ANNUAL REPORT AND ACCOUNTS | 2017

مؤسسة الخليج للاستثمار
Gulf Investment Corporation

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MISSION **STATEMENT**

GIC's mission is to foster the economic growth, the economic diversity, and the capital markets development of the GCC.

FINANCIAL **HIGHLIGHTS**

(US$ million) For the year	2015	2016	2017
Gross Operating and Other Income	209	133	236
Operating Expenses	57	54	55
Net Profit	110	57	121
At year end			
Total Assets	5,097	4,592	4,228
Interest Bearing Securities and Funds	1,969	1,584	1,168
Equities and Managed Funds	611	619	536
Projects and Equity Participations	1,376	1,565	1,873
Deposits	919	570	571
Shareholders› Equity	2,491	2,520	2,647
Selected Ratios (%)			
Profitability			
Return on Paid-up Capital	5.2	2.7	5.8
Return on Adjusted Shareholders› Equity	4.0	2.1	4.6
Capital			
BIS Ratios			
- Total	45.9	45.6	40.5
- Tier 1	45.9	45.6	40.5
Shareholders› Equity as a % of Total Assets	48.9	54.9	62.6
Asset Quality			
Marketable Securities as a % of Total Assets	44.1	42.5	36.0
GCC Country Risk as a % of Total Assets	63.8	75.9	79.8
Liquidity			
Liquid Assets Ratio	65.1	62.3	52.4
Productivity			
Operating Income as Multiple of Operating Expenses	3.7	2.5	4.3

BOARD OF **DIRECTORS**

State of Qatar

H.E. Shaikh Fahad Faisal Al-Thani * ****

Chairman of the Board

Minister of State

H.E. Dr. Hussain Ali Al-Abdula Al-Abdulla ** ***

Minister of State & Board Member
Qatar Investment Authority

State of Kuwait

H.E. Mr. Bader Al-Ajeel * ***

Chairman of the Executive Committee

Executive Director - General Reserve Sector
Kuwait Investment Authority

H.E. Mr. Faisal M.H. Boukhadour ** ****

Advisor in the Diwan of H.H.,
the Prime Minister

United Arab Emirates

H.E. Mr. Faisal Ali Almansouri * ***

Director of Macro-Fiscal Policy,
Ministry of Finance

H.E. Mr. Majed Ali Omran Al Shamsi ** ****

Chairman of Audit Committee

Advisor at the Ministry of Finance

Kingdom of Bahrain

H.E. Mr. Mazen Ibrahim Abdulkarim * ****

Businessman

H.E. Mr. Hesham Khonji ** ***

Chairman of the Risk Management Committee

Head of Treasury and Capital Markets
Bahrain Mumtalakat Holding Company B.S.C.

Kingdom of Saudi Arabia

H.E. Mr. Khaled S. Al-Khattaf * ***

CEO of Lafana Investment Company

H.E. Mr. Turki Almalik ** ****

Chairman of Remuneration
and Human Resources Committee

Deputy Chief Executive Officer
Chief Operations Officer,
Sanabil Investments Company

Sultanate of Oman

H.E. Mr. Abdulsalam Mohammed Al Murshidi * ****

Executive President,
State General Reserve Fund

H.E. Mr. Darwish Ismail Ali Al-Bulushi ** ***

Minister Responsible for Financial Affairs,
Ministry of Finance

* Member of the Executive Committee

** Member of the Audit Committee

*** Member of the Risk Management Committee

**** Member of the Remuneration and Human Resources Committee

CHAIRMAN'S **STATEMENT**

On behalf of the Board of Directors, it is my privilege to present the Annual Report on the Corporation's activities and its financial results for the year ended 31 December 2017. The Corporation continued its success despite the economic and geopolitical challenges which reflects its accumulated operational experience in dealing effectively within an evolving business environment, gained over three decades.

The working environment surrounding the Corporation has witnessed significant developments, the most of which was the change in GCC fiscal policies resulting from the budget deficit of some GCC countries. Other developments include, the tendency of interest rates to rise; the implementation of economic reform policies and the continued geopolitical risks surrounding the region. Despite the direct and indirect impact of these developments on investment activities, the Corporation, through its well-diversified and geographically distributed investment mix, has reported net profits of US $121 million in 2017, more than double of previous year result. These profits come after US $60 million of provisions for the investment portfolio. These results have been achieved through the contribution of the Corporation's main business lines, Principal Investments and Global Markets. In this context, it should be noted that the Corporation adheres to strict standards in terms of capital adequacy ratios, asset quality, liquidity ratios, cash flows and prudent risk management. This has been reflected in the achievement of good financial indicators as detailed in this year's Annual Report.

In parallel to the improvement in the financial performance indicators, the Corporation has supported the portfolio of principal investment in some of the new projects operating in promising sectors, in which the Corporation sees opportunities for growth and value added for the GCC countries, such as the UAE-based Tri-Star that works in the logistics sector, Sudair Pharmaceutical Manufacturing plant in the Kingdom of Saudi Arabia, as well as a stake in Horizon Investment for Education in the UAE. In addition, the Corporation led-consortium has been selected for undertaking Solid Waste Project (Kabad) in the State of Kuwait which is a PPP project for an investment period of 25 years. It is noteworthy that the portfolio includes investments in various sectors such as infrastructure, energy, services, metals and petrochemicals.

The Board of Directors adopted a new investment policy to be implemented in 2018, aimed at reducing the leverage to avoid escalating borrowing costs as interest rates rise and focus more on principal investment while maintaining exposure to global investments to distribute risk and maximize returns. As part of this trend, the Corporation has succeeded in reducing the leverage ratio in 2017 after redemption of maturing bonds amounting to US $500 million.

GIC has established its pioneering position in the region, through its strong financial position and its dedicated human capital. This has been evidenced by the reaffirmation of both Moody's and Fitch of the Corporation's credit rating in 2017 at A2 and A- respectively, with a stable outlook. These rating affirmations are a consequence of the continuous improvement in key financial indicators of the Corporation, despite global and regional economic challenges and uncertainties, which encourage us for more achievements in the future.

Finally, on behalf of the Board of Directors, I wish to take this opportunity to extend my appreciation to their Royal Highnesses, Kings and Emirs, rulers of the GCC countries for their continuous support. Special thanks to the State of Kuwait for hosting GIC's headquarters, and for providing all necessary business needs. I would also like to extend my appreciation to their Excellences Ministers of Finance of the Gulf Cooperation Council for their support. I would also like to express my appreciation to the Board of Directors and all members of the executive management, and staff for their commitment and effort during the year in achieving the Corporation's goals.

H.E. Shaikh Fahad Faisal Al-Thani

Chairman

CEO'S STATEMENT

The Corporation recorded commendable growth in profits during 2017 with net operating profits, before provisions, reaching US $181 million. Net provisions of US $60 million were provided to offset the decline in the fair value of certain investments, resulting in reported profits of US $121 million, compared to US $57 million in the previous year. Principal investments and investment in the global markets contributed to these gains. Several factors were behind this improvement in the business results including improved operational performance of some of the key projects; a significant improvement in hedge fund profits; higher stock trading profits and higher exit earnings from private equity funds compared to last year.

These results have been achieved despite the challenging economic conditions surrounding the Corporation as the regional business environment faced several challenges. The major challenges included the continuing budget deficits which led to reconsidering subsidies and fees on services and commodities; squeezing profitability of various economic sectors and increasing geopolitical risks. Above all, the budget deficits have led to downgrading of various GCC countries' sovereign credit ratings. In addition, global markets had witnessed a continuation of the wave of interest rate hikes which negatively impacted the performance of all capital markets, particularly fixed income.

In a sign of the excellent performance, solid financial position and positive cash flow, Moody's affirmed the long-term rating of GIC at A2 and its short-term rating at P1 with a stable outlook. Fitch concurred its long-term ratings at A- and short-term rating at F1, with a stable outlook. In addition, Malaysia's RAM agency reaffirmed its AAA credit rating with a stable outlook.

By the end of 2017, the Board of Directors adopted a new business strategy to guide the Corporation towards implementing an investment policy aimed at achieving the highest possible returns within acceptable risk levels, through investments allocation, in addition to measuring performance against market indices. Based on this investment policy, the management has taken operational measures to evaluate the portfolio of projects; reallocate the financial investment portfolio and move towards reducing financial liabilities in the context of interest rates rise and increasing the risk perceived from investing in capital markets.

During the year 2017, the Corporation continued its record investment activity which started four years ago. The Corporation acquired a stake in United Arab Emirates' Tri-Star, which operates in the field of logistics, for US $100 million. Likewise, the Corporation acquired a stake in the Sudair Pharmaceutical Manufacturing plant in Saudi Arabia for US $24 million and a stake in Al-Horizon for investment in education for US $55 million. During the year, the Corporation led-consortium has been selected for undertaking Solid Waste Project (Kabad) in the State of Kuwait with a total investment of US $900 million, which is a PPP project for an investment period of 25 years, in which the Corporation contributes 15%.

I would like to take this opportunity to thank the shareholders, the Board of Directors and its sub-committees for their continued support and valuable strategic guidance. I would also like to express my appreciation of the efforts, commitment and dedication to GIC staff. I am proud of what we accomplished in 2017 and even more excited about the opportunities that lie ahead. This represents a motivation to continue our success and contributes effectively in supporting GCC's economic development and helps bring added value to our shareholders.

Ibrahim Al-Qadhi
CEO

ECONOMIC
REVIEW

1. INTRODUCTION

The GCC economies continued to implement substantial fiscal consolidation during the year, mainly focused on expenditure reduction. However, this has weakened non-oil growth initially but as the pace of fiscal consolidation slow, non-oil growth eventually increased in 2017 to 2.6%, from 1.8% in 2016. In addition, the recovery in oil prices during the second half of the year as well as improving non-hydrocarbon GDP growth, and lowering the overall fiscal balance helped the region to sustain a lower real GDP growth of 0.5% in 2017, than its 2.2% pace in 2016.

In addition, a broad based cyclical global recovery continued in 2017 supported by a rebound in investment and trade particularly in advanced economies. The pickup in global growth has been broad based as well with notable upside surprises in Europe and Asia. This growth upturn was driven by favorable financing conditions, generally accommodative policies, improved confidence and firming commodity prices. The rebound in energy prices raised headline inflation in advanced economies, but wage and core price inflation remained weak. Among EM economies, headline and core inflation ticked up slightly later of the year after declining earlier in 2017. During the year, the low interest rate environment and improved global growth outlook supported a search for yield and strong demand for emerging market and developing economies (EMDEs) assets. However, financial markets have seen a sustained run up in asset prices and very low volatility, despite policy and geopolitical uncertainties.

The economic review below is in four sections. The first section deals with global economy, as it illustrates major developments in GDP growth, inflation, macro policies, capital flows and trade. The second section reviews oil market dynamics. The third section reviews GCC economies, while the last section tracks developments in GCC equity markets.

1.1. Global Growth

The global GDP growth picked up to 3.7% in 2017, from 3.2% in 2016. This upside growth was evident in Europe and Asia and was driven by a rebound in global investment growth accompanied by solid employment gains and policy stimulus. The pickup in investment, particularly among advanced economies, provided a substantial boost to global exports and imports and global trade gathered significant momentum since mid-2016 and become increasingly broad based across economies. Trade volume grew by 4.8% in 2017, compared to 2.6% in 2016, largely due to a recovery in import demand from both advanced economies and EMDEs. This trade upturn was driven by the recovery in Europe, the strong pick up in electronic trade in Asia, and a shift in the composition of demand towards investment, which was more import intensive[1].

Table 1: Real GDP and Trade Growth, Regional Comparison

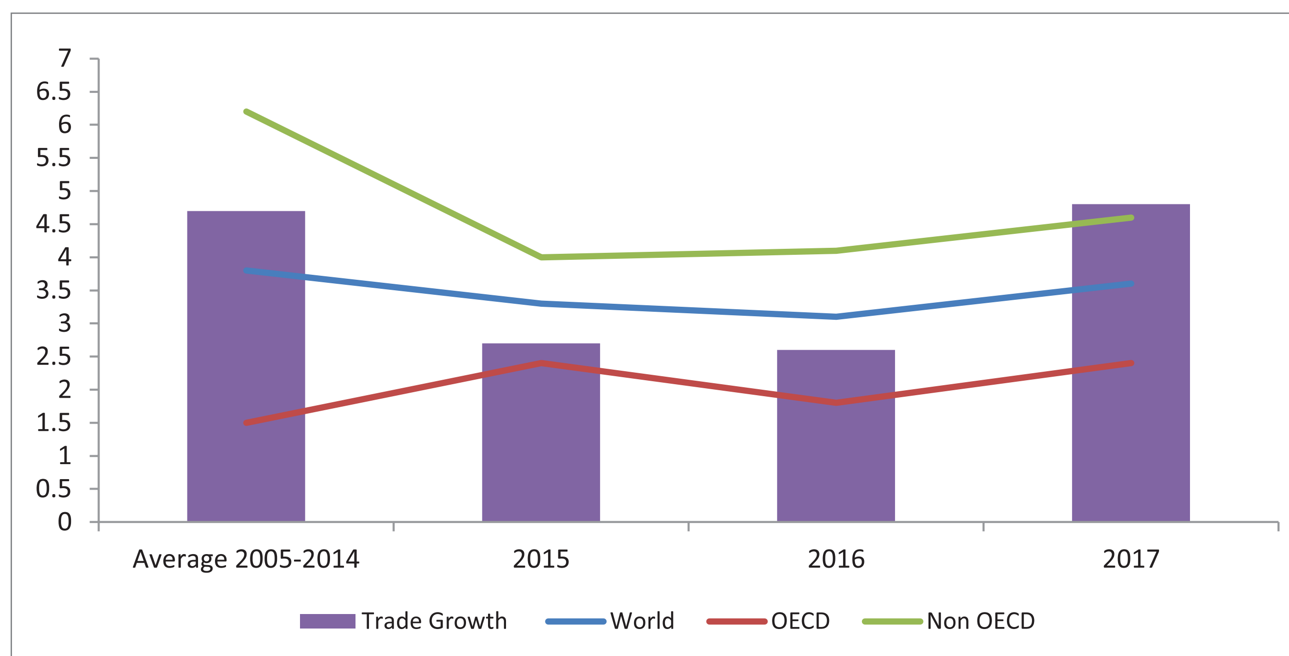
Real GDP growth	Average 2005-2014	2015	2016	2017
World	**3.8**	**3.3**	**3.1**	**3.6**
OECD	1.5	2.4	1.8	2.4
United States	1.5	2.9	1.5	2.2
Euro area	0.8	1.5	1.8	2.4
Japan	0.6	1.1	1.0	1.5
Non-OECD	6.2	4.0	4.1	4.6
China	10.0	6.9	6.7	6.8
World Real Trade Growth	**4.7**	**2.7**	**2.6**	**4.8**

Source: OECD Economic Outlook, Volume 2017 Issue 2, December 2017.

Figure 1 show regional growth estimates for both real GDP and trade growth according to the OECD economic outlook which estimates global GDP growth at 3.6% and trade volume growth at 4.8%.

1. IMF, WEO Update & World Bank, "Global Economic Prospects" January 2018.

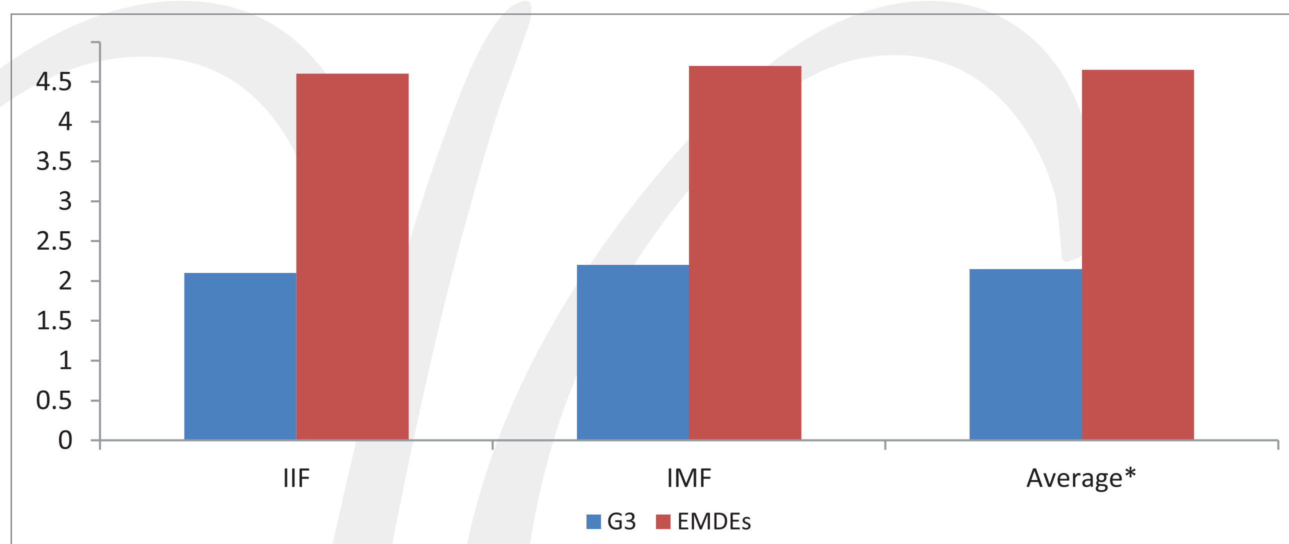
Figure 1: Real Global GDP and Trade Growth, y-o-y (% Change)



Source: OECD Economic Outlook No 102, November 2017.

In advanced economies, growth rebounded to 2.3%, driven by a pickup in capital spending and exports, an improvement in inventories, and strengthening external demand. While growth accelerated in all major economies, the improvement was markedly stronger than expected in the Euro Area. Figure 2 shows that aggregate GDP in G3 grew by 2.2% on average in 2017 while that of emerging markets and developing economies (EMDEs) grew by 4.5% based on consensus forecasts of the IIF and the IMF.

Figure 2: Comparison of GDP Growth Forecasts in 2017, (% Change)



**Simple Average.*

Source: IMF, January 2018 & IIF Forecast Table, December 2017.

The US growth picked up in 2017 to 2.3%, from 1.5% in 2016, supported by strengthening private investment. This recovery reflected a diminished drag from capacity adjustments in the energy sector, rising profits, a weakening dollar, and robust external demand. Also, private consumption continued to grow at a robust pace despite modest real income gains and moderate wage growth, as the personal savings rate fell further. Households' income expectations continued to recover following a prolonged period of weakness and labor market slack diminished further though employment growth slowed[2].

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2. *World Bank, "Global Economic Prospects" January 2018.*

In the Euro Area, growth gained substantial momentum in 2017, edging up to 2.4%, from 1.8% in 2016, with broad based improvements across member countries supported by policy stimulus, stronger momentum in domestic demand and higher external demand. In particular, private sector credit continued to respond to the expansionary stance of the European Central Bank (ECB), and both domestic demand and import growth were robust. The unemployment rate reached its lowest level since 2009, and labor shortages became increasingly prevalent in some countries though wage growth remained subdued[3].

In the UK, GDP growth eased to 1.7% y-o-y, in 2017, from 1.9% in 2016, despite a strong global growth and supportive macroeconomic policies as the impact of the decision to exit the European Union weighed on private domestic demand. Business investment growth was lower than would be expected in the context of strong global growth and high levels of capacity utilization, owing to heightened uncertainty about economic prospects. The softening of domestic demand was partially offset by a rise in goods exports, supported by strong growth in trading partners and weaker sterling. The employment rate has remained around record highs, but the sharp depreciation of sterling following the referendum pushed up consumer price inflation, squeezing household real income and consumption[4].

In Japan, growth picked up in 2017 to 1.8% from 0.9% in 2016 as domestic demand strengthened, supported by a gradual recovery in consumer spending and investment, the implementation of a fiscal stimulus package, and highly accommodative financial conditions. Exports accelerated in response to strengthening global demand, but the net trade contribution to growth remained unchanged as imports picked up as well. Labor market conditions continued to tighten and business sentiment continued to improve with the unemployment rate at a 22-year low amid growing labor shortages[5].

Growth among EMDEs accelerated to 4.7% in 2017, reflecting firming activity in commodity exporters and continued sloid growth in commodity importers. The recovery in commodity Exporters, notably Brazil and Russia, with 1.8% pace of growth reflected an upturn in private consumption and investment amid improved confidence and diminishing drag from earlier policy tightening. The contribution of net exports declined in commodity exporters, as import growth rebounded substantially. Among the largest commodity exporters, growth in Brazil rebounded to an estimated 1.1% in 2017 following two years of contraction, reflecting a recovery of domestic demand supported by easier monetary conditions and improved confidence. In Russia, activity in 2017 was stronger than previously expected, with growth reaching an estimated 1.8%, in response to higher oil prices, banking sector support, targeted fiscal stimulus, and reduced external imbalances amid exchange rate flexibility.

In commodity importers, growth remained robust in 2017, at 6%, supported by solid domestic demand and strong exports. Excluding China, growth was 5.1%, reflecting a continued strong contribution from India. Accommodative policies, amid easing global financing conditions and low inflation, supported domestic demand. In particular, investment growth generally strengthened, although it varied across regions. Meanwhile, export and import growth accelerated, reflecting firming global and domestic demand, respectively[6].

In China, growth edged up slightly to 6.8% in 2017, from 6.7% in 2016, reflecting continued fiscal support and the effects of reforms, as well as a stronger-than expected recovery of exports and a slight positive contribution from net trade. Domestic rebalancing continued, with drivers of activity shifting away from state-led investment. China's trade flows recovered markedly in 2017, partly reflecting rising commodity imports amid tightly enforced production cuts as well as strengthening foreign demand. In India, the economy continued to strengthen, albeit at a slower pace, with GDP growth eased to 6.7% y-o-y in 2017, from 7.1% in 2016 despite some disruptions related to idiosyncratic factors such as adjustment to the new goods and services tax[7].

1.2. Inflation

Despite the strengthening of activity, Inflation in advanced economies remained subdued in 2017. In the euro area, wage growth moderated and the appreciation of the euro during the year delayed a pickup in inflation as it put downward pressure on import prices. Likewise, wage growth moderated in Japan with inflation below 1%. Median headline inflation rates recovered in advanced OECD economies in 2017 to 1.6%, up from 0.98% in 2016, largely due to the increase in fuel prices but wage and core price inflation remained weak. In the US, the annual percentage change of headline inflation eased to 1.5% in the fourth quarter of 2017, from 1.6% in Q42016. While headline inflation remained flat in Japan, at 0.3%, it increased in the Euro Area to 1.4%, from 0.7% in 2016. Core inflation fell in the US to 1.4% and turned into a mild deflation in Japan at -0.09%, but increased in the Euro Area to 1.3% in the fourth quarter of the year[8].

Among emerging market economies, headline and core inflation ticked up slightly at the yearend after declining earlier in 2017. Median headline inflation in EMDEs eased to 3.0% in the fourth quarter of the year, slightly down from 3.3% in Q42016. In China, consumer price inflation increased steadily throughout the year but remained below target, while producer price inflation was stable, supporting a recovery of industrial profits. Consumer price inflation in EMDEs fell to 4.1% on average in 2017, from 4.3%. It eased to 4.2% and 2.6% in both Latin America and Emerging Asia respectively, but it edged up to 6.8% and 6.0% both in MENAP and Emerging Europe regions respectively, from 5.1% and 3.3% in 2016[9].

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3. IMF, WEO Update, January 2018.

4. IMF, 2017 UK Article IV, December 20, 2017.

5. BOJ "Summary of Opinions at the Monetary Policy Meeting, December 20-21, 2017.

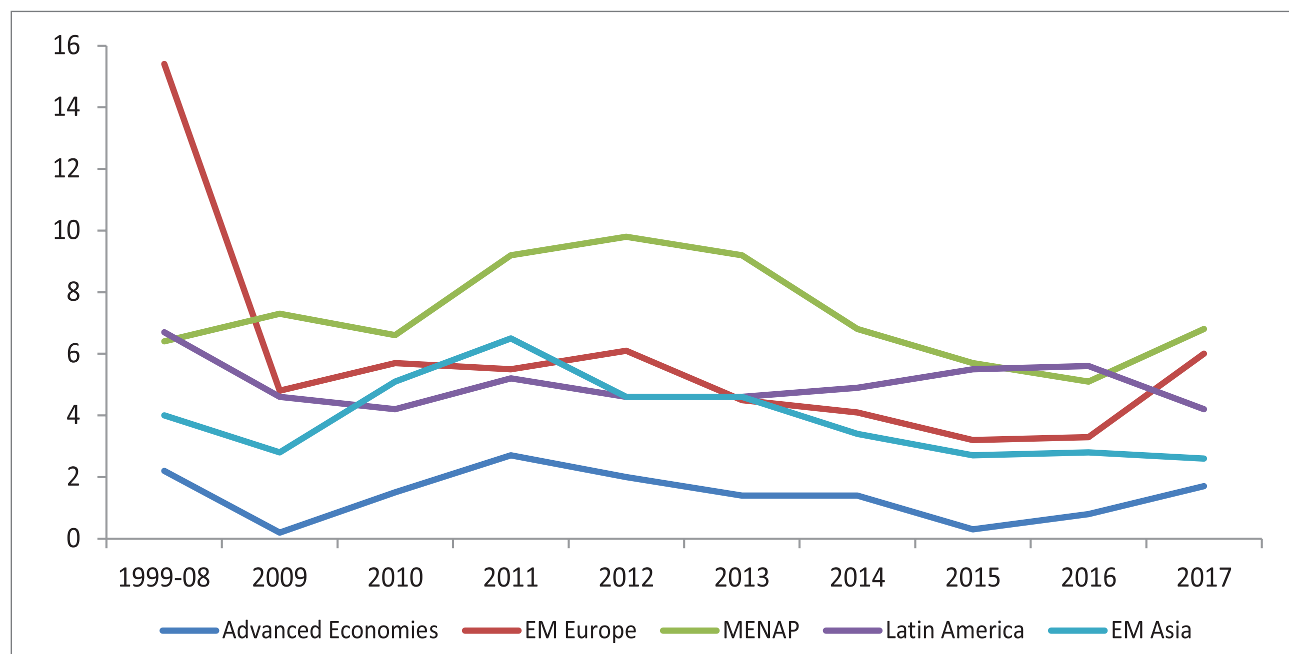
6. World Bank, "Global Economic Prospects" January 2018.

7. World Bank, "Global Economic Prospects" January 2018.

8. OECD Economic Outlook, volume 2017 Issue 2 December 2017.

9. IMF, WEO Update, January 2018 & IMF WEO October 2016.

Figure 3: Consumer Prices across EM Regions (Annual % change)



Source: IMF.

1.3. Financial Markets

Easy financing conditions continued globally, benefiting from an improved global growth outlook and historically low interest rates, despite prospects of further monetary policy normalization in major advanced economies. Despite prospects of tighter monetary policy, US and Euro Area bond yields remained at historically low levels throughout 2017, reflecting subdued inflation trends and expectations of structurally low real interest rates[10]. Amid low nominal and real interest rates, financial market volatility remained subdued despite policy and geopolitical uncertainties. Stronger-than-expected growth in the Euro Area combined with a relatively stable outlook for the US economy has contributed to some weakening of the US dollar, following three years of significant appreciation. Highly accommodative financing conditions in major advanced economies supported a search for yield and strong demand for EMDEs assets in 2017. This was reflected in declining bond spreads, particularly for EMDEs investment grade borrowers, and an increase in capital flows, including portfolio and international bond issuances. Among commodity-exporting EMDEs, the declining effect of the terms-of-trade shock, combined with moderating inflation and external imbalances, helped support market sentiment. Overall, capital inflows rose as a share of EMDEs GDP in 2017, recovering further from their post crisis low in 2015. The increase was particularly notable in Asia and Eastern Europe and Central Asia, while flows into Latin America remained weak. A rise in portfolio and bank lending flows were the main drivers of the overall improvement. Although foreign direct investment (FDI) flows were broadly stable in aggregate, the experience varied across regions. FDI flows to Asia remained strong supported by a robust growth outlook and policy efforts to attract foreign investment. FDI inflows to Middle East and North Africa posted modest growth, supported by privatization plans and improvements in business regulations[11].

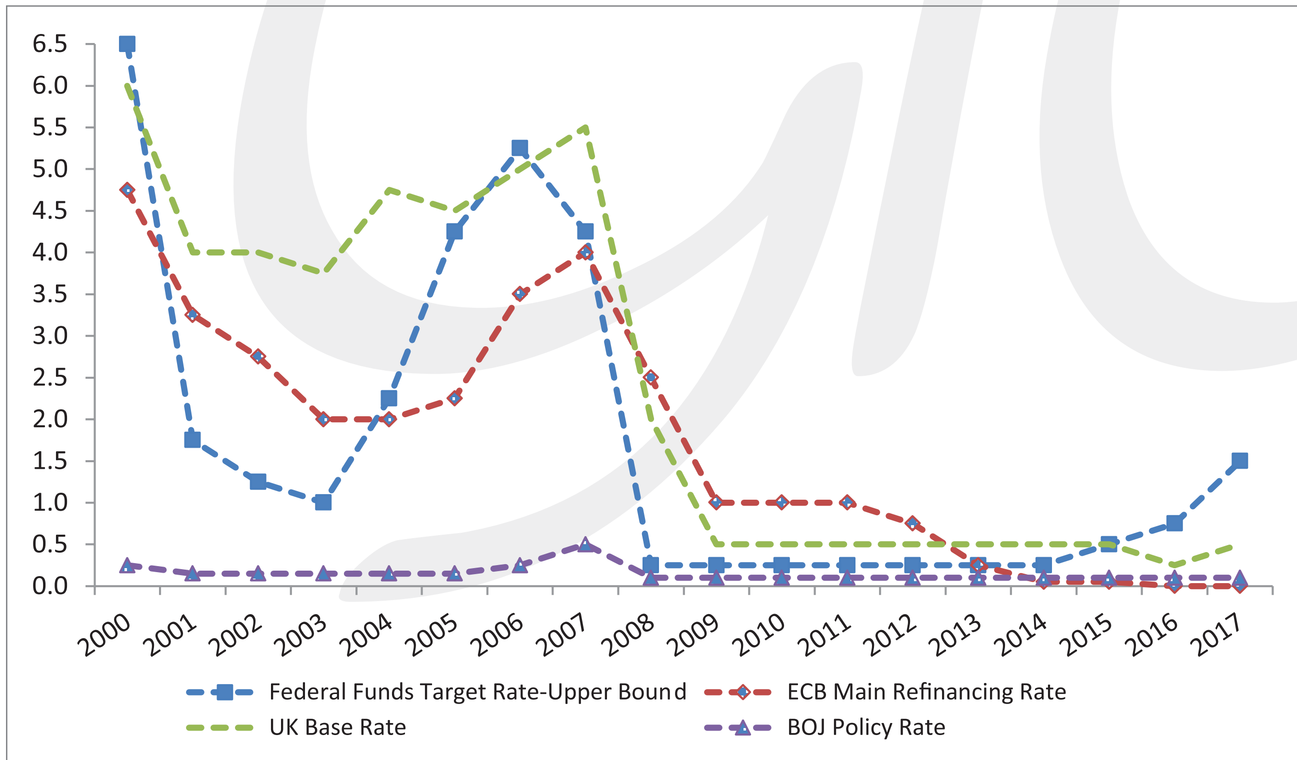
1.3.1. Monetary Policy and Central Banks' Balance Sheets

G4 central bank assets continued to climbs as a percentage of GDP, reaching 37.6% in 2017. As its June meeting, the Fed announced it would begin shrinking its balance sheet by $ 10 billion a month, dropping its assets to $ 4.44 trillion by December, or 23% of GDP. In contrast, other major central banks continued to expand their assets as central banks in both the euro area and Japan increased the size of their stimulus measures. During the year, the ECB continued to buy corporate bonds, raising its total assets over $ 5.3 trillion, or about 40% of the euro area GDP. It remained far behind Japan however, with the BOJ $ 4.6 trillion total assets are equivalent to about 93% of the country's GDP[12].

10. Rachel, L., and T.D. Smith, "Are Low Real Interest Rates Here to Stay" International Journal of Central Banking, 2017.
11. World Bank, "Global Economic Prospects" January 2018.
12. Global Economic Briefing, Yardeni Research, January 2018.

With the economy moving closer to full employment, and despite inflation running below target, the US Federal Reserve continued to normalize monetary policy in 2017, raising policy interest rates three times and by a cumulative 125 basis points since the start of its tightening cycle in December 2015. It also began to gradually reduce the size of its balance sheet in October 2017. The European Central bank (ECB) maintained its policy rates unchanged at its historically low levels. The Bank of England raised its policy rate in November 2017 for the first time since 2007 by 0.25% to 0.50% in view of diminishing slack in the economy and above target inflation driven by the past sterling appreciation. In this context, the Bank of Japan left policy rates unchanged in 2017 and continued to adjust its bond purchases to stabilize long-term bond yields around zero[13].

Figure 4: The Fed and ECB Benchmarks (%)



Source: Bloomberg, December 2017.

Table 2 exhibits the level of short term interest rates pre and post the global financial crisis. By December 2017, policy rates ranged between 0.0% in the Euro area, 0.10% in Japan, 0.50% in the UK, 1.0% in Canada and 1.5% in the US. Monetary policy stances varied across emerging market economies during the year, reflecting these economies' diverse cyclical positions. In India, rising price pressures, along with firming economic growth, kept the policy repo rate unchanged at 6.0% but reduced reverse repo rate to 5.75%. In China, the central bank raised the reverse repo rate to 2.5% in response to the market uptrend and to contain leverage[14].

13. IMF, WEO Update, January 2018.
14. Financial Times, December 14, 2017.

Table 2: Short-Term Policy Rates (%)

Date	USA	Canada	Euro Area	UK	Japan	China*	India
Q1 2008	2.25	3.50	4.00	5.25	0.50	NA	6.00
Q2 2008	2.00	3.00	4.00	5.00	0.50	NA	6.00
Q3 2008	2.00	3.00	4.25	5.00	0.50	NA	6.00
Q4 2008	0.25	1.50	2.50	2.00	0.10	NA	5.00
Q1 2009	0.25	0.50	1.50	0.50	0.10	NA	3.50
Q2 2009	0.25	0.25	1.00	0.50	0.10	NA	3.25
Q3 2009	0.25	0.25	1.00	0.50	0.10	NA	3.25
Q4 2009	0.25	0.25	1.00	0.50	0.10	NA	3.25
Q1 2010	0.25	0.25	1.00	0.50	0.10	NA	3.50
Q2 2010	0.25	0.50	1.00	0.50	0.10	NA	3.75
Q3 2010	0.25	1.00	1.00	0.50	0.10	NA	5.00
Q4 2010	0.25	1.00	1.00	0.50	0.10	NA	5.25
Q1 2011	0.25	1.00	1.00	0.50	0.10	NA	5.75
Q2 2011	0.25	1.00	1.25	0.50	0.10	NA	6.50
Q3 2011	0.25	1.00	1.50	0.50	0.10	NA	7.25
Q4 2011	0.25	1.00	1.00	0.50	0.10	NA	7.50
Q1 2012	0.25	1.00	1.00	0.50	0.10	NA	7.50
Q2 2012	0.25	1.00	1.00	0.50	0.10	3.30	7.00
Q3 2012	0.25	1.00	0.75	0.50	0.10	3.35	7.00
Q4 2012	0.25	1.00	0.75	0.50	0.10	3.35	7.00
Q1 2013	0.25	1.00	0.75	0.50	0.10	3.35	6.50
Q2 2013	0.25	1.00	0.50	0.50	0.10	3.35	6.25
Q3 2013	0.25	1.00	0.50	0.50	0.10	3.90	6.50
Q4 2013	0.25	1.00	0.25	0.50	0.10	4.10	6.75
Q1 2014	0.25	1.00	0.25	0.50	0.10	4.10	7.00
Q2 2014	0.25	1.00	0.15	0.50	0.10	4.10	7.00
Q3 2014	0.25	1.00	0.05	0.50	0.10	4.10	7.00
Q4 2014	0.25	1.00	0.05	0.50	0.10	4.10	7.00
Q1 2015	0.25	0.75	0.05	0.50	0.10	3.55	6.50
Q2 2015	0.25	0.75	0.05	0.50	0.10	2.50	6.25
Q3 2015	0.25	0.50	0.05	0.50	0.10	2.35	5.75
Q4 2015	0.50	0.50	0.05	0.50	0.10	2.25	5.75
Q1 2016	0.50	0.50	0.00	0.50	0.10	2.25	5.75
Q2 2016	0.50	0.50	0.00	0.50	0.10	2.25	6.00
Q3 2016	0.50	0.50	0.00	0.25	0.10	2.25	6.00
Q4 2016	0.75	0.50	0.00	0.25	0.10	2.25	5.75
Q1 2017	1.00	0.50	0.00	0.25	0.10	2.45	5.75
Q2 2017	1.25	0.50	0.00	0.25	0.10	2.45	6.00
Q3 2017	1.25	1.00	0.00	0.25	0.10	2.45	5.75
Q4 2017	1.50	1.00	0.00	0.50	0.10	2.50	5.75

** Bank of China's 7-day Reverse Repurchase rate.*

Source: Bloomberg, December 2017.

