BANK ALKHAIR B.S.C. (c)

CONSOLIDATED FINANCIAL STATEMENTS

31 December 2012

Commercial registration	:	53462 (registered with the Central Bank of Bahrain as a wholesale Islamic bank).
Registered Office	:	4^{th} Floor Building No. 2304, Road 2830, Seef District 428 PO Box 31700, Manama, Kingdom of Bahrain
Directors	:	Yousef A. Al-Shelash, *Chairman* Hethloul Saleh Al-Hethloul Bader Abdulaziz Kanoo Abdullatif Abdullah Al-Shalash Ayman Abdullah Boodai Ayman Ismail Abudawood Abdulaziz Naif Al Orayer Ahmed Saleh Dehailan Adel Yousef Al Saqabi Khalil Nooruddin (w.e.f. 2 April 2012) Khalid Shaheen (w.e.f. 2 April 2012)
Chief Executive Officer	:	Khalil Nooruddin
Auditors	:	KPMG Fakhro, Bahrain

CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2012

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CHAIRMAN'S REPORT
for the year ended 31 December 2012

We are pleased to present the consolidated audited financial statements for the year ended December 2012, which was the Bank's ninth year of operation. The operating environment in 2012 remained challenging due to continued political and economic turmoil across regions worldwide – from the deterioration of the Eurozone debt crisis and the continued slow recovery in the US to the weaker than projected growth in emerging markets. In the Middle East, continued disruptions in the countries in transition constrained economic growth. These events had a marked impact on the global financial sector, draining investor confidence and constricting lending on the part of financial institutions.

In this challenging environment, we pursued a two pronged approach during the year to strengthen our operations and our overall business. On the one hand, we streamlined our operations in Bahrain and Turkey and devised a more focused business approach for both offices. On the other hand, we continued to build our operations in Saudi Arabia and Malaysia to support our business initiatives in both markets.

In Bahrain, Bank Alkhair consolidated its multi business lines to focus on one primary business function, namely the management of alternative assets. Bank Alkhair revised its Investment Banking strategy to focus on sourcing and structuring alternative investment opportunities in the MENA region and placing them with the Bank's client base in the GCC. This change in strategy will see the Bank generate recurring income from management fees and third party placements going forward.

During the year, Bank Alkhair's Investment Banking division actively engaged in managing and bolstering the performance of the Bank's portfolio investments, positioning them for continuous growth and profitable future exits. The Investment Banking team worked closely alongside the executive teams of the Bank's investee companies to strengthen the management and governance within the companies. This resulted in the completion of significant milestones in 2012, including the successful opening of Al Tajamouat Mall in Jordan, the expansion of Bahrain Financing Group's global branch network, the announcement of t'azur's expansion into Oman and Burj Bank's successful return to profitability after a three year loss making period. Accordingly, the Bank witnessed a substantial improvement in the performance of its portfolio assets, and recorded a 66% increase in profits from its share of associate activities, from US$6.4 million in 2011 to US$10.6 million in 2012.

Bank Alkhair also successfully exited its stake in Goknur Foods Import Export Trading and Production Co. (Goknur), generating a return of 20%. Goknur is one of the largest and fastest growing fruit juice and puree producers and the largest fruit juice concentrate exporter in Turkey.

In Turkey, we restructured our operations to complement our investment banking business function in Bahrain. This will further facilitate Alkhair Capital Turkey's (Alkhair Turkey's) mission of acting as a bridge for Middle Eastern capital seeking access to the Turkish market, one of the fastest growing economies in the world. With the support of Alkhair Turkey, our Investment Banking division commenced an active investment development plan in 2012 focused on the energy, food and real estate segments in the Turkish market.

In Saudi Arabia, we continued to invest in Alkhair Capital Saudi Arabia's resources and infrastructure to support its refocused business model, which was set in place in 2011. Alkhair Saudi's business model revolves around three core business lines: Asset Management, Investment Banking and Brokerage. This will see the growth of Alkhair Saudi's revenues in line with its business objectives over the coming years.

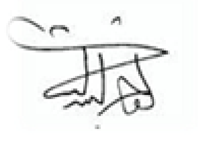
In Malaysia, we revised our strategy to focus on maintaining an optimal asset mix and generating further income from fee-based transactions. During the year, we repositioned our global Capital Markets division to operate out of our Malaysia subsidiary, Alkhair International Islamic Bank Berhad (Alkhair Malaysia). Accordingly, Alkhair Malaysia witnessed a 36.58% increase in net profit, from US$ 0.82 million in 2011 to US$1.12 million in 2012.This was mainly due to an increase in advisory fees generated by Alkhair Malaysia's Capital Markets division.

Despite the considerable progress Bank Alkhair and its subsidiaries made during the year, the Group reported a loss of US$39.8 million for the year ended 31 December 2012. This was primarily attributable to the conservative accounting methodology Bank Alkhair adopts towards the valuation of its portfolio assets. The loss was mainly due to a mark to market loss on one of the Bank's major investments in Al Tajamouat mall, an upscale shopping and entertainment complex in Amman, Jordan. Furthermore, the significant measures taken to strengthen the Bank's operations in Saudi Arabia and Malaysia as well as the reduced overall business activity as a result of the volatile operating environment in 2012 also contributed to the loss.

However, overall, we are pleased with the significant strides Bank Alkhair achieved during the year in terms of its business objectives. We believe that the important steps taken to turnaround the Bank's operations leave Bank Alkhair as well as its subsidiaries in a strong position to develop further business in the year ahead. Also, the substantial improvement in the valuation of the Bank's portfolio assets will see the Bank strategically exit a number of its investments over the coming years. We are confident that with the increase in business activity and the potential profitable exits, the Bank will return to profitability in 2013.

We would like to take this opportunity to welcome Mr. Khalil Nooruddin who officially joined the Bank in June 2012 as Managing Director and Chief Executive Officer. Mr. Nooruddin brings to the Bank in depth investment banking experience, gained over 35 years of serving international and regional institutions in an executive, board and advisory capacity. We would also like to welcome Mr. Khalid Shaheen, who joined the Bank's Board of Directors in April 2012. Mr. Shaheen has over 30 years of experience in the financial services sector and serves on the Boards of prominent financial institutions in Bahrain.

In closing, we would like to express our tremendous gratitude, as always, to all of our stakeholders for their continuous support and confidence in the Bank. We are also immensely grateful to the Central Bank of Bahrain for its invaluable guidance and support.



Yousef A. Al-Shelash
Chairman of the Board
28 February 2013

SHARI'AH SUPERVISORY BOARD REPORT TO THE SHAREHOLDERS OF BANK ALKHAIR B.S.C. (c)

Asslamo A'laikom WA Rahmatu Allah WA Barakatuh

In compliance with the terms of our letter of appointment, we are required to report as follows:

We have reviewed through the Shari'ah department and under our supervision the principles and the contracts relating to the transactions conducted by Bank Alkhair B.S.C. (c) ("the Bank") and its subsidiaries (together "the Group") during the year ended 31 December 2012. We have conducted our review with a view to form an opinion as to whether the Group has complied with rules and principles of Islamic Shari'ah and also with the specific fatwa's, rulings and guidelines issued by us.

The Group's management is responsible for ensuring that the Group conducts its business in accordance with the rules and principles of Islamic Shari'ah. It is our responsibility to form an independent opinion, based on our review of the operations of the Group, and to report this to you.

We conducted our review through the Shari'ah department and under our supervision which included examining, on a test basis, each type of transaction and the relevant documentation and procedures adopted by the Group. We planned and performed our review so as to obtain all the information and explanations that we considered necessary in order to provide us with sufficient evidence to give assurance that the Group has not violated any rules and principles of Islamic Shari'ah.

In our opinion:

a) The contracts, transactions and dealings entered into by the Group during the year ended 31 December 2012 are in compliance with the rules and principles of Islamic Shari'ah. Except the investment in Taj Mall project which the Shari'ah Board advised in a previous resolution to exit as soon as possible.

b) The allocation of profit and charging of losses relating to investment accounts conform to the basis that had been approved by us in accordance with Islamic Shari'ah rules and principles.

c) The Shari'ah Board advised the Bank's management that all earnings that have been realized from sources or by means prohibited by rules and principles of Islamic Shari'ah principles shall be disposed off and given to charity under the supervision of the Shari'ah Board.

d) The calculation of Zakah is in compliance with the rules and principles of Islamic Shari'ah.

We supplicate to Allah the Almighty to grant us success and a straight path.

Wa Asslamo A'laikom Wa Rahmatu Allah Wa Barakatuh.

Dr. Khalid Al Mathkoor
Chairman

28 February 2013

KPMG Fakhro
Audit
5th Floor
Chamber of Commerce Building
PO Box 710, Manama
Kingdom of Bahrain

CR No. 6220
Telephone +973 17 224807
Fax +973 17 227443
Internet www.kpmg.com.bh

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS
BANK ALKHAIR BSC (c)
Manama, Kingdom of Bahrain

28 February 2013

Report on the consolidated financial statements

We have audited the accompanying consolidated financial statements of Bank Alkhair BSC (c) (the "Bank") and its subsidiaries (together the "Group"), which comprise the consolidated statement of financial position as at 31 December 2012, and the consolidated income statement, the consolidated statement of changes in equity, the consolidated statement of cash flows and the consolidated statement of changes in restricted investment accounts for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Respective responsibilities of board of directors and auditors

These consolidated financial statements and the Group's undertaking to operate in accordance with Islamic Shari'ah rules and principles are the responsibility of the board of directors of the Bank. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

Basis of opinion

We conducted our audit in accordance with Auditing Standards for Islamic Financial Institutions issued by Accounting and Auditing Organisation for Islamic Financial Institutions. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

Opinion

In our opinion, the consolidated financial statements give a true and fair view of the financial position of the Group as at 31 December 2012, and of the consolidated results of its operations, its consolidated cash flows, consolidated changes in equity and consolidated changes in restricted investment accounts for the year then ended, in accordance with Financial Accounting Standards issued by the Accounting and Auditing Organisation for Islamic Financial Institutions and the Shari'a rules and principles as determined by the Shari'a Supervisory Board of the Bank.

Report on other regulatory requirements

As required by the Bahrain Commercial Companies Law and the Central Bank of Bahrain (CBB) Rule Book (Volume 2), we report that the Bank has maintained proper accounting records and the consolidated financial statements are in agreement therewith; the financial information contained in the chairman's report is consistent with the consolidated financial statements; we are not aware of any violations of the Bahrain Commercial Companies Law, the Central Bank of Bahrain and Financial Institutions Law, the CBB Rule Book (Volume 2, applicable provisions of Volume 6 and CBB directives), or the terms of the Bank's memorandum and articles of association having occurred during the year that might have had a material adverse effect on the business of the Bank or on its financial position; and satisfactory explanations and information have been provided to us by the management in response to all our requests.

