# Annual Report


LGB BANK

بنك لبنان والخليج ش.م.ل

# Contents

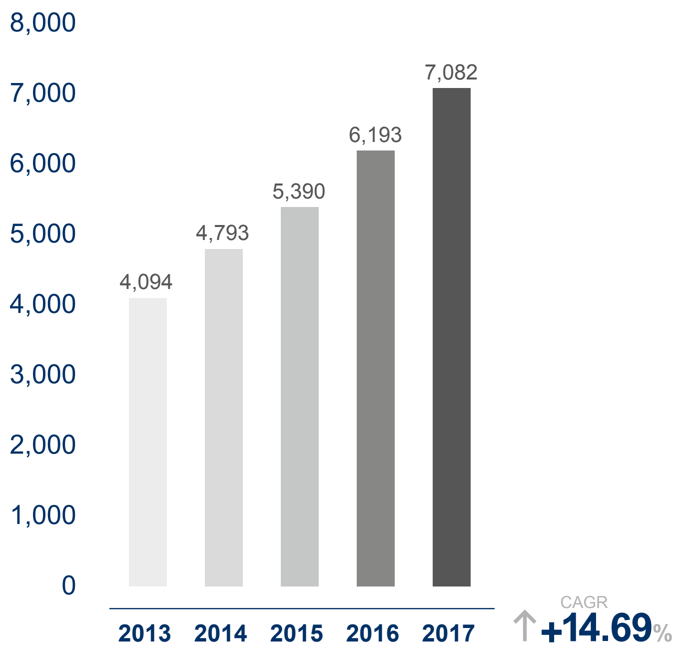
01

# Financial Highlights

**In millions of LBP** — **As at December 31**

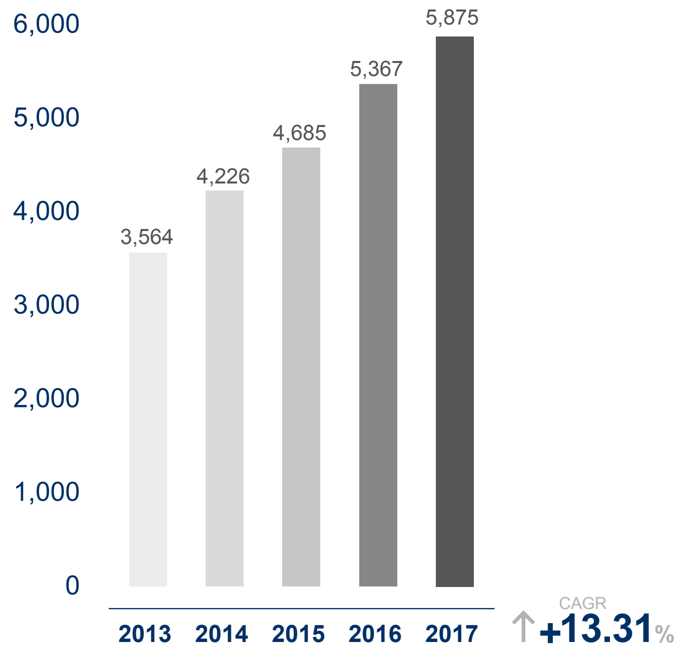
| | 2017 | 2016 | 2015 | 2014 | 2013 |
|---|---|---|---|---|---|
| **Balance Sheet** | | | | | |
| Total Assets | 7,082,117 | 6,192,588 | 5,389,716 | 4,793,244 | 4,093,660 |
| Customers' Deposits | 5,874,637 | 5,367,228 | 4,684,857 | 4,225,906 | 3,564,320 |
| Loans & Advances | 2,045,368 | 2,171,898 | 2,086,028 | 1,923,909 | 1,596,134 |
| Equity | 578,173 | 527,923 | 482,585 | 412,122 | 368,647 |
| **Financial Results** | | | | | |
| Net Operating Income | 134,372 | 114,968 | 102,105 | 95,284 | 81,274 |
| Net Interest Income | 72,676 | 77,222 | 73,918 | 67,380 | 63,766 |
| Net Non-interest Income | 72,800 | 48,306 | 35,882 | 33,265 | 31,383 |
| Net Income | 60,290 | 53,425 | 46,218 | 40,849 | 34,125 |

**Total Assets**
**In billions of LBP**

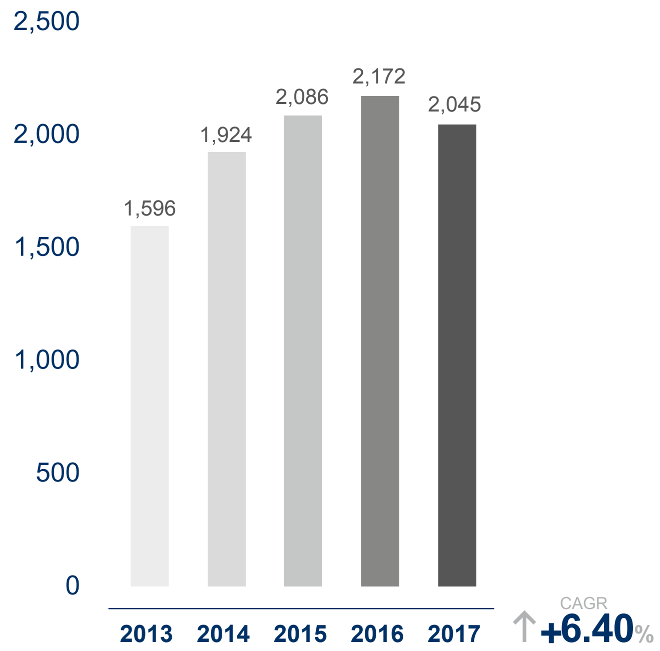



*CAGR:*
*Compounded Annual Growth Rate*

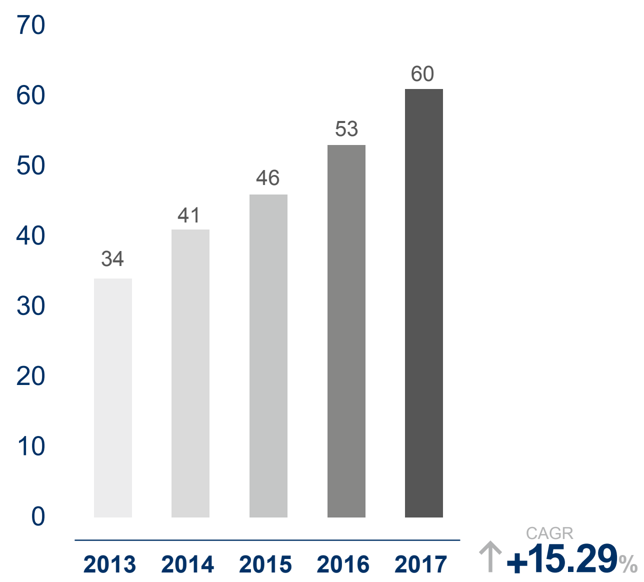
**Total Customers' Deposits**
**In billions of LBP**



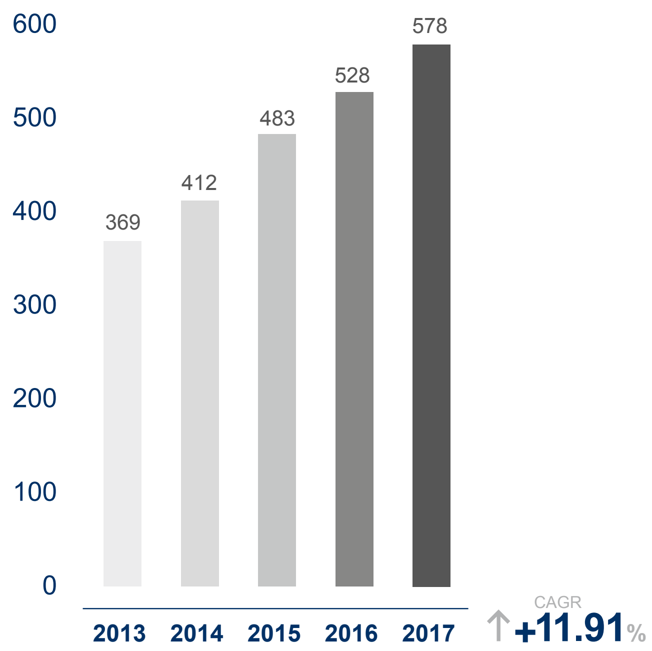

**Total Loans & Advances**
**In billions of LBP**




**Net Income**
**In billions of LBP**




**Total Equity**
**In billions of LBP**



**Key Performance Indicators** — As at December 31

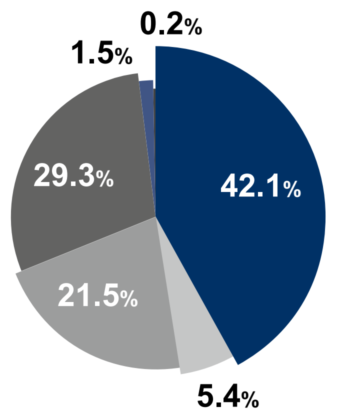
| | 2017 | 2016 | 2015 | 2014 | 2013 |
|---|---|---|---|---|---|
| **Liquidity Ratios** | | | | | |
| Liquid Assets to Total Deposits | 83.19% | 72.11% | 66.47% | 63.12% | 57.64% |
| Net Loans to Total Assets | 28.88% | 35.07% | 38.70% | 40.14% | 40.08% |
| Net Loans to Stable Funds | 30.01% | 37.48% | 41.12% | 42.85% | 42.04% |
| **Profitability Ratios** | | | | | |
| Return on Average Assets | 0.91% | 0.92% | 0.91% | 0.92% | 0.89% |
| Return on Average Equity | 10.90% | 10.57% | 10.33% | 10.45% | 10.45% |
| Return on Average Common Equity | 12.48% | 12.19% | 12.72% | 12.59% | 12.50% |
| Cost to Income | 37.84% | 40.53% | 42.10% | 43.44% | 43.14% |
| Net Interest Margin | 1.12% | 1.37% | 1.49% | 1.56% | 1.65% |

**Key Performance Indicators** — As at December 31

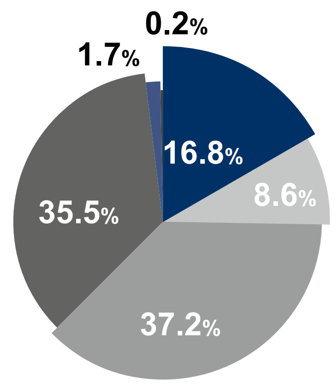
| | 2017 | 2016 | 2015 | 2014 | 2013 |
|---|---|---|---|---|---|
| **Asset Quality Ratios** | | | | | |
| Non Performing Loans to Gross Loans | 7.50% | 6.64% | 4.61% | 5.18% | 7.19% |
| Loan Loss Reserve to Non Performing Loans | 49.52% | 51.07% | 79.59% | 76.90% | 61.84% |
| **Capital Adequacy Ratios** | | | | | |
| Capital Adequacy | 14.61% | 14.30% | 12.52% | 12.18% | 11.11% |
| Risk Weighted Assets to Total Assets | 54.24% | 59.91% | 64.20% | 63.62% | 71.85% |
| Equity to Assets | 8.16% | 8.52% | 8.95% | 8.60% | 9.01% |
| Book Value / Share | $29.68 | $26.20 | $23.19 | $20.95 | $18.57 |
| Earning / Share | $3.49 | $3.01 | $2.65 | $2.42 | $2.00 |

**BREAKDOWN OF ASSETS**

**2017**



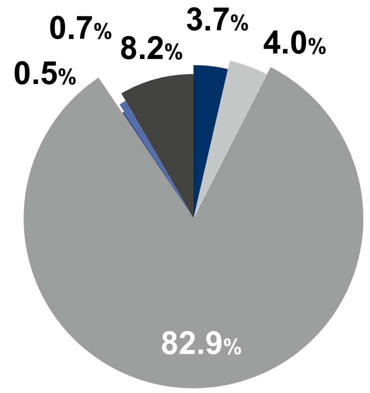

**2016**



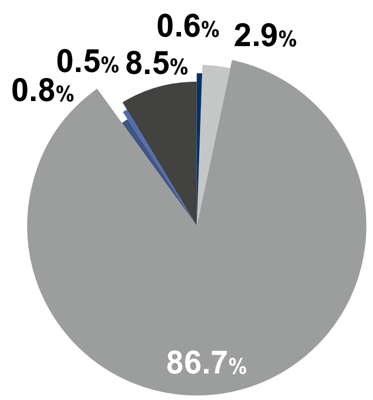

- Central Bank
- Bank Placements
- Portfolio Securities
- Net Loans
- Fixed Assets
- Other Assets

**BREAKDOWN OF LIABILITIES**

**2017**




**2016**




- Central Bank
- Bank's Deposits
- Customer's Deposits
- Other Liabilities
- Provisions
- Equity

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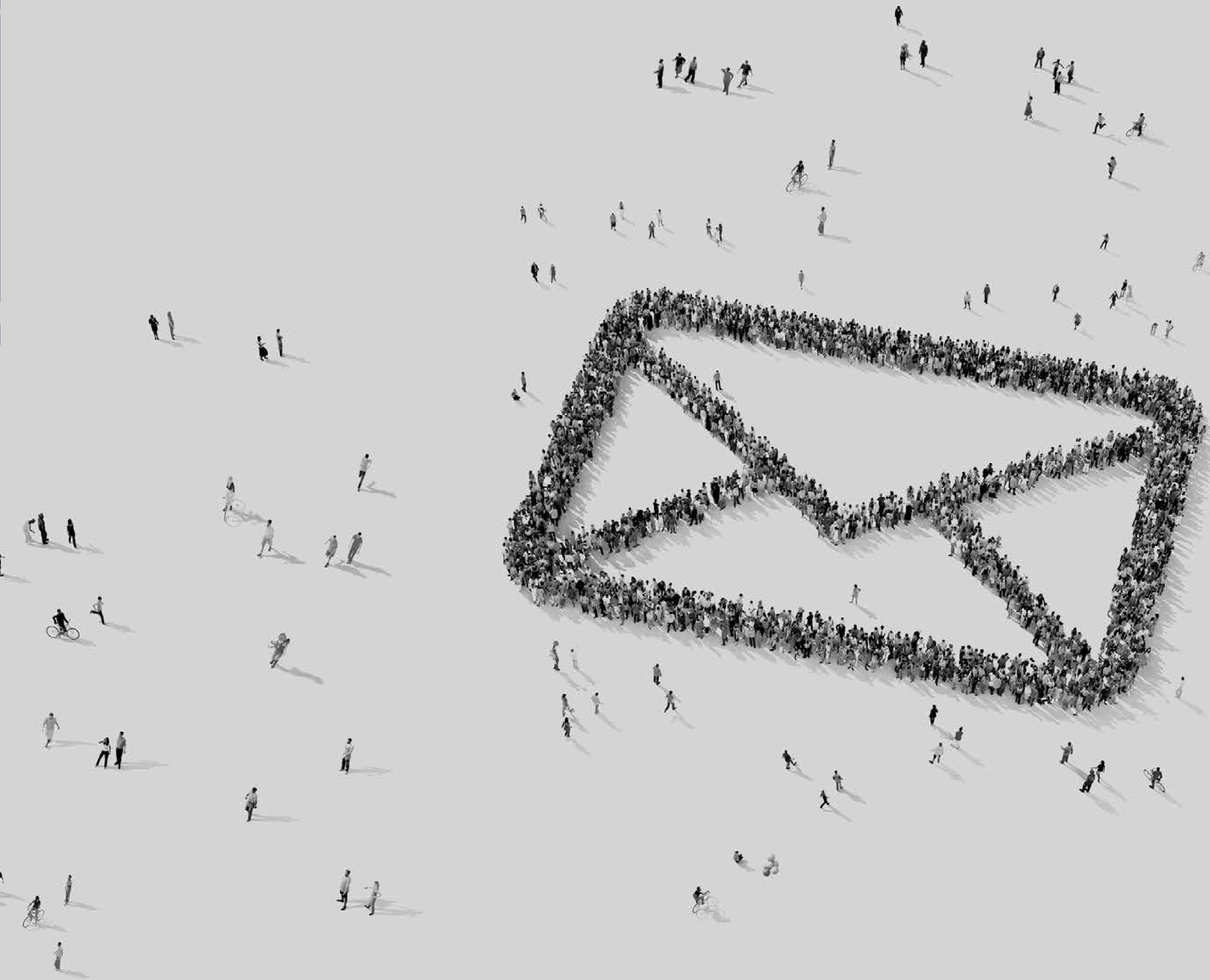
# Chairman & Vice Chairman's Letter



LGB BANK's performance in 2017 was marked by solid financial results and a continuing growth momentum despite the local and regional tensions. Total assets increased by 14.4%, the second highest percentage growth among competing alpha banks. A remarkable increase of 9.5% was also achieved in customer deposits, compared to a 3.5% growth in deposits for the overall alpha banks group.

In terms of key financial highlights, a superior growth and performance was sustained while maintaining a sound and robust risk profile. Profitability increased by 12.8% in 2017 reaching LBP 60.29 billion, up from LBP 53.42 billion in 2016. In parallel, total assets increased by LBP 890 billion, to reach LBP 7,082 Billion. The main driver behind the increase in total assets was the superior growth in customers' deposits reaching LBP 5,874 billion by the end of 2017. In accordance with the Bank's long-term growth strategy, all earnings were retained which resulted in an increase in total shareholders' equity to LBP 578 billion, up by 9.5% from LBP 528 billion in 2016.

In terms of capitalization, and in line with its conservative risk strategy, LGB BANK maintained conformity to regulatory requirements during all reporting periods. The Bank's regulatory capital amounted LBP 561 billion, leading to a capital adequacy ratio of 14.61% as at 31/12/2017.

In terms of competitive position, LGB BANK's objective in enhancing both "Out of the Box" as well as "Tailored" products proved successful, as evidenced by the superior financial results. Pricing also remained on the front-line of the Bank's operational strategy, whereby thorough analysis was conducted in order to maintain the optimal mix between the internal cost structure as well as customer affordability.

As stated earlier, LGB BANK's sound financial position and remarkable performance were achieved while maintaining a conservative risk approach. It is the Bank's foremost objective to maintain a constructive balance between risk and reward. This entails an effective, holistic, and proactive risk management function which remains fundamentally essential for achieving long-term strategic goals. In a more deliberate manner, management believes that enhancement and continuous improvement of the Bank's "Liquidity Position" and "Asset Quality" will add significant long-term value to the Bank and its shareholders.

In order to safeguard the interests of all stakeholders, the Bank is fully devoted to implementing best corporate governance practices and enforcing stringent Compliance and Anti-Money Laundering requirements, all of which render furthermore confidence and trust in the Bank, both regionally and internationally.

At the business strategy level, the successful stream of strategic decisions made throughout the years resulted in a network of 18 branches across Lebanon, one branch in Larnaca-Cyprus and one Representative office in Dubai-UAE. This strategy depicts further expansion, both locally and regionally, with the aim of building and nurturing solid relationships and partnerships on all fronts.

As further evidence of sound strategic objectives, LGB BANK signed a USD 67.5 million syndicated funding agreement with well-renowned international Development Finance Institutions (DFIs) namely, The Dutch Development Bank (FMO), The OPEC Fund for International Development (OFID) and The Development Bank of Austria (OeEB) for the purpose of supporting Small and Medium Enterprises in the country. The Environmental and Corporate Social Responsibility milestones achieved by LGB BANK as a result of this agreement exemplified to peers a superior model in adopting international banking standards.

At the level of IT infrastructure, LGB BANK remains keen to implement state-of-the-art business and technological enhancements throughout all core business lines. Nevertheless, the ultimate obligation and goal is to preserve the confidentiality and privacy of all customer-related data. Significant efforts are exerted in enhancing existing IT security measures and practices, while continuously training employees on all levels regarding the rigorous procedures that are adopted in order to provide customers with the highest degree of information protection.

Similarly to previous years, LGB BANK once again attracted the recognition of major renowned institutions. Most importantly, the Bank was awarded "Fastest Growing Commercial Bank Lebanon" and "Best Bank for Investor Relations Lebanon" by Global Banking and Finance Review for the year 2017.

The professionalism, integrity, demeanor and skill demonstrated by LGB BANK's staff have been the key drivers behind the Bank's success. The unfaltering trust of our valued customers has been equally significant. Therefore as a final word, we extend to our staff and customers the sincerest gratitude and appreciation.

**Abdul Hafiz M. Itani**
Chairman-General Manager

**Samer A.H Itani**
Vice Chairman- Chief Executive Officer

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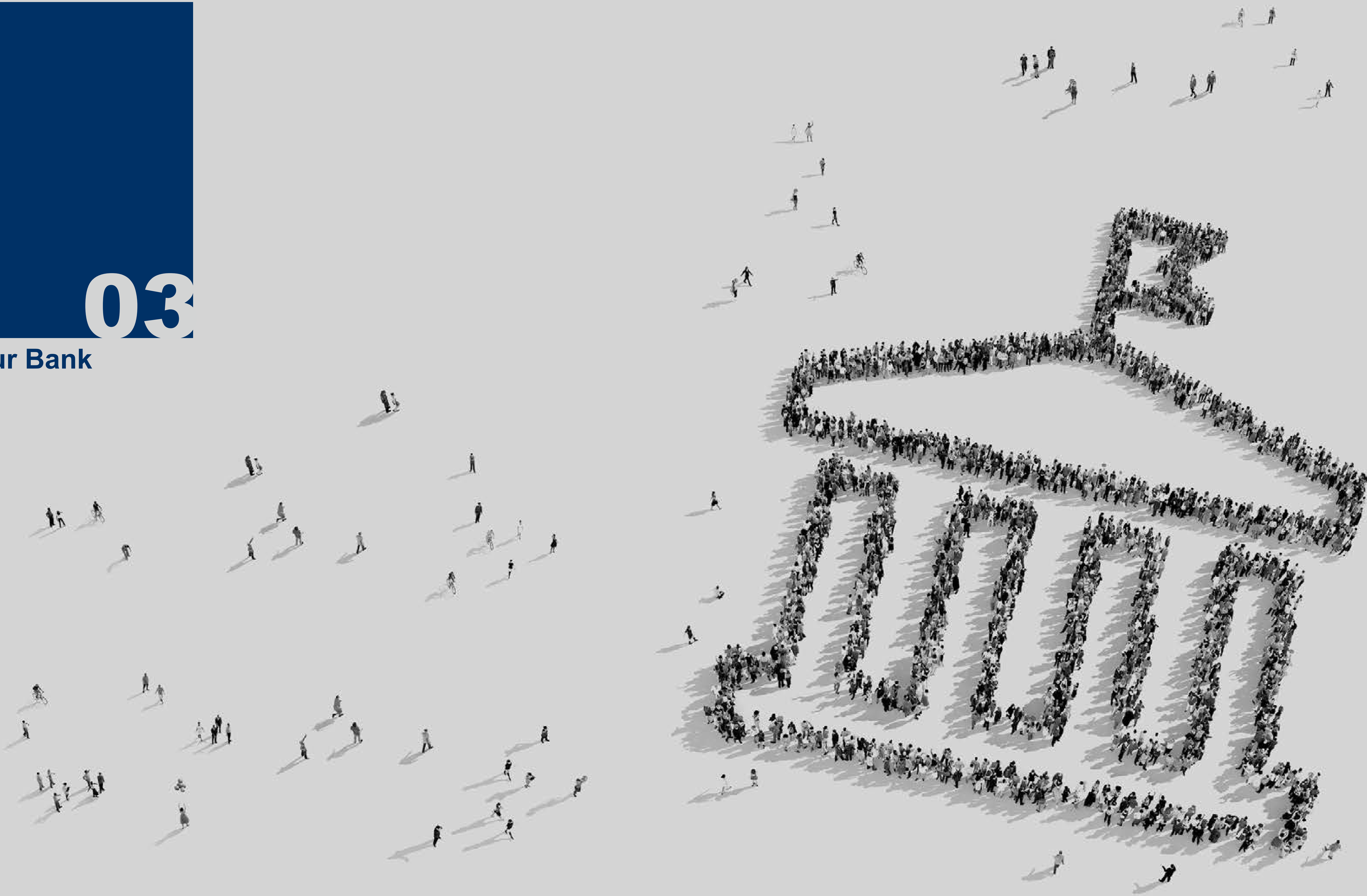
## Our Bank



## Historical Foundation

With more than 50 years of banking tradition, trust and excellence in customer service, LGB BANK stands today as one of Lebanon's deeply rooted banks.

Established in 1963 under the name of Banque de Credit Agricole S.A.L., LGB BANK adopted its current name and shareholders form in 1980 when a group of businessmen (led by the current Chairman) acquired the majority of its shares.
The Bank currently operates from its head office which is located in Beirut Central District, and is backed by a powerful network of 18 branches spread across the country, along with a branch in Cyprus since 1986, and a Representative Office in Dubai, UAE.

As one of the most evolving and vibrant institutions in the country today, LGB BANK is committed to a regular systematic expansion strategy. As such, the Bank had embarked on a new branding effort which, aligned with its business strategy, promised to propel it to new heights. This strategy has transformed into an enhancement of LGB BANK's operational and information technology infrastructure, a substantial growth in profits and deposits, and most importantly into a concentrated modernization and development of the human capital. Major changes in the Bank's new identity aimed at reflecting its core values and attributes in terms of quality and professionalism. The latter has affected LGB BANK's corporate image, achievements and premises, amongst others. The Bank's expansion strategy runs simultaneously in Lebanon and the Middle East, as LGB BANK is continuously tapping into potential prospective markets.

With its dedication and clear vision, LGB BANK continues to build strong relationships with its clients through a personalized approach coupled with sophisticated services and innovative products that match the customers' financial aspirations. Accordingly LGB BANK received numerous awards and recognitions from prestigious international institutions to include Excellence in E-banking and Mobile Banking award, Retail Bank of the Year, Best Financial Transformation, Best Credit Card and Best Co-Branded Credit Card, as well as Fastest Growing Commercial Bank Lebanon and Best Bank for Investor Relations Lebanon.

## Vision

Based on its ongoing pursuit of excellence and optimized customer satisfaction, LGB BANK aims to become the bank of choice for Lebanese and regional customers. Through a consolidated and growing network of branches and affiliates, we aim to establish lasting relationships with our customers and continuously improve our performance to gradually become a cornerstone in the banking industry.



## Mission

At LGB BANK, we thrive to provide our customers with best in line products and services that meet their evolving short and long term needs. Our mission is to establish trustful and personalized relations with each and every one of our clients; while giving them access to a team of reliable professionals, who are committed to a high quality financial performance. We value excellence over quantity and settle for nothing less than outstanding results that surpass our clients' expectations.

## Values

**/// Legacy**

From one generation to another, the Bank has cumulated a valuable experience thus, building a successful and proven track record. LGB BANK firmly believes in the consistency and continuity that a valuable banking legacy can offer.

**/// Integrity**

At LGB BANK we put our customers' best interests at the forefront of our operations. We believe that delivering genuinely good services will undoubtedly lead us to achieve success. This is why we adopt a widely transparent strategy while dealing with our clients.

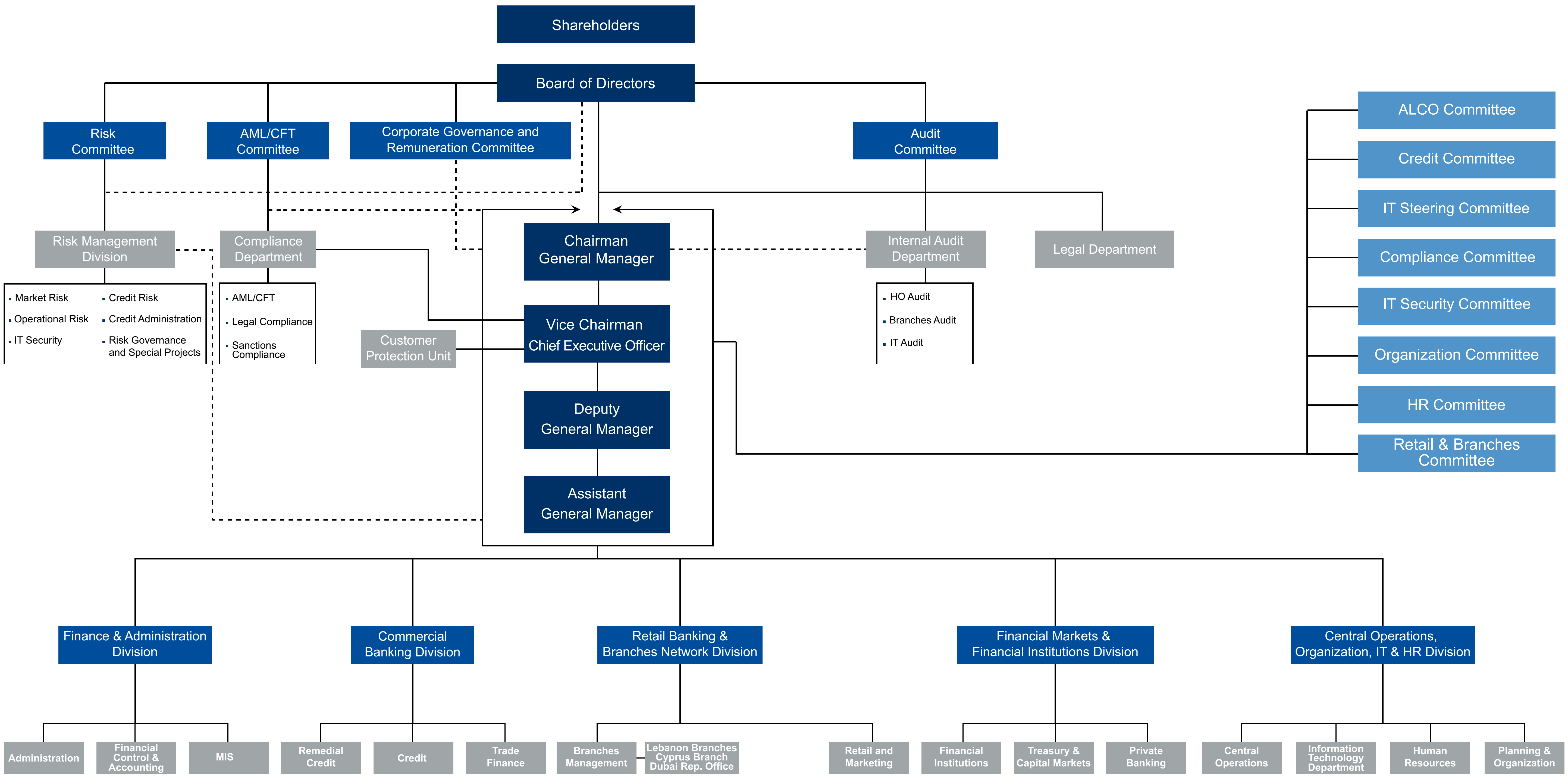
**/// Quality**

LGB BANK has a long and proven track record in the Lebanese market; one that is marked by the delivery of high quality products and services. Indeed, premium quality remains at the heart of our business strategy which aims at preserving high levels of customer satisfaction by offering impeccable services.

**/// Accountability**

LGB BANK is a reliable banking partner for Lebanese and foreign customers. We provide them with a diversified portfolio of offerings, based on thorough analysis of the market and the local customers' needs. We also put at the disposition of our clients the expertise of a pool of industry experts who offer professional advice and reliable solutions.

## Organizational Chart



# 04

# Corporate Governance

## GOVERNANCE

LGB BANK is keen on ensuring complete compliance with local and international governance practices. Armed with the core values of integrity, transparency, and accountability, the Bank's governance culture has been progressively evolving to encompass robust risk management and control practices that direct it in sustaining business performance and delivering long term value to stakeholders.

The Board's key governance responsibilities are to set the Bank's strategic objectives while relying on Management's relevant and timely controls to facilitate complex decision making. The board also sets the Bank's internal controls and risk appetite through a well defined policy supported by proper oversight to ensure the accurate and comprehensive implementation of these controls.

LGB BANK recognizes its responsibility towards its stakeholders in ensuring safe, sound, and ethical financial operations. It is essential therefore; that our risk culture supports our risk profile and our adopted risk management practices.

LGB BANK acknowledges that long term success is achieved by having the right leaders in place. Thus, talent development and strategic succession planning are critical components of sustainable success at the Board and Executive Management levels.

/// **CORPORATE GOVERNANCE FRAMEWORK**

The Bank's Corporate Governance Framework is specifically designed to guide the Board in achieving the Bank's aims, led by the highest ethical standards and interests of its stakeholders.The Bank's Corporate Governance Policies, including the Code of Corporate Governance, Board Charter, Code of Conduct and Code of Ethics, lay a solid foundation for transparent and accountable decision making. . In addition, as part of its continuous commitment to sound corporate governance, the Bank fortified its Disclosure Policy to ensure that all required regulatory disclosures are done effectively and efficiently. The Bank's corporate governace guidelines are available on the Bank's website at www.lgbbank.com.

/// **BOARD SELECTION AND ELECTION**

Board members are appointed on merit, based on the required diversity for effective decision making. Board members' selection relies on integrity, character, range of skills, professional experience and background, and finally, willingness to commit adequate time and effort to the Bank Shareholders elect the Board to oversee management and to assure that the shareholders' rights are protected LGB BANK is governed by 11 members ( out of which 7 are independent members ) elected by the general Assembly of shareholders for terms not exceeding 3 years.