1.4. Exchange Rates and Capital Flows

1.4.1. Exchange Rates Movements

The US dollar and the euro remained close to their August level in real effective terms. The Japanese yen has depreciated by 5% on widening interest rate differentials, while the sterling has appreciated by close to 4% as the Bank of England raised interest rates in November and as expectations of a Brexit deal rose. Across emerging market currencies, the renminbi has appreciated by around 2%; the Malaysian ringgit has rebounded by about 7% on an improved growth outlook and stronger commodity prices, and the South African rand by close to 6% on perceptions of reduced political uncertainty. In contrast, the Mexican peso has depreciated by 7% owing to renewed uncertainty associated with the ongoing NAFTA negotiations and the Turkish lira by 4.5% on higher inflation readings. Capital flows to emerging economies have remained resilient through the third quarter of 2017, with continued strength in non-resident portfolio inflows[15].

1.4.2. Total Portfolio Flows to Emerging Markets

Total net non-resident portfolio inflows were $ 9.4 billion in December, with emerging market debt and equity markets receiving $ 5.2 and $ 4.2 billion respectively, closing out the best year for portfolio flows to EMs since 2014 with $ 235.42bn billion in inflows as shown in table 3. Debt Inflows into emerging markets dominated 2017, reaching $ 170.6bn, as EM governments and corporates issued debt at a fast pace. EM Asia region accumulated over half of total flows to EMs, at $ 134.8bn, due to favorable FX considerations, attractive yields, solid credit ratings, strong growth, and further opening of bond markets. As a result, net flows to EMs excluding China, exceeded $ 185 billion in 2017 compared with $ 90 billion in 2016 which enabled EM central banks to accumulate more than $ 132 billion of FX reserves, marking a sharp improvement from massive reserve losses in 2015 and 2016[16].

Table 3: Net Non-Resident Portfolio Flows to Emerging Markets ($bn)

	Emerging Asia	Latin America	Emerging Europe	ME & Africa	Total
Debt Flows					
2014	88.24	90.21	22.55	3.83	204.84
2015	34.40	36.49	11.14	6.88	88.91
2016	14.55	-9.04	20.84	9.94	36.29
2017	97.55	27.60	30.93	14.49	170.56
Total	234.74	145.26	85.45	35.15	500.61
Equity Flows					
2014	52.12	23.79	10.70	4.29	90.90
2015	7.69	18.59	7.69	3.48	37.46
2016	43.75	26.51	1.52	-8.73	63.04
2017	37.22	17.67	11.24	-1.27	64.86
Total	140.77	86.55	31.16	-2.23	256.25
Portfolio Flows (Equity and Debt)					
2014	140.36	113.99	33.26	8.13	295.74
2015	42.09	55.08	18.83	10.37	126.37
2016	58.30	17.47	22.36	1.21	99.33
2017	134.76	45.27	42.17	13.22	235.42
Total	375.51	231.82	116.61	32.92	756.86

Source: IIF, January 2018.

Private capital flows to Emerging Markets increased to $ 769.4 billion in 2017 from $ 639.7 billion in 2016. Emerging Asia and Latin American regions were the largest recipient of private capital flows at $ 348.4 billion and $ 242.1 billion respectively, following $ 277.7 billion and $ 236.3 billion flows in 2016. Likewise, private capital inflows to Emerging Europe and Middle East and Africa regions increased to $ 61.7 billion and $ 117.2 billion respectively[17].

15. IMF, WEO Update, January 2018.
16. IIF "Capital Flows Tracker", January 2018.
17. IIF "Capital Flows Report", December 2017.

Table 4: Private Capital Inflows to Emerging Markets ($bn)

Region	2014	2015	2016	2017
Middle East / Africa	86.6	93.3	99.9	117.2
Latin America	288.2	199.9	236.3	242.1
Emerging Europe	44.3	14.7	25.7	61.7
Emerging Asia	621.3	-44.5	277.7	348.4
Emerging Markets	1040.3	263.4	639.7	769.4

Source: IIF Capital Flows Report Tables.

1.5. Global Trade

World trade volumes grew by 4.8% in 2017, up from 2.6% in 2016. In 2017, trade upturn was driven from Asia including China as their contributions to world trade growth increased to 1.8% in 2017, up from just 0.7% in 2016. The Euro Area followed at 1.2% contribution then both Northern American and commodity producers' countries at 0.5% share in world trade growth. The ratio of trade volumes growth to GDP growth, known as the global trade intensity growth, remained low however, at 1.54% compared with its 1970-2015 average but high relative to its 2016 level.

Table 5: World Trade Growth and Global Trade Intensity Growth

A. Contributions to world trade growth	2013	2014	2015	2016	2017
China	0.9	0.6	0.0	0.4	0.7
Other Asia	0.7	0.8	0.2	0.3	1.1
Commodity producers	0.5	0.2	-0.2	0.0	0.5
Euro area	0.4	1.2	1.6	1.0	1.2
North America	0.3	0.7	0.5	0.1	0.5
Rest of the world	0.7	0.5	0.6	0.7	0.7
World	3.5	3.9	2.7	2.6	4.8
B. Global Trade Intensity	**2013**	**2014**	**2015**	**2016**	**2017**
Ratio trade growth to GDP growth	1.31	1.37	1.00	1.10	1.54
Average 1970-2015	1.78	1.78	1.78	1.78	1.78
Average 1987-2007	2.16	2.16	2.16	2.16	2.16

Source: OECD Economic Outlook, Volume 2017 Issue 2, December 2017.

Table 6 shows that world trade volume (goods and services) grew at 4.7% in 2017, up from 2.5% in 2016. Volume of exports in advanced economies grew by 4.1% in 2017, up from 1.9% in 2016, surpassing its long term average of 2.7%. In emerging market and developing economies volume of exports accelerated by 4.4% in 2017, up from 2.6% in 2016. In addition, volume of imports grew at 4.5% in advanced economies, up from 2.3% in 2017 and it accelerated by 4.4% in EMDEs, up from 2.4%[18].

Table 6: World Trade Volume (Percent Change %)

World Trade Volume (%)	Average 2009-18		2016		2017	
	EXP	**IMP**	**EXP**	**IMP**	**EXP**	**IMP**
Advanced Economies	2.7	2.4	1.9	2.3	4.1	4.5
EM & Developing Economies	3.7	3.8	2.6	2.4	4.4	4.4
World Trade Volume	**2.9**		**2.5**		**4.7**	

Source: UN, World Economic Situation Prospects, 2017 & IMF, WEO Update, January 2018.

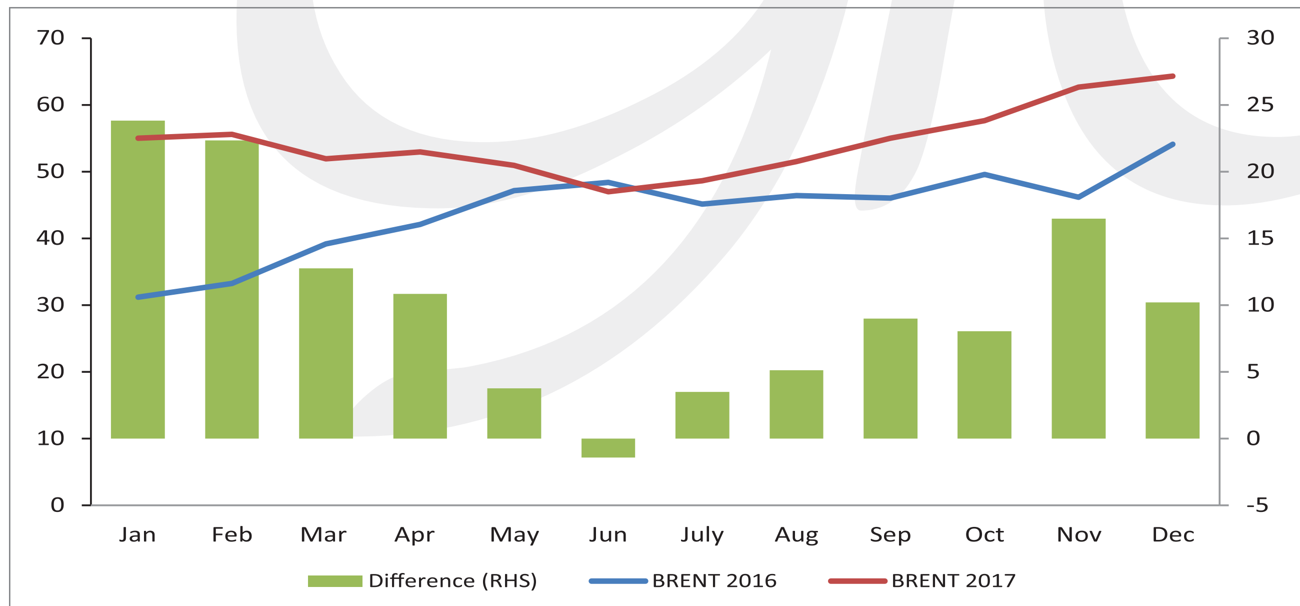
18. IMF WEO October 2017.

2. OIL DYNAMICS

The year started with relatively stable oil prices due to the agreement between OPEC and non-OPEC major oil producers to extend production cuts to the end of 2018. However, volatile prices were evident throughout the year with Brent reaching a minimum of $ 44.31 a barrel in June, and WTI reaching its lowest level at $ 42.31 a barrel in the same month. Since then, oil prices witnessed a solid recovery amid vulnerability to geopolitical developments and economic challenges. Nonetheless, crude oil prices rebounded to their year-high by the end of 2017 as Brent closed at $ 66.82 a barrel while WTI settled at $ 60.42 a barrel[19]. The recovery of oil prices in the second half was mainly attributed to shrinking surpluses together with the agreement between OPEC and other major producers to cut oil production that took place in January 2017.

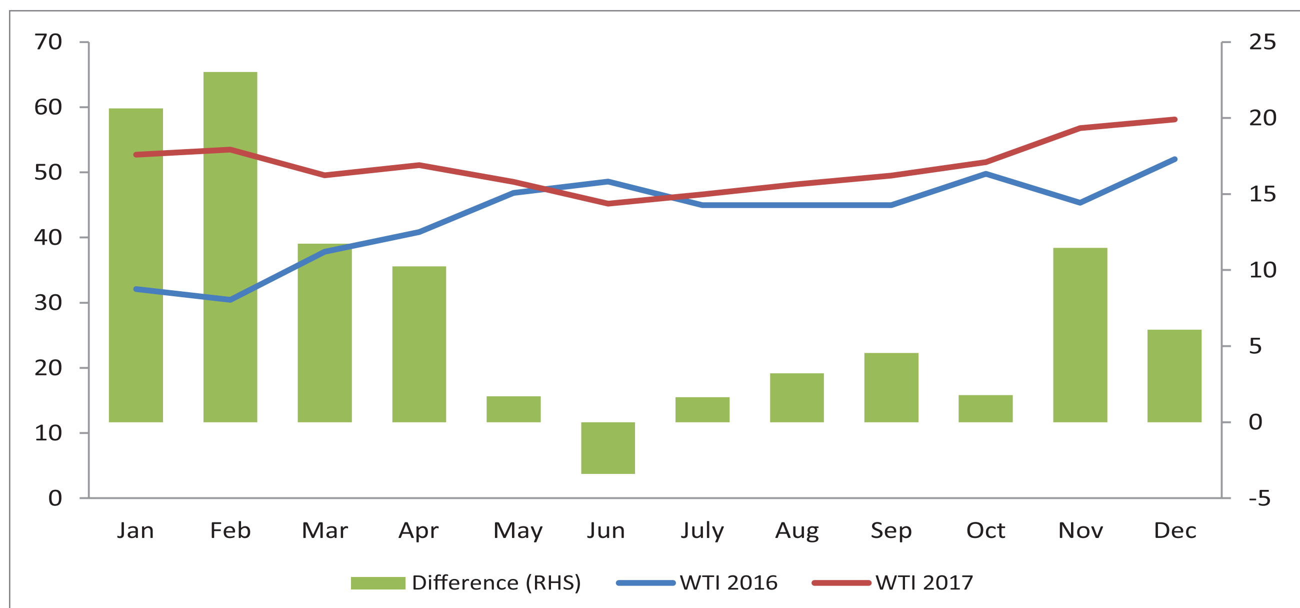
Similarly, Brent averaged $ 52.20 per barrel in the first half, $ 56.60 a barrel in the second half, and $ 54.42 per barrel for the whole year compared to 2016's average price of $ 44.08. This is slightly higher than WTI which averaged $ 50.06 per barrel in the first half, $ 51.77 per barrel in the second half, and $ 50.92 per barrel for the year, compared to an average of $ 43.25 a barrel in 2016.

Figure 5: Brent Average Monthly Prices in 2016 and 2017 ($/b)



Source: Bloomberg and GIC Research.

Figure 6: WTI Average Monthly Prices in 2016 and 2017 ($/b)



Source: Bloomberg and GIC Research.

19. Bloomberg and GIC Research.

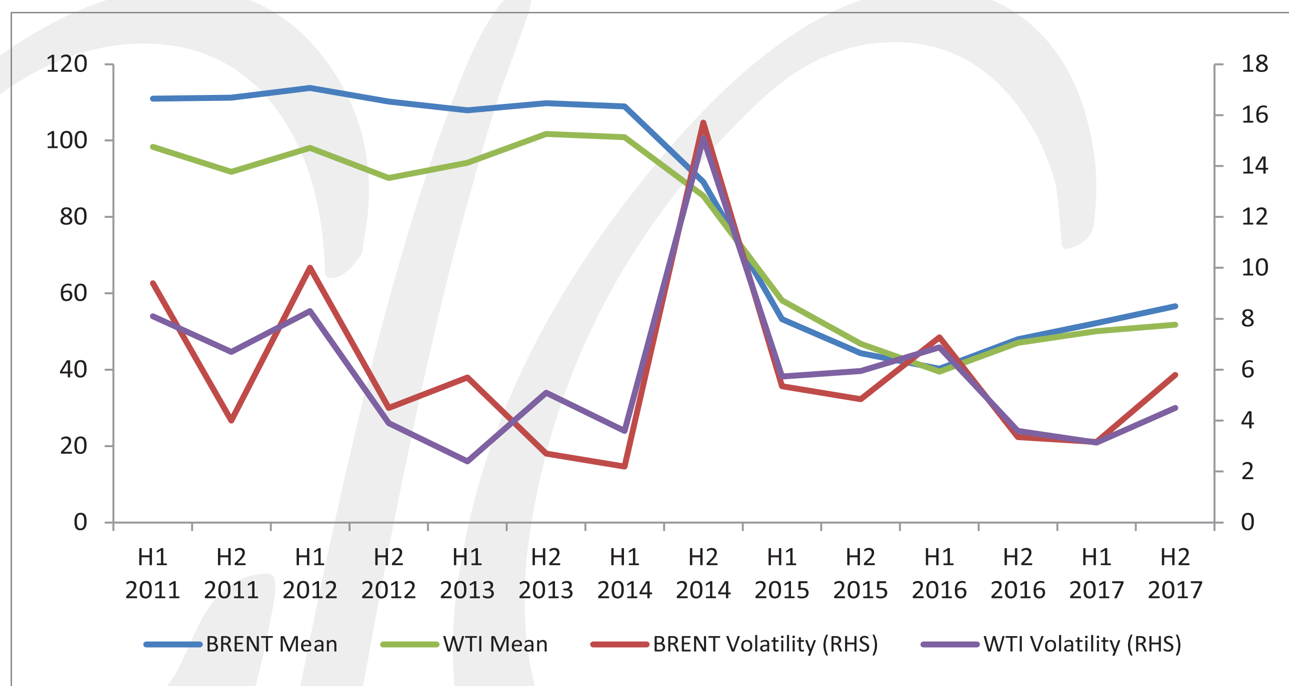
When compared to the first half of the year, BRENT and WTI prices gained around 8.42% and 3.41% respectively in the second half of 2017, bringing down the average volatility coefficients for the year to 5.17 from 6.64 for BRENT, and to 3.98 from 6.71 for WTI.

Table 7: Brent and WTI Mean & Volatility ($/b)

	BRENT		WTI	
	Mean	**Volatility**	**Mean**	**Volatility**
H1 2011	111.0	9.4	98.3	8.1
H2 2011	111.2	4.0	91.8	6.7
H1 2012	113.8	10.0	98.1	8.3
H2 2012	110.2	4.5	90.2	3.9
H1 2013	107.9	5.7	94.2	2.4
H2 2013	109.8	2.7	101.7	5.1
H1 2014	108.9	2.2	100.9	3.6
H2 2014	89.2	15.7	85.5	15.1
H1 2015	53.23	5.35	58.1	5.73
H2 2015	44.33	4.84	46.81	5.95
H1 2016	40.25	7.27	39.5	6.88
H2 2016	47.93	3.35	47.03	3.59
H1 2017	52.2	3.16	50.06	3.14
H2 2017	56.6	5.8	51.77	4.5

Source: Bloomberg and GIC Research.

Figure 7: OPEC, WTI, and Brent Mean and Volatility ($/b)



Source: Bloomberg and GIC Research.

2.1. Oil Fundamentals and Prices

Shrinking excess oil supply and the consequent fall in inventories were among the main factors that placed some upward pressures on oil prices during the year, allowing a relatively solid recovery in the price of oil which hovered around $ 54 a barrel. According to EIA estimates, the average inventory decline of global petroleum and other liquids in 2017 was 0.4 mb/d, thus recording the first year of inventory draws since 2013[20].

Total oil production witnessed a modest increase in 2017 compared to 2016 as a result of higher production that came from Canada, China, and other Non-OECD members. However, OPEC production fell slightly by an average 0.7% to reach 39.4 mb/d in 2017, from 40.50 mb/d in 2016[21]. The overall oil production slightly increased from 97.14 mb/d in the first quarter to 98.64 mb/d in the fourth quarter of 2017.

Table 8: International Petroleum and Other Liquids Production (mb/d, 2017)

	Q1	Q2	Q3	Q4
OECD	27.12	26.92	27.09	27.83
US	15.00	15.32	15.48	16.25
Canada	5.05	4.71	5.00	4.85
Non-OECD	70.02	70.78	71.30	70.81
OPEC	38.84	39.32	39.68	39.40
Crude Oil Portion	32.08	32.32	32.89	32.58
Other Liquids	6.77	7.00	6.79	6.82
Eurasia	14.43	14.31	14.23	14.34
China	4.82	4.82	4.73	4.76
Other Non-OECD	11.93	13.34	12.65	12.31
Total World	**97.14**	**97.70**	**98.39**	**98.64**

Source: EIA. "Short-Term Energy Outlook". January 2018.

Meanwhile, global consumption for the year grew on average by 1.6 mb/d to 98.38 mb/d compared to 95.8 mb/d in 2016. Oil demand increased modestly from 97.51 mb/d in the first quarter to 98.96 mb/d in the last quarter of 2017. Initially, the increase in consumption was due to rising demand from Non-OECD members and Other Asia. In the last quarter of 2017 however, oil demand eased in OECD, Canada, and Europe.

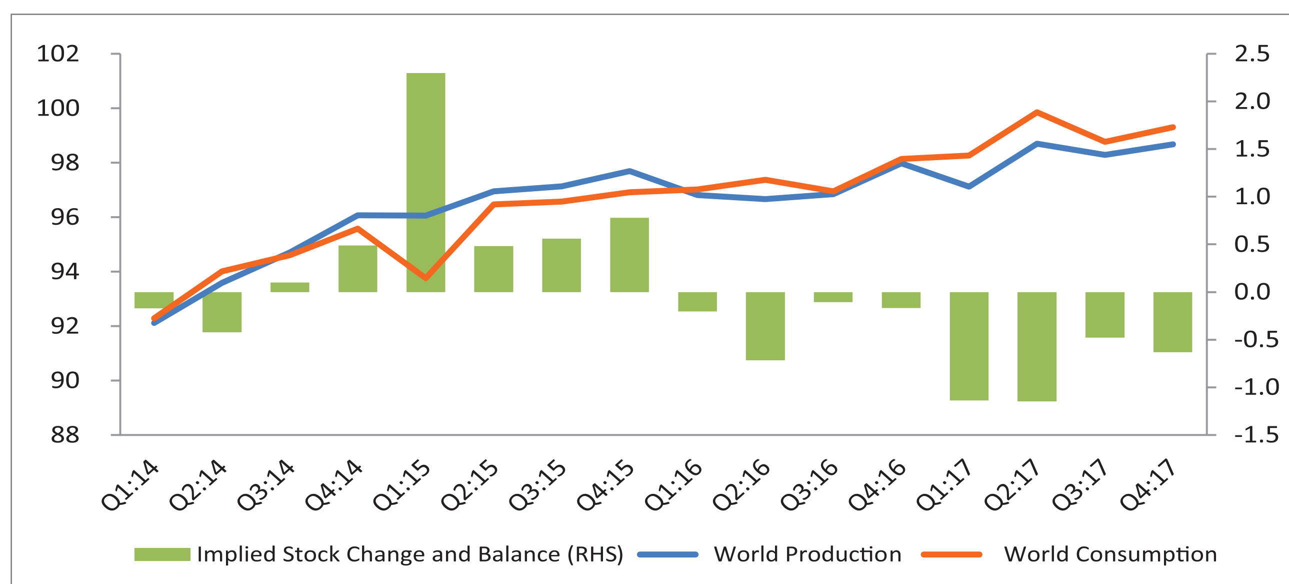
Table 9: International Petroleum and Other Liquids Consumption (mb/d)

	Q1	Q2	Q3	Q4
OECD	46.78	46.91	47.43	47.33
US	19.49	20.03	19.92	19.90
Canada	2.35	2.34	2.50	2.44
Europe	13.93	14.32	14.73	14.24
Japan	4.33	3.64	3.69	4.05
Non-OECD	50.73	51.35	51.38	51.63
Eurasia	4.76	4.75	5.02	4.89
China	11.25	11.87	11.72	11.77
Other Asia	12.99	13.31	12.97	13.44
Other Non-OECD	18.85	19.36	19.77	19.27
Total World	**97.51**	**98.26**	**98.81**	**98.96**

Source: EIA. "Short-Term Energy Outlook". January 2018.

20. EIA. "Short-Term Energy Outlook". January 2018.
21. EIA. "Short-Term Energy Outlook". January 2018.

Figure 8: World Liquid Fuels Production and Consumption Balance (mb/d)



Source: EIA, Short Term Energy Outlook. January 2018.

3. GCC Economies Review

GCC's real GDP is expected to have grown at a slower rate in 2017 than those realized in the past years due to modest oil prices during the year. Bahrain has realized the highest growth rate in 2017 at 3.5% followed by the UAE, at 1.4%, Qatar at 1.3%, and 0.4% in Oman. In contrast, real GDP of both Kuwait and Saudi Arabia contracted during the year by 2.2% and 0.5%, respectively.

Table 10: Real GDP Growth (% Change)

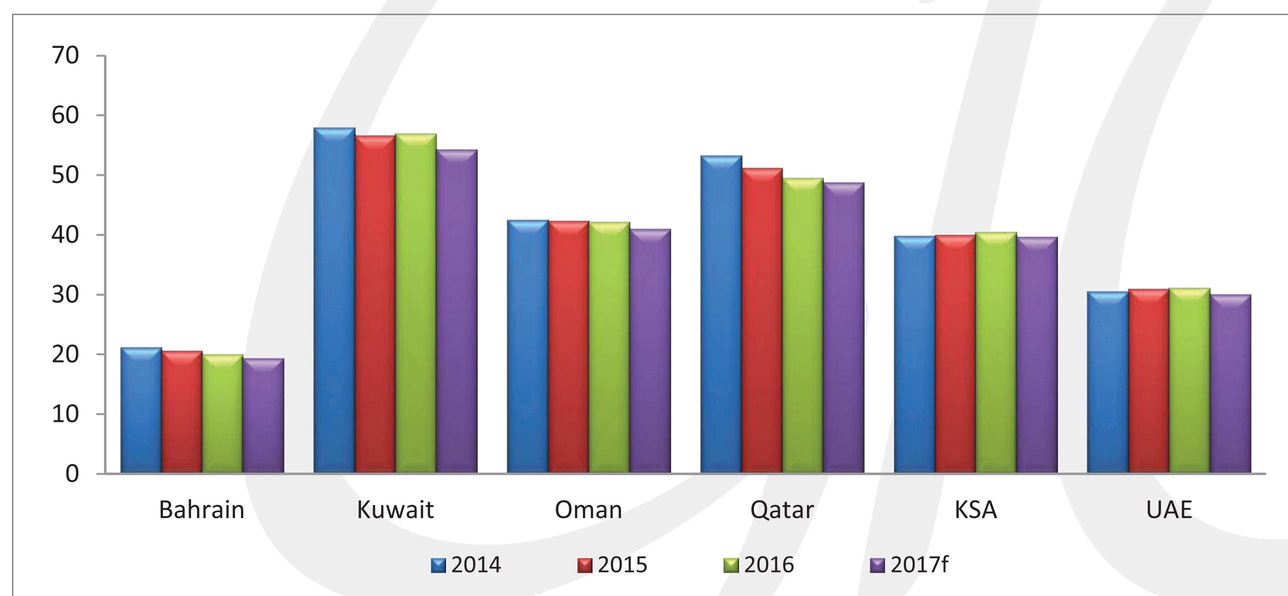
Country	2014	2015	2016	2017f
Bahrain	4.4	2.9	3.2	3.5
Kuwait	0.5	1.8	2.5	-2.2
Oman	2.8	4.7	3.0	0.4
Qatar	4.0	3.6	2.2	1.3
Saudi Arabia	3.7	4.1	1.7	-0.5
United Arab Emirates	3.3	3.8	3.0	1.4
GCC	**3.4**	**3.8**	**2.3**	**0.2**

f: Forecast.

Source: Institute of International Finance (IIF), respective country's database.

Meanwhile, the average contribution of hydrocarbons to real GDP in the GCC slightly dropped from 40% in 2016 to 38.8% in 2017. Kuwait was the most dependent member on hydrocarbons, as hydrocarbons accounted for more than 54% of its real GDP. Bahrain was the least hydrocarbons-dependent with 19%. Noteworthy, the average dependence on hydrocarbons slightly dropped in 2017 compared to the past couple of years.

Figure 9: Hydrocarbon's Contribution to Real GDP in GCC (%)



f: Forecast.
Source: Institute of International Finance (IIF), GCC Country Database.

Non-hydrocarbon real GDP for GCC economics registered a fair growth in 2017. Bahrain registered the highest real non-hydrocarbon growth of 4.5%, followed by Qatar at 3.6%, Kuwait and Oman with 2.5%. Meanwhile, it increased in Saudi Arabia from 0.2% in 2016 to 0.8% in 2017 while it decreased in the UAE from 2.6% in 2016 to 2% in 2017.

Table 11: Non-Hydrocarbon Real GDP Growth (% Change)

Country	2014	2015	2016	2017
Bahrain	4.7	3.6	4.1	4.5
Kuwait	4.8	0.4	2.0	2.5
Oman	5.7	5.0	3.3	2.5
Qatar	9.8	8.2	5.6	3.6
Saudi Arabia	4.9	3.2	0.2	0.8
United Arab Emirates	5.4	3.2	2.6	2.0

Source: Institute of International Finance (IIF), February 2018.

Furthermore, the steadiness of oil prices and the modest new norm supported better fiscal balances during the year. However, GCC's overall fiscal balance as percent of GDP shrank from 11.5% deficit in 2016 to 6.2% in 2017. Kuwait remained the only country that attained a positive fiscal balance while both of Bahrain and Oman were struggling with the heaviest deficits.

Table 12: GCC Overall Fiscal Balance (% GDP)

Country	2014	2015	2016	2017[f]
Bahrain	-1.6	-18.4	-17.8	-12.4
Kuwait	18.5	0.0	0.6	1.6
Oman	-2.1	-17.5	-20.6	-12.4
Qatar	12.3	-1.9	-9.0	-5.0
Saudi Arabia	-3.4	-15.7	-16.9	-7.8
United Arab Emirates	1.9	-3.4	-4.4	-3.0
GCC	**2.8**	**-9.4**	**-11.5**	**-6.2**

f: Forecast.
Source: IIF. Respective Country's Database.

On a positive note, the average fiscal breakeven price continued to fall shaving another $ 2 in 2017 to stand at $ 73. Kuwait continued to hold the lowest fiscal breakeven price in the region at $ 51 followed by Qatar at $ 57. Similarly, Bahrain endured the highest breakeven price of $ 103 in 2017; however, it was lower than previous years.

Table 13: GCC Fiscal Breakeven Prices ($/b)

Country	2014	2015	2016	2017
Bahrain	116	118	107	103
Kuwait	56	49	47	51
Oman	103	96	89	84
Qatar	54	50	53	57
Saudi Arabia	106	95	96	78
United Arab Emirates	83	65	60	65
GCC	86	78	75	73

Source: IIF. "Research Note: Hydrocarbon Exporters Breakeven Oil Prices Have Declined". February 1, 2018.

3.1. Inflation

Inflation rates varied among the GCC members with a mild deflation of (-0.4%) in Saudi Arabia and a maximum of 2.5% in Kuwait. The average inflation rate for the region was estimated at 0.9% for 2017, fairly lower than 2016's level of 2.8%.

Table 14: Average Consumer Prices (Y-o-Y % Change)

Country	2014	2015	2016	2017[f]
Bahrain	2.7	1.8	2.8	1.5
Kuwait	2.9	3.3	3.2	2.5
Oman	1.0	0.1	1.1	1.6
Qatar	3.3	1.9	2.7	2.1
Saudi Arabia	2.7	2.2	3.5	-0.4
United Arab Emirates	2.3	4.1	1.8	1.6
GCC	2.6	2.6	2.8	0.9

f: IIF's Forecast.
Source: IIF. Respective Country's Database.

3.2. GCC's Competitiveness

According to the World Economic Forum (WEF), the competitiveness of the GCC economies weakened in 2017. UAE outperformed the region as it ranked among the Top-20, while the rest were ranked among the Top-50 with the exception on Kuwait and Oman.

Table 15: GCC's Global Competitiveness Index Rankings

Country	2016-2017	2017-2018
UAE	16	17
Qatar	18	25
Saudi Arabia	29	30
Bahrain	48	44
Kuwait	38	52
Oman	66	62

Source: The Global Competitiveness Report 2017-2018.

3.3. GCC Trade

GCC hydrocarbon exports increased fairly in 2017 on the back of steadier more modest oil prices. With hydrocarbon exports constituting more than 50% of total exports, all the member's total exports surpassed last year's level. Saudi Arabia's hydrocarbon exports in 2017 exceeded their level of 2016 by 7%. Noteworthy, The UAE was the only country in the region to have non-hydrocarbon exports exceeding the hydrocarbons, with a ratio of 4:1.

On the other hand, changes in the level of total imports varied among member countries. Saudi imports continued to decline for the second consecutive year while Qatar's imports slightly dropped down in 2017 after logging an increase in the previous year. All other countries marked an increase in the level of total imports averaging at 7% on annual basis.

Table 16: GCC's Trade ($bn)

	2014	2015	2016	2017[f]
Hydrocarbon Exports				
Bahrain	14.50	7.74	6.08	7.48
Kuwait	104.53	54.46	46.51	50.06
Oman	35.14	21.16	15.94	19.91
Qatar	107.13	62.69	47.09	54.05
KSA	284.40	152.91	134.89	164.15
UAE	111.57	63.72	54.63	60.67
Non-Hydrocarbon Exports				
Bahrain	9.00	8.80	6.70	7.17
Kuwait	95.62	48.48	41.46	44.00
Oman	18.36	14.48	11.57	13.89
Qatar	19.57	14.61	10.17	11.90
KSA	57.87	50.63	48.72	60.90
UAE	231.50	236.76	243.99	252.36
Total Imports				
Bahrain	19.78	15.71	13.59	14.90
Kuwait	26.99	26.55	26.40	27.54
Oman	27.85	26.53	21.26	22.93
Qatar	31.15	28.50	31.93	30.28
KSA	158.46	159.27	127.84	125.78
UAE	234.61	223.91	230.31	242.22

f: Forecast.
Source: IIF. Respective Country's Database.

3.4. GCC Ease of Doing Business

The performance of the region on the Doing Business Index 2017 varied across the GCC. The UAE ranked among the Top-30 tier for the second year in a row marking the 26th place among all comparators in the index. Bahrain and Oman also improved their rankings to stand as the 63rd and 66th. The other members' performance was modest in 2017 with Kuwait being the only country out the Top-100 tier.

Table 17: GCC's Ease of Doing Business

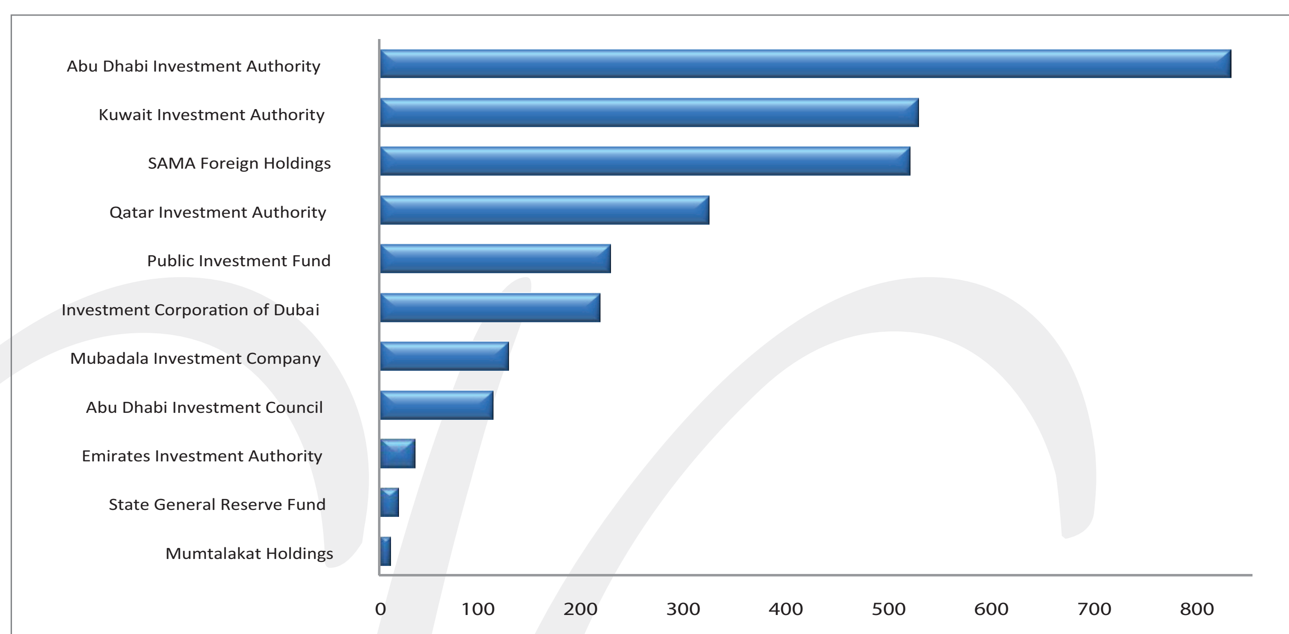
	2016	2017
UAE	31	26
Bahrain	65	63
Oman	70	66
Qatar	68	83
Saudi Arabia	82	94
Kuwait	101	102

Source: Doing Business 2016 and 2017.