KPMG

CONSOLIDATED STATEMENT OF FINANCIAL POSITION
As at 31 December

US$ 000's

	Note	31 December 2012	31 December 2011
ASSETS			
Cash and balances with banks	4	7,985	11,081
Placements with financial institutions		63,733	66,477
Financing receivables	5	86,623	95,838
Investment securities	6	112,905	130,383
Assets held-for-sale	7	18,932	2,560
Equity-accounted investees	8	106,006	114,952
Investment property	9	17,706	17,706
Other assets	10	25,988	38,552
Equipment		2,277	5,483
TOTAL ASSETS		**442,155**	483,032
LIABILITIES AND EQUITY			
LIABILITIES			
Due to financial institutions	11	153,121	143,178
Due to customers	12	68,176	88,483
Other liabilities	13	24,978	16,205
TOTAL LIABILITIES		**246,275**	247,866
EQUITY			
Share capital	14	207,862	207,862
Statutory reserve		337	337
Fair value reserve		114	(227)
Foreign currency translation reserve		(8,485)	(8,642)
(Accumulated losses) / retained earnings		(32,715)	4,153
Equity attributable to the shareholders of the parent		**167,113**	203,483
Non-controlling interests		28,767	31,683
TOTAL EQUITY (page 6)		**195,880**	235,166
TOTAL LIABILITIES AND EQUITY		**442,155**	483,032

The consolidated financial statements consisting of pages 4 to 50 were approved by the Board of Directors on 28 February 2013 and signed on its behalf by:

Yousef Abdullah Al-Shelash
Chairman

Hethloul Saleh Al-Hethloul
Board Member

The accompanying notes 1 to 35 form an integral part of these consolidated financial statements.

CONSOLIDATED INCOME STATEMENT
for the year ended 31 December 2012

US$ 000's

	Note	**2012**	2011
Finance income		8,742	9,687
Finance expense		(7,814)	(9,218)
Net finance income		**928**	469
Income from investment securities	15	(10,676)	8,265
Fees and commission	16	3,754	8,715
Share of profit of equity-accounted investees	8	10,575	6,444
Other income		709	2,191
Total income		**5,290**	26,084
Staff cost		19,080	25,319
Legal and professional expenses		13,394	2,154
Premises cost		2,848	3,506
Business development expenses		1,066	1,478
Depreciation		1,881	2,157
Other operating expenses		6,229	7,008
Total expenses		**44,498**	41,622
Loss for the year before Zakah and impairment		**(39,208)**	(15,538)
Provision for Zakah	17	(1,719)	(1,800)
Reversal of impairment	18	1,100	4,010
Loss for the year from continuing operations		**(39,827)**	(13,328)
Income from assets held-for-sale and discontinued operations		64	14,497
(Loss) / profit for the year		**(39,763)**	1,169
Attributable to:			
Shareholders of the parent		(36,868)	3,371
Non-controlling interests		(2,895)	(2,837)
Non-controlling interests relating to assets held-for-sale		-	635
		(39,763)	1,169

The accompanying notes 1 to 35 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
for the year ended 31 December 2012 US$ 000's

	Attributable to the shareholders of the parent							
2012	**Share Capital**	**Statutory reserve**	**Fair value reserve**	**Foreign currency translation reserve**	**Accumulated losses**	**Total**	**Non-controlling interests**	**Total equity**
As at 1 January 2012	207,862	337	(227)	(8,642)	4,153	203,483	31,683	235,166
Loss for the year	-	-	-	-	(36,868)	(36,868)	(2,895)	(39,763)
Foreign currency translation differences	-	-	-	417	-	417	(21)	396
Fair value changes	-	-	192	-	-	192	-	192
Share of changes in reserves of equity-accounted investees	-	-	149	(260)	-	(111)	-	(111)
Total recognised income and expense for the year	**-**	**-**	**341**	**157**	**(36,868)**	**(36,370)**	**(2,916)**	**(39,286)**
As at 31 December 2012	**207,862**	**337**	**114**	**(8,485)**	**(32,715)**	**167,113**	**28,767**	**195,880**

The accompanying notes 1 to 35 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY *(continued)*
for the year ended 31 December 2012 US$ 000's

2011	Attributable to the shareholders of the parent: Share capital	Share premium	Statutory reserve	Fair value reserve	Foreign currency translation reserve	Retained earnings	Total	Non-controlling interests	Non-controlling interests relating to assets held-for-sale	Total equity
As at 1 January 2011	215,578	141,708	15,580	(262)	(6,112)	(213,964)	152,528	34,605	15,273	202,406
Profit / (loss) for the year	-	-	-	-	-	3,371	3,371	(2,837)	635	1,169
Foreign currency translation differences	-	-	-	-	(2,577)	-	(2,577)	(85)	-	(2,662)
Fair value changes	-	-	-	235	-	-	235	-	-	235
Transfer on sale	-	-	-	(79)	-	79	-	-	-	-
Share of changes in reserves of equity-accounted investees	-	-	-	(121)	47	-	(74)	-	-	(74)
Total recognised income and expense for the year	-	-	-	35	(2,530)	3,450	955	(2,922)	635	(1,332)
Transfer to statutory reserve	-	-	337	-	-	(337)	-	-	-	-
Conversion of subordinated murabaha	50,000	-	-	-	-	-	50,000	-	-	50,000
Capital reduction	(57,716)	(141,708)	(15,580)	-	-	215,004	-	-	-	-
Disposal of subsidiaries	-	-	-	-	-	-	-	-	(15,908)	(15,908)
As at 31 December 2011	207,862	-	337	(227)	(8,642)	4,153	203,483	31,683	-	235,166

The accompanying notes 1 to 35 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS
for the year ended 31 December 2012 US$ 000's

	2012	2011
OPERATING ACTIVITIES		
(Loss) / profit for the year	(39,763)	1,169
Adjustments for:		
Provision for Zakah	1,719	1,800
Gain on sale of investment securities	(1,375)	(6,739)
Fair value changes in investment securities	13,386	(591)
Share of profit of equity-accounted investees	(10,575)	(6,444)
Income from assets held-for-sale	-	(14,497)
Other income	-	(2,481)
Depreciation and amortisation	1,881	2,157
Sukuk amortisation	(1,054)	(973)
Reversal of impairment	(1,100)	(4,010)
	(36,881)	(30,609)
Changes in:		
Financing receivables	9,215	135,086
Other assets	16,914	(22,454)
Due to financial institutions	(5,167)	(36,334)
Due to customers	(20,307)	2,288
Other liabilities	7,054	(6,718)
Proceeds from sale of investment securities	17,970	31,329
Purchase of investment securities	(13,000)	(34,619)
Net cash (used in) / generated from operating activities	**(24,202)**	37,969
INVESTING ACTIVITIES		
Purchase of equipment	(275)	(66)
Investments in equity-accounted investees	3,252	(7,394)
Disposal of assets held-for-sale	-	60,417
Net cash generated from investing activities	**2,977**	52,957
FINANCING ACTIVITIES		
Draw down of bank financing	15,110	-
Repayment of syndicated borrowing	-	(128,273)
Net cash generated from / (used in) financing activities	**15,110**	(128,273)
NET DECREASE IN CASH AND CASH EQUIVALENTS	**(6,115)**	(37,347)
Effect of exchange rate changes on cash and cash equivalents	275	(1,475)
Cash and cash equivalents at the beginning of the year	77,558	116,380
CASH AND CASH EQUIVALENTS AT THE END OF THE YEAR	**71,718**	77,558
Cash and cash equivalents comprise:		
Cash and balances with banks	7,985	11,081
Placements with financial institutions	63,733	66,477
	71,718	77,558

The accompanying notes 1 to 35 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN RESTRICTED INVESTMENT ACCOUNTS
for the year ended 31 December 2012 US$ 000's

2012	**At 1 January 2012**	**Deposit**	**Gross income**	**Wakil fee**	**Withdrawals**	**At 31 December 2012**
Wakala contract	3,604	-	91	(36)	(3,659)	**-**

2011	At 1 January 2011	Deposit	Gross income	Wakil fee	Withdrawals	At 31 December 2011
Wakala contract	-	23,602	758	(215)	(20,541)	3,604

The accompanying notes 1 to 35 form an integral part of these consolidated financial statements.

for the year ended 31 December 2012 US$ 000's

1. REPORTING ENTITY

Bank Alkhair B.S.C. (c) ("the Bank") was incorporated in the Kingdom of Bahrain and registered with the Ministry of Industry and Commerce under Commercial Registration No. 53462 on 29 April 2004 and operates under a wholesale Islamic banking license granted by the Central Bank of Bahrain (CBB). The Bank's registered office is at the 4th floor of Building No. 2304, Road No. 2830, Seef District 428, Manama, Kingdom of Bahrain.

The Bank and its subsidiaries (together referred to as "the Group") aim to provide a full range of investment banking products and services that are compliant with Shari'ah principles. The principal products and services offered by the Group are:

- financial advisory services;
- private equity, equity structuring, private placements and initial public offerings;
- facility structuring, restructuring and placement including project finance, securitisation and Sukuk;
- structuring and marketing of both open and closed end mutual funds as well as client portfolio management and brokerage services that aim to meet investor driven return and asset criteria;
- advisory and investment services for takaful (Islamic insurance) and retakaful (Islamic reinsurance) providers; and
- mergers and acquisitions, including deal sourcing, structuring, valuations and advisory.

Consolidated financial statements

The consolidated financial statements comprise the financial statements of the Bank and its subsidiaries.

The following are the principal subsidiaries of the Bank that are consolidated:

Subsidiary	Ownership	Year of incorporation	Country of incorporation	Principal activity
UIB Capital Inc.	100%	2004	USA	The main activity of UIB Capital Inc. was to monitor the performance of the acquired companies on behalf of the Bank and investors. The operations of UIB Inc. were closed in 2010 to focus on the Middle East and Levant regions.
Alkhair International Islamic Bank Malaysia Berhad	100%	2004	Malaysia	Alkhair International Islamic Bank Malaysia Berhad was established in 2004 to source investment opportunities in the Far East and monitor the performance of the acquired companies on behalf of the Bank and investors and to establish distribution channels for the Group. In 2007, Alkhair International Islamic Bank Malaysia Berhad was granted an investment banking license by Bank Negara Malaysia to carry out investment banking activity in currencies other than the Malaysian Ringgit.
Alkhair Capital Menkul Degerler A.S.	91.9%	2007	Turkey	The main activities of Alkhair Capital Menkul Degerler A.S. are to provide investment consultancy and asset management.
Alkhair Capital Saudi Arabia	53.4%	2009	Kingdom of Saudi Arabia	Alkhair Capital Saudi Arabia was incorporated in March 2009 and registered with Capital Markets Authority. Its principal activities are Asset Management, Corporate Finance & Investment banking and Brokerage.

The Bank has other special purpose entities (SPE's) holding companies and subsidiaries which are set up to supplement the activities of the Bank and its principal subsidiaries.

2. BASIS OF PREPARATION

(a) Statement of compliance

The consolidated financial statements have been prepared in accordance with Financial Accounting Standards ('FAS') issued by the Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI). In line with the requirement of AAOIFI and the CBB Rule Book, for matters that are not covered by FAS, the Group uses guidance from the relevant International Financial Reporting Standards ('IFRS').