/// **BOARD RESPONSIBILITIES**

The Board sets strategic objectives and policies that are focused on delivering long-term value and providing overall strategic direction within the set framework of risk appetite and controls.. It governs transparently the Bank through monitoring business performance, operations and the integrity of internal controls. Through establishing clear lines of responsibility, accountability and communication throughout the Bank, the Board performs its responsibilities as a supervisory entity while delegating management the responsibility of implementing the policies, guidelines and parameters set by the Board in compliance with the laws and regulations. In addition, the Board is responsible for guaranteeing that management maintains an effective Risk Management and oversight process at the highest level.

## BOARD COMMITTEES

/// **AUDIT COMMITTEE**

The Audit Committee's mission resides in assessing the integrity of the Bank's financial reporting, the effectiveness of internal controls in addition to the performance of the Bank's Internal Audit Unit and External Auditors with respect to the suitability and relevance of the submitted reports. The Audit Committee supports the Board in protecting the interests of shareholders and other stakeholders by acting with the right level of diligence to assure that appropriate and prudent judgments have been made with respect to financial reporting given that the financial statements provide a realistic view of the Bank's financial position and that the auditor's independent analysis on behalf of shareholders is both objective and effective.

/// **RISK COMMITTEE**

The Risk Committee reviews and recommends the Bank's Risk Policies and Risk Appetite directly to the Board. It is also responsible for identifying and monitoring the Bank's risk profile for all types of risks and ensuring that the overall Bank's risk profile and risk appetite remain appropriate, in addition to recognizing and assessing future potential risks. The Committee oversees the Risk Management Framework, assesses its effectiveness, and supervises the proper implementation of Risk Management policy in order to adapt to regulations.

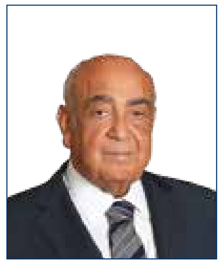
/// **CORPORATE GOVERNANCE AND REMUNERATION COMMITTEE**

The general purpose of the Corporate Governance and Remuneration Committee of LGB BANK is to develop and recommend sound Corporate Governance principles; including corporate governance guide and follow up on their implementation in accordance with the guidelines issued by the Basel Committee and Supervisory Authorities.

The committee is also responsible for developing the Remuneration policy and the Remuneration System at the Bank, presenting them to the Board of Directors and overseeing their implementation. The Bank's remuneration structure comes to support sound corporate governance through assisting Board members in identifying potential nominees to the Board and senior management. It oversees their remuneration, evaluates their performance and ensures that staff salaries and incentives are in line with the Bank's culture, objectives and strategy.

/// **AML/CFT COMMITTEE**

The AML/CFT Board Committee was established to assist the Board of Directors in its functions and supervisory role with respect to Fighting Money Laundering and Terrorist Financing, understanding the related risks, along with providing assistance for sound decision makings  in this regard. The role of the AML/CFT Board Committee also includes protecting the Bank from other compliance risk related issues and, more generally, overseeing the Bank's compliance with AML/CFT applicable laws, policies and regulations. From a risk-averse point of view, the committee reviews the reports submitted by the AML/CFT Compliance Unit and the Internal Audit Division. It also reviews all the adopted procedures in terms of unusual operations and high-risk accounts in order to recommend suitable decision in this context.



## MR. ABDUL HAFIZ M. ITANI

Chairman – General Manager

Mr. Abdul Hafiz Itani has been the Chairman - General Manager since 1980 upon acquiring the majority of the Bank's shares along with a group of local and Gulf investors.
With more than 65 years of experience in the banking and finance industries, Mr. Itani's professional career, crowned with his successful management of a long-lasting established family business, impelled him to lead LGB BANK through affluent and challenging times to be one of the leading banks in Lebanon.
During his career timeline, Mr. Itani has occupied several key positions in the Lebanese banking sector.

## MR. SAMER A.H. ITANI

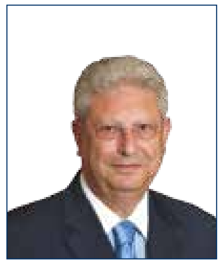
Vice Chairman – CEO

Mr. Samer Itani started his Banking career at LGB BANK by occupying several managerial positions in different divisions at the Bank, prior to being selected in 1995 as a member of the Board of Directors.
Mr. Itani was appointed to his current position in 2007 and is currently responsible for leading the restructuring and expansion strategies of the Bank, thus positioning it as one of the best performing Lebanese banks.
Mr. Itani holds a degree in Finance and International Management from Georgetown University in Washington DC. He attended advanced management programs at both INSEAD and London Business School.

## MR. JOSEPH M. HAKIM

Deputy General Manager - Board Member

Mr. Hakim occupies currently the position of Deputy General Manager and Head of International Banking Division. He is also a member of both the Risk and the AML/CFT Board Committees. Mr. Hakim has 55 years of experience as he joined LGB BANK in 1980. Today, the banking veteran is considered to be one of the founders in the new entity of LGB BANK.
In his former professional life, Mr. Hakim worked in different local commercial banks and held several managerial positions. The skilled banker earned a degree in General Commerce from the American University of Beirut.



## ME. ANTOINE J. CHADER

Board Member

Me. Chader is a member of both the Risk and the AML/CFT Board Committees. He was nominated as a Member of the Lebanese Parliament and has over 50 years of experience in law, banking and financial institutions. Me.Chader's professional career is marked with key positions, appointed Chairman and General Manager of two local banks and the President of Association of Banks in Lebanon. Me. Chader is a prominent Lebanese lawyer and holds a degree from the Saint Joseph University's Law School.

## H.E. ABDUL KAREEM H. ARKOBI

Board Member

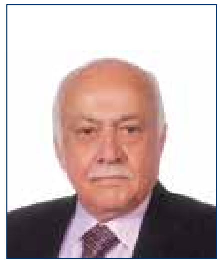
H.E. Arkobi is an independent member of the Board of Directors. He has a vast experience in banking and firms management in the MENA region. His Excellency is now the Chief Executive Officer and owner of Gold Inspiration Company for Trade, Al Safir al Mout'lek Contracting Company and Shaybah Holding. His career was marked with key positions as he has been appointed General Manager, Advisor and Deputy Minister in the Saudi Royal Court for the past fifteen years.

## MR. MOUNIB M. HAMMOUD

Board Member

Mr. Hammoud is an independent member of the Board of Directors. Mr. Hammoud has over 35 years of extensive experience in banking, institutional finance, city making, land development, real estate development, retail and tourism projects development, strategic planning, corporate finance and financial architecture, as well as sales and marketing of real estate projects, in the Middle East, North Africa and Europe. He holds a Master's degree in Business Administration from the American University of Beirut.





## JUDGE SAID M. MIRZA

Board Member

Judge Mirza is an independent member of the Board of Directors and he is the Chairman of the AML/CFT Board Committee. Judge Mirza has a vast experience of more than 50 years in law where he occupied many judicial functions until his nomination as Attorney General of the Court of Cassation until his retirement. Additionally, he participated in the documentation of legal texts, rulings, legal research and analysis. Judge Mirza holds a law degree from the Lebanese University.

## DR. MOHAMMED A.H. CHEAIB

Board Member

Dr. Cheaib is an independent member of the Board of Directors and he is the Chairman of the Corporate Governance & Remuneration Committee and a member of the Risk Committee. Dr. Cheaib is the Chairman-General Manager of INTRA Investment Company S.A.L., and a board member of a local commercial bank. Additionally, he is a member of the International Association of Arab Bankers. Dr. Cheaib has over 50 years of banking experience and has several studies published in Lebanese media outlets. Dr. Cheaib holds a doctorate in Economics from Aix-Marseille University in France.

## MR. RABIH A.K. EL-NOUEIRI

Board Member

Mr. Noueiri is an independent member of the Board of Directors and he is the Chairman of the Audit Committee and a member of the Corporate Governance & Remuneration Committee. Mr. Noueiri has a wide experience of more than 35 years in American, European, and local banking. He was the Executive Manager at American Express Bank in London, Member of the Executive Management at Union Bancaire Privée in London, Senior Vice President at Chase Manhattan Bank in addition to several key positions in local commercial banks.

Mr. Noueiri holds a Business and Commerce Master's degree from Beirut Arab University.

## MR. PHILIPPE A. SALEH

Board Member

Mr. Saleh is an independent member of the Board of Directors and he is the Chairman of the Risk Committee and member of the Audit Committee. Mr. Saleh has over 35 years of experience in the banking sector. After having started his career in the Corporate Banking Division at Citibank N.A., Mr. Saleh has held several managerial positions at a local leading commercial bank, the latest of which was Chief Risk Officer (CRO) – AGM, Head of Group Risk Management Division. He demonstrated expertise in developing an integrated risk management framework for all aspects of risk across the organization, and implementing a set of risk metrics and Basel II and Basel III compliant reporting.
Mr. Saleh holds a Master's degree in Business Administration from Paris IX Dauphine University, a Masters in Science from the Faculty of Lyon as well as the "Citibank Management Certificate".

## MR. FOUAD N. TOUMA

Board Member

Mr. Touma is an independent member of the Board of Directors. He is also a member of the Board of Directors of Hotel Dieu de France (HDF) of the Saint Joseph University (USJ) and a member of both the Audit Committee and the Corporate Governance & Remuneration Committee.
Mr. Touma has a notable experience of more than 55 years in local banking where he handled great responsibilities and managed major directorates such as the Secretariat of the Board. He is currently giving banking courses at the Higher Institute of Banking Studies (ISEB) of Saint Joseph University. Additionally, Mr. Touma is the holder of the Belgian Insignia of Officer of the Order of Leopold II, Treasurer of the Alumni Association of Jamhour College, and Member of the Alumni Executive Committee of the Faculty of Law of Saint Joseph University. The banking expert holds a Master's degree in Law and Banking from Saint Joseph University and has participated in several banking seminars in France and Belgium.

# 05
## Our Business

## Corporate & Commercial Banking

LGB BANK maintains a well-established position in the commercial lending field, with a concentration on corporate banking services through a distinctive approach for quality planning and trustworthy financial consultancy. After years of success in the local financial market, and with the unwavering reliability of its clientele, the Bank has been acknowledged as a highly reliable business partner rather than just an ordinary financing service provider.
With the support of its skilled personnel and solid financial and logistical resources, LGB BANK is able to keep a close eye on its customers' businesses and projects. Consequently, the Bank enables its clients to achieve all their goals by granting them financial counseling and proper orientation.
The customer portfolio at LGB BANK is composed of small, medium and large scaled enterprises, all of which benefit from a variety of products and services tailored to meet their specific financial needs. Our offerings include traditional overdraft facilities, project financing, loan syndication, structured business solutions, supply chain finance and various trade finance products and services.
LGB BANK constantly aims to enhance its commercial client-base while maintaining adequate collateralized debt obligations and while remaining in full compliance with the regulations of the Central Bank of Lebanon.

## Investment & Private Banking

Backed by a solid track record and a proven know-how in customer handling and servicing, LGB BANK provides its Clients with a wide range of products and services through a specialized cell of professionals well trained in Investment and Private Banking practices, offering reliable non-discretionary consultancy and personalized solutions with access to a broad spectrum of Local and International Markets.

**/// Treasury and Capital Markets**
Apart from its strategic role in the efficient Assets and Liabilities' Management of the Bank including but not limited to the recommendation of financial engineering solutions that would secure optimum returns on investments while boosting the Bank's profitability, within the internal and regulatory guidelines; the Treasury and Capital Markets Department at LGB BANK is the clients' key access to International Foreign Exchange, Money and Capital Markets.
Skilled team members provide the Bank's clients with reliable information and an eclectic range of investment products, including stocks, bonds, funds and structured products…
In addition to the above, LGB BANK provides Brokerage services and Safekeeping of various types of financial instruments.

**/// Private Banking**
In a highly competitive market, LGB BANK has managed to accustom a niche segment of high net worth customers by offering them impeccable services.
To maintain such strong bonds, the Bank's Private Banking teams have been able to provide their customers with Financial Products based on a clear understanding of their objectives.
Backed by a high sense of resourcefulness, in-depth business knowledge and solid commitment towards the Bank, the teams' performance has been commendable from all angles.

## Retail Banking

LGB BANK has kept up with the evolving requirements of the markets, at all times, and based its product development policy around the client's ever-changing needs. In parallel, the Bank was always keen to continuously improve the customer's banking experience, by providing a totally modern and transparent service based on trust and knowledge of the client's aspirations whilst capitalizing on the role of new technologies.
The Bank continues to develop its portfolio of targeted products and services, aligning its actions with its broad product strategy and succeeding in widening its clientele base, while remaining faithful to its quality standards.

**/// Innovative Services**
In light of its wider corporate strategy, LGB BANK has been a leader in the field of retail banking.

It is to be remembered that the Bank was the first to introduce the SMS alert service. The "Banking by Night" service is another one of the Bank's pioneering initiatives which provide customers with flexible banking hours, making the Bank one of the very few financial institutions in Lebanon to open its doors for a second shift from 7:00 PM to 10:00 PM.

**/// Payment Cards**
With an objective to introduce innovative payment solutions that offer value added benefits to cardholders, comes the mobile payment platform, a ground-breaking service at LGB BANK; it is a highly safe payment solution linked to a credit card. This service enables customers to make secure and reliable purchases within the application.
A real pioneer in this field, LGB BANK was one of the first banks to issue MasterCard in Lebanon, back in 1992. Today the Bank offers a wide range of payment cards from Titanium, Platinum, and Black under both MasterCard and Visa brands.
Responding to evolving banking needs and modern lifestyles, LGB BANK presents an extended line-up of MasterCard and Visa to choose from, including Debit, Credit and Prepaid cards.
In collaboration with MasterCard, the Bank launched the First UAE Dirham Credit Card that has been specifically designed for UAE visitors and residents, offering its holders exclusive benefits and rewards while sparing inconvenient change rates, in addition to many currencies such as USD, LBP, Euro, Sterling Pounds, Turkish Lira, and Saudi Riyal.
LGB BANK cards are developed with appealing payment facilities and flexible use limits which are constantly revised to meet the customers' increasing demand for cash.
In addition to the regular payment cards that come handy anytime and anywhere, the Bank also offers a Debit MasterCard with an exclusive Pin Trigger, a feature through which customers can activate their cards via the Bank's ATMs or any other ATM related to CSCBank SAL so as to avoid fraudulent attempts.
Topping this range of retail offerings is the LGB Black Card. Considered as an exclusive "MasterCard World Card", a global access to a group of internationals has now been exclusively offered to the most valued customers, as Black Card holders can take advantage of the generous services, exclusive offers and luxurious experiences presented to the very few. Moreover, the Bank launched a high end co-branded credit card for Porsche Club members, offering lots of benefits and privileges under the motto "Adding Privilege to Power".
Further in line with its customer centric strategy, the Bank initiated its LGB Miles Program under "More Miles, More Destinations". This Loyalty concept allows LGB BANK credit cardholders to earn 1.5 Miles for each USD 1 spent, or equivalent in other currency, on any LGB Credit Card, in addition to free access to more than 500 airport lounges in more than 300 cities around the world with no previous registration needed. Cardholders will also benefit from special travel offers to visit more than 55 touristic destinations on most of the international airlines. In this sense, LGB BANK reconfirms its intent to provide an unmatched banking experience by rewarding its customers for their loyalty as well as their frequent use of its payment cards. The Loyalty and Miles Program rewarding experience also offers a unique shopping experience, where cardholders can redeem their earned points from over 4,000 carefully selected gift items and vouchers, or even simply cash back the points earned anytime.

**/// Consumer Loans**
With a rising demand on loan products, LGB BANK has developed services that aim to improve its customers' quality of life, whether from a personal or a professional standpoint.
In addition to the usual common loans such as the Home, Personal and Car loans, the Bank has launched the Public Sector Personal Loan which allows public employees to obtain a competent credit facility against an attractive rate and within favorable conditions. Along with the private offer for salary domiciliation which allows private sector employees to benefit from a wide range of free services.

**/// The e-LGB BANK Platform**

Over the past few years, the world has witnessed a real electronic revolution, pushing most businesses to leverage their operations through an online system. In this line, LGB BANK is continuously updating the modern and upbeat version of its corporate website, www.lgbbank.com, with user friendly functions including both corporate and retail banking products and services, thus creating a comprehensive interface to browse and explore.
Digital specialists have implemented the Online Banking platform, "LGB Online Banking", allowing the Bank's customers to benefit from a number of products and services from the comfort of their homes or offices. LGB Mobile Banking platform was made also available on Apple Store and Google Play. The online banking platform is currently being renovated in order to provide customers with the newest and most up-to-date technology.
LGB BANK is also present on all digital platforms such as Facebook, Twitter, LinkedIn , Instagram, YouTube, and is committed to keeping its customers up-to-date at all times with news, product launches, services, as well as the opening of all branches.

## International & Financial Institutions

With the ongoing growth of the Bank and an unprecedented challenge to keep up with international standards, the financial institution department has a vital role in managing its relationships, being aware that compliance and profitability go hand in hand. The Department is set to align its strategy with the Bank's future plans, while securing efficient and profitable relations globally, through:

**SECURING WHAT WAS:**

- Detecting any change in the risk profile or any risk mitigation measures by performing a thorough compliance review.
- Adopting the ongoing regulations of the correspondent banks to confirm with all policies, while trying to balance between compliance requirements and costs.

**MAINTAINING WHAT IS:**

- Enhancing established relations with correspondents in order to ensure growth and diversification, as well as granting an access to different financial services in different jurisdictions to secure a competitive edge for the Bank.
- Advising clients about the partners' requirements thus providing full transparency to all parties involved in any transaction.

**DEVELOPING WHAT COULD:**

- Taking benefit from the innovative products and services offered by the correspondents, related to payment solutions, capital market services and international trade.
- Exploring new relationships for the Bank so to address apparent needs and find best global providers in the market.

## Marketing & Communication

With a clear vision for development and efficient management, LGB BANK continues to build strong relationships with its clients through a personalized approach coupled with innovative services and "out of the box products" products, tailored to meet the customers' fast-changing financial needs.

Recognized as a banking institution striving for excellence and driven by ambitious growth, LGB BANK was able to win several international industry awards; a clear recognition of its standing and business philosophy.

Awards include:

- Excellence in E-banking and Mobile Banking from the World Union of Arab Bankers
- Retail Bank of the Year by MEFTECH
- Best Co-branded Credit Card, Best Credit Card and Best Financial Transformation by Banker Middle East–CPI Financial
- Fastest Growing Commercial Bank Lebanon and Best Bank for Investor Relations Lebanon by Global Banking and Finance Review

Beyond being a testimony of the Bank's constant advancement and singularity, LGB BANK also believes that the awards are a stimulus that motivates it to strive for more accomplishments and more innovative services.

Further leveraging its efforts to meet the latest banking trends, LGB BANK continues to provide a world class experience to its customers in its 18 various branches across Lebanon, in addition to a branch in Cyprus and a representative office in Dubai.

Today, the Bank's main communication priority remains to highlight its customer centric strategy using a mix of conventional and disruptive tools; as such LGB BANK has recently increased its digital presence to meet the modern users' expectations. This has enabled the Bank to make an impact on the Lebanese banking scene, gaining engagement and momentum in communication penetration and market share.

LGB BANK manages to retain and sustain its customers' trust with a rightfully communicated and reliable performance. The Bank doesn't build its reputation on commercial promotions, but rather on factual servicing. This strategy has supported the Bank to further enhance its Brand Awareness over the years, from adapting its new corporate identity, to keeping customers and the Lebanese market up-to-date by launching successful marketing campaigns such as the LGB Miles Campaign.

Furthermore, the Bank has adopted an "open door" communication policy whether towards the customers or between employees, aiming at safeguarding its image from all possible angles: well thought internal communication activities that enhance the synergy between the employees and promote teamwork; corporate social responsibility communication that supports community initiatives including the constant endorsement of Lebanese non profitable associations; and campaigns that highlight the competitive edge of the Bank's products and services.

LGB BANK sponsors and supports various social and community initiatives, based on the Bank's commitment and mandate to supporting community organizations and institutions addressing various humanitarian and social issues in Lebanon.

## Human Resources

In 2017, the Human Resources Department continued to support the Bank's mission in numerous ways starting with establishing trustful and tailored relations with each and every one of our clients while giving them access to a team of trustworthy professionals delivering high quality financial performance to settling for nothing less than outstanding results. Continuing to aggressively apply our vision of "becoming the Bank of choice for Lebanese and regional customers," the Human Resources Department carried on to strengthen employees expertise so that they are better placed to deliver the Bank's strategy.

LGB BANK relies, first and foremost, on its employees. The Bank seeks to build the capabilities of managers and staff to help them develop and to drive the Bank towards endless success while providing an atmosphere that supports sustainable performance and promotes continual professional and personal growth for all employees.

Our Bank is committed to an inclusive culture that respects and embraces the diversity of employees. Moreover its leaders cultivate an inclusive and respectful work environment where all employees can be themselves, contribute their best work and succeed based on merit.

We trust that a successful organization is made up of passionate, motivated leaders - endowed people who can articulate our vision; gain organizational understanding and support for specific business initiatives; and energize those whom they lead. We are sure that delivering our best to LGB BANK customers takes men and women who give us their best every day. To that end, Human Resource philosophies and policies are an essential component of our business strategies. We pay particular attention to managing people as our most imperative resource and a significant stakeholder. The officers and staff of LGB BANK are the vital channel for expressing our brand to customers and prospects alike.

Our service philosophy is guided by the goals and priorities of the Bank's Values: Legacy, Integrity, Quality and Accountability. The Human Resources Department is committed to working with the Bank in attracting and retaining top-talented personnel. To attain these objectives, the Department provides a full-range of support services, programs and resources in the areas of employee benefits, compensation, compliance, employee relations, recognition, talent management and professional development training programs. We know our employees are the key to providing an ideal banking experience. As a result, the Human Resources Department is committed to creating a high-performance, varied and inclusive staff. Similarly important is consistently recognizing the skills and capabilities of our employees. This is why we offer regular learning and development opportunities, enabling staff to preserve and enhance their skills and potentials.

## Information Technology

LGB BANK has embraced the technological revolution to ride the wave of sustainable growth in a challenging world economy. In line with this, LGB BANK has invested - and will keep investing- in technology and infrastructure that introduce highly scalable digital platforms, the leverage on technology to sculpt the customer experience, the internal evolution and external partnering in seeking new digital innovation. Yet, integrating new technologies in its internal processes is not the only policy LGB BANK implemented to become a modern financial institution. The Bank has actually worked on developing innovative electronic banking solutions to deliver even higher performance, by providing employees with special online tools that could facilitate their daily chores; and by allowing customers to access a set of online services that simplify their banking transactions. The Bank has also boosted its IT platform by increasing the number of ATMs across the Lebanese territory getting strategically closer to the Lebanese customers. The Bank is always working to enhance the functionality of its core banking system and automate its business processes, coupled with a comprehensive reengineering and improvement of its human and technological resources.

A real pioneer in this field, LGB BANK was one of the very first banks in Lebanon to adopt such technological updates in the industry. In fact, the technological reform stipulated the upgrade of the infrastructure to introduce better risk and security controls ,thus improving productivity. A full security framework based on ISO27001-27005 has been adopted and making benefits from innovative security technologies in order to increase the Bank's resilience against cybercrime and fraudulent activities.

Hybrid integration architecture between systems has been deployed by LGB BANK allowing great flexibility in terms of work flow and transactions' processing; in addition allowing employees to share information internally, creating a solid synergy between departments. All units are linked together by a robust IT system and supported by highly qualified and skilled engineers who are ready to assist with any request.

06

# Management Discussion & Analysis

## BASIS OF PRESENTATION

The following part which covers the Management Discussion and Analysis section (MD&A) enables readers to assess the performance of Lebanon & Gulf Bank S.A.L for the year ended December 31, 2017 as compared to its previous year ended December 31, 2016.
MD&A should be taken in conjunction with our Financial Statements and Related Notes for the year ended December 31, 2017. Amounts are primarily derived from the Bank's Annual Financial Statements prepared in accordance with International Financial Accounting Standards (IFRS).

## ECONOMIC ENVIRONMENT

The Lebanese economy growth remains low, despite the slight improvement in GDP reaching 1.5% in 2017 up from 1.0% in 2016, driven by the regional and domestic political challenges that still govern the area and the slow activity of the main sectors of the Lebanese economy – more specifically the real estate and construction sectors which have witnessed a decline in prices of more than 10% in 2017.
However, several indicators anticipate a recovery in the Lebanese Economy during the coming year starting with the Lebanese Government approving the 2018 budget and the funds raised in April 2018 under the "Cedre" convention as well as the parliamentary elections in May 2018.
Trade deficit widened by 29% (year on year) to reach USD 20.3 Billion due to decreasing exports (6.7% yoy) and growing imports (23.5% yoy).
The Balance of Payments registered a mild deficit of USD 150 Million during 2017 which was mainly contained by the measures taken by the BDL. Gross Foreign Currency Reserves also increased by 5.3% during 2017 to stand at USD 35.8 Billion.
Moreover, gross public debt increased by 6.2% to reach USD 79.5 Billion. Debt in local currency stood at USD 49.1 billion at end of December 2016, accounting for 61.8% of the gross public debt. Debt in foreign currency amounted to USD 30.4 Billion in the mentioned period; constituting 38.2% of the total gross public debt. Gross debt to GDP maintained a slightly higher ratio of 151% in 2017 against 148% at end of 2016.
According to the Ministry of Finance, fiscal deficit decreased by 24% (y-o-y) to reach USD 3.8 Billion by the end of 2017. This was attributed to the 17.2% yearly increase in fiscal revenues, to USD 11.6 Billion, outpacing the 3.5% annual rise, to USD 15.4 Billion, in government expenditures.
As for the monetary situation, the Lebanese banking sector proved its strong stability, even in difficult times. The money aggregate M3 increased by 4.2% to reach USD 138 Billion.

**Major Economic Indicators in Lebanon**

**USD Billion** — **As at December 31**

| | 2017 | 2016 | % Growth |
|---|---|---|---|
| Nominal GDP | 52.7 | 50.5 | 4.4% |
| Real GDP growth | 1.5% | 1.0% | 0.5% |
| Imports | 23.1 | 18.7 | 23.5% |
| Exports | 2.8 | 3.0 | -6.7% |
| Trade deficit | -20.3 | -15.7 | 29.3% |
| Balance of payments | -0.2 | 1.2 | -112.1% |
| Gross Public Debt | 79.5 | 74.9 | 6.2% |
| Gross Public Debt/GDP | 151% | 148% | 3.0% |
| Fiscal Deficit | 3.8 | 4.9 | -24.0% |
| Gross Foreign Currency Reserves | 35.8 | 34.0 | 5.3% |

Source: BDL, Ministry of Finance, IMF, ABL, IIF

## LEBANESE BANKING ENVIRONMENT

The Lebanese banking sector, once again, proved its resilience and robustness in facing political and economic downturns during the year 2017. Despite the limited economic growth and political instability, customer deposits grew by USD 6.2 Billion, and growth in lending activity remained stable, expanding by USD 3.1 Billion.
The Lebanese banking sector successfully emerged from the political crisis of November 2017 which entailed PM Hariri's resignation. In light of this event, negative repercussions on the Lebanese banking sector were short-lived whereby the BDL successfully implemented its sound strategy of widening the interest rate gap between Local and Foreign currency deposits.
Total consolidated assets of commercial banks operating in Lebanon amounted to USD 219.9 Billion at the end of December 2017, thus increasing by 7.6% from end of December 2016.
Lebanese banks depend on deposits as a primary source of funds (constituting 76.7% of total assets); an expansion of 3.8% in total deposits was noted in the year 2017 with an equivalent of USD 168.7 Billion up from USD 162.5 Billion in year 2016.
Loans to customers showed a growth of 5.5% to reach USD 60.3 Billion. Loans to deposits ratio slightly increased to stand at 35.8% at end of December 2017 up from 35.2% in 2016.
The dollarization ratio of deposits increased in 2017 to reach 68.7% compared to 65.8% in 2016. The dollarization of loans, on the other hand, witnessed a drop in 2017 reaching 70.9% down from 72.6% in 2016.

**USD Billion** — **As at December 31**

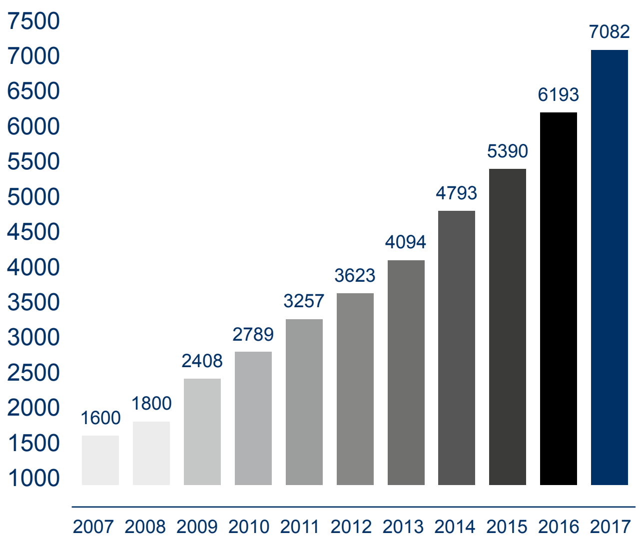
| | 2017 | 2016 | % Growth |
|---|---|---|---|
| Total assets | 219.9 | 204.3 | 7.6% |
| Total deposits | 168.7 | 162.5 | 3.8% |
| o/w in LBP | 52.7 | 55.5 | -5.0% |
| o/w in FC | 116.0 | 107.0 | 8.4% |
| Total loans | 60.3 | 57.2 | 5.5% |
| o/w in LBP | 17.5 | 15.7 | 11.5% |
| o/w in FC | 42.8 | 41.5 | 3.1% |
| Equity | 19.1 | 18.3 | 4.9% |
| Dollarization of deposits (%) | 68.7% | 65.8% | + 290 BPS |
| Dollarization of loans (%) | 70.9% | 72.6% | - 170 BPS |
| Loans/Deposit Ratio (%) | 35.8% | 35.2% | + 60 BPS |
| Deposits/Assets (%) | 76.7% | 79.5% | - 280 BPS |
| Equity/Assets Ratio (%) | 8.7% | 8.9% | - 23 BPS |

Source: BDL, ABL

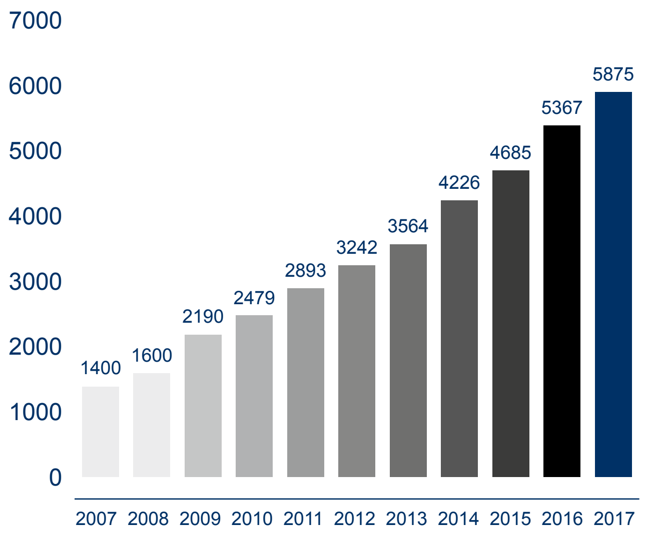
## The Bank’s Growth

Between 2007 and 2017, LGB BANK managed to achieve a steady and continuous growth in all main financial indicators.

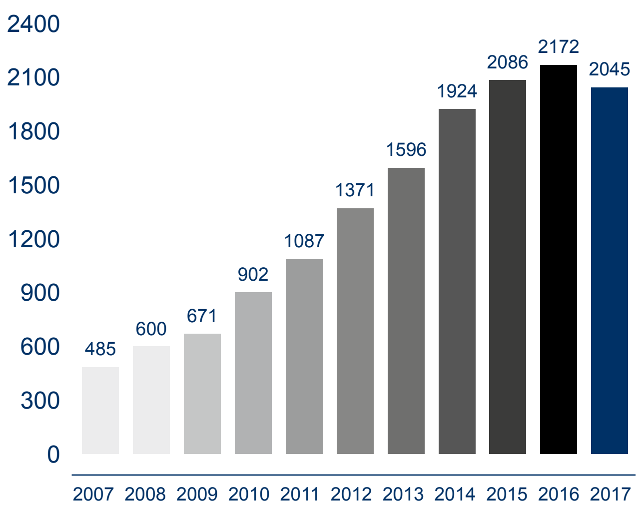
**/// TOTAL ASSETS in Billions of LBP**
During the period of 2007-2017, the total assets of the Bank increased from LBP 1,600 billion (USD 1,061 million) as of December 2007 to LBP 7,082 billion (USD 4,698 million) as of December 2017, reflecting a remarkable growth of 343%.



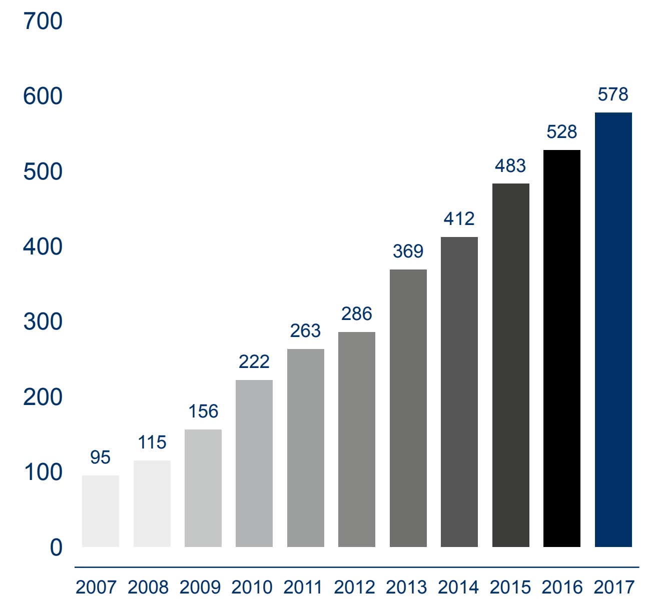

**/// CUSTOMERS’ DEPOSITS in Billions of LBP**
The growth in the Bank’s assets during the period of 2007-2017 reflected a similar growth in Customers’ Deposits which increased by 320% from LBP 1,400 billion (USD 929 million) as of December 2007 to LBP 5,875 billion (USD 3,897 million) as of December 2017.




