risk weighted assets)	9%
65	of which: capital conservation buffer requirement	2.5%
66	of which: bank specific countercyclical buffer requirement (N/A)	0%
67	of which: D-SIB buffer requirement (N/A)	0%
68	**Common Equity Tier 1 available to meet buffers (as a percentage of risk weighted assets)**	**54.63%**
	National minima including CCB (if different from Basel 3)	
69	CBB Common Equity Tier 1 minimum ratio	9%
70	CBB Tier 1 minimum ratio	10.5%
71	CBB total capital minimum ratio	12.5%
	Amounts below the thresholds for deduction (before risk weighting)	
72	Non-significant investments in the capital of other financials	-
73	Significant investments in the common stock of financials	-
74	Mortgage servicing rights (net of related tax liability)	-
75	Deferred tax assets arising from temporary differences (net of related tax liability)	-
	Applicable caps on the inclusion of provisions in Tier 2	
76	Provisions eligible for inclusion in Tier 2 in respect of exposures subject to standardized approach (prior to application of cap)	-
77	Cap on inclusion of provisions in Tier 2 under standardized approach (1.25% of Credit Risk weighted Assets)	-
78	NA	-
79	NA	-
	Capital instruments subject to phase-out arrangements (only applicable between 1 Jan 2020 and 1 Jan 2024)	
80	Current cap on CET1 instruments subject to phase out arrangements	-
81	Amount excluded from CET1 due to cap (excess over cap after redemptions and maturities)	-
82	Current cap on AT1 instruments subject to phase out arrangements	-
83	Amount excluded from AT1 due to cap (excess over cap after redemptions and maturities)	-
84	Current cap on T2 instruments subject to phase out arrangements	-
85	Amount excluded from T2 due to cap (excess over cap after redemptions and maturities	-

APPENDIX 4

Disclosure template for main feature of regulatory capital instruments

Disclosure template for main features of regulatory capital instruments		
1	Issuer	SICO
2	Unique identifier (e.g. CUSIP, ISIN or Bloomberg identifier for private	SICO BI EQUITY
	placement)	
3	Governing law(s) of the instrument	Commercial Companies Law, Bahrain
	Regulatory treatment	
4	Transitional CBB rules	NA
5	Post-transitional CBB rules	NA
6	Eligible at solo/group/group & solo	Yes
7	Instrument type (types to be specified by each jurisdiction)	Common shares
8	Amount recognized in regulatory capital (Currency in mil, as of most recent reporting date)	BD 41.25 million
9	Par value of instrument	100 fils per share
10	Accounting classification	Shareholders' equity
11	Original date of issuance	1995
12	Perpetual or dated	NA
13	Original maturity date	NA
14	Issuer call subject to prior supervisory approval	NA
15	Optional call date, contingent call dates and redemption amount	NA
16	Subsequent call dates, if applicable	NA
	Coupons / dividends	
17	Fixed or floating dividend/coupon	NA
18	Coupon rate and any related index	NA
19	Existence of a dividend stopper	NA
20	Fully discretionary, partially discretionary or mandatory	NA
21	Existence of step up or other incentive to redeem	NA
22	Noncumulative or cumulative	NA
23	Convertible or non-convertible	NA
24	If convertible, conversion trigger (s)	NA
25	If convertible, fully or partially	NA
26	If convertible, conversion rate	NA
27	If convertible, mandatory or optional conversion	NA
28	If convertible, specify instrument type convertible into	NA
29	If convertible, specify issuer of instrument it converts into	NA
30	Write-down feature	NA
31	If write-down, write-down trigger(s)	NA
32	If write-down, full or partial	NA
33	If write-down, permanent or temporary	NA
34	If temporary write-down, description of write-up mechanism	NA
35	Position in subordination hierarchy in liquidation (specify instrument type	NA
	immediately senior to instrument)	NA
36	Non-compliant transitioned features	NA
37	If yes, specify non-compliant features	NA