3.5. Sovereign Wealth Funds

The GCC Sovereign Wealth Funds (SWF's) remained close in value to its level of the previous year, totaling slightly above $ 2.9 trillion. The UAE accounted for 45% of the total GCC SWF's in 2017, followed by Saudi Arabia with 25% of the total. Furthermore, Abu Dhabi Investment Authority stood as the largest fund in the area with assets of $ 828 bn, comprising about 63% of UAE's total and 28% of GCC's.

Figure 10: Selected GCC Sovereign Wealth Funds ($bn)



Source: Sovereign Wealth Funds Institute.

3.6. Sovereign Credit Ratings

Recent geopolitical developments in the region placed negative pressures on sovereign credit ratings. During the past year, S&P has downgraded all of the GCC economies with the exception of Kuwait. Both Kuwait and Abu Dhabi remained rated in upper tiers with stable outlook.

Table 18: GCC Sovereign Credit Ratings (Foreign Currency Long-Term Debt)

	Moody's		S&P		Fitch	
	Rating	Outlook	Rating	Outlook	Rating	Outlook
Bahrain	Ba2	Negative	B+	Stable	BB+	Negative
Kuwait	Aa2	Stable	AA	Stable	AA	Stable
Oman	Baa1	Negative	BB	Stable		
Qatar	Aa3	Negative	AA-	Negative	AA-	Negative
KSA	A1	Stable	A-u	Stable	A+	Stable
UAE - Abu Dhabi	Aa2	Stable	AA	Stable	AA	Stable

Source: Bloomberg, January 2018.

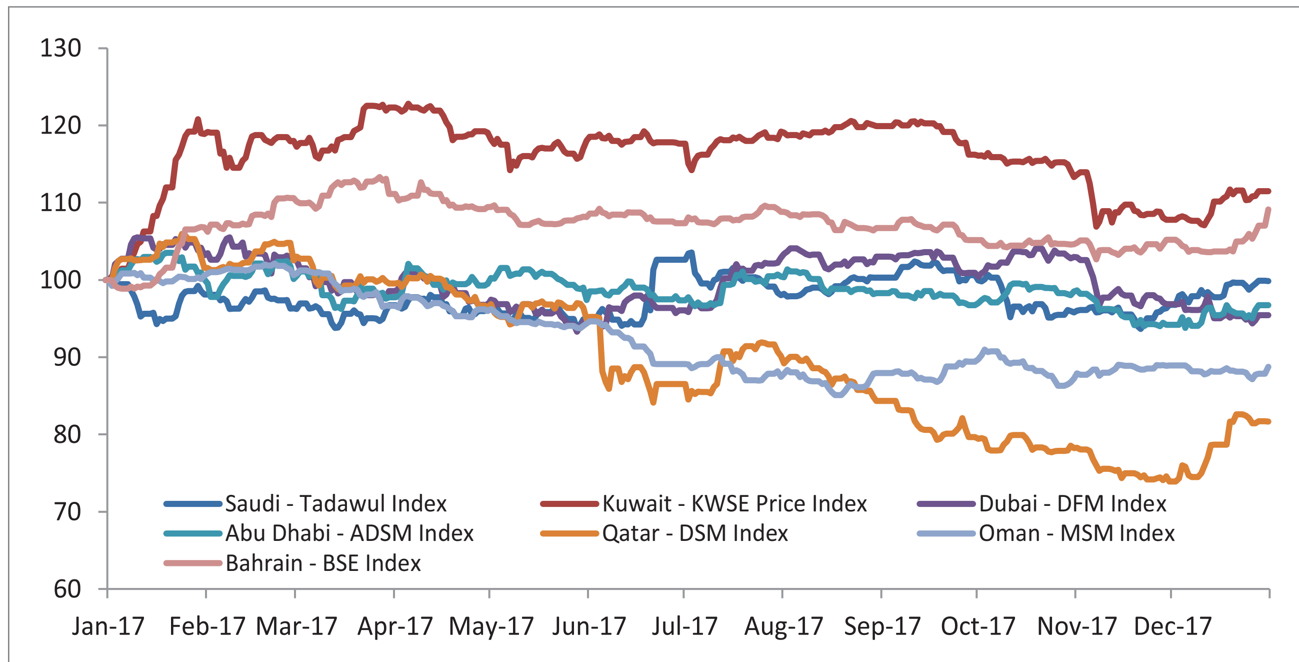
4. Equity Markets Review

4.1. GCC Equity Markets Overview

2017 was a year of contrasts for the GCC equity markets, as a promising first half was replaced by tenuous returns across most markets in the second half, as the GCC indices failed to replicate the positive momentum that surged through most global equity markets, both emerging and developed, through 2017.

Though the steady recovery in oil prices could have been a potential trigger, it was offset by the unprecedented geopolitical uncertainty in the region that weighed heavily on investor sentiment and caused widespread outflows of liquidity from the GCC markets. The S&P GCC composite index added a net 3.3% for the year, as weak returns during the fourth quarter erased most of the earlier advance during the year.

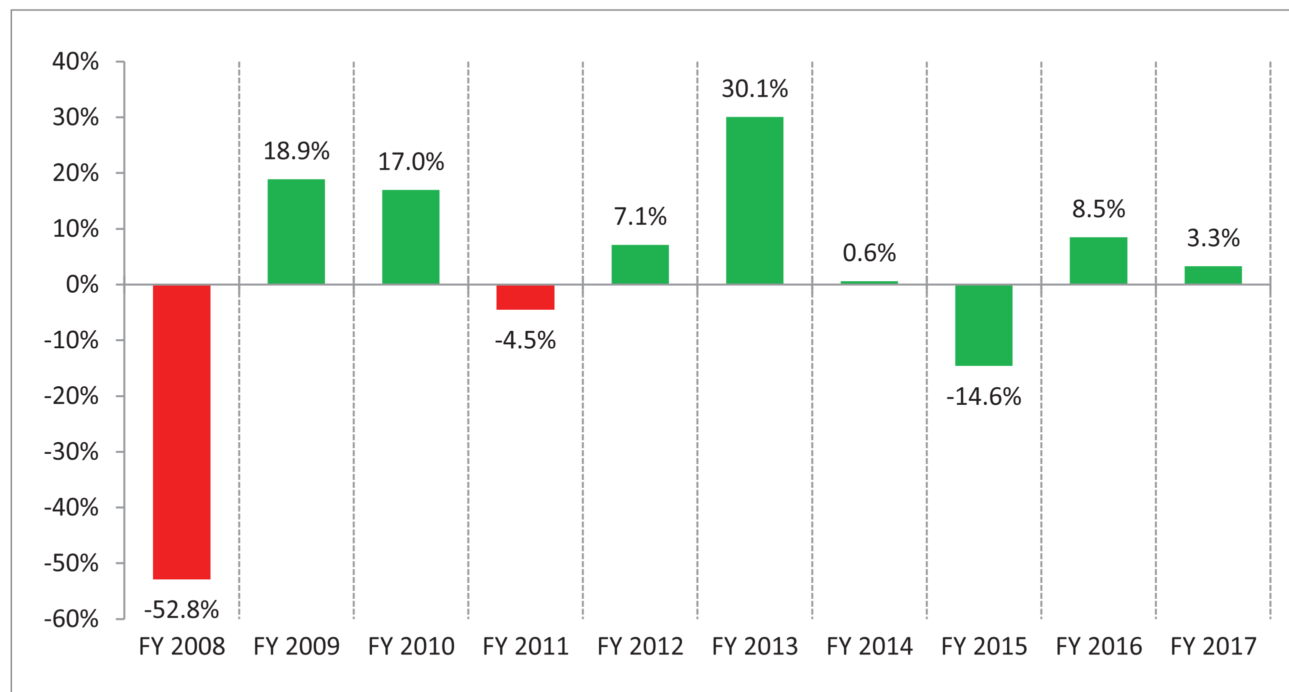
Figure 11: Rebased Performance of GCC indices, 2017



Source: Bloomberg, GIC Research.

We also witnessed an extended decoupling of the earlier correlation between oil prices and equity markets in the GCC, and the GCC composite failed to reflect the strong improvement in oil prices during the year. The outflow of foreign institutional funds towards the end of the year, led to an increase in the influence of retail investors on market direction, thus increasing the volatility of market returns.

Figure 12: Performance of S&P GCC Composite Index (2008-2017)



Source: Bloomberg, GIC Research.

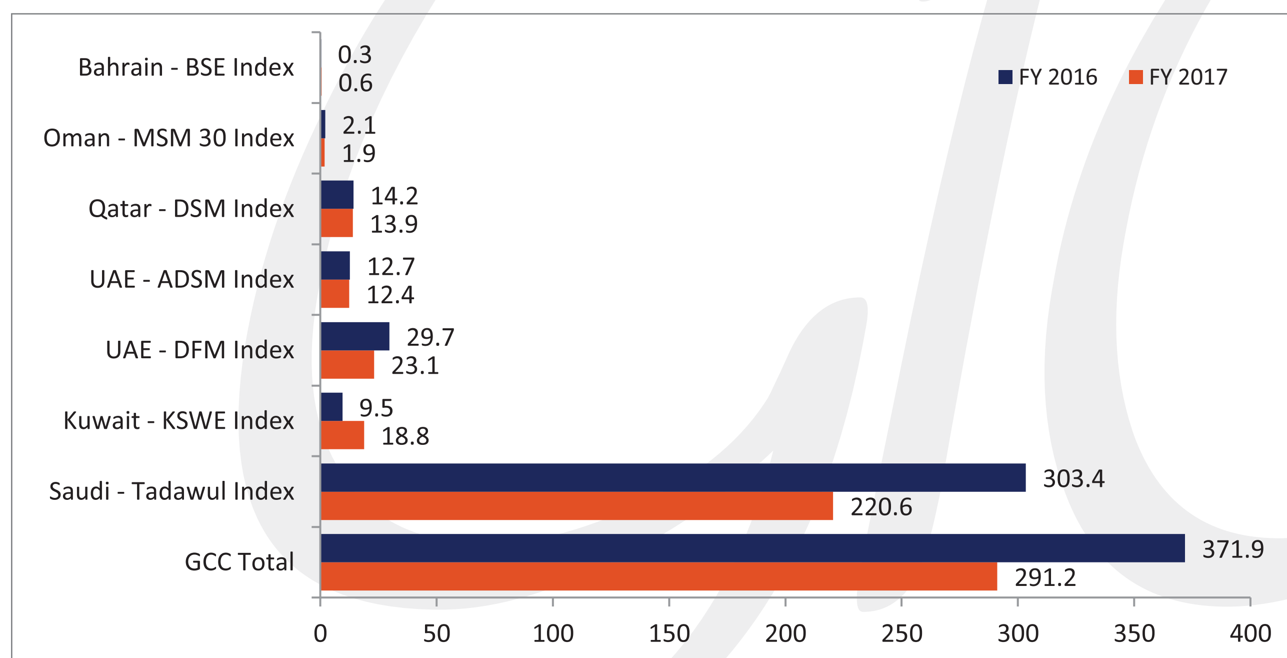
The year started on an optimistic tone for most GCC markets, as they carried forward the positive sentiment from the end of 2016. However the momentum could not be sustained for long, and the first quarter ended on a weak note, as most markets were dragged down by weakness in oil prices, poor earnings from several key companies, as well as ex-dividend trades on a large number of stocks towards the end of March. The Kuwait bourse stood out with its strong returns for the quarter, as investors continued to be enthused by the catch-up story and improvements in the regulatory framework.

There was a moderate resurgence in the second quarter, largely driven by a rebound in Saudi Arabia after expectations of a potential inclusion of the Saudi bourse to the FTSE EM index, and the elevation of the country's Deputy Crown Prince to his new role as Crown Prince. The quarter ended on a positive note with Saudi Arabia emerging the clear winner, despite the geopolitical uncertainties in the region and some weakness in oil prices.

The GCC equity markets had a lackluster third quarter, anr the GCC index closed with modest gains for the quarter. The Kuwait bourse continued to forge ahead, with earlier gains further bolstered by confirmation of its entry to the FTSE EM index. However, the Saudi bourse witnessed a reversal following the decision to defer its inclusion to the FTSE EM index till March 2018 at the earliest. Qatar remained the biggest laggard as a result of weak index returns.

The strong surge in oil prices during the fourth quarter failed to support the equity markets, and the year ended on a weak note, as geopolitical tensions and the erosion of investor sentiment undermined the improvement in macro fundamentals and the positive benefits of continued reform measures for the region. With the exception of Qatar and Bahrain, all the other country indices ended with losses for the quarter, though the relief rally in Qatar did little to dent earlier losses in the market.

Figure 13: Trading activity on individual GCC indices for 2016 and 2017 ($bn)



Source: Bloomberg, GIC Research.

Trading activity in the GCC also witnessed a significant decline during 2017, as cumulative traded values on the seven benchmark indices declined by around 22% to $ 291 bn in 2017. The decline in activity in Saudi Arabia was more pronounced, as the traded value declined by nearly 27% to $ 221 bn, largely due to outflow of foreign institutional investments from the region amid the escalation in geopolitical tensions.

4.2. GCC Markets Volatility

The GCC market indices witnessed an elevation in volatility, both in relation to the previous year, as well as in comparison to global and regional markets. This can largely be attributed to the weak investor sentiment and geopolitical uncertainties across the region, which was exacerbated by concerns about the short-term impact of several reform measures being implemented in several countries.

Table 19: Volatility of indices across the GCC markets, 2017

	Year Opening	Year Closing	Year High	Year Low	Index Volatility
S&P GCC	150.33	155.26	159.61	147.59	7.6%
UAE - DFM index	3530.88	3370.07	3725.93	3293.60	10.9%
UAE - ADSM index	4546.37	4398.44	4704.70	4263.62	10.2%
Qatar - DSM index	2869.16	2452.49	11057.83	7714.26	15.4%
Saudi - Tadawul index	7210.43	7226.32	7493.45	6778.32	11.8%
Oman - MSM 30 index	5782.71	5099.28	5867.46	4889.28	6.6%
Bahrain - BSE index	1220.45	1331.71	1382.71	1206.40	7.4%
Kuwait - KSWE Price index	5748.09	6408.01	7059.61	5775.03	11.1%

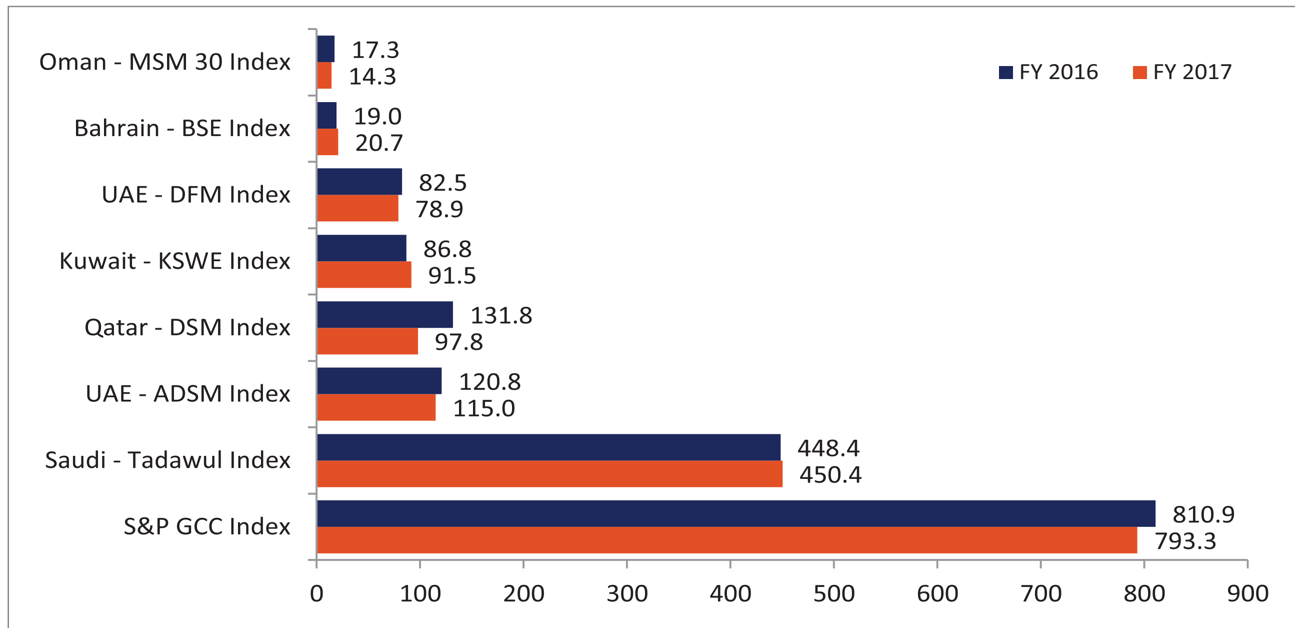
Source: Bloomberg, GIC Research.

4.3. GCC Market Capitalization

The total market capitalization of the S&P GCC Composite Index declined by 2.2% to $ 793.3 bn at the end of 2017, compared to $ 810.9 billion at the end of 2016. Of the individual country bourses, only Bahrain and Kuwait reported any noticeable gains, as the market capitalization of their respective markets rose by 8.7% and 6.8% at the end of the year. The market capitalization of the Saudi

Tadawul remained largely unchanged with a negligible addition of 0.5% to $ 450.4bn. The Qatar bourse recorded the biggest decline as the market capitalization declined by 26.3% for the year.

Figure 14: GCC Market Capitalization for 2016 and 2017 ($ billion)

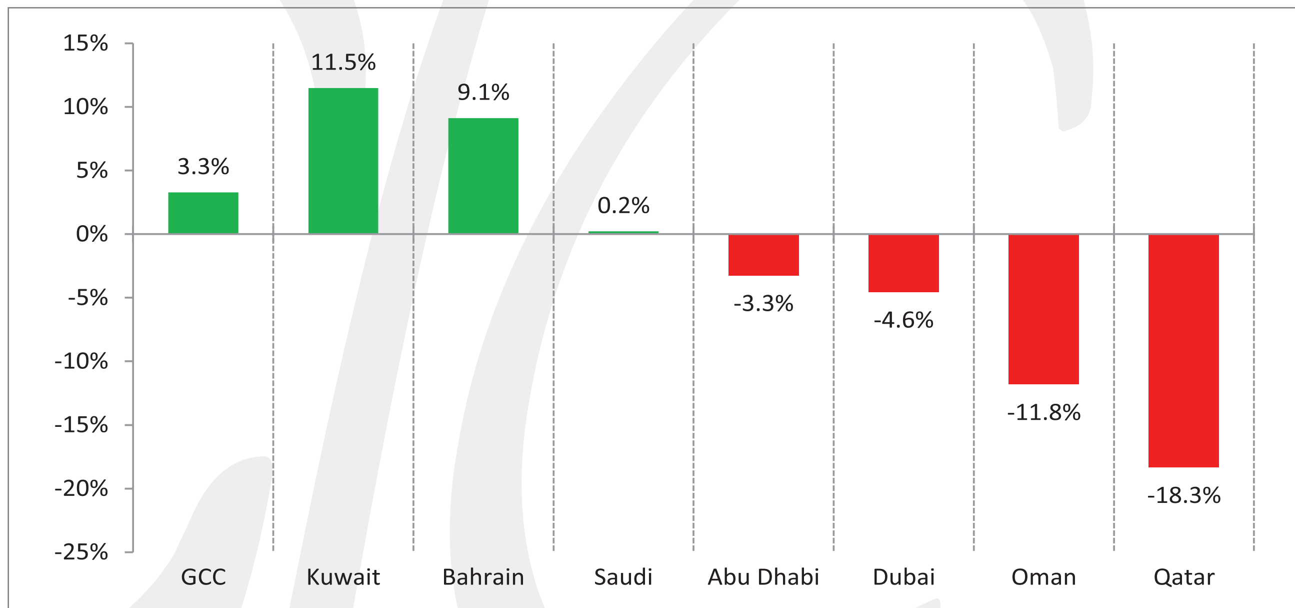


Source: Bloomberg, GIC Research.

4.4. Country Performances

The Kuwait bourse closed the year as the best performing among its GCC peers, even as late losses eroded some of the strong gains in the first quarter. Both Kuwait and Bahrain, which managed to close the year with robust gains, benefitted from investor attention after being largely sidelined by international investors for much of the last few years. The Saudi and UAE markets suffered from the weakness in investor sentiment during most of the second half, particularly among international investors. Meanwhile, Qatar ended the year as the least performing among its GCC peers.

Figure 15: Index Returns, 2017



Source: Bloomberg, GIC Research.

The KWSE Price index on Boursa Kuwait was the best-performing index in the GCC for 2017, with a net gain of 11.5%, while the KWSE Weighted index and the large-cap KSX 15 indices added 5.6% and 3.4% respectively. The bourse witnessed a strong rally at the beginning of the year, continuing the positive trend seen at the end of 2016. The rally gained further momentum following expectations of the market's entry into the FTSE EM index, and peaked in September before witnessing a prolonged, albeit modest, correction during the fourth quarter. The Basic Materials, Industrials and Banks sectors were the best performing for the year, while the Consumer Goods and Financial Services sectors featured prominently amongst the laggards.

The Bahrain market emerged the second-best performing index for the year, as the BHSE index added a net 9.1% for the year. The gains were fueled largely by investors pursuing a "catch-up" story on the market, despite the lack of any significant change in macro-fundamentals or the state of the economy. The Banks and Industries sectors secured strong returns for the year, while the Services sector lagged.

The Saudi bourse closed nearly flat for the year, with a negligible gain of 0.2% on the Tadawul index, at the end of a rather turbulent year that witnessed sharp swings in direction. After a lackluster first quarter, there was a rapid surge towards the end of the second quarter following expectations of a potential inclusion to the FTSE EM index, and the elevation of the country's Deputy Crown Prince to his new role as Crown Prince. However, failure by the market to clear the entry requirements by FTSE in its September review caused a sharp correction in early October. There was a sustained recovery in the index towards the end of the year as it tracked the improvement in oil prices. The Retail, Food Staples and Banks sectors were the best performing for the year.

The UAE bourses failed to capitalize on the improvement in oil prices and macro-fundamentals, as investor sentiment from the perspective of international investors remained skewed towards the negative. The DFM index in Dubai dropped by 4.6% for the year, while the ADSM index in Abu Dhabi edged down to a loss of 3.3%. The large-cap Real Estate and Telecom sectors were negatively affected in both markets, but the Banks sector in Dubai managed to end with net gains even as the Abu Dhabi Banks index ceded a net loss for the year. The Services sector was the best-performing in Dubai while in Abu Dhabi, it was the Energy sector that scored the biggest gains.

The Oman bourse witnessed a sharp reversal in 2017 after robust gains in 2016, and the MSM 30 index ended the year with a net loss of 11.8%, with negative returns across all three sector indices. Lackluster outlook for the macro-economic environment and weakness in corporate earnings affected investor sentiment, while an increase in geopolitical tensions across the region stemmed international investor flows.

Qatar Exchange ended the year as the least performing market among its GCC peers, with the benchmark DSM 20 index shedding a net 18.3%, while the broader QE All Share index declined by 14.5%. The losses reflect the erosion in investor sentiment following unprecedented political developments in the region. All sectors in the market registered losses, though the large-cap Banks and Telecom sectors fared better than most of the others.

Table 20: Index Returns for 2017

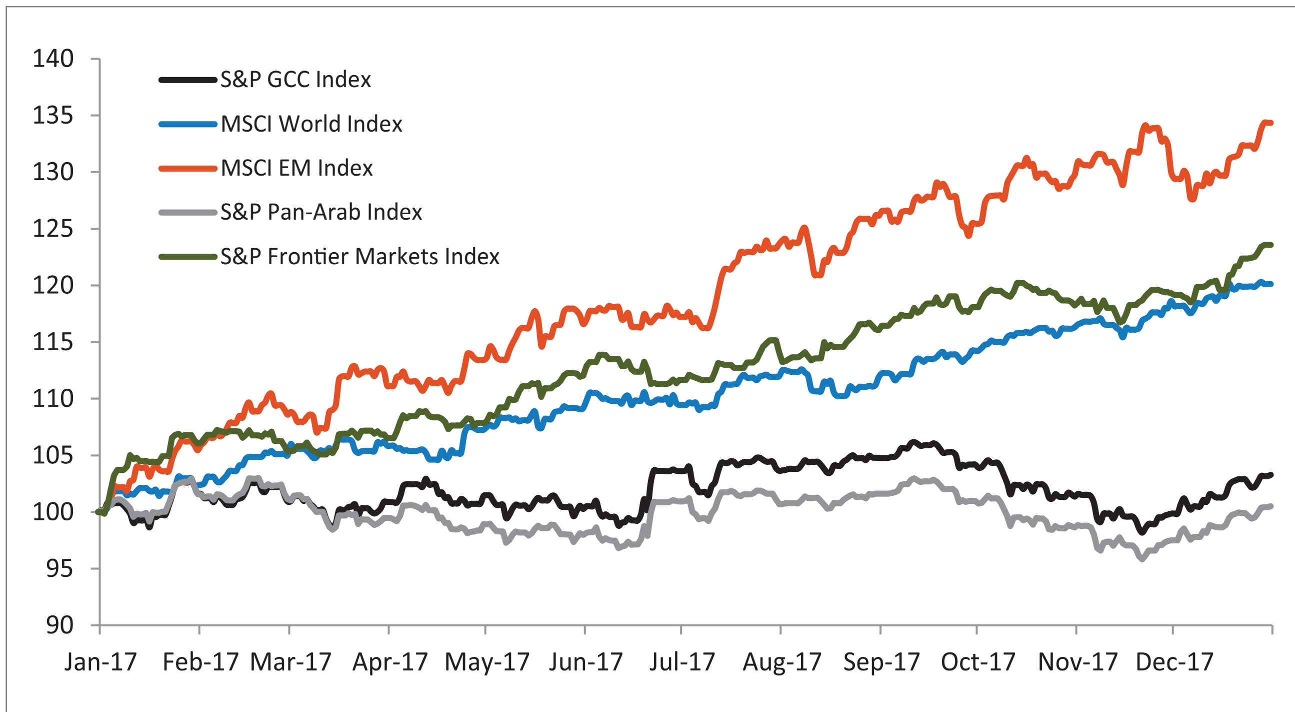
	31 December 2016	31 December 2017	% Change
S&P GCC Composite Index	150.33	155.26	3.3%
UAE - DFM Index	3,530.88	3,370.07	-4.6%
UAE - ADSM Index	4,546.37	4,398.44	-3.3%
Qatar - DSM Index	10,436.76	8,523.38	-18.3%
Saudi - Tadawul Index	7,210.43	7,226.32	0.2%
Oman - MSM 30 Index	5,782.71	5,099.28	-11.8%
Bahrain - BSE Index	1,220.45	1,331.71	9.1%
Kuwait - KSWE Price Index	5,748.09	6,408.01	11.5%

Source: Bloomberg, GIC Research.

4.5. Relative Performance of S&P GCC Composite Index to Global Benchmarks

During the year, the S&P GCC Composite Index underperformed most of the international benchmarks, including the MSCI EM, MSCI World, and MSCI Frontier Markets indices by a large margin. The net 2017 gain on the MSCI World index was recorded at 20.1%, while those on the MSCI EM and Frontier Markets indices were 34.4% and 23.6% respectively, compared to 3.3% on the S&P GCC Composite index. However, returns on the GCC benchmark managed to stay above that for the S&P Pan-Arab index for most of the year, which in turn added a net 0.5% at the end of the year.

Figure 16: Rebased Performance of S&P GCC Composite Index to Global Benchmarks ($bn)

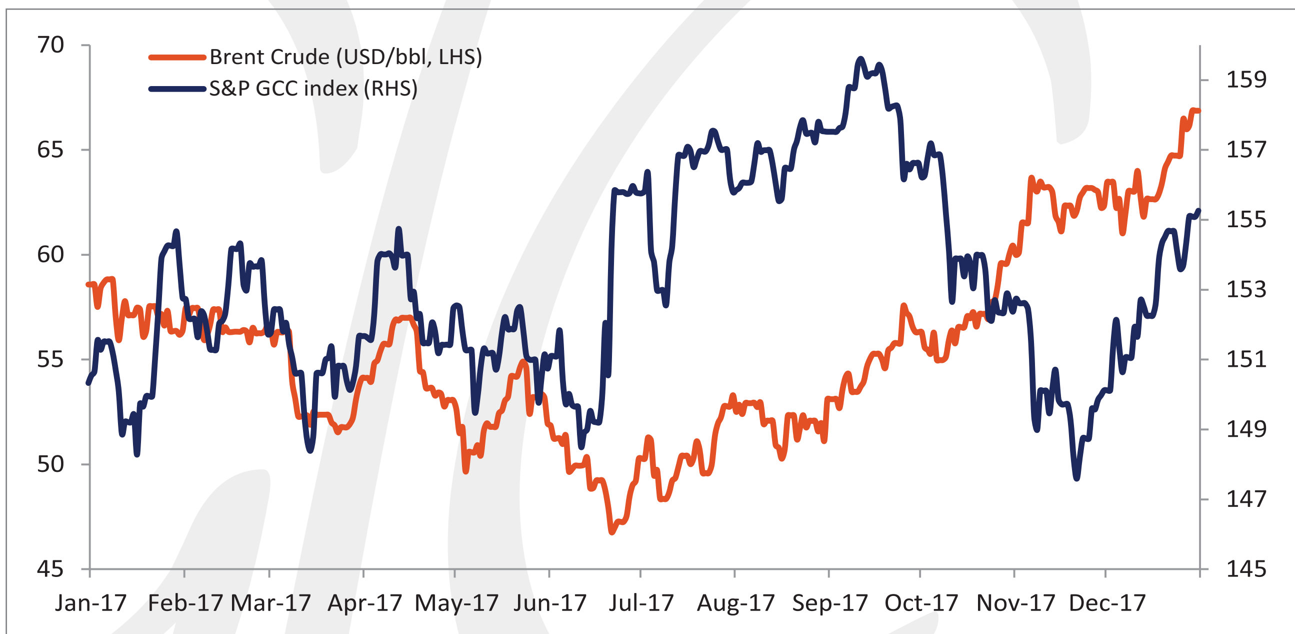


Source: Bloomberg, GIC Research.

4.6. Relative Performance of S&P GCC Composite Index to Oil Prices

During 2017, we witnessed a decoupling of the otherwise strong correlation between Oil prices and GCC markets, as geopolitical developments emerged as the key driving force for market direction and investor sentiment through most of the year. Brent crude averaged $ 55.4 a barrel for the year, and ended the year with a net gain of 14.2%. However, these returns were not reflected in the GCC equity markets, despite the improvement in macro-economic fundamentals across the region.

Figure 17: Rebased Performance of S&P GCC Composite Index to Global Benchmarks, 2017

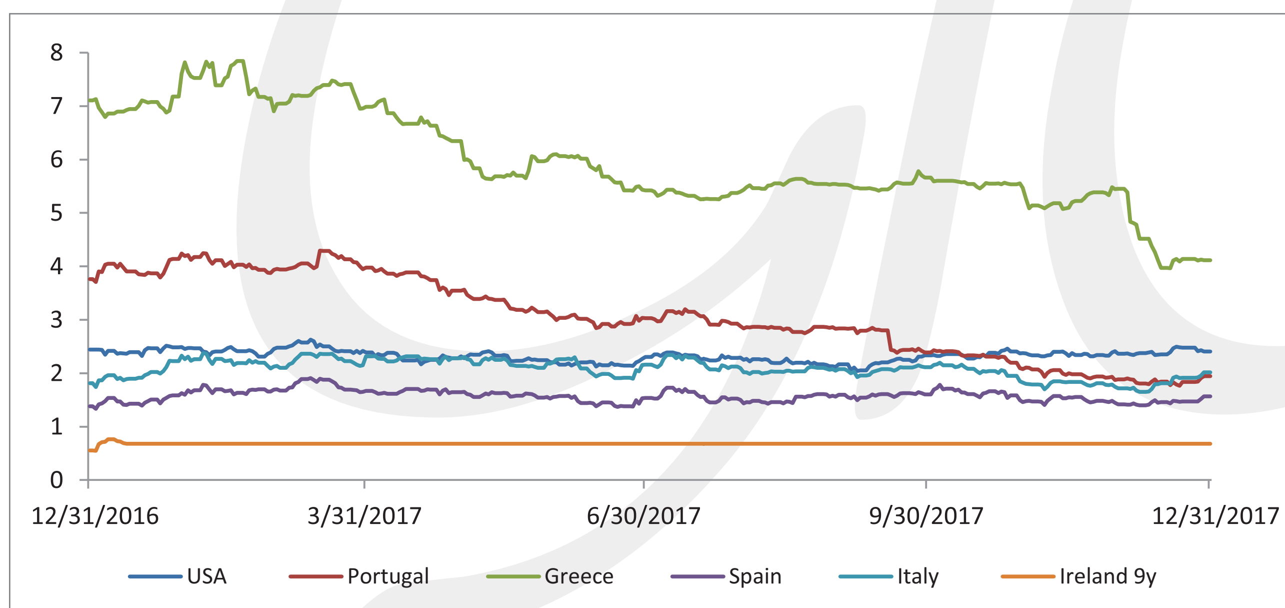


Source: Bloomberg, GIC Research.

4.7. Treasuries

The downfall in the 2017 bond yields is considered a clear outcome of the implemented central bank policies, having its tolls on the financial markets[22]. Most of the European economies witnessed a drop in their 10-year government bond yields during 2017. Greece remains with the highest yields in the euro zone, opening the year at 7.107%, yet closing at 4.115%. Ireland, which did not change much during the year, settled at 0.678%. US yields started the year at 2.444% and closed the year at 2.405%, low by all historical standards.

Figure 18: Euro Area and US 10-year Government Bond Yields during 2017



Source: Bloomberg.

Table 21: Volatility of Spreads, 2017

	US	Portugal	Greece	Spain	Italy	Ireland
Opening Value	2.444	3.764	7.107	1.384	1.815	0.552
Closing Value	2.405	1.943	4.115	1.567	2.016	0.678
Average	2.326	3.064	5.965	1.576	2.081	0.678
Standard Deviation	0.109	0.760	0.917	0.111	0.175	0.015
Minimum Value	2.039	1.766	3.963	1.332	1.651	0.551
Maximum Value	2.626	4.297	7.842	1.906	2.376	0.764

Source: Bloomberg. January, 2017.

Table 22: Government Bond Yields (%) during 2017

	US	Portugal	Greece	Spain	Italy	Ireland
Q1	2.3874	3.978	6.986	1.667	2.318	0.678
Q2	2.3037	3.027	5.424	1.539	2.158	0.678
Q3	2.3336	2.388	5.662	1.604	2.111	0.678
Q4	2.4054	1.943	4.115	1.567	2.016	0.678

Source: Bloomberg. January, 2017.

22. Wolf Street, October 19, 2017.

4.8. Credit Default Swaps (CDS)

CDS displayed realizable decreases during the year in the Euro area. Greece, for instance, witnessed a 62% drop during 2017. Portugal also witnessed a 70% drop over the course of the year. The US also experienced decreases during 2017, from 26.75 bps in the beginning of the year to 23.76 bps at year end. The GCC's region CDS demonstrated mild drops this year. Bahrain remained the highest in the region in terms of CDS, closing the year at 276.56 bps. Dubai followed, dropping from 150.10 bps to 122.43 bps.