**/// LOANS & ADVANCES in Billions of LBP**
The Bank (intentionally decreased - successfully grew) its commercial and retail lending portfolio. Accordingly, Loans & Advances to customers increased from LBP 485 billion in 2007 (USD 322 million) to reach LBP 2,045 billion (USD 1,357 million) as of December 2017, reflecting a growth of 322%.




**/// EQUITY in Billions of LBP**
The increase in Equity from LBP 95 billion in 2007 (USD 63 million) to LBP 578 billion in 2017 (USD 383 million) reflected a growth of 508%.




## The Bank’s Performance

Despite the difficult aftermath of the recent turmoil, 2017 was another successful year for LGB BANK. The Bank maintained a strong performance where total assets increased by 14.4% to reach LBP 7,082 billion and customers’ deposits rose by 9.5% to stand at LBP 5,875 billion. The Bank’s loan portfolio decreased by 5.8% to reach LBP 2,045 billion in 2017. Moreover, shareholders’ equity rose by 9.5% to stand at LBP 578 billion. Net income witnessed an increase of 12.8% to reach LBP 60 billion with a stable ratio for Return on Average Assets (ROAA) accounting for 1% in 2016 & 2017, as well as a steady ratio for Return on Average Equity (ROAE) declared at 10.9% in 2017 compared to 10.6% in 2016.

**/// 1. Profitability**
Profitability for the period ending on December 31st, 2016 and 2017 was as follows:

**In millions of LBP** — **As at December 31**

| | 2017 | 2016 | Amount | Growth % |
|---|---|---|---|---|
| Net Income | 60,290 | 53,425 | 6,865 | 12.8 |
| Net Interest Income | 72,676 | 77,222 | -4,546 | -5.9 |
| Net Fees and Commission Income | 13,786 | 14,167 | -381 | -2.7 |
| Net Non-Interest Income | 72,800 | 48,306 | 24,494 | 50.7 |
| Net Operating Income | 134,372 | 114,968 | 19,404 | 16.9 |
| Total Operating Expenses | 55,042 | 50,880 | 4,162 | 8.2 |

**1.1 Net Interest Income**
The decrease in net interest income in 2017 of LBP 4.6 billion, or 5.9% to LBP 72.7 billion compared to LBP 77.2 billion in 2016, was primarily driven by higher interest expenses on deposits from customers, mainly driven by strong client activity and increased client balances. Also contributing to the increase were favorable increase in interest income by 11.8% and an unfortunate increase in interest expenses by 17.6% in 2017.

**Breakdown of Interest and Similar Income**

**In millions of LBP** — **As at December 31**

| | 2017 | 2016 |
|---|---|---|
| Interest received from investments securities | 126,195 | 158,929 |
| Interest received from loans and advances | 117,362 | 129,014 |
| Interest received from banks and financial institutions | 107,607 | 26,040 |
| Interest received from related parties | 120 | 167 |
| **TOTAL** | **351,284** | **314,150** |

**Breakdown of Interest and Similar Expense**

**In millions of LBP** — **As at December 31**

| | 2017 | 2016 |
|---|---|---|
| Interest paid on deposits from customers | 267,299 | 230,515 |
| Interest paid on banks and financial institutions | 3,911 | 2,595 |
| Interest paid to banks under repurchase agreements | 6,864 | 3,011 |
| Interest paid on related parties’ deposits | 534 | 807 |
| **TOTAL** | **278,608** | **236,928** |

### 1.2 Net Fees and Commissions Income

A decrease in loan services and trade finance business in 2017 resulted in a 2.7% decrease in net fees and commissions income, compared to a 5.9% decrease in 2016.

| In millions of LBP | As at December 31 | |
|---|---|---|
| | 2017 | 2016 |
| **Fee and commission income** | | |
| Credit related fees and commissions | 7,040 | 6,643 |
| Trade Finance | 4,049 | 4,657 |
| General banking transactions | 2,826 | 2,717 |
| Electronic banking | 741 | 765 |
| Other services | 46 | 49 |
| | **14,702** | **14,831** |
| **Fee and commission expense** | | |
| Correspondents' accounts | -916 | -664 |
| **NET FEE AND COMMISSION INCOME** | **13,786** | **14,167** |

### 1.3 Net Non-Interest Income

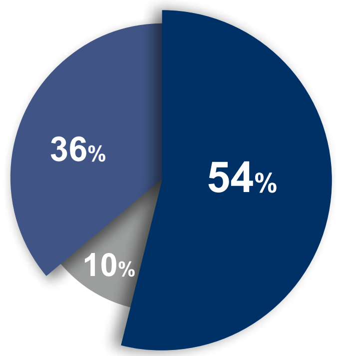
Non-interest income increased by 50.7% from LBP 48.3 billion in 2016, up to LBP 72.8 billion in 2017.This is mainly due to the increase in net gain on financial investments by 167.8% in 2017 from LBP 18.3 billion in 2016 to LBP 48.9 billion in 2017.

| In millions of LBP | As at December 31 | |
|---|---|---|
| | 2017 | 2016 |
| Net fees and commissions | 13,786 | 14,167 |
| Net trading income | 7,550 | 13,638 |
| Net gain on financial investments | 48,476 | 18,259 |
| Other operating incomes | 2,988 | 2,242 |
| **TOTAL** | **72,800** | **48,306** |

### 1.4 Net Operating Income

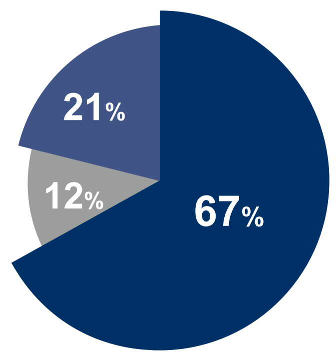
Net Operating Income registered an increase of 16.9% from LBP 115 billion in 2016, to LBP 134.4 billion in 2017, where the total operating expenses registered an increase of 8.2%, going up from LBP 50.9 billion in 2016, to LBP 55 billion in 2017.

**Net Operating Income Breakdown 2017**




Net Interest Income
Net Fee And Commission Income
Other Income

**Net Operating Income Breakdown 2016**




Net Interest Income
Net Fee And Commission Income
Other Income

**Breakdown of Total Operating Expenses**

| In millions of LBP | As at December 31 | |
|---|---|---|
| | 2017 | 2016 |
| Personnel expenses | 33,622 | 29,745 |
| Depreciation of property and equipment | 3,859 | 3,504 |
| Other operating expenses | 17,561 | 17,631 |
| **TOTAL** | **55,042** | **50,880** |

### /// 2. Sources and Uses of Funds

| In millions of LBP | | | As at December 31 | |
|---|---|---|---|---|
| | 2017 | 2016 | Amount | Growth % |
| Total assets | 7,082,117 | 6,192,588 | 889,529 | 14.4 |
| Customers' deposits | 5,874,637 | 5,367,228 | 507,409 | 9.45 |
| Loans and advances to customers (net) | 2,045,368 | 2,171,898 | -126,530 | -5.83 |
| Security portfolio | 1,524,793 | 2,305,632 | -780,839 | -33.87 |
| Total equity | 578,173 | 527,923 | 50,250 | 9.52 |
| Net income for the year | 60,290 | 53,425 | 6,865 | 12.85 |
| Dollarization of deposits | 65.1% | 61.6% | 0 | 5.68 |
| Dollarization of loans | 76.7% | 72.5% | 0 | 5.79 |

### 2.1 Sources of Funds

Similar to all Lebanese banks, LGB BANK's main source of funds is Customers' Deposits, which accounted for 83% of its overall funding sources in 2017 compared to 86.7% in 2016. Shareholders' Equity accounted for 8.2% in 2017 compared to 8.5% in 2016.

**Breakdown of Funding Sources**

| In millions of LBP | | | | | As at December 31 | |
|---|---|---|---|---|---|---|
| | 2017 | % | 2016 | % | Amount | Growth % |
| Customers' Deposits | 5,874,637 | 83.0 | 5,367,228 | 86.7 | 507,409 | 9.5 |
| Shareholders' Equity | 578,173 | 8.2 | 527,923 | 8.5 | 50,250 | 9.5 |
| Banks Under Repo agreements | 199,801 | 2.8 | 90,973 | 1.5 | 108,828 | 119.6 |
| Banks and Financial Institutions | 51,305 | 0.7 | 58,518 | 0.9 | -7,213 | -12.3 |
| Other Liabilities | 112,429 | 1.6 | 109,443 | 1.8 | 2,986 | 2.7 |
| Due to Central Banks | 265,772 | 3.8 | 38,503 | 0.6 | 227,269 | 590.3 |
| **TOTAL** | **7,082,117** | **100** | **6,192,588** | **100** | **889,529** | **14** |

### 2.1.1 Customers' Deposits

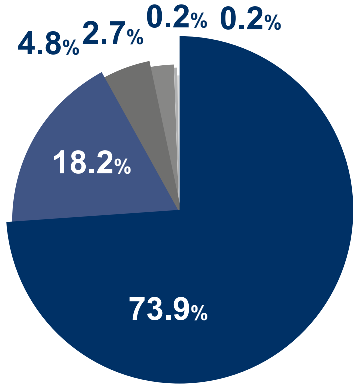
Constituting the main funding source, Customers' Deposits recorded a continuous growth over the years, reaching LBP 5,875 billion as of December 31, 2017 and representing an increase of 9.5% in comparison to LBP 5,367 billion on December 31, 2016.

**Deposit Distribution by Type**

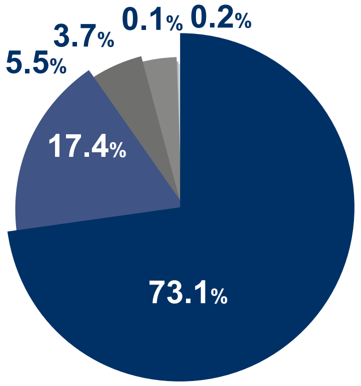
**In millions of LBP** **As at December 31**

| | 2017 | % | 2016 | % | Amount | Growth % |
|---|---|---|---|---|---|---|
| Sight Deposits | 284,777 | 4.8 | 292,647 | 5.5 | -7,870 | -2.7 |
| Time Deposits | 1,068,260 | 18.2 | 935,178 | 17.4 | 133,082 | 14.2 |
| Saving Accounts | 4,339,216 | 73.9 | 3,922,815 | 73.1 | 416,401 | 10.6 |
| Credit Accounts Against Debit Accounts | 161,351 | 2.7 | 200,717 | 3.7 | -39,366 | -19.6 |
| Margin & Collateral Accounts | 9,866 | 0.2 | 6,757 | 0.1 | 3,109 | 46.0 |
| Related Parties Account | 11,167 | 0.2 | 9,114 | 0.2 | 2,053 | 22.5 |
| **TOTAL** | **5,874,637** | **100** | **5,367,228** | **100** | **507,409** | **9.5** |

**Distribution by Type 2017**




**Distribution by Type 2016**



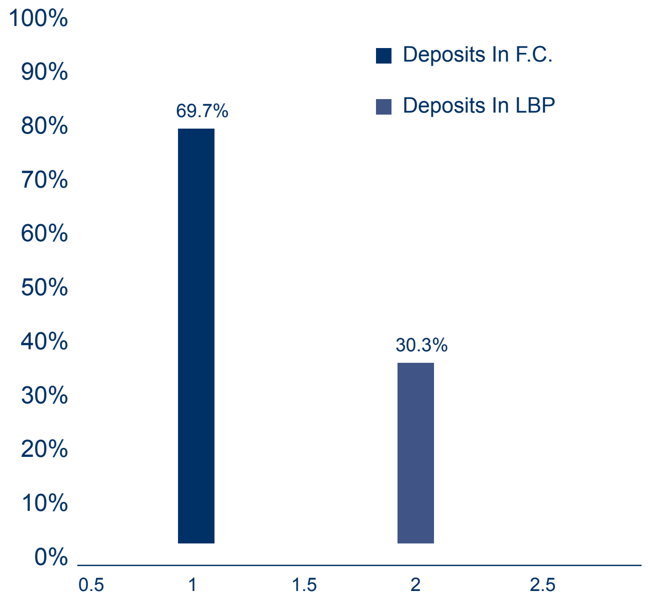

Saving Accounts · Time Deposits · Sight Deposits · Credit Account Against Debit Accounts · Margin & Collateral Accounts · Related Parties Accounts

Saving Accounts · Time Deposits · Sight Deposits · Credit Account Against Debit Accounts · Margin & Collateral Accounts · Related Parties Accounts

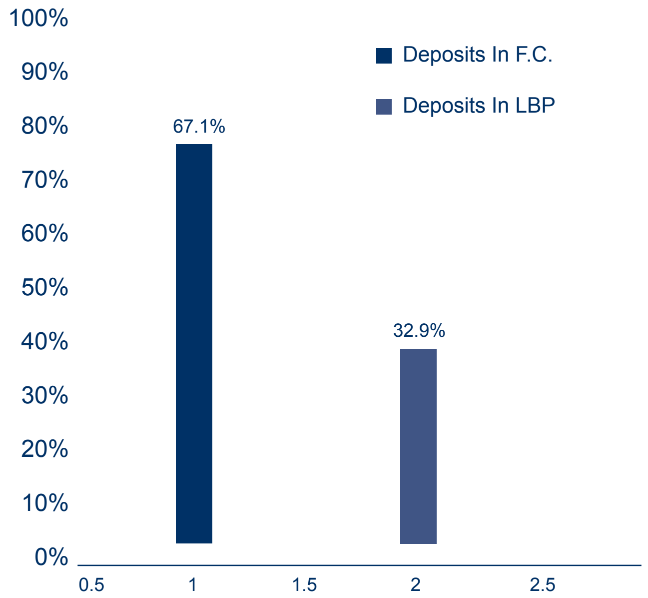
**Deposit Distribution by Currency**

The breakdown of deposits' growth indicates that deposits denominated in LBP increased by 0.7% from 2016 to 2017 compared to those denominated in foreign currencies which increased by 13.8%. The deposits denominated in foreign currencies to total deposits slightly increased from 67.1% as of December 31st, 2016 compared to 69.7% as of December 31st, 2017. This has led to a rise by approximately 2.6%.

**Distribution by Currency 2017**




**Distribution by Currency 2016**




### 2.1.2 Shareholders' Equity

The Bank's current equity profile is mainly composed of supportive, core shareholders maintaining the Bank's policy of retaining full earnings. These earnings have served to reinforce the capital base over the previous years. Total equity increased by 9.5% year on year to reach USD 383.5 million at the end of 2017 compared to USD 350.2 million at the end of 2016, contributing to nearly 8.2 % of total assets in 2017 and 8.5% 2016. The increase in equity of year 2017 is driven by the retention of profits after dividend distribution of preferred shares amounting to USD 33.3 million. This measure falls in line with the Bank's strategy of growing organically and at a steady pace.

### 2.2 Uses of Funds

Maintaining high asset quality and adequate liquidity remains one of the Bank's fundamental priorities. Loans and Advances to customers accounted for 28.9% from total assets in 2017 in comparison to 35.1% in 2016, while Loans to Deposit ratio decreased from 40.5% in 2016 to 34.8% in 2017, as per the Bank's lending policy. The share of cash and balances with the Central Bank recorded an increase from 16.8% in 2016 to 42.1% in 2017. The shares of Security Portfolio decreased from 37.2% in 2016 & to 21.5% in 2017. Moreover the Bank's total exposure to the Lebanese Government decreased from 20.6% in 2016 to 14.6% in 2017.

**In millions of LBP** **As at December 31**

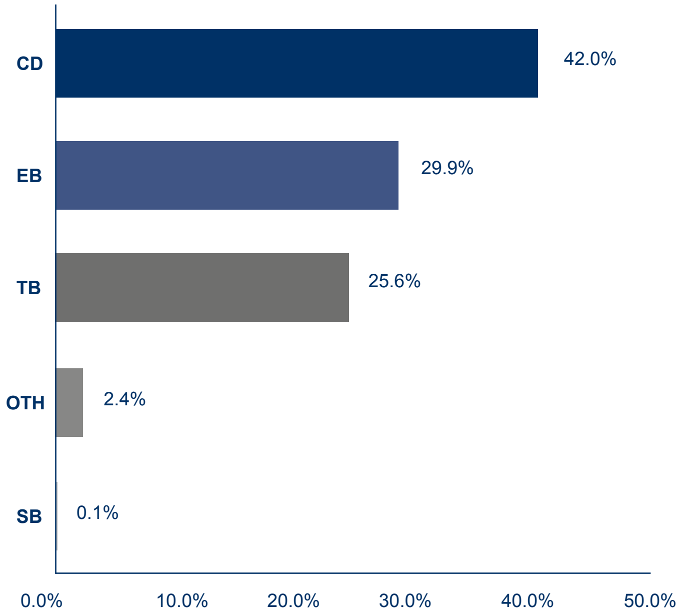
| | 2017 | % | 2016 | % | Amount | Growth % |
|---|---|---|---|---|---|---|
| Cash and Balances with Central Bank | 2,984,201 | 42.1 | 1,039,759 | 16.8 | 1,944,442 | 187.0 |
| Banks and Financial Institutions | 380,676 | 5.4 | 526,177 | 8.5 | -145,501 | -27.7 |
| Loans to banks and financial institutions | 4,011 | 0.1 | 4,964 | 0.1 | -953 | -19.2 |
| Security Portfolio | 1,524,793 | 21.5 | 2,305,632 | 37.2 | -780,839 | -33.9 |
| Loans and Advances to Customers | 2,045,368 | 28.9 | 2,171,898 | 35.1 | -126,530 | -5.8 |
| Other Assets | 143,068 | 2.0 | 144,158 | 2.3 | -1,090 | -0.8 |
| **TOTAL** | **7,082,117** | **100** | **6,192,588** | **100** | **889,529** | **14** |

### 2.2.1 Security Portfolio

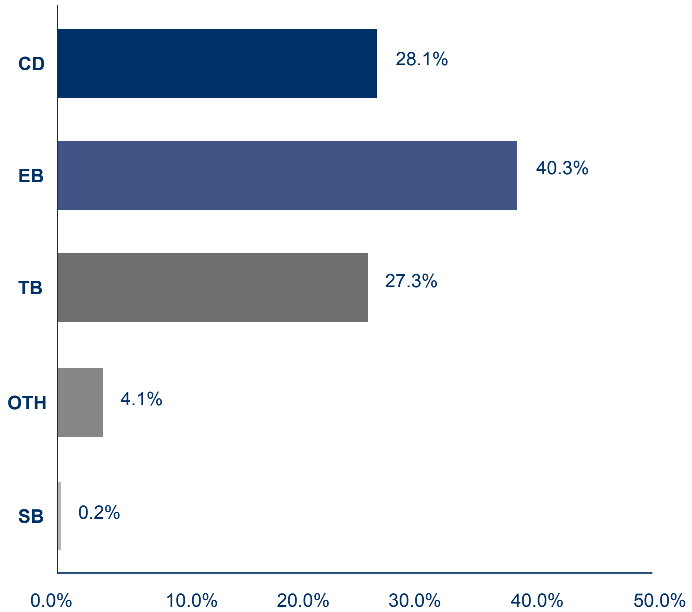
**In millions of LBP** **As at December 31**

| | 2017 | % | 2016 | % | Amount | Growth % |
|---|---|---|---|---|---|---|
| Treasury Bills | 415,991 | 27.3 | 589,224 | 25.6 | -173,233 | -29.4 |
| Lebanese Government Bonds | 614,107 | 40.3 | 689,624 | 29.9 | -75,517 | -11.0 |
| Certificate of Deposits issued by the Central Bank Of Lebanon | 429,123 | 28.1 | 967,451 | 42.0 | -538,328 | -55.6 |
| Subordinated Bonds | 3,027 | 0.2 | 3,027 | 0.1 | 0 | 0.0 |
| Other Investments | 62,545 | 4.1 | 56,306 | 2.4 | 6,239 | 11.1 |
| **TOTAL** | **1,524,793** | **100** | **2,305,632** | **100** | **-780,839** | **-34** |

**Distribution by Type 2017**




**Distribution by Type 2016**




**In millions of LBP** **As at December 31**

| | FVTPL | % | Fair Value | % | Amortized Cost | % | Total | 2017 % |
|---|---|---|---|---|---|---|---|---|
| Treasury Bills | - | - | - | - | 415,991 | 28.4 | 415,991 | 27.3 |
| Lebanese Government Bonds | - | - | - | - | 614,107 | 42.0 | 614,107 | 40.3 |
| Certificate of Deposits issued by the Lebanese Government | - | - | - | - | 429,123 | 29.3 | 429,123 | 28.1 |
| Subordinated Bonds | - | - | - | - | 3,027 | 0.2 | 3,027 | 0.2 |
| Others | 56,225 | 100 | 6,320 | 100 | - | - | 62,545 | 4.1 |
| **TOTAL** | **56,225** | **100** | **6,320** | **100** | **1,462,248** | **100** | **1,524,793** | **100** |
| **Per Cent to Total** | | **3.7** | | **0.4** | | **63** | | **100** |



**In millions of LBP** **As at December 31**

| | FVTPL | % | Fair Value | % | Amortized Cost | % | Total | 2016 % |
|---|---|---|---|---|---|---|---|---|
| Treasury Bills | - | - | - | - | 589,224 | 26.2 | 589,224 | 25.6 |
| Lebanese Government Bonds | - | - | - | - | 689,624 | 30.7 | 689,624 | 29.9 |
| Certificate of Deposits issued by the Lebanese Government | - | - | - | - | 967,451 | 43.0 | 967,451 | 42.0 |
| Subordinated Bonds | - | - | - | - | 3,027 | 0.1 | 3,027 | 0.1 |
| Others | 49,986 | 100 | 6,320 | 100 | - | - | 56,306 | 2.4 |
| **TOTAL** | **49,986** | **100** | **6,320** | **100** | **2,249,326** | **100** | **2,305,632** | **100** |
| **Per Cent to Total** | | **2.2** | | **0.3** | | **97.6** | | **100** |

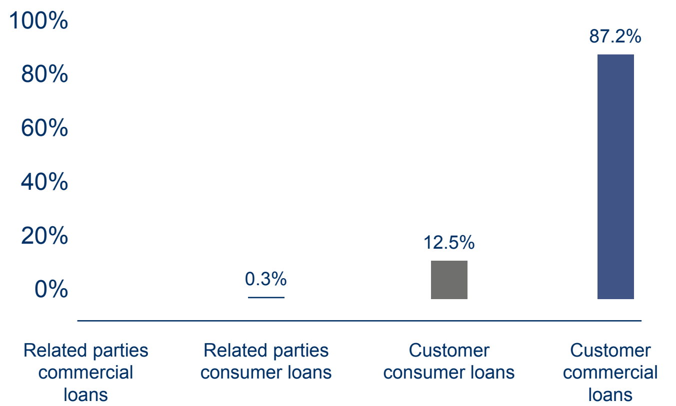
### 2.2.2 Net Loans and Advances to Customers

The “Loans and Advances to Customers” portfolio witnessed a decrease of 5.9% in 2017, reaching LBP 2,045 billion compared to LBP 2,172 billion in 2016. Following the Bank’s lending policy, the Bank slightly decreased its “Loan to Deposit Ratio”, which stood at 34.8% at the end of 2017 compared to 40.5% at the end of 2016.

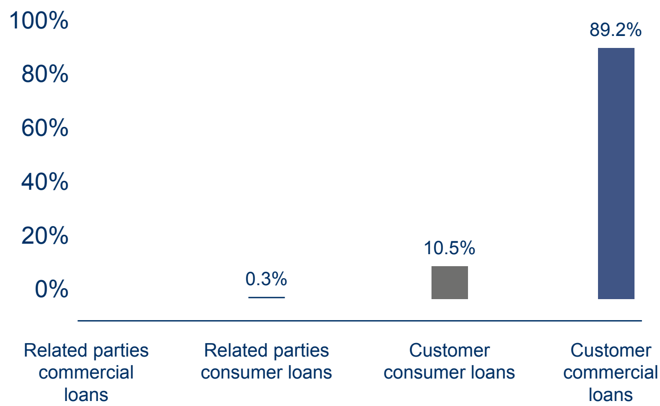
**In millions of LBP** **As at December 31**

| | 2017 | % | 2016 | % | Amount | Growth % |
|---|---|---|---|---|---|---|
| **Net Loans and Advances to Customers** | **2,038,666** | **99.7** | **2,165,502** | **99.7** | **-126,836** | **-5.9** |
| Corporate Loans | 1,783,571 | 87.2 | 1,936,940 | 89.2 | -153,369 | -7.9 |
| Retail Consumer Loans | 255,095 | 12.5 | 228,562 | 10.5 | 26,533 | 11.6 |
| **Net Loans and Advances to Related Parties** | **6,702** | **0.3** | **6,396** | **0.3** | **306** | **4.8** |
| Corporate Loans | 762 | 0.0 | 688 | 0.0 | 74 | 10.8 |
| Retail Consumer Loans | 5,940 | 0.3 | 5,708 | 0.3 | 232 | 4.1 |
| **TOTAL** | **2,045,368** | **188** | **2,171,898** | **100** | **-126,530** | **-5.8** |

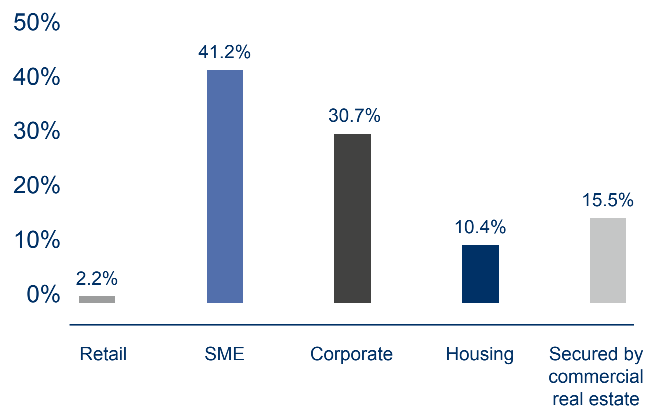
**Distribution by Type 2017**



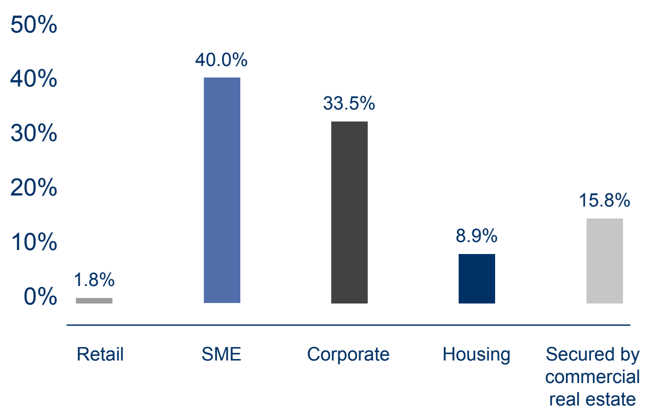

**Distribution by Type 2016**



**Breakdown by Type 2017**




**Breakdown by Type 2016**




## RISK MANAGEMENT

LGB BANK's Risk Management framework provides a robust and consistent approach to Risk Management across the Bank and is a core component of the Bank's Internal Governance framework. The Bank has a well-established risk governance structure, with an active and engaged Board of Directors supported by an experienced senior management team and a centralized Risk Management function that is independent of business lines.

The Board of Directors, either directly or through related committees, ensures that decision-making is aligned with the Bank's strategies and risk appetite. The Board receives regular updates on key risks of the Bank – including periodic comprehensive summary of the Bank's risk profile and performance of the portfolio against defined goals, which is also presented to the Board Risk Committee – and approves key risk policies, limits, strategies, and risk appetite.

The Chief Risk Officer (CRO) is responsible for Risk Management under the oversight of the Board Risk committee. The CRO, who oversees the Risk Management division of the Bank, has direct access to the Board Risk Committee.

The Bank's Risk Management framework is subject to constant evaluation to ensure that it meets the challenges and requirements of the global markets in which the Bank operates, including regulatory standards and industry best practices. It consists of three key elements: Risk Governance, Risk Appetite, and Risk Management Techniques.

The Bank aims to ensure that its risk profile remains within the overall risk appetite framework, as approved by the Bank's Board of Directors.

In 2018, LGB's Risk Management focus remains to strengthen its resilience against hazardous risks such as cyber, compliance and other potential risks.

**/// IFRS 9 PREPARATION**

In preparation of the implementation of IFRS 9, LGB BANK exerted significant efforts in preparing the infrastructure for Expected Credit Loss (ECL) calculation on the level of its financial assets. This exercise entailed developing a well-elaborated methodology for the estimation of Probability of Default (PD), Loss Given Default (LGD), and Exposure at Default (EAD) for the different financial assets held at the Bank. The Risk Management Division, in collaboration with various departments at the Bank, namely the IT, Accounting, Credit and Treasury Departments, successfully developed the IFRS 9 framework and initiated the periodic reporting required to regulatory authorities.

**/// RECOVERY PLAN**

Following the implementation of BCCL circular 294, requesting Banks operating in Lebanon to put forth a recovery plan that enables them to face potential difficulties and be able to restore their financial stability within a set timeline, LGB BANK



developed its recovery plan document in line with its strategic plan, risk appetite, risk management practices and stress testing methodologies and covering its core indicators including Early Warning Indicators (EWIs) and "Triggers Levels".

## CREDIT RISK

The Board of Directors reviews and approves the Bank's credit risk strategy and policy. The objective of the credit risk strategy is to ensure that target markets and products' offerings are well defined and the risk parameters for the portfolios are clearly specified.

Risk Management develops the credit risk management framework and policies that detail the delegation of authority for granting credit, the credit risk rating architecture and associated parameter estimates, and the calculation of the allowance for credit losses.

Credit Risk Management regularly reviews the various segments of the credit portfolio on an enterprise-wide basis to assess the impact of economic trends or specific events on the performance of the portfolio and to determine whether corrective action is required. The results of these reviews are reported to the Risk Committee and, when significant, to the Board.

Stress testing is conducted regularly as a supplementary tool to assess resilience to adverse market conditions and to act upon if mitigating actions are deemed necessary. Stress testing framework helps ensure our portfolio is not overly exposed to extreme market events. Stress tests and their results are reviewed by the Board Risk Committee and potential Management actions are proposed if necessary.

## MARKET RISK

The Board of Directors reviews and approves market risk policies and limits. The Bank's Asset and Liability Committee (ALCO) and Market Risk Management oversee the application of the framework set by the Board, and monitor the Bank's market risk exposures and activities.

Risk Management provides independent oversight of all significant market risks, supporting the ALCO with thorough analysis, quantification and recommendation regarding new investments and products.

The applied market risk measurement methodologies support risk quantification, scenario analysis and stress testing, for the range of different types of market risks exposed by the Bank. Various scenarios are performed to take into account changes in the operating environment in Lebanon and the region.

## LIQUIDITY RISK

The Bank supports a strong liquidity risk management culture and ensures association to the Bank's strategic objectives while taking into consideration all supervisory circulars and Basel guidelines. The Risk Management division is responsible for the oversight and validation of the Bank's liquidity risk framework, limits, reporting and funding related issues.

Stress testing and scenario analysis play a central role in the Bank's liquidity Risk Management framework and is considered as part of its liquidity monitoring, a continuous update of its Contingency Funding Plan, which incorporates an assessment of asset liquidity under various stress scenarios.

In terms of Liquidity coverage ratio and pursuant to BDL circular 145 and BCCL circular 295, used for measuring short term liquidity coverage (over 30 days), LGB BANK periodically computes the LCR for each significant currency and exhibits comfortable levels well above the required 100% ratio in each currency. Moreover, LGB BANK applies additional scenarios in the LCR exercise such as calculating the net cash outflow for 90 days instead of 30 days.

## OPERATIONAL RISK

Operational Risk Management is at the core of the Bank's operations - integrating Risk Management practices into processes, systems and cultures. As a pro-active partner to senior management, the value of Risk Management lies in supporting and challenging the later to align the business control environment with the Bank's strategy.

The three lines of defense model help to ensure proper accountability and clearly define the roles and responsibilities for Operational Risk Management. The first line of defense is the business unit, who owns the risks in their businesses and operations. The second line of defense is led by an Operational Risk department within the Risk Management division, with support from control functions across the Bank. The third line of defense is the Internal Audit.

LGB BANK has implemented an operational risk umbrella that encompasses all aspects of potential risks - bank protection, fraud prevention, key risk indicators, capture of operational loss data, business line risk oversight and new products and initiatives for data security.

## INFORMATION SECURITY

LGB BANK has implemented an information security Management System following best practices and ISO 27001:27005 standards.

The Information Security department, responsible for enhancing the information Security program, manages the development, implementation, and enforcement of information systems' security polices and related recommended guidelines, operating procedures and technical standards, as well as ensures appropriate risk mitigation and control process for security incidents which are operated as required.

The department also provides direction and guidance on safeguarding the confidentiality, integrity and availability of LGB BANK's information and computing assets, thus conducting security awareness sessions and training to LGB BANK's staff. In addition, the Information Security department continuously enhances the risk management program that ensures the identification of vulnerabilities and threats to the information resources, while putting into practice countermeasures in order to reduce risk to an acceptable level, based on the value of the information resource to the organization.