(b) Basis of measurement

The consolidated financial statements have been prepared under the historical cost convention except for certain investment securities and investment properties carried at fair value. The consolidated financial statements are presented in United States Dollars (US$), being the functional currency of the Group's operations. All financial information presented in US$ has been rounded to the nearest thousands, except when otherwise indicated.

Going concern

The Bank's management has made an assessment of the Group's ability to continue as a going concern and is satisfied that the Group has the resources to continue in business for foreseeable future. The management is not aware of any material uncertainties that may cast significant doubt upon the Bank's ability to continue as a going concern, and accordingly, the consolidated financial statements have been prepared on a going concern basis.

(c) Basis of consolidation

(i) Subsidiaries

Subsidiaries are those enterprises (including special purpose entities) controlled by the Bank. Control exists when the Group has the power, directly or indirectly, to govern the financial and operating policies of an enterprise so as to obtain benefits from its activities. Subsidiaries are consolidated from the date on which control is transferred to the Group and de-consolidated from the date that control ceases.

Special purpose entities (SPEs) are entities that are created to accomplish a narrow and well-defined objective such as the securitisation of particular assets, or the execution of a specific borrowing or investment transaction. An SPE is consolidated if, based on an evaluation of the substance of its relationship with the Group and the SPE's risks and rewards, the Group concludes that it controls the SPE. The assessment of whether the Group has control over an SPE is carried out at inception and normally no further reassessment of control is carried out in the absence of changes in the structure or terms of the SPE, or additional transactions between the Group and the SPE. Where the Group's voluntary actions, such as lending amounts in excess of existing liquidity facilities or extending terms beyond those established originally, change the relationship between the Group and an SPE, the Group performs a reassessment of control over the SPE.

The Group in its fiduciary capacity also manages and administers assets held in trust and other investment vehicles on behalf of investors. The financial statements of these entities are not included in these consolidated financial statements except when the Group controls the entity. Information about the Group's fiduciary assets under management is set out in note 20.

Loss of control

Upon the loss of control, the Group derecognises the assets and liabilities of the subsidiary, any non-controlling interests and the other components of equity related to the subsidiary. Any surplus or deficit arising on the loss of control is recognised in the consolidated income statement. If the Group retains any interest in the previous subsidiary, then such interest is measured at fair value at the date that control is lost. Subsequently it is accounted for as an equity-accounted investee or in accordance with the Group's accounting policy for financial instruments depending on the level of influence retained.

2. BASIS OF PREPARATION *(continued)*

Non-controlling interests
Interests in the equity of subsidiaries not attributable to the parent are reported in consolidated statement of financial position as non-controlling interests. Profits or losses attributable to non-controlling interests are reported in the consolidated income statement as income attributable to non-controlling interests. Losses applicable to the non-controlling interests in a subsidiary are allocated to the non-controlling interests even if doing so causes the non-controlling interests to have a deficit balance.

The Group treats transactions with non-controlling interests as transactions with equity owners of the Group. For purchases from non-controlling interests, the difference between any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary is recorded in equity. Gains or losses on disposals to non-controlling interests are also recorded in equity.

When the Group ceases to have control or significant influence, any retained interest in the entity is remeasured to its fair value, with the change in carrying amount recognised in the consolidated income statement. The fair value is the initial carrying amount for the purposes of subsequently accounting for the retained interest as an associate, joint venture or financial asset. In addition, any amounts previously recognised in equity in respect of that entity are accounted for as if the Group had directly disposed of the related assets or liabilities. This may mean that amounts previously recognised in other equity are reclassified to the consolidated income statement.

(ii) Investment in associates (Equity-accounted investees)
Associates are those entities in which the Group has significant influence, but not control or joint control, over the financial and operating policies. Significant influence is presumed to exit when the Group holds between 20% and 50% of the voting power of another entity.

On initial recognition of an associate, the Group makes an accounting policy choice as to whether the associate shall be equity accounted or designated as at fair value through income statement. The Group makes use of the exemption in FAS 24 – *Investment in Associates* for venture capital organisation and designates certain of its investment in associates, as 'investments carried at fair value through income statement'. These investments are managed, evaluated and reported on internally on a fair value basis (refer to note 3 (b)).

If the equity accounting method is chosen for an associate, these are initially recognised at cost and the carrying amount is increased or decreased to recognise the investor's share of the profit or loss of the investees after the date of acquisition. Distributions received from an investee reduce the carrying amount of the investment. Adjustments to the carrying amount may also be necessary for changes in the investor's proportionate interest in the investees arising from changes in the investee's equity. When the Group's share of losses exceeds its interest in an equity-accounted investee, the Group's carrying amount is reduced to nil and recognition of further losses is discontinued except to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of the equity-accounted investees.

Any excess of the cost of acquisition over the Group's share of the net fair value of the identifiable assets, liabilities and contingent liabilities of an equity-accounted investee at the date of acquisition is recognised as goodwill, and included within the carrying amount of the investment. When the excess is negative, a bargain purchase gain is recognised immediately in the consolidated income statement.

If the ownership interest in an equity-accounted investee is reduced but significant influence is retained, only a proportionate share of the amounts previously recognised in equity is reclassified to the consolidated income statement where appropriate.

2. BASIS OF PREPARATION *(continued)*

(iii) Transactions eliminated on consolidation and equity accounting

Intra-group balances and transactions, and any unrealised gains or losses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Intra-group gains on transactions between the Group and its equity-accounted investees are eliminated to the extent of the Group's interest in the investees. Unrealised losses are also eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

The reporting period of the Group's subsidiaries and equity-accounted investees are identical and their accounting policies conform to those used by the Bank for like transactions and events in similar circumstances. The accounting policies of the subsidiaries and equity-accounted investees have been changed where necessary to ensure consistency with the policies adopted by the Group.

3. SIGNIFICANT ACCOUNTING POLICIES

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements, and have been applied consistently by Group entities.

a) Foreign currency transactions

Items included in the consolidated financial statements of the Group are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The consolidated financial statements are presented in US$, which is the Bank's functional and presentation currency.

Foreign currency transactions are translated using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the consolidated income statement. Translation differences on non-monetary items carried at their fair value, such as certain equity securities measured at fair value through equity, are included in investments fair value reserve.

Other group companies

As at the reporting date, the assets and liabilities of subsidiaries, equity-accounted investees and joint venture are translated into the Bank's functional currency at the rate of exchange prevailing at the reporting date, and their statements of income are translated at the average exchange rates for the year. Exchange differences arising on translation are taken directly to a separate reserve in equity. On disposal of a foreign entity, the deferred cumulative amount recognised in equity relating to that particular foreign operation is recognised in the consolidated income statement.

b) Investment securities

Investment securities comprise debt and equity instruments, but exclude investment in subsidiaries and equity-accounted investees (note 2 (c ii)).

(i) Classification

The Group segregates its investment securities into debt-type instruments and equity-type instruments.

Debt-type instruments

Debt-type instruments are investments that provide fixed or determinable payments of profits and capital. Investments in debt-type instruments are classified in the following categories:

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

b) Investment securities (continued)

At fair value through income statement (FVTIS)
These investments are either not managed on contractual yield basis or designated on initial recognition at FVTIS to avoid any accounting mismatch that would arise on measuring the assets or liabilities or recognising the gains or losses on them on different bases. Currently, the Group does not have any investment under this category.

At amortised cost
This classification is for debt-type instruments which are not designated as FVTIS and are managed on contractual yield basis. These include investments in medium to long-term sukuk.

Equity-type instruments
Equity-type instruments are investments that do not exhibit features of debt-type instruments and include instruments that evidence a residual interest in the assets of an entity after deducting all its liabilities. Investments in equity type instruments are classified in the following categories:

At fair value through income statement (FVTIS)
Equity-type instruments classified and measured at FVTIS include investments held-for-trading or designated on initial recognition at FVTIS.

Investments are classified as held-for-trading if acquired or originated principally for the purpose of generating a profit from short-term fluctuations in price or dealers margin or that form part of a portfolio where there is an actual pattern of short-term profit taking. The Group currently does not have any of its investments classified as investments held-for-trading purposes.

On initial recognition, an equity-type instrument is designated as FVTIS only if the investment is managed and its performance is evaluated and reported on internally by the management on a fair value basis. This category currently includes investment in private equity, funds and investment in associates (refer note 2 (c) (ii))

At fair value through equity (FVTE)
Equity-type instruments other than those designated at FVTIS are classified as at fair value through equity. This category includes investment in unquoted equity securities.

(ii) Recognition and de-recognition
Investment securities are recognised at the trade date i.e. the date that the Group contracts to purchase or sell the asset, at which date the Group becomes party to the contractual provisions of the instrument. Investment securities are derecognised when the rights to receive cash flows from the financial assets have expired or where the Group has transferred substantially all risk and rewards of ownership.

(iii) Measurement
Investment securities are measured initially at fair value, which is the value of the consideration given. For investments carried at FVTIS transaction costs are expensed in the consolidated income statement. For other investment securities, transaction costs are included as a part of the initial recognition.

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

b) Investment securities (continued)

Subsequent to initial recognition, investments carried at FVTIS and FVTE are re-measured to fair value. Gains and losses arising from a change in the fair value of investments carried at FVTIS are recognised in the consolidated income statement in the period in which they arise. Gains and losses arising from a change in the fair value of investments carried at FVTE are recognised in the consolidated statement of changes in equity and presented in a separate fair value reserve within equity.

When the investments carried at FVTE are sold, impaired, collected or otherwise disposed of, the cumulative gain or loss previously recognised in the statement of changes in equity is transferred to the consolidated income statement.

Investments carried at FVTE where the entity is unable to determine a reliable measure of fair value on a continuing basis, such as investments that do not have a quoted market price or where there are no other appropriate methods from which to derive reliable fair values, are stated at cost less impairment allowances.

Subsequent to initial recognition, debt-type investments other than those carried at FVTIS are measured at amortised cost using the effective profit method less any impairment allowances.

(iv) Measurement principles

Amortised cost measurement

The amortised cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus capital repayments, plus or minus the cumulative amortisation using the effective profit method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment. The calculation of the effective profit rate includes all fees and points paid or received that are an integral part of the effective profit rate.

Fair value measurement

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction on the measurement date.

The Group measures the fair value of quoted investments using the market bid-prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm's length basis.

If a market for a financial instrument is not active or the instrument is not quoted, the Group establishes fair value using a valuation technique. Valuation techniques include using recent arm's length transactions between knowledgeable, willing parties (if available), discounted cash flow analyses and other valuation models with accepted economic methodologies for pricing financial instruments.

c) Financing receivables

Financing receivables comprise shari'ah compliant financing contracts with fixed or determinable payments. These include financing provided through Murabaha contracts. Financing assets are recognised on the date at which they are originated and are carried at their amortised cost.