Table 23: CDS Performance, 2017

	Portugal	Ireland	Greece	Spain	Italy	US	Bahrain	Abu Dhabi	Dubai
Opening	272.29	64.55	1,047.53	74.71	154.36	26.75	303.04	61.25	150.10
Closing	80.64	25.29	397.70	55.76	117.37	23.76	276.56	61.66	122.43
Average	188.192	42.807	689.677	69.079	150.767	24.666	241.792	53.772	123.651
Minimum Value	62.905	14.178	227.617	7.296	22.843	1.751	21.249	9.018	10.469
Maximum Value	80.637	25.290	381.425	53.094	111.836	20.085	211.520	38.040	103.885

Source: Bloomberg.

4.9. GCC Monetary Policy

Private sector credit growth in the GCC eased during the past few years. As shown in the following table, Saudi private sector credit growth trended downward from 2.4% in 2016 to (-0.8%) in 2017, in Bahrain from 1.5% to 0.9%, and in the UAE from 5.8% to 1.7%, and in Oman from 9.5% to 6% for the same period. Meanwhile, private sector credit growth has steadied in Qatar while it increased in Kuwait from 2.5% in 2016 to 2.9% in 2017.

Table 24: Private Sector Credit Growth (% Change)

	2013	2014	2015	2016	2017
Bahrain	6.6	-5.9	7.6	1.5	0.9
Kuwait	7.2	5.2	7.9	2.5	2.9
Oman	9.6	14.9	12.2	9.5	6.0
Qatar	13.5	20.3	19.7	6.5	6.4
KSA	12.3	11.6	9.2	2.4	-0.8
UAE	-6.6	11.5	8.4	5.8	1.7

Source: IIF, February 2018.

The year 2015 marked the beginning of a number of rate hikes in the GCC. In Bahrain, we noted a jump from 0.5% to 0.75% in 2015, to reach 1.75% in 2017. In Kuwait, policy rates increased from 2.5% in 2016 to 2.75% in 2017. Meanwhile, Oman, interest rates almost doubled from 2015 to 2017 to reach 2%. Steadier changes we exhibited in Qatar and the UAE. Noteworthy, the policy rate in the Saudi economy doubled from 0.75% in 2016 to 1.5% in 2017.

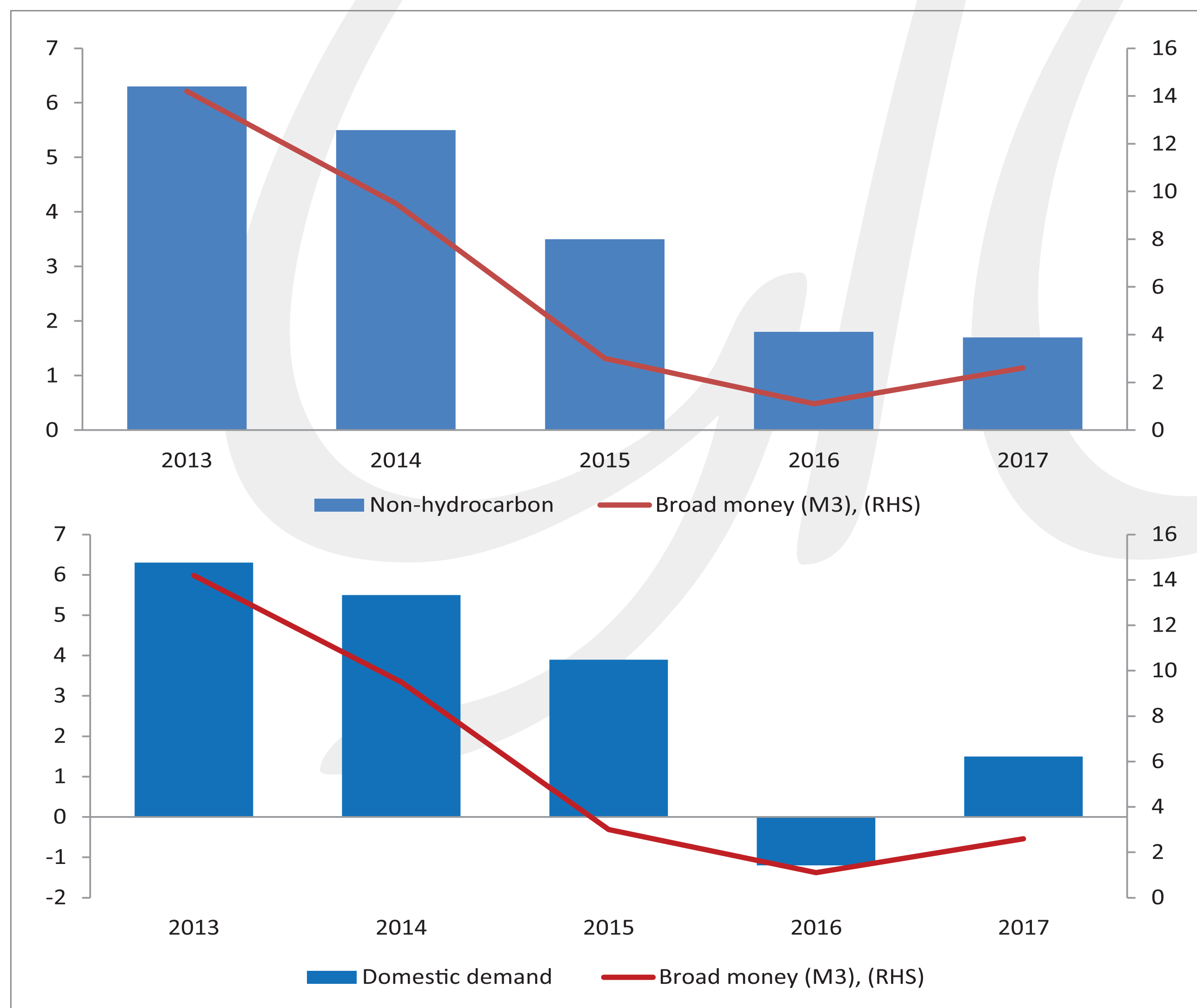
Table 25: Policy Rate (EOP)

	2013	2014	2015	2016	2017f
Bahrain	0.50	0.50	0.75	1.00	1.75
Kuwait	2.00	2.00	2.25	2.50	2.75
Oman	1.00	1.00	1.00	1.19	1.99
Qatar	1.02	1.00	1.31	1.90	2.20
KSA	0.25	0.25	0.50	0.75	1.50
UAE	1.00	1.00	1.25	1.50	2.00

Source: IIF, February 2018.

The following figures show a close association between broad monetary aggregate (M3) and both domestic demand and non-hydrocarbon GDP growth. Moderating growth in domestic demand and non-hydrocarbon GDP came in conjunction with a decline in broad money growth.

Figure 19: The Relationship between Money Supply, Non-Hydrocarbon Growth, and Domestic Demand in the GCC (% Change)



Source: IIF, January 2018.

In addition, money supply growth rate has varied across the GCC in recent years. For instance, while the growth rate of monetary aggregate (M3) has declined in Kuwait and Saudi Arabia to 2.6% and 0.5% in 2017, M3 increased sharply in Qatar from (-4.6%) in 2016 to 21.3% in 2017. The UAE and Oman witnessed slightly higher growth rates of 4.1% and 5.1% respectively, while it increased sharply in Bahrain from 1.1% in 2016 to 4.2% in 2017.

Table 26: M3 % Change

	2013	2014	2015	2016	2017
Bahrain	7.5	3.7	2.2	1.1	4.2
Kuwait	10.1	3.2	1.7	3.5	2.6
Oman	9.4	15.3	10	1.8	5.1
Qatar	19.6	10.6	3.4	-4.6	21.3
KSA	11	12	2.6	0.9	0.5
UAE	20.9	7.9	5.5	3.3	4.1

Source: IIF, February 2018.

FINANCIAL
REVIEW

Net Income Analysis

Gulf Investment Corporation (GIC) posted consolidated net profit of US$ 121 million for the year 2017 compared to US$57 million in 2016. This is after impairment provisions of US$60 million (2016: US$22 million) which mainly relates to an unquoted equity participation and provision for other assets in a subsidiary. Net change in revaluation reserves of financial assets available for sale and share of the revaluation reserves of associates totaling to US$ 6 million (2016: US$105 million) taking the consolidated total comprehensive income to US$ 127 million (2016: US$ 162 million).

Increase in profit compared to previous year was mainly due to the good results from two companies operating in cyclical industries which reported losses in the previous year. In addition to well preformed projects investment, the Hedge funds and Quoted equity investments outperformed compared to previous year.

Analysis of the contributing components to the net profit confirms good asset quality and the strength of GIC's investment philosophy.

Interest Income

Interest income is generated from the portfolio of debt securities, structured products and the money market book.

Gross interest income for the year US$56 million is 3% lesser than previous year. 89% of the interest income is contributed by securities. The gross interest income from securities decreased due to the decline in average volume compared to last year. The reduction in securities balance was in line with the repayment of the term finance US$ 500 million matured during the year.

Net Gains from Investments

Net gains from investments represent the realized gain on sale of financial assets, investment in associate, investment in subsidiaries and fair value gain on financial assets at fair value through statement of income.

GIC recorded a net gain of US$ 82 million during 2017 (2016: US$ 75 million) comprise of realized gains on financial assets available for sale of US$ 60 million (2016: US$ 42 million) and fair value gain of US$ 22 million (2016: loss of -US$ 2 million) from financial assets at fair value through statement of income. During the year 2016, GIC recorded gain on sale of a subsidiary company amounting to US$ 9 million, gain on sale of an associate amounting to US$ 10 million and a bargain purchase gain of US$ 16 million on acquisition of an associate company.

Dividend Income

Dividend income of US$ 12 million (2016: US$ 12 million) comprises of receipts from equity participations, private equity funds, equities and managed funds. Dividends from principal investment portfolio amounted to US$5 million compared to US$ 6 million in 2016. The balance contribution is from quoted GCC equities portfolio US$ 5 million and private equity funds US$ 2 million.

Share of Results of Associates

Share of results from associates accounted during the year amounted to profit of US$ 131 million compared to prior year profit of US$ 32 million. The major factor in the improved share of results compared to previous year was due to the recovery of major associates operating in Chemical and metal industries from losses in previous year supported by good operating performance from power & water, telecommunication and aircraft leasing companies.

Net Fees, Commission and Other Income

Income for the year amounted to US$ 3 million (2016: US$ 5 million) including the change in fair value of contingent consideration on acquisition of an associate.

Other Operating Income

Other operating income represents the income from consolidated subsidiaries amounting to US$ 1 million compared to US$ 8 million in previous year (note 17).

Interest Expense

Interest expense decreased by 14% compared to prior year to reach US$ 49 million for the year, which can be mainly attributed to the decrease in the overall funding volume compared to last year with the maturity of US$ 500 million whereas the interest rates slightly increased from last year.

Operating Expenses

Efficiency in operations and higher productivity was maintained with strict control over operating expenses with only a slight incline of 1% compared to last year to reach US$ 55 million.

Impairment losses

Net charge for the year in impairment losses totaled US$ 60 million, compared to US$ 22 million recorded in 2016. Impairment losses for 2017 related mainly to exposures in an unquoted GCC company and investment in a subsidiary company. The Corporation continues to adhere to its conservative provisioning policy, based on mark-to-market/fair valuations where-ever possible.

A detailed breakdown is provided in Note 18 to the Financial Statements.

Balance Sheet Analysis

Under the changing global scenario with declining business opportunities, emphasis is placed on risk adjusted return criterion in asset allocation continued focus mainly on the GCC region. Initiatives were implemented both, on the assets and liabilities sides maintaining the asset base at US$ 4,228 million. Equity at US$ 2,647 million increased by US$ 127 million compared to last year restated balance. Details of the restatement is provided in Note 6 to the Financial statements.

The Corporation's strategic focus continues to be on the GCC states. Note 20 to the Financial Statements sets out the geographic distribution of the Corporation's credit risk exposure.

The following sections provide details on the key components of the balance sheet:

Financial Assets at Fair Value through Statement of Income

This category includes investments in Debt instruments of US$ 49 million, Hedge funds and other alternative investments of US$ 340 million. The hedge funds portfolio decreased by net disposal amounting to US$ 99 million.

Financial Assets Available for Sale

As at 31 December 2017, financial assets available for sale amounted to US$ 1,702 million declined 23% from the prior year mainly due to the reduction in GCC debt portfolio. Debt and other interest bearing securities, constituting 66% of the financial assets available for sale decreased by US$ 435 million or 28% during the year. GIC reduced its investments in GCC and Islamic bonds by US$ 429 million compared to previous year end. Exposure to Emerging market bonds were increased during the year whereas International and Structured debt instruments decreased compared to previous year.

The debt portfolio is mainly made up of plain floating rate notes, fixed rate securities and structured products. This portfolio is monitored against stringent internal guidelines, ensuring that high quality is maintained. Major portion of the portfolio is comprised of investment grade issuers and high quality GCC sovereign credits. A credit risk analysis of the investment securities portfolio is provided in the risk management section of this report.

Financial assets available for sale also include investments in Equities and managed funds of US$ 196 million, Equity participation amounting to US$283 million and International & GCC private equity fund exposures of US$ 104 million. Investment in Equities and managed funds maintained at the same level by increasing exposure in global equities by US$ 9 million to compensate the reduction in GCC quoted equity investments of US$ 8 million. Decrease in Equity participations is mainly due to decrease in the market value of quoted projects of US$ 16 million and impairment loss taken on an unquoted investment of US$ 22 million partially offset by the increase in revaluation of unquoted securities by US$ 12 million.

The private equity funds are principally invested in equity investments of a structured finance nature with a wide range of externally managed private equity funds. These funds invest in leveraged and un-leveraged acquisitions, privatizations, recapitalizations, rapidly growing companies, expansion financings, turnaround situations, and other special equity situations.

Details on financial assets available for sale are provided in Note 5 to the financial statements.

Investment in Associates

An associate is a company over which the Group exerts significant influence. The Corporation's investments in associates are accounted for using the equity method of accounting. Under the equity method, investment in associate is initially recognized at cost and adjusted thereafter for the post-acquisition change in the Corporation's share of net assets of the investee company.

Principal investments in viable business ventures in the GCC region is a core activity of GIC. The focus has been on niche sectors like metal, petrochemical, power & utilities, financial services and building materials.

Investment in associates at US$ 1,590 million increased by US$337 million or 27%, which is mainly due to the investment in new associate companies, additional contributions to the existing companies, dividend received, share of results and share of net change in revaluation reserves.

Other Assets

Including property and fixed assets, total other assets amounted to US$ 274 million at 31 December 2017. Of this US$60 million related to property and other fixed assets and US$46 million relating to Margin money paid on derivative instruments. The remaining amount comprised of accrued income receivable, trade & accounts receivables, positive fair value of derivative instruments, prepaid expenses and other miscellaneous assets. Details are set out in Note 7 to the Financial Statements.

Liquidity and Funding

Total borrowings at US$ 1,367 million comprise of deposits from banks and other financial institutions of US$ 571 million and term finance US$ 796 million. Term finance decreased by US$ 472 million compared to previous year end mainly due to the maturity of US$ 500 million issue of Term loan during the year offset by US$ 28 million of foreign exchange movement.

A more detailed discussion on liquidity and funding, the various risks associated with our business activities, and capital strength is included in the Risk Management section that follows.

Other Liabilities

At US$214 million other liabilities comprise of trade payables of subsidiaries, accrued interest, accrued expenses, margin money for derivative products and negative fair value of derivative instruments. Decrease in other liabilities is mainly due to the decrease in negative fair value of derivative instruments entered mainly to hedge the currency exposure of term finance issues.

Equity

Equity at US$ 2,647 million increased by US$ 127 million mainly due to other comprehensive profit of US$ 6 million and net profit US$ 121 million.

RISK MANAGEMENT

Unequivocally, GIC remains a significantly resilient, measurably strong and stable financial institution. Risk management will continue to be an important aspect of corporate strategy and every effort will be made to ensure it is adaptive, effective and value adding.

The financial goal of the Corporation is to consistently earn competitive returns while maintaining risks within acceptable levels - defined risk appetite. Recognizing the relationship between risk and return, the management of risk forms an integral part of the corporate strategic objective. The continuous and rapidly changing business environment has increased the complexity and diversity of risks. The goal of risk management is to understand, analyze and manage these risks. Besides its vital role as the business protector, the risk function of the Corporation strives to contribute as a business enabler as well.

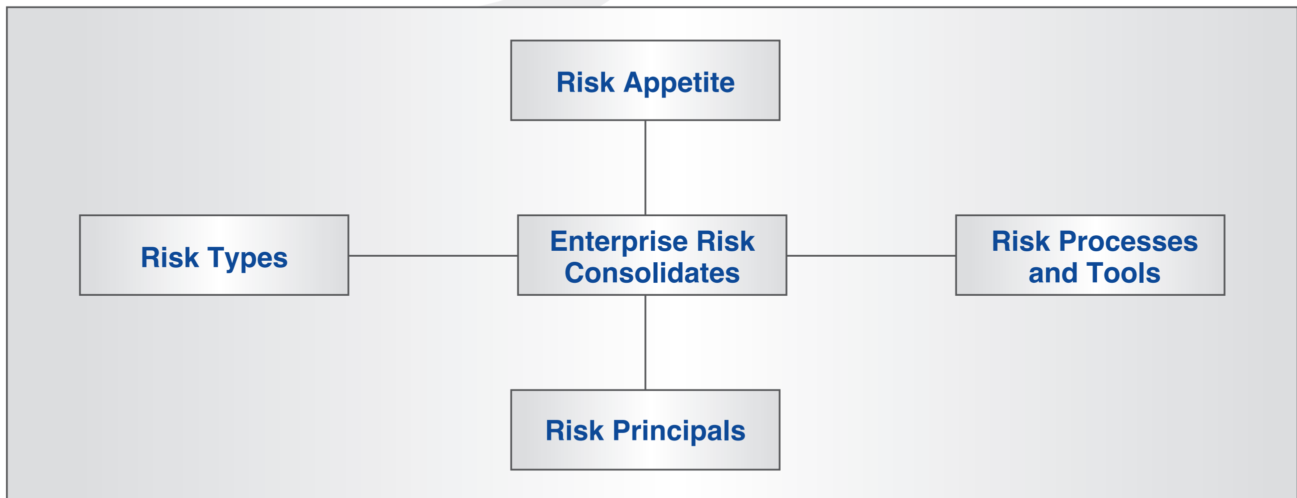
GIC's resilience during 2017, a challenging year in many respects, is testimony to strong business capabilities and a robust enterprise risk framework. Unequivocally, GIC remains a significantly resilient, measurably strong and stable financial institution. Risk management will continue to be an important aspect of corporate strategy and every effort will be made to ensure it is adaptive, effective and value adding.

The goal of risk management is not to avoid risks, but to comprehend and manage them.

The various business activities of the Corporation expose GIC to a wide spectrum of risks. The primary goal of the risk management is to ensure that an appropriate balance is maintained between risk taking activities, the expected return and GIC's risk appetite.

An independent Risk Management Division (RMD) formalizes the Enterprise Risk Management (ERM) framework. The ERM framework encompasses all facets of prudent risk management via strong enterprise-wide policies, procedures and limits.

With these tools Risk Management is able to identify strategic opportunities and reduce uncertainty from both operational and strategic perspectives. It also enhances GIC's ability to manage risks, evaluate performance and allocate capital.



The ERM framework identifies and defines a broad spectrum of risks to which GIC's business and operations may be exposed. These risks are: Credit, Market, Funding and Liquidity, and Operational risks.

Management of these risks through investment in knowledge and systems has been a priority at GIC. A successful blend of talent, experienced staff working with quantitative-based analytical tools, and utilizing continuously-upgraded technological infrastructure are critical resources that GIC applies in order to manage risks effectively. The qualitative and quantitative techniques utilized to optimize the risk return profile incorporate information from the past with emerging trends in the current business environment along with futuristic scenarios and expectations.

Structurally, risk management begins with the Risk Management Committee (RMC), composed of members from GIC's Board of Directors and senior management, which defines and recommends the Corporation's risk appetite to the Board of Directors'. Sequentially, this is followed by a three step process:

a) Identifying and measuring the various risks generated,

b) Monitoring, reporting and controlling them, and finally,

c) Optimizing in relation to the return.

The Risk Management team of GIC acts as a critical link between management and risk taking divisions by first assisting management to define / quantify risk appetite. The team then effectively communicates these risk appetite parameters to concerned risk takers in the Corporation in order to ensure that the risk taking activity is within the management's acceptable levels.

Within the Corporation, responsibility for the management of risk is not restricted to a single division. The philosophy has been to encourage a culture of prudent risk management across all business and support areas.

From an "Internal Control" perspective, the process of risk management is facilitated by a set of independent functions in addition to RMD. These units reporting directly to senior management include Financial Control, Internal Audit, Legal and Compliance. This multi-faceted approach enables the effective management of risks by identifying and monitoring them from a variety of perspectives.

The process of managing the risk categories identified above is discussed in more detail in the following sections.

CREDIT RISK

Credit risk refers to the risk of an economic loss that might arise from the failure of counterparty to fulfill its contractual obligations.

The world credit markets during 2017 were marked by increased volatilities on the backdrop of new US policy of trade protectionism and global trade readjustment and its impact on export driven economies across the globe, uncertainties surrounding Brexit and future of UK – European union partnership. As we move into 2018, volatility in the market is expected to remain high as markets digest a higher rate environment, a potential trade war between US and China and geopolitical risks. GIC with its active portfolio management registered an impressive performance on the credit portfolios. GIC remained relatively unscathed during the year, registering nil credit losses, thanks to prudent proactive measures, stringent control frameworks and continuous monitoring. While the Corporation's credit portfolio, mainly made up of debt securities, constitutes a material portion of the overall asset base, strong internal risk guidelines and proactive portfolio management ensure that high quality is maintained at all times. Notwithstanding the Corporation's rigorous and prudent policies for provisioning, no material write-downs were required during 2017. This is a reflection of the good quality of the portfolio. Gains of approximately US$ 8.4 million were realized during the year in review within GIC's credit portfolios.

GIC continued to focus on regional credit markets where the team has a better understanding of inherent risks. This has resulted in an enhanced risk return profile.

The Corporation continued to be flexible and ready to adapt rapidly to unforeseen events supported by the efficient utilization of conventional risk management tools, including mathematical and statistical models.

The primary tool used in the management of credit risk is a set of well-defined credit policies and procedures. In addition to communicating management's risk appetite in the form of country, product, industry and obligor limits, these policies also detail the process of measurement, monitoring and reporting. The stringent credit approval framework mandates a rigorous and thorough evaluation of creditworthiness of each obligor, after which limits are approved by management. Additionally, limits for product and industry are also defined to ensure broad diversification of credit risk. Credit policies and procedures are designed to identify, at an early stage, exposures which require more detailed monitoring and review.

The credit risk management process applies pertinent statistical methods as well, to estimate expected and unexpected loss amounts for the various business activities. The system, based on the Creditmetrics methodology, enables accurate credit risk measurement on an individual exposure as well as a portfolio basis. Expected and Unexpected loss estimates are computed based on Probabilities of Default (PD) and Loss Given Default (LGD) data published by leading rating agencies.

The Debt Capital Markets (DCM) portfolio which forms the largest asset class and constitutes approximately 29% of the balance sheet is monitored against a Credit Value at Risk (Credit VaR) limit, approved by the board. The US$ 255 million VaR limit (99.96% confidence, 1 year), which supplements the existing notional limits for this portfolio, is based on the Creditmetrics methodology and is measured using Monte Carlo simulation techniques.

The table below provides the Credit VaR figures for the DCM Portfolios. On 31st December 2017 the market value of this portfolio was US$ 1,181.3 million. As of 1st Jan 2017, it was US$ 1,598.7 million. The average and year end Credit VaR were down as compared to previous year end. The decrease in Credit VaR was in line with the overall reduction under DCM Portfolios.

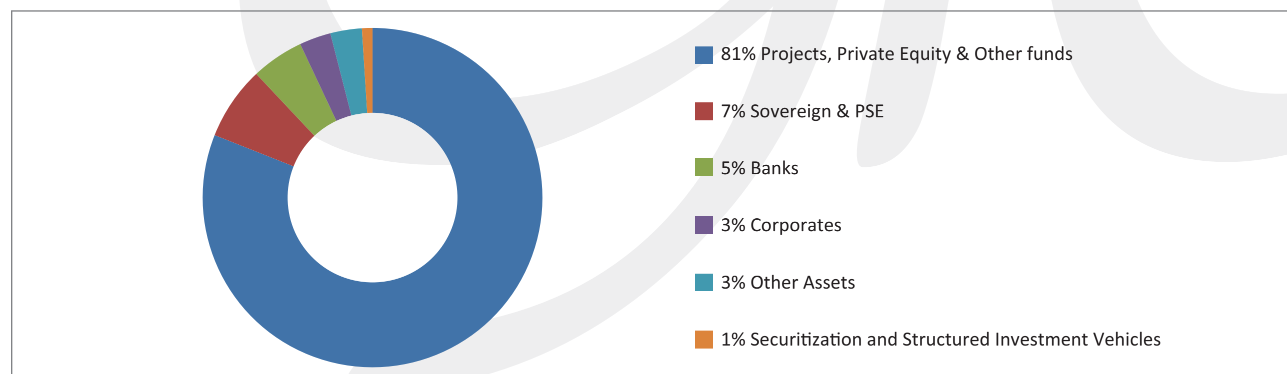
Table 1: 2017 Credit Value at Risk - 99.96% confidence level, 1 year holding period

US$ 000's	Average	Minimum	Maximum	31 Dec 2017
Debt Portfolios	196,491	145,514	254,207	145,889

Although, business units are responsible for maintaining exposures within limits, actual exposures are continuously monitored by independent control functions including Risk Management, Financial Control, Compliance and Internal Audit. Technology is a key element in the monitoring process. To illustrate, cutting edge systems that are capable of approaching "real time" monitoring and control of risk taking activities, are effectively utilized.

An activity-wise break down of the principal sources of credit risk is illustrated in the pie chart below. The proportions reflect Credit Risk Weighted Exposure, computed based on BIS capital Adequacy Guidelines. Additional details, including credit exposures by rating, sector, geography and maturity are provided in the comprehensive Basel III Disclosure section.

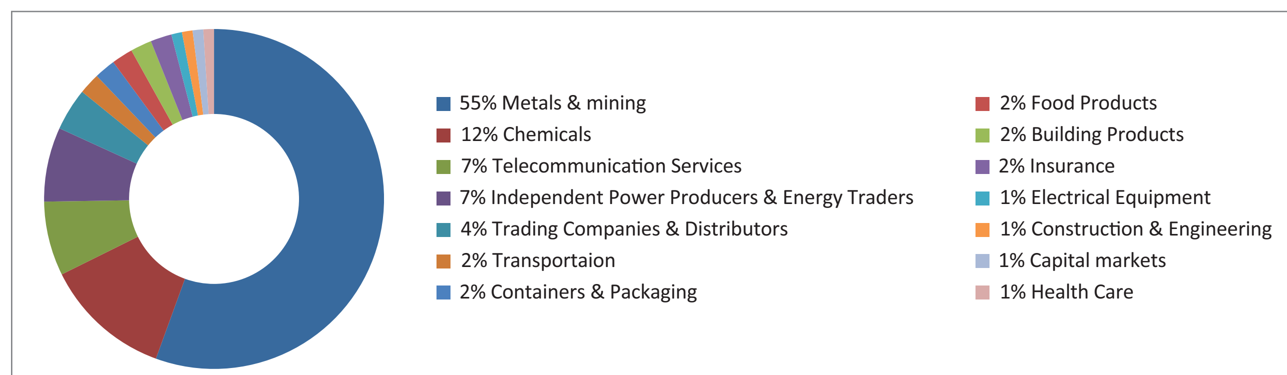
Chart 1: Sources of Credit Risk (Weighted Credit Risk Exposure)



Noteworthy, most of the realignment in the credit risk pie at the end of 2017 compared to the previous year-end, pertained to Projects, Private Equity & other funds. Credit risk weighted exposure for Projects, Private Equity & other funds increased from 67% of total in 2016 to 81% at the 2017 year-end and for Banks decreased from 11% in 2016 to 5% at the 2017 year-end and for Sovereigns & PSE decreased from 12% of total in 2016 to 7% at the 2017 year-end. The two key components of total credit risk exposure were Projects, Private Equity & other funds, and debt securities of banks, sovereign & PSE and Corporates.

The projects activity mainly focuses on the GCC countries, a region whose thriving dynamics we comprehend well and where we have a better understanding of the inherent risks. Investments are made after rigorous qualitative and quantitative analysis, and where the desired risk-return objectives are met. As highlighted in the graph below, a healthy diversification across industry sectors is maintained within this portfolio. Private Equity and other Equity Funds represent investments made with third party fund managers typically in the United States and Europe who are selected after careful assessment of their records and extensive due diligence.

Chart 2: Principal Investing (Projects) by Industry



Off-balance Sheet Financial Instruments

In the normal course of its business, the Corporation utilizes derivatives and foreign exchange instruments to meet its financial needs, to generate trading revenues and to manage its exposure to market risk.

In the case of derivatives and foreign exchange transactions, procedures similar to on balance sheet products are used for measuring and monitoring credit risk. Credit risk weighted exposure to off balance sheet products amounted to nearly 0.1% of total credit risk weighted exposure.

At the year-end 2017, there were no outstanding derivatives held for trading. Off balance sheet transactions also include credit-related contingent items designed to meet the financial requirement of the Corporation's customers. A detailed credit risk analysis of credit- related contingent items, derivatives and foreign exchange products is set in Notes 20, 21 & 22 to the Consolidated Financial Statements.

In an uncertain and volatile global credit market, the Corporation will continue to adhere to strong internal risk controls.

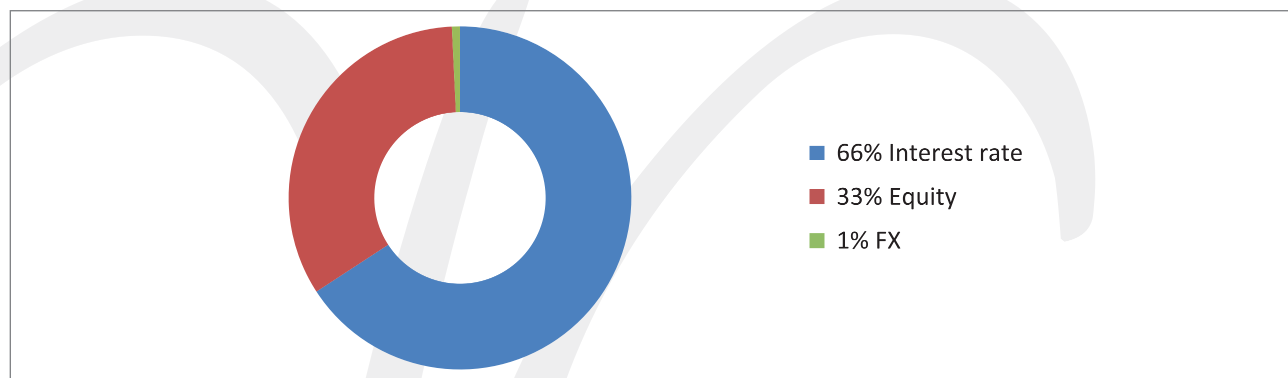
While the mechanism of risk monitoring and control has been fostered further, the risk management function is now more engaged with the business units, having been brought forward within the investment process. In addition to incorporating additional credit information, including Credit Default Swap (CDS) prices, equity prices and market implied ratings within the credit analyses framework, the monitoring and reporting frequency has also been increased.

MARKET RISK

Market risk is the possibility of loss from changes in value of financial instruments, resulting from an adverse change in market factors.

Within the Corporation, market risk is made up of three key risk constituents - interest rate risk, equity risk and foreign exchange risk. A breakdown, based on risk constituents, is provided below for the combined mark-to-market and investment activities, within the Global Markets Group alone (strategic equity positions within the Principal Investment business are not included). The percentages shown on the pie chart reflect average VaR amounts, considered independently, and ignore the effects of diversification across risk classes.

Chart 3: Market Risk Constituents - Overall



Market risk is measured, monitored and managed, both on a notional basis, and using a Market Value-at-Risk (Market VaR) concept. A blend of quantitative statistical methods combined with expert judgments and experienced talent is used to effectively manage market risk. A system of limits and guidelines restrain the risk taking activity with regard to individual transactions, net positions, volumes, maturities, concentrations, maximum allowable losses and other parameters. It ensures that risks are within the acceptable levels in terms of notional amounts. The VaR based system provides a more dynamic measure of market risk, capturing in a timely manner the impact of changes in the business environment on the value of the portfolio of financial instruments.

Market VaR is calculated and reported to senior management on a daily basis at various levels of consolidation including portfolio, business unit and Corporation.

The following table provides Total Value-at-Risk statistics for Global Markets Group by risk factor (please note: Total Global Markets Group VaR excludes Strategic Equity investments within Principal Investing). These VaR measures are based on a 95% confidence level, 25 day holding period and use historical data sets.

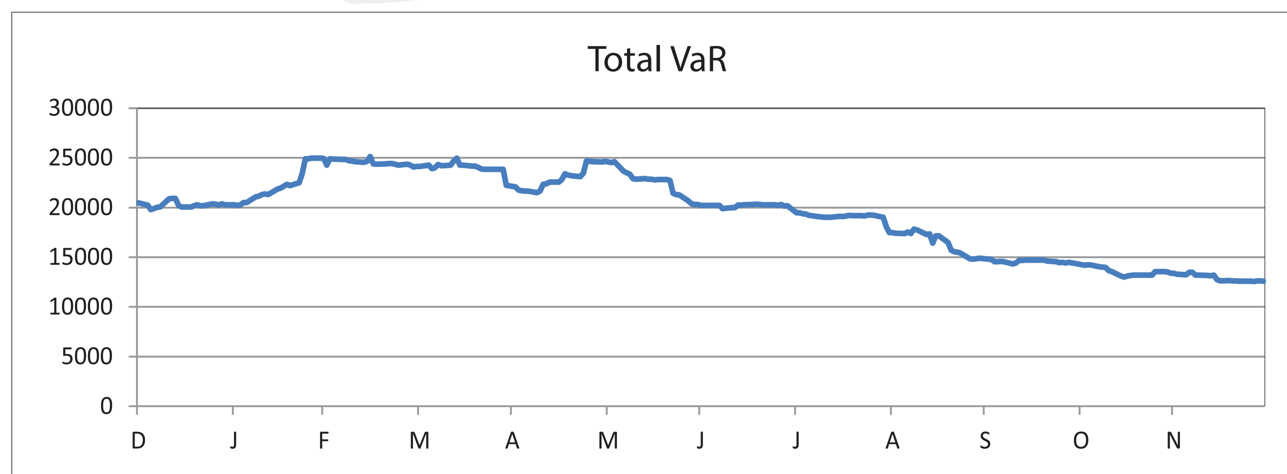
Table 2: Market Value at Risk for Global Markets Group alone - 25 day holding period, 95% confidence level

2017				
US$ 000's	Average	Minimum	Maximum	31-Dec-16
Interest rate	18,587	10,951	24,982	10,791
Equity	9,446	6,755	12,927	7,29
Foreign Exchange	214	141	706	399
Total*	19,430	12,564	25,120	12,288
2016				
US$ 000's	Average	Minimum	Maximum	31-Dec-16
Interest rate	21,677	18,816	25,290	20,596
Equity	15,176	11,588	18,520	12,666
Foreign Exchange	1,140	266	4,211	532
Total*	22,660	19,394	26,369	20,420

** Total VaR incorporates benefits of diversification*

On an average basis, VaR pertaining to market risk is approximately lower as compared to the previous year. The 5 year fixed rate liability issued in 2012 continues to act as a hedge, offsetting some of the interest rate risk at the corporate level. As at 31st December 2017, total market risk VaR reached US$ 12.3 million. Total market risk VaR remained within limits as approved by the Risk Management Committee and the Board of Directors. The Corporation will closely monitor the operating environment and seek to take on appropriate market risk at opportune times.