LGB BANK is continually working to enhance its cybercrime resilience by investing in innovative security solutions which enhance the Bank preventive, detective and corrective controls.

Moreover, LGB BANK is constantly committed to protect the interest of its customers and to maintain a high quality of service with minimum business disruption. Several initiatives were implemented during the past year to enhance the Business continuity plan.

## OTHER RISKS

A good reputation and a positive public image is an invaluable asset to our Bank. Risk Management monitors all business activities, policies and procedures, to guarantee their compliance with legal requirements.

Reputational Risk is managed and controlled throughout the Bank by codes of conduct, governance practices and Risk Management programs, policies, procedures and training. Many relevant checks and balances are undertaken by Risk Management procedures, particularly operational risk, where reference is made to the Bank's well-established compliance program. All directors, officers and employees have a responsibility to conduct their activities in accordance with the LGB BANK Guidelines for Business Conduct.

## CAPITAL FUNDS AS PER BASEL III

The Bank conducts an annual strategic planning process, which lays out the development of its future strategic direction for its business areas. The adequacy of capital is actively managed and monitored where the primary objective of the Bank's capital management is to ensure that the Bank maintains a sufficient level of capital to exceed all regulatory requirements and to achieve a strong credit rating, while optimizing shareholders' value.

This is done through a greater focus on the Bank's own estimates of capital demand and targeted earnings through a more formalized assessment of key risks, risk bearing capacity and the use of enterprise stress testing to assess impact of capital demand, capital supply and liquidity, as a complement to economic and regulatory capital.

The targets are monitored on an ongoing basis in ALCO and Risk Committee meetings. Any projected shortfall from limits and targets is discussed together with potential mitigating strategies seeking to ensure that we remain on track. Amendments to the strategic and capital plan must be approved by the Board.

The Bank is fully compliant with Basel III Capital Guidelines and with the BDL circular no.44 and its intermediate circular no.436. The current Bank's adequate capital ratios are the result of its internal capital generation, management of the balance sheet and periodic cash injection by existing shareholders and issuance of preferred shares. Those ratios are calculated in accordance with the Standardized Approach for Credit Risk and Market Risk, the Basic Indicator Approach for Operational Risk.

## INTERNAL CAPITAL ADEQUACY ASSESSMENT PROCESS (ICAAP)

The ICAAP, performed on a yearly basis, is becoming more and more of a corner stone in setting the Bank's strategy, which includes ongoing assessment of risks and updates of measurement techniques and controls, set by the Bank for all its risks to reach the best mitigation and assessment of overall required capital to cover any unanticipated losses.

The Board and senior management are liable for incorporating capital planning and capital management into the Bank's overall management culture and approach. They ensure that the reliability of the Capital Planning Process is communicated, implemented and supported by sufficient authority and resources. The Board's main concern is to ensure that the Bank maintains an adequate level of near and longer term capital needs and capital expenditures required for the foreseeable future to exceed all regulatory requirements.

## INTERNAL AUDIT DIVISION

As an independent line of defense from management, the Internal Audit Division closely monitors all functions of LGB BANK to evaluate the adequacy, quality and effectiveness of the Bank's internal control framework, risk management and governance processes. This includes providing assurance and consulting services to the management in purpose of strengthening the Bank's control systems through adding value recommendations.

The Internal Audit Division reports functionally to the Board Audit Committee. During the year 2017, the IAD has conducted several audit assignments as per the approved Internal Audit plan. All identified material weaknesses in the internal control system were reported to the Audit Committee. The Audit Committee discussed all weaknesses identified during its periodic meetings and actively follows up on the corrective measures taken by management to ensure that identified weaknesses have been mitigated by appropriate controls to safeguard the interest of the Bank.

In line with the International Standards for the Professional Practice of Internal Auditing and the approved Internal Audit Charter the main objectives of the Internal Audit Division are:

- Identify and audit areas of high risk by performing risk assessment and preparing annual audit plan which is approved by the Audit Committee.

- Understand, analyze, evaluate, examine and recommend on the Bank's operations to provide reasonable assurance to Senior Management and the Board that Bank's business and operations are aligned with the overall Bank's goals and objectives.
- Offer sound recommendations and assist in the resolution of problems by maintaining good working relationships and being responsive to management's needs.

To achieve its objectives, the work of Internal Audit Division is distributed between three main departments:

**Head Office Audit**

The Head Office Audit Department is responsible for assessing the efficiency and effectiveness of LGB Operations covering the activities of business, operations, control and supporting functions centralized in the Head Office

**Branches Audit**

The Branches Audit Department is responsible for assessing the efficiency and effectiveness of internal controls institutionalized in different transactions conducted in LGB BANK branches.

**Information Technology Audit**

The Information Technology Audit Department is responsible for assessing the efficiency, effectiveness, security and reliability of IT operations, by mainly covering IT key general controls, reviewing the Bank's applications and reasonably ensuring compliance with international standards and best practices.

## COMPLIANCE MANAGEMENT

It is the policy of LGB BANK that the Bank and its employees must comply with all applicable laws and regulations as well as ethical standards. The Bank's activities to mitigate compliance risk should live up to the best practices in the countries in which the Bank operates.

The Compliance Function is an independent function that identifies, evaluates, advises on, monitors and reports on Bank's compliance risk, that is, the risk of legal or regulatory sanctions, financial loss or loss of reputation the Bank may suffer as a result of its failure to comply with all or any of the applicable laws, regulations, codes of conduct for employees and senior management and standards of sound practices issued by regulators.

The Management of Compliance Risk follows a Risk-Based approach where the most significant compliance risks are identified firstly, and then Compliance Managers propose controls to mitigate those risks.
The above approach covers the following independent areas:

- Money Laundering
- Financing of Terrorism
- Sanctions
- Regulatory Laws and Circulars
- Tax Evasion (FATCA and CRS)
- Cybercrime
- Data Protection Laws and Customer Rights

In each area, a three-line-of-defense mechanism has been adopted where each line is identified of having:

- 1st Line of Defense is primary responsible for the results, the execution, the compliance and effectiveness of risk management
- 2nd Line of Defense is responsible for setting policies and advising as well as objectively controlling and reporting on the execution, management, control and reporting of risks.
- 3rd Line of Defense is responsible for the independent assurance on the set-up and functioning of both lines of defenses.

**/// Compliance with AML/CFT**

LGB BANK has implemented a set of rules that apply to all Bank's activities to ensure compliance with Lebanese AML/CFT laws and regulations as well as International standards.

The Bank has in place policies and procedures for the better knowledge of the customers' activities and their expected use of Bank's products and services. This includes the following:

- Verifying customer's identity
- Gathering information about the scope and purpose of the customer relationship
- Paying attention to typical transactions and identifying suspicious ones
- Informing the FIU about any suspicious case that was not resolved

**/// Compliance with International Sanctions**

The Central Bank of Lebanon has issued regulations asking Lebanese Banks to comply with rules and regulations of the countries of correspondent banks with whom a Lebanese bank has a banking relationship.

Having, the above legal framework in mind, LGB BANK pays specific attention to sanctions imposed by the UN, US and EU.

LGB BANK, through the use of technology and third parties, has various processes in place to ensure compliance with international financial sanctions, including restrictions related to payments that involve certain countries, individuals, entities, vessels and products.

**/// Compliance with Tax Evasion Initiatives**

LGB BANK fully understands and adheres to International efforts to fight tax evasion. The Bank has in place policies and procedures to execute what is required under the FATCA Law and the CRS initiative by the OECD.

**/// Compliance with Local Laws and Regulations**

After The Compliance Department has compiled a full database of Lebanese regulations issued by the Central Bank and other Lebanese regulatory authorities, and in close coordination association with the Legal Department, the Compliance Department implements the sets off monitoring of new, updated as well as prospective Laws and Regulations applicable to the Bank and Memos by all regulatory Bodies in Lebanon and countries where the Bank has presence in.

The above mentioned is monitoring comprises of: Receiving, Analyzing, Assuring Compliance with Laws and Regulations then Testing and Reporting Bank's Compliance to Management.

## TRANSPARENCY AND DISCLOSURES

In an endeavor to further strengthen its corporate governance standards and enhance transparency and disclosure in its financial reports, the Bank has adopted one of the strongest global standards of transparency in financial reporting, the International Financial Reporting Standards (IFRS) as certified by the International Accounting Standards Board.
The Board directs the process of disclosure and communication with stakeholders, to ensure that they are fair, transparent, comprehensive and timely. These disclosures include the Bank's profile, statements of its vision and mission, strategy and objectives as well as its financial statements.
The appropriate financial and practical information is disclosed through our main shareholders, annual report, website, brochures, newsletters as well as regular announcements in the media.

## SOCIAL RESPONSIBILITY PROGRAMS

LGB BANK plays a dynamic role in supporting and sponsoring various local social and community initiatives and programs that are aligned with the Bank's business and corporate social responsibility communication strategy. LGB BANK is committed to support and endorse Lebanese non-profit associations and community institutions that address different humanitarian and social issues in Lebanon.

# 07

# Auditors' Report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## Independent Auditors' Report

To the shareholders of
LEBANON & GULF BANK S.A.L.

### Qualified Opinion

We have audited the separate financial statements of Lebanon & Gulf Bank S.A.L. (the "Bank"), which comprise the separate statements of financial position as at 31 December 2017, and the separate statements of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and notes to the separate financial statements, including significant accounting policies and other explanatory information.

In our opinion, except for the effects of the matters described in the *"Basis for Qualified Opinion"* section of our report, the accompanying separate financial statements present fairly, in all material respects, the separate financial position of the Bank as at 31 December 2017, and its separate financial performance and its separate cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

### Basis for Qualified Opinion

As disclosed in note 16 to the separate financial statements, during the year ended 31 December 2016, the Bank did not recognise in its separate statement of profit or loss and other comprehensive income an amount of LBP 32,292 million (net of tax) in gains realised from certain transactions on financial instruments with the Central Bank of Lebanon. The Bank recognised this amount under "Deferred revenues" within "Other liabilities" in compliance with Central Bank of Lebanon's Intermediate Circular number 446 dated 30 December 2016. Deferred revenue amounts to LBP 15,212 million as at 31 December 2017 (2016: LBP 32,292 million). Furthermore, as disclosed in note 17 to the separate financial statements, the Bank recorded excess provisions amounting to LBP 37,080 million (2016: LBP 20,000 million) under "Provisions for risks and charges" in order to comply with the provisioning requirements of Central Bank of Lebanon's Intermediate Circular number 439 dated 8 November 2016. The Bank's accounting for the above-mentioned transactions departs from the requirements of International Financial Reporting Standards (IFRSs).This caused us to qualify our audit opinion on the separate financial statements relating to the years ended 31 December 2017 and 31 December 2016.Had the Bank properly accounted for these transactions, events and conditions, in accordance with International Financial Reporting Standards, the effects on the separate financial statements would have been as follows:

- No effect on the net income for the year ended 31 December 2017 as the additional excess provision amounting to LBP 17,080 million was directly transferred from the "Deferred revenues" account and did not impact the profit or loss for the year (Net income for the year ended 31 December 2016 would have increased by LBP 52,292 million through an increase in "Net gain from sale of financial assets at amortised cost" by LBP 37,991 million, a decrease in "Provisions for risks and charges" by LBP 20,000 million and an increase in "Income tax expense" by LBP 5,699 million);

## Independent Auditors' Report (continued)

### Basis for Qualified Opinion (continued)

- Total liabilities as at 31 December 2017 would have decreased by LBP 52,292 million through a decrease in "Deferred revenues" (reflected under "Other liabilities") by LBP 15,212 million and a decrease in "Provisions for risks and charges" by LBP 37,080 million (Total liabilities would have decreased by LBP 52,292 million for the year ended 31 December 2016:, through a decrease in "Deferred revenues" (reflected under "Other liabilities") by LBP 32,292 million and a decrease in "Provisions for risks and charges" by LBP 20,000 million); and

- Equity as at 31 December 2017 would have increased, through an increase in retained earnings by LBP 52,292 (31 December 2016: equity would have increased through an increase in net income LBP 52,292 million).

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditors' Responsibilities for the Audit of the Separate Financial Statements* section of our report. We are independent of the Bank in accordance with the *International Ethics Standards Board for Accountants Code of Ethics for Professional Accountants (IESBA Code)* together with the ethical requirements that are relevant to our audit of the separate financial statements in Lebanon, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified opinion.

### Other information

Other information consists of the information included in the Bank's 2017 Annual Report other than the separate financial statements and our auditors' report thereon. Management is responsible for the other information. The Bank's 2017 Annual Report is expected to be made available to us after the date of this auditors' report.

Our opinion on the separate 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 separate 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 separate financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

When we read the Annual Report, if we conclude that there is a material misstatement therein, we are required to communicate the matter to the audit committee and we will exercise professional judgement to determine whether we need to take appropriate action to seek to have the uncorrected misstatement appropriately brought to the attention of users for whom the auditors' report is prepared.

As described in the Basis for Qualified Opinion section above, the recorded excess provisions for risks and charges in the statement of financial position. When we read the Annual Report, we will consider whether the other information included in the Annual Report is also materially misstated for these matters. If we conclude that there is a material misstatement therein, we are required to communicate the matter to the audit committee and we will exercise professional judgement to determine whether we need to take appropriate action to seek to have the uncorrected misstatement appropriately brought to the attention of users for whom the auditors' report is prepared.





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Independent Auditors' Report (continued)

### Key Audit Matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the separate financial statements of the year ended 31 December 2017. In addition to the matter described in the *Basis for qualified opinion section,* we have determined the matters described below to be the key audit matters to be communicated in our report. These matters were addressed in the context of our audit of the separate financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

### Impairment of loans and advances to customers

Due to the inherently judgmental nature of the computation of impairment provisions for loans and advances, there is a risk that the amount of impairment may be misstated. The impairment of loans and advances is estimated by Management through the application of judgement and the use of subjective assumptions. Due to the significance of loans and advances and related estimation uncertainty, this is considered a key audit risk. The corporate loan portfolio generally comprises larger loans that are monitored individually by Management. The assessment of loan loss impairment is therefore based on management's knowledge of each individual borrower. This includes the analysis of the financial performance of the borrower, historic experience when assessing the likelihood of incurred losses in the portfolios and the adequacy of collateral for secure lending. However, consumer loans generally comprise much smaller value loans to a much greater number of customers. Provisions are not calculated on an individual basis, but are determined by grouping by product into homogeneous portfolios. The portfolios are then monitored through delinquency statistics, which drive the assessment of loan loss provision.

The risks outlined above were addressed by us as follows:

- For corporate customers, we tested the key controls over the credit grading process, to assess if the risk grades allocated to the counterparties were appropriate. We then performed detailed credit assessment of all loans in excess of a defined threshold and loans in excess of a lower threshold in the watch list category and impaired category together with a selection of other loans.

- Where impairment allowance was calculated on a collective basis for performing corporate loans, we tested the completeness and accuracy of the underlying loan information used in the impairment model by agreeing details to the Bank's source systems as well as re-performing the calculation of the modelled impairment allowances. For the key assumptions in the model, we assessed whether those assumptions were appropriate in the circumstances.

- For consumer loans, specific and collective impairment allowances are calculated using a simple model, which are based on a percentage of repayments due but not yet paid. We understood and critically assessed the model used and checked that no undue changes had been made in model parameters and assumptions. We tested the completeness and accuracy of data from underlying systems that is used in this model. We also re-performed the calculation of the modelled impairment allowance.

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**Responsibilities of Management and the Audit Committee for the Separate Financial Statements**

Management is responsible for the preparation and fair presentation of the separate financial statements in accordance with IFRS, and for such internal control as management determines is necessary to enable the preparation of separate financial statements that are free form material misstatement, whether due to fraud or error.

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

The audit committee is responsible for overseeing the Bank's financial reporting process.

**Auditors' responsibilities for the Audit of the Separate Financial Statements**

Our objectives are to obtain reasonable assurance about whether the separate 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 the economic decisions of users taken on the basis of these separate financial statements.

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

- Identify and assess the risks of material misstatement of the separate 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 Bank's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.



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**Auditors' responsibilities for the Audit of the Separate Financial Statements (continued)**

- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank'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 separate 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 Bank to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the separate financial statements, including the disclosures, and whether the separate financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with the 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 audit committee with a statement that we have complied with relevant ethical requirements regarding independence, and 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 audit committee, we determine those matters that were of most significance in the audit of the separate 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.

The engagement partners on the audit resulting in this independent auditor's report are Mr. Wissam Safwan for KPMG and Mr. Nehmé Semaan for BDO, Semaan, Gholam & Co.

BDO, Semaan, Gholam & Co.

KPMG

KPMG

25 April 2018
Beirut, Lebanon

# 08

# Financial Statements

**Separate statement of financial position**

| In millions of LBP | Note | 2017 | 2016 |
|---|---|---|---|
| | | As at December 31 | |
| **Assets** | | | |
| Cash and balances with Central Banks | 3 | 2,984,201 | 1,039,759 |
| Due from banks and financial institutions | 4 | 380,676 | 526,177 |
| Financial assets at fair value through profit or loss | 5 | 56,225 | 49,986 |
| Loans to banks and financial institutions | | 4,011 | 4,964 |
| Loans and advances to customers at amortized cost | 6 | 2,038,666 | 2,165,502 |
| Loans and advances to related parties at amortized cost | 7 | 6,702 | 6,396 |
| Debtors by acceptances | | 29,131 | 30,098 |
| Financial assets at amortized cost | 8 | 1,462,248 | 2,249,326 |
| Investment in a subsidiary | 9 | 6,320 | 6,320 |
| Property and equipment | 10 | 50,942 | 51,473 |
| Assets obtained in settlement of debt | 11 | 57,293 | 52,360 |
| Other assets | 12 | 5,702 | 10,227 |
| **Total assets** | | **7,082,117** | **6,192,588** |
| **Liabilities** | | | |
| Due to the Central Bank | 13 | 265,772 | 38,503 |
| Due to banks and financial institutions | 14 | 51,305 | 58,518 |
| Due to banks under repurchase agreements | 14 | 199,801 | 90,973 |
| Deposits from customers | 15 | 5,863,470 | 5,358,114 |
| Deposits from related parties | 7 | 11,167 | 9,114 |
| Engagements by acceptances | | 29,131 | 30,098 |
| Other liabilities | 16 | 37,386 | 51,497 |
| Provisions for risks and charges | 17 | 45,912 | 27,848 |
| **Total liabilities** | | **6,503,944** | **5,664,665** |
| **Equity** | | | |
| Share capital - common shares | 18 | 194,068 | 194,068 |
| Share capital - preferred shares | 18 | 18,879 | 18,879 |
| Share premium - preferred shares | 18 | 121,482 | 121,482 |
| Non distributable reserves | 19 | 112,000 | 88,560 |
| Retained earnings | 20 | 71,454 | 51,509 |
| Net results of the financial year - profit | 20 | 60,290 | 53,425 |
| **Total equity** | | **578,173** | **527,923** |
| **Total liabilities and equity** | | **7,082,117** | **6,192,588** |

The notes on pages 10 to 79 are an integral part of these separate financial statements.
The financial statements were authorised for issue on behalf of the board of directors on 25 April 2018.

**Separate statement of profit or loss and other comprehensive income**

| In millions of LBP | Note | 2017 | 2016 |
|---|---|---|---|
| | | As at December 31 | |
| Interest and similar income | 21 | 351,284 | 314,150 |
| Interest and similar expense | 21 | (278,608) | (236,928) |
| **Net interest and similar income** | | **72,676** | **77,222** |
| Fee and commission income | 22 | 14,702 | 14,831 |
| Fee and commission expense | 22 | (916) | (664) |
| **Net fee and commission income** | | **13,786** | **14,167** |
| Net gain from financial assets at fair value through profit or loss | 23 | 7,550 | 13,638 |
| Net gain from financial assets amortized cost | 24 | 48,476 | 18,259 |
| Other operating income | 25 | 2,988 | 2,242 |
| **Total operating income** | | **145,476** | **125,528** |
| Net impairment loss | 26 | (11,104) | (10,560) |
| **Net operating income** | | **134,372** | **114,968** |
| Personnel expenses | 27 | (33,622) | (29,745) |
| Depreciation of property and equipment | 10 | (3,859) | (3,504) |
| Other operating expenses | 28 | (17,561) | (17,631) |
| **Total operating expenses** | | **(55,042)** | **(50,880)** |
| Net loss on disposal of property and equipment | | (82) | (165) |
| **Profit before tax** | | **79,248** | **63,923** |
| Income tax expense | 29 | (18,958) | (10,498) |
| **Profit for the year** | | **60,290** | **53,425** |
| **Other comprehensive income** | | **–** | **–** |
| **Total other comprehensive income for the year** | | **60,290** | **53,425** |

The notes on pages 10 to 79 are an integral part of these separate financial statements.

**Separate statement of changes in equity**

**In millions of LBP** **As at December 31**

| | Note | Share capital-Common shares | Share capital-Preferred shares | Share premium -Preferred shares | Non distributable reserves | Retained earnings | Net results of the financial year - profit | Total equity |
|---|---|---|---|---|---|---|---|---|
| **Balance at 1 January 2017** | | **194,068** | **18,879** | **121,482** | **88,560** | **51,509** | **53,425** | **527,923** |
| **Transactions with owners of the Bank** | | | | | | | | |
| **Contributions and distributions** | | | | | | | | |
| Appropriation of 2016 profits | 20 | – | – | – | 23,440 | 29,985 | (53,425) | – |
| Dividends distributions | 30 | – | – | – | – | (10,040) | – | (10,040) |
| Total contributions and distributions | | – | – | – | 23,440 | 19,945 | (53,425) | (10,040) |
| **Total comprehensive income** | | | | | | | | |
| Profit for the year | | – | – | – | – | – | 60,290 | 60,290 |
| Total comprehensive income | | – | – | – | – | – | 60,290 | 60,290 |
| **Balance at 31 December 2017** | | **194,068** | **18,879** | **121,482** | **112,000** | **71,454** | **60,290** | **578,173** |
| **Balance at 1 January 2016** | | **194,068** | **18,879** | **121,482** | **66,669** | **35,269** | **46,218** | **482,585** |
| **Transactions with owners of the Bank** | | | | | | | | |
| **Contributions and distributions** | | | | | | | | |
| Appropriation of 2015 profits | 20 | – | – | – | 21,891 | 24,327 | (46,218) | – |
| Dividends distributions | 30 | – | – | – | – | (8,087) | – | (8,087) |
| Total contributions and distributions | | – | – | – | 21,891 | 16,240 | (46,218) | (8,087) |
| **Total comprehensive income** | | | | | | | | |
| Profit for the year | | – | – | – | – | – | 53,425 | 53,425 |
| Total comprehensive income | | – | – | – | – | – | 53,425 | 53,425 |
| **Balance at 31 December 2016** | | **194,068** | **18,879** | **121,482** | **88,560** | **51,509** | **53,425** | **527,923** |

The notes on pages 10 to 79 are an integral part of these separate financial statements.

**Separate statement of cash flows**

**In millions of LBP** — **As at December 31**

| | Note | 2017 | 2016 |
|---|---|---|---|
| **Operating activities** | | | |
| Profit for the year before tax | | 79,248 | 63,923 |
| Adjustments for: | | | |
| Depreciation of property and equipment | 10 | 3,859 | 3,504 |
| Provision for employees' end of service benefits | 17 | 1,039 | 675 |
| Net impairment loss | 26 | 11,104 | 10,560 |
| Net gain on disposal of assets obtained in settlement of debt | 25 | (379) | (154) |
| Net loss on disposal of property and equipment | | 82 | 165 |
| Net gain on financial assets at amortized cost | 24 | (48,476) | (18,259) |
| Net unrealized gain on financial assets at fair value through profit or loss | 23 | (3,124) | (4,189) |
| Realized gain on financial assets at fair value through profit or loss | 23 | – | (5,570) |
| Provision for structural exchange position | 17 | 26 | 87 |
| **Operating profit before working capital changes** | | **43,379** | **50,742** |
| ***Changes in operating assets and liabilities:*** | | | |
| Cash and balances with central banks | | (1,755,675) | (233,887) |
| Due from banks and financial institutions | | (13,608) | (4,898) |
| Financial assets at fair value through profit or loss | | (4,534) | 25,777 |
| Loans and advances to customers at amortized cost | | 115,732 | (95,199) |
| Loans and advances to related parties at amortized cost | | (306) | (1,231) |
| Assets obtained in settlement of debt | | (6,035) | (29,306) |
| Proceeds from disposal of assets obtained in settlement of debt | | 1,481 | 3,153 |
| Other assets | | 4,525 | (3,944) |
| Due to banks and financial institutions | | (34,700) | 27,847 |
| Deposits from customers | | 505,356 | 685,249 |
| Deposits from related parties | | 2,053 | (2,878) |
| Other liabilities | | 883 | 40,551 |
| Provisions for risks and charges | | 17,080 | 20,000 |
| **Cash (used in) from operations** | | **(1,124,369)** | **481,976** |
| Taxation paid | | (33,952) | (8,676) |
| Retirement benefits paid | 17 | (81) | (96) |
| **Net cash (used in) from operating activities** | | **(1,158,402)** | **473,204** |

The notes on pages 10 to 79 are an integral part of these separate financial statements.

**Separate statement of cash flows (continued)**

**In millions of LBP** — **As at December 31**

| | Note | 2017 | 2016 |
|---|---|---|---|
| **Investing activities** | | | |
| Financial assets classified at amortized cost | | 835,554 | (295,860) |
| Loans to banks and financial institutions | | 953 | 953 |
| Net acquisitions of property and equipment | 10 | (3,594) | (4,689) |
| Proceeds from sale of property and equipment | | 197 | 330 |
| Dividends received | 23 | 1,419 | 1,319 |
| **Net cash from (used in) investing activities** | | **834,529** | **(297,947)** |
| **Financing activities** | | | |
| Dividends paid | 30 | (10,040) | (8,087) |
| Due to banks under repurchase agreements | | 108,828 | 51 |
| Due to central bank | | 227,269 | 3,248 |
| **Net cash from (used in) financing activities** | | **326,057** | **(4,788)** |
| **Net effect of foreign exchange** | | **(13)** | **5** |
| **Increase in cash and cash equivalents** | | **2,171** | **170,474** |
| Cash and cash equivalents at 1 January | | 580,415 | 409,941 |
| **Cash and cash equivalents at 31 December** | 31 | **582,586** | **580,415** |

The notes on pages 10 to 79 are an integral part of these separate financial statements.

# 09

# Notes to the Separate Financial Statements

# 1. Basis of preparation

## 1.1 Reporting entity

Lebanon & Gulf Bank SAL (the “Bank”) is a Lebanese joint stock company incorporated in 1963 under the name of Agricultural Credit Bank. The name of the Bank was changed to Lebanon & Gulf Bank SAL in year 1980. The Bank is registered under No 43171 in the Beirut Register of Commerce and under No 94 on the banks’ list published by the Central Bank of Lebanon.

The Bank provides a full range of commercial banking activities through its headquarter located in Beirut Central District, Allenby street, Beirut, Lebanon, and its branches in Lebanon and a foreign branch in Larnaca (Cyprus).

On 14 March 2013, the Central Bank of the United Arab Emirates licensed the Bank to open a representative office in Dubai. This license is valid for 5 years. The representative office conducted its business starting from the above date.

## 1.2 Basis of accounting

The separate financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB)

**Presentation of separate financial statements**
The financial statements relate to the Bank and are presented on a non-consolidated basis. The Bank also separately prepares consolidated financial statements in accordance with IFRS. The consolidated financial statements can be obtained from Lebanon & Gulf Bank SAL registered office. Users of the separate financial statements should read them together with the Group’s consolidated financial statements for the year ended 31 December 2017 in order to obtain full information on the statement of financial position and results of operations for the Group as a whole.

The Bank presents its separate statement of financial position broadly in order of liquidity. An analysis regarding recovery or settlement within 12 months after the separate statement of financial position date (current) and more than 12 months after the separate statement of financial position date (non-current) is presented in the notes.

Financial assets and financial liabilities are offset and the net amount reported in the separate statement of financial position only when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the assets and settle the liability simultaneously. Income and expense are not offset in the income statement unless required or permitted by any accounting standard or interpretation, as specifically disclosed in the accounting policies of the Bank.

## 1.3 Functional and presentation currency

The separate financial statements are presented in Lebanese Pound (LBP) which is the functional and presentation currency of the Bank and all amounts are rounded to the nearest million (LBP million) except when otherwise indicated.

## 1.4 Use of judgements and estimates

In preparing these financial statements, management has made judgements, estimates and assumptions that affect the application of the Bank’s accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to estimates are recognised prospectively.

***A. Judgements***
Information about judgements made in applying accounting policies that have the most significant effects on the amounts recognised in the separate financial statements are included below:

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

*Business model*
In making an assessment whether a business model’s objective is to hold assets in order to collect contractual cash flows, the Bank considers at which level of its business activities such assessment should be made. Generally, a business model is a matter of fact which can be evidenced by the way business is managed and the information provided to management. However, in some circumstances it may not be clear whether a particular activity involves one business model with some infrequent asset sales or whether the anticipated sales indicate that there are two different business models.

In determining whether its business model for managing financial assets is to hold assets in order to collect contractual cash flows the Bank considers:

- management’s stated policies and objectives for the portfolio and the operation of those policies in practice;
- how management evaluates the performance of the portfolio;
- whether management’s strategy focuses on earning contractual interest revenues;
- the degree of frequency of any expected asset sales;
- the reason for any asset sales; and
- whether assets that are sold are held for an extended period of time relative to their contractual maturity.

*Contractual cash flows of financial assets*
The Bank exercises judgement in determining whether the contractual terms of financial assets it originates or acquires give rise on specific dates to cash flows that are solely payments of principal and interest on the principal outstanding and so may qualify for amortized cost measurement. In making the assessment the Bank considers all contractual terms, including any prepayment terms or provisions to extend the maturity of the assets, terms that change the amount and timing of cash flows and whether the contractual terms contain leverage.

***B. Assumptions and estimation uncertainties***
Information about assumptions and estimation uncertainties that have a significant risk of resulting in a material adjustment in the year ending 31 December 2017 is set out below in relation to the impairment of financial instruments and in the following notes in relation to other areas:

- Note 33- determination of the fair value of financial instruments with significant unobservable inputs.
- Note 17 and 32- recognition and measurement of provisions and contingencies: Key assumptions about the likelihood and magnitude of an outflow of resources.

***Fair value of financial instruments***
Where the fair values of financial assets and financial liabilities recorded on the separate statement of financial position cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The inputs to these models are derived from observable market data where possible, but where observable market data is not available, judgement is required to establish fair values. The judgements include considerations of liquidity and model inputs such as volatility for longer dated derivatives and discount rates, prepayment rates and default rate assumptions for asset backed securities. The valuation of financial instruments is described in more details in the notes.

***Impairment losses on loans and advances***
The Bank reviews its individually significant loans and advances at each statement of financial position date to assess whether an impairment loss should be recorded in the income statement. In particular, judgement by management is required in the estimation of the amount and timing of future cash flows when determining the impairment loss. In estimating these cash flows, the Bank makes judgements about the borrower’s financial situation and the net realizable value of collateral. These estimates are based on assumptions about a number of factors and actual results may differ, resulting in future changes to the allowance.

Loans and advances that have been assessed individually and found not to be impaired and all individually insignificant loans and advances are then assessed collectively, in groups of assets with similar risk characteristics, to determine whether provision should be made due to incurred loss events for which there is objective evidence but whose effects are not yet evident.

The collective assessment takes account of data from the loan portfolio (such as credit quality, levels of arrears, credit utilization, loan to collateral ratios etc.), concentrations of risks and economic data (including levels of unemployment, real estate price indices, country risk and the performance of different individual groups).

# 2. Accounting policies

## 2.1 Basis of measurement

The separate financial statements have been prepared on a historical cost basis except for the measurement at fair value of financial assets at fair value through profit or loss.

## 2.2 Changes in accounting policies

Except for the changes below, the Bank has consistently applied the accounting policies as set out in note 2.3 to all years presented in these separate financial statements.

These improvements, effective from 1 January 2017 did not have a material impact on the Bank. They include:

Disclosure Initiative (Amendments to IAS 7)

Recognition of Deferred Tax Assets for Unrealised Losses (Amendments to IAS 12)

Annual Improvements to IFRSs 2014 – 2016 Cycle (Amendments to IFRS 1, 12 and IAS 28)

- IFRS 1 First-time Adoption of IFRS
- IFRS 12 Disclosure of Interest in Other Entities
- IAS 28 Investments in Associates and Joint Venture

## 2.3 Summary of significant accounting policies

Except for the changes explained in note (2.2), the Bank has consistently applied the following accounting policies to all years presented in these separate financial statements.

**(a) Foreign currency**
***(I) Foreign currency transactions***
Transactions in foreign currencies are translated into the respective functional currencies of the Bank at the spot exchange rates at the date of the transactions.
Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated into the functional currency at the spot exchange rate at that date. Non-monetary assets and liabilities measured at fair value in a foreign currency are translated into the functional currency at the spot exchange rate at the date on which the fair value is determined. Non- monetary items that are measured based on historical cost in a foreign currency are translated using the spot exchange rate at the date of the transaction.

***(II) Foreign operations***
As at the reporting date, the assets and liabilities of overseas branches are translated into the Bank's presentation currency at the rate of exchange as at the statement of financial position date, and their income statements are translated at the weighted average exchange rates for the year. Exchange differences arising on translation are taken directly to a separate component of equity. On disposal of a foreign branch, the deferred cumulative amount recognized in equity relating to that particular foreign branch is recognized in the income statement.