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

d) Placements with financial institutions

These comprise inter-bank placements made using Shari'ah compliant contracts. Placements are usually for short-term and are stated at their amortised cost.

e) Due to financial institutions

These comprise funds payable to financial institutions received using Shari'ah compliant contracts. Due to financial institutions are stated at their amortised cost.

f) Due to customers

These comprise funds payable to corporate customers received using Shari'ah compliant contracts. Due to customers are stated at their amortised cost.

g) Impairment of assets

The Group assesses at each reporting date whether there is objective evidence that a specific financial asset or a group of financial assets may be 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 have occurred after the initial recognition of the asset (an incurred "loss event") and that the loss event(s) have an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated.

Financial assets carried at amortised cost

For financial assets carried at amortised cost impairment is measured as the difference between the carrying amount of the financial assets and the present value of estimated cash flows discounted at the assets' original effective profit rate. Losses are recognised in consolidated income statement and reflected in an allowance account. When a subsequent event causes the amount of impairment loss to decrease, the impairment loss is reversed through the consolidated income statement. The Group considers evidence of impairment for financial assets carried at amortised cost at both a specific asset and collective level. All individually significant financial assets are assessed for specific impairment. All individually significant financial assets found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Financial assets that are not individually significant are collectively assessed for impairment by grouping together assets with similar risk characteristics.

Investments carried at fair value through equity (FVTE)

In the case of investments in equity securities classified as FVTE, a significant or prolonged decline in the fair value of the security below its cost is an objective evidence of impairment. If any such evidence exists for FVTE investments, the unrealised re-measurement loss shall be transferred from equity to the consolidated income statement.

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 income statement is removed from equity and recognised in the consolidated income statement. Impairment losses recognised in the consolidated income statement on equity instruments are subsequently reversed through equity.

For FVTE investments carried at cost less impairment due to the absence of reliable fair value, the Group makes an assessment of whether there is an objective evidence of impairment for each investment by assessment of financial and other operating and economic indicators. Impairment is recognised if the estimated recoverable amount is assessed to be below the cost of the investment.

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

g) Impairment of assets (continued)

Non-financial assets
The carrying amount of the Group's assets or its cash generating unit, other than financial assets carried at amortised cost and investments carried at FVTE, are reviewed at each reporting date to determine whether there is any indication of impairment. A cash generating unit is the smallest identifiable asset group that generates cash flows that largely are independent from other asset and groups. If any such indication exists, the asset's recoverable amount is estimated. The recoverable amount of an asset or a cash generating unit is the greater of its value in use or fair value less costs to sell.

In assessing value in use, the estimated future cash flows are discounted to their present value using a discount rate that reflects current market assessments of expected return and the risks specific to the asset or cash generating unit. An impairment loss is recognised whenever the carrying amount of an asset or its cash generating unit exceeds its estimated recoverable amount. Impairment losses are recognised in the consolidated income statement. Impairment losses are reversed only if there is an indication that the impairment loss may no longer exist and there has been a change in the estimates used to determine the recoverable amount. Separately recognised goodwill is not amortised and is tested annually for impairment and carried at cost less accumulated impairment losses. Impairment losses on separately recognised goodwill are not reversed.

h) Investment property
Investment property is investments that earn rental income and/or are expected to benefit from capital appreciation. Investment properties are measured initially at cost, including transaction costs. Subsequent to initial recognition, investment properties are stated at fair value, which reflects market conditions at the reporting date. Gains or losses arising from changes in the fair values of investment properties are included in the consolidated income statement in the period in which they arise.

Investment properties are derecognised when they have been disposed of or when the investment property is permanently withdrawn from use and no future economic benefit is expected from its disposal. Any gains or losses on the retirement or disposal of an investment property are recognised in the consolidated income statement in the year of retirement or disposal.

i) Equipment
Equipment includes computers, office equipment, fixtures and fittings. Equipment is recorded at cost less accumulated depreciation. Depreciation is computed using the straight-line method to write-off the cost of the assets over their estimated useful lives ranging from 1 to 8 years. The assets residual values and useful lives are reviewed, and adjusted if appropriate, at each reporting date.

j) Assets held-for-sale and discounted operations
i) Classification
The Group classifies non-current assets or disposal groups as held-for-sale if its carrying amount is expected to be recovered principally through a sale transaction rather than through continuing use within twelve months. A disposal group is a group of assets to be disposed of, by sale or otherwise, together as a group in a single transaction, and liabilities directly associated with those assets that will be transferred in the transaction. A subsidiary acquired exclusively with a view to resale is classified as disposal group held-for-sale and income and expense from its operations are presented as part of discontinued operation.

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

j) Assets held-for-sale and discounted operations (continued)

If the criteria for classification as held for sale are no longer met, the entity shall cease to classify the asset (or disposal group) as held for sale and shall measure the asset at the lower of its carrying amount before the asset (or disposal group) was classified as held-for-sale, adjusted for any depreciation, amortisation or revaluations that would have been recognised had the asset (or disposal group) not been classified as held-for-sale and its recoverable amount at the date of the subsequent decision not to sell.

Any impairment loss on a disposal group is allocated first to goodwill, and then to the remaining assets and liabilities on a pro rata basis, except that no loss is allocated to financial assets and investment property carried at fair value, which continue to be measured in accordance with the Group's other accounting policies. Impairment losses on initial classification as held-for-sale and subsequent gains and losses on remeasurement are recognised in the consolidated income statement. Gains are not recognised in excess of any cumulative impairment loss.

ii) Measurement

Non-current assets or disposal groups classified as held for sale, other than financial instruments, are measured at the lower of its carrying amount and fair value less costs to sell. Financial instruments that are non-current assets and 'held-for-sale' continue to be measured in accordance with their stated accounting policies. On classification of equity-accounted investee as held-for-sale, equity accounting is ceased at the time of such classification as held-for-sale.

iii) Discounted operations

A discontinued operation is a component of the Group's business, the operations and cash flows of which can be clearly distinguished from the rest of the Group and which:

- represents a separate major line of business or geographical area of operations;
- is part of a single co-ordinated plan to dispose of a separate major line of business or geographical area of operations; or
- is a subsidiary acquired exclusively with a view to re-sale.

Classification as a discontinued operation occurs on disposal or when the operation meets the criteria to be classified as held-for-sale, if earlier. When an operation is classified as a discontinued operation, the comparative consolidated income statement is re-presented as if the operation had been discontinued from the start of the comparative year.

k) Restricted investment accounts

Restricted investment accounts represent funds received by the Group from third parties for investment in specified products as directed by the investment account holders. These assets are managed in a fiduciary capacity and the Group has no entitlement to these assets. Clients bear all of the risks and earn all of the rewards on these investments. Restricted investments are not included in the consolidated statement of financial position since the Group does not have the right to use or dispose these investments except within the conditions of the contract between the Group and holders of restricted investment accounts.

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

l) Revenue Recognition (continued)

l) Revenue recognition

Revenue is recognised when it is probable that future economic benefits will flow to the Group and the amount of the revenue can be reliably measured. Revenue earned by the Group and gain / loss on assets are recognised on the following basis:

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

Gain / (loss) on sale of investment securities (realised gain / (loss)) is recognised on trade date at the time of decongestion of the investment securities. The gain or loss is the difference between the carrying value on the trade date and the consideration receive or receivable.

Fair value gain / (loss) on investment securities (unrealised gain or loss) is recognised on each measurement date in accordance with the accounting policy for equity-type instruments carried at fair value through income statement (refer note 3 d).

Sukuk Income comprises the coupon profit on Sukuk and realised gain or loss on the sale of Sukuk. The coupon profit is recognised through the effective profit rate in accordance with the accounting policy for debt-type instrument carried at amortised costs (refer to 3 b). Realised gain or loss on sale of Sukuk is recognised on trade date at the time of de-recognition of the Sukuk. The gain or loss is the difference between the carrying value on the trade date and the fair value of consideration received or receivable.

Fees and Commission represents advisory fees, arrangement fees, management fees and brokerage fees. Fees and Commission is recognised at the fair value of consideration received or receivable and when the service is provided and income is earned. This is usually when the Group has performed all significant acts in relation to a transaction and it is highly probable that the economic benefits from the transaction will flow to the Group. Significant acts in relation to a transaction are determined based on the terms for each transaction.

Finance income and expense

Finance income and expense is recognised on a time apportioned basis over the period of the shari'ah complaint contracts based on effective profit rate.

m) Employee benefits

(i) Short-term benefits

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided. A provision is recognised for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

(ii) Post-employment benefits

Pensions and other social benefits for local employees are covered by the Social Insurance Organisation scheme, which is a "defined contribution scheme" in nature, and to which employees and employers contribute monthly on a fixed-percentage-of-salaries basis. Contributions by the Group are recognised as an expense in the consolidated income statement when they are due. Termination benefits are recognised as an expense when the Group is committed demonstrably, without realistic possibility of withdrawal, to a formal detailed plan to either terminate employment before the normal retirement date, or to provide termination benefits as a result of an offer made to encourage voluntary redundancy.

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

(ii) Post-employment benefits (continued)

Certain employees on fixed contracts are also entitled to leaving indemnities payable, based on length of service and final remuneration. Provision for this unfunded commitment has been made by calculating the notional liability had all employees left at the reporting date. These benefits are in the nature of "defined benefit scheme" and any increase or decrease in the benefit obligation is recognised in the consolidated income statement.

n) Earnings prohibited by Shari'ah

The Bank is committed to avoid recognising any income generated from non-Islamic sources. Accordingly, all non-Islamic income is credited to a charity account where the Bank uses these funds for charitable purposes.

o) Zakah

The Bank is not obliged to pay Zakah on behalf of its shareholders. However, the Bank is required to calculate and notify individual shareholders of their pro-rata share of the Zakah payable amount.

p) Provision for Zakah

Provision for Zakah represents Zakah from operation in Kingdom of Saudi Arabia and computed in accordance with Saudi Arabia Zakah regulations.

q) Offsetting of financial instruments

Financial instruments comprise of financial assets and financial liabilities. Financial assets include cash and balances with banks, placements with financial institutions, financing receivables, investment securities and other assets. Financial liabilities include due to financial institutions, due to customers, other liabilities and financial guarantees.

Financial assets and financial liabilities are only offset and the net amounts reported in the consolidated statement of financial position when there is a legally enforceable right to set off the recognised amounts and the Group intends to either settle these on a net basis, or intends to realise the asset and settle the liability simultaneously.

r) Statutory reserve

The Bahrain Commercial Companies Law 2001 requires that 10 percent of the annual net profit be appropriated to a statutory reserve which is normally distributable only on dissolution. Appropriations may cease when the reserve reaches 50 percent of the paid up share capital.

s) Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. A provision for restructuring is recognised when the Group has approved a detailed and formal restructuring plan, and the restructuring either has commenced or has been announced publicly. Future operating losses are not provided for.