Chart 4: Profile of daily VaR - 25 day holding period, 95% confidence level, VaR (US$ 000's):



It should be noted that certain portfolios and positions are not included in the Market VaR analysis, where VaR is not the most suitable measure of risk. These include the principal project investments in the GCC and the portfolio of international private equity funds. The market risk relating to these investments are measured in terms of a 10% sensitivity measure - an estimated decline in asset values. The fair values of the underlying positions may be sensitive to changes in a number of factors, including but not limited to: the financial performance of the companies, projected timing and amount of future cash flows, discount rates, trends within sectors and underlying business models. The table below provides the sensitivity measure for 2017 and 2016. The principal investment and private equity portfolios are both categorized as available-for-sale; hence, the 10% sensitivity measure provided in the table below reflects the impact on shareholders equity and not on profits.

Table 3: Sensitivity Measure: for assets not included in market VaR (US$ 000s)

Asset Categories	**10% sensitivity measure**	**10% sensitivity measure (impact on shareholders' equity)**	
		31-Dec-17	31-Dec-16
Principal Investments	Underlying asset value	192,210	165,140
Private Equity Funds	Underlying asset value	10,385	14,410

Likewise, scenario analysis is an essential component of the market risk management framework. The assumption of normality on which the statistical models are based may become invalid due to the occurrence of certain events. Future scenarios that result in a breakdown of the historical behavior and relationships between risk constituents are projected, and potential loss amounts are determined. Most of these scenarios are derived from historical macroeconomic trends adjusted for fermenting and unfolding developments and expectations about futuristic events.

Liquidity Risk Management

Liquidity risk is the failure to meet all present and future financial obligations in a timely manner and without undue effort, whether it is a decrease in liabilities or increase in assets. This risk may be further compounded by the inability of the Corporation to raise funds at an acceptable cost to meet its obligations in due time.

There are two sources of liquidity risk that GIC takes into account, which are:

a) Cash flow illiquidity, arising from the inability to honor financial commitments or to procure funds at reasonable rates and required maturities; and

b) Asset illiquidity, relating to the lack of market depth during times when assets are to be liquidated on a forced basis.

The Corporation believes that capital plays a special role in liquidity planning inasmuch as liquidity problems could arise in the short run if the market believes that capital has been so impaired that in the long run the Corporation may not be able to pay-off its liabilities.

GIC's management of liquidity considers an overall balance sheet approach that brings together all sources and uses of liquidity. More specifically, liquidity requirements cover various needs that are addressed by the Corporation's senior management. Among these needs are:

a) Meeting day-to-day cash outflows;

b) Providing for seasonal fluctuation of sources of funds;

c) Providing for cyclical fluctuations in economic conditions that may impact availability of funds;

d) Minimizing the adverse impact of potential future changes in market conditions affecting GIC's ability to fund itself; and

e) Surviving the consequences of loss of confidence that might induce fund providers to withdraw funding to GIC.

Liquidity Limits

As part of the funding and liquidity plan, liquidity limits, liquidity ratios, market triggers, and assumptions for periodic stress tests are established and approved. The size of the limit depends on the size of the balance sheet, depth of the market, the stability of the liabilities, and liquidity of the assets. Generally, limits are established such that in stressed scenarios, GIC could be self-funded.

The liquidity limits that are regularly monitored include the following:

a) Maximum daily cash outflow limit for major currencies;

b) Maximum cumulative cash outflow which should include likely outflows as a result of draw-down of commitments, etc.; and

c) Net liquid asset ratio - this ratio is calculated by taking a conservative view of marketability of liquid assets, with a discount to cover price volatility and any drop in price in the event of a forced sale. The ratio is the proportion of such liquid assets to volatile liabilities.

The net liquid asset ratio as of 31st December 2017 was 255%. This figure was determined taking into account the following basic criteria:

a) A 3-month remaining maturity is used to establish the time threshold by which balance sheet items are determined to be liquid or illiquid, stable or volatile;

b) Appropriate "haircuts" are applied on liquid assets to reflect potential market discounts; and

c) A "business as usual" posture is maintained in ascertaining the level of assets to be liquidated or pledged to avoid sending a wrong signal to the market.

The Corporation's investment portfolio is managed so that the holdings of un-pledged, marketable securities that are comprised of strategic reserves are equivalent to approximately 50% of the projected maximum 30 day cumulative cash outflow. By the end of December 2017, investments in marketable securities tallied at approximately US$ 1.3 billion, and are primarily made up of investment grade securities.

The quantities of pledged securities are reviewed periodically in order to ensure that the quantity of pledged securities does not exceed the amounts actually required to secure funding or for other purposes. Additionally, to the greatest extent possible, the selection of securities to be pledged is made in a manner whereby the longest term and/or least marketable securities are utilized.

Market Access for Liquidity

Effective liquidity management includes assessing market access and determining various funding options. That said, GIC deems it critical to maintain market confidence to attain the flexibility necessary to capitalize on opportunities for business expansion, and to protect the Corporation's capital base.

Proactive and prudent liquidity management requires a stable and diversified funding structure. To this end, GIC always maintains a well-balanced portfolio of liabilities in order to generate a stable flow of financing and to provide protection against sudden market disruptions. To the extent practical and consistent with other GIC objectives, the Corporation emphasizes both minimal reliance on short-term borrowed funds as well as the use of intermediate and long-term borrowings in place of short-term funding.

A diversity of funding sources, currencies, and maturities are used in order to gain a broad access to the investor base. The proactive steps GIC undertook during the previous years, particularly in terms of raising medium term financing, enabled the Corporation to secure a sound asset-liability maturity profile. As of 31 December 2017, the Corporation's term financing stood at US$ 790 million.

Further, the Corporation was successful in enhancing the diversity of its depositor base, a reflection of increased market confidence. At year-end 2017 the Corporation's deposit base stood at about US$ 571 million, 100% of which is due to GCC depositors. GCC deposits have proven to be a stable source of funds over the years.

The table below provides the breakdown of the Corporation's funding source for the comparative years 2016 to 2017.

US$ Millions	2017 (US$)	2017 (%)	2016 (US$)	2016 (%)
GCC Deposits	571	14	570	13
International Deposits	0	0	0	0
Repo Financing	0	0	0	0
Term Financing	791	19	1, 260	28
Shareholder'sfunds andothers	2,746	67	2,654	59
Total	**4,107**	**100**	**4,483**	**100**

Contingency Funding Plan

Within GIC, liquidity is managed through a well-defined process to ensure that all funding requirements are met properly. This process includes establishment of an appropriate contingency funding plan (CFP).

GIC's CFP prepares the Corporation for the unlikely event of a liquidity crisis caused by material changes in the financial market conditions, including credit rating downgrades. CFP procedures are articulated clearly in the Corporation's Liquidity Policy Document.

These procedures include:

a) A suite of measures to be undertaken in the absence of liquidity crisis to enhance GIC's available liquidity in the event of a crisis;

b) Careful identification of specific triggers that would prompt activation of CFP; and;

c) Specification of exact guidelines for adequate management of liquidity crisis.

Throughout the challenging year, our liquidity position remained adequate to carry on with our strategy.

Interest Rate Gapping Risk

GIC actively manages its interest rate exposure to enhance net interest income and limit potential losses arising from the mismatches between placements, investments and borrowings. It is one of the primary responsibilities of the Treasury management group. The Interest Rate Gap is measured in Eurodollar futures contract equivalents. It is widely accepted that the rate calculated from short-dated (up to two years) Eurodollar futures contract is effectively the forward interest rate of the underlying. Any funding, placements or borrowing that has a maturity or re-pricing of over two (2) years are either matched or hedged.

Since GIC also runs gapping positions in other major currencies apart from the USD, the gaps on these currency positions are translated to USD equivalents in order to estimate the equivalent number of Eurodollar futures contract.

The Eurodollar futures contract, given its liquidity, is a reasonable proxy to gauge interest rate risk on the short-term funding gap. The rationale behind this type of measurement is, if necessary, positive (negative) gaps within a given time bucket could be covered by selling (buying) Eurodollar futures contracts equivalent to the notional amount of the gaps. Potential contracts from individual time buckets are accumulated for each currency and then subsequently aggregated for all major currencies. The maximum number of notional contract is currently set at 3,500.

Treasury is responsible for monitoring and ensuring that potential short-term interest rate risk exposure remains within the authorized limits. However, proper escalation procedures are in place to address temporary and permanent excesses.

The Eurodollar futures contract position value as at December 31, 2017 was 2,080 contracts, with an estimated VaR of US$ 600,00. This is higher than the levels of the previous year (31st December 2016: 1,846 contracts). This is excluding the impact of the fixed rate EMTN issuance.

Maturity profile of assets and liabilities

A detailed breakdown of the maturity profile by individual asset and liability category is provided in Note 20.1 to financial statements. At December 31st 2017, roughly 43% of total assets were due to mature within 3 months, based on internal assessment of the Corporation's right and ability to liquidate these instruments. Comparatively, on the same basis, approximately 37% of total liabilities were in the same time bucket. The sizable portfolio of high quality marketable securities contributed to the relatively high ratio of liquid assets. The Corporation's GCC retention record shows that short maturity deposits from GCC governments, central banks and other regional financial institutions have been regularly renewed over the past several years. With the success achieved in raising medium term finance, the Corporation was able to optimize the asset liability maturity gap, especially within the medium and long term buckets.

CREDIT RATING

In 2017, both rating agencies (Moody's & Fitch) reaffirmed GIC's credit ratings. GIC's strong financial indicators were acknowledged in the rating reports. As of end 2017, GIC's long term deposits were rated A2 by Moody's and A- by Fitch.

All ratings carry a stable outlook. GIC continues to be rated AAA by Rating Agency Malaysia (RAM).

	Moody's	Fitch	RAM
Long-term Deposits	A2	A-	AAA
Short-term Deposits	P1	F1	P1

CAPITAL STRENGTH

Capital represents the shareholder's investment and is a key strategic resource which supports the Corporation's risk taking business activities. In line with the Corporation's financial objective, management strives to deploy this resource in an efficient and disciplined manner to earn competitive returns. Capital also reflects financial strength and security to the Corporation's creditors and depositors. Capital management is fundamental to GIC's risk management philosophy, and takes into account economic and regulatory requirements.

The Corporation's capital base stood at US$ 2,647.6 billion at 2017 year end. GIC continues to be one of the best capitalized financial institutions in the region.

OPERATIONAL RISK

Operational Risk is the risk of loss resulting from inadequate or failed processes, people, or systems, either internally or externally, and unexpected significant and unusual one-time events.

- Other risks to which GIC is exposed to include Regulatory, Strategic, and Reputational;
- Regulatory risk is controlled through a framework of Compliance policies and procedures;
- Strategic risk is managed through the close monitoring of reviews, targets and goals, by senior management; and
- Reputational risk is controlled through clear and transparent guidelines and the GIC Code of Conduct.

KEY AIMS:

The management of Operational Risk has the following key objectives:

- to identify, assess, control and mitigate operational risk and the effective reporting of risk and emerging risk issues; and
- to embed operational risk awareness in all our activities, including the practices and controls used to manage other types of risks.

OVERVIEW:

GIC's Operational Risk Framework is composed of four key components:-

a) Risk and Control Self-Assessment framework;

b) Loss Event framework;

c) Corrective Action Plans framework; and

d) Operational Risk Reporting framework.

By providing a basis for the institutional understanding of Operational Risk, the framework supports a culture in which employees are aware of the risk inherent in the daily operations, and are encouraged to proactively identify existing, emerging and/or other potential problems.

a) Risk and Control Self-Assessment (RCSA) Framework.

The RCSA procedures establish a consistent framework for describing the key business activities, risks and controls. The controls are then assessed on a regular frequency. It is a process which transparently assesses the business's risks and analyzes the strength or weakness of controls that are put in place to in order to manage the identified risks.

The assessment of fraud detection controls have also been integrated within the RCSA process.

b) Loss Event Framework

Operational loss events are reported in a central database. Comprehensive information about these events is collected, and includes information regarding the amount, occurrence, discovery date, business area and product involved, and detailed root cause analysis.

In keeping with our broad definition of Operational Risk, we began to include data on events with non-monetary impacts and near- miss events in our collection and analysis activities.

c) Corrective Action Plans (CAPs) Framework

The CAPs framework is a key component of management practice to identify, document and resolve control issues or any high risk exposures. This includes issues identified through our integrated RCSA and monitoring program, internal audits, Compliance reviews, or Operational Risk loss event reporting.

It will enable management to demonstrate to audit (internal and external) and regulators, that management is aware and is actively addressing issues as well as monitoring the timely resolution of these issues.

The Risk Management Committee will be kept abreast of all material Operational Risk issues that have been identified.

d) Operational Risk Reporting Framework

The Reporting framework is used to ensure that all Operational Risk types and events are categorized and reported consistently following the Basel II ratings methodology. This will help to:

- establish a common language regarding Operational Risk, throughout the Corporation; and
- facilitate the correlation of similar events and to identify causes (rather than symptoms) of risk within departments.

OPERATION RISK WEIGHTED EXPOSURE:

The Operational Risk Weighted Exposure sets out the risk measurement framework, i.e. the quantitative criteria for calculating the capital charge for operational risk that follows the Standardized Approach developed by the Basel Committee on Banking Supervision.

The Corporation's business activities are categorized within the identified business lines to be used i.e. Principal Investment, Debt Capital Market, Equities Investments, Alternative Investments, Treasury, and Head Quarters.

INSURANCE:

As part of the Enterprise Risk Management solution, the Corporation uses a comprehensive suite of insurance policies to mitigate the impact of operational risks and to ensure adequate coverage. These policies are closely aligned to the operational risk profile and are cost beneficial to GIC.

BUSINESS CONTINUITY AND DISASTER RECOVERY PLANNING:

The Business Continuity Plan Team, led by Operational Risk and Information Technology, are responsible for creating, managing and continuously improving GIC's disaster recovery planning. Currently there are three active and fully tested disaster recovery sites:-

- Kuwait (Local)
- Bahrain (Regional)
- Luxembourg (Outer-Regional)

LEGAL RISK MANAGEMENT:

GIC has a dedicated General Counsel, for the effective management of legal risks by the provision of legal advice and litigation management.

INFORMATION SECURITY FRAMEWORK:

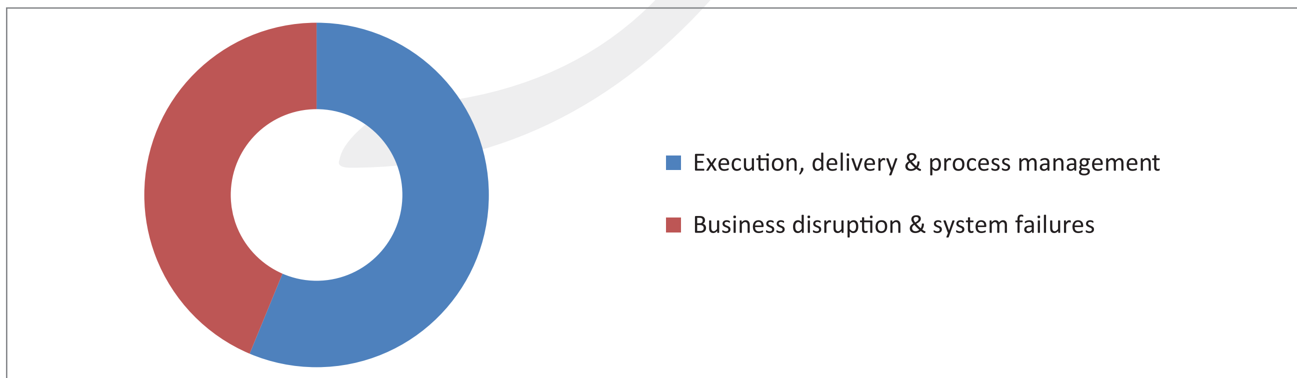
A secure information security framework is in place to identify the responsibilities at every level of information handling, i.e. from data ownership (encoding) to data access. Periodic audits are conducted to ensure compliance with the policies and standards set, by Internal Audit, Information Security Risk Officer and the Risk and Control Self-Assessment review. During 2015, the Corporation's Information Security Management obtained the ISO 27001:2013 certification.

OPERATIONAL LOSS EVENT PROFILE FOR 2017:

The Corporation monitors the loss events by the Basel II loss event categories.

There are no threshold limits - all events whether a loss or gain are captured, including near misses.

During 2017, the highest frequency of events occurred under the following categories:



BASEL III
DISCLOSURE

Basel III Rationale:

Aligning banking risk management with Capital Requirements

In response to the lessons learnt from the global financial and economic crisis in 2008, and to address the market failures across the banking sector revealed by the same, the Basel Committee issued the Basel III framework. Basel III regulations aim to strengthen the quality of capital and increase the regulatory capital requirements to help absorb losses. In addition, the introduction of capital buffers as part of prudential policies is applied by regulatory authorities to prevent global risks and enhance financial stability.

With Basel III, the Basel Committee is raising the resilience of the banking sector by strengthening the regulatory capital framework, building on the three pillars of the Basel II framework. The reforms raise both the quality and quantity of the regulatory capital base and enhance the risk coverage of the capital framework. They are underpinned by a leverage ratio that serves as a backstop to the risk-based capital measures, is intended to constrain excess leverage in the banking system and provide an extra layer of protection against model risk and measurement error. Finally, the Committee is introducing a number of macro prudential elements into the capital framework to help contain systemic risks arising from procyclicality and from the interconnectedness of financial institutions.

Also, the Basel Committee is introducing internationally harmonised global liquidity standards. As with the global capital standards, the liquidity standards will establish minimum requirements and will promote an international level playing field to help prevent a competitive race to the bottom.

The Architecture of Basel III - Capital and Liquidity

With Basel III, the Basel Committee continues with the three-pillar that seeks to align regulatory requirements with economic principles of risk management. Principles of sound liquidity risk management and supervision have been incorporated into the standard on account of lessons learned during the crisis and is based on a fundamental review of sound practices for managing liquidity risk in banking organizations.

The Three Pillars Defined

Pillar 1 - Minimum Capital Requirements

Pillar 1 sets out minimum regulatory capital requirements -meaning the amount of capital banks must hold against risks. Greater focus under the new accord is on quality and level of capital, capital loss absorption at the point of non-viability, capital conservation buffer and countercyclical buffer. The new framework provides for higher risk coverage for certain complex securitizations, significantly higher capital for trading and derivatives activities, substantial strengthening of the counterparty credit risk framework and risk coverage for bank exposure to central counterparties. A key measure introduced under the new accord is a non-risk based leverage ratio to serve as a backstop to the risk-based capital requirement and to helps contain system wide buildup of leverage. The new accord provides for a continuum of approaches from basic to advanced methodologies for the measurement of both credit and operational risks. It provides a flexible structure in which banks, subject to supervisory review, will adopt approaches that best fit their level of sophistication and their risk profile. The framework also deliberately builds in rewards for stronger and more accurate risk measurement.

Pillar 2 - Risk Management and Supervision

Pillar 2 defines the process for supervisory review of a bank's governance and risk management framework and ultimately, its capital adequacy. It sets out specific oversight responsibilities for the board and senior management, thus reinforcing principles of internal controls and corporate governance practices. Financial supervisors would be responsible for evaluating how well banks are assessing their capital adequacy needs relative to their risks. Intervention would be exercised, where appropriate.

Pillar 3 - Market Discipline

Pillar 3 aims to bolster market discipline through enhanced disclosure by banks. It sets out disclosure requirements and recommendations in several areas, including the way a bank calculates its capital adequacy and its risks assessment methods. The intended result is enhanced transparency and comparability with other banks.

Gulf Investment Corporation G.S.C. (GIC or 'the Corporation') -

Market Disclosure

The following sections set out the Corporation's disclosure details prepared in line with the new accord's requirements via its publication dated December 2010- Basel III: A global regulatory framework for more resilient banks and banking systems and revisions to the same and Liquidity coverage ratio disclosure standards dated January 2014 and revisions to the same.

1. Capital Structure

GIC is an investment company incorporated in the State of Kuwait on November 15, 1983 as a Gulf Shareholding Company. It is equally owned by the governments of the six member states of the Gulf Cooperation Council (GCC), i.e., Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates. The Corporation has no subsidiaries or significant investments in banking, insurance, securities, and other financial entities.

Table 1 presents the Corporation's regulatory capital resources for the years ending December 2017 and December 2016. Basel III permits recognition of general provision (albeit subject to a maximum of 1.25% of credit risk weighted assets) as part of Tier 2 capital. Meanwhile, the exposures to 'securitization' that fall below a cut-off risk grade are deducted 50% from Tier 1 and 50% from Tier 2 capital, respectively. For 2017, full deduction is made from Tier 1 capital due to negative fair value adjustment. Total eligible regulatory capital was US$ 2,560.0 million by year-end December 2017 compared to US$ 2,477.4 million recorded in December 2016. The Corporation has adopted a conservative policy for the treatment of net fair value reserve, wherein, if negative - the total amount is deducted from eligible capital, and if positive - only 45% of fair value reserve is included within eligible capital.

Table 1: Regulatory Capital Resources

In US$ millions	**31 December 2017**	**31 December 2016**
Paid-up capital	2,100.0	2,100.0
Disclosed reserves	525.5	571.0
Retained earnings	55.1	0.0
Less: Goodwill	67.4	38.8
Less: Deductions	1.2	1.5
Less: Adjustment for Fair value reserve	52.0	153.3
Total Tier 1 Capital	2,560.0	2,477.0
Total Tier 2 Capital	-	-
Total eligible regulatory capital	2,560.0	2,477.0
In US$ millions	**31 December 2017**	**31 December 2016**
Common Equity Tier 1 (CET1)	2,560.0	2,477.0
Additional Tier 1 (AET 1)	-	-
Total Tier 1 Capital	2,560.0	2,477.0
Total Tier 2 Capital	-	-
Total eligible regulatory capital	2,560.0	2,477.0

2. Capital Adequacy Management

The Corporation's primary guiding principle to its capital adequacy management is to maintain a strong capital base that could support current as well as future growth in business activities, and at the same time, with the objective of maintaining satisfactory capital ratios and high credit ratings.

GIC's process of assessing the capital requirements commences with the compilation of the annual business plan by individual business units which are then consolidated into the annual budget plan of the Corporation. The annual budget plan provides the estimated overall growth in assets, its impact on capital and targeted profitability for the forthcoming fiscal year. Utilizing the financial projections generated from the budget plan, capital is allocated to the various business units in such a way that the allocations remain consistent with the risk profile of the business activity. These capital allocations as well as corresponding Return On Risk-Adjusted Capital (RORAC) are reviewed on an ongoing basis during the budget year in order to optimally deploy capital to achieve targeted returns. Whilst the Corporation acknowledges the benefits of higher leverage to Return on Equity (ROE), it also believes in the advantage and benefit of keeping a strong capital position. As such, GIC maintains a prudent balance among the major components of its capital. Current internal policy aims to maintain a floor of 16% total capital adequacy ratio.

The annual dividend payout, meanwhile, is prudently determined and proposed by the Board of Directors, endeavoring to meet shareholder expectations while ensuring adequate retention of capital to support organic growth. Finally, the Corporation targets a credit risk rating of single 'A' or better. This would allow easy access to capital from the market at competitive pricing in the event additional funding needs to be appropriated. GIC is among a select few financial institutions in the region to maintain high ratings by both major international agencies (Moody's & Fitch). Details of the Corporation's ratings are provided on page 48 of this annual report.

Table 2: Capital Adequacy Ratios

In US$ millions	Risk-weighted assets	Capital requirement
Credit Risk	4,383.5	350.7
Market Risk	1,498.5	119.9
Operational Risk	431.9	34.5
Total	6,313.9	505.1
Capital Adequacy Ratios		
Total CAR	40.5%	
Common Equity Tier 1 (CET1)	40.5%	
Tier 1 Ratio	40.5%	
Leverage Ratio (Non risk based)	33.1%	

Table 2 details the risk-weighted assets together with their corresponding regulatory capital requirements as at 31 December 2017. Total capital adequacy ratio and Tier 1 capital ratio are likewise calculated. The numbers were generated by applying the 'Standardized' approach for credit and operational risks, while the 'Internal Model' approach was utilized to yield market risk positions. Total risk-weighted exposures of US$ 6,313.9 million, as at 31 December 2017, requires regulatory capital of US$ 505.1 million to meet the minimum Basel III CAR of 8%. Should the minimum CAR threshold be raised to GIC's internal target of 16%, the required regulatory capital increases to about US$ 1,010.2 million. The reported eligible regulatory capital of US$ 2,560.0 million still provides sufficient cushion to support business expansions.

Table 3: Risk Exposure Break-down

In US$ millions	31 December 2017
Credit Risk (RWA)	
Claims on sovereigns	211.1
Claims on Public Sector Entities	99.0
Claims on Banks	222.5
Claims on Corporates	156.2
Securitization and Structured Investment Vehicle	9.1
Venture Capital and Private Equity	119.7
Investments in Commercial Entities	3,253.5
Investments in Other Funds and Quoted Equities	192.6
Other Assets	119.8
Total	4,383.5
Market Risk (VaR)	
Interest rate risk position	5.8
Foreign exchange risk position	0.0
Equity risk position	23.8
(Total VaR + Stress VaR) x 3	88.8
Specific risk position	31.1
Total capital requirement	119.9
Total RWA (capital requirement x 12.5)	1,498.5
Operational Risk (RWA):	
Operational risk capital charge	34.5
Total RWA (capital charge x 12.5)	431.9

3. Risk Management Structure

To address the continuously changing and complex business environment, the Corporation adapts an agile and effective risk management process. Management realizes that not all risks needs to be eliminated; however, they need to be systematically identified and measured in order to be properly managed. To this end, the Corporation established an effective Enterprise Risk Management framework to enable a process of achieving an appropriate balance between risk and reward, by optimizing profits and ensuring that GIC is protected from unwarranted exposures that are likely to threaten the viability of the Corporation.

The Corporation's risk management process is an integral part of the organization's culture, and is embedded into the organization's practices as well as in all those involved in the risk management process.

The Risk Management Committee (RMC) is established by the Board of Directors. The RMC focuses on the effectiveness and appropriateness of the internal risk management strategy, risk management framework and risk controls (collectively the Enterprise Risk Management).

The RMC comprises members of the Board of Directors and senior management. Its key aims, with the Risk Management Division (RMD), are to:

a) Review and assess the Enterprise Risk Management governance structure;

b) Review the Risk Management framework (encompassing risk assessment guidelines and policies regarding Credit, Market, Liquidity, Interest Rate, and Operational risk management);

c) Oversee policies and guidelines for determining the macro Enterprise Risk Limit levels, and review the utilization of these limits;

d) Review the adequacy of GICs' capital allocations including economic and regulatory, incorporating the risk adjusted return on capital;

e) Review and assess the integrity and adequacy of the Risk Management Division of the Corporation; and

f) Receive and review reports on selected risk topics as management deems appropriate from time to time.

The RMC, senior management, risk officers, and line managers contribute to effective Enterprise-wide Risk Management. The RMC defines its expectations, and through its oversight determines its accomplishment. The Board of Directors has ultimate responsibility for risk management as they set the tone and other components of an enterprise risk management.

Risk officers have the responsibility for monitoring progress and for assisting line managers in reporting relevant risk information and the line managers are directly responsible for all business risk generated in their respective domains. The effective relationship between these parties significantly contributes to the improvement in the Corporation's overall risk management practices as this leads to the timely identification of risk and facilitation of appropriate response.

The RMD structure has a distinct identity and independence from business units. The RMD ensures that risk exposures remain within tolerable levels relative to the Corporation's capital and financial position. The RMD reports directly to the Chief Executive Officer, and is manned by dedicated risk specialists in all disciplines to address the pertinent business risks exposure of the Corporation. Its main responsibilities are to:

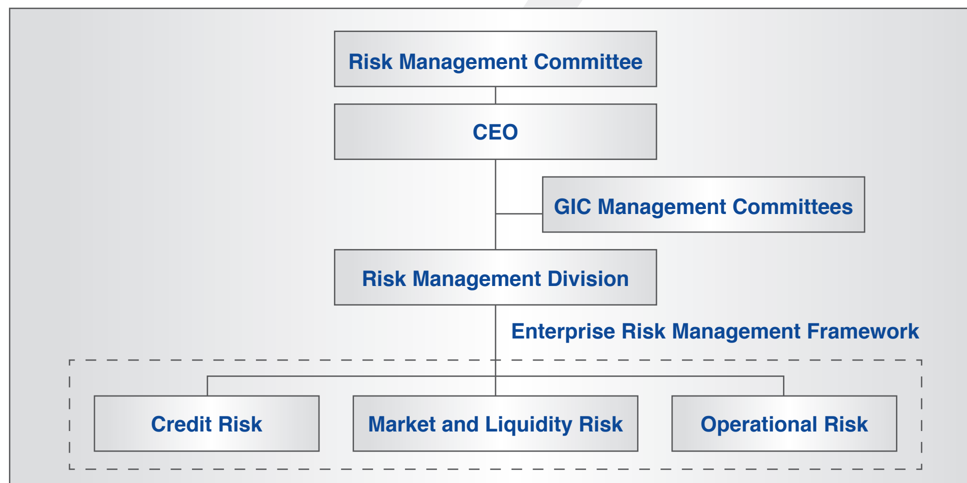
a) Evaluate and analyze the enterprise wide risk profile by developing risk monitoring techniques;

b) Set up and develop criteria for defining the Corporation's risk threshold in terms of various risks;

c) Develop and establish tools for the measurement of the Corporation's various risk types; and

d) Recommend appropriate strategies/actions for mitigating risk and ensuring a sound risk asset structure for the Corporation.

The abridged organizational structure of GIC's risk management structure is shown below:



The following management committees have the responsibility and authority for the day-to-day risk management activities of the Corporation, and where by such authorities are being exercised within the objectives and policies approved by the RMC:

a) Management Committee covers mainly general management issues including performance review vis-à-vis budget, and assessment of status quo against strategic business plan;

b) Global Markets Group Investment Committee translates investment strategy directions into asset allocation guidelines, recommends investment proposals, and reviews investment portfolios. The committee also functions as a surrogate Asset-Liability Committee;

c) Principle Investing Investment Committee evaluates proposals for investments and divestiture of assets and ensures compliance to investment criteria as well as investment procedures at each phase of the investment process;

d) Human Resource Committee which reviews strategic HR issues;

e) Systems Steering Committee provides the forum to review the IT architecture and its condition to meet current and future business requirements; and

f) Provisioning Committee ensures that all provisioning activity (making or writing back provisions), covering all of GIC's on and off balance sheet items.

The objectives and policies for measurement and reporting of the major risk areas, i.e., Credit, Market, Liquidity and Operational, are detailed in the Risk Management section. The same section includes the approach adopted by the Corporation towards management and mitigation of these risks.

4. Credit Risk Exposure

The Corporation follows both qualitative and quantitative approaches to credit risk management. These approaches are clearly articulated in the Corporation's Credit Policy document which aims to promote a strong credit risk management architecture that includes credit procedures and processes. The policy defines the areas and scope of investment activities undertaken by the Corporation and its main goal is not simply to avoid losses, but to ensure achievement of targeted financial results with a high degree of reliability. The Corporation's credit risk management focuses on the dynamic and interactive relationship between three credit process phases: portfolio strategy and planning, investment origination and maintenance, and performance assessment and reporting. Each of these phases is discussed briefly below.

Portfolio Strategy and Planning

The overall desired financial results, the portfolio strategy of each business unit, and the credit standards required to achieve the targets are defined during the planning phase. The business strategies are developed in such a way that they integrate risk and that they meet the defined hurdles in terms of RORAC. Portfolio management establishes composition targets, monitors the results of these diverse business strategies on a continual basis, and allows the Corporation to manage concentrations that can result from seemingly unrelated activities. Specifically, portfolio management involves setting concentration limits by standard dimensions so that no one category of assets or dimension of risk can materially harm the overall performance of the Corporation. The Board has set specific limits for individual borrowers and groups of borrowers and for geographical and industry segments. These limits consider the individual credit of the various counterparties as well as the overall portfolio risk.

The Investment Committees

The Committees monitor and approve investment proposals and review portfolio concentrations in terms of economic sectors and asset class. These limits are reviewed annually to ensure that there are no undue concentrations in one sector or asset class, and that the limits are within those set out by the Corporation. For counter-party limits, such as limits for banks and financial institutions, credit line approval follows a strict process of credit review, with proper authority levels delegated to senior credit officers. Foreign exchange trading and interest rate gap limits, together with ancillary limits (e.g., daylight, overnight, stop loss, etc.) are recommended by Treasury for the review of risk management, and eventual approval by the RMC. The RMD quantifies the Corporation's credit risk appetite in line with the overall strategy. The RMD employs a process of allocating capital on a portfolio level for the total credit exposure assumed by each business unit. The business units' actual capital consumption is assessed against the budget, and variances are appropriately reported to senior management.

Investment Origination and Maintenance

The business units solicit, evaluate, and manage credit exposure according to the strategies and portfolio parameters established during the portfolio strategy and planning phase. Investments are generated within well- defined criteria, product structure, and are approved on the basis of risk and return assessment. The processes involved under credit maintenance include documentation review and disbursement, and review of the status of exposures. Within this phase, origination and underwriting for distribution to investors takes place. The business units remain the sponsor and main risk managers of their proposals. While the risk management team independently reviews investment/product proposals prior to granting approvals to ensure that the proposals are within the tolerable risk appetite of the Corporation and are consistent with its policy, prior to disbursement of funds.

Performance Assessment and Reporting

The performance assessment and reporting phase allow both the senior management and business units to monitor results and improve performance continually. Both portfolio and process trends are monitored in order to make appropriate and timely adjustments to business strategies, portfolio parameters, credit policies and investment origination and maintenance practices. This phase of the credit process draws on information within the Corporation and external benchmarks to help evaluate performance. The goal of performance assessment is to achieve a balanced portfolio of assets, well diversified, and generating returns consistent with targets. Credit performance is assessed through analysis of:

a) Portfolio concentrations by obligor, industry, risk rating, maturity, asset class, as well as other dimensions;

b) Generated Return On Capital Employed (ROCE);

c) Additional economic value created by individual projects;

d) Exceptions to risk acceptance criteria; and

e) Other policy exceptions.

Inherent in the Corporation's business activity is the presence of 'portfolio risk', which arises whenever there is high positive correlation between individual credit portfolios. To address this particular risk, the Corporation employs the 'Credit Manager' system promoted by the Risk Metrics Inc. (part of MSCI). The system is a quantitative based program where overall portfolio 'Credit Value at Risk' (CreditVaR) is measured and controlled. This model calculates CreditVaR based on credit ratings of the names, default probabilities, loss given default, current market prices of the credits, while considering the impact of correlation of the various credits in the portfolio. In order to institute a common language for understanding and dimensioning credit risk across GIC's range of investments in projects, RMD is in the process of developing an Internal Credit Risk Rating (ICRR) model that would assist management in determining level of capital allocation and other strategic schemes applicable to the investment credit rating. Naturally, the model will also be used to benchmark the required return given a particular level of risk. Additionally, the rating results will subsequently be used as valuable inputs into the 'Credit Manager' system mentioned above.

Credit Risk as per Basel III Standardized Approach

Under the credit risk 'Standardized' approach, credit exposures are categorized to standard portfolios that are subject to a distinctive risk-weighting scale based on standard characteristics of the nature of borrower as well as the external credit assessments of international rating agencies where available. GIC uses the credit ratings assigned by Moody's and Fitch for this purpose. When more than one counter-party rating is available, Basel III's multiple assessment guidelines are invoked. In order to provide a common platform into which different notations used by the aforementioned rating agencies can be mapped, a scale of uniform Credit Quality Grades (CQG) represented by the numerals 1 to 5 or 6 are used to represent the relevant risk weights of each standard portfolio. Separate scales are prepared for risk-weighting both long and short-term issues.