**(b) Financial assets and financial liabilities**
***(I) Recognition***
The Bank initially recognises loans and advances and deposits on the date on which they are originated. All other financial instruments (including regular-way purchases and sales of financial assets) are recognised on the trade date, which is the date in which the Bank becomes a party to the contractual provisions of the instrument.

A financial asset or financial liability is measured initially at fair value plus, for an item not at FVTPL, transaction cocts that are directly attributable to its acquisition or issue.

All financial assets and liabilities are initially recognised on the trade date, i.e. the date that the Bank becomes a party to the contractual provisions of the instrument. This includes "regular way trades": purchases or sales of financial assets that require delivery of assets within the time frame generally established by regulation or convention in the market place.

***(II) Classification***
***(i) Financial assets***
The classification of financial assets depends on the basis of the entity's business model for managing the financial assets and the contractual cash flow characteristics of the financial asset. Assets are initially measured at fair value plus, in the case of a financial asset not at fair value through profit or loss, particular transaction costs. Assets are subsequently measured at amortized cost or at fair value.

An entity may, at initial recognition, irrevocably designate a financial asset as measured at fair value through profit or loss if doing so eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as an 'accounting mismatch') that would otherwise arise from measuring assets or liabilities or recognizing the gains and losses on them on different basis. An entity is required to disclose such financial assets separately from those mandatorily measured at fair value.

Financial assets that meet both of the following conditions are subsequently measured at amortized cost less any impairment loss (except for financial assets that are designated at fair value through profit or loss upon initial recognition):

• The asset is held within a business model whose objective is to hold assets in order to collect contractual cash flows; and
• The contractual terms of the instrument give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

These financial assets are initially recognised at cost, being the fair value of the consideration paid for the acquisition of the investment. All transaction costs directly attributed to the acquisition are also included in the cost of investment. After initial measurement, these financial assets are measured at amortized cost using the effective interest rate method, less allowance for impairment. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees and costs that are an integral part of the effective interest rate. The amortization is included in "Interest and similar income" in the income statement. The losses arising from impairment are recognised in the income statement in "Net impairment loss".

Although the objective of an entity's business model may be to hold financial assets in order to collect contractual cash flows, the entity need not hold all of those instruments until maturity. Thus an entity's business model can be to hold financial assets to collect contractual cash flows even when sales of financial assets occur. However, if more than an infrequent number of sales are made out of a portfolio, the entity needs to assess whether and how such sales are consistent with an objective of collecting contractual cash flows. If the objective of the entity's business model for managing those financial assets changes, the entity is required to reclassify financial assets.

Gains and losses arising from the derecognition of financial assets measured at amortized cost are reflected under "Net gain from financial assets at amortized cost" in the income statement.

Balances with central banks, due from banks and financial institutions, loans to banks and financial institutions and net loans and advances to customers and related parties – at amortized cost.

After initial measurement, "Balances with central banks", "Due from banks and financial institutions", "Loans to banks and financial institutions" and "Net loans and advances to customers and related parties" are subsequently measured at amortized cost using the Effective Interest Rate (EIR) method, less allowance for impairment. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees and costs that are an integral part of the EIR. The amortization is included in 'Interest and similar income' in the income statement. The losses arising from impairment are recognised in the income statement in "Net impairment loss".

***Financial assets at fair value through profit or loss***
Included in this category are those debt instruments that do not meet the conditions in "Financial assets at amortized cost" above, debt instruments designated at fair value through profit or loss upon initial recognition and equity instruments at fair value through profit or loss.

*Debt instruments at fair value through profit or loss*
These financial assets are recorded in the statement of financial position at fair value. Changes in fair value and interest income are recorded under "Net gain from financial assets at fair value through profit or loss" in the income statement showing separately, those related to financial assets designated at fair value upon initial recognition from those mandatorily measured at fair value.

Gains and losses arising from the derecognition of debt instruments at fair value through profit or loss are also reflected under "Net gain from financial assets at fair value through profit or loss" in the income statement showing separately, those related to financial assets designated at fair value upon initial recognition from those mandatorily measured at fair value.

*Equity instruments at fair value through profit or loss*
Investments in equity instruments are classified at fair value through profit or loss, unless the Bank designates at initial recognition an investment that is not held for trading as at fair value through other comprehensive income.

These financial assets are recorded in the statement of financial position at fair value. Changes in fair value and dividend income are recorded under "Net gain from financial assets at fair value through profit or loss" in the income statement. Gains and losses arising from de-recognition of equity instruments at fair value through profit or loss are also reflected under "Net gain from financial assets at fair value through profit or loss" in the income statement.

***(ii) Financial liabilities***
The Bank classifies all financial liabilities as subsequently measured at amortized cost using the effective interest method.
Financial liabilities measured at amortized cost consist of due to the Central Bank, due to banks and financial institutions, and deposits from customers' and related parties.

***"Due to central bank, due to banks and financial institutions, due to banks under repurchase agreements, customers' and related parties' deposits"***
After initial measurement, due to central bank, due to banks and financial institutions, due to banks under repurchase agreements, customers' and related parties' deposits are measured at amortized cost less amounts repaid using the effective interest rate method. Amortized cost is calculated by taking into account any discount or premium on the issue and costs that are an integral part of the effective interest rate method.

***(III) Day 1 profit or loss***
When the transaction price differs from the fair value of other observable current market transactions in the same instrument or based on a valuation technique whose variables include only data from observable markets, the Bank immediately recognizes the difference between the transaction price and fair value (a "Day 1" profit or loss) in the income statement. In cases where fair value is determined using data which is not observable, the difference between the transaction price and model value is only recognised in the income statement when the inputs become observable, or when the instrument is derecognised.

***(IV) Reclassification***
The Bank reclassifies financial assets if the objective of the business model for managing those financial assets changes. Such changes are expected to be very infrequent. Such changes are determined by the Bank's senior management as a result of external or internal changes when significant to the Bank's operations and demonstrable to external parties.

If financial assets are reclassified, the reclassification is applied prospectively from the reclassification date, which is the first day of the first reporting period following the change in business model that results in the reclassification of financial assets. Any previously recognised gains, losses or interest are not restated.

If a financial asset is reclassified so that it is measured at fair value, its fair value is determined at the reclassification date. Any gain or loss arising from a difference between the previous carrying amount and fair value is recognised in profit or loss. If a financial asset is reclassified so that it is measured at amortized cost, its fair value at the reclassification date becomes its new carrying amount.

***(V) Derecognition***
***(i) Financial assets***
A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognised when:

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

When the Bank has transferred its rights to receive cash flows from an asset or has entered into a pass- through arrangement, and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Bank's continuing involvement in the asset. In that case, the Bank also recognizes an associated liability. The transferred asset and the associated liability are measured on a basis that reflects rights and obligations that the Bank has retained.

Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Bank could be required to repay.

***(ii) Financial liabilities***

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability. The difference between the carrying value of the original financial liability and the consideration paid is recognised in the income statement.

***(VI) Fair value measurement***

The Bank measures financial instruments designated at fair value through profit or loss at fair value at each statement of financial position date. Also, fair values of financial instruments measured at amortized cost are disclosed in the notes.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- In the principal market for the asset or liability, or
- In the absence of a principal market, in the most advantageous market for the asset or liability to which the Bank has access at that date.

The principal or the most advantageous market must be accessible by the Bank. The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.
A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

When available, the Bank measures the fair value of an instrument using the quoted price in an active market for that instrument. A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.
If there is no quoted price in an active market, then the Bank uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

All assets and liabilities for which fair value is measured or disclosed in the separate financial statements are categorized within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

- Level 1 — Quoted (unadjusted) market prices in active markets for identical assets or liabilities.
- Level 2 — Valuation techniques for which the lowest level input that is significant to the fair value measurement is directly (i.e., as prices) or indirectly (i.e., derived from prices) observable.
- Level 3 — Valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable and has a significant effect on the instrument's valuation.

The objective of valuation techniques is to arrive at a fair value measurement that reflects the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price – i.e., the fair value of the consideration given or received. If the Bank determines that the fair value at initial recognition differs from the transaction price and the fair value is evidenced neither by a quoted price in an active market for an identical asset or liability nor based on a valuation technique that uses only data from observable markets, then the financial instrument is initially measured at fair value, adjusted to defer the difference between the fair value at initial recognition and the transaction price. Subsequently, that difference is recognised in profit or loss on an appropriate basis over the life of the instrument but no later than when the valuation is wholly supported by observable market data or the transaction is closed out.

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

The fair value of a demand deposit is not less than the amount payable on demand, discounted from the first date on which the amount could be required to be paid.
For assets and liabilities that are recognised in the separate financial statements on a recurring basis, the Bank determines whether transfers have occurred between levels in the hierarchy by re-assessing categorization (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period. The Bank's management determines the policies and procedures for recurring fair value measurement, such as unquoted financial assets.

At each reporting date, management analyses the movements in the values of assets and liabilities which are required to be re-measured or re-assessed as per the Bank's accounting policies. For this analysis, management verifies the major inputs applied in the latest valuation by agreeing the information in the valuation computation to contracts and other relevant documents.

For the purpose of fair value disclosures, the Bank has determined classes of assets and liabilities on the basis of the nature, characteristics and risks of the asset or liability and the level of the fair value hierarchy as explained above.

***(VII) Impairment of financial assets***

The Bank assesses at each statement of financial position date whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated.

Evidence of impairment may include indications that the borrower or a group of borrowers is experiencing significant financial difficulty, the probability that they will enter bankruptcy or other financial reorganization, default or delinquency in interest or principal payments and where observable data indicates that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

***Objective evidence of impairment***

At each reporting date, the Bank assesses whether there is objective evidence that financial assets not carried at FVTPL are impaired. A financial asset or a group of financial assets is 'impaired' when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset(s) and that the loss event has an impact on the future cash flows of the asset(s) that can be estimated reliably.
Objective evidence that financial assets are impaired includes:

- significant financial difficulty of the borrower or issuer;
- default or delinquency by a borrower;
- the restructuring of a loan or advance by the Bank on terms that the Bank would not consider otherwise;
- indications that a borrower or issuer will enter bankruptcy;
- the disappearance of an active market for a security; or
- observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the Bank, or economic conditions that correlate with defaults in the Bank.

In addition, for an investment in an equity security, a significant or prolonged decline in its fair value below its cost is objective evidence of impairment. In general, the Bank considers a decline of 20% to be 'significant' and a period of nine months to be 'prolonged'. However, in specific circumstances a smaller decline or a shorter period may be appropriate.

In making an assessment of whether an investment in sovereign debt is impaired, the Bank considers the following factors.

- The market's assessment of creditworthiness as reflected in the bond yields.
- The rating agencies' assessments of creditworthiness.
- The country's ability to access the capital markets for new debt issuance.
- The probability of debt being restructured, resulting in holders suffering losses through voluntary or mandatory debt forgiveness.

***(i) Amortised cost measurement***

The 'amortised cost' of a financial asset of financial liability is the amount at which the financial asset or financial liability is measured at initial recognition, minus principle repayments, plus or minus the cumulative amortisation using the effective interest method of any differences between the initial amount recognised and the maturity amount, minus any reduction for impairment.

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

If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not yet been incurred). The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the income statement.

Loans together with the associated allowance are written off when there is no realistic prospect of future recovery and all collateral has been realized or has been transferred to the Bank. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognised, the previously recognised impairment loss is increased or reduced by adjusting the allowance account. If a future write-off is later recovered, the recovery is credited to the "Net impairment loss" in the income statement.

For the purpose of a collective evaluation of impairment, financial assets are grouped on the basis of the Bank's internal credit grading system, that considers credit risk characteristics such as asset type, industry, geographical location, collateral type, past-due status and other relevant factors.

A collective component of the total allowance is established for:

- groups of homogeneous loans that are not considered individually significant; and
- groups of assets that are individually significant but that were not found to be individually impaired (loss 'incurred but not reported' or IBNR).

The collective allowance for groups of homogeneous loans is established using statistical methods such as roll rate methodology or, for small portfolios with insufficient information, a formula approach based on historical loss rate experience. The roll rate methodology uses statistical analysis of historical data on delinquency to estimate the amount of loss. Management applies judgement to ensure that the estimate of loss arrived at on the loss of historical information is appropriately adjusted to reflect the economic conditions and product mix at the reporting date. Roll rates and loss rates are regularly benchmarked against actual loss experience.

The IBNR allowance covers credit losses inherent in portfolios of loans and advances, and held-to- maturity investment securities with similar credit risk characteristics when there is objective evidence to suggest that they contain impaired items but the individual impaired items cannot yet be identified.

***(ii) Renegotiated loans***

Where possible, the Bank seeks to restructure loans rather than to take possession of collateral. This may involve extending the payment arrangements and the agreement of new loan conditions. Once the terms have been renegotiated, any impairment is measured using the original effective interest rate as calculated before the modification of terms and the loan is no longer considered past due. Management continuously reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur. The loans continue to be subject to an individual or collective impairment assessment, calculated using the loan's original effective interest rate.

***(iii) Collateral valuation***

The Bank seeks to use collateral, where possible, to mitigate its risks on financial assets. The collateral comes in various forms, such as cash, securities, letters of credit/ guarantees, real estate, other non- financial assets and credit enhancements such as netting agreements. The fair value of collateral is generally assessed, at a minimum, at inception and periodically updated based on the Bank's policies and type of collateral.

To the extent possible, the Bank uses active market data for valuing financial assets held as collateral. Other financial assets which do not have readily determinable market value are valued using models. Non-financial collateral, such as real estate, is valued based on data provided by third parties, such as independent accredited experts and other independent sources.

**(c) Leases**

The determination of whether an arrangement is a lease or contains a lease, is based on the substance of the arrangement and requires an assessment of whether the fulfillment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset.

*Bank as a lessee*

Leases which do not transfer to the Bank substantially all the risks and benefits incidental to ownership of the leased items are operating leases. Payments made under operating leases are recognised in profit or loss on a straight-line basis over the term of the lease. Lease incentives received are recognised as an integral part of the total lease expense, over the term of the lease.

**(d) Recognition of income and expenses**

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Bank and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised.

***(i) Interest and similar income and expense***

For all financial instruments measured at amortized cost, interest income or expense are recognised in profit or loss using the effective interest rate (EIR) method. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial asset or financial liability (or, where appropriate, a shorter period), to the carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Bank estimates future cash flows considering all contractual terms of the financial instrument, but not future credit losses.

The calculation of the effective interest rate includes transaction costs and fees paid or received that are an integral part of the effective rate. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial asset or financial liability. Interest income and expense presented in the statement of profit or loss and OCI include interest or financial assets and financial liabilities measured at amortised cost calculated on an effective interest basis.

Interest income and expense on the trading assets are considered to be incidental to the Bank's trading operations and are presented with other changes in the fair value of trading assets in:"Net gain from financial assets at fair value through profit or loss".

***(ii) Fee and commission***

The Bank earns fee and commission income from a diverse range of services it provides to its customers. Fee income can be divided into the following two categories:

*Fee income earned from services that are provided over a certain period of time*

Fees earned for the provision of services over a period of time are accrued over that period. These fees include commission income and asset management, custody and other management and advisory fees.

Loan commitment fees for loans that are likely to be drawn down and other credit related fees are deferred (together with any incremental costs) and recognised as an adjustment to the effective interest rate on the loan.

*Fee income from providing transaction services*

Fees arising from negotiating or participating in the negotiation of a transaction for a third party, such as the arrangement of the acquisition of shares or other securities, are recognised on completion of the underlying transaction. Fees or components of fees that are linked to a certain performance are recognised after fulfilling the corresponding criteria. Other fees and commission expense relate mainly to transaction and service fees which are expensed as the services are received.

***(iii) Dividend income***

Dividend income is recognised when the right to receive the income is established. Usually, this is the ex-dividend date for quoted equity securities. Dividends are presented in "Net gain from financial assets at fair value through profit or loss".

***(iv) Net gain from financial assets at fair value through profit or loss***

Results arising from financial assets at fair value through profit or loss, include all gains and losses from changes in fair value and related income or expenses, dividends for financial assets at fair value through profit or loss, foreign exchange differences and all realized and unrealized fair value changes.

**(e) Cash and cash equivalents**

Cash and cash equivalents as referred to in the cash flow statement comprise cash on hand, unrestricted balances held with central banks and highly liquid financial assets with original maturities of a period of three months or less from the acquisition date that are subject to an insignificant risk of changes in their fair value, and are used by the Bank in the management of its short-term commitments including: cash and balances with central banks, due from banks and financial institutions and due to banks and financial institutions.

Cash and cash equivalents are carried at amortized cost in the separate statement of financial position.

**(f) Property and equipment**

**(i) Recognition and measurement**

Items of property and equipment are measured at cost excluding the costs of day-to-day servicing, less accumulated depreciation and any accumulated impairment losses.

Purchased software that is integral to the functionality of the related equipment is capitalized as part of that equipment.

If significant parts of an item of property and equipment have different useful lives, then they are accounted for as separate items (major components) of property and equipment. Any gain or loss on disposal of an item of property and equipment is recognised within other income in profit or loss. Property and equipment is derecognised on disposal or when no future economic benefits are expected from its use. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is recognised in "Net loss on disposal of property and equipment" in the year the asset is derecognised.

**(ii) Subsequent costs**

Subsequent expenditure is capitalised only when it is probable that the future economic benefits of the expenditure will flow to the Bank. Ongoing repairs and maintenance are expensed as incurred.

**(iii) Depreciation**

Depreciation is calculated using the straight line method to write off the cost of items of property and equipment to their residual values over their estimated useful lives and is generally recognised in profit or loss. Land is not depreciated. The estimated useful lives are as follows:

- Freehold land and buildings 50 years;
- V ehicles 10 years;
- Office installations 16.66 years;
- Furniture 12.5 years; and
- Computer equipment 5 years.

The asset's residual values, useful lives and methods of depreciation are reviewed at each financial year end and adjusted prospectively if appropriate.

**(g) Assets obtained in settlement of debt**

The Bank occasionally acquires assets in settlement of certain loans and advances that are in default. Repossessed properties are measured at the lower of carrying amount and fair value less costs to sell and reported within "Assets obtained in settlement of debt" which is in accordance with the Central Bank of Lebanon main circular 78 and the Banking Control Commission circulars 173 and 267.

Upon sale of repossessed assets, any gain or loss realized is recognised in the income statement under "Other operating income" or "Other operating expenses". Gains resulting from the sale of repossessed assets are transferred to "Reserves for assets in settlement of debts disposed off" in the following financial year. These reserves cannot be distributed as dividends.

**(h) Impairment of non-financial assets**

The Bank assesses at each reporting date whether there is an indication that an asset may be impaired. If any indication exists, or when annual impairment testing for an asset is required, the Bank estimates the asset's recoverable amount. The 'recoverable amount' of an asset is the greater of its value in use and its fair value less costs to sell. 'Value in use" is based on the estimated future cash flows discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. In determining fair value less costs to sell, an appropriate valuation model is used.

An impairment loss is recognised if the carrying amount of an asset exceeds its recoverable amount. For assets other than goodwill, an impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

**(i) Financial guarantees and loan commitments**

In the ordinary course of business, the Bank gives financial guarantees, consisting of letters of credit, guarantees and acceptances. Financial guarantees are contracts that require the Bank to make specified payments to reimburse the holder for a loss that it incurs because a specified debtor fails to make payment when it is due in accordance with the terms of a debt instrument. Subsequent to initial recognition, the Bank's liability under each guarantee is measured at the higher of this amortised amount, and the amount of loss allowance. Loan commitments are firm commitments to provide credit under pre-specified terms and conditions. Liabilities arising from financial guarantees and loan commitment are included within provisions.

**(j) Provisions for risks and charges**
Provisions are recognised when the Bank has a present obligation (legal or constructive) as a result of a past event, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Provisions are determined based on management best estimates. The expense relating to any provision is presented in the income statement net of any reimbursement.

**(k) Employees' end-of-service benefits**
The Bank is subscribed to the compulsory defined benefit plan of the National Social Security Fund.

For the Bank and its branches operating in Lebanon, end-of-service benefit subscriptions paid and due to the National Social Security Fund (NSSF) are calculated on the basis of 8.5% of the staff salaries. The final end-of-service benefits due to employees after completing 20 years of service, at the retirement age, or if the employee permanently leaves employment, are calculated based on the last salary multiplied by the number of years of service. The Bank is liable to pay to the NSSF the difference between the subscriptions paid and the final end-of-service benefits due to employees. The Bank provides for end-of-service benefits on that basis.

End-of-service benefits for employees at foreign branches are accrued for in accordance with the laws and regulations of the respective countries in which the branches are located.

**(l) Income tax**
Income tax expense comprises current tax. It is recognised in profit or loss except to the extent that it relates to items recognised directly in equity or in profit or loss and other comprehensive income.

Taxes are provided for in accordance with regulations and laws that are effective in the countries where the Bank and its branches operate.

Current tax for the current and prior years is measured at the amount expected to be paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the statement of financial position date. Current tax also includes any tax arising from dividends.

The Bank's profits from operations in Lebanon are subject to a tax rate of 17% (15% applicable for the period starting 1 January 2017 till 26 October 2017 inclusive, while 17% starting 27 October 2017). In addition, the Ministry of Finance published a new Decision no. 1504/1 dated 22 December 2017 regarding the implementation of Article 51 of Law no. 497/2003 which states that interest income is subject to a tax rate of 7% (5% applicable for the period starting 1 January 2017 till 26 October 2017 inclusive, while 7% starting 27 October 2017) and Banks can no longer benefit from deducting the tax on interest received when calculating the income tax.
Dividends are subject to a flat 10% tax.

**(m) Assets held in custody and under administration**
The Bank provides custody and administration services that result in the holding or investing of assets on behalf of its clients. Assets held in custody or under administration, are not treated as assets of the Bank and accordingly are recorded as off financial position items.

**(n) Dividends on ordinary shares**
Dividends on ordinary shares are recognised as a liability and deducted from equity when they are approved by the Bank's shareholders. Interim dividends are deducted from equity when they are declared and no longer at the discretion of the Bank.
Dividends for the year that are approved after the reporting date are disclosed as an event after the reporting date.

**(o) Customers' acceptances**
Customers' acceptances represent term documentary credits which the Bank has committed to settle on behalf of its clients against commitments by those clients (acceptances). The commitments resulting from these acceptances are stated as a liability in the statement of financial position for the same amount.

## 2.4 Standards issued by not yet effective

A number of new standards and amendments to standards are effective for annual periods beginning after 1 January 2017 and earlier application is permitted; however, the Bank has not early adopted the following new or amended standards in preparing these separate financial statements. The new standards and amendments listed below are those that could potentially have an impact on the Bank's performance, financial position or disclosures.

**IFRS 15** *Revenue from Contracts with Customers*
IFRS 15 establishes a comprehensive framework for determining whether, how much and when revenue is recognised. It replaces existing revenue recognition guidance, including IAS 18 *Revenue*, IAS 11 *Construction Contracts* and IFRIC 13 *Customer Loyalty Programmes*. IFRS 15 is effective for annual reporting periods beginning on or after 1 January 2018, with early adoption permitted. The Bank earns fee and commission income mainly on retail and corporate banking and financial guarantees. IFRS 15 is not expected to have a material impact on the timing of recognition or measurement of fees and commission income.

**IFRS 16 Leases**
IFRS 16 introduces a single, on-balance lease sheet accounting model for lessees. A lessee recognises a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. There are optional exemptions for short-term leases and leases of low value items. Lessor accounting remains similar to the current standard – i.e. lessors continue to classify leases as finance and operating leases.

IFRS 16 replaces existing leases guidance including IAS 17 Leases, IFRIC 4 Determining whether an Arrangement contains a Lease, SIC-15 Operating Leases- Incentives and SIC-27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease.

The standard is effective for annual reporting periods beginning on or after 1 January 2019. Early adoption is permitted for entities that apply IFRS 15 Revenue from Contracts with Customers at or before the date of initial application of IFRS 16.

The Bank is currently assessing the potential impact on its condensed consolidated financial statements resulting from the application of IFRS 16 but is not expected to have a significant effect.

**IFRS 9 Financial Instruments**
In July 2014, the IASB issued the final version of IFRS 9 Financial Instruments. IFRS 9 is effective for annual periods beginning on or after 1 January 2018, with early adoption permitted. It replaces IAS 39

*Financial Instruments: Recognition and Measurement.*
In October 2017, the IASB issued Prepayment Features with Negative Compensation (*Amendments to IFRS 9*). The amendments are effective for annual periods beginning on or after 1 January 2019, with early adoption permitted.

The Bank will apply IFRS 9 as issued in July 2014 initially on 1 January 2018 and will early adopt the amendments to IFRS 9 on the same date. Based on assessments undertaken to date, the total estimated adjustment (net of tax) of the adoption of IFRS 9 on the opening balance of the Bank's equity at 1 January 2018 is approximately LBP 1,430 million representing:

- a reduction of approximately LBP 1,430 million related to classification and measurement requirements of securities at FVOCI, other than impairment, and
- no other reduction in equity since Expected Loss Allowances are fully covered by provisions constituted by the bank in previous periods. Any shortfall from the constituted provisions would have impacted the bank's equity. Incurred loss model is estimated approximately LBP 103 billion.

The above assessment is preliminary because not all transition work has been finalised. The actual impact of adopting IFRS 9 on 1 January 2018 may change because:

- IFRS 9 will require the Bank to revise its accounting processes and internal controls and these changes are not yet complete;
- Although parallel runs were carried out in 2018, the new systems and associated controls in place have not been operational for more extended period;
- The Bank has not finalized the testing and assessment of controls over its new IT systems and changes it its governance framework;
- The Bank is refining and finalizing its models for ECL calculations; and
- The new accounting policies, assumptions, judgements and estimation techniques employed are subject to change until the Bank finalized its first financial statements that include the date of initial application.

*(i) Classification – Financial assets*
The Bank has early adopted classification and measurement requirements as issued in IFRS 9 (2009) and IFRS (2010). In the July 2014 publication of IFRS 9, the new measurement category FVOCI was introduced for financial assets that satisfy the contractual cash flow characteristics (SPPI test). This category is aimed at portfolio of debt instruments for which amortised cost information, as well as fair value information is relevant and useful. This will be the case if these assets are held within a business model whose objective is achieved by both collecting contractual cash flows and selling the financial assets.

As the date of application of IFRS 9 (2014), the Bank reassessed the classification and measurement for all financial assets debt instruments that satisfy the contractual cash flow characteristic (SPPI test) and classified them within the category that it is consistent with the business model for managing these financial assets in the bases of facts and circumstances that existed at that date.

The classification and measurement requirements for financial assets that are equity instruments or debt instruments that do not meet the contractual cash flow characteristics (SPPI test) and financial liabilities remain unchanged from previous versions of IFRS 9.

The expected impact on the classification of the Bank financial assets and their carrying value and equity is disclosed above.

*(ii) Impairment- Financial assets, loan commitments and financial guarantee contracts*
IFRS 9 replaces the 'incurred loss' model in IAS 39 with a forward-looking credit loss' model.

This will require considerable judgement over how changes in economic factors affect ECLs, which will be determined on a probability-weighted basis.

The new impairment model applies to the following financial instruments that are not measured at FVTPL:

- financial assets that are debt instruments,
- loan commitments and financial guarantee contracts issued (previously impairment was measured under IAS 37 *Provisions, Contingent Liabilities* and *Contingent Assets*).

Under IFRS 9, no impairment loss is recognized on equity investments.

IFRS 9 requires a loss allowance to be recognised at an amount equal to either 12-month ECLs or lifetime ECL. Lifetime ECLs are the ECLs that result from all possible default events over the expected life of a financial instrument, whereas 12-month ECLs are the portion of ECLs that result from default events that are possible within the 12 months after the reporting date.

The Bank will recognise loss allowances at an amount equal to lifetime ECLs, except in the case of financial instruments for which credit risk has not increased significantly since initial recognition, for which the amount recognised will be 12-month ECLs.

The impairment requirements of IFRS 9 are complex and require management judgement estimates and assumptions, particularly in the following areas which are discussed in detail below:

- assessing whether the credit risk of an instrument has increased significantly since initial recognition:
- incorporating forward-looking information into the measurement of ECLs.

*Measurement of ECLs*
ECLs are a probability weighted estimate of credit losses and will be measured as follows:

- financial assets that are not credit-impaired at the reporting date: the present value of all cash shortfalls—i.e. the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Bank expects to receive,
- financial assets that are credit-impaired at the reporting date the difference between the gross carrying amount and the present value of estimated future cash flows;
- undrawn loan commitments: the present value of the difference between the contractual cash flows that are due to the Bank if the commitment is drawn down and the cash flows that the Bank expects to receive: and
- financial guarantee contracts: the present value of the expected payments to reimburse the holder less any amounts that the Bank expects to recover.

Financial assets that are credit-impaired are defined by IFRS 9 in a similar way to financial assets that are impaired under IAS 39.

*Definition of default*
Under IFRS 9, the Bank will consider a financial asset to be in default when:

- the borrower is unlikely to pay its credit obligations to the Bank in full,
- the borrower is more than 90 days past due on any material credit obligation to the Bank. Overdrafts are considered past due when the borrower fails to deposit any credit transaction for a period exceeding 180 days.

In assessing whether a borrower is in default, the Bank will consider indicators that are:

- qualitative: eg. breaches of covenant;
- quantitative: e.g overdue status
- based on data developed internally and obtained from external sources.

*Significant increase in credit risk*
Under IFRS 9, when determining whether the credit risk (i.e. risk of default) on a financial instrument has increased significantly since initial recognition, the Bank will consider reasonable and supportable information that is relevant and available without undue cost or effort, including both quantitative and qualitative information and analysis based on the Bank historical experience, expert credit assessment and forward-looking information.

The Bank primarily identifies whether a significant increase in credit risks has occurred for an exposure by monitoring the below indicators:
For Amortized Loans:

- More than 60 days past due,
- In the case of 1 renegotiation of a deal.

For Overdrafts:

- 90 days with no credit transactions,
- Credit amount is less than the charged interest over 2 consecutive quarters.

*Credit risk grades*
The Bank will allocate each exposure to a credit risk grade based on a variety of data that determined to be predictive of the risk of default and applying experienced credit judgement. The Bank will use these grades in identifying significant increase in credit risk under IFRS 9. Credit risk grades are defined using qualitative and quantitative factors that are indicative of the risk of default. These factors may vary depending on the nature of the exposure and the type of borrower.

Each exposure will be allocated to credit risk grade on initial recognition based on available information about the borrower. Exposures will be subject to ongoing monitoring, which may result in an exposure being moved to a different credit risk grade.

*Generating the term structure of PD*
Credit risk grades will be a primary input into the determination of the term structure of PD for exposures.

The Bank will employ statistical models to analyse the data collected and generate estimates of the remaining lifetime PD of exposures and how these are expected to change as a result of the passage of time.

This analysis will include the identification and calibration of relationships between changes in default rates and changes in key macro-economic factors. For most exposures, the prospect GDP growth indicator published by the IMF or any renowned source will be considered as the key macro-economic indicators.

*Modified financial assets*
The Bank renegotiates loans to customers financial difficulties (referred to as 'forbearance activities' to maximise collection opportunities and minimise the risk of default). The revised terms usually include extending the maturity, changing the timing of interest payments and amending the terms of loan covenants. Both retail and corporate loans are subject to the forbearance policy. The Bank Credit Committee regularly reviews reports on forbearance activities.

For financial assets modified as part of the Banks' forbearance policy, the estimate of PD will reflect whether the modification has improved or restored the Banks' ability to collect interest and principle and the Bank's previous experience of similar forbearance action.

Following forbearance, a customer needs to demonstrate consistently good payment behaviour over a period at time before the exposure is no longer considered to be in default/ credit-impaired or the PD is considered to have decreased such that the loss allowance reverts to being measured at an amount equal to 12-month ECLs.

*Inputs into measurement of ECLs*
The key inputs into the measurement of ECLs are likely to be the term structures of the following variables:

- probability of default (PD); and
- loss given default (LGD); and
- exposure at default (EAD).

These parameters will be derived from internally developed statistical models and other historical data that leverage regulatory models.

PD estimates are estimates at a certain date, which will be calculated based on statistical rating models and assessed using rating tools tailored to the various categories of counterparties and exposures.

LGD is the magnitude of the likely loss if there is a default.
EAD represents the expected exposure in the event of default. The EAD of a financial asset will be the gross carrying amount at default.

Where modelling of a parameter is carried out on a collective basis, the financial instruments will be grouped on the basis of shared risk characteristics that include:

- instrument type,
- credit risk grading,
- industry
- geographic location of the borrower.

*Impact assessment*
The most significant impact on the Bank's financial statements from the implementation of IFRS 9 is expected to result from the new impairment requirements. Impairment losses will increase for financial instruments in the scope of the IFRS 9 impairment model.

The Bank, however, has estimated that, on the adoption of IFRS 9 at 1 January 2018, the increase in loss allowances (before tax) will have no impact on the bank's equity, since the bank has already constituted collective and general provisions in previous periods, which cover the increase in loss allowances. Any shortfall from the constituted provisions would have impacted the bank's equity.

*(iv) Derecognition and contract modification*
IFRS 9 incorporates the requirements of IAS 39 for the derecognition of financial assets and financial liabilities without substantive amendments.

*(v) Disclosures*
IFRS 9 will require extensive new disclosures, in particular about hedge accounting, credit risk and ECLs.

## 3. Cash and balances with central banks

**In millions of LBP**

| | 2017 | 2016 |
|---|---|---|
| Cash on hand | 22,771 | 20,769 |
| Current accounts with Central Bank | 160,527 | 181,128 |
| Deposits with the Central Banks | 2,800,903 | 837,862 |
| | **2,984,201** | **1,039,759** |

Cash and balances with the Central Banks include balances with the Central Bank in coverage of the obligatory reserve requirements for all banks operating in Lebanon on deposits in Lebanese Pound as required by the Lebanese banking rules and regulations.