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

t) Contingent liabilities and contingent assets

Contingent liabilities are not recognised in the financial statements, but are disclosed unless the possibility of an outflow of resources embodying economic benefits is probable. Contingent assets are not recognised in the financial statements, but are disclosed when an inflow of economic benefits is probable.

u) Financial guarantees

Financial guarantees are contracts that require the Group to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument. Financial guarantee liabilities are recognised initially at their fair value, and the initial fair value is amortised over the life of the financial guarantee. The financial guarantee liability is subsequently carried at the higher of this amortised amount and the present value of any expected payment when a payment under the guarantee has become probable.

v) Leases

Payments under operating lease are recognised in the consolidated income statement on a straight line basis over the term of the lease. Lease incentives are recognised as an integral part of the total lease expense, over the term of the lease.

w) Onerous contracts

A provision for onerous contracts is recognised when the expected benefits to be derived by the Group from the contract are lower than the unavoidable cost of meeting its obligations under the contract. The provision is measured at the present value of the lower of the expected cost of terminating the contract and the expected net cost of continuing with the contract.

x) Trade date accounting

All "regular way" purchases and sales of financial assets are recognised on the trade date, i.e. the date that the Group commits to purchase or sell the asset.

y) Cash and cash equivalents

For the purpose of consolidated statement of cash flows, cash and cash equivalents comprise cash in hand, bank balances and placements with financial institutions with maturities of three months or less from the acquisition date that are subject to insignificant risk of changes in fair value and are used by the Group in the management of its short-term commitments.

z) Critical accounting estimates and judgements

The Group makes estimates and assumptions that effect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectation of future events that are believed to be reasonable under the circumstances.

Judgements

(i) Classification of investments

In the process of applying the Group's accounting policies, management decides on acquisition of an investment whether it should be classified as investments at fair value through income statement or investments carried at fair value through equity or investments carried at amortised cost. The classification of each investment reflects the management's judgement in relation to its strategy for each investment and is subject to different accounting treatments based on such classification [note 3 (b)].

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

z) Critical accounting estimates and judgements (continued)

(ii) Special purpose entities

The Group sponsors the formation of special purpose entities (SPE's) primarily for the purpose of allowing clients to hold investments. The Group provides corporate administration, investment management and advisory services to these SPE's, which involve the Group making decisions on behalf of such entities. The Group administers and manages these entities on behalf of its clients, who are by and large third parties and are the economic beneficiaries of the underlying investments. The Group does not consolidate SPE's that it does not have the power to control.

In determining whether the Group has the power to control an SPE, judgements are made about the objectives of the SPE's activities, its exposure to the risks and rewards, as well as about the Group intention and ability to make operational decisions for the SPE and whether the Group derives benefits from such decisions.

Estimations

(i) Fair value of financial instruments

Where the fair values of financial assets and financial liabilities cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The inputs to these models are derived from observable market data where possible, but where observable market data are not available, judgment is required to establish fair values. The judgments include considerations of inputs such as liquidity risk, credit risk and volatility for discount rates.

Fair value is determined for each investment individually in accordance with the valuation policies set out below:

- For investment that is actively traded in an active and liquid market, fair value is determined by reference to the quoted market price prevailing on the reporting date;
- For investment in unquoted equity securities, the Bank establishes fair value by using valuation techniques. Valuation techniques include using recent arm's length market transactions between knowledgeable, willing parties, if available, reference to the current fair value of another instrument that is substantially the same and discounted cash flow analysis; and
- Investments in funds or similar investment entities are carried at the latest net asset valuation provided by the fund administrator.

The impact on fair value of financial instruments measured at fair value for changes in key assumptions is given in note 19.

(ii) Impairment of financing receivables

Each counterparty exposure is evaluated individually for impairment and is based upon management's best estimate of the present value of the cash flows that are expected to be received. In estimating these cash flows, management makes judgements about a counterparty's financial situation and the net realisable value of any underlying assets/ collaterals. Each impaired asset is assessed on its merits, and the workout strategy and estimate of cash flows considered recoverable are independently evaluated by the Risk Management Department. All individually significant financing receivables are tested for specific impairment. Those found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Financing receivables that are not individually significant are collectively assessed for impairment by grouping together assets with similar risk characteristics.

3. Significant accounting polices (continued)

z) Critical accounting estimates and judgements (continued)

(ii) Impairment of financing receivables (continued)

In assessing collective impairment, the Group uses historical trends of the probability of default, the timing of recoveries and the amount of loss incurred, adjusted for management's judgement as to whether current economic and credit conditions are such that the actual losses are likely to be greater or lesser than suggested by historical trends.

An impairment loss in respect of a financing receivables measured at amortised cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the asset's original effective profit rate. Losses are recognised in profit or loss and reflected in an allowance account against financing receivable.

Profit on the impaired asset does not continue to be recognised. When an event occurring after the impairment was recognised causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through consolidated income statement.

(iii) Fair value of investment property

The Group conducts valuation of its investment property periodically using external independent valuers. The fair value is determined based on the market value of the property through the comparable method, analysing the land rates in the vicinity for similar assumed zoning regulations. The Group's investment property is situated in Bahrain. Given the dislocation in the local property market and infrequent property transactions it is reasonably possible, based on existing knowledge, that the current determination of fair value could require a material adjustment to the carrying amount of these assets within the next financial year due to significant changes in assumptions underlying such assessments.

(iv) Impairment of cash generating units

Cash generating units include the Group's investments in certain subsidiaries and equity-accounted investees that generate cash flows that are largely independent from other assets and activities of the Group. The basis of impairment assessment for such cash generating units is described in accounting policy 3 (g). For equity-accounted investees with indicators of impairment, the recoverable amounts have been determined based on higher of fair value less costs to sell or value in use.

Value in use for the equity-accounted investees was determined by discounting the future cash flows expected to be generated from continuing operations, comparison to similar instruments for which market observable prices exist and other valuation models.

The objective of valuation techniques is to arrive at a fair value determination that reflects the price of the financial instrument at the reporting date that would have been determined by market participants acting at arm's length. Fair value less costs to sell of certain cash generating units is based on indicative offer prices received by the Group.

Key assumptions used in the calculation of value in use were the following: cash flows were projected based on 3-5 year business plans, after ensuring consistency with historical operating results and forecasted economic growth rates for mature companies. Terminal growth rates were determined based on the IMF's forecast GDP growth rate in 5 years' time. The forecast period is based on the Group's long term perspective with respect to the operations of these CGU's.

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3. Significant accounting polices (continued)

z) Critical accounting estimates and judgements (continued)

(iv) Impairment of cash generating units (continued)

Discount rates were based on a CAPM formula, with the risk-free rate obtained from the yield on 10-year bonds issued by the government in the relevant market and in the same currency as the cash flows, adjusted for a risk premium to reflect both the increased risk of investing in equities generally, as well as liquidity and control factors. The key assumptions described above may change as economic and market conditions change.

4. CASH AND BALANCES WITH BANKS

	31 December 2012	31 December 2011
Cash on hand	19	20
Balances with banks	7,966	11,061
	7,985	11,081

5. FINANCING RECEIVABLES

	31 December 2012	31 December 2011
Gross murabaha receivables	87,735	97,695
Less: Deferred profits	(862)	(1,857)
Less: Collective impairment allowances	(250)	-
	86,623	95,838

Financing receivables comprise due from customers under murabaha financing contracts. The average profit on these balances during the year was 7.6% per annum (2011: 6.6% per annum).

6. INVESTMENT SECURITIES

	31 December 2012	31 December 2011
Equity type instruments		
At fair value through income statement:		
- Quoted equity securities	23,691	38,896
- Unquoted equity securities *	32,771	32,994
- Unquoted funds *	28,397	27,150
- Quoted funds	1,983	1,495
	86,842	100,535
At fair value through equity:		
- Unquoted equity securities **	-	6,452
Total equity type investments	**86,842**	106,987
Debt type instruments		
At amortised cost:		
- Sukuk	26,063	23,396
	112,905	130,383

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6. INVESTMENT SECURITIES (continued)

* Unquoted equity securities and unquoted funds carried at fair value through income statement primarily comprise assets managed by the Group. These investments are carried at fair value determined based on valuation techniques. During the year, the Group recognised a net fair value gain of US$ 1.4 million (31 December 2011: fair value gain of US$ 0.6 million) on these investments.

****** Unquoted equity securities at fair value through equity comprise investment in private equity managed by external investment manager. The investment is carried at cost less impairment allowances in the absence of a reliable measure of fair value. During the year, the Group recognised an impairment loss of US$ 1.7 million (31 December 2011: US$ 2.8 million) on investments carried at FVTE.

The Group intends to exit this investment principally by means of private placements, strategic buy outs, sale of underlying assets or through initial public offerings.

Movement on Investments carried at fair value through income statement as follows:

	At 1 January 2012	Additions during the year	Disposals during the year	Foreign exchange changes	Fair value changes	**At 31 December 2012**
Investment in associates	97,201	-	(163)	-	(13,729)	83,309
Quoted funds	1,495	-	(8)	153	343	1,983
Equity investments (< than 20% stake)	1,839	-	(289)	-	-	1,550
	100,535	**-**	**(460)**	**153**	**(13,386)**	**86,842**

Movement on Investments carried at fair value through equity as follows:

	At 1 January 2012	Additions during the year	Disposals during the year	Foreign exchange changes	Fair value changes	Impairment	**At 31 December 2012**
Equity investments (< than 20% stake)	6,452	-	(5,000)	-	198	(1,650)	-
	6,452	**-**	**(5,000)**	**-**	**198**	**(1,650)**	**-**

7. ASSETS HELD-FOR-SALE

Assets held-for-sale represents investment in Burj Bank Limited, an equity-accounted investee, for which the Group has active plan to sell in the foreseeable future (refer note 8). During the year the Group has reclassified its stake in Burj Bank Limited as held-for-sale pursuant to the sale agreement entered into by the Bank with a prospective buyer.

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8. EQUITY-ACCOUNTED INVESTEES

	31 December 2012	31 December 2011
BFC Group Holdings Ltd.	93,205	89,102
t'azur Company B.S.C. (c)	12,801	9,515
Burj Bank Limited	16,372	18,895
	122,378	117,512
Less: reclassified to assets held-for-sale (note 7)	(16,372)	(2,560)
	106,006	114,952

The Bank has 43.36% stake (2011: 44.88%) in BFC Group Holdings Ltd. ("BFC"), a company incorporated in the United Arab Emirates. BFC is a holding company of group money changers in different jurisdictions. BFC is engaged in buying and selling foreign currencies and traveller's cheques, handling of remittance business and provision of other exchange house services in both local and foreign currencies.

The Bank has 25.86% stake (2011: 25.86%) in t'azur B.S.C. (c), an unlisted regional takaful company incorporated in the Kingdom of Bahrain. The equity-accounted investee has a commitment to provide a qard hassan loan to the extent of the accumulated deficit in the participants' fund of US$ 25.9 million at 31 December 2012 (2011: US$ 21.2 million). The Group's share of the commitment is US$ 6.7 million (2011: US$ 5.5 million)

The Bank has 36.9% stake (2011: 36.9%) in Burj Bank Limited, an unlisted Islamic commercial bank in Pakistan. The Bank has an active plan to sell all its stake in the investment and accordingly, this has been classified as assets held-for-sale (refer to note 7).