Table 4: CQG Mapping

Corporates Credit Quality Grades	Moody's	Fitch
1	Aaa	AAA
	Aa1	AA+
	Aa2	AA
	Aa3	AA-
2	A1	A+
	A2	A
	A3	A-
3	Baa1	BBB+
	Baa2	BBB
	Baa3	BBB-
4	Ba1	BB+
	Ba2	BB
	Ba3	BB-
5	B1	B+
	B2	B
	B3	B-
6	Caa1	CCC+
	Caa2	CCC
	Caa3	CCC-
	Ca	CC
	C	C
		D

Table 4: serves as a sample of mapping notations of rating agencies into CQGs for claims on Corporates. At 31 December 2017, rated credit exposures accounted for about 16% of total credit exposures. Note that the numbers are after applying the equivalent risk- weights (credit conversion) as provided under the Basel III accord. Meanwhile, gross credit exposure to rated assets was recorded at approximately 27% of total gross credit exposure. Assets that are rated single 'A' or better comprised 49% of rated gross credit exposure.

Table 5: Credit Exposure (post-credit conversion)

	31 December 2017		
In US$ millions	**Rated**	**Unrated**	**Total**
Claims on Sovereigns	211.1	-	211.1
Claims on Public Sector Entities	99.0	-	99.0
Claims on Banks	222.5	-	222.5
Claims on Corporate	156.2	-	156.2
Securitization and SIVs	9.1	-	9.1
Venture Capital and Private Equity	-	119.7	119.7
Investments in Commercial Entities	-	3,253.5	3,253.5
Other Funds and Quoted Equities	-	192.6	192.6
Other Assets	-	119.8	119.8
Total	697.9	3,685.6	4,383.5
In Percent	15.9%	84.1%	100.0%

Table 6: Gross Credit Exposure (pre-credit conversion)

	31 December 2017		
In US$ millions	**Rated**	**Unrated**	**Total**
Claims on Sovereigns	354.7	-	354.7
Claims on Public Sector Entities	194.0	-	194.0
Claims on Banks	611.7	-	611.7
Claims on Corporate	208.6	-	208.6
Securitization and SIVs	17.7	-	17.7
Venture Capital and Private Equity	-	119.7	119.7
Investments in Commercial Entities	-	3,253.5	3,253.5
Other Funds and Quoted Equities	-	192.6	192.6
Other Assets	-	119.7	119.7
Total	1,386.7	3,685.5	5,072.2
In Percent	27.3%	72.7%	100.0%

Tables 5 and 6 present the breakdown of credit exposures pre and post-credit conversion.

Table 7: Gross Credit Exposure before Credit Risk Mitigation (CRM)

	31 December 2017		
In US$ millions	**Funded**	**Unfunded**	**Total**
Claims on Sovereigns	354.7	-	354.7
Claims on Public Sector Entities	194.0	-	194.0
Claims on Banks	601.3	10.4	611.7
Claims on Corporate	208.6	-	208.6
Securitization and SIVs	17.7	-	17.7
Venture Capital and Private Equity	87.9	31.8	119.7
Investments in Commercial Entities	3,026.8	226.7	3,253.5
Other Funds and Quoted Equities	192.6	-	192.6
Other Assets	119.7	-	119.7
Total	4,803.3	268.9	5,072.2
In Percent	94.7%	5.3%	100.0%

In terms of facility type (Table 7), US$ 4,803.3 million or approximately 95% is funded. The balance is ascribed to guarantees issued and commitments made by the Corporation, as well as credit exposures on outstanding forward and swap transactions with banks.

Table 8: Gross Credit Exposure by Geographic Distribution

	31 December 2017				
In US$ millions	**GCC**	**Europe**	**Americas**	**Others**	**Total**
Claims on Sovereigns	323.2	-	-	31.5	354.7
Claims on Public Sector Entities	190.9	-	3.1	-	194.0
Claims on Banks	526.7	53.8	10.4	20.8	611.7
Claims on Corporate	153.5	16.4	20.0	18.7	208.6
Securitization and SIVs	-	13.7	4.0	-	17.7
Venture Capital and Private Equity	12.0	12.0	83.8	11.9	119.7
Investments in Commercial Entities	3,233.5	-	20.0	-	3,253.5
Other Funds and Quoted Equities	85.4	49.8	57.4	-	192.6
Other Assets	83.8	12.0	-	23.9	119.7
Total	4,609.0	157.7	198.7	106.8	5,072.2
In Percent	90.9%	3.1%	3.9%	2.1%	100.0%

The geographical distribution (Table 8) is based on either the primary purpose of the exposure or the place of incorporation of the debt security issuer, or incorporation of the fund manager. A sizable portion of credit exposure is in the GCC region tallying at US$ 4,609.0 million or 90.9% of the total. Following suit are exposures to Americas and Europe, 3.9% and 3.1% respectively. These exposures are due in great part to investments in global securities and funds with varying investment themes.

Table 9: Gross Credit Exposure by Industry Sector

	31 December 2017					
In US$ millions	**Banks & Financial Institutions**	**Trading & Manufacturing**	**Energy &Utilities**	**Government Agencies**	**Others**	**Total**
Claims on Sovereigns	-	-	-	354.7	-	354.7
Claims on Public Sector Entities	56.3	24.3	113.4	-	-	194.0
Claims on Banks	611.7	-	-	-	-	611.7
Claims on Corporate	-	6.9	98.9	-	102.8	208.6
Securitization and SIVs	17.7	-	-	-	-	17.7
Venture Capital and Private Equity	119.7	-	-	-	-	119.7
Investments in Commercial Entities	77.8	2,366.6	680.8	-	128.3	3,253.5
Other Funds and Quoted Equities	192.6	-	-	-	-	192.6
Other Assets	58.7	49.1	3.6	2.4	5.9	119.7
Total	1,134.5	2,446.9	896.7	357.1	237.0	5,072.2
In Percent	22.4%	48.2%	17.7%	7.0%	4.7%	100.0%

The table on industry distribution (Table 9) of the gross credit exposure reveals a concentration on Trading & Manufacturing sector and Energy & Utilities, amounting to 65.9% of total exposure which, is in line with GIC's commitment to support the industrial growth within the GCC region.

Table 10: Credit Exposure by Residual Contractual Maturity

	31 December 2017				
In US$ millions	**Within 3 months**	**3 months to 1 year**	**1 to 5 years**	**Over 5 years**	**Total**
Claims on Sovereigns	-	10.2	187.5	157.0	354.7
Claims on Public Sector Entities	-	-	122.7	71.3	194.0
Claims on Banks	289.5	118.1	185.2	18.9	611.7
Claims on Corporate	15.5	32.3	87.4	73.4	208.6
Securitization and SIVs	-	-	2.0	15.7	17.7
Venture Capital and Private Equity	-	-	-	119.7	119.7
Investments in Commercial Entities	-	-	-	3,253.5	3,253.5
Other Funds and Quoted Equities	-	-	-	192.6	192.6
Other Assets	18.3	11.8	36.3	53.3	119.7
Total	323.3	172.4	621.1	3,955.4	5,072.2
In Percent	6.4%	3.4%	12.2%	78.0%	100.0%

The residual maturity of gross credit exposure broken down by standard credit risk exposure is shown in Table 10. Approximately 78% of gross credit exposure falls within the longest time bucket of over five years.

Recognition of Impairment of Assets

The Corporation assesses at each balance sheet date whether there is any objective evidence that a financial asset is impaired. Investments are treated as impaired when there has been a significant or prolonged decline in the fair value below its cost or where other objective evidence of impairment exists. The determination of what is 'significant' or 'prolonged' requires considerable judgment. In addition, the Corporation evaluates other factors, including normal volatility in share price for quoted equities and the future cash flows and the discount factors for projects and unquoted equities. The Corporation reviews its problem loans and advances, and investment in debt instruments at each reporting date to assess whether a provision for impairment should be recorded in the statement of income. In particular, considerable judgment by management is required in the estimation of the amount and timing of future cash flows when determining the level of provisions required. Such estimates are necessarily based on assumptions about several factors involving varying degrees of judgment and uncertainty, and actual results may differ resulting in future changes to such provisions. Noteworthy, the Corporation has taken a strategic decision to wind down its lending activities. An insignificant amount of impaired assets stemming from project loan provided to a manufacturing company based in the GCC has been fully provided for.

5. Securitization Activities

The Corporation's securitization exposure comes by way of its investments in structured products, which can be generally classified under synthetic securitization. Capital cover treatment of securitization exposures follows the 'Ratings Based' approach as recommended in the Basel III capital adequacy guidelines. As such, the external credit assessments provided by Moody's is considered when determining credit risk weights for securitization exposures.

Table 11: Credit Exposure on Securitization and SIVs

	31 December 2017	
In US$ millions	**Gross Exposure**	**Post-credit Conversion**
CQG 1	11.7	2.3
CQG 2	3.4	1.7
CQG 3	-	-
CQG 4	1.4	5.1
CQG 5	-	(deduction from capital)
CQG 6	-	
Unrated	-	
Total	17.7	9.1

Table 11 provides the credit rating breakdown of the Corporation's investment in securitization and structured investment vehicles (SIVs): Exposures that are rated CQG 5 and lower are deducted directly from regulatory capital.

6. Market Risk

This section focuses regulatory capital adequacy computations based on the VaR measurement for the 'Trading' book. More details on VaR and Market Risk monitoring are provided in the Risk Management section of the annual report. The regulatory capital adequacy ratios are computed under Basel III. GIC follows the Internal Models Approach (IMA) to quantify the capital charge associated with market risk within the trading portfolio.

The Corporation uses the 'Risk Manager' system, developed by MSCI Risk Metrics, and utilizes a parametric computational method based on the variance - covariance concept. In line with the capital accord, the parameters used in determining the VaR are a 10 day holding period and 99% confidence level. The computation utilizes an equally weighted historical data set going back one year. The computation ignores the correlation benefit amongst the three risk types (interest rate, equity and foreign exchange), with Total Market Risk VaR being equal to the arithmetic sum of the three components. The capital charge relating to market risk is determined for all portfolios categorized as trading (the trading book), which includes the following (Ref Notes 4 of 2017 consolidated financial statements):

(US$ million)	**2017**	**2016**
Quoted debt instruments	49	29
Hedge and Other unquoted alternative funds	340	425
	389	454

Policies relating to recognition, classification, fair value measurement and gain/loss computation are detailed in Note 2 of consolidated financial statements. GIC believes that it is prudent to provide an explicit capital cushion for price risks to which it is exposed. Such risk of loss arising from the adverse changes in market variables is predominantly within the trading book. Within the Corporation, capital charge for market risk comprises three main categories: interest rate risk and equity risk (within the trading book) and foreign exchange risk for the entire Corporation.

The Value-at-Risk concept is a sound basis for the quantification of market risk, and the variance-co-variance methodology adequately suits the Corporation's asset types. Most of the exposures within the trading book entail very little optionality and are mostly linear in nature. The VaR based system provides a dynamic measure of market risk capturing, in a timely manner, the impact of changes in environment on the value of the portfolio of financial instruments. The VaR model is a statistical tool, based on simplifying assumptions, and as such has certain limitations (examples: occurrence of 'fat tails', non-normal distributions and event risks; the past not being a good approximation of future, etc). To a large extent, these limitations are addressed by the back-testing exercise and related multiplication factor used. For all the portfolios within the trading book, the same variance - co-variance methodology is used to compute VaR, which is computed on a daily basis as per the parameters described above.

Scenario analysis and stress testing is an essential component of the market risk management framework. The assumption of normality on which the statistical models are based may become invalid due to the occurrence of certain events.

Future scenarios, which result in a breakdown of the historical behavior and relationships between risk constituents, are projected, and potential loss amounts are determined. Most of these scenarios are derived from macroeconomic events of the past, modified with the expectations for the future.

Back-testing

The objective of 'Back-testing' is to measure/validate the accuracy of the internal VaR model. Back-testing essentially deals with the process of comparing actual trading results with the model generated risk measures (estimates). Back testing is conducted in line with the 'Supervisory Framework Document' issued by the Basel Committee. The parameters for back-testing are a one-day holding period and 99% confidence level. To the extent that the back-testing program is viewed purely as a statistical test of the integrity of the calculation of Value-at Risk (VaR) measure, the Corporation felt it appropriate to utilize the 'hypothetical portfolio' approach. In this approach, a static hypothetical model portfolio, with similar characteristics of the actual portfolio, is created and daily change in market value is computed based on actual price observations. VaR is also computed for this static portfolio using the model and comparisons are made between actual results and model estimates. The advantage of this method is that the value change outcomes are not 'contaminated' by changes in the portfolio (which could happen if the actual portfolio were used).

The multiplication factor of 3 is used for capital calculation, in line with the Basel guidelines. Capital charge for market risk is determined based on the following formula:

Capital Charge (market risk) = (Max {Vavg,Vend} + Max {SVavg,SVend})X Mf

Where, Vavg equals: Average Total VaR for the trading book over the previous 60 business days

Vend equals: End of period Total VaR for the trading book

SVavg equals: Average Stressed VaR for the trading book over the previous 60 business days

SVend equals: End of period Stressed VaR for the trading book

Mf equals: Multiplication factor (a factor of three issued based on the results of back-testing)

Table 12: Trading Book VaR (US$ 000's) - 10 day holding period, 99% confidence level. For the last 60 business days in 2017

In US$ millions	Interest Rate	Equity	FX	Total
Max	1.3	5.0	0.3	6.6
Min	0.4	2.6	0.0	3.0
Average	1.0	4.8	0.0	5.8
31-Dec-17	0.8	4.9	0.0	5.7
Stress VaR	4.8	19.0	0.0	23.8

7. Operational Risk

The Corporation currently adopts the' Standardized' approach in the estimation of regulatory capital to support potential operational risk exposure.

In keeping with the accord's guidelines, gross income for each business line is determined using the transfer pricing methodology being employed by the Corporation. The identified business lines as well as its major business segments are presented in Table 13.

Table 13: Business Lines for Operational Risk

Business lines	Major business segments	Activity Groups
Principal Investments	Investment and Equity Participation	Venture Capital, Greenfield Investments, Mergers and acquisitions, Privatizations, Equity Participation, IPOs, Secondary Private Placements
Debt Capital Markets	Investments of debt securities	International Corporate Securities, Sovereign Debts, GCC Issues/Bonds, Convertible Bonds, Islamic Bonds, ABSs,FRNs, SIVs, Structured Finance, Credit Funds, Emerging Market debts, High Yield Debt, Trading Bonds & Derivatives
Equity Investments	Portfolio of investments in equity funds and proprietary funds	Gulf Equities, Equity Portfolios
Alternative Investments	Portfolio of investments in an array of different asset classes and managed funds	Hedge Funds, Real Estate, Managed Funds, MBSs, Private Equity, Global Equity
Treasury	Sales	Fixed Income, Equity, Foreign Exchanges, Commodities, Credit, Funding, Own Position Securities, Lending and Repos, Derivatives
	Market Making	
	Proprietary Positions	
	Advisory Services	
Asset Management	Discretionary Fund Management	Pooled, Segregated, Retail, Institutional, Closed, Open
	Non-Discretionary Fund Management	Pooled, Segregated, Retail, Institution, Closed, Open
Head-quarters	Income classified for Head-quarters as per internal FTP (Fund Transfer Pricing) method, and other income that cannot be classified in any other business line	Income from Free Capital, Rental Income, Other Income, etc

Capital risk charge for each business line is computed and reported on a quarterly basis. The capital requirement for each business line and the corresponding capital charge are in Table 14.

Table 14: Operational Risk Capital Charge

	31 December 2017		
In US$ millions	**3 year Average Gross Income**	**Beta Factor**	**Capital Charge**
Principal Investment	94.0	18%	16.9
Debt Capital Market	56.0	18%	10.0
Equities Investments	10.6	18%	1.9
Alternative Investments	27.4	18%	4.9
Treasury	-	18%	-
Asset management	-	12%	-
Head-quarters	4.0	18%	0.8
Total	192.0		34.5
Risk-weighted exposure			431.9

The highest beta factor of 18% is applied on all business lines save for the 'Asset Management' business line, where a beta factor of 12% is used as suggested in the capital accord.

The Corporation realizes that the accord offers a continuum of approaches from the simplest basic indicator approach to the more advanced measurement approaches. In its endeavor to adopt a more risk-sensitive approach to operational risk capital management, the Corporation plans to implement a more disciplined 'bottom-up' method whereby the approach is anchored on objective loss data. To implement such an approach, a four-stage progression will be followed:

(1) Risk and Control Self-Assessment Framework;

(2) Loss Event Framework;

(3) Corrective Action Plans Framework; and

(4) Operational Risk Reporting Framework.

8. Equity Risk in the Banking Book

Equity investments in the banking book are classified at the time of acquisition into those acquired for realizing capital gains and to those purchased for strategic investments. The decision where to classify investments is arrived at after considering significant factors that include business and strategic advantages to the Corporation, and the amount of planned investments. All investment decisions require the approval of the Investment Committees, or the Executive Committee, depending on the amount of exposure. Investments acquired with a view to generating income and profits from capital appreciation are reviewed periodically and disposed of at opportune instances. Meanwhile, the strategic investment portfolios are reviewed based on the industry, market and economic developments, and the Corporation decides whether to liquidate or further consolidate its holdings in these investments. In accordance with International Financial Reporting Standards, equity positions in the banking book are classified as available for sale securities. These investments are fair valued periodically and revaluation gains/losses are accounted as cumulative changes in fair value in equity. Accounting treatment of equity investments can be found under 'Significant accounting judgments and estimates' in the notes to the consolidated financial statements.

Publicly traded investments represent quoted equities traded in the local and international stock exchanges. Privately held investments represent investments in unquoted entities and projects. The total value of equity investments in the banking book at the end of December 2017 is US$ 582.2 million, net of provision (refer to Table 15 below). Cumulative realized gain from sale or exchange of available for sale securities and projects is approximately US$ 53.3 million, of which a significant portion is from privately held equity holdings. Meanwhile, the total un-realized loss recorded in equity is US$ 23.2 million.

Table 15: Equity Holdings in Banking Book

	31 December 2017		
In US$ millions	**Publicly Traded**	**Privately Held**	**Total**
Fair Value of Equity Investments	365.1	217.1	582.2
Realized gains recorded in P/L	24.9	28.3	53.3
Unrealized gain/(loss) recorded in equity	(22.4)	(0.8)	(23.2)
Unrealized gain/(loss) in Tier 2 Capital	(22.4)	(0.8)	(23.2)

9. Interest Rate Risk in the Banking Book

Treasury manages short term interest rate gapping by means of monitoring overall interest rate exposure in the next 24 months as measured in Eurodollar futures contract equivalents. Treasury is not allowed to mismatch positions over two years unless appropriate management approval has been obtained. Any funding, placements or borrowing that has a maturity or re-pricing profile of more than two years are either matched or hedged. The rate calculated from short dated (up to two years) Eurodollar futures contract is effectively the forward interest rate of the underlying, i.e. Eurodollar deposits. Total USD placements and borrowings transacted by Treasury are profiled in time buckets from one week and then monthly thereafter until 24 months. The same procedure is applied to other currencies; the gaps on these currency positions are translated to USD equivalents in order to ascertain the equivalent number of Eurodollar futures contracts for the individual major currencies.

A maximum limit of 3,500 Eurodollar contracts is currently set, with the maximum VaR at US$ 3.08 million. The calculation of VaR equivalent is derived from the 30 day average price volatility of 3 month Eurodollar futures. The current yield is adjusted by the average volatility before it is applied on the position value. The resulting number is then scaled up to a 95% level of confidence.

The Eurodollar futures contract position value as at December 31, 2017 was 2,080 contracts, with an estimated VaR of US$ 0.6 million. This is higher than the levels of the previous year (31st December 2016: 1,846 contracts). This is excluding the impact of the fixed rate EMTN issuance.

10. Funding liquidity Assessment

The Basel committee as a foundation of its liquidity framework in 2008 published Principles for Sound Liquidity Risk Management and Supervision ("Sound Principles"). The Sound Principles provide detailed guidance on the risk management and supervision of funding liquidity risk and should help promote better risk management in this critical area, but only if there is full implementation by banks and supervisors. A key reform in developing a more resilient banking sector was the introduction of Liquidity Coverage Ratio (LCR)

Liquidity Coverage Ratio (LCR)

The objective of the LCR is to promote the short-term resilience of the liquidity risk profile of banks. It does this by ensuring that banks have an adequate stock of unencumbered high-quality liquid assets (HQLA) that can be converted easily and immediately in private markets into cash to meet their liquidity needs for a 30 calendar day liquidity stress scenario.

Against a prescribed minimum of 80%, GIC's LCR as of 31 December 2017 was 194%.

Table 16: Liquidity Coverage Ratio

In US$ millions	**31 December 2017**
Value of stock of High quality liquid assets (HQLA)	919.6
Total Net Cash outflow over the next 30 calendar days	473.9
Liquidity Coverage Ratio (LCR)	194%

CONSOLIDATED

FINANCIAL STATEMENTS

31 December 2017

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The Shareholders
Gulf Investment Corporation G.S.C.
State of Kuwait

Report on the Audit of the Consolidated Financial Statements

Opinion

We have audited the consolidated financial statements of Gulf Investment Corporation G.S.C. ("the Corporation") and its subsidiaries (together "the Group"), which comprise the consolidated statement of financial position as at 31 December 2017, the consolidated statements of income, other comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising significant accounting policies and other explanatory information.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2017, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards ("IFRS").

Basis for Opinion

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

Other Information

Management is responsible for the other information. The other information comprises the information included in the Group's annual report, but does not include the consolidated financial statements and our auditor's report thereon.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed on the other information obtained prior to the date of this auditor's report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of Management and Those Charged with Governance for the Consolidated Financial Statements

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

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

Those charged with governance are responsible for overseeing the Group's financial reporting process.

Auditor's Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISA 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 consolidated financial statements.

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

Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.

Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

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 Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.

Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance 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.

Report on Other Legal and Regulatory Requirements

We further report that we have obtained the information and explanations that we required for the purpose of our audit and the consolidated financial statements include the information required by the Corporation's Agreement of Incorporation and Articles of Association. In our opinion, proper books of account have been kept by the Corporation and an inventory count was carried out in accordance with recognized procedures and the accounting information given in the Board of Directors' report agrees with the books of accounts of the Corporation. We have not become aware of any violations of the provisions of the Corporation's Agreement of Incorporation and Articles of Association during the year ended 31 December 2017 that might have had a material effect on the business of the Corporation or on its consolidated financial position.

Safi A. Al-Mutawa
License No 138 "A"
of KPMG Safi Al-Mutawa & Partners
Member firm of KPMG International

Kuwait: 16 April 2018

Consolidated statement of financial position

as at 31 December 2017

(All amounts in US$ millions)

	Note	2017	2016
			(restated)
Assets			
Cash and cash equivalents		41	98
Placements with banks	3	232	281
Financial assets at fair value through statement of income	4	389	454
Financial assets available for sale	5	1,702	2,205
Investments in associates	6	1,590	1,253
Other assets	7	274	301
Total assets		**4,228**	4,592
Liabilities and equity			
Liabilities			
Deposits from banks and other financial institutions	8	571	570
Term finance	9	796	1,268
Other liabilities	10	214	228
Total liabilities		**1,581**	2,066
Equity			
Share capital	11	2,100	2,100
Reserves	11	504	486
Retained earnings / (accumulated losses)		43	(66)
Equity attributable to equity holders of the Corporation		**2,647**	2,520
Non-controlling interests		-	6
Total equity		**2,647**	2,526
Total liabilities and equity		**4,228**	4,592

The accompanying notes 1 to 28 form an integral part of these consolidated financial statements.

Shaikh Fahad Bin Faisal Al- Thani
Chairman

Ibrahim Ali AlQadhi
Chief Executive Officer

Consolidated Statement of Income

for the year ended 31 December 2017

(All amounts in US$ millions)

	Note	**2017**	2016
Interest income	12	56	58
Net gains from investments	13	82	75
Dividend income	14	12	12
Share of results of associates	6	131	32
Net fee, commission and other income	15	3	5
Total income		**284**	182
Interest expense	16	(49)	(57)
Other operating income	17	1	8
Net operating income		**236**	133
Staff costs		(37)	(37)
Premises costs		(3)	(2)
Other operating expenses		(15)	(15)
Impairment losses	18	(60)	(22)
Profit for the year		**121**	57
Attributable to:			
Equity holders of the Corporation		121	57
Non-controlling interests		-	-
		121	57

The accompanying notes 1 to 28 form an integral part of these consolidated financial statements.

Consolidated Statement of other Comprehensive Income

for the year ended 31 December 2017

(All amounts in US$ millions)

	Note	**2017**	2016
Profit for the year		**121**	57
Other comprehensive income that may be re-classified to consolidated statement of income in subsequent periods:			
Financial assets available for sale:			
- Net unrealised gain arising during the year		10	121
- Transferred to consolidated statement of income on sale	13	(60)	(42)
- Transferred to consolidated statement of income on impairment	18	31	8
Share of other comprehensive income of associates		25	18
Other comprehensive income for the year		**6**	105
Total comprehensive income for the year		**127**	162
Attributable to:			
Equity holders of the Corporation		127	162
Non-controlling interests		-	-
		127	162

The accompanying notes 1 to 28 form an integral part of these consolidated financial statements.

Consolidated Statement of Changes in Equity

for the year ended 31 December 2017

(All amounts in US$ millions)

		Reserves								
	Share capital	Compulsory reserve	Voluntary reserve	Investment revaluation reserve	Cash flow hedge reserve	Foreign currency translation reserve	(Accumulated losses)/ retained earnings	Total	Non-controlling interests	Total equity
Balance as at 1 January 2016 (audited)	2,100	394	236	24	(121)	(133)	(9)	2,491	6	2,497
IFRS adoption by an associate (note 6)	-	-	-	1	-	84	(112)	(27)	-	(27)
Balance as at 1 January 2016 (restated)	2,100	394	236	25	(121)	(49)	(121)	2,464	6	2,470
Profit for the year	-	-	-	-	-	-	57	57	-	57
Other comprehensive income / (loss)	-	-	-	103	11	(9)	-	105	-	105
Total comprehensive income	-	-	-	103	11	(9)	57	162	-	162
Transfer to reserves (note 11)	-	6	5	-	-	-	(11)	-	-	-
Transfer from voluntary reserve (note 11)	-	-	(9)	-	-	-	9	-	-	-
Dividend (note 11)	-	-	(105)	-	-	-	-	(105)	-	(105)
Accumulated rounding off adjustment	-	-	(2)	-	-	1	-	(1)	-	(1)
Balance as at 31 December 2016 (restated)	2,100	400	125	128	(110)	(57)	(66)	2,520	6	2,526
Balance as at 1 January 2017 (restated)	2,100	400	125	128	(110)	(57)	(66)	2,520	6	2,526
Profit for the year	-	-	-	-	-	-	121	121	-	121
Other comprehensive (loss) / income	-	-	-	(16)	12	10	-	6	-	6
Total comprehensive income	**-**	**-**	**-**	**(16)**	**12**	**10**	**121**	**127**	**-**	**127**
Transfer to reserves (note 11)	-	12	-	-	-	-	(12)	-	-	-
Net movement in minority interest	-	-	-	-	-	-	-	-	(6)	(6)
Balance as at 31 December 2017	**2,100**	**412**	**125**	**112**	**(98)**	**(47)**	**43**	**2,647**	**-**	**2,647**

The accompanying notes 1 to 28 form an integral part of these consolidated financial statements.

Consolidated Statement of Cash Flows

for the year ended 31 December 2017

(All amounts in US$ millions)

	Note	**2017**	2016
Cash flows from operating activities:			
Profit for the year		121	57
Non-cash and other adjustments to reconcile profit for the year to net cash flows:			
Impairment losses	18	60	22
Realised gain on financial assets available for sale	13	(60)	(42)
Realised gain on sale of subsidiary	13	-	(9)
Realised gain on sale of associates	13	-	(10)
Gain on bargain purchase of an associate	13	-	(16)
Share of results of associates	6	(131)	(32)
Amortisation of net discount / premium on debt securities		7	7
		(3)	(23)
Changes in operating assets and liabilities:			
Placements with banks		49	53
Securities purchased under resale agreement		-	112
Financial assets at fair value through statement of income		65	(19)
Financial assets available for sale		515	492
Deposits from banks and other financial institutions		1	(349)
Movement in other assets and other liabilities		1	(12)
Net cash flows generated from operating activities		**628**	254
Cash flows from investing activities:			
Proceeds from sale of a subsidiary		-	9
Dividends from associates		31	25
Proceeds from sale of investment in associates		-	51
Purchase of associates		(130)	-
Repayment of advances to associate		-	4
Additional contribution to associates		(86)	(138)
Net cash flows used in investing activities		**(185)**	(49)
Cash flows from financing activities:			
Decrease in securities sold under repurchase agreements		-	(321)
Term finance repaid		(500)	(329)
Term finance issued		-	609
Dividend paid	11	-	(105)
Net cash flows used in financing activities		**(500)**	(146)
Net change in cash and cash equivalents		(57)	59
Cash and cash equivalents at 1 January		98	39
Cash and cash equivalents at 31 December		**41**	98

The accompanying notes 1 to 28 form an integral part of these consolidated financial statements.

Notes to the Consolidated Financial Statements

for the year ended 31 December 2017

(All amounts in US$ millions)

1 Incorporation and activity

Gulf Investment Corporation G.S.C. ("the Corporation") is an investment company incorporated in the State of Kuwait on 15 November 1983 as a Gulf shareholding company. It is equally owned by the governments of the six member states of the Gulf Co-operation Council ("GCC") – Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates. The Corporation is engaged in various investing and financing activities including investment advisory and asset management services.

The Corporation is domiciled in Kuwait and its registered office is at Jaber Al Mubarak Street, Al Sharq, State of Kuwait.

The consolidated financial statements of the Corporation and its subsidiaries (collectively "the Group") for the year ended 31 December 2017 were approved by the Board of Directors on 8 March 2018. The Annual General Assembly of shareholders has the power to amend these consolidated financial statements after issuance.

The Corporation's Agreement of Incorporation and Articles of Association gives it a special, supranational status. In particular, Article 8 of GIC's Agreement of Incorporation provides that local laws in each GCC state complement the provisions of GIC's Agreement of Incorporation and Articles of Association provided that such laws do not conflict with GIC's Agreement of Incorporation or Articles of Association. To the extent there is such a conflict, GIC's Agreement of Incorporation and Articles of Association prevail over local laws, including the Kuwait Companies Law.

2 Significant accounting policies

2.1 Statement of compliance

The consolidated financial statements of the Group have been prepared in accordance with the International Financial Reporting Standards ("IFRS") promulgated by the International Accounting Standards Board ("IASB"), interpretations issued by the International Financial Reporting Committee of the IASB. In addition, the consolidated financial statements have been prepared in accordance with the Corporation's Agreement of Incorporation and Articles of Association.

2.2 Basis of preparation

The consolidated financial statements are prepared on a historical cost basis modified for the revaluation of the fair value of financial assets at fair value through statement of income, financial assets available for sale, derivative financial instruments and financial assets / liabilities carried at amortised cost which are part of effective fair value hedging relationships to the extent of risk being hedged.

The consolidated financial statements are presented in United States Dollars, rounded to the nearest million.

Changes in accounting policy and disclosures

The accounting policies used in the preparation of these consolidated financial statements are consistent with those used in previous year, except for the following new and amended IFRS effective as of 1 January 2017.

A number of new standards and amendments to standards are effective for annual periods beginning after 1 January 2017, and have been applied in preparing these financial statements. The new amendments relevant to the Corporation are discussed below:

- Disclosure initiatives (Amendments to IAS 7)
- Annual improvements to IFRSs 2014-2016 cycle-various standards

The implementation of new and amended IFRS did not have a significant impact on the Group's consolidated financial statements.

2.3 Basis of consolidation

The consolidated financial statements comprise the financial statements of the Corporation and its subsidiaries including special purpose entities. Specifically, the Group controls an investee if, and only if, the Group has:

- Power over the investee (i.e. existing rights that give it the current ability to direct the relevant activities of the investee);
- Exposure, or rights, to variable returns from its involvement with the investee, and;
- The ability to use its power over the investee to affect its returns.

Notes to the Consolidated Financial Statements

for the year ended 31 December 2017

(All amounts in US$ millions)

2 Significant accounting policies (continued)

2.3 Basis of consolidation (continued)

When the Group has less than a majority of the voting or similar rights of an investee, the Group considers all relevant facts and circumstances in assessing whether it has power over an investee, including:

- The contractual arrangement with the other vote holders of the investee;
- Rights arising from other contractual arrangements;
- The Group's voting rights and potential voting rights.

The Group re-assesses whether or not it controls an investee, if facts and circumstances indicate that there are changes to one or more of the three elements of control.

Consolidation of a subsidiary begins when the Group obtains control over the subsidiary and ceases when the Group loses control of the subsidiary. Assets, liabilities, income and expenses of a subsidiary acquired or disposed off during the year are included in the consolidated financial statements from the date the Group gains control till the date the Group ceases to control the subsidiary.

Profit or loss and each component of other comprehensive income are attributed to the equity holders of the Corporation and to the non-controlling interests, even if this results in the non-controlling interests having a deficit balance. When necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with the Group's accounting policies. All intra-group assets and liabilities, equity, income, expenses and cash flows relating to transactions between members of the Group are eliminated in full on consolidation.

A change in the ownership interest of a subsidiary, without a loss of control, is accounted for as an equity transaction. If the Group loses control over a subsidiary, it:

- Derecognises the assets (including goodwill) and liabilities of the subsidiary;
- Derecognises the carrying amount of any non-controlling interests;
- Derecognises the cumulative translation differences recorded in equity;
- Recognises the fair value of the consideration received;
- Recognises the fair value of any investment retained;
- Recognises any surplus or deficit in consolidated statement of income;and
- Reclassifies its share of components previously recognised in other comprehensive income to profit or loss or retained earnings, as appropriate, as would be required if the Group had directly disposed of the related assets or liabilities.

2.4 Business combination and goodwill

Business combinations are accounted for using the acquisition accounting method. The cost of an acquisition is measured as the aggregate of the consideration transferred, measured at acquisition date fair value and the amount of any non-controlling interest in the acquiree. For each business combination, the acquirer measures the non-controlling interest in the acquiree either at fair value or at the proportionate share of the acquiree's identifiable net assets. Acquisition costs incurred are expensed and included in the consolidated statement of income.

When the Group acquires a business, it assesses the financial assets and liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic circumstances and pertinent conditions as at the acquisition date. This includes the separation of embedded derivatives in host contracts by the acquiree.

If the business combination is achieved in stages, the acquisition date fair value of the acquirer's previously held equity interest in the acquiree is remeasured to fair value at the acquisition date through the consolidated statement of income.

Any contingent consideration to be transferred by the acquirer will be recognised at fair value at the acquisition date. Subsequent changes to the fair value of the contingent consideration which is deemed to be an asset or liability, will be recognised in accordance with IAS 39 either in statement of income or as a change to other comprehensive income. If the contingent consideration is classified as equity, it should not be remeasured until it is finally settled within equity.

Notes to the Consolidated Financial Statements

for the year ended 31 December 2017

(All amounts in US$ millions)

2 Significant accounting policies (continued)

2.4 Business combination and goodwill (continued)

Goodwill is initially measured at cost being the excess of the cost of the business combination over the Group's share in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the consolidated statement of income.

After initial recognition, goodwill is measured at cost less any accumulated impairment losses. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash-generating units that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units.

Where goodwill forms part of a cash-generating unit (group of cash generating units) and part of the operations within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash generation unit retained.

2.5 Cash and cash equivalents

Cash and cash equivalents comprise of cash and balances with banks and financial institutions, balances with central banks and placements with banks and other financial institutions maturing within seven days.

2.6 Placements with banks

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

2.7 Financial assets

i. Recognition

Regular way purchases and sales of financial assets are recognised on trade date, the date on which the Group commits to purchase and sell the assets. Regular-way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame generally established by regulation or convention in the market place.

Financial assets are recognised initially at fair value plus, in the case of financial assets other than fair value through statement of income, directly attributable transaction costs.

The Group's financial assets include quoted and unquoted financial instruments, other assets and derivative financial instruments.

ii. Classification and measurement

The classification of financial assets is determined by the Group at initial recognition depending upon the purpose for which the financial assets were acquired and their characteristics.

Financial assets at fair value through statement of income includes financial assets held for trading and financial assets designated upon initial recognition at fair value through statement of income.