This obligatory reserve is calculated on the basis of 25% of the weekly average of current accounts denominated in Lebanese Pounds and 15% of the weekly average of term deposits. Accordingly, the obligatory reserve amounted to LBP 127,897 million at 31 December 2017 (2016: LBP 142,020 million).

In addition to the above, all banks operating in Lebanon are required to deposit with the Central Bank of Lebanon placements equivalents to 15% of total deposits in foreign currencies regardless of their nature. These placements amounted to US$ 414,800 thousands (equivalent to LBP 625,311 million) as at 31 December 2017 (2016: US$ 358,069 thousands equivalent to LBP 539,789 million).

Foreign branches are also subject to obligatory reserve requirements with varying percentages, according to the banking rules and regulations of the countries in which they are located.

The obligatory reserve at Cyprus branch at 31 December 2017 amounted to € 53,851 equivalent to LBP 97 million (2016: € 50,919 equivalent to LBP 81 million).

## 4. Due from banks and financial institutions

**In millions of LBP**

| | 2017 | 2016 |
|---|---|---|
| Current accounts | 243,585 | 363,953 |
| Term accounts | 89,566 | 127,665 |
| Checks for collection | 23,120 | 23,762 |
| Blocked accounts | 24,405 | 10,797 |
| | **380,676** | **526,177** |

## 5. Financial assets at fair value through profit or loss

**In millions of LBP**

| | 2017 | 2016 |
|---|---|---|
| Equity instruments | 56,225 | 49,986 |

**In millions of LBP**

| | 2017 | 2016 |
|---|---|---|
| *Detailed as follows:* | | |
| CSC Bank SAL | 47,350 | 44,173 |
| Other equity instruments | 8,875 | 5,813 |
| | **56,225** | **49,986** |

During 2016, the Bank sold 500,000 shares owned by the Bank which represent 12.5% of the shares of CSC Bank SAL, thus decreasing the ownership of the Bank from 39% to 27.4%.

## 6. Loans and advances to customers at amortized cost

**In millions of LBP**

| | 2017 | 2016 |
|---|---|---|
| Corporate loans | 1,862,501 | 2,013,198 |
| Retail consumer loans | 255,095 | 228,562 |
| | **2,117,596** | **2,241,760** |
| Less: | (70,724) | (69,991) |
| Allowance for impairment losses (a) | (8,206) | (6,267) |
| Allowance for unrealised interest on impaired loans (b) | 2,038,666 | 2,165,502 |

**Impairment allowance for loans and advances to customers at amortized cost**
a) The movement of the allowance for impairment losses for loans and advances to customers at amortized cost during the year was as follows:

**In millions of LBP**

| | Note | 2017 | 2016 |
|---|---|---|---|
| Balance at 1 January | | 69,991 | 74,218 |
| Add: | | | |
| Charge for the year * | 26 | 10,042 | 11,828 |
| Foreign exchange difference | | 220 | (109) |
| | | 80,253 | 85,937 |
| Less: | | | |
| Provisions related to loans written-off | | (8,906) | (14,680) |
| Write-back of provisions | 26 | (623) | (1,266) |
| **Balance at 31 December** | | **70,724** | **69,991** |
| | | | |
| Individual impairment | | 56,082 | 55,350 |
| Collective impairment | | 14,642 | 14,641 |
| | | 70,724 | 69,991 |
| | | | |
| Gross amount of loans individually determined to be impaired | | 76,723 | 74,647 |
| Gross amount of loans classified as substandard | | 82,656 | 74,677 |
| | | | |
| * The charge for the year is detailed as follows: | | | |
| *In millions of Lebanese Pound* | | 2017 | 2016 |
| Individual impairment | | 10,028 | 10,727 |
| Collective impairment | | 14 | 1,101 |
| | | 10,042 | 11,828 |

b) The movement of allowance for unrealized interest on impaired loans during the year was as follows:

**In millions of LBP**

| | Note | 2017 | 2016 |
|---|---|---|---|
| **Balance at 1 January** | | 6,267 | 5,186 |
| Add: | | | |
| - Unrealized interest for the year | | 3,832 | 3,055 |
| | | 10,099 | 8,241 |
| Less: | | | |
| - Recoveries of unrealized interest | 26 | (511) | (227) |
| - Unrealized interest related to loans written-off | | (1,382) | (1,747) |
| | | (1,893) | (1,974) |
| | | | |
| **Balance at 31 December** | | 8,206 | 6,267 |
| | | | |
| *In millions of Lebanese Pound* | | 2017 | 2016 |
| Unrealized interest on substandard loans | | 5,278 | 2,192 |
| Unrealized interest on doubtful loans | | 999 | 2,133 |
| Unrealized interest on bad loans | | 1,929 | 1,942 |
| | | **8,206** | **6,267** |

## 7. Related parties balances and transactions

Related parties of the Bank include Key Management Personnel of the Bank, close family members of Key Management Personnel and entities controlled or jointly controlled by Key Management Personnel or their close family members.
Key Management Personnel are defined as those persons having authority and responsibility for planning, directing and controlling the activities of the Bank, directly or indirectly, including the Directors of the Bank.
Entities under common directorships are defined as those entities for which members of the Bank's board or Key Management Personnel also serve as directors.

**Terms and conditions of transactions with related parties**
The Bank enters into transactions with major related parties in the ordinary course of business at normal commercial interest and commission rates.
The following table provides the total amount of transactions and the amount of outstanding balances (including commitments) with related parties for the relevant financial year.

**In millions of LBP**

| | 2017 | | 2016 | |
|---|---|---|---|---|
| | **Outstanding balance** | **Income (expense)** | **Outstanding balance** | **Income (expense)** |
| **Key Management Personnel** | | | | |
| Loans and advances | 5,940 | 65 | 5,708 | 140 |
| Deposits | 11,167 | (534) | 9,114 | (807) |
| Guarantees taken | 106 | – | 103 | – |
| **Entities under common directorships** | | | | |
| Loans and advances | 762 | 55 | 688 | 27 |

Compensation of Key Management Personnel of the Bank

**In millions of LBP**

| | 2017 | 2016 |
|---|---|---|
| Short-term benefits * | 1,633 | 1,531 |

*Short-term benefits comprise salaries, bonuses, attendance fees and other short-term benefits to Key Management Personnel.

- During the year ended 31 December 2017, the Bank paid attendance fees to the members of the board of directors amounting to LBP 738 million (2016: LBP 756 million);
- During the year ended 31 December 2017, the Bank received dividends amounting to LBP 1,184 million (2016: LBP 1,110 million) from CSC Bank S.A.L.

## 8. Financial assets at amortized cost

**In millions of LBP**

| | 2017 | 2016 |
|---|---|---|
| Quoted investment securities | | |
| Governmental debt securities | 614,107 | 689,624 |
| Unquoted investments securities | | |
| Central Bank's certificates of deposits | 429,123 | **967,451** |
| Governmental debt securities | 415,991 | **589,224** |
| Subordinated bonds | 3,027 | **3,027** |
| | 848,141 | **1,559,702** |
| | 1,462,248 | **2,249,326** |

## 9. Investment in a subsidiary

**In millions of LBP**

| Company | Country of incorporation | % of ownership 2017 | % of ownership 2016 | 2017 | 2016 |
|---|---|---|---|---|---|
| L & Gulf Company Limited | U.A.E | 100 | 100 | 6,320 | 6,320 |

During 2014, the Bank acquired 100% of shares of L & Gulf Company Limited a newly incorporated entity in UAE. The principal activity of the offshore company is to purchase and own an office in Dubai for Lebanon & Gulf Bank Rep Office.

## 10. Property and equipment

**In millions of LBP**

| | Freehold land and buildings | Vehicles | Furniture, office installations and computer equipment | Total |
|---|---|---|---|---|
| Cost | | | | |
| At 1 January 2017 | 38,716 | 2,330 | 49,561 | 90,607 |
| Additions | – | 852 | 2,742 | 3,594 |
| Disposals | – | (573) | (10) | (583) |
| Write offs | – | (13) | (6) | (19) |
| Translation difference | 17 | 6 | 76 | 99 |
| At 31 December 2017 | 38,733 | 2,602 | 52,363 | 93,698 |
| | | | | |
| Accumulated depreciation | | | | |
| At 1 January 2017 | 6,305 | 708 | 32,121 | 39,134 |
| Depreciation for the year | 653 | 241 | 2,965 | 3,859 |
| Disposals | – | (308) | (6) | (314) |
| Write offs | – | (6) | (3) | (9) |
| Translation difference | 12 | **6** | **68** | **86** |
| At 31 December 2017 | 6,970 | **641** | **35,145** | **42,756** |
| Carrying amount: | | | | |
| **Balance at 31 December 2017** | 31,763 | **1,961** | **17,218** | **50,942** |

**In millions of LBP**

| | Freehold land and buildings | Vehicles | Furniture, office installations and computer equipment | Total |
|---|---|---|---|---|
| Cost | | | | |
| At 1 January 2016 | 38,720 | 2,595 | 45,451 | 86,766 |
| Additions | – | 432 | 4,257 | 4,689 |
| Disposals | – | (688) | (22) | (710) |
| Write offs | – | (8) | (105) | (113) |
| Translation difference | (4) | (1) | (20) | (25) |
| At 31 December 2016 | 38,716 | 2,330 | 49,561 | 90,607 |
| | | | | |
| Accumulated depreciation | | | | |
| At 1 January 2016 | 5,657 | 679 | 29,642 | 35,978 |
| Depreciation for the year | 652 | 236 | 2,616 | 3,504 |
| Disposals | – | (201) | (17) | (218) |
| Write offs | – | (5) | (105) | (110) |
| Translation difference | **(4)** | **(1)** | **(15)** | **(20)** |
| At 31 December 2016 | 6,305 | **708** | **32,121** | **39,134** |
| Carrying amount: | | | | |
| **Balance at 31 December 2016** | 32,411 | **1,622** | **17,440** | **51,473** |

## 11. Assets obtained in settlement of debt

**In millions of LBP**

| | 2017 | 2016 |
|---|---|---|
| Net carrying amount: | | |
| At 1 January | 52,360 | 26,053 |
| Acquisitions | 5,145 | 28,130 |
| Rehabilitation and formality fees | 890 | **1,176** |
| Disposals | (1,102) | **(2,999)** |
| At 31 December | 57,293 | **52,360** |

These assets represent properties acquired in settlement of defaulting client's facilities. As stipulated by the code of money and credit, banks have two years from the date of acquisition to liquidate those assets, otherwise banks are required to constitute reserves (through appropriation from retained earnings) against these assets, prior to distribution of dividends.

## 12. Other assets

**In millions of LBP**

| | 2017 | 2016 |
|---|---|---|
| Prepayments | 3,620 | 4,560 |
| Due from National Social Security Fund | 1,609 | 1,077 |
| Deposits for auctions against assets to be obtained | | |
| in settlement of debt | – | **2,379** |
| Others assets | 473 | **2,211** |
| | 5,702 | **10,227** |

## 13. Due to the Central Bank

Following the Central Bank of Lebanon basic decision no. 6116 related to basic circular no. 23 and intermediate circular no. 367 issued on 11 August 2014, the Central Bank of Lebanon offered the commercial banks facilities that are subject to an interest rate of 1% per annum payable on a yearly basis. These facilities were given subject to granting mainly housing loans back to clients at an average interest rate of 5.44%.

## 14. Due to banks and financial institutions

**In millions of LBP**

| | 2017 | 2016 |
|---|---|---|
| Time deposits | 31,292 | 53,505 |
| Medium and long term deposits | 17,336 | – |
| Current accounts | 2,677 | 5,009 |
| Margin accounts | – | **4** |
| | 51,305 | **58,518** |

**Due to banks under repurchase agreements**

**In millions of LBP**

| | 2017 | 2016 |
|---|---|---|
| Repurchase agreements | 198,990 | 90,450 |
| Interest payable | 811 | 523 |
| | 199,801 | 90,973 |

During 2017, the Bank entered into two new repurchase agreements as the following:

- For an aggregate amount of USD 60 million (c/v LBP 90,450 million) having a fixed rate of 4.75% per annum against quoted investment securities held at amortized cost having a nominal value of USD 104.5 million (c/v LBP 157,534 million).
- For an aggregate amount of USD 12 million (c/v LBP 18,090 million) having a fixed rate of 6% per annum against quoted investment securities held at amortized cost having a nominal value of USD 26.7 million (c/v LBP 40,250 million).
- During 2015, the Bank entered into repurchase agreements, for an aggregate amount of USD 60 million (c/v LBP 90,450 million) of which USD 30 million having a fixed rate and USD 30 million with a floating rate renewable over 180 days against quoted investment securities held at amortized cost having a nominal value of USD 100 million (c/v LBP 150,750 million). The blocked account against these repurchase agreements amounted to USD 2.69 million (c/v LBP 4,059 million) at 31 December 2017 (31 December 2017: USD 2.69 million c/v LBP 4,055) (Note 4).

## 15. Deposits from customers

**In millions of LBP**

| | 2017 | 2016 |
|---|---|---|
| Sight deposits | 284,777 | **292,647** |
| Time deposits | 1,068,260 | **935,178** |
| Saving accounts | 4,339,216 | **3,922,815** |
| Credit accounts and deposits against debit accounts | 161,351 | **200,717** |
| Margins on letters of credit | 9,866 | **6,757** |
| | **5,863,470** | **5,358,114** |

Customers' deposits include coded deposit accounts amounting to LBP 5,668 million as of 31 December 2017 (2016: LBP 10,862 million). These accounts were opened under the provisions of article 3 of the banking secrecy law dated 3 September 1956 governing banks in Lebanon. As per the terms of this article, the Bank is not permitted to disclose the identities of the coded deposit accounts to third parties including its auditors.

## 16. Other liabilities

**In millions of LBP**

| | 2017 | 2016 |
|---|---|---|
| Deferred revenues** | 15,212 | 32,292 |
| Current tax liability | 17,173 | 14,521 |
| Other taxes | 3,473 | 3,946 |
| Due to National Social Security Fund | 508 | 345 |
| Accrued expenses and other regularization accounts | 402 | 324 |
| Sundry creditors | 551 | - |
| Other liabilities | 67 | 69 |
| | 37,386 | 51,497 |

** During 2016, the Central Bank of Lebanon issued Intermediate Circular number 446 dated 30 December 2016 relating to the gain realized by banks from certain financial transactions with the Central Bank of Lebanon, consisting of the sale of financial instruments denominated in Lebanese Lira and the purchase of financial instruments denominated in US Dollars. In accordance with the provisions of this circular, banks should recognize in the income statement, only part of the gain net of tax, caped to the extent of the losses recorded to comply with recent regulatory provisioning requirements (refer to note 17) and the shortage needed to comply with the capital adequacy requirements. Lebanese banks may further recognize up to 70% of the remaining balance of the gain realized net of tax in the income statement as non-distributable profits to be appropriated to reserves for capital increase, qualifying for inclusion within regulatory Common Equity Tier One.

The Bank did not recognize in its separate statement of profit or loss and other comprehensive income for the year ended 31 December 2016 an amount of LL 32,292 million (net of tax) in gains realized from certain financial transactions with the Central Bank of Lebanon. The related taxes amounting to LL 5,699 million were recorded directly in current tax liability. The amount recorded as deferred revenues qualifies for inclusion within regulatory Tier 2 Capital in accordance with the provisions of the circular.

During 2017, the Bank transferred from the “Deferred revenues” account the remaining balance of the collective provisions equivalent to 2% of 2016 consolidated risk weighted loans and advances to customers balance constituted in line with the Central Bank of Lebanon Intermediate Circular number 439 which amounted to LBP 17,080 million (2016: LBP 20,000 million) (Note 17).

## 17. Provisions for risks and charges

**In millions of LBP**

| | 2017 | 2016 |
|---|---|---|
| Other provisions** | 37,080 | 20,000 |
| Provision for employees' end of service benefits* | 8,514 | 7,556 |
| Structural exchange position | 243 | 217 |
| Net trading foreign exchange position | 75 | 75 |
| | 45,912 | 27,848 |

* The movement in the provision for employees’ end of service benefits during the year is as follows:

**In millions of LBP**

| | Note | 2017 | 2016 |
|---|---|---|---|
| Balance at 1 January | | 7,556 | 6,977 |
| Charge for the year | 27 | 1,039 | 675 |
| Benefits paid | | (81) | (96) |
| Balance at 31 December | | 8,514 | 7,556 |

** During November 2016, the Central Bank of Lebanon issued Intermediate Circular number 439 which required banks operating in Lebanon to constitute collective provisions equivalent to 2% of consolidated risk weighted loans and advances to customers. As such, provisions for risks and charges as at 31 December 2017 include an amount of LL 37,080 million in excess of the provisioning requirements of IAS 39 (2016: LL 20,000 million). These provisions were directly transferred from “Deferred revenues” within “Other liabilities” to “Provisions for risks and charges”. There was no effect on the tax expense during 2017 (2016: the related taxes amounting to LL 3,530 million were recorded directly in “Current tax liability” within “Other liabilities”) (note 16).

## 18. Share capital and share premium

**In millions of LBP**

| | 2017 Share capital | 2017 Share premium | 2016 Share capital | 2016 Share premium |
|---|---|---|---|---|
| Common shares – Authorized, issued and fully paid | | | | |
| 9,560,000 nominal shares at LBP 20,300 each (2014: 9,560,000 nominal shares at LBP 20,300 each) | 194,068 | – | 194,068 | – |
| Preferred shares – Authorized, issued and fully paid | | | | |
| 300,000 (2010 issue) of LBP 20,300 each (2014: LBP 20,300 each) | 6,090 | 39,245 | 6,090 | 39,245 |
| 230,000 (2013 issue) of LBP 20,300 each (2014: LBP 20,300 each) | 4,669 | 30,057 | 4,669 | 30,057 |
| 200,000 (2014 issue) of LBP 20,300 each (2014: LBP 20,300 each) | 4,060 | 26,090 | 4,060 | 26,090 |
| 200,000 (2015 issue) of LBP 20,300 each (2015: LBP 20,300 each) | 4,060 | 26,090 | 4,060 | 26,090 |
| | 18,879 | 121,482 | 18,879 | 121,482 |

**The table below summarizes all preferred shares series issued by the Bank and outstanding at 31 December 2017:**

| | 2010 issue | 2013 issue | 2014 issue | 2015 issue |
|---|---|---|---|---|
| Date of Extraordinary General Assembly Resolution | 1 September 2010 | 26 October 2013 | 19 September 2014 | 27 July 2015 |
| Date of Central Bank of Lebanon approval | 20 October 2010 | 20 November 2013 | 5 November 2014 | 30 September 2015 |
| Number of shares | 300,000 | 230,000 | 200,000 | 200,000 |
| Issue price | 100 USD | 100 USD | 100 USD | 100 USD |
| Par value of issued shares (LBP 20,300 per share) | LBP 6,090 million | LBP 4,669 million | LBP 4,060 million | LBP 4,060 million |
| Premium calculated in USD as the difference between the issue price and the counter value of the nominal value per share based on the exchange rate at the subscription dates | (USD 26,033 thousands) LBP 39,245 million | (USD 19,938 thousands) LBP 30,057 million | (USD 17,307 thousands) LBP 26,090 million | (USD 17,307 thousands) LBP 26,090 million |
| Distributions (non-cumulative, subject to the approval of the general assembly and the availability of distributable income) calculated on a pro rata basis in the year of issuance | 7.5% | 7% | 7% | 7% |
| Call option redeemable, pursuant to the exercise of that option, 60 days after the annual general assembly dealing with the accounts for the years | 2015 and any of the following years | 2018 and any of the following years | 2019 and any of the following years | 2020 and any of the following years |
| Redemption price per share (no entitlement to dividend in the year of redemption) | 104 USD | 103.50 USD | 103.50 USD | 103.50 USD |

In the event of any liquidation, dissolution or winding-up of the Bank, the holders of any series of preferred shares shall be entitled to be paid out of the assets of the Bank available for distribution to its shareholders on a pro rata basis, before any payment shall be made to common shareholders.
Refer to note 30 for information about dividends declared and paid during the year.

## 19. Non distributable reserves

**In millions of LBP**

| | Reserve for general banking risks | Other reserves | Legal reserve | Reserve for assets in settlement of debts | Reserve for capital increase | Reserve for redemption of preferred shares | Total |
|---|---|---|---|---|---|---|---|
| At 31 December 2015 | 37,990 | 1,904 | 7,497 | 10,585 | 1,288 | 7,405 | 66,669 |
| Appropriation of 2015 profits | 10,393 | – | 4,622 | 2,125 | 1,012 | 3,739 | 21,891 |
| At 31 December 2016 | 48,383 | 1,904 | 12,119 | 12,710 | 2,300 | 11,144 | 88,560 |
| Appropriation of 2016 profits | 11,130 | – | 5,342 | 3,124 | 632 | 3,212 | 23,440 |
| At 31 December 2017 | 59,513 | 1,904 | 17,461 | 15,834 | 2,932 | 14,356 | 112,000 |

**Reserve for general banking risks**
In compliance with the Central Bank of Lebanon's regulations basic circular 50, banks are required to appropriate from their annual net profit a minimum of 0.2 percent and a maximum of 0.3 percent of total risk weighted assets and off statement of financial position accounts as a reserve for general banking risks. The consolidated ratio should not be less than 1.25 percent of these risks by the year 2007 and 2 percent by the year 2017 as per BCC memo number 13/2015. This reserve is considered part of Tier I capital and is not available for distribution.

**Legal reserve**
According to the Lebanese Code of Commerce and to the Money and Credit article number 132, banks operating in Lebanon have to appropriate 10% of their annual net profit to legal reserve. This reserve is not available for distribution.
**Reserve for assets in settlement of debts**
In compliance with the Central Bank of Lebanon circular 78, banks are required to deduct from annual profits an amount of 20% or 5% of the carrying value of its properties acquired in settlement of debts within 2 years from the date of acquisition. The required reserves are established through appropriation of retained earnings. This reserve is not considered as part of the Bank's tier capital nor is available for distribution. Upon disposal of these properties, this reserve is transferred to a reserve specifically restructured to future increases in share capital.
**Reserve for capital increase**
In compliance with Banking Control Commission circular no. 173, all gains recognised on the sale of properties acquired in settlement of debt (note 11) should be appropriated from retained earnings and recorded as "Reserve for capital increase".
**Reserve for redemption of preferred shares**
In accordance with the resolutions of the Ordinary General Assembly of Shareholders of the Bank, held on 12 June 2017 (2016: 15 April 2016), an amount of LBP 3,212 million (2016: LBP 3,739 million) has been appropriated to the reserve for the redemption of preferred shares (issue 2010 and 2014).

## 20. Retained earnings

**In millions of LBP**

| | 2017 | 2016 |
|---|---|---|
| Retained earnings - portion that is available for distribution | 63,441 | 45,134 |
| Retained earnings - portion not available for distribution | | |
| (BCC circular no. 270) (b) | 8,013 | 6,375 |
| | 71,454 | 51,509 |

a) In accordance with the resolutions of the Ordinary General Assembly of Shareholders held on 12 June 2017 (2016: 15 April 2016), the profits of the Bank were appropriated and distributed as follows:

**In millions of LBP**

| | 2017 | 2016 |
|---|---|---|
| Prior year retained earnings | 51,509 | 35,269 |
| Prior year profit | 53,425 | 46,218 |
| Dividends declared to preferred shareholders (note 30) | (10,040) | (8,087) |
| Appropriations to: | | |
| - legal reserve | (5,342) | (4,622) |
| - reserve for general banking risks | (11,130) | (10,393) |
| - reserve for assets in settlement of debts | (3,124) | (2,125) |
| - reserve for redemption of preferred shares | (3,212) | (3,739) |
| - reserve for capital increase | (632) | (1,012) |
| | (23,440) | (21,891) |
| At 31 December | 71,454 | 51,509 |

b) Retained earnings - portion not available for distribution under BCC 270
Cumulative unrealised gains (gross of losses) on revaluation of financial assets at fair value through profit or loss are not available for distribution until their disposal.
Movement on the undistributable portion of retained earnings under BCC 270 is summarised as follows:

**In millions of LBP**

| | 2017 | 2016 |
|---|---|---|
| At 1 January | 6,375 | 939 |
| "Unrealised gain on investment securities " | | |
| at fair value through profit or loss (note 23) | 4,230 | 7,021 |
| Revaluation gains related to investment | | |
| securities subsequently sold (transferred to realised) | (2,592) | (1,585) |
| At 31 December | 8,013 | 6,375 |

## 21. Net interest and similar income

**Interest and similar income**

**In millions of LBP**

| | 2017 | 2016 |
|---|---|---|
| Financial assets at amortized cost | 126,195 | 181,656 |
| Loans to bank and financial institutions | 107,607 | 5,872 |
| Loans and advances to customers at amorized cost | 117,362 | 126,455 |
| Loans and advances to related parties at amorized cost | 120 | 167 |
| | 351,284 | 314,150 |

**Interest and similar expense**

**In millions of LBP**

| | 2017 | 2016 |
|---|---|---|
| Due to banks and financial institutions | 3,911 | 2,608 |
| Due to banks under repurchase agreements | 6,864 | 3,011 |
| Deposit from customers | 267,299 | 230,502 |
| Deposits from related parties | 534 | 807 |
| | 278,608 | 236,928 |
| Net interest and similar income | 72,676 | 77,222 |



## 22. Net fee and commission income

**In millions of LBP**

| | 2017 | 2016 |
|---|---|---|
| **Fee and commission income** | | |
| Credit related fees and commissions | 7,040 | 6,643 |
| Trade finance | 4,049 | 4,657 |
| General banking transactions | 2,826 | 2,717 |
| Electronic banking | 741 | 765 |
| Other services | 46 | 49 |
| | 14,702 | 14,831 |
| **Fee and commission expense** | | |
| Correspondents' accounts | (916) | (664) |
| **Net fee and commission income** | **13,786** | **14,167** |

## 23. Net gain from financial assets at fair value though profit or loss

**In millions of LBP**

| | 2017 | 2016 |
|---|---|---|
| **Net gain from debt instruments at fair value through** | | |
| profit or loss | | |
| Realized gain on sale of governmental debts securities | – | 23 |
| **Net gain from equity instruments at fair value** | | |
| through profit or loss | | |
| -Unrealized gain from revaluation | 3,287 | 4,230 |
| -Unrealized loss from revaluation | (163) | (41) |
| -Dividend income | 1,419 | 1,319 |
| -Realized gain on sale of equity securities | – | 5,547 |
| **Net gain from equity instruments at fair value** | | |
| through profit or loss | 4,543 | 11,055 |
| Foreign exchange income | 3,007 | 2,560 |
| **Net gain from financial assets at fair value** | | |
| through profit or loss | 7,550 | 13,638 |

## 24. Net gain from financial assets at amortized cost

Derecognition of financial assets at amortized cost were made during the year due to liquidity gap and yield management, in addition to the exchange transaction with the Lebanese Central Bank.
The schedule below details the gains arising from the derecognition of these financial assets:
**Lebanese sovereign and Central Bank of Lebanon:**

**In millions of LBP**

| | 2017 Gains | 2016 Gains (losses) |
|---|---|---|
| Central Bank's certificates of deposits | 24,215 | 309 |
| Treasury bills | 22,988 | 18,138 |
| Eurobonds | 1,273 | (188) |
| | 48,476 | 18,259 |

Below is the total nominal value and net gain on sale from certificate of deposits and treasury bills during the year ending 31 December 2017:

**In millions of LBP**

| Type of investment securities | Nominal value | Net gain on sale |
|---|---|---|
| Certificates of deposits (LBP) | 399,000 | 24,215 |
| Lebanese Treasury Bills (LBP) | 317,036 | 22,988 |
| | 716,036 | 47,203 |

## 25. Other operating income

**In millions of LBP**

| | 2017 | 2016 |
|---|---|---|
| Net gain from disposal of assets obtained in settlement of debt | 379 | 154 |
| Other income | 2,609 | 2,088 |
| | 2,988 | 2,242 |

## 26. Net impairment loss

**In millions of LBP**

| | Note | 2017 | 2016 |
|---|---|---|---|
| **Charges for the year:** | | | |
| Provision for doubtful loans and advances | 6 | (10,042) | (11,828) |
| Bad debts directly written-off to income statement | | (2,196) | (225) |
| **Recoveries during the year:** | | | |
| Write-back of provisions for loans and advances | 6 | 623 | 1,266 |
| Unrealized interest on loans and advances | | | |
| to customers | 6 | 511 | 227 |
| | | (11,104) | (10,560) |

## 27 Personnel expenses

**In millions of LBP**

| | Note | 2017 | 2016 |
|---|---|---|---|
| Salaries and related charges | | 22,873 | 21,390 |
| Social security contributions | | 3,351 | 2,938 |
| Bonus | | 1,464 | – |
| Provision for end of service indemnity | 17 | 1,039 | 675 |
| Additional allowances paid | | 4,895 | 4,742 |
| | | 33,622 | 29,745 |

## 28. Other operating expenses

**In millions of LBP**

| | Note | 2017 | 2016 |
|---|---|---|---|
| Maintenance and repairs | | 2,558 | 2,181 |
| Fees for guarantee of deposits | | 2,337 | 2,016 |
| Professional fees | | 1,252 | 1,295 |
| Rent and related charges | | 970 | 1,006 |
| Travel expenses | | 966 | 905 |
| Postage and telecommunications | | 902 | 886 |
| Subscriptions and fees | | 812 | 1,075 |
| Board of directors' attendance fees | 7 | 738 | 756 |
| Marketing and advertising | | 689 | 1,678 |
| Donations | | 617 | 609 |
| Electricity and fuel | | 526 | 650 |
| Stationery and printing | | 444 | 500 |
| Taxes and fees | | 439 | 291 |
| Insurance premiums | | 275 | 333 |
| Other expenses | | 4,036 | 3,450 |
| | | 17,561 | 17,631 |

## 29. Income tax expense

The components of income tax expense for the years ended 31 December 2017 and 2016 are detailed as follows:

**In millions of LBP**

| | 2017 | 2016 |
|---|---|---|
| Lebanon branches | 12,765 | 9,290 |
| Cyprus branch | 1 | 1 |
| Tax related to previous years | 6,192 | 1,207 |
| | 18,958 | 10,498 |

The Bank's books and records were reviewed by the Department of Income Tax for the years 2009 to 2012.
The books and records of the Bank remain subject to review by the Department of Income Tax for the years 2013 to 2017.
A reconciliation between the tax expense and the accounting profit for the years ended 31 December 2017 and 2016 is as follows:

**In millions of LBP**

| | 2017 | 2016 |
|---|---|---|
| Accounting profit before income tax - Lebanon branches | 79,176 | 63,968 |
| Add: | | |
| Non deductible collective provision | – | 1,101 |
| | 79,176 | 65,069 |
| Less: | | |
| Share of profit on financial assets under equity method | (3,287) | (4,230) |
| Dividends received and previously subject to income tax | (1,419) | (1,319) |
| Non taxable income | (911) | – |
| Taxable profit | 73,559 | 59,520 |
| Effective income tax rate | 15.34% | 15.00% |
| **Income tax due** | **11,284** | **8,928** |

The components of income tax expense for the years ended 31 December 2017 and 2016 are detailed as follows:

**In millions of LBP**

| | 2017 | 2016 |
|---|---|---|
| Income tax on profit for the year | 6,009 | 3,293 |
| Tax paid on interest revenue during the year | | |
| 5% | 4,128 | 5,488 |
| 7% | 911 | – |
| Tax on interest calculated in previous period | | |
| 5% | 1,406 | 509 |
| 7% | 311 | – |
| | 12,765 | 9,290 |

## 30. Dividends declared and paid

According to the Ordinary General Assembly of Shareholders held on 12 June 2017 (2016: 15 April 2016), dividends amounting to LBP 10,040 million were declared and paid to the preferred shareholders (2016: LBP 8,087 million).

## 31. Cash and cash equivalents

**In millions of LBP**

| | 2017 | 2016 |
|---|---|---|
| Cash and balances with central banks | 258,812 | 70,045 |
| Due from banks and financial institutions | 356,271 | 515,380 |
| Due to banks and financial institutions | (32,497) | (5,010) |
| | 582,586 | 580,415 |

## 32. Contingent liabilities and commitments

**Credit-related commitments and contingent liabilities**
To meet the financial needs of customers, the Bank enters into various commitments, guarantees and other contingent liabilities, which are mainly credit-related instruments including both financial and non-financial guarantees and commitments to extend credit. Even though these obligations may not be recognised on the statement of financial position, they do contain credit risk and are therefore part of the overall risk of the Bank.
The table below discloses the nominal principal amounts of credit-related commitments and contingent liabilities. Nominal principal amounts represent the amount at risk should the contracts be fully drawn upon any clients default.
As a significant portion of guarantees and commitments is expected to expire without being withdrawn, the aggregate amount of the nominal principal is not indicative of future liquidity requirements.
The Bank has the following credit related commitments:

**In millions of LBP**

| | 2017 | 2016 |
|---|---|---|
| Commitments issued to financial institutions | 23,823 | 34,931 |
| Commitments issued to customers | 44,527 | 45,897 |
| Guarantees issued to financial institutions | 4,484 | 5,186 |
| Guarantees issued to customers | 117,735 | 127,801 |
| Acceptances | 29,131 | 30,098 |
| Undrawn credit lines | 65,061 | 51,975 |
| Balance at 31 December | 284,761 | 295,888 |

*Commitments*
Documentary credits commit the Bank to make payments to third parties, on production of documents, which are usually reimbursed immediately by customers.
*Guarantees*
Guarantees are given as security to support the performance of a customer to third parties. The main types of guarantees provided are:
- Financial guarantees given to banks and financial institutions on behalf of customers to secure loans, overdrafts, and other banking facilities; and
- Other guarantees are contracts that have similar features to the financial guarantees contracts. These include mainly performance and tender guarantees.

