REPORT ON THE AUDIT OF THE CONSOLIDATED FINANCIAL STATEMENTS

Opinion
We have audited the accompanying consolidated financial statements of BBK B.S.C. ("the Bank") and its subsidiaries (together "the Group"), which comprise the consolidated statement of financial position as at 31 December 2016, and the consolidated statements of profit or loss, other comprehensive income, changes in equity and cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2016, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards ("IFRS").

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

Key audit matters
Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements for the year ended 31 December 2016. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. For each matter below, our description of how our audit addressed the matter is provided in that context.

We have fulfilled the responsibilities described in the Auditor's responsibilities for the audit of the consolidated financial statements section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the consolidated financial statements. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying consolidated financial statements.

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<tr>
<th>Key audit matter</th>
<th>How the key audit matter was addressed in the audit</th>
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<tr>
<td><strong>1. Impairment of carrying value of loans and advances</strong></td>
<td>• We gained understanding of the Group’s key credit processes comprising granting, booking, monitoring and provisioning and tested the operating effectiveness of key controls over these processes;</td>
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<td>• For exposures determined to be individually impaired, we tested a sample of loans and advances and examined management’s estimate of future cash flows, assessed their reasonableness and checked the resultant provision calculations; and</td>
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<td>• For provision against exposures classified as Stage 1 and Stage 2 on early adoption of IFRS 9, we obtained an understanding of the Group’s provisioning methodology, assessed the reasonableness of the underlying assumptions and the sufficiency of the data used by the management. Our procedures in this regard are discussed in further detail below under the key audit matter &quot;Early adoption of IFRS 9&quot;.</td>
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<td><strong>2. Early adoption of IFRS 9</strong></td>
<td>With respect to classification and measurement of financial assets and financial liabilities, our audit procedures comprised the following:</td>
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<td>• We read the Group’s IFRS 9 based classification and measurement of financial assets and financial liabilities policy and compared it with the requirements of IFRS 9;</td>
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<td>• We obtained an understanding and checked the Group’s business model assessment and the test on the contractual cash flows, which give rise to cash flows that are ‘solely payments of principal and interest’ [SPPI test] performed by the Group’s consultant; and</td>
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<td>• We checked the appropriateness of the opening balance adjustments.</td>
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With respect to impairment methodology, our audit procedures comprised the following:

• We read the Group’s IFRS 9 based impairment provisioning policy and compared it with the requirements of IFRS 9;

• We obtained an understanding of the Group’s internal rating models for loans and advances and read the rating validation report prepared by the Group’s consultant to gain comfort that the discrimination and calibration of the rating model is appropriate. Further, we performed procedures to ensure the competence, objectivity and independence of the Group’s consultant;
REPORT ON THE AUDIT OF THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

Key audit matters (continued)

2. Early adoption of IFRS 9 (continued)

The key changes arising from early adoption of IFRS 9 are that the Group's credit losses are now based on expected losses rather than an incurred loss model, and the change in the classification and measurement of the Group's financial assets and liabilities, which are detailed in note 3 to the consolidated financial statements. There were no significant changes arising from the early adoption of the hedge accounting requirements of IFRS 9.

- We checked the appropriateness of the Group's determination of significant increase in credit risk and the resultant basis for classification of exposures into various stages;
- For a sample of exposures, we checked the appropriateness of the Group's staging;
- We checked and understood the key data sources and assumptions for data used in the Expected Credit Loss (ECL) models (the Models) used by the Group to determine impairment provisions;
- For forward looking assumptions used by the Group's management in its ECL calculations, we held discussions with management and corroborated the assumptions using publicly available information;
- For a sample of exposures, we checked the appropriateness of determining Exposure at Default, including the consideration of prepayments and repayments in the cash flows and the resultant arithmetical calculations;
- For Probability of Default (PD) used in the ECL calculations we checked the Through the Cycle (TTC) PDs calculation and checked the appropriateness of conversion of the TTC PDs to point in time (PIT) PDs;
- We checked the calculation of the Loss Given Default (LGD) used by the Group in the ECL calculations, including the appropriateness of the use of collateral and the resultant arithmetical calculations;
- We checked the completeness of loans and advances, off balance sheet items, investment securities, placements and other financial assets included in the ECL calculations as of 31 December 2016; we understood the theoretical soundness and tested the mathematical integrity of the Models;
- Where relevant, we used Information System specialists to gain comfort on data integrity;
- We checked consistency of various inputs and assumptions used by the Group's management to determine impairment provisions; and
- We checked the appropriateness of the opening balance adjustments.

With respect to hedge accounting, we read the Group's IFRS 9 based policy and compared it with the requirements of IFRS 9, further we have checked the appropriateness of the policy implementation.

We assessed the financial statement disclosures arising on early adoption of IFRS 9 to determine if they were in accordance with the requirements of the Standard. Refer to the accounting policies, critical accounting estimates and judgements, disclosures of loans and advances and credit risk management in notes 3, 7 and 32 to the consolidated financial statements.

Other information included in the Group’s 2016 annual report

Other information consists of the information included in the Group’s 2016 Annual Report, other than the consolidated financial statements and our auditor’s report thereon. The Board of Directors is responsible for the other information. Prior to the date of this auditor’s report, we obtained the Board of Directors’ report, which will form part of the annual report, and the remaining sections of the annual report are expected to be made available to us after that date.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon. In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above when it becomes available and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed on the other information obtained prior to the date of the auditor’s report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.
Responsibilities of the Board of Directors for the consolidated financial statements.

The Board of Directors is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRS and for such internal control as the Board of Directors determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

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

Auditors’ Responsibilities for the audit of the consolidated financial statements

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

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

• Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion.
• The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
• Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group’s internal control
• Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Board of Directors.
• Conclude on the appropriateness of the Board of Directors’ use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group’s ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor’s report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor’s report. However, future events or conditions may cause the Group to cease to continue as a going concern.
• Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
• Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

We communicate with the Group’s Audit Committee regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the Group’s Audit Committee with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

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

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

As required by the Bahrain Commercial Companies Law and Volume 1 of the Central Bank of Bahrain (CBB) Rule Book, we report that:

a) the Bank has maintained proper accounting records and the consolidated financial statements are in agreement therewith;
b) the financial information contained in the Board of Directors’ report is consistent with the consolidated financial statements;
c) we are not aware of any violations of the Bahrain Commercial Companies Law, the Central Bank of Bahrain and Financial Institutions Law, the CBB Rule Book (Volume 1 and applicable provisions of Volume 6) and CBB directives, regulations and associated resolutions, rules and procedures of the Bahrain Bourse or the terms of the Bank’s memorandum and articles of association during the year ended 31 December 2016 that might have had a material adverse effect on the business of the Bank or on its consolidated financial position; and
d) satisfactory explanations and information have been provided to us by Management in response to all our requests.

The partner in charge of the audit resulting in this independent auditor’s report is Ashwani Siotia.

Ernst & Young
Partner’s registration no.117
27 February 2017
Manama, Kingdom of Bahrain