The movement on equity-accounted investees is as follows:

	2012	2011
At 1 January	114,952	104,745
Acquisitions during the year	-	7,393
Share of profits of equity-accounted investees	10,575	6,444
Share of reserves of equity-accounted investees	103	(1,070)
Transferred to assets held-for-sale (note 7)	(16,372)	(2,560)
Dividends received	(3,252)	-
At 31 December	**106,006**	114,952

Summarised financial information of associates that have been equity accounted not adjusted for the percentage ownership held by the Group (based on most recent audited financial statements / most recent management accounts):

	2012	2011
Assets	324,670	614,865
Liabilities	(79,164)	(310,865)
Revenue	66,853	63,485
Profit for the year	19,428	12,600

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9. INVESTMENT PROPERTY

Investment property comprises a plot of vacant land in the Kingdom of Bahrain. The fair value of this investment property as at 31 December 2012 has been determined by accredited independent valuers using comparable recent market transactions on arm's length terms. The investment property is mortgaged to a financial institution as security for a financing facility (refer note 11).

10. OTHER ASSETS

	31 December 2012	31 December 2011
Advance for purchase of investments	7,145	14,163
Fees and expenses recoverable	4,314	6,293
Prepayments and advances	1,353	1,662
Receivable from sale of investment securities	11,900	19,904
Others	5,044	5,298
	29,756	47,320
Less: Provision for impairment		
Fee and expenses recoverable	-	(5,000)
Others	(3,768)	(3,768)
	25,988	38,552

11. DUE TO FINANCIAL INSTITUTIONS

	31 December 2012	31 December 2011
Placements from financial institutions	138,011	143,178
Bank financing	15,110	-
	153,121	143,178

Bank financing represents financing for one year obtained from a financial institution during the year secured by a mortgage over the Group's investment property and carries a profit rate of 5.5% per annum. The facility was repaid on 14 February 2013 (refer note 9).

The average profit rate on placements from financial institutions was 3.81% per annum (2011: 3.99% per annum).

12. DUE TO CUSTOMERS

This includes deposits from corporate customers on Wakala basis mainly raised by Alkhair International Bank Malaysia Berhad with maturities ranging from 3 months to 1 year (2011: 1 month to 1 year) and carries an average profit rate of 2.74% per annum (2011: 3.12% per annum).

13. OTHER LIABILITIES

	31 December 2012	31 December 2011
Provision for legal and professional expenses	6,800	-
Accruals and other provisions	1,564	1,120
Restructuring provision	419	2,105
Deal-related payables	4,740	4,919
Staff-related payables	2,240	2,710
Trade and other payables	9,215	5,351
	24,978	16,205

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14. SHARE CAPITAL

	31 December 2012	31 December 2011
Authorised:		
750,000,000 (2011: 750,000,000) ordinary shares of US$1 each	750,000	750,000
Issued and fully paid up:		
186,070,234 (2011: 186,070,234) ordinary shares of US$1 each, issued against cash	186,070	186,070
20,371,807 (2011: 20,371,807) ordinary shares of US$1 each, issued in kind	20,372	20,372
1,419,873 (2011: 1,419,873) ordinary shares of US$1 each, granted to employees	1,420	1,420
	207,862	207,862

15. INCOME FROM INVESTMENT SECURITIES

	2012	2011
Dividend income	28	21
Fair value (loss) / gain on investment securities carried at FVTIS	(13,386)	591
Gain on sale of investment securities carried at FVTE	1,011	4,838
Gain on sale of investment securities carried at FVTIS	282	273
Sukuk Income		
- Sukuk profit	1,307	914
- Gain on sale of sukuk	82	1,628
	(10,676)	8,265

16. FEES AND COMMISSION

	2012	2011
Advisory fees	75	3,988
Arrangement fees	1,135	1,944
Management fees	2,170	2,783
Brokerage fees	374	-
	3,754	8,715

17. PROVISION FOR ZAKAH

Provision for Zakah represents the Zakah from operations of Alkhair Capital Saudi Arabia, calculated in accordance with the Zakah Regulations of the Kingdom of Saudi Arabia.

18. REVERSAL OF IMPAIRMENT

	2012	2011
Impairment allowance on:		
Investment carried at fair value through equity	(1,650)	(2,837)
Financing receivables	(250)	-
Equipment	(2,000)	-
Reversal of impairment allowance on:		
Financing receivables	-	1,511
Other assets	5,000	5,336
	1,100	4,010

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19. FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair value is the amount for which an asset could be exchanged or a liability settled between knowledgeable and willing parties in an arm's length transaction.

Fair value of quoted securities are derived from quoted market prices in active markets, if available. In case of unquoted securities, the fair value is estimated using appropriate valuation techniques. Such techniques may include using recent arm's length market transactions; reference to the current fair value of another instrument that is substantially the same; discounted cash flow analysis or other valuation models.

The fair values of unquoted funds are based on net asset values which are determined by the fund manager using the quoted market prices of the underlying assets, if available, or other acceptable methods such as a recent price paid by another investor, the market value of a comparable company or other proprietary valuation models.

The fair values of other financial instruments on the consolidated statement of financial position are not significantly different from the carrying values included in the consolidated financial statements.

The Group uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

Level 1 quoted (unadjusted) prices in active markets for identical assets or liabilities;

Level 2 other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly; and

Level 3 techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

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

31 December 2012	**Level 1**	**Level 2**	**Level 3**	**Total**
Investments carried at fair value through income statement	23,691	30,380	32,771	86,842
Investments carried at fair value through equity	-	-	-	-
	23,691	**30,380**	**32,771**	**86,842**

31 December 2011	Level 1	Level 2	Level 3	Total
Investments carried at fair value through income statement	39,119	28,645	32,771	100,535
Investments carried at fair value through equity	-	5,000	-	5,000
	39,119	33,645	32,771	105,535

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19. FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

Movements in level 3 financial instruments
The following table shows the reconciliation of the opening and closing amount of Level 3 financial assets which are recorded at fair value:

	At 1 January 2012	**Total losses recorded in consolidated income statement**	**Total gains recorded in equity**	**Purchases**	**Sales/ transfers**	**At 31 December 2012**
Investments carried at fair value through:						
- income statement	32,771	-	-	-	-	32,771
- equity	-	-	-	-	-	-
	32,771	**-**	**-**	**-**	**-**	**32,771**

	At 1 January 2011	Total gains recorded in consolidated income statement	Total gains recorded in equity	Purchases	Sales/ transfers	At 31 December 2011
Investments carried at fair value through:						
- income statement	34,326	2,702	-	300	(4,557)	32,771
- equity	-	-	-	-	-	-
	34,326	2,702	-	300	(4,557)	32,771

The Group has not recognised any gains or losses on level 3 financial instruments during the year (2011: US$ 2.7 million unrealised gains).

Transfers between level 1, level 2 and level 3
There were no transfers between the levels during the year ended 31 December 2012.

The following table shows the impact on fair value of level 3 financial instruments using reasonably possible alternative assumptions.

For investment securities the Bank adjusted the discount rate ± 1% and carrying values ± 5% where appropriate, which is considered by the Bank to be within a range of reasonably possible alternatives.

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19. FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

	Carrying amount	Effects of reasonably possible alternative assumptions on carrying amount
31 December 2012		
Investments carried at fair value through income statement	**32,771**	**1,639**
31 December 2011		
Investments carried at fair value through income statement	32,771	1,639

20. ASSETS UNDER MANAGEMENT

	31 December 2012	31 December 2011
Proprietary	61,168	59,924
Clients	169,946	164,390
	231,114	224,314

Proprietary assets are included in the consolidated statement of financial position under "investment securities". Client assets, which represent client investments, are managed in a fiduciary capacity without recourse to the Group and are not included in the consolidated statement of financial position.

21. COMMITMENTS AND CONTINGENCIES

	31 December 2012	31 December 2011
Lease commitments	2,882	4,698
Guarantees	3,315	3,292
	6,197	7,990

Pursuant to the resolution of shareholders Extraordinary General Meeting held in October 2010, the Bank's Board of Directors was mandated by the General Assembly to bring legal action against the former Chief Executive Officer & Managing Director. Accordingly, the Bank has filed various legal proceedings against the former Chief Executive Officer & Managing Director before the Civil and Criminal Courts of the Kingdom of Bahrain. In view of the results made by the General Prosecutor and the advice received by the Bank from its legal counsel, management is confident that damages will be awarded to the Bank.

Employment claims against the Bank have been filed by former Bank employees. Based on the advice the Bank received from its external legal counsel, it is premature to quantify the amount or timing of liability, if any. The external legal counsel has also confirmed that the Bank has strong grounds to successfully defend itself against these claims. Accordingly, no provision for these claims has been made in the consolidated financial statements. No further disclosures regarding contingent liabilities arising from any of the employment claims are being made by the Bank as the directors of the Bank believe that such disclosures may be prejudicial to the Bank's position.

The Group's share of commitments arising from its equity-accounted investees is given in note 8.

22. RELATED PARTY TRANSACTIONS

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial and operating decisions. Related parties include significant shareholders and entities over which the Bank and shareholders exercise significant influence, directors, members of Shari'a Supervisory Board and executive management of the Bank.

Compensation of key management personnel

Key management personnel of the Group comprise of the Board of Directors and key members of management having authority and responsibility for planning, directing and controlling the activities of the Group. The key management personnel compensation during the year is as follows:

	2012	2011
Short term employee benefits	3,153	4,709
Post-employment benefits	548	264
	3,701	4,973

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22. RELATED PARTY TRANSACTIONS *(continued)*

The significant related party transactions and balances included in this consolidated financial statements are as follows:

	2012				2011			
Assets	**Associates**	**Significant shareholders/ entities in which directors have interest**	**Senior management**	**Other entities**	Associates	Significant shareholders/ entities in which directors have interest	Senior management	Other entities
Financing receivables	6,556	-	-	7,108	6,548	-	-	6,006
Investment securities	83,309	-	-	11,181	97,201	-	-	9,557
Assets held-for-sale	18,932	-	-	-	2,560	-	-	-
Equity-accounted investees	106,006	-	-	-	114,952	-	-	-
Other assets	2,536	-	90	842	1,290	-	706	819
Liabilities								
Due to financial institutions	26,191	-	-	-	25,378	-	-	-
Due to customers	-	-	-	660	5,943	-	-	2,615
Other liabilities	152	1,284	548	66	-	825	792	66

	2012				2011			
Income / (expenses)	**Associates**	**Significant shareholders/ entities in which directors have interest**	**Senior management**	**Other entities**	Associates	Significant shareholders/ entities in which directors have interest	Senior management	Other entities
Income from investment securities	(13,729)	-	-	1,199	121	-	-	(201)
Fees and commission	2,067	-	-	1,228	2,595	-	-	444
Net finance income / (expense)	(663)	-	-	577	(1,018)	-	-	(282)
Share of profit of equity-accounted investees	10,575	-	-	-	6,444	-	-	-
Other income	-	-	-	-	-	1,469	-	914
Reversals of impairment	-	-	-	-	4,037	-	-	-
Directors' and Shari'ah board remuneration and expenses	-	(818)	-	(52)	-	(716)	-	(220)

23. RISK MANAGEMENT

Risk is an inherent part of the Group's business activities. The Group's risk management and governance framework is intended to provide progressive controls and continuous management of the major risks involved in the Group's activities. Risks are managed by a process of identification, measurement and monitoring, and are subject to risk limits and other controls. The process of risk management is critical to the Group's operations and each business unit within the Group is accountable for the risk exposures relating to their responsibilities. The Group's main risk exposure categories are Investment and Credit risk, Market risk, Liquidity risk and Operational risks.