Financial assets are classified as held for trading if they are acquired for the purpose of selling in the near term or principally held for the purpose of short-term profit taking. Derivatives are classified as held for trading unless they are designated as effective hedging instruments.

The Group designates an investment as at fair value through statement of income in the following cases:

- The designation eliminates or significantly reduces the inconsistent treatment that would otherwise arise from measuring the assets or liabilities or recognising gains or losses on them on a different basis; or
- When the assets and liabilities are part of a group of financial assets which are managed and their performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy.

Notes to the Consolidated Financial Statements

for the year ended 31 December 2017

(All amounts in US$ millions)

2 Significant accounting policies (continued)

2.7 Financial assets (continued)

ii. Classification and measurement (continued)

After initial recognition financial assets at fair value through statement of income are remeasured at fair value with all changes in fair value recognised in the consolidated statement of income.

Financial assets held to maturity are financial assets with fixed or determinable payments and fixed maturity that the Group has the intention and ability to hold to maturity. Held to maturity investments are measured at amortised cost, less provision for impairment in value, if any. The losses arising from impairment of such investments are recognised in the consolidated statement of income.

Loans and receivables are non-derivative financial assets with fixed or determinable payments other than those financial assets acquired with the intention of short-term profit taking or financial assets quoted in an active market. Loans and receivables are stated at amortised cost using the effective interest method less any amounts written off and provision for impairment. The calculation takes into account any premium or discount on acquisition and includes transaction costs and fees that are an integral part of the effective interest rate.

Financial assets available for sale are those non-derivative financial assets that are designated as available-for-sale or are not classified in any of the preceding categories.

After initial measurement, financial assets available for sale are subsequently measured at fair value with gains or losses being recognised in other comprehensive income in the investment revaluation reserve until the investment is derecognised or the investment is determined to be impaired, at which time the cumulative gain or loss is recognised in the consolidated statement of income. Investments whose fair value cannot be reliably measured are carried at cost less impairment losses, if any.

The Group evaluates whether its ability and intention to sell its financial assets available for sale in the near term is still appropriate. When the Group is unable to trade these financial assets due to inactive markets and/or the management's intent significantly changes to do so in the foreseeable future, the Group may elect to reclassify these financial assets in rare circumstances.

Derivatives include interest rate swaps, futures, cross currency swaps, forward exchange contracts and options on interest rates and foreign currencies. Derivatives are recorded at fair value and carried as assets when their fair value is positive and as liability when their fair value is negative. Changes in fair value of derivatives held for trading are recognised in the consolidated statement of income.

iii. Impairment

The Group assesses at each reporting date whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred 'loss event') and that loss event has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that the debtors or a group of debtors is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganisation and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

Financial assets carried at amortised cost

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

If there is objective evidence that an impairment loss has 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 present value of the estimated future cash flows is discounted at the financial asset original effective interest rate. If a financial asset has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate.

Notes to the Consolidated Financial Statements

for the year ended 31 December 2017

(All amounts in US$ millions)

2 Significant accounting policies (continued)

2.7 Financial assets (continued)

iii. Impairment (continued)

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 consolidated statement of income. 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.

Financial assets available for sale

For financial assets available for sale, the Group assesses at each reporting date whether there is objective evidence that an investment or a group of investments is impaired.

In the case of equity investments classified as available for sale, objective evidence would include a significant or prolonged decline in the fair value of the investment below its cost. 'Significant' is to be evaluated against the original cost of the investment and 'prolonged' against the period in which the fair value has been below its original cost. Where there is evidence of impairment, the cumulative loss (measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognised in the consolidated statement of income) is removed from other comprehensive income and recognised in the consolidated statement of income. Impairment losses on equity investments are not reversed through the consolidated statement of income. Any increase in fair value after impairment is recognised directly in other comprehensive income.

In the case of debt instruments classified as available for sale, impairment is assessed based on the same criteria as financial assets carried at amortised cost. Subsequent increase in fair value of a debt instrument which is objectively related to an event occurring after the impairment loss was recognised, is credited to the consolidated statement of income.

iv. Derecognition

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; or
- The Group 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 Group has transferred substantially all the risks and rewards of the asset, or (b) the Group has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

When the Group 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 Group's continuing involvement in the asset.

In that case, the Group also recognises an associated liability. The transferred asset and the associated liability are measured on a basis that reflects the rights and obligations that the Group 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 Group could be required to repay.

2.8 Financial liabilities

i. Recognition

Financial liabilities are classified as financial liabilities at fair value through statement of income or loans and borrowings, as appropriate. The Group determines the classification of its financial liabilities at initial recognition.

Financial liabilities are recognised initially at fair value and, in the case of term finance, including directly attributable transaction costs.

The Group's financial liabilities include debt issued, other borrowings and accounts payable and accruals.

Notes to the Consolidated Financial Statements

for the year ended 31 December 2017

(All amounts in US$ millions)

2 Significant accounting policies (continued)

2.8 Financial liabilities (continued)

ii. Classification and measurement

The measurement of financial liabilities depends on their classification as follows:

Loans and borrowings

After initial measurement, all non-trading financial liabilities, debt issued and other borrowings are subsequently measured at amortised cost using the effective interest rate method. Amortised cost is calculated by taking into account any discount or premium on the issue and fees that are an integral part of the effective interest rate.

Accounts payable and accruals

Liabilities are recognised for amounts to be paid in the future for goods or services received, whether billed by the supplier or not.

Deposits from banks and financial institutions

Deposits from banks and financial institutions are stated at amortised cost using the effective interest method.

Term finance

Term finance is initially recognised at fair value of consideration received less directly attributable transaction costs. After initial recognition, interest bearing loans and borrowings are subsequently measured at amortised cost using the effective interest rate method.

Financial guarantees

The Group gives financial guarantees on behalf of its subsidiaries and associates. These guarantees are initially recognised in the consolidated financial statements at fair value on the date the guarantee is given, being the premium received. Subsequently, the Group recognises its liability under each guarantee at the higher of the amortised premium and the best estimate of expenditure required to settle any financial obligation arising as a result of the guarantee. Any increase in the liability is recognised in the consolidated statement of income. The Group recognises the premium received in the consolidated statement of income on a straight line basis over the life of the guarantee.

iii. Derecognition

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, and the difference in the respective carrying amounts is recognised in the consolidated statement of income.

2.9 Offsetting

Financial assets and liabilities are offset and the net amount is reported in the consolidated statement of financial position if, and only if, there is a currently enforceable legal 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 liabilities simultaneously.

2.10 Fair value of financial instruments

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.

The principal or the most advantageous market must be accessible to by the Group.

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.

Notes to the Consolidated Financial Statements

for the year ended 31 December 2017

(All amounts in US$ millions)

2 Significant accounting policies (continued)

2.10 Fair value of financial instruments (continued)

For investments and derivatives traded in organised financial markets, fair value is determined by reference to quoted market bid prices at the close of business on the reporting date. The fair value of mutual fund investments, unit trusts or similar investment vehicles is based on the last reported net asset values from the fund managers.

For investments where there is no quoted market price, a reasonable estimate of the fair value is determined by using valuation techniques such as recent arm's length transactions, reference to the current fair value of another instrument that is substantially the same, an earnings multiple, or is based on the expected cash flows of the investment discounted at current rates applicable for items with similar terms and risk characteristics. Fair value estimates take into account liquidity constraints and assessment for any impairment.

The Group 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.

Investments with no reliable measure of their fair values and for which no fair value information could be obtained are carried at their initial cost less impairment in value.

The fair value of interest bearing financial instruments is estimated based on discounted cash flows using interest rates for items with similar terms and risks characteristics.

An analysis of fair value of financial instruments and further details as to how they are measured are set out in note 24.

2.11 Impairment of non-financial assets

The Group assesses at each reporting date whether there is an indication that a non-financial asset may be impaired. If any such indication exists, or when annual impairment testing for an asset is required, the Group estimates the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or cash-generating unit's (CGU) fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets. Where the carrying amount of an asset or CGU exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are 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. These calculations are corroborated by valuation multiples, quoted share prices for publicly traded entities or other available fair value indicators.

Impairment losses of continuing operations are recognised in the consolidated statement of income in those expense categories consistent with the function of the impaired asset.

An assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists, the Group estimates the assets or CGUs recoverable amount. A previously recognised impairment loss is reversed only if there has been a change in the assumptions used to determine the asset's recoverable amount since the last impairment loss was recognised. The reversal is limited so that the carrying amount of the assets does not exceed its recoverable amount, nor exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognised for the asset in prior years. Such reversal is recognised in the consolidated statement of income.

2.12 Repurchase and resale arrangements

The Group enters into purchases / sales of securities under agreements to resell / repurchase substantially identical securities at a specified date in the future at a fixed price.

Securities sold under repurchase agreements continue to be recognised in the consolidated statement of financial position and are measured in accordance with the relevant accounting policy for that investment. The proceeds from the sale of the investments are reported as part of liabilities as securities sold under repurchase agreements. The difference between the sales price and repurchase price is treated as interest expense and is accrued over the life of the agreement using the effective interest method.

Securities purchased under resale agreements are not recognised in the consolidated statement of financial position. The difference between the purchase price and resale price is treated as interest income and is accrued over the life of the agreement using the effective interest method.

Notes to the Consolidated Financial Statements

for the year ended 31 December 2017

(All amounts in US$ millions)

2 Significant accounting policies (continued)

2.13 Investment in associates

An associate is an entity over which the Group exerts significant influence, usually evidenced by a holding of 20% to 50% of the voting power of the investee company. The Group's investment in associates is accounted for using the equity method of accounting. Where an associate is acquired and held exclusively for resale, it is accounted for as a non-current asset held for sale under IFRS 5.

Under the equity method, investment in associate is initially recognised at cost and adjusted thereafter for the post-acquisition change in the Group's share of net assets of the investee. Goodwill relating to an associate is included in the carrying amount of the investment and is not amortised or separately tested for impairment. The Group recognises in the consolidated statement of income its share of the results of the associate from the date that influence effectively commenced until the date that it effectively ceases. Where there has been a change recognised directly in the equity of the associate, the Group recognises its share of any changes and discloses this, when applicable, in the consolidated statement of comprehensive income.

Distributions received from an associate reduce the carrying amount of the investment.

Unrealised gains on transactions with an associate are eliminated to the extent of the Group's share in the associate. Unrealised losses are also eliminated unless the transaction provides evidence of impairment in the asset transferred.

The reporting dates of the associates and the Group are identical and in case of different reporting date of an associate, which are not more than three months, from that of the Group, adjustments are made for the effects of significant transactions or events that occur between that date and the date of the Group's consolidated financial statements. The associate's accounting policies conform to those used by the Group for like transactions and events in similar circumstances.

After application of the equity method, the Group determines whether it is necessary to recognise an additional impairment loss on the Group's investment in its associates. The Group determines at each reporting date whether there is any objective evidence that the investment in the associate is impaired. If this is the case the Group calculates the amount of impairment as the difference between the recoverable amount of the associate and its carrying value and recognises the amount in the consolidated statement of income.

Associates of the Group are listed in note 27.

2.14 Other provisions

Other provisions are recognised in the consolidated statement of financial position when the Group has a present obligation (legal or constructive) as a result of a past event, from which it is both probable and measurable that an outflow of economic benefits will be required to settle the obligation.

2.15 Property, plant and equipment

Property, plant and equipment is carried at historical cost less accumulated depreciation and impairment losses. An impairment loss is recognised in the consolidated statement of income whenever the carrying amount of an asset exceeds its recoverable amount. The recoverable amount of assets is the greater of their fair value less estimated cost to sell and value in use. Depreciation is computed on a straight-line basis over the estimated useful life of each asset category.

2.16 Hedge accounting

The Group enters into derivative instrument transactions to manage exposure to interest rate and foreign currency. All derivative financial instruments of the Group are recorded in the consolidated statement of financial position at fair value. The fair value of a derivative is the equivalent of the unrealised gain or loss from marking to market the derivative using prevailing market rates or internal pricing models. Positive and negative fair values are reported as assets and liabilities respectively and are offset when there is both an intention to settle net and a legal right to offset exists.

For the purposes of hedge accounting, hedges are classified into two categories: (a) fair value hedges which hedge the exposure to changes in the fair value of a recognised asset or liability and (b) cash flow hedges which hedge exposure to variability in cash flows that is either attributable to a particular risk associated with a recognised asset or liability or a forecasted transaction.

Notes to the Consolidated Financial Statements

for the year ended 31 December 2017

(All amounts in US$ millions)

2 Significant accounting policies (continued)

2.16 Hedge accounting (continued)

A hedging relationship exists where:

- at the inception of the hedge there is formal documentation of the hedge;
- the hedge is expected to be highly effective;
- the effectiveness of the hedge can be reliably measured;
- the hedge is highly effective throughout the reporting period; and
- for hedges of a forecasted transaction, the transaction is highly probable and presents an exposure to variations in cash flows that could ultimately affect profit or loss.

In relation to fair value hedges which meet the conditions for hedge accounting, any gain or loss from re-measuring the hedging instrument is recognised immediately in the consolidated statement of income. The hedged items are also adjusted for fair value changes relating to the risk being hedged and the difference is recognised in the consolidated statement of income.

In relation to cash flow hedges which meet the conditions for hedge accounting, the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised initially in equity and any ineffective portion is recognised in the consolidated statement of income. The gains or losses on cash flow hedges recognised initially in equity are transferred to the consolidated statement of income in the period in which the hedged transaction impacts the consolidated statement of income. Where the hedged transaction results in the recognition of an asset or liability, the associated gains or losses that had initially been recognised in equity are included in the initial measurement of the cost of the related asset or liability.

For hedges that do not qualify for hedge accounting, any gains or losses arising from changes in fair value of the hedging instrument are taken directly to the consolidated statement of income.

Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated or exercised, no longer qualifies for hedge accounting or is revoked by the Group. For cash flow hedges, any cumulative gain or loss on the hedging instrument recognised in equity remains in equity until the forecasted transaction occurs. In the case of fair value hedges of interest bearing financial instruments, any adjustment relating to the hedge is amortised over the remaining term to maturity. Where the hedged transaction is no longer expected to occur, the net cumulative gain or loss recognised in equity is transferred to the consolidated statement of income.

2.17 Recognition of income and expenses

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. Revenue is measured at the fair value of the consideration received. The following specific recognition criteria must also be met before revenue is recognised.

Interest income and expense

Interest income and expense are recognised in the consolidated statement of income for all interest bearing financial assets and liabilities using the effective interest rate 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 liability or a shorter period, where appropriate to the net carrying amount of the financial asset or liability.

Fees which are considered an integral part of the effective yield of a financial asset are recognised using the effective interest rate method.

Fees and commission income

Fees earned for providing of services over a period of time are accrued over that period. Fee income for providing transaction services are recognised on completion of the underlying transaction. Performance fees are recognised when earned, being the time the risk of realisation of such fees no longer exists.

Investment income

Investment income represents results arising from investment trading activities, including all gains and losses from changes in fair value and related interest income or expense and dividends for financial assets and financial liabilities held for trading.

Notes to the Consolidated Financial Statements

for the year ended 31 December 2017

(All amounts in US$ millions)

2 Significant accounting policies (continued)

2.17 Recognition of income and expenses (continued)

Dividend income

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

Sale of goods

Revenue from sale of goods is recognised when the significant risks and rewards of ownership have been transferred to the customer.

2.18 End of service benefits

Provision is made for amounts payable to employees under the Kuwaiti Labour Law, employee contracts and applicable labour laws in the countries where the subsidiaries operate. This liability, represents the amount payable to each employee as a result of involuntary termination on the reporting date. The obligations are paid into a plan which is administrated by an independent trustee.

2.19 Foreign currency

The consolidated financial statements are presented in US Dollars which is also the Corporation's functional currency. Each entity in the Group determines its own functional currency and items included in the financial statements of each entity are measured using that functional currency.

Transactions in foreign currencies are translated to US Dollars at the rate of exchange prevailing at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into US Dollars at market rates of exchange prevailing on the reporting date. Realised and unrealised foreign exchange gains and losses are included in the consolidated statement of income.

Non-monetary items that are measured in terms of historical costs in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Translation gains or losses on non-monetary items are included in equity as part of the fair value adjustment on financial assets available for sale, unless they form part of an effective hedging strategy.

Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined. Translation differences on non-monetary items at fair value through statement of income are recognised in the consolidated statement of income within the fair value net gain or loss. Any goodwill arising on the acquisition of a foreign operation and any fair value adjustments to the carrying amounts of assets and liabilities arising on the acquisition are treated as assets and liabilities of the foreign operations and translated at closing rate of exchange at the reporting date.

As at the reporting date, the assets and liabilities of foreign subsidiaries, and the carrying amount of foreign associates, are translated into the Group's presentation currency at the rate of exchange ruling at the reporting date and their statements of income are translated at the weighted average exchange rates for the year. Exchange differences arising on translation are taken directly to foreign exchange translation adjustments within equity. On disposal of a foreign entity, the cumulative amount recognised in equity relating to the particular foreign operation is recognised in the consolidated statement of income.

2.20 Segment reporting

A segment is a distinguishable component of the Group that is engaged either in providing products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments.

2.21 Standards issued but not yet effective

Standards issued but not yet effective up to the date of issuance of the Corporation's financial statements are listed below. The Corporation intends to adopt those standards when they become effective.

Notes to the Consolidated Financial Statements

for the year ended 31 December 2017

(All amounts in US$ millions)

2 Significant accounting policies (continued)

2.21 Standards issued but not yet effective (continued)

IFRS 9: Financial Instruments

The IASB issued the final version of IFRS 9, Financial Instruments in July 2014, that replaces IAS 39, Financial Instruments: Recognition and Measurement and all previous versions of IFRS 9. IFRS 9 brings together all three aspects of the accounting for financial instruments project: classification and measurement, impairment and hedge accounting. IFRS 9 is effective for annual periods beginning on or after 1 January 2018 and the Group is required to adopt IFRS 9 from 1 January 2018. Further, the Group will avail exemption, allowing it not to restate comparative information for prior periods with respect to classification and measurement (including impairment) changes. Differences in the carrying amounts of financial assets and financial liabilities resulting from the adoption of IFRS 9 will be recognised in retained earnings and reserves as at 1 January 2018.

During the year 2017, the Group has performed a detailed impact assessment that the initial application of IFRS 9, will have on its consolidated financial statements . The assessment is based on currently available information and may be subject to changes arising from further reasonable and supportable information being made available to the Group in 2018. The assessment of the estimated impact on the adoption of the standard on the Group's equity as at 1 January 2018 is based on the assessment undertaken to date and is summarised below.

	As at 31 December 2017	Estimated adjustments due to adoption of IFRS 9	Estimated adjusted opening balance at 1 January 2018
Reserves	504	(82)	422
Retained earnings	43	82	125

i. Classification and measurement

IFRS 9 contains new classification and measurement approach for financial assets that reflect the business model in which assets are managed and their cash flow characteristics. IFRS 9 contains three classification categories for financial assets: measured at Amortised Cost, Fair Value through Other Comprehensive Income ("FVOCI") (with and without recycling of gains or losses to profit or loss on derecognition of debt and equity securities, respectively) and Fair Value Through Profit or Loss ("FVTPL"). The standard eliminates the existing IAS 39 categories of Held to Maturity ("HTM"), Loans and Receivables and Available for Sale ("AFS").

The Group has evaluated the classification and measurement criteria to be adopted for various financial assets, which fall under the purview of IFRS 9. The Group expects to continue measuring all financial assets at their fair value, which are currently classified as FVTPL, under IAS 39. Further all the equity shares, debt securities and funds currently classified as AFS with gains and losses recorded in Other Comprehensive Income ("OCI"), henceforth will be classified as FVTPL considering the management assessment of the business model. The AFS reserve of US$ 82 million relating to these securities, which are currently presented as accumulated OCI, will be reclassified to retained earnings.

Based on the business model assessment, the Group decided to classify debt securities under FVTPL as per IFRS 9, as the Group's intent is to hold the assets for collecting contractual cash flows, whilst actively trading a significant amount on a relatively frequent basis at their current fair value.

ii. Impairment

IFRS 9 replaces the 'incurred loss' model in IAS 39 with a forward-looking 'expected credit loss' ("ECL") model. Under IFRS 9 requirements, the impairment requirements apply to financial assets measured at amortised cost, debt instruments classified as FVOCI.

The Group is to record expected credit losses on all of its debt securities, loans and trade receivables, either on a 12-month or lifetime basis. However, the Group will have no impact due to this change as all current debt instruments will be classified at FVTPL.

iii. Hedge accounting

As IFRS 9 does not change the general principles of how an entity accounts for effective hedges, therefore the hedging requirements of IFRS 9 will not have a significant impact on Group's consolidated financial statements.

iv. Financial liabilities

IFRS 9 does not change the general principles of classification of financial liabilities. Since the Group classifies its financial liabilities as measured at amortized cost and therefore will have no change due to the adoption of IFRS 9.

Notes to the Consolidated Financial Statements

for the year ended 31 December 2017

(All amounts in US$ millions)

2 Significant accounting policies (continued)

2.21 Standards issued but not yet effective (continued)

IFRS 15: Revenue from Contracts with Customers

IFRS 15 specifies how and when an entity recognises revenue as well as requiring such entities to provide users of financial statements with more informative, relevant disclosures. The standard provides a single, principles based five-step model to be applied to all contracts with customers. The standard was issued in May 2014 and applies to annual financial statements beginning on or after 1 January 2018. This new standard would remove inconsistencies and weaknesses in previous revenue requirements, provide a more robust framework for addressing revenue issues and improve comparability of revenue recognition practices across entities, industries, jurisdictions and capital markets.

IFRS 15 is effective for annual reporting periods beginning on or after 1 January 2018, with early adoption permitted. The Group does not expect to have a significant impact on its consolidated financial statements on the adoption of IFRS 15.

IFRS 16 – Leases

The IASB issued the new standard for accounting for leases, IFRS 16, Leases in January 2016. The new standard does not significantly change the accounting for leases for lessors. However, it does require lessees to recognise most leases on their balance sheets as lease liabilities, with the corresponding right-of-use assets. Lessees must apply a single model for all recognised leases, but will have the option not to recognise 'short-term' leases and leases of 'low-value' assets. Generally, the profit or loss recognition pattern for recognised leases will be similar to today's finance lease accounting, with interest and depreciation expense recognised separately in the statement of income.

IFRS 16 is effective for annual periods beginning on or after 1 January 2019. Early application is permitted provided the new revenue standard, IFRS 15, is applied on the same date. Lessees must adopt IFRS 16 using either a full retrospective or a modified retrospective approach.

The Group is in the process of quantifying the impact of this standard on the Group's financial statements, when adopted.

2.22 Significant accounting judgements and estimates

The preparation of the Group's consolidated financial statements require management to make judgements, estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities and the disclosure of contingent liabilities, at the reporting date. However, uncertainty about the assumptions and estimates could result in outcomes that require a material adjustment to the amount of the asset or liability affected in future periods.

Judgements

In the process of applying the Group's accounting policies, management has made the following judgements, which have the most significant effect in the amounts recognised in the consolidated financial statements.

Classification of investments

Management decides on acquisition of a security whether it should be classified as held to maturity, held for trading, designated at fair value through statement of income or available for sale.

For those deemed to be held to maturity, management ensures that the requirements of IAS 39 are met and in particular, the Group's intention and ability to hold these to maturity.

The Group classifies securities as trading if they are acquired primarily for the purpose of making a short term profit by the dealers.

Classification of investments designated at fair value through statement of income depends on how management monitors the performance of these investments. When they are not classified as held for trading but have readily available reliable fair values and the changes in fair values are reported as part of profit or loss in the management accounts, they are classified as fair value through statement of income.

All other investments are classified as available for sale.

Impairment of equity investments

The Group treats investments as impaired when there has been a significant or prolonged decline in the fair value below its cost or where other objective evidence of impairment exists. The determination of what is "significant" or "prolonged" requires considerable judgement. In addition, the Group evaluates other factors, including normal volatility in share price for quoted equities and the future cash flows and the discount factors for projects and unquoted equities.

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for the year ended 31 December 2017

(All amounts in US$ millions)

2 Significant accounting policies (continued)

2.22 Significant accounting judgements and estimates (continued)

Estimation uncertainty

The key assumptions concerning the future and other key sources of estimation uncertainty at the reporting date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

Impairment losses on investment in debt instruments

The Group reviews its investment in debt instruments at each reporting date to assess whether a provision for impairment should be recorded in the consolidated statement of income. In particular, considerable judgment by management is required in the estimation of the amount and timing of future cash flows when determining the level of provisions required. Such estimates are necessarily based on assumptions about several factors involving varying degrees of judgment and uncertainty, and actual results may differ resulting in future changes to such provisions.

Valuation of unquoted equity investments

Valuation of unquoted equity investments is normally based on one of the following:

- recent arm's length market transactions;
- current fair value of another instrument that is substantially the same;
- the expected cash flows discounted at current rates applicable for items with similar terms and risk characteristics; or
- other valuation models.

The determination of the cash flows and discount factors for unquoted equity investments requires significant estimation. There are a number of securities where this estimation cannot be reliably determined and these are carried at cost as disclosed in note 5. The Group updates the valuation techniques periodically and tests these for validity using either prices from observable current market transactions in the same instrument or other available observable market data.

3 Placements with banks

	2017	2016
Local banks	-	49
Other GCC banks	232	222
International bank	-	10
	232	281

Placements with banks carry an effective interest rate of 1.40% per annum (2016: 0.98% per annum).

4 Financial assets at fair value through statement of income

	2017	2016
Quoted debt instruments	49	29
Hedge and other unquoted alternative funds	340	425
	389	454

Notes to the Consolidated Financial Statements

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5 Financial assets available for sale

	2017	2016
Debt instruments		
International bonds	108	144
GCC and Islamic bonds	932	1,361
Emerging market bonds	61	21
Structured debt instruments	18	28
	1,119	1,554
Equities and managed funds		
Quoted equity investments and funds	**196**	195
Equity participations		
Quoted equity investments	170	194
Unquoted equity investments	113	118
	283	312
Private equity funds		
Managed funds portfolio	89	130
Real estate funds portfolio	15	14
	104	144
	1,702	2,205

Investments in private equity funds are carried at net asset values as reported by the investment managers. Due to the nature of these investments, the net asset values reported by the investment managers represent the best estimate of fair value available for these investments.

Management has performed an analysis of financial assets available for sale and have concluded that the impairment losses of US$ 31 million (2016: US$ 8 million) recognized in the consolidated statement of income are adequate (note 18).

6 Investments in associates

The carrying amount of investments in associates includes goodwill amounting to US$ 68 million (2016: US$ 39 million).

The Group’s investments in associates that are listed on a stock exchange have a carrying value of US$ 161 million (2016: US$ 144 million) and a market value of US$ 202 million (2016: US$ 156 million).

Notes to the Consolidated Financial Statements

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6 Investments in associates (continued)

The following table illustrates the summarised financial information of the Group's investments in associates:

	2017	2016 (Restated)
Share of assets	4,258	4,003
Share of liabilities	(2,688)	(2,740)
Share of net assets	**1,570**	1,263
Goodwill	68	39
Impairment losses	(48)	(49)
Carrying amount of investments	**1,590**	1,253
Share of revenue	1,767	1,558
Share of results for the year	131	32

Associates of the Group are listed in note 27.

Summarised financial information of material associates of the Group is as follows:

2017	**Foulath Holding B.S.C. (C)**	**The National Titanium Dioxide Co., Ltd. (Cristal)**	**Jeddah Cable Company Ltd.**	**Wataniya Telecom Algerie S.P.A.**	**Gulf Re Holdings Limited**	**Aviation Lease and Finance Company K.S.C.**
Assets	2,279	3,799	488	1,519	52	3,658
Liabilities	(1,045)	(2,964)	(259)	(696)	-	(2,715)
Non-controlling interests	(262)	(35)	-	-	-	-
Net assets	**972**	**800**	**229**	**823**	**52**	**943**
Revenue	1,046	2,142	353	940	-	397
Results for the year	21	85	1	136	-	116
Other comprehensive income / (loss) for the year	3	101	3	(32)	3	-

2016	Foulath Holding B.S.C. (C)	The National Titanium Dioxide Co., Ltd. (Cristal) (restated)	Jeddah Cable Company Ltd.	Wataniya Telecom Algerie S.P.A.	Gulf Re Holdings Limited	Aviation Lease and Finance Company K.S.C.
Assets	2,381	3,647	521	1,575	244	2,771
Liabilities	(1,261)	(3,022)	(295)	(827)	(195)	(1,912)
Non-controlling interests	(280)	(29)	-	-	-	-
Net assets	840	596	226	748	49	859
Revenue	794	1,735	519	1,025	63	255
Results for the year	(25)	(198)	13	254	-	53
Other comprehensive income / (loss) for the year	4	(24)	10	(15)	-	7

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for the year ended 31 December 2017

(All amounts in US$ millions)

6 Investments in associates (continued)

The movement during the year is as follows:

2017	**Foulath Holding B.S.C. (C)**	**The National Titanium Dioxide Co., Ltd. (Cristal)**	**Jeddah Cable Company Ltd.**	**Wataniya Telecom Algerie S.P.A.**	**Gulf Re Holdings Limited**	**Aviation Lease and Finance Company K.S.C.**
Opening balance	840	596	226	748	49	859
Shareholders advance	108	18	-	-	-	-
Dividend	-	-	-	(29)	-	(32)
Results	21	85	1	136	-	116
Other comprehensive income / (loss)	3	101	2	(32)	3	-
Closing balance	**972**	**800**	**229**	**823**	**52**	**943**

2016	Foulath Holding B.S.C. (C)	The National Titanium Dioxide Co., Ltd. (Cristal) (restated)	Jeddah Cable Company Ltd.	Wataniya Telecom Algerie S.P.A.	Gulf Re Holdings Limited	Aviation Lease and Finance Company K.S.C.
Opening balance	861	781	203	509	49	716
Capital increase	-	-	-	-	-	98
Shareholders advance	-	37	-	-	-	-
Dividend	-	-	-	-	-	(15)
Results	(25)	(198)	13	254	-	53
Other comprehensive income / (loss)	4	(24)	10	(15)	-	7
Closing balance	840	596	226	748	49	859

Summarised financial information of individually immaterial associates of the Group before any elimination is as follows:

	2017	2016
Assets	5,217	5,786
Liabilities	(3,351)	(3,820)
Net assets	**1,866**	1,966
Revenue	1883	1,521
Results for the year	219	155
Other comprehensive income for the year	32	52

On 2 February 2017, the Corporation has invested US$ 13 million for the acquisition of 35% ownership in Sudair Pharmaceutical for Drugs Company Limited, a limited liability company incorporated in the Kingdom of Saudi Arabia. The investment is classified as an associate.

On 2 August 2017, the Corporation has invested US$ 17 million for the acquisition of 35% ownership in Horizon (AD) Investment Ltd, a limited liability company incorporated in the Cayman Islands. The investment is classified as an associate.

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6 Investments in associates (continued)

On 24 October 2017, the Corporation acquired 100,000 shares for US$ 100 million, resulting in a 19.61% voting interest, in Tristar Holding Limited a limited liability company incorporated in the United Arab Emirates. The initial payment includes contingent consideration of US$ 20 million paid in advance and the fair value of the contingent consideration was US$ 16 million on the date of acquisition. Based on initial assessment, the fair value of identifiable assets acquired was US$ 67 million resulting in goodwill of US$ 29 million. The investment is classified as an associate.

The National Titanium Dioxide Company Limited ("Cristal"), an associate company of the Group, has adopted IFRS from current Saudi accounting standards for the period starting 1 January 2017. Cristal has opted for the transitional provisions of IFRS and adjusted opening retained earnings and other reserves directly in the equity statement. Cristal management has used the option available only on first time adoption of IFRS to transfer the foreign currency translation reserve to retained earnings. Further, management of Cristal has used judgement in assessing the impairment of assets and changed assumptions previously used to assess impairment, mainly discount rate, cash flow projections and growth rate. The net impact of the adjustment in Group's consolidated financial statement amounted to US$ 112 million reduction in Group's retained earnings and US$ 84 million increase in foreign currency translation reserve and US$ 1 million increase in investment revaluation reserve.

7 Other assets

	2017	2016
Accrued interest, fees, commissions and dividends	13	16
Positive fair value of derivative instruments	4	1
Prepayments	2	4
Property, plant and equipment	60	65
Margin money paid on derivative instruments	46	75
Others, including trade receivable of subsidiaries	149	140
	274	301

8 Deposits from banks and other financial institutions

	2017	2016
Deposits from central banks	55	200
Deposits from other financial institutions	457	290
Other deposits	59	80
	571	570

At 31 December 2017, deposits from central banks and other institutions headquartered in the GCC states amounted to US$ 571 million (2016: US$ 570 million).

Deposits from banks and other financial institutions carry an effective interest rate of 1.46 % per annum (2016: 1.54% per annum).

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9 Term finance

	Interest rate %	2017	2016
KWD medium term deposits maturing in 2018	3.00 % per annum	99	98
USD medium term deposits maturing in 2018	2.25 % per annum	300	300
USD medium term deposits maturing in 2021	6 months LIBOR plus 180 bps	100	100
AED bank loans (Subsidiary loans)	Floating rate ranging from 3.00 % to 7.00 %	7	8
Medium Term Note Issues (EMTN)			
USD medium term fixed rate note due in 2017	3.25 % per annum (semi annual)	-	500
MYR medium term fixed rate note due in 2021	5.10 % per annum (semi annual)	111	100
MYR medium term fixed rate note due in 2022	5.10 % per annum (semi annual)	42	38
MYR medium term fixed rate note due in 2023	4.52 % per annum (semi annual)	99	89
MYR medium term fixed rate note due in 2027	5.30 % per annum (semi annual)	38	35
		796	1,268

10 Other liabilities

	2017	2016
Accrued interest	27	20
Negative fair value of derivative instruments	50	75
Others, including trade payable of subsidiaries and accrued expenses	137	133
	214	228

11 Equity

11.1 The authorised, issued and fully paid capital comprises of 2.1 million shares of US$ 1,000 each (2016: 2.1 million shares of US$ 1,000 each).

11.2 In accordance with the Corporation's Articles of Association, 10% of the profit for the year attributable to the equity holders of the Corporation is required to be transferred to a non-distributable compulsory reserve until the reserve reaches a minimum of 50% of share capital.

11.3 In accordance with the Corporation's Articles of Association, 10% of the profit for the year attributable to the equity holders of the Corporation is required to be transferred to the voluntary reserve. The transfer to this reserve may be discontinued by a resolution adopted in the general assembly meeting of the shareholders. This reserve is available for distribution to shareholders. As mentioned in note 28, the Board of Directors have recommended not to transfer the 10% of the profit for the current year to the voluntary reserve.

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(All amounts in US$ millions)

11 Equity (continued)

11.4 The Annual General Assembly meeting of shareholders held on 3 April 2016 approved the payment of cash dividend from voluntary reserve of US$ 50 per share for the year ended 31 December 2015, amounting to US$ 105 million (31 December 2016:nil). The Annual General Assembly meeting of shareholders also approved the transfer of US$ 9 million from voluntary reserve to accumulated losses.

12 Interest income

	2017	2016
Placements with banks	6	5
Financial assets available for sale	48	52
Financial assets at fair value through statement of income	2	1
	56	58

13 Net gains from investments

	2017	2016
Realized gain from financial assets available for sale	60	42
Realized gain from financial assets at fair value through statement of income	7	1
Unrealized gain / (loss) from financial assets at fair value through statement of income	15	(3)
Gain on bargain purchase of an associate	-	16
Realized gain on sale of subsidiary	-	9
Realized gain on sale of associate	-	10
	82	75

14 Dividend income

	2017	2016
Private equity funds	2	1
Quoted equity investments and funds	5	5
Equity participations available for sale	5	6
	12	12

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for the year ended 31 December 2017

(All amounts in US$ millions)

15 Net fee, commission and other income

	2017	2016
Change in fair value of contingent consideration	2	-
Other income	1	5
	3	5

16 Interest expense

	2017	2016
Deposits from banks and other financial institutions	(9)	(12)
Securities sold under repurchase agreements	-	(1)
Term finance	(40)	(44)
	(49)	(57)

17 Other operating income

Other operating income represents net income from subsidiaries engaged in manufacturing and service activities.