*Undrawn credit lines and other commitments*
Undrawn credit lines and other commitments to lend are agreements to lend a customer in the future, subject to certain conditions. Such commitments are either made for a fixed period, or have no specific maturity but are cancellable by the lender subject to notice requirements.
**Legal claims**
Litigation is a common occurrence in the banking industry due to the nature of the business undertaken. The Bank has formal controls and policies for managing legal claims. Once professional advice has been obtained and the amount of loss reasonably estimated, the Bank makes adjustments to account for any adverse effects which the claims may have on its financial standing. At year end, the Bank had several unresolved legal claims.
Based on advice from legal counsel, management believes that legal claims will not result in any material financial loss to the Bank.
**Lease arrangements**
The Bank does not have material capital expenditures and operating lease payments as of the separate statement of financial position date.
**Other contingencies**
The Bank's books for the year 2013 to 2017 are still subject to review by the tax authorities. The ultimate outcome of such review cannot be presently determined.
The Bank's books in Lebanon have not been reviewed by the National Social Security Fund (NSSF) since 1 November 2006. The ultimate outcome of any review by the NSSF on the Bank's books in Lebanon cannot be presently determined.

## 33. Fair value of the financial instruments

See accounting policy in Note 2.3 (VI).
*A. Valuation models*
The Group measures fair values using the following fair value hierarchy, which reflects the significance of the Inputs used in making the measurements.
*Level 1*: Inputs that are quoted market prices (unadjusted) in active markets for identical instruments.
*Level 2:* Inputs other than quoted prices included within Level 1 that are observable either directly (i.e. as prices) or indirectly (i.e. derived from prices). This category includes instruments valued using: quoted market prices in active markets for similar instruments; quoted prices for identical or similar instruments in markets that are considered less than active; or other valuation techniques in which all significant inputs are directly or indirectly observable from market data.
*Level 3:* Inputs that are unobservable. This category includes all instruments for which the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments for which significant unobservable adjustments or assumptions are required to reflect differences between the instruments.
Valuation techniques include net present value and discounted cash flow models, comparison with similar instruments for which observable market prices exist.
The objective of valuation techniques is to arrive at a fair value measurement that reflects the price that would be received to sell the asset or paid to transfer the liability in an orderly transaction between market participants at the measurement date.
*B. Fair value hierarchy*
The following table analyses financial instruments measured at fair value at the reporting date, by the level in the fair value hierarchy into which the fair value measurement is categorised. The amounts are based on the values recognised in the statement of financial position. The fair values include any deferred differences between the transaction price and the fair value on initial recognition when the fair value is based on a valuation technique that uses unobservable inputs.

**In millions of LBP** **31 December 2017**

| | "Fair Value Valuation techniques" | | | | Carrying amount |
|---|---|---|---|---|---|
| | Quoted market price Level 1 | Observable inputs Level 2 | Unobservable inputs Level 3 | Total | |
| **Financial assets measured at fair value :** | | | | | |
| Financial assets at fair value through profit or loss | 191 | – | 56,034 | 56,225 | 56,225 |
| Quoted equity securities | 191 | – | – | 191 | 191 |
| Unquoted equity instruments | – | – | 56,034 | 56,034 | 56,034 |
| **Financial assets not measured at fair value:** | | | | | |
| Cash and balances with central banks | 22,771 | 2,961,430 | – | 2,984,201 | 2,984,201 |
| Due from banks and financial institutions | – | 380,676 | – | 380,676 | 380,676 |
| Loans to banks and financial institutions | – | 4,011 | – | 4,011 | 4,011 |
| Loans and advances to customers at amortized cost | – | 2,037,137 | – | 2,037,137 | 2,038,666 |
| Loans and advances to related parties at amortized cost | – | 6,702 | – | 6,702 | 6,702 |
| Financial assets at amortized cost | 581,919 | 830,955 | 3,027 | 1,415,901 | 1,462,248 |
| *Governmental debt securities* | 581,919 | 416,078 | – | 997,997 | 1,030,098 |
| *Certificates of deposit - Central Bank of Lebanon* | – | 414,877 | – | 414,877 | 429,123 |
| Subordinated bonds | – | – | 3,027 | 3,027 | 3,027 |
| **Financial liabilities not measured at fair value:** | | | | | |
| Due to Central Bank | – | 265,772 | – | 265,772 | 265,772 |
| Due to banks and financial institutions | – | 51,305 | – | 51,305 | 51,305 |
| Due to banks under repurchase agreements | – | 199,801 | – | 199,801 | 199,801 |
| Deposits from customers | – | 5,863,470 | – | 5,863,470 | 5,863,470 |
| Deposits from related parties | – | 11,167 | – | 11,167 | 11,167 |

**In millions of LBP** **31 December 2016**

| | "Fair Value Valuation techniques" | | | | Carrying amount |
|---|---|---|---|---|---|
| | Quoted market price Level 1 | Observable inputs Level 2 | Unobservable inputs Level 3 | Total | |
| **Financial assets measured at fair value :** | | | | | |
| Financial assets at fair value through profit or loss | 166 | – | 49,820 | 49,986 | 49,986 |
| Quoted equity securities | 166 | – | – | 166 | 166 |
| Unquoted equity instruments | – | – | 49,820 | 49,820 | 49,820 |
| **Financial assets not measured at fair value:** | | | | | |
| Cash and balances with central banks | 20,769 | 1,018,990 | – | 1,039,759 | 1,039,759 |
| Due from banks and financial institutions | – | 526,177 | – | 526,177 | 526,177 |
| Loans to banks and financial institutions | – | 4,964 | – | 4,964 | 4,964 |
| Loans and advances to customers at amortized cost | – | 2,165,502 | – | 2,165,502 | 2,165,502 |
| Loans and advances to related parties at amortized cost | – | 6,396 | – | 6,396 | 6,396 |
| Financial assets at amortized cost | 663,640 | 1,594,882 | 3,027 | 2,261,549 | 2,249,326 |
| *Governmental debt securities* | 663,640 | 615,518 | – | 1,279,158 | 1,278,848 |
| *Certificates of deposit - Central Bank of Lebanon* | – | 979,364 | – | 979,364 | 967,451 |
| *Subordinated bonds* | – | – | 3,027 | 3,027 | 3,027 |
| **Financial liabilities not measured at fair value:** | | | | | |
| Due to Central Bank | – | 38,503 | – | 38,503 | 38,503 |
| Due to banks and financial institutions | – | 58,518 | – | 58,518 | 58,518 |
| Due to banks under repurchase agreements | – | 90,973 | – | 90,973 | 90,973 |
| Deposits from customers | – | 5,358,114 | – | 5,358,114 | 5,358,114 |
| Deposits from related parties | – | 9,114 | – | 9,114 | 9,114 |

## 34. Maturity analysis of assets and liabilities

The table below shows an analysis of assets and liabilities analyzed according to when they are expected to be recovered or settled.
The maturity profile of the Bank's assets and liabilities as at 31 December 2017 is as follows:

**In millions of LBP** **31 December 2017**

| | Amounts without contractual maturity | Less than one year | More than one year | Total |
|---|---|---|---|---|
| **Assets** | | | | |
| Cash and balances with Central Banks | 22,771 | 548,702 | 2,412,728 | 2,984,201 |
| Due from banks and financial institutions | 380,653 | – | 23 | 380,676 |
| Financial assets at fair value through profit or loss | 56,225 | – | – | 56,225 |
| Loans to banks and financial institutions | – | 504 | 3,507 | 4,011 |
| Loans and advances to customers at amortized cost | – | 1,581,434 | 457,232 | 2,038,666 |
| Loans and advances to related parties at amortized cost | – | 3,452 | 3,250 | 6,702 |
| Debtors by acceptances | – | 29,131 | – | 29,131 |
| Financial assets at amortized cost | – | 127,241 | 1,335,007 | 1,462,248 |
| Investment in a subsidiary | 6,320 | – | – | 6,320 |
| Property and equipment | 50,942 | – | – | 50,942 |
| Assets obtained in settlement of debt | – | – | 57,293 | 57,293 |
| Other assets | 5,702 | – | – | 5,702 |
| **Total assets** | **522,613** | **2,290,464** | **4,269,040** | **7,082,117** |
| **Liabilities** | | | | |
| Due to Central Bank | – | 98,562 | 167,210 | 265,772 |
| Due to banks and financial institutions | 33,914 | – | 17,391 | 51,305 |
| Due to banks under repurchase agreements | – | – | 199,801 | 199,801 |
| Deposits from customers | – | 5,863,470 | – | 5,863,470 |
| Deposits from related parties | – | 11,167 | – | 11,167 |
| Engagement by acceptances | – | 29,131 | – | 29,131 |
| Other liabilities | – | 37,386 | – | 37,386 |
| Provisions for risks and charges | 45,912 | – | – | 45,912 |
| **Total liabilities** | **79,826** | **6,039,716** | **384,402** | **6,503,944** |
| **Net** | **442,787** | **(3,749,252)** | **3,884,638** | **578,173** |

The maturity profile of the Bank's assets and liabilities as at 31 December 2016 is as follows:

**In millions of LBP** **31 December 2016**

| | Amounts without contractual maturity | Less than one year | More than one year | Total |
|---|---|---|---|---|
| **Assets** | | | | |
| Cash and balances with Central Banks | 20,769 | 589,090 | 429,900 | 1,039,759 |
| Due from banks and financial institutions | 521,630 | – | 4,547 | 526,177 |
| Financial assets at fair value through profit or loss | 49,986 | – | – | 49,986 |
| Loans to banks and financial institutions | – | – | 4,964 | 4,964 |
| Loans and advances to customers at amortized cost | – | 1,457,394 | 708,108 | 2,165,502 |
| Loans and advances to related parties at amortized cost | – | 3,957 | 2,439 | 6,396 |
| Debtors by acceptances | – | 30,098 | – | 30,098 |
| Financial assets at amortized cost | – | 113,976 | 2,135,350 | 2,249,326 |
| Investment in a subsidiary | 6,320 | – | – | 6,320 |
| Property and equipment | 51,473 | – | – | 51,473 |
| Assets obtained in settlement of debt | – | – | 52,360 | 52,360 |
| Other assets | 10,227 | – | – | 10,227 |
| **Total assets** | **660,405** | **2,194,515** | **3,337,668** | **6,192,588** |
| | | | | |
| **Liabilities** | | | | 38,503 |
| Due to Central Bank | – | 3,043 | 35,460 | 58,518 |
| Due to banks and financial institutions | – | 58,518 | – | 90,973 |
| Due to banks under repurchase agreements | – | – | 90,973 | 5,358,114 |
| Deposits from customers | – | 5,358,114 | – | 9,114 |
| Deposits from related parties | – | 9,114 | – | 30,098 |
| Engagement by acceptances | – | 30,098 | – | 51,497 |
| Other liabilities | – | 51,497 | – | 27,848 |
| Provisions for risks and charges | 27,848 | – | – | 5,664,665 |
| **Total liabilities** | **27,848** | **5,510,384** | **126,433** | **527,923** |
| **Net** | **632,557** | **(3,315,869)** | **3,211,235** | |

# 35. Financial risk management

## 35.1 Risk management framework

The Bank manages its business activities within risk management guidelines as set by the Bank's "Risk Management Policy" approved by the board of directors (the "Board"). The Bank recognizes the role of the Board and executive management in the risk management process as set out in the Banking Control Commission circular 242. In particular, it is recognised that ultimate responsibility for establishment of effective risk management practices and culture lies with the Board as does the setting up of Bank's risk appetite and tolerance levels. The Board delegates through its risk management committee the day–to–day responsibility for establishment and monitoring of risk management process across the Bank to the Chief Risk Officer, who is directly appointed by the Board, in coordination with executive management at the Bank.

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

The Board's risk management committee has the mission to periodically (1) review and assess the Bank's charter risks, (2) review the adequacy of the Bank's capital and its allocation within the Bank, and (3) review risk limits and reports and make recommendations to the Board.

The Chief Risk Officer undertakes his responsibilities through the "Risk Management Division" overseeing and monitoring risk management activities throughout the Bank. The Risk Manager is responsible for establishing the function of Risk Management and its employees across the Bank.

Lebanon & Gulf Bank's risk management division aids executive management in controlling and actively managing the Bank's overall risk. The division mainly ensures that:

- Risk policies and methodologies are consistent with the Bank's risk appetite.
- Limits and risk across banking activities are monitored throughout the Bank.

Through a comprehensive risk management framework, transactions and outstanding risk exposures are quantified and compared against authorized limits, whereas non-quantifiable risks are monitored against policy guidelines as set by the Bank's "Risk Management Policy". Discrepancies, breaches or deviations are escalated to executive senior management in a timely manner for appropriate action.

The major objective of risk management is the implementation of sound risk management practices and the Basel framework as well as all related regulatory requirements within the Bank. Pillar I capital adequacy calculations have been generated since December 2004, while preparations for moving on to the more advanced approaches of pillar I have been initiated. Risk Management is progressively complying with the requirements of pillars II and III of the Basel framework.

**Excessive risk concentration**
Concentrations arise when the Bank has significant exposure to one borrower or a group of related borrowers or to a number of counterparties engaging in similar business activities or activities in the same geographic region, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations indicate the relative sensitivity of the Bank's performance developments affecting a particular industry or geographic location.

In order to avoid excessive concentrations of risk, the Bank's policies and procedures include specific guidelines to focus on maintaining a diversified portfolio. Identified concentrations of credit risks are controlled and managed accordingly. Selective hedging is used within the Bank to manage risk concentrations at both the relationship and industry levels.

## 35.2 Credit risk

Credit risk is the risk of financial loss to the Bank if a customer or counterparty to a financial instrument fails to meet its contractual obligations and arises principally from the Bank's loans and advances to customers and other banks, and investment debt securities. For risk management reporting purposes, the Bank considers and consolidates all elements of credit risk exposure (such as individual obligor default risk, country and sector risk).
The Bank manages credit risk in line with the regulatory guidelines. The Bank has set a credit risk policy which lays down norms for credit risk governance, methodologies and procedures for credit risk management and measurement. It consists of the following:

- The permissible activities, segments, programs and services that the Bank intends to deliver and the acceptable limits;
- The mechanism of the approval on credit-facilities;
- The mechanism for managing and following up credit-facilities; and
- The required actions for analyzing and organizing credit files.

**Credit initiation and approval**
Credit granting comprises the identification of suitable business to include in the portfolio and the best approaches to capture it. The process begins at the Board level by developing the Bank strategy. Once the strategy is approved, the Senior Management executes it. The Board does not interfere with the execution process, but observes and monitors the execution of the strategy to ensure its proper implementation, as per set guidelines.
The Bank is essentially split into two parts: (1) the one that generates the business, and (2) the one that monitors and ensures that this business is in line with the strategy of the Bank. And accordingly, the credit processing stage is governed by three major steps, namely:

a) Business Origination Unit: This centralized Unit is the generator of the business and includes all the relationship officers and analysts that liaise with clients. The main function of this Unit is to identify, analyze and recommend potential clients and the suitable facilities to these clients.
In essence, the Business Origination Unit is the engine of the Bank that creates the requisite business and manages it in a

manner to ensure that sufficient profitability is attained to compensate the Bank for the operating expenses and risks taken. The Business Origination Unit benefits directly from risk adjusted profits generated from clients, as such, has a vested interest in ensuring that credits are passed and processed quickly. For internal fraud avoidance, the Client Relationship and the Transaction Processing sides of the Business Origination Unit are managed and controlled separately with sufficient Chinese walls to allow the Business Origination Unit head to function efficiently.

b) Credit Control and Review Unit: For each recommended credit, a separate independent Unit within the Risk Management Division called the Control and Review Unit will examine it to ensure that the analysis and recommendations are in line with the Bank's Policies and Procedures Guidelines. This Unit acts on behalf of the Credit Committee to guarantee the sanctity of the credit granting process.

c) Credit Committee: The credit is finally passed on to the Credit Committee, which approves or disapproves the credit based on various parameters. Should the credit be approved, the Credit Administration Unit, which acts as a separate clerical control function and custodian of the credit requisite documentation and limits, enters the credit's characteristics and features into the Bank's core system.
Any amendments to the granted credits, renewals, or any excess to the approved limit need a special approval based on a predefined credit grid. The grid assigns approval levels based primarily on the riskiness of the credit, nature of credit and the credit's risk exposure. The delegation of authority involves the allocation of such limits to designated credit functionaries within the Bank. Such functionaries hold independent positions, but caution is exercised to ensure that a functionary cannot recommend, approve and/or process credits singularly.

**Loans follow up and monitoring**
The Bank's Risk Management is designed to identify and set appropriate risk limits and to monitor the risk adherence to these limits. Actual exposures against the limits are monitored daily, monthly and periodically. Bank Risk Management is responsible for monitoring the risk profile of the Bank's loan portfolio by producing internal reports highlighting any exposure of concern in commercial and consumer lending. The Bank examines the level of concentration whether by credit quality, client groupings or economic sector and collateral coverage. Further, the Bank monitors non-performing loans and takes the required provisions for these loans.
The Bank in the ordinary course of lending activities holds collaterals and guarantees as securities to mitigate credit risk from the loans and advances. These collaterals mostly include cash collateral, quoted shares and debt securities, real estate mortgages, personal guarantees and others. In addition, the recovery unit in the Bank dynamically manages and takes remedial actions for non-performing loans.
In compliance with credit best practices, and within the framework of the supervisory directives with regards to Basel implementation and more specifically the Central Bank of Lebanon Intermediary Circular 256 dated 27 April 2011, the Bank uses an Internal Risk Rating System to grade the credit risk of obligors in the Corporate and Middle market business.
For this purpose, and for the time being, the Bank will use two classification schemes; the first will be an internal rating system (that will be referred to as "The Internal Loan Grading System") purchased from Moody's and divided into ten grades, and the second will be a more subjective loan classification system (that will be referred to as "Supervisory Classification System"), divided into six grades, of which three grades relate to the performing portfolio (regular credit facilities: risk ratings "OA" and special mention – watch list: risk rating "B1" and "B2"), one grade relates to substandard loans (risk rating "OC") and two grades relate to non-performing loans (risk ratings "OD" and "OE").
Credit cards, personal loans, car loans and housing loans are classified in compliance with Banking Control Commission Circular 280 dated 2 January 2015. Each individual borrower is classified based on an internally developed scoring model that evaluates risk based on financial and qualitative inputs. These scores are reviewed on an annual basis. In addition to that, the bank works in full compliance with the new supervisory circulars. Non-performing loans are managed proactively by a dedicated collection unit. These loans are closely monitored and well provisioned, with appropriate corrective actions taken.

***Impairment allowance***
For accounting purposes, the Bank uses an incurred loss model for the recognition of losses on impaired financial assets.
The main considerations for the loan impairment assessment include whether any payments of principal or interest are overdue or whether there are any known difficulties in the cash flows of counterparties, credit rating downgrades, or infringement of the original terms of the contract. The Bank addresses impairment assessment in two areas: individually assessed allowances and collectively assessed allowances, in compliance with Banking Control Commission Circular 280 dated 2 January 2015.

*Individually assessed allowances*
The Bank determines the allowances appropriate for each individually significant loan or advance on an individual basis. Items considered when determining allowance amounts include the sustainability of the counterparty's business plan, its ability to improve performance once a financial difficulty has arisen, projected receipts and the expected payout should bankruptcy ensue, the availability of other financial support, the realisable value of collateral, and the timing of the expected cash flows. The impairment losses are evaluated at each reporting date, unless unforeseen circumstances require more careful attention.

*Collectively assessed allowances*
Allowances are assessed collectively for losses on loans and advances. They are also assessed individually as per BCC 280 for significant loans and advances that have been assessed individually and found to be impaired.
The Bank generally bases its analyses on historical experience. However, when there are significant market developments, regional and/or global, the Bank would include macroeconomic factors within its assessments. These factors include, depending on the characteristics of the individual or collective assessment: unemployment rates, current levels of bad debts, changes in laws, changes in regulations, bankruptcy trends, and other consumer data. The Bank may use the aforementioned factors as appropriate to adjust the impairment allowances.
Allowances are evaluated separately on yearly basis with each portfolio. The collective assessment is made for groups of assets with similar risk characteristics, in order to determine whether any provision should be made due to incurred loss events for which there is objective evidence but whose effects are not yet evident in the individual loans assessments. The collective assessment takes account of data from the loan portfolio (such as historical losses on the portfolio, levels of arrears, credit utilization, loan to collateral ratios and expected receipts and recoveries once impaired) or economic data (such as current economic conditions, unemployment levels and local or industry-specific problems). This approximate delay between the time a loss is likely to have been incurred and the time it will be identified as requiring an individually assessed impairment allowance is also taken into consideration. Local management is responsible for deciding the length of this period which can extend for as long as one year. The impairment allowance is then reviewed by credit management to ensure alignment with the Bank's overall policy.

**Collateral and other credit enhancements**
The following table shows the maximum exposure to credit risk by class of financial asset. It further shows the total loans collateralized against financial and non-financial assets and the net exposure to credit risk.

**In millions of LBP** **31 December 2017**

| | | Amounts collateralized against: | | | | |
|---|---|---|---|---|---|---|
| | Maximum exposure | Cash | Securities | Letters of credit / guarantees | Real estate | Net credit exposure |
| Balances with central banks | 2,961,430 | – | – | – | – | 2,961,430 |
| Due from banks and financial institutions | 380,676 | – | – | – | – | 380,676 |
| Loans to banks and financial institutions | 4,011 | – | – | – | – | 4,011 |
| Loans and advances to customers at amortized cost | 2,038,666 | 151,124 | 16,205 | 9,086 | 1,421,271 | 440,980 |
| *Corporate loans* | 1,783,571 | 139,711 | 16,205 | 9,086 | 1,243,221 | 375,348 |
| *Retail consumer loans* | 255,095 | 11,413 | – | – | 178,050 | 65,632 |
| Loans and advances to related parties at amortized cost | 6,702 | – | – | – | – | 6,702 |
| Debtors by acceptances | 29,131 | – | – | – | – | 29,131 |
| Financial assets at amortized cost | 1,462,248 | – | – | – | – | 1,462,248 |
| | 6,882,864 | 151,124 | 16,205 | 9,086 | 1,421,271 | 5,285,178 |
| Guarantees | 122,219 | 36,171 | – | – | – | 86,048 |
| Documentary credits | 23,823 | 2,973 | – | – | – | 20,850 |
| Undrawn credit lines | 65,061 | – | – | – | – | 65,061 |
| | 7,093,967 | 190,268 | 16,205 | 9,086 | 1,421,271 | 5,457,137 |

**In millions of LBP** **31 December 2016**

| | Maximum exposure | Amounts collateralized against: Cash | Securities | Letters of credit / guarantees | Real estate | Net credit exposure |
|---|---|---|---|---|---|---|
| Balances with central banks | 1,018,990 | – | – | – | – | 1,018,990 |
| Due from banks and financial institutions | 526,177 | – | – | – | – | 526,177 |
| Loans to banks and financial institutions | 4,964 | – | – | – | – | 4,964 |
| Loans and advances to customers at amortized cost | 2,165,502 | 228,889 | 11,182 | 3,361 | 1,380,909 | 541,161 |
| *Corporate loans* | 1,937,702 | 196,845 | 11,182 | 3,361 | 1,187,582 | 538,732 |
| *Retail consumer loans* | 227,800 | 32,044 | – | – | 193,327 | 2,429 |
| Loans and advances to related parties at amortized cost | 6,396 | – | – | – | – | 6,396 |
| Debtors by acceptances | 30,098 | – | – | – | – | 30,098 |
| Financial assets at amortized cost | 2,249,326 | – | – | – | – | 2,249,326 |
| | 6,001,453 | 228,889 | 11,182 | 3,361 | 1,380,909 | 4,377,112 |
| Guarantees | 132,987 | 29,682 | – | – | – | 103,305 |
| Documentary credits | 34,931 | 3,882 | – | – | – | 31,049 |
| Undrawn credit lines | 51,975 | – | – | – | – | 51,975 |
| | 6,221,346 | 262,453 | 11,182 | 3,361 | 1,380,909 | 4,563,441 |

The amount, type and valuation of collateral are based on guidelines specified in the risk management framework. The main types of collateral obtained include real estate, bonds and shares, cash collateral and bank guarantees.
Management monitors the market value of collateral, requests additional collateral in accordance with the underlying agreement, and monitors the market value of collateral obtained during its review of the adequacy of the allowance for impairment losses.

The main types of collateral obtained are as follows:

*Securities:*
The balances shown above represent the fair value of the securities.

*Letters of credit / guarantees:*
The Bank holds in some cases guarantees, letters of credit and similar instruments from banks and financial institutions which enable it to claim settlement in the event of default on the part of the counterparty. The balances shown represent the notional amount of these types of guarantees held by the Bank.

*Real estate (commercial and residential):*
The Bank holds in some cases a first degree mortgage over residential property (for housing loans) and commercial property (for commercial loans). The value shown above reflects the fair value of the property up to the related mortgaged amount.

*Other:*
In addition to the above, the Bank also obtains guarantees from parent companies for loans to their subsidiaries, personal guarantees for loans to companies owned by individuals and assignments of insurance proceeds and revenues, which are not reflected in the above table.

**Credit quality analysis**
The credit quality of financial assets is managed by the Bank using internal and external credit ratings. The table below shows the credit quality of asset for all financial assets exposed to credit risk, based on the Bank's internal credit rating system and the relationship with external credit rating. The amounts presented are gross of impairment allowances.



**In millions of LBP** **31 December 2017**

| | Neither past due nor impaired: High grade | Standard grade | Past due but not impaired | Individually impaired Non performing | Total |
|---|---|---|---|---|---|
| Balances with central banks | 2,961,430 | – | – | – | 2,961,430 |
| Due from banks and financial institutions | 380,676 | – | – | – | 380,676 |
| Loans to banks and financial institutions | 4,011 | – | – | – | 4,011 |
| Loans and advances to customers at amortized cost | 1,063,621 | 866,021 | 28,505 | 159,449 | 2,117,596 |
| Loans and advances to related parties at amortized cost | 6,702 | – | – | – | 6,702 |
| Debtors by acceptances | 29,131 | – | – | – | 29,131 |
| Financial assets at amortized cost | 1,462,248 | – | – | – | 1,462,248 |
| Total | 5,907,819 | 866,021 | 28,505 | 159,449 | 6,961,794 |

**In millions of LBP** **31 December 2016**

| | Neither past due nor impaired: High grade | Standard grade | Past due but not impaired | Individually impaired Non performing | Total |
|---|---|---|---|---|---|
| Balances with central banks | 1,018,990 | – | – | – | 1,018,990 |
| Due from banks and financial institutions | 526,177 | – | – | – | 526,177 |
| Loans to banks and financial institutions | 4,964 | – | – | – | 4,964 |
| Loans and advances to customers at amortized cost | 1,395,326 | 673,757 | 23,253 | 149,424 | 2,241,760 |
| Loans and advances to related parties at amortized cost | 6,396 | – | – | – | 6,396 |
| Debtors by acceptances | 30,098 | – | – | – | 30,098 |
| Financial assets at amortized cost | 2,249,326 | – | – | – | 2,249,326 |
| Total | 5,231,277 | 673,757 | 23,253 | 149,424 | 6,077,711 |

Aging analysis of past due but not impaired loans per class of financial assets:

| In millions of LBP | | | | 31 December 2017 |
|---|---|---|---|---|
| | Less than 90 days | 91 to 180 days | More than 181 days | Total |
| Loans and advances to customers at amortized cost: | 13,995 | 7,775 | 6,283 | 28,053 |
| - Corporate loans | 157 | 218 | 77 | 452 |
| - Retail consumer loans | 14,152 | 7,993 | 6,360 | 28,505 |

| In millions of LBP | | | | 31 December 2016 |
|---|---|---|---|---|
| | Less than 90 days | 91 to 180 days | More than 181 days | Total |
| Loans and advances to customers at amortized cost: | 10,318 | 7,060 | 5,765 | 23,143 |
| - Corporate loans | 79 | 9 | 22 | 110 |
| - Retail consumer loans | 10,397 | 7,069 | 5,787 | 23,253 |

The classification of loans and advances to customers and related parties at amortized cost by grade according to Central Bank of Lebanon circular 58 are as follows:

| In millions of LBP | | | | 31 December 2017 |
|---|---|---|---|---|
| | Gross balance | Unrealised interest | Impairment allowances | Net balance |
| Regular | 1,022,928 | – | – | 1,022,928 |
| Follow up | 472,332 | – | – | 472,332 |
| Follow up and regularization | 469,660 | – | – | 469,660 |
| Substandard | 82,656 | (5,278) | – | 77,378 |
| Doubtful | 71,996 | (999) | (53,285) | 17,712 |
| Bad | 4,726 | (1,929) | (2,797) | – |
| | 2,124,298 | (8,206) | (56,082) | 2,060,010 |
| Collective impairment | – | – | (14,642) | (14,642) |
| | 2,124,298 | (8,206) | (70,724) | 2,045,368 |



| In millions of LBP | | | | 31 December 2016 |
|---|---|---|---|---|
| | Gross balance | Unrealised interest | Impairment allowances | Net balance |
| Regular | 1,455,576 | – | – | 1,455,576 |
| Follow up | 565,013 | – | – | 565,013 |
| Follow up and regularization | 78,243 | – | – | 78,243 |
| Substandard | 74,677 | (2,192) | – | 72,485 |
| Doubtful | 67,427 | (2,133) | (50,129) | 15,165 |
| Bad | 7,220 | (1,942) | (5,221) | 57 |
| | 2,248,156 | (6,267) | (55,350) | 2,186,539 |
| Collective impairment | – | – | (14,641) | (14,641) |
| | 2,248,156 | (6,267) | (69,991) | 2,171,898 |

**Renegotiated Loans**
Restructuring activity aims to manage customer relationships, maximize collection opportunities and, if possible, avoid foreclosure or repossession. Such activities include extended payment arrangements, deferring foreclosure, modification, loan rewrites and/or deferral of payments pending a change in circumstances.
Restructuring policies and practices are based on indicators or criteria which, in the judgement of local management, indicate that repayment will probably continue. The application of these policies varies according to the nature of the market and the type of the facility. As of 31 December 2017, renegotiated loans amounted to LBP 11,176 million (2016: LBP 12,296 million).

**Analysis of risk concentration**
The Bank's concentrations of risk are managed on a client or counterparty basis, by geographical region and by industry sector.

The Bank's exposure to the highest concentration at 31 December 2017 amounted to LBP 52,460 million (2016: LBP 59,683 million) before taking account of collateral or other credit enhancements and LBP 37,457 million (2016: LBP 51,388 million) net of such protection.

The following tables show the maximum exposure to credit risk for the components of the separate statement of financial position by geography of counterparty and by industry before the effect of mitigation through the use of netting and collateral agreements.