- Risk identification: The Group's exposure to risk through its business activities, including investment in Private Equity, Brokerage, and Capital Markets, is identified through the Group's risk management infrastructure.
- Risk measurement: The Group measures risk using basic risk management position methodologies which reflect the Group's investment risks, foreign exchange and profit rate exposure risks. The Bank relies on both quantitative and qualitative approaches in quantifying risks.
- Risk monitoring: The Group's risk management policies and procedures incorporate respective limits and the Group's activities are regularly reviewed. The Bank has also reviewed and strengthened its corporate governance arrangements.
- Risk reporting: The Group undertakes reporting of all core risks relevant to its businesses on a consolidated basis. In line with the board-approved risk framework. The Bank has risk governance arrangements to oversee risk management and transaction approval and key governance committees include; the Group Asset and Liability Committee ("ALCO") which oversees liquidity, cash flow planning and general asset liability management, the Group Risk Executive Committee ("REXCO") which oversees risk management across the group including review and approval of risk limits, credit facilities and key risk processes and the Investment and Post Investment Management Committee ("IPIMC") which is responsible for review and approval of new investments, funding requirements, divestments and general investment processes.

Group Risk Framework and Governance
The Board of Directors is ultimately accountable for the risk management of the Group. The Board has advocated a wholly integrated risk management process within the Group, in which all business activities are aligned to the risk framework. The Group Risk Framework establishes Group risk management standards, risk processes, structures, and defines the Bank's risk philosophy.

Board of Directors
The Board of Directors is responsible for defining the Group's risk appetite within which it manages its risk exposures and reviews the Group's compliance with delegated risk authorities.

Audit Committee
The Audit Committee is appointed by the Board of Directors and consists of four non-executive Board members. The Audit Committee assists the Board in carrying out its responsibilities with respect to assessing the quality and integrity of financial reporting and oversight of the Internal Audit function.

Shari'ah Supervisory Board
The Group's Shari'ah Supervisory Board is vested with the responsibility of ensuring that the Group complies with the Shari'ah rules and principles in its transactions, activities and general philosophy.

23. RISK MANAGEMENT (continued)

Group Risk Executive Committee

Group Risk Executive Committee REXCO has the overall responsibility for ensuring that the Group develops appropriate risk policies and strategies for the relevant business activities, and makes preparations for forthcoming regulatory arrangements in line with Basel Committee recommendations. It oversees the risk management activities of the Group, reviews and approves risk management principles, frameworks, policies, limits, processes and procedures. It is responsible for assessing fundamental risk issues within the general development strategy of the Group.

Internal Audit and Independent Review

All key operational, financial and risk management processes are audited by Internal Audit according to risk based auditing standards. Internal Audit examines the adequacy of the relevant policies and procedures and the Group's compliance with internal policies and regulatory guidelines. Internal Audit discusses the result of all assessments with management and reports its findings and recommendations to the Audit Committee. The Internal Audit recommendations are tracked for resolution via the Committee.

Group Asset and Liability Committee (ALCO)

The Group Asset and Liability Committee establishes the funding, liquidity and market risk policies for the Group. It is composed of the heads of key business areas and finance, risk, operations and control areas. ALCO's objectives are to manage the assets and liabilities of the Group, determine the statement of financial position mix and appropriate risk and return profile. It oversees all treasury and capital markets activities and all areas affected by liquidity and market risk. Cash flow management is a major focus of ALCO and ALCO regularly reviews the business line investment plans to ensure that sufficient funding is in place. ALCO ensures that the appropriate mix of short and long term funding strategies are developed in conjunction with the Group's treasury and capital markets functions.

Risk Management

The Risk Management function is responsible for designing and implementing the Group's risk framework, including policies, processes and systems. With the establishment of the Board Risk Committee, the Chief Risk Officer now reports functionally to the Board Risk Committee and administratively to the Chief Executive Officer. Risk Management conducts risk assessments of individual transactions (including their respective credit, investment, counterparty and operational risks), products and services. Risk Management is responsible for ensuring that the Group's processes capture all sources of transaction risk and that appropriate limit methodologies are developed for use in the management of business risk. In addition to the above the Risk Function also supports investment processes throughout the investment cycle including periodic valuation and reporting.

Treasury Activities

Treasury is responsible for managing the Group's day to day funding, liquidity management, foreign exchange and profit rate exposures, under the review of Risk Management and the supervision of ALCO.

Investment Monitoring and Reporting

Proprietary investment risks are identified and assessed via extensive due diligence activities conducted by the respective departments. This is supported by Risk Management which undertakes an independent risk assessment of every investment transaction. Post-acquisition investment management is rigorously exercised, mainly via board representation within the investee company, during the life of the investment transaction.

The Group has exposure to the following risks from its use of financial instruments:

- credit risk
- liquidity risk
- market risk
- operational risk

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23. RISK MANAGEMENT (continued)

The information about the Group's exposure to each of the above risks, its objectives, policies and processes for measuring and managing risk, and the Bank's management of capital is explained in notes 24 to 27 and 34.

24. CREDIT RISK

Credit Risk Policy Framework
The Bank has a Group Credit Risk Policy framework establishing Group credit risk appetite, credit risk origination, underwriting and administration standards. The credit policy articulates key credit markets, minimum criteria for the granting of credit, minimum requirements on collateral and defines roles and responsibilities for credit risk management. The policy provides a guideline to business units when originating credit business.

In order to strengthen the Bank's credit risk management processes through a rigorous and consistent analysis of credit worthiness, the Bank introduced Internal Credit Rating Models covering corporate entities, banking counterparties and real estate exposures. The ratings coming out of the rating models are used together with other supporting information on the obligor's creditworthiness when making credit decisions.

Credit Risk Management
Credit risk is the risk that the Group will incur a loss of principal or profit earned because its customers, clients or counterparties fail to discharge their contractual obligations and arises principally from the Group's balances with banks, placements with financial institutions, financing receivables, investment securities – sukuk and other receivables. Institutional Banking proposes limits for its interbank placement activities and other client groups for review and approval by REXCO. Further, Risk Management independently analyses the applications and rates for the respective counterparties. Based on this an independent recommendation is forwarded to the REXCO for approval. REXCO periodically reviews these limits for appropriateness in prevailing market conditions.

The table below shows the maximum exposure to credit risk for the components of the consolidated statement of financial position. There is no significant use of master netting and collateral agreements.

	Maximum exposure 2012	Maximum exposure 2011
<u>On balance sheet</u>		
Balances with banks	7,966	11,061
Placements with financial institutions	63,733	66,477
Financing receivables	86,623	95,838
Investment securities – Sukuk	26,063	23,396
Other assets	23,359	35,477
<u>Off balance sheet</u>		
Guarantees	3,315	3,292
	211,059	235,541

Risk Exposure Concentration
Risk concentration arises 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 geographical location.

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24. CREDIT RISK (continued)

In order to avoid excessive concentrations of risk, the Group's policies and procedures include guidelines to focus on maintaining a diversified portfolio. In line with regulatory requirements, the bank has a group level Large Exposure Policy which details the Bank's approach in managing concentration risk to sectors, asset classes, single obligors and countries including defining specific limits.

Concentration of risks is managed by counterparty, by geographical region and by industry sector. The maximum credit exposure to any client, or counterparty, or group of closely related counterparties as of 31 December 2012 was US$ 30.8 million (2011: US$ 39.2 million), relating to "placement with financial institution and financing receivables".

Geographical Exposure Distribution
The analysis by geographical region of the Group's financial assets having credit risk exposure is as follows:

REGION	Total Assets	Off-balance sheet	Total 2012	Total 2011
Bahrain	22,761	-	22,761	24,808
Other Middle East	109,237	-	109,237	111,672
North America	1,145	3,000	4,145	16,530
Asia Pacific	69,206	-	69,206	75,384
Europe	5,395	315	5,710	7,147
Total	**207,744**	**3,315**	**211,059**	235,541

Industry Sector Exposure
The distribution of assets and off-statement of financial position items by industry sector is as follows:

INDUSTRY SECTOR	Total Assets	Off-balance sheet	Total 2012	Total 2011
Banking and finance	94,947	315	95,262	108,505
Industrial	13,706	-	13,706	17,624
Real estate and construction	43,384	-	43,384	43,898
Technology	3,512	3,000	6,512	6,090
In-house funds	2,381	-	2,381	263
Trade	41,670	-	41,670	48,284
Government	6,775	-	6,775	2,732
Individual	1,369	-	1,369	8,145
Total	**207,744**	**3,315**	**211,059**	235,541

Collateral and other credit enhancements
The Group utilizes collateral and other credit enhancements mostly on its credit facilities, in line with Shari'ah requirements. Before taking any form of collateral the Bank pre-assesses impediments that may restrict accessibility to collateral should the need arise as well as acceptability from a Shari'ah perspective. In this respect the Bank will formally agree with the customer at the time of signing the offer letter on the usage, redemption and utilization of collateral when the customer/counterparty defaults. In the past year, the Bank has obtained

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24. CREDIT RISK (continued)

collateral including shareholders' personal guarantees, cash, real estate, unlisted equity shares and debentures. The Bank's credit policy discourages taking collateral value where there is positive correlation between collateral value and obligor's ability to pay.

Credit quality per class of financial assets

The Group did not apply a standard credit rating to its investment business, as the Group assessed credit quality according to the policies of the respective business areas. Management considers the credit quality of the Group's financial assets to be of standard quality as of 31 December 2012. Following is an analysis of credit quality by class of financial assets:

	2012				
	Neither past due nor impaired	Past due but not impaired	Individually impaired	Impairments / provisions	Total
Balances with banks	7,966	-	-	-	7,966
Placements with financial institutions	63,733	-	-	-	63,733
Financing receivables	86,623	-	-	-	86,623
Investment securities – Sukuk	26,063	-	-	-	26,063
Other assets	8,676	13,314	5,137	(3,768)	23,359
Guarantees	3,315	-	-	-	3,315
Total	**196,376**	**13,314**	**5,137**	**(3,768)**	**211,059**

Exposures that are past due but not impaired are either past due for less than 90 days and the financial condition of the customer is sound, or has adequate unimpaired collateral coverage. Provisioning is driven by the performance of the customer against laid down terms and conditions of the facility, internal credit grading and classification system calculated on net exposure after deducting the discounted value of recoverable collateral and any disposal costs.