	2017	2016
Sales	66	116
Cost of sales	(51)	(88)
Gross profit	**15**	28
Other (loss) / income	(2)	1
Selling and distribution expenses	(6)	(4)
Administrative expenses	(6)	(17)
	1	8

18 Impairment losses

	2017	2016
Financial assets available for sale :		
Equity participations	(23)	-
Equities and managed funds	(6)	(13)
Private equity funds	(2)	(1)
Interest bearing securities	-	6
	(31)	(8)
Other assets	(29)	(14)
	(60)	(22)

Notes to the Consolidated Financial Statements

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19 Retirement and other terminal benefits

The Corporation has defined voluntary contribution and end of service indemnity plans which cover all its employees. Contribution to the voluntary plan is based on a percentage of pensionable salary and consists of contribution by employees and a matched contribution, up to a certain limit, by the Corporation. Contribution to the end of service indemnity plan is based on a percentage of pensionable salary and number of years of service by the employees. The amounts to be paid at the end of service benefits are determined by reference to the amounts of the contributions and investment earnings thereon.

The Corporation also pays contributions to Government defined contribution pension plan for certain employees in accordance with the legal requirements in Kuwait as well as contribution in line with the labour law in the countries where its subsidiaries operate.

The total cost of retirement and other end of service benefits included in staff expenses for the year ended 31 December 2017 amounted to US$ 7 million (2016: US$ 8 million).

20 Risk management

This note represents information on the Group's exposure to risks arising from the use of financial instruments. Risk is an inherent part of the Group's business activities. It is managed through a process of ongoing identification, assessment, measurement and monitoring of the business activities, subject to risk limits and other controls. This process of risk management is critical to the Group's continuing profitability and each individual within the Group is accountable for the risk exposures relating to his or her responsibilities.

The Group is exposed to liquidity risk, market risk and credit risk. Market risk is subdivided into interest rate risk, foreign currency risk and equity price risk.

Risk management begins with the Risk Management Committee which is composed of members from the Corporation's Board of Directors and senior management, which defines and recommends the Group's risk appetite to the Board of Directors. The Board of Directors is ultimately responsible for the overall risk management approach and for approving the risk strategies and principles.

20.1 Liquidity risk

Liquidity risk is the risk that the Group will be unable to meet its liabilities when they fall due. To limit this risk, management has arranged diversified funding sources, manages assets with liquidity in mind, and monitors liquidity on a daily basis.

The liquidity profile of financial liabilities reflects the projected cash flows, based on contractual repayment obligations which include future interest payments over the life of these financial liabilities. The liquidity profile of undiscounted financial liabilities at 31 December was as follows:

31 December 2017	Within 3 months	3 months to 1 year	1 to 5 years	Over 5 years	Total
Deposits from banks and other financial institutions	131	445	-	-	576
Term finance	404	15	313	147	879
Gross settled derivative instruments:					
- Contractual amount payable	565	-	162	172	899
- Contractual amount receivable	(564)	-	(153)	(137)	(854)
Other liabilities	62	41	73	38	214
Total undiscounted financial liabilities	**598**	**501**	**395**	**220**	**1,714**
Commitments	-	33	99	-	132
Contingent liabilities	20	62	3	313	398

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(All amounts in US$ millions)

20 Risk management (continued)

20.1 Liquidity risk (continued)

31 December 2016	Within 3 months	3 months to 1 year	1 to 5 years	Over 5 years	Total
Deposits from banks and other financial institutions	314	259	-	-	573
Term finance	5	539	662	177	1,383
Gross settled derivative instruments:					
- Contractual amount payable	538	-	108	226	872
- Contractual amount receivable	(540)	-	(100)	(162)	(802)
Other liabilities	37	38	83	70	228
Total undiscounted financial liabilities	354	836	753	311	2,254
Commitments	-	32	88	-	120
Contingent liabilities	-	40	67	326	433

The asset and liability maturity profile shown in the table below is based on management's assessment of the Group's right and ability (and not necessarily the intent) to liquidate these instruments based on their underlying liquidity characteristics.

	Within 3 months	**3 months to 1 year**	**1 to 5 years**	**Over 5 years**	**Total**
At 31 December 2017					
Assets					
Cash and cash equivalents	41	-	-	-	41
Placements with banks	232	-	-	-	232
Financial assets at fair value through statement of income	57	332	-	-	389
Financial assets available for sale	1,467	19	13	203	1,702
Investment in associates	-	-	-	1,590	1,590
Other assets	42	27	83	122	274
Total assets	**1,839**	**378**	**96**	**1,915**	**4,228**
Liabilities					
Deposits from banks and other financial institutions	130	441	-	-	571
Term finance	399	-	260	137	796
Other liabilities	62	41	73	38	214
Total liabilities	**591**	**482**	**333**	**175**	**1,581**
Net gap	**1,248**	**(104)**	**(237)**	**1,740**	

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20 Risk management (continued)

20.1 Liquidity risk (continued)

	Within 3 months	3 months to 1 year	1 to 5 years	Over 5 years	Total
At 31 December 2016					
Assets					
Cash and cash equivalents	98	-	-	-	98
Placements with banks	281	-	-	-	281
Financial assets at fair value through statement of income	37	417	-	-	454
Financial assets available for sale	1,915	30	58	202	2,205
Investment in associates	-	-	-	1,253	1,253
Other assets	50	32	83	136	301
Total assets	2,381	479	141	1,591	4,592
Liabilities					
Deposits from banks and other financial institutions	314	256	-	-	570
Term finance	2	502	602	162	1,268
Other liabilities	36	38	86	68	228
Total liabilities	352	796	688	230	2,066
Net gap	2,029	(317)	(547)	1,361	

20.2 Market risk

Market risk arises from fluctuations in interest rates, foreign exchange rates and equity prices. The nature of these risks is as follows:

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 Group is exposed to interest rate risk as a result of mismatches of interest rate repricing of assets and liabilities.

Foreign exchange risk

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

Equity price risk

Equity price risk arises from the change in fair values of equity investments.

Market risk pertaining to investments in Debt Capital Market, Equity and Alternative Investments and Treasury divisions are measured, monitored and managed both on a notional basis and using a Market Value at Risk (Market VaR) concept. The table below shows Total Value at Risk (Total VaR) by risk factor. These VaR measures are based on a 95% confidence level, 25 day holding period and use historical market data.

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20 Risk management (continued)

20.2 Market risk (continued)

2017	***Average***	***Minimum***	***Maximum***	***31 December 2017***
Interest rate	19	11	25	11
Equity price	9	7	13	7
Foreign exchange	-	-	1	-
Total*	**19**	**13**	**25**	**12**

2016	*Average*	*Minimum*	*Maximum*	*31 December 2016*
Interest rate	22	19	25	21
Equity price	15	12	19	13
Foreign exchange	1	-	4	1
Total*	23	19	26	20

** Total VaR incorporates benefits of diversification.*

The Principal Investment division monitors its quoted equity participation investments using a sensitivity analysis as indicated below. The effect on equity as a result of a change in the fair value of the quoted equity participation investments due to a reasonably possible change in equity indices, with all other variables held constant is as follows:

Market indices	*Change in equity price*	***Effect on equity***	
		2017	2016
Saudi Stock Exchange	+/-10	**20**	21
Other GCC indices	+/-10	**1**	2

The analysis is based on the assumption that the equity indexes if increased / decreased by 10% with other variables held constant and all the Principal Investment division's quoted equity instruments moved according to the historical correlation with the index.

Please refer note 23 for distribution of assets and liabilities between the divisions.

20.3 Credit risk

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. The Corporation's Board of Directors has set limits for individual borrower and groups of borrowers and for geographical and industry segments. The Group also monitors credit exposures, and continually assesses the creditworthiness of counterparties. In addition, the Group obtains security where appropriate, enters into master netting agreements and collateral arrangements with counterparties, and limits the duration of exposures.

As at 31 December 2017 and 2016 the Group has not obtained any collateral on any of the financial assets.

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20 Risk management (continued)

20.3 Credit risk (continued)

20.3.1 Maximum exposure to credit risk

The maximum credit exposure of the Group is as follows:

	Maximum exposure	
	2017	2016
Cash and cash equivalents	41	98
Placements with banks	232	281
Debt securities at fair value through statement of income	49	29
Debt securities available for sale	1,119	1,554
Other assets	212	199
Credit exposure on assets	**1,653**	**2,161**
Credit commitments	398	433
Total credit exposure	**2,051**	**2,594**

Credit risk in respect of derivative financial instruments is limited to those with positive fair values, which are included under other assets.

Concentrations arise when a number of counterparties are engaged 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 Group's performance to developments affecting a particular industry or geographic location. The maximum credit exposure to a single counterparty is US$ 134 million (2016: US$ 122 million).

The Group's concentration of credit risk exposure by geographic region is as follows:

	GCC	**Europe**	**America**	**Asia / Africa**	**Total**
At 31 December 2017					
Cash and cash equivalents	40	1	-	-	41
Placements with banks	232	-	-	-	232
Debt securities at fair value through statement of income	-	19	10	20	49
Debt securities available for sale	932	81	37	69	1,119
Other assets	158	5	-	49	212
Credit exposure on assets	**1,362**	**106**	**47**	**138**	**1,653**
Credit commitments	388	-	-	10	398
Total credit exposure	**1,750**	**106**	**47**	**148**	**2,051**

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20 Risk management (continued)

20.3 Credit risk (continued)

20.3.1 Maximum exposure to credit risk (continued)

	GCC	Europe	America	Asia / Africa	Total
At 31 December 2016					
Cash and cash equivalents	33	65	-	-	98
Placements with banks	271	10	-	-	281
Debt securities at fair value through statement of income	-	7	8	14	29
Debt securities available for sale	1,362	61	112	19	1,554
Other assets	108	10	11	70	199
Credit exposure on assets	1,774	153	131	103	2,161
Credit commitments	414	-	-	19	433
Total credit exposure	2,188	153	131	122	2,594

The Group's concentration of credit risk exposure by industry sector is as follows:

	Banks & FIs.	**Trading & Mftg.**	**Energy & Utilities**	**Govt. agencies**	**Other**	**Total**
At 31 December 2017						
Cash and cash equivalents	41	-	-	-	-	41
Placements with banks	232	-	-	-	-	232
Debt securities at fair value through statement of income	13	7	16	13	-	49
Debt securities available for sale	482	4	233	303	97	1,119
Other assets	59	106	10	3	34	212
Credit exposure on assets	**827**	**117**	**259**	**319**	**131**	**1,653**
Credit commitments	-	46	303	49	-	398
Total credit exposure	**827**	**163**	**562**	**368**	**131**	**2,051**

	Banks & FIs.	Trading & Mftg.	Energy & Utilities	Govt. agencies	Other	Total
At 31 December 2016						
Cash and cash equivalents	98	-	-	-	-	98
Placements with banks	281	-	-	-	-	281
Debt securities at fair value through statement of income	-	3	3	23	-	29
Debt securities available for sale	706	-	308	443	97	1,554
Other assets	98	82	4	5	10	199
Credit exposure on assets	1,183	85	315	471	107	2,161
Credit commitments	-	58	297	78	-	433
Total credit exposure	1,183	143	612	549	107	2,594

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20 Risk management (continued)

20.3 Credit risk (continued)

20.3.2 Credit quality of financial assets

In managing its portfolio, the Group utilises external ratings and other measures and techniques which seek to take account of all aspects of perceived risk. Credit exposures classified as 'Investment grade' quality are those where the ultimate risk of financial loss from the obligor's failure to discharge its obligation is assessed to be low. These include exposure to corporate entities with financial condition, risk indicators and capacity to repay which are considered to be good to excellent. All investment grade securities are rated by well-known rating agencies. Credit exposures classified as 'Unrated' quality comprise all other exposures whose payment performance is fully compliant with contractual conditions and which are not 'impaired', but are not assigned any published ratings.

The table below shows the credit quality by class of assets:

	Neither past due nor impaired		**Total**
At 31 December 2017	**Investment grade**	**Unrated**	
Cash and cash equivalents	41	-	41
Placements with banks	232	-	232
Debt securities at fair value through income statement	49	-	49
Debt securities available for sale	1,119	-	1,119
Other assets	63	149	212
Credit exposure on assets	**1,504**	**149**	**1,653**
Credit commitments	398	-	398
Total credit exposure	**1,902**	**149**	**2,051**

	Neither past due nor impaired		Total
	Investment grade	Unrated	
At 31 December 2016			
Cash and cash equivalents	98	-	98
Placements with banks	281	-	281
Debt securities at fair value through income statement	29	-	29
Debt securities available for sale	1,554	-	1,554
Other assets	92	107	199
Credit exposure on assets	2,054	107	2,161
Credit commitments	433	-	433
Total credit exposure	2,487	107	2,594

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21 Commitments and contingent liabilities

In the usual course of meeting the requirements of the operations of Group companies, the Group has commitments to extend credit and provide financial guarantees and letters of credit to guarantee the performance of Group companies to third parties. The credit risk on these transactions is generally less than the contractual amount. The table below sets out the notional principal amounts of outstanding commitments.

	Notional principal amount	
	2017	2016
Credit Risk Amounts		
Transaction-related contingent items:		
- Letter of guarantees	**398**	433

Certain letters of guarantees are issued by the Corporation on behalf of its related parties (note 25).

The above commitments and contingent liabilities have off balance-sheet credit risk because only origination fees and accruals for probable losses are recognised in the consolidated financial statements until the commitments are fulfilled or expired. Many of the contingent liabilities and commitments will expire without being advanced in whole or in part. Therefore, the amounts do not represent expected future cash flows.

The Group had the following non-credit commitments as at the reporting date:

	2017	2016
Undrawn commitments for investments in private equity funds	64	68
Undrawn commitments for investments in associates	63	39
Other commitments	5	13
	132	120

22 Derivatives

Derivatives instruments are utilised by the Group as part of its asset and liability management activity to hedge its own exposure to market, interest rate and currency risk.

In the case of derivative transactions, the notional principal typically does not change hands. It is simply a quantity, which is used to calculate payments. While notional principal is a volume measure used in the derivatives and foreign exchange markets, it is neither a measure of market nor credit risk. The Group's measure of credit exposure is the cost of replacing contracts at current market rates should the counterparty default prior to the settlement date. Credit risk amounts represent the gross unrealised gains on transactions before taking account of any collateral held or any master netting agreements in place.

Hedge accounting

Interest rate swaps under which the Group pays a fixed rate and receives a floating rate are used in fair value hedges of fixed income financial assets available for sale. The Group also uses interest rate futures to hedge the fair value interest rate risk.

As at the reporting date, the notional amount of interest rate swaps and interest rate futures used to hedge interest rate risk amounted to US$ 22 million (2016: US$ 32 million) and its net fair value was a swap loss of US$ 1 million (2016: US$ 2 million).

Cross currency swaps are used to hedge non US$ term finance issued in fixed rate coupon. As at the reporting date, the notional amount of cross currency swaps amounted to US$ 333 million (2016: US$ 334 million) and its net fair value was a swap loss of US$ 43 million (2016: US$ 72 million).

For the year ended 31 December 2017, the Group recognised unrealised gain of US$ 1 million (2016: US$ 3 million) and realised loss of nil (2016: nil) on interest rate hedging instruments. The corresponding unrealised loss and realised gain on the hedged fixed income securities amounted to US$ 1 million (2016: US$ 3 million) and nil (2016: nil) respectively.

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22 Derivatives (continued)

The table below summarises the aggregate notional amounts and net fair value of derivative financial instruments.

	2017			2016		
	Positive fair value	**Negative fair value**	**Notional amount**	Positive fair value	Negative fair value	Notional amount
Derivatives held for hedging						
- Interest rate swaps	-	(1)	22	-	(2)	32
- Cross currency swaps	4	(47)	333	-	(72)	334
- Forward foreign exchange Contracts	-	(2)	899	1	(1)	872
	4	**(50)**	**1,254**	1	(75)	1,238

Maturity analysis

	Within 1 year	**Year 1 to 5**	**Above 5 years**	**Total**
At 31 December 2017				
Notional amounts				
Interest rate swaps	-	22	-	22
Cross currency swaps	-	161	172	333
Forward foreign exchange contracts	565	162	172	899
	565	**345**	**344**	**1,254**

	Within 1 year	Year 1 to 5	Above 5 years	Total
At 31 December 2016				
Notional amounts				
Interest rate swaps	5	27	-	32
Cross currency swaps	-	108	226	334
Forward foreign exchange contracts	538	108	226	872
	543	243	452	1,238

23 Segmental information

The Group organises and manages its operations by business divisions, primarily divided into Principal Investments, Debt Capital Markets, Equity and Alternative Investments, Treasury, and Corporate and Other. Management treats the operations of these business divisions separately for the purposes of decision making, resource allocation and performance assessment. Business division performance is evaluated based on segmental return on investments.

The Principal Investment division is responsible for actively investing in projects and equity participations.

Debt Capital Market division provides a stable coupon/spread income and a reserve of additional liquidity. The investments consist of high quality marketable debt securities diversified across a wide range of geographic and industry sectors.

Equities and Alternative Investments division manages a diversified set of portfolios in an array of different asset classes and investment themes that comprise investments ranging from equities to structured finance, private equity, market neutral funds, hedge funds and other alternative assets.

The Treasury division manages the Group's liquidity, short-term interest rate and foreign exchange activities using a variety of on and off-balance sheet treasury applications. The division trades in spot and forward foreign exchange and options, cash money markets, floating rate notes, interest rate swaps and other derivatives. Interest is charged / credited to business segments based on rates which approximate the marginal cost of funds on external borrowings while considering the equity as free capital.

Notes to the Consolidated Financial Statements

for the year ended 31 December 2017

(All amounts in US$ millions)

23 Segmental information (continued)

The Corporate and Other division comprises items which are not directly attributable to specific business divisions. Other operations of the Group includes operations, risk management and finance

	Principal Investments	**Debt Capital Markets**	**Equity and Alternative Investments**	**Treasury**	**Corporate and Other**	**Eliminations**	**Total**
31 December 2017							
Interest income	2	53	1	48	-	(48)	56
Interest expense	(28)	(13)	(8)	(48)	-	48	(49)
Share of results from associates	131	-	-	-	-	-	131
Other operating income	14	10	74	-	-	-	98
Net operating income	**119**	**50**	**67**	**-**	**-**	**-**	**236**
Other operating expenses	(13)	(2)	(3)	(3)	(34)	-	(55)
Impairment losses	(52)	-	(8)	-	-	-	(60)
Profit for the year	**54**	**48**	**56**	**(3)**	**(34)**	**-**	**121**
Segment assets	2,058	1,179	672	3,866	10	(3,557)	4,228
Segment liabilities	1,949	1,056	679	1,375	79	(3,557)	1,581
Equity							2,647
Total liabilities and equity							4,228
Other information							
Investment in associates	1,590	-	-	-	-	-	1,590

	Principal Investments	Debt Capital Markets	Equity and Alternative Investments	Treasury	Corporate and Other	Eliminations	Total
31 December 2016							
Interest income	2	56	-	49	-	(49)	58
Interest expense	(29)	(12)	(10)	(55)	-	49	(57)
Share of results from associates	32	-	-	-	-	-	32
Other operating income	53	22	20	-	5	-	100
Net operating income	58	66	10	(6)	5	-	133
Other operating expenses	(13)	(2)	(3)	(4)	(32)	-	(54)
Impairment losses	(14)	6	(15)	-	1	-	(22)
Profit for the year	31	70	(8)	(10)	(26)	-	57
Segment assets	1,768	1,597	776	4,275	15	(3,839)	4,592
Segment liabilities	1,676	1,511	784	1,921	13	(3,839)	2,066
Equity							2,526
Total liabilities and equity							4,592
Other information							
Investment in associates	1,253	-	-	-	-	-	1,253

Notes to the Consolidated Financial Statements

for the year ended 31 December 2017

(All amounts in US$ millions)

24 Fair value information

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in orderly transactions between market participants at the measurement date. Fair values are determined from quoted prices in active markets for identical financial assets or financial liabilities where these are available. Where the market for a financial instrument is not active, fair value is established using a valuation technique. These valuation techniques involve a degree of estimation, the extent of which depends on the instrument's complexity and the availability of market-based data. Investment securities classified as 'Available for sale' and 'Fair value through statement of income' are stated at fair value except for certain investments carried at cost. For other financial asset and liabilities carried at cost less impairment or amortized cost, the carrying value is not significantly different from their fair values as most of these assets and liabilities are of short term maturity or re-priced immediately based on market movement in interest rates.

Determination of fair value and fair value hierarchy:

The Group uses the following hierarchy for determining and disclosing the fair values of financial instruments:

Level 1: quoted prices in active market for the same instrument.

Level 2: quoted prices in active market for similar instruments or other valuation techniques for which all significant inputs are based on observable market data and

Level 3: valuation techniques for which any significant input is not based on observable market data including the NAV of private equity funds where the underlying investments are unquoted private companies / real estate assets.

The following table shows an analysis of financial instruments recorded at fair value by level of the fair value hierarchy:

	Level 1	Level 2	Level 3	Total
2017				
Assets measured at fair value				
Financial assets at fair value through statement of income				
Investment in quoted debt instruments	49	-	-	49
Hedge funds & other alternative funds	-	340	-	340
Financial assets available for sale				
Debt instruments	1,101	-	18	1,119
Equities and managed funds	196	-	-	196
Equity participations	170	-	113	283
Private equity funds	-	-	104	104
Other assets - derivative financial instruments				
Cross currency swaps	-	-	4	4
	1,516	**340**	**239**	**2,095**
Other liabilities - derivative financial instruments				
Interest rate swaps	-	1	-	1
Cross currency swaps	-	-	47	47
Forward foreign exchange Contracts	-	-	2	2
	-	**1**	**49**	**50**

Notes to the Consolidated Financial Statements

for the year ended 31 December 2017

(All amounts in US$ millions)

24 Fair value information (continued)

	Level 1	Level 2	Level 3	Total
2016				
Assets measured at fair value				
Financial assets at fair value through statement of income				
Investment in quoted debt instruments	29	-	-	29
Hedge funds & other alternative funds	-	425	-	425
Financial assets available for sale				
Debt instruments	1,526	-	28	1,554
Equities and managed funds	195	-	-	195
Equity participations	194	-	-	194
Private equity funds	-	-	144	144
Other assets - derivative financial instruments				
Forward foreign exchange contracts	-	-	1	1
	1,944	425	173	2,542
Other liabilities - derivative financial instruments				
Interest rate swaps	-	2	-	2
Cross currency swaps	-	-	72	72
Forward foreign exchange Contracts	-	-	1	1
	-	2	73	75

The following table shows a reconciliation of the beginning and closing balances of the financial instruments classified in Level 3 of the fair value hierarchy:

	At 1 January 2017	**Gain / (loss) recorded in the consolidated statement of income**	**Gain / (loss) recorded in equity**	**Net purchases, sales, transfers and settlements**	**At 31 December 2017**
31 December 2017					
Assets measured at fair value					
Financial assets available for sale					
Debt instruments	28	-	2	(12)	18
Equity participation	-	-	12	101	113
Private equity funds	144	27	(21)	(46)	104
Other assets - derivative financial instruments					
Cross currency swaps	-	4	-	-	4
Other liabilities -derivative financial instruments					
Cross currency swaps	72	(25)	-	-	47
Forward foreign exchange contracts	1	1	-	-	2

Notes to the Consolidated Financial Statements

for the year ended 31 December 2017

(All amounts in US$ millions)

24 Fair value information (continued)

	At 1 January 2016	Gain / (loss) recorded in the consolidated statement of income	Gain / (loss) recorded in equity	Net purchases, sales, transfers and settlements	At 31 December 2016
31 December 2016					
Assets measured at fair value					
Financial assets available for sale					
Debt instruments	62	-	2	(36)	28
Private equity funds	186	13	(5)	(50)	144
Other assets - derivative financial instruments					
Forward foreign exchange contracts	2	(1)	-	-	1
Other liabilities - derivative financial instruments					
Cross currency swaps	190	(118)	-	-	72
Forward foreign exchange contracts	2	(1)	-	-	1

Measurement of Level 3 fair values

i. Debt instruments: The fair values are based on broker quotes, prices quoted on Bloomberg and Reuters and independent valuation.

ii. Private equity funds: The fair values are based on fund statements sent by the fund managers .

iii. Cross currency swaps and forward foreign exchange contracts: The fair values are calculated using foreign exchange rates available in the market.

iv. Equity participation: The fair values are calculated using various valuation techniques like discounted cash flows, price multiples etc.

25 Related party transactions

Related parties represent major shareholders, Directors and key management personnel of the Corporation, and entities controlled, jointly controlled or significantly influenced by such parties. Pricing policies and terms of these transactions are approved by the Corporation's management.

Significant transactions with associates during the year are as follows:

	2017	2016
Guarantees and commitments	348	355
Receivables from associates	13	7

Compensation of key management personnel

The remuneration of key management personnel during the year is as follows:

	2017	2016
Salaries and short-term employee benefits	9	10
Post-employment and termination benefits	2	2
	11	12

Notes to the Consolidated Financial Statements

for the year ended 31 December 2017

(All amounts in US$ millions)

26 Capital management

The Corporation's capital represents shareholders' investment and is a key strategic resource which supports the Corporation's risk taking business activities.

The objective of the Group is to deploy this resource in an efficient and profitable manner to earn competitive returns.

The Corporation manages its capital taking into account both regulatory and economic requirements.

No changes were made in the objectives, policies or processes from the previous year. Consistent with others in the industry, the Group monitors capital on the basis of the gearing ratio. This ratio is calculated as net debt divided by total equity as follows:

	2017	2016
Interest-bearing deposits, term finance and other borrowings	1,367	1,838
Other liabilities	214	228
Less: Cash and cash equivalents, Securities purchased under resale agreement and placements with banks	(273)	(379)
Net debt	**1,308**	1,687
Equity attributable to equity holders of the Corporation	**2,647**	2,520
Gearing ratio (net debt / equity)	**0.5**	0.7

27 Principal subsidiaries and associates

The principal subsidiaries and associates of the Corporation are set out below:

Subsidiaries	**Country of incorporation**	**% of shareholding**		**Financial statements reporting date**	**Principal business activity**
		2017	**2016**		
Bituminous Products Company Limited (Bitumat)	Saudi Arabia	100	100	31 December 2017	Building material manufacturing
Gulf Electronic Tawasul Company KSCC	Kuwait	86.8	86.8	31 December 2017	Information Technology
GIC Technologies Company W.L.L	Kuwait	80	80	31 December 2017	Technical advisory
Gulf Jyoti International L.L.C	UAE	70	70	31 December 2017	Construction & Engineering
Associates	**Country of incorporation**	**% of shareholding**		**Financial statements reporting date**	**Principal business activity**
		2017	**2016**		
Gulf Re Holdings Limited	Channel Islands	50.0	50.0	31 December 2017	Re-insurance
Foulath Holding B.S.C (c)	Bahrain	50.0	50.0	31 December 2017	Holding company
Al Ezzel Power Company B.S.C. (c)	Bahrain	45.0	45.0	31 December 2017	Power & Water Utility project
Sudair Pharmaceutical for Drugs Company Limited	Saudi Arabia	35.0	-	31 December 2017	Pharmaceutical
Horizon Investment Ltd	Cayman Islands	35.0	-	31 December 2017	Education

Notes to the Consolidated Financial Statements

for the year ended 31 December 2017

(All amounts in US$ millions)

27 Principal subsidiaries and associates (continued)

Associates	Country of incorporation	% of shareholding		Financial statements reporting date	Principal business activity
		2017	2016		
Shuqaiq International Power and Water Company Limited	Saudi Arabia	33.3	33.3	31 December 2017	Power & Water Utility project
SGA Marafiq Holdings W.L.L.	Bahrain	33.3	33.3	31 December 2017	Power & Water Utility project
Technical Supplies & Services Co. Ltd.	UAE	30.7	30.7	31 December 2017	Refrigeration & Cooling Services
Osool Poultry Company S.A.O.C	Oman	26.7	26.7	31 December 2017	Poultry & Dairy Products
Bahrain LNG W.L.L.	Bahrain	24.0	24.0	31 December 2017	Oil and Gas
Al Dur Holding Company Limited	UAE	25.0	25.0	31 December 2017	Power & Water Utility project
Jeddah Cable Company Ltd.	Saudi Arabia	25.0	25.0	31 December 2017	Manufacturing Cables
Moon Iron and Steel Company SAOC	Oman	25.0	25.0	31 December 2017	Iron and steel
Interplast Company Limited (L.L.C.)	UAE	23.5	23.5	31 December 2017	Plastic
Celtex Weaving Mills Co. Ltd.	Bahrain	23.0	23.0	31 December 2017	Textiles
Rawabi Emirates (PJSC)	UAE	22.5	22.5	31 December 2017	Dairy Products
Dubai Wellness Centre	UAE	21.6	21.6	31 December 2017	Medical services
Wataniya Telecom Algerie S.P.A.	Algeria	20.0	20.0	31 December 2017	Telecom service provider
Gulf Stone Company SAOG	Oman	20.0	20.0	31 December 2017	Building Materials
A'Saffa Foods SAOG	Oman	20.0	20.0	31 December 2017	Poultry & Dairy Products
The National Titanium Dioxide Co., Ltd. (Cristal)	Saudi Arabia	20.0	20.0	31 December 2017	Production of Titanium Dioxide
Tristar Holdings Limited	UAE	19.6	-	31 December 2017	Logistics
Aviation Leasing and Finance Co	Kuwait	14.0	14.0	30 September 2017	Aviation Leasing

28 Subsequent events

Subsequent to the reporting date, The National Titanium Dioxide Co., Ltd. (Cristal), an associate of the Corporation received zakat assessments for the years from 2012 to 2014 claiming additional zakat liability of US$ 56 million. The share of the Corporation in regard to the zakat assessment is US$ 11 million. The management of Cristal is in the process of reviewing and objecting to the basis of the additional zakat liability.

The Board of Directors meeting held on 8 March 2018, proposed cash dividend of US$ 50 per share amounting to US$ 105 million for the year ended 31 December 2017. The Board of Directors further recommended not to transfer the 10% of the profit for the year ended 31 December 2017 to the voluntary reserve.

Gulf Investment Corporation G.S.C.

Stand-alone Statement of Financial Position

as at 31 December 2017

(All amounts in US$ millions)

The following appendix represents the statement of financial position of Gulf Investment Corporation excluding the assets and liabilities of its subsidiaries do not form part of the consolidated financial statements of the Corporation.

	2017	2016
Assets		
Cash and cash equivalents	28	83
Placements with banks	229	277
Financial assets at fair value through statement of income	389	454
Financial assets available for sale	1,702	2,205
Investments in associates	1,584	1,245
Investment in subsidiaries	55	67
Other assets	119	126
Total assets	**4,106**	4,457
Liabilities and equity		
Liabilities		
Deposits from banks and other financial institutions	571	570
Term finance	790	1,260
Other liabilities	98	107
Total liabilities	**1,459**	1,937
Equity		
Share capital	2,100	2,100
Reserves	504	486
Retained earnings /(accumulated losses)	43	(66)
Total equity	**2,647**	2,520
Total liabilities and equity	**4,106**	4,457

Principal Investing

Major Projects and Equity Participations

As of 31 December 2017

	Name of the Project	Location	GIC Effective holding %	GIC holding type
	Subsidiaries and Associates of GIC			
1	Bituminous Products Company Limited (Bitumat)	Saudi Arabia	100.00%	Direct
2	Gulf Electronic Tawasul Company	Kuwait	90.83%	Direct/Indirect
3	Gulf Jyoti International	UAE	70.00%	Direct
4	Foulath Holding	Bahrain	50.00%	Direct
5	Al Ezzel Power Company	Bahrain	45.00%	Direct
6	Sudair Pharmaceutical for Drugs Co.	Saudi Arabia	35.00%	Direct
7	Horizon (AD) Investment Ltd.	Cayman Islands	35.00%	Direct
8	Technical Supplies & Services Co. Ltd.	UAE	30.67%	Direct
9	Osool Poultry	Oman	26.68%	Direct
10	Jeddah Cable Company Ltd & Energya Group	Saudi Arabia	25.00%	Direct
11	Al Dur Power & Water Co.	Bahrain	25.00%	Indirect
12	Moon Iron and Steel Company	Oman	25.00%	Direct
13	Bahrain LNG	Bahrain	24.00%	Direct
14	Interplast Company Limited	UAE	23.50%	Direct
15	Rawabi Emirates	UAE	22.54%	Direct
16	The Dubai Wellness Center Limited	UAE	21.63%	Direct
17	A›Saffa Foods Co.	Oman	20.01%	Direct
18	The National Titanium Dioxide Co., Ltd. (CRISTAL)	Saudi Arabia	20.00%	Direct
19	Gulf Stone Company *	Oman	20.00%	Indirect
20	Wataniya Telecom Algerie	Algeria	20.00%	Indirect
21	Jubail Water & Power Co.	Saudi Arabia	20.00%	Indirect
22	Shuqaiq Water & Electricity Co.	Saudi Arabia	20.00%	Indirect
23	Tristar Holdings Limited	UAE	19.61%	Direct
24	Aviation Lease & Finance Co. (ALAFCO)	Kuwait	14.00%	Direct

* The shares in this associate are owned by GIC's subsidiary Bitumat

Principal Investing

Major Projects and Equity Participations

As of 31 December 2017

	Name of the Project	Location	GIC Effective holding %	GIC holding type
	Equity Participations			
1	Moobility Telecom International Holding Ltd.	British Virgin Islands	17.20%	Direct
2	TMK Gulf International Pipe Industry	Oman	14.20%	Direct
3	Ras Laffan Power Company Limited	Qatar	10.00%	Direct
4	Gulf Bridge International Inc.	Virgin Island	9.00%	Direct
5	KGL Logistics Company	Kuwait	5.43%	Direct
6	Securities and Investment Company	Bahrain	7.70%	Direct
7	Gulf Aluminium Rolling Mill Co.	Bahrain	5.90%	Direct
8	National Industrialization Co. (TASNEE)	Saudi Arabia	5.58%	Direct
9	Perella Weinberg Partners	USA	1.81%	Indirect

Corporate Directory 2017

Senior Management Team

Mr. Ibrahim Ali AlQadhi
Chief Executive Officer

Mr. Shafic Ali
Group Head of Principal Investment

Mr. Talal Al-Tawari
Group Head of Global Markets

Mr. Hani Al-Shakhs
Group Head of Support

Global Markets Group

Mr. Talal Al-Tawari
Acting Head of GCC Equities Div.

Mr. Osama Al-Musallam
Head of Treasury Div.

Mr. Fahad Al-Bader
Head of Managed Funds Div.

Mr. Raffaele Bertoni
Head of Debt Capital Markets Div.

Principal Investment Group

Mr. Fadi Twainy
Head of Light Industry Projects Div.

Mr. Meshary M. Al-Judaimi
Head of Financial Services & Utilities Div.

Mr. Faisal Al-Roomi
Head of Manufacturing Projects Div.

Mr. Mohammad Al-Fares
Head of Diversified Projects Div.

Mr. Meshari Al-Bader
Head of Principal Investment Analytics Div.

Support Group

Mr. Hani Al-Shakhs
Acting Head of Operations Div.

Mr. Mohammed Al-Jallal
Head of Human Resources Div.

Mr. Amer Al-Dakhail
Head of Information Technology Div.

Mr. Qais Al-Shatti
Head of Public Relations Dept.

Corporate Office

Mr. Fahad Al-Abdulkader
Head of BOD Secretariat Div.

Mr. Malek Al-Ajeel
Advisor to CEO

Mr. Pervaz Akthar
Acting Head of Risk Management Div.

Mr. Hazem El-Rafie
Head of Finance Div.

Dr. Khaled Bukhamseen
Head of Internal Audit Div.

Dr. Mohamed Elliwa
Head of Legal & Compliance Div.

Dr. Mohammad Al-Omar
Head of Research Div.

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