**Industry analysis**
An industry sector analysis of the Bank's financial assets, before taking into account any collateral held or other credit enhancements, is as follows:

**In millions of LBP** — **As at December 31 2017**

| | Commercial | Industrial | Agriculture | Services | Banks and other financial institutions | Construction | Retail | Governmental | Other | Total |
|---|---|---|---|---|---|---|---|---|---|---|
| Balances with central bank | – | – | – | – | – | – | – | 2,961,430 | – | 2,961,430 |
| Due from banks and financial institutions | – | – | – | – | 380,676 | – | – | – | – | 380,676 |
| Loans to banks and financial institutions | – | – | – | – | 4,011 | – | – | – | – | 4,011 |
| Loans and advances to customers at amortized cost | 869,912 | 190,590 | 14,426 | 88,483 | – | 518,447 | 304,129 | – | 52,679 | 2,038,666 |
| *Corporate loans* | 855,784 | 183,061 | 14,406 | 87,592 | – | 510,911 | 79,713 | – | 52,104 | 1,783,571 |
| *Retail consumer loans* | 14,128 | 7,529 | 20 | 891 | – | 7,536 | 224,416 | – | 575 | 255,095 |
| Loans and advances to related parties at amortized cost | – | – | – | – | – | – | 6,702 | – | – | 6,702 |
| *Corporate loans* | – | – | – | – | – | – | 762 | – | – | 762 |
| *Retail consumer loans* | – | – | – | – | – | – | 5,940 | – | – | 5,940 |
| Debtors by acceptances | 26,662 | 2,450 | – | – | – | 19 | – | – | – | 29,131 |
| Financial assets at amortized cost | – | – | – | – | 3,027 | – | – | 1,459,221 | – | 1,462,248 |
| *Lebanese governmental bonds* | – | – | – | – | – | – | – | 1,030,098 | – | 1,030,098 |
| *Certificates of deposit by BDL* | – | – | – | – | – | – | – | 429,123 | – | 429,123 |
| *Subordinated bonds* | – | – | – | – | 3,027 | – | – | – | – | 3,027 |
| | 896,574 | 193,040 | 14,426 | 88,483 | 387,714 | 518,466 | 310,831 | 4,420,651 | 52,679 | 6,882,864 |

**In millions of LBP** — **As at December 31 2016**

| | Commercial | Industrial | Agriculture | Services | Banks and other financial institutions | Construction | Retail | Governmental | Other | Total |
|---|---|---|---|---|---|---|---|---|---|---|
| Balances with central bank | – | – | – | – | – | – | – | 1,018,990 | – | 1,018,990 |
| Due from banks and financial institutions | – | – | – | – | 526,177 | – | – | – | – | 526,177 |
| Loans to banks and financial institutions | – | – | – | – | 4,964 | – | – | – | – | 4,964 |
| Loans and advances to customers at amortized cost | 837,981 | 164,345 | 12,874 | 112,098 | – | 686,878 | 301,434 | – | 49,892 | 2,165,502 |
| *Corporate loans* | 836,012 | 164,047 | 12,833 | 111,207 | – | 685,731 | 81,674 | – | 46,198 | 1,937,702 |
| *Retail consumer loans* | 1,969 | 298 | 41 | 891 | – | 1,147 | 219,760 | – | 3,694 | 227,800 |
| Loans and advances to related parties at amortized cost | – | – | – | – | – | – | 6,396 | – | – | 6,396 |
| *Corporate loans* | – | – | – | – | – | – | 688 | – | – | 688 |
| *Retail consumer loans* | – | – | – | – | – | – | 5,708 | – | – | 5,708 |
| Debtors by acceptances | 26,801 | 3,297 | – | – | – | – | – | – | – | 30,098 |
| Financial assets at amortized cost | – | – | – | – | 3,027 | – | – | 2,246,299 | – | 2,249,326 |
| *Lebanese governmental bonds* | – | – | – | – | – | – | – | 1,278,848 | – | 1,278,848 |
| *Certificates of deposit by BDL* | – | – | – | – | – | – | – | 967,451 | – | 967,451 |
| *Subordinated bonds* | – | – | – | – | 3,027 | – | – | – | – | 3,027 |
| | 864,782 | 167,642 | 12,874 | 112,098 | 534,168 | 686,878 | 307,830 | 3,265,289 | 49,892 | 6,001,453 |

*Geographic analysis*
An analysis of concentration of credit risk by geographic location is shown below:

**In millions of LBP** **31 December 2017**

| | Domestic | North America | Europe | Asia Pacific | Middle East and Africa | Australia | Total |
|---|---|---|---|---|---|---|---|
| **Financial assets** | | | | | | | |
| Balances with central banks | 2,961,331 | – | 99 | – | – | – | 2,961,430 |
| Due from banks and financial institutions | 118,779 | 166,419 | 57,356 | 35,524 | 2,399 | 199 | 380,676 |
| *Current accounts* | 31,359 | 164,157 | 40,812 | 27,685 | 2,376 | 199 | 266,588 |
| *Time deposits* | 87,420 | 2,262 | 16,544 | 7,839 | 23 | – | 114,088 |
| Loans to banks and financial institutions | 4,011 | – | – | – | – | – | 4,011 |
| Loans and advances to customers at amortized cost: | 1,873,408 | 7,226 | 51,729 | 64,044 | 42,259 | – | 2,038,666 |
| *Corporate loans* | 1,618,313 | 7,226 | 51,729 | 64,044 | 42,259 | – | 1,783,571 |
| *Retail consumer loans* | 255,095 | – | – | – | – | – | 255,095 |
| Loans and advances to related parties at amortized cost | 6,702 | – | – | – | – | – | 6,702 |
| *Corporate loans* | 762 | – | – | – | – | – | 762 |
| *Retail consumer loans* | 5,940 | – | – | – | – | – | 5,940 |
| Debtors by acceptances | 28,837 | – | – | – | 294 | – | 29,131 |
| Financial assets at amortized cost | 1,462,248 | – | – | – | – | – | 1,462,248 |
| *Lebanese governmental bonds* | 1,030,098 | – | – | – | – | – | 1,030,098 |
| *Certificates of deposit by BDL* | 429,123 | – | – | – | – | – | 429,123 |
| *Subordinated bonds* | 3,027 | – | – | – | – | – | 3,027 |
| **Total credit exposure** | **6,455,316** | **173,645** | **109,184** | **99,568** | **44,952** | **199** | **6,882,864** |

**In millions of LBP** **31 December 2016**

| | Domestic | North America | Europe | Asia Pacific | Middle East and Africa | Australia | Total |
|---|---|---|---|---|---|---|---|
| **Financial assets** | | | | | | | |
| Balances with central banks | 1,018,905 | – | 85 | – | – | – | 1,018,990 |
| Due from banks and financial institutions | 184,412 | 244,866 | 62,803 | 57 | 33,107 | 932 | 526,177 |
| *Current accounts* | 82,973 | 242,605 | 52,029 | 57 | 9,119 | 932 | 387,715 |
| *Time deposits* | 101,439 | 2,261 | 10,774 | – | 23,988 | – | 138,462 |
| Loans to banks and financial institutions | 4,964 | – | – | – | – | – | 4,964 |
| Loans and advances to customers at amortized cost: | 2,000,922 | 6,685 | 58,209 | 63,744 | 35,942 | – | 2,165,502 |
| *Corporate loans* | 1,773,122 | 6,685 | 58,209 | 63,744 | 35,942 | – | 1,937,702 |
| *Retail consumer loans* | 227,800 | – | – | – | – | – | 227,800 |
| Loans and advances to related parties at amortized cost | 6,396 | – | – | – | – | – | 6,396 |
| *Corporate loans* | 688 | – | – | – | – | – | 688 |
| *Retail consumer loans* | 5,708 | – | – | – | – | – | 5,708 |
| Debtors by acceptances | 29,382 | – | – | 435 | 281 | – | 30,098 |
| Financial assets at amortized cost | 2,249,326 | – | – | – | – | – | 2,249,326 |
| *Lebanese governmental bonds* | 1,278,848 | – | – | – | – | – | 1,278,848 |
| *Certificates of deposit by BDL* | 967,451 | – | – | – | – | – | 967,451 |
| *Subordinated bonds* | 3,027 | – | – | – | – | – | 3,027 |
| **Total credit exposure** | **5,494,307** | **251,551** | **121,097** | **64,236** | **69,330** | **932** | **6,001,453** |

## 35.3 Liquidity risk

'Liquidity risk' is the risk that the Bank will encounter difficulty in meeting obligations associated with financial liabilities that are settled by delivering cash or another financial asset. Liquidity risk arises because of the possibility that the Bank might be unable to meet its payment obligations when they fall due under both normal and stress circumstances. To limit this risk, management has arranged diversified funding sources in addition to its core deposit base, and adopted a policy of managing assets with liquidity in mind and of monitoring future cash flows and liquidity on a daily basis. The Bank has developed internal control processes and contingency plans for managing liquidity risk. This incorporates an assessment of expected cash flows and the availability of high grade collateral which could be used to secure additional funding if required.

The Bank maintains a portfolio of highly marketable and diverse assets that can be easily liquidated in the event of an unforeseen interruption of cash flow. In addition, the Bank maintains statutory deposits with Central Banks. As per Lebanese banking regulations, the Bank must retain obligatory reserves with the Central Bank of Lebanon calculated on the basis of 25% of the sight deposits and 15% of term deposits denominated in Lebanese Pounds, in addition to interest bearing placements equivalent to 15% of all deposits in foreign currencies regardless of their nature.

The liquidity position is assessed and managed under a variety of scenarios, giving due consideration to stress factors relating to both the market in general and specifically to the Bank. The Bank maintains a solid ratio of highly liquid net assets in foreign currencies to deposits and commitments in foreign currencies taking market conditions into consideration.

*Regulatory ratios and limits*
In accordance with the Central Bank of Lebanon circulars, the ratio of net liquid assets to deposits in foreign currencies should not be less than 10%. The net liquid assets consist of cash and all balances with the Central Bank of Lebanon (excluding reserve requirements), certificates of deposit issued by the Central Bank of Lebanon irrespective of their maturities and deposits due from other banks that mature within one year, less deposits due to the Central Bank of Lebanon and deposits due to banks that mature within one year. Deposits are composed of total customers' deposits (excluding blocked accounts) and due from financial institutions irrespective of their maturities and all certificates of deposits and acceptances and other debt instruments issued by the Bank and loans from the public sector that mature within one year.

The Bank stresses the importance of customers' deposits as source of funds to finance its lending activities. This is monitored by using the advances to deposits ratio, which compares loans and advances to customers and related parties as a percentage of clients' deposits.

| | Loans to deposits | |
|---|---|---|
| | 2017 % | 2016 % |
| Year-end | 34.82 | 40.47 |

### 35.3.1 Maturity analysis of financial assets and financial liabilities

The table below shows the remaining contractual maturities of the Bank's financial assets and financial liabilities.

**In millions of LBP** **31 December 2017**

| | Less than 3 monts | 3 to 12 months | 1 to 5 years | Over 5 years | Total |
|---|---|---|---|---|---|
| **Financial assets** | | | | | |
| Cash and balances with central banks | 397,120 | 174,353 | 636,241 | 1,776,487 | 2,984,201 |
| Due from banks and financial institutions | 380,653 | – | 23 | – | 380,676 |
| Loans to banks and financial institutions | – | 504 | 3,507 | – | 4,011 |
| Loans and advances to customers at amortized cost | 886,244 | 695,190 | 324,405 | 132,827 | 2,038,666 |
| Loans and advances to related parties at amortized cost | 3,452 | – | – | 3,250 | 6,702 |
| Debtors by acceptances | 21,895 | 7,236 | – | – | 29,131 |
| Financial assets at amortized cost | 52,491 | 74,750 | 195,806 | 1,139,201 | 1,462,248 |
| **Total undiscounted financial assets** | **1,741,855** | **952,033** | **1,159,982** | **3,051,765** | **6,905,635** |
| **Financial liabilities** | | | | | |
| Due to central bank | 812 | 97,750 | 35,162 | 132,048 | 265,772 |
| Due to banks and financial institutions | 33,914 | – | 17,391 | – | 51,305 |
| Due to banks under repurchase agreements | – | – | 199,801 | – | 199,801 |
| Deposits from customers | 3,689,004 | 2,174,466 | – | – | 5,863,470 |
| Deposits from related parties | 11,167 | – | – | – | 11,167 |
| Engagements by acceptances | 21,895 | 7,236 | – | – | 29,131 |
| **Total undiscounted financial liabilities** | **3,756,792** | **2,279,452** | **252,354** | **132,048** | **6,420,646** |
| Net undiscounted financial assets / (liabilities) | (2,014,937) | (1,327,419) | 907,628 | 2,919,717 | 484,989 |

**In millions of LBP** **31 December 2016**

| | Less than 3 months | 3 to 12 months | 1 to 5 years | Over 5 years | Total |
|---|---|---|---|---|---|
| **Financial assets** | | | | | |
| Cash and balances with central banks | 587,498 | 22,361 | 171,514 | 258,386 | 1,039,759 |
| Due from banks and financial institutions | 521,630 | – | 4,547 | – | 526,177 |
| Loans to banks and financial institutions | – | – | 755 | 4,209 | 4,964 |
| Loans and advances to customers at amortized cost | 656,446 | 800,948 | 545,852 | 162,256 | 2,165,502 |
| Loans and advances to related parties at amortized cost | 3,957 | – | – | 2,439 | 6,396 |
| Debtors by acceptances | 23,162 | 6,936 | – | – | 30,098 |
| Financial assets at amortized cost | 59,895 | 54,081 | 296,404 | 1,838,946 | 2,249,326 |
| **Total undiscounted financial assets** | **1,852,588** | **884,326** | **1,019,072** | **2,266,236** | **6,022,222** |
| **Financial liabilities** | | | | | |
| Due to central bank | 1,011 | 2,032 | 12,273 | 23,187 | 38,503 |
| Due to banks and financial institutions | 50,318 | 8,200 | – | – | 58,518 |
| Due to banks under repurchase agreements | – | – | 90,973 | – | 90,973 |
| Deposits from customers | 3,487,387 | 1,870,727 | – | – | 5,358,114 |
| Deposits from related parties | 8,951 | 163 | – | – | 9,114 |
| Engagements by acceptances | 23,162 | 6,936 | – | – | 30,098 |
| **Total undiscounted financial liabilities** | **3,570,829** | **1,888,058** | **103,246** | **23,187** | **5,585,320** |
| Net undiscounted financial assets / (liabilities) | (1,718,241) | (1,003,732) | 915,826 | 2,243,049 | 436,902 |

The table below shows the contractual expiry by maturity of the Bank's contingent liabilities and commitments. Each undrawn loan commitment is included in the time band containing the earliest date it can be drawn down.

**In millions of LBP** **31 December 2017**

| | Less than 3 months | 3 to 12 months | 1 to 5 years | Total |
|---|---|---|---|---|
| Financial guarantees | 57,715 | 52,734 | 11,770 | 122,219 |
| Documentary credits | 9,768 | 58,582 | – | 68,350 |
| Undrawn credit lines | 8,426 | 30,744 | 25,891 | 65,061 |
| | 75,909 | 142,060 | 37,661 | 255,630 |

**In millions of LBP** **31 December 2016**

| | Less than 3 months | 3 to 12 months | 1 to 5 years | Total |
|---|---|---|---|---|
| Financial guarantees | 61,021 | 55,894 | 16,072 | 132,987 |
| Documentary credits | 21,875 | 58,953 | – | 80,828 |
| Undrawn credit lines | 12,320 | 24,186 | 15,469 | 51,975 |
| | 95,216 | 139,033 | 31,541 | 265,790 |

The Bank expects that not all of the contingent liabilities or commitments will be demanded before maturity.

### 35.4 Market risk

'Market risk' is the risk that changes in market prices such as interest rates, equity prices, foreign exchange and credit spreads (not relating to changes in the obligor's/issuer's credit standing)- will affect the Bank's income or the value of its holding of financial instruments. The objective of the Bank's market risk management is to manage and control market risk exposures within acceptable parameters to ensure the Bank's solvency while optimizing the return on risk.

Risk Management is responsible for generating internal reports quantifying the Bank's earnings at risk due to extreme movements in interest rates, while daily monitoring the sensitivity of the Bank's trading portfolio of fixed income securities to changes in market prices and / or market parameters. Interest rate sensitivity gaps are reported to executive management on a monthly basis. The Bank's Asset and Liability Management policy assigns authority for its formulation, revision and administration to the Asset / Liability Management Committee (ALCO) of the Bank. Risk Management is responsible for monitoring compliance with all limits set in the policy ranging from core foreign currency liquidity to liquidity mismatch limits to interest sensitivity gap limits.

### 35.4.1 Interest rate risk

Interest rate risk arises from the possibility that changes in interest rates will affect future profitability or the fair values of financial instruments. The Bank is exposed to interest rate risk as a result of mismatches of interest rate repricing of assets and liabilities and off-financial position items that mature or reprice in a given period. The Bank manages this risk by matching the repricing of assets and liabilities through risk management strategies.

**Interest rate sensitivity**
The following table analyses the sensitivity to a reasonably possible change in interest rates, with all other variables held constant of the Bank's profit or loss and other comprehensive income.

The sensitivity of the income statement is the effect of the assumed changes in interest rates on the net interest income for one year, based on the floating rate non-trading financial assets and financial liabilities held at the year end, including the effect of hedging instruments.

**In millions of LBP** **31 December 2017**

| Currency | Increase in basis points | Sensitivity of net interest income |
|---|---|---|
| Lebanese Pound | 200 | (17,775) |
| United States Dollar | 100 | (16,229) |
| Euro | 50 | (258) |

**In millions of LBP** **31 December 2016**

| Currency | Increase in basis points | Sensitivity of net interest income |
|---|---|---|
| Lebanese Pound | 200 | (18,396) |
| United States Dollar | 100 | (10,759) |
| Euro | 50 | (281) |

A decrease in basis points will have an opposite effect on net interest income.

**Interest sensitivity gap**
The table below analyses the Bank's interest rate risk exposure on financial assets and liabilities. The Bank's assets and liabilities are included at carrying amount and categorized by the earlier of contractual re-pricing or maturity dates.

**In millions of LBP** **31 December 2017**

| | Up to 1 month | 1 to 3 months | 3 months to 1 year | (1-2) years | (2-5) years | More than 5 years | Non-interest sensitive | Total |
|---|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | | |
| Cash and balances with central banks | 203,801 | – | 174,115 | 165,071 | 469,978 | 1,772,066 | 199,170 | 2,984,201 |
| Due from banks and financial institutions | 104,151 | 9,799 | – | 23 | – | – | 266,703 | 380,676 |
| Loans to banks and financial institutions | – | – | – | 500 | 3,500 | – | 11 | 4,011 |
| Financial assets at fair value through profit or loss | – | – | – | – | – | – | 56,225 | 56,225 |
| Loans and advances to customers at amortized cost | 346,106 | 358,334 | 1,006,097 | 134,743 | 94,842 | 3,454 | 95,090 | 2,038,666 |
| Loans and advances to related parties at amortized cost | 3,452 | – | – | – | – | 3,250 | – | 6,702 |
| Debtors by acceptances | 14,685 | 7,210 | 7,236 | – | – | – | – | 29,131 |
| Financial assets at amortized cost | – | 51,277 | 73,640 | 17,319 | 195,485 | 1,101,892 | 22,635 | 1,462,248 |
| **Total** | **672,195** | **426,620** | **1,261,088** | **317,656** | **763,805** | **2,880,662** | **639,834** | **6,961,860** |
| **Liabilities** | | | | | | | | |
| Due to central bank | – | – | 97,553 | – | 35,162 | 132,046 | 1,011 | 265,772 |
| Due to banks and financial institutions | 21,065 | 8,755 | 18,548 | – | – | – | 2,937 | 51,305 |
| Due to banks under repurchase agreements | – | 45,225 | 63,315 | 90,450 | – | – | 811 | 199,801 |
| Deposits from customers | 3,700,876 | 1,056,754 | 807,243 | 6,607 | – | – | 291,990 | 5,863,470 |
| Deposits from related parties | 5,757 | 2,738 | 187 | – | – | – | 2,485 | 11,167 |
| Engagements by acceptances | 14,685 | 7,210 | 7,236 | – | – | – | – | 29,131 |
| **Total** | **3,742,383** | **1,120,682** | **994,082** | **97,057** | **35,162** | **132,046** | **299,234** | **6,420,646** |
| **Total interest rate sensitivity gap** | **(3,070,188)** | **(694,062)** | **267,006** | **220,599** | **728,643** | **2,748,616** | **340,600** | **541,214** |

**In millions of LBP** **31 December 2016**

| | Up to 1 month | 1 to 3 months | 3 months to 1 year | (1-2) years | (2-5) years | More than 5 years | Non-interest sensitive | Total |
|---|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | | |
| Cash and balances with central banks | 106,730 | 278,090 | 22,348 | – | 171,228 | 253,075 | 208,288 | 1,039,759 |
| Due from banks and financial institutions | 117,780 | 16,049 | – | 4,547 | – | – | 387,801 | 526,177 |
| Loans to banks and financial institutions | – | – | – | – | 750 | 4,200 | 14 | 4,964 |
| Financial assets at fair value through profit or loss | – | – | – | – | – | – | 49,986 | 49,986 |
| Loans and advances to customers at amortized cost | 456,923 | 403,507 | 937,321 | 164,550 | 111,445 | 4,048 | 87,708 | 2,165,502 |
| Loans and advances to related parties at amortized cost | 6,396 | – | – | – | – | – | – | 6,396 |
| Debtors by acceptances | 11,994 | 11,168 | 6,936 | – | – | – | – | 30,098 |
| Financial assets at amortized cost | 5 | 58,380 | 53,814 | 123,542 | 168,252 | 1,809,604 | 35,729 | 2,249,326 |
| **Total** | **699,828** | **767,194** | **1,020,419** | **292,639** | **451,675** | **2,070,927** | **769,526** | **6,072,208** |
| **Liabilities** | | | | | | | | |
| Due to central bank | 337 | 674 | 2,032 | 2,875 | 9,398 | 23,187 | – | 38,503 |
| Due to banks and financial institutions | 16,457 | 28,376 | 8,017 | – | – | – | 5,668 | 58,518 |
| Due to banks under repurchase agreements | – | 22,613 | 22,613 | 45,225 | – | – | 522 | 90,973 |
| Deposits from customers | 3,215,430 | 1,017,982 | 865,962 | 5,492 | – | – | 253,248 | 5,358,114 |
| Deposits from related parties | 9,114 | – | – | – | – | – | – | 9,114 |
| Engagements by acceptances | 11,994 | 11,168 | 6,936 | – | – | – | – | 30,098 |
| **Total** | **3,253,332** | **1,080,813** | **905,560** | **53,592** | **9,398** | **23,187** | **259,438** | **5,585,320** |
| **Total interest rate sensitivity gap** | **(2,553,504)** | **(313,619)** | **114,859** | **239,047** | **442,277** | **2,047,740** | **510,088** | **486,888** |

### 35.4.2 Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rate.

The Bank is allowed to maintain a net trading position not to exceed 1 percent of its net Tier 1 equity, as long as the global foreign position does not exceed, at the same time, 40 percent of net Tier 1 equity. This is subject to the Bank's commitment to comply in a timely and consistent manner with the required capital adequacy ratio.
The table below indicates the separate statement of financial position detailed in Lebanese Pound (LBP) and foreign currencies, translated into LBP.

**In millions of LBP** — **31 December 2017**

| | | Foreign currencies in Lebanese Pound | | | | |
|---|---|---|---|---|---|---|
| | Lebanese Pound | US Dollar in LBP | Euro in LBP | Other foreign currencies in LBP | Total foreign currencies in LBP | Total |
| **Assets** | | | | | | |
| Cash and balances with central banks | 1,405,965 | 1,504,718 | 71,724 | 1,794 | 1,578,236 | 2,984,201 |
| Due from banks and financial institutions | 16,380 | 254,844 | 42,754 | 66,698 | 364,296 | 380,676 |
| Financial assets at fair value through profit or loss | 49,122 | 7,103 | – | – | 7,103 | 56,225 |
| Loans to banks and financial institutions | 4,011 | – | – | – | – | 4,011 |
| Loans and advances to customers at amortized cost | 369,573 | 1,566,313 | 101,986 | 794 | 1,669,093 | 2,038,666 |
| Loans and advances to related parties at amortized cost | 4,495 | 2,186 | 21 | – | 2,207 | 6,702 |
| Debtors by acceptances | – | 26,693 | 1,831 | 607 | 29,131 | 29,131 |
| Financial assets at amortized cost | 486,664 | 955,988 | 19,596 | – | 975,584 | 1,462,248 |
| Investment in a subsidiary | – | – | – | 6,320 | 6,320 | 6,320 |
| Property and equipment | 50,873 | – | 69 | – | 69 | 50,942 |
| Assets obtained in settlement of debt | 46 | 57,247 | – | – | 57,247 | 57,293 |
| Other assets | 5,569 | 73 | 14 | 46 | 133 | 5,702 |
| **Total assets** | **2,392,698** | **4,375,165** | **237,995** | **76,259** | **4,689,419** | **7,082,117** |
| **Financial liabilities** | | | | | | |
| Due to central bank | 262,850 | 2,922 | – | – | 2,922 | 265,772 |
| Due to banks and financial institutions | 6,730 | 44,275 | 260 | 40 | 44,575 | 51,305 |
| Due to banks under repurchase agreements | – | 199,801 | – | – | 199,801 | 199,801 |
| Deposits from customers | 1,772,301 | 3,816,409 | 235,434 | 39,326 | 4,091,169 | 5,863,470 |
| Deposits from related parties | 5,484 | 5,395 | 232 | 56 | 5,683 | 11,167 |
| Engagements by acceptances | – | 26,693 | 1,830 | 608 | 29,131 | 29,131 |
| Other liabilities | 33,915 | 3,361 | 110 | – | 3,471 | 37,386 |
| Provisions for risks and charges | 45,912 | – | – | – | – | 45,912 |
| **Total liabilities** | **2,127,192** | **4,098,856** | **237,866** | **40,030** | **4,376,752** | **6,503,944** |
| **Net exposure** | **265,506** | **276,309** | **129** | **36,229** | **312,667** | **578,173** |

**In millions of LBP** — **31 December 2016**

| | | Foreign currencies in Lebanese Pound | | | | |
|---|---|---|---|---|---|---|
| | Lebanese Pound | US Dollar in LBP | Euro in LBP | Other foreign currencies in LBP | Total foreign currencies in LBP | Total |
| **Assets** | | | | | | |
| Cash and balances with central banks | 426,786 | 573,452 | 37,825 | 1,696 | 612,973 | 1,039,759 |
| Due from banks and financial institutions | 6,255 | 349,239 | 134,470 | 36,213 | 519,922 | 526,177 |
| Financial assets at fair value through profit or loss | 45,947 | 4,039 | – | – | 4,039 | 49,986 |
| Loans to banks and financial institutions | 4,964 | – | – | – | – | 4,964 |
| Loans and advances to customers at amortized cost | 484,332 | 1,570,743 | 89,962 | 20,465 | 1,681,170 | 2,165,502 |
| Loans and advances to related parties at amortized cost | 2,845 | 3,490 | 36 | 25 | 3,551 | 6,396 |
| Debtors by acceptances | – | 26,674 | 3,424 | – | 30,098 | 30,098 |
| Financial assets at amortized cost | 1,098,167 | 1,133,844 | 17,315 | – | 1,151,159 | 2,249,326 |
| Investment in a subsidiary | – | – | – | 6,320 | 6,320 | 6,320 |
| Property and equipment | 51,376 | – | 97 | – | 97 | 51,473 |
| Assets obtained in settlement of debt | 36 | 52,324 | – | – | 52,324 | 52,360 |
| Other assets | 5,745 | 4,438 | 44 | – | 4,482 | 10,227 |
| **Total assets** | **2,126,453** | **3,718,243** | **283,173** | **64,719** | **4,066,135** | **6,192,588** |
| **Financial liabilities** | | | | | | |
| Due to central bank | 38,503 | – | – | – | – | 38,503 |
| Due to banks and financial institutions | 9,688 | 31,352 | 17,459 | 19 | 48,830 | 58,518 |
| Due to banks under repurchase agreements | – | 90,973 | – | – | 90,973 | 90,973 |
| Deposits from customers | 1,761,224 | 3,300,287 | 261,824 | 34,779 | 3,596,890 | 5,358,114 |
| Deposits from related parties | 4,670 | 4,153 | 251 | 40 | 4,444 | 9,114 |
| Engagements by acceptances | – | 26,674 | 3,424 | – | 30,098 | 30,098 |
| Other liabilities | 49,631 | 1,812 | 54 | – | 1,866 | 51,497 |
| Provisions for risks and charges | 27,848 | – | – | – | – | 27,848 |
| **Total liabilities** | **1,891,564** | **3,455,251** | **283,012** | **34,838** | **3,773,101** | **5,664,665** |
| **Net exposure** | **234,889** | **262,992** | **161** | **29,881** | **293,034** | **527,923** |

**Bank's sensitivity to currency exchange rates**

The table below shows the currencies to which the Bank has significant exposure at 31 December 2017 and 2016 on its monetary assets and liabilities and its forecast cash flows. The analysis calculates the effect of a reasonably possible movement of the currency rate against the Lebanese Pound, with all other variables held constant, on the income statement (due to the potential change in fair value of currency sensitive monetary assets and liabilities). A negative amount reflects a potential net reduction in income while a positive amount reflects a net potential increase.

| Currency | Change in currency rate % | 2017 Effect on profit before tax | 2016 Effect on profit before tax |
|---|---|---|---|
| US Dollar | 5 | +/-11,118 | +/-10,402 |
| Euro | 5 | +/-8 | +/-4 |
| Other currencies | 5 | +/-1,493 | +/-1,178 |

**Prepayment risk**
Prepayment risk is the risk that the Bank incurs a financial loss because its customers and counterparties repay or request repayment earlier than expected, such as fixed rate housing loans when interest rates fall. The fixed rate financial assets of the Bank are not significant compared to the total assets. Moreover, other market conditions causing prepayment are not significant in the markets in which the Bank operates. Therefore, the Bank considers the effect of prepayment on net interest income as not material after taking into account the effect of any prepayment penalties.

### 35.5 Operational risk

Operational risk is the risk of loss arising from systems failure, human error, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to financial loss. The Bank cannot expect to eliminate all operational risks, but through a control framework and by monitoring and responding to potential risks, the Bank is able to manage the risks. Controls include effective segregation of duties, access, authorization and reconciliation procedures, staff awareness and assessment of processes, including the use of internal audit.

## 36 Capital management

By maintaining an actively managed capital base, the Bank's objectives are to cover risks inherent in the business, to retain sufficient financial strength and flexibility to support new business growth, and to meet national and international regulatory capital requirements at all times. The adequacy of the Bank's capital is monitored using, among other measures, the rules and ratios established by the Central Bank of Lebanon of Basic Circular No 44 and related amendments (latest in March 2014). These ratios measure capital adequacy by comparing the Bank's eligible capital with its statement of financial position assets and off-financial position commitments at a weighted amount to reflect their relative risk. To satisfy Basel III capital requirements, the Central Bank of Lebanon requires maintaining the below capital adequacy requirements for 2016, 2017, and 2018.

The bank must achieve a total regulatory capital to risk-weighted assets at or above 14% in 2016, 14.5% in 2017, and 15% in 2018.

Common Equity tier 1 Ratio should increase to 8.5% in 2016, 9% in 2017, and 10% in 2018.

Tier 1 Ratio should increase to 11% in 2016, 12% in 2017, and 13% in 2018.

**In millions of LBP** **31 December**

| Risk weighted assets | 2017 | 2016 |
|---|---|---|
| Credit risk | 3,547,132 | 3,430,821 |
| Market risk | 109,457 | 94,945 |
| Operational risk | 184,359 | 184,081 |
| Total risk weighted assets | 3,840,948 | 3,709,847 |

The capital base as per Basel III requirements as of 31 December is as follows:

**In millions of LBP** **31 December**

| | Excluding net income for the year | | Including net income for the year less proposed dividends | |
|---|---|---|---|---|
| | 2017 | 2016 | 2017 | 2016 |
| Tier 1 Capital | 488,772 | 452,001 | 544,047 | 495,386 |
| Tier 2 Capital | 17,116 | 34,196 | 17,116 | 34,196 |
| Total Capital | 505,888 | 486,197 | 561,163 | 529,582 |

The Bank manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of its activities.

The capital adequacy ratio as of 31 December is as follows:

**In millions of LBP** **31 December**

| | Excluding net income for the year | | Including net income for the year less proposed dividends | |
|---|---|---|---|---|
| | 2017 | 2016 | 2017 | 2016 |
| Capital adequacy - Tier 1 | 12.73% | 12.18% | 14.16% | 13.35% |
| Capital adequacy - Total Capital | 13.17% | 13.11% | 14.61% | 14.28% |

# 10

# List of Major Correspondents

## NORTH AMERICA

**CANADA**
- Bank of Montreal

**UNITED STATES OF AMERICA**
- The Bank of New York Mellon
- Standard Chartered Bank

## SOUTH AMERICA

**BRAZIL**
- Banco Safra SA

## EUROPE

**AUSTRIA**
- Unicredit Bank Austria AG

**BELGIUM**
- KBC Bank N.V

**DENMARK**
- Danske Bank A/S
- Saxo Bank A/S

**FINLAND**
- Danske Bank A/S

**FRANCE**
- Natixis
- Banque Fédérative du Crédit Mutuel - CIC
- Union De Banques Arabes et Francaises - UBAF

**GERMANY**
- Commerzbank AG
- Deutsche Bank AG
- The Bank of New York Mellon

**ITALY**
- Intesa Sanpaolo SPA
- Unicredit SpA
- Banca UBAE SPA

**SPAIN**
- Banco de Sabadell S.A.

**SWEDEN**
- Skandinaviska Enskilda Banken AB

**SWITZERLAND**
- Banque de Commerce et de Placements SA

**TURKEY**
- Turkiye Is Bankasi AS
- A&T Bank
- Turkiye Garanti Bankasi AS
- Yapi Ve Kredi

**UNITED KINGDOM**
- Standard Chartered Bank

## AUSTRALIA

**AUSTRALIA**
- Standard Chartered Bank

## ASIA

**CHINA**
- Bank of China Limited ltd
- Industrial and Commercial Bank of China LTD
- Standard Chartered Bank (China) Ltd

**INDIA**
- Indian Overseas Bank
- Mashreqbank PSC
- Canara Bank

**JAPAN**
- Sumitomo Mitsui Banking Corporation

**KOREA**
- KEB Hana Bank

**MALAYSIA**
- Malayan Banking Berhad

**PHILIPPINES**
- Philippines National Bank

**SRI LANKA**
- Bank of Ceylon

**THAILAND**
- Export-Import Bank of Thailand

## MIDDLE EAST & NORTH AFRICA

**BAHRAIN**
- Mashreqbank PSC
- The Housing Bank for Trade & Finance

**EGYPT**
- Mashreqbank PSC

**JORDAN**
- The Housing Bank for Trade & Finance

**KUWAIT**
- Burgan Bank SAK
- The Gulf Bank K.S.C.

**MOROCCO**
- Banque Marocaine du Commerce Exterieur SA
- Attijariwafa

**QATAR**
- Doha Bank
- Qatar National Bank SAQ

**SAUDI ARABIA**
- The National Commercial Bank

**TUNISIA**
- Banque de Tunisie SA
- Banque Internationale Arabe de Tunisie SA

**U.A.E.**
- Mashreqbank PSC
- Emirates NBD
- First Abu Dhabi Bank

# 11

# Head Office & Branches Network

## HEAD OFFICE

LGB BANK HEADQUARTERS
Allenby Street, Beirut Central District
P.O. Box: 11-3600 Riad El Solh, Lebanon
Tel: +961 1 965000 / Fax: +961 1 965699
Swift: LGBALBBE
E-mail: info@lgbbank.com
Website: www.lgbbank.com

## DEALING ROOM

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Fax: +961 1 965499
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## AFFILIATED AND PARTICIPATIONS

- CSCBank SAL
- Société Financière du Liban S.A.L
- Banque de L'Habitat S.A.L
- Société de Garantie des Prêts aux Petites et Moyennes Entreprises S.A.L

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