	2011				
	Neither past due nor impaired	Past due but not impaired	Individually impaired	Impairments / provisions	Total
Balances with banks	11,061	-	-	-	11,061
Placements with financial institutions	66,477	-	-	-	66,477
Financing receivables	95,838	-	-	-	95,838
Investment securities – Sukuk	23,396	-	-	-	23,396
Other assets	35,250	227	8,768	(8,768)	35,477
Guarantees	3,292	-	-	-	3,292
Total	235,314	227	8,768	(8,768)	235,541

Ageing analysis of past due but not impaired by class of financial assets:

	2012			
	Less than 120 days	Less than 365 days	More than 365 days	Total
Other assets	11,971	1,224	119	13,314

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24. CREDIT RISK (continued)

	2011			
	Less than 120 days	Less than 365 days	More than 365 days	Total
Other assets	11	99	117	227

25. LIQUIDITY RISK MANAGEMENT

Liquidity risk is the risk that the Group will encounter difficulty in meeting obligations associated with its financial liabilities that are settled by delivering cash or another financial assets.

The key features of the Group's liquidity methodology are:

– The Group Asset and Liability Committee ("ALCO") is responsible for liquidity monitoring, cash flow planning and general asset liability management.
– In accordance with the Basel recommendations on liquidity management, the Group measures liquidity according to two criteria: "normal business", reflecting day-to-day expectations regarding the funding of the Group; and "crisis scenario", reflecting simulated extreme business circumstances in which the Group's survival may be threatened.
– The Group's liquidity policy is to hold sufficient liquid assets to cover its committed statement of financial position requirements, plus its budgeted expenses for the liquidity horizon and its forecast investment commitments over the liquidity horizon.

Analysis of financial liabilities

The table below summarises the maturity profile of the Group's financial liabilities based on contractual undiscounted repayment obligations.

	Gross undiscounted cash flows				
	Less than 3 months	**3 to 12 months**	**Over 1 year**	**Total**	**Carrying value**
At 31 December 2012					
Due to financial Institutions	130,521	23,552	-	154,073	153,121
Due to customers	42,006	26,522	-	68,528	68,176
Other liabilities	17,508	-	2,233	19,741	19,741
Total financial liabilities	**190,035**	**50,074**	**2,233**	**242,342**	**241,038**

	Gross undiscounted cash flows				
	Less than 3 months	3 to 12 months	Over 1 year	Total	Carrying value
At 31 December 2011					
Due to financial Institutions	104,762	39,620	-	144,382	143,178
Due to customers	87,372	1,641	-	89,013	88,483
Other liabilities	7,099	-	2,389	9,488	9,488
Total financial liabilities	199,233	41,261	2,389	242,883	241,149

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25. LIQUIDITY RISK MANAGEMENT (continued)

The table below shows the contractual expiry by maturity of the Group's commitments.

	On demand	3 to 12 months	Over 1 year	Carrying value
31 December 2012				
Commitments	-	1,676	1,206	2,882
Guarantees	3,315	-	-	3,315
Total	**3,315**	**1,676**	**1,206**	**6,197**

	On demand	3 to 12 months	Over 1 year	Carrying value
31 December 2011				
Commitments	-	2,325	2,373	4,698
Guarantees	3,292	-	-	3,292
Total	3,292	2,325	2,373	7,990

26. MARKET RISK MANAGEMENT

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to adverse changes in market variables such as profit rates, foreign exchange rates, equity prices and commodities. The Group classifies exposures to market risk into either trading or non-trading portfolios. The Group does not currently engage in trading activity. Non-trading positions are managed and monitored using sensitivity analysis.

Market Risk: Non-trading

Profit rate risk

Profit rate risk arises from the possibility that changes in profit rates will affect future cash flows or the fair values of the financial instruments. The Board has set limits on profit rate positions by maturity. The Group currently has limited exposure to profit rate risk. The Group's assets and liabilities that are exposed to profit rate risk include: placements with financial institutions, financing receivables, investments in sukuk and due to financial and non-financial institutions.

The following table demonstrates the sensitivity to a reasonable possible change in profit rates by 200 bps, with all other variables held constant. The effect of decreases in profit rate is expected to be equal and opposite to the effect of the increases shown.

	2012			2011		
	Balance	Change in profit rate (+/-)	Effect on net profit (+/-)	Balance	Change in profit rate (+/-)	Effect on net profit (+/-)
Assets						
Placements with financial institutions	63,733	200	1,246	66,477	200	1,301
Financing receivables	86,623	200	1,523	95,838	200	1,556
Investment securities – Sukuk	26,063	200	19	23,396	200	14
Liabilities						
Due to financial institutions	153,121	200	(2,609)	143,178	200	(2,312)
Due to customers	68,176	200	(1,135)	88,483	200	(1,483)
Total			**(956)**			(924)

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26. MARKET RISK MANAGEMENT (continued)

Currency risk
Currency risk is the risk that the value of a financial instrument will fluctuate due to adverse changes in foreign exchange rates. The Board has set limits on positions by currency. Positions are monitored regularly to ensure that positions are maintained within established limits.

The table below indicates the currencies to which the Group has significant exposure. The analysis shows the impact of a 20% movement in the currency rate against the United States Dollar, with all other variables held constant on the consolidated statement of income and equity. The effect of decreases in the currency rates is expected to be equal and opposite to the effect of the increases shown.

	2012			2011		
Currency	Exposure (USD equivalent)	Effect on net profit (+/-)	Effect on equity (+/-)	Exposure (US$ equivalent)	Effect on net profit (+/-)	Effect on equity (+/-)
Kuwaiti Dinar	(12,160)	(2,432)	-	(12,275)	(2,455)	-
Turkish Lira	7,074	322	1,093	8,370	243	1,431
Malaysian Ringgit	42	8	-	2,588	518	-
Euro	141	28	-	(12)	(2)	-
Jordanian Dinar	23,732	4,746	-	38,868	7,774	-
Sterling Pounds	157	31	-	315	63	-

Equity price risk
Equity price risk is the risk that the fair value of equities decreases as the result of adverse changes in the levels of equity prices and the value of individual stocks. Equity price risk arises from the Group's investment portfolio. The Group conducts significant investment activity in private equity, mainly in unquoted entities. The Group manages this risk through diversification of its investments in terms of geographical distribution and industry concentration by arranging representation on the Board of Directors within the investee company, wherever possible. Investments are managed within maximum concentration risk limits, approved by the Board of Directors of the Bank.

Sensitivity analysis
Quoted securities – Investment securities carried at fair value through income statement:
The Group's listed equity investment is listed on Amman Stock Exchange. This investments classified as investment carried at fair value through income statement, a 2 percent increase / decrease in Aman Stock Exchange Index at the end of the year would have increased / decrease the profit for the year by US$ 9.4 million (2011: an increase / decrease of US$ 15.8 million)

Unquoted securities - Investment securities carried at fair value through income statement:
The effect on profit as a result of a change in the fair value of equity instruments at 31 December 2012 due to a reasonable possible change (i.e. +/-15%) in the value of individual investments, with all other variables held constant, is US$ 9.2 million (2011: US$ 9 million). The effect of decrease in the value of individual investments is expected to be equal and opposite to the effect of an increase.

Prepayment risk
Prepayment risk is the risk that the Group will incur a financial loss because its customers and counterparties prepay or request repayment earlier than expected. The Group is not exposed to any significant prepayment risk.

27. OPERATIONAL RISK

Operational risk is the risk of unexpected losses resulting from inadequate or failed internal controls or procedures, systems failures, fraud, business interruption, compliance breaches, human error, management failure or inadequate staffing. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications or lead to financial loss.

While operational risks cannot be entirely eliminated, they are managed and mitigated by ensuring that appropriate infrastructure, controls, systems, procedures and trained and competent people are in place throughout the Group.

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28. MATURITY ANALYSIS OF ASSETS AND LIABILITIES

The table below shows an analysis of assets and liabilities analysed according to when they are expected to be recovered or settled.

	31 December 2012							
	Up to 1 month	1 to 3 months	3 to 6 months	6 to 12 months	Total up to 1 year	Over 1 year	Undated	Total
ASSETS								
Cash and balances with banks	7,985	-	-	-	7,985	-		7,985
Placements with financial institutions	63,489	244	-	-	63,733	-		63,733
Financing receivables	9,197	8,968	18,506	49,952	86,623	-		86,623
Investment securities	154	93	33,230	1,550	35,027	77,878		112,905
Assets held-for-sale	-	18,932	-	-	18,932	-		18,932
Equity-accounted investees	-	-	-	-	-	-	106,006	106,006
Investment properties	-	-	-	-	-	-	17,706	17,706
Other assets	15	25,400	-	-	25,415	573	-	25,988
Equipment	-	-	-	-	-	-	2,277	2,277
Total assets	**80,840**	**53,637**	**51,736**	**51,502**	**237,715**	**78,451**	**125,989**	**442,155**
LIABILITIES								
Due to financial institutions	61,380	68,551	21,881	1,309	153,121	-	-	153,121
Due to customers	23,626	18,260	25,679	611	68,176	-	-	68,176
Other liabilities	-	17,507	-	5,238	22,745	2,233	-	24,978
Total liabilities	**85,006**	**104,318**	**47,560**	**7,158**	**244,042**	**2,233**	**-**	**246,275**
Commitments	3,315	362	362	952	4,991	1,206	-	6,197
Net liquidity gap	**(7,481)**	**(51,043)**	**3,814**	**43,392**	**(11,318)**	**75,012**	**125,989**	**189,683**
Net cumulative gap	**(7,481)**	**(58,524)**	**(54,710)**	**(11,318)**	**(11,318)**	**63,694**	**189,683**	

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28. MATURITY ANALYSIS OF ASSETS AND LIABILITIES (continued)

	31 December 2011							
	Up to 1 month	1 to 3 months	3 to 6 months	6 to 12 months	Total up to 1 year	Over 1 year	Undated	Total
ASSETS								
Cash and balances with banks	11,081	-	-	-	11,081	-	-	11,081
Placements with financial institutions	62,945	2,656	876	-	66,477	-	-	66,477
Financing receivables	9,224	19,760	19,110	47,744	95,838	-	-	95,838
Investment securities	-	-	11,646	29,202	40,848	89,535	-	130,383
Assets held-for-sale	-	2,560	-	-	2,560	-	-	2,560
Equity-accounted investees	-	-	-	-	-	-	114,952	114,952
Investment properties	-	-	-	-	-	-	17,706	17,706
Other assets	726	37,147	-	-	37,873	679	-	38,552
Equipment	-	-	-	-	-	-	5,483	5,483
Total assets	83,976	62,123	31,632	76,946	254,677	90,214	138,141	483,032
LIABILITIES								
Due to financial institutions	52,345	51,958	37,664	1,211	143,178	-	-	143,178
Due to customers	15,720	71,142	1,018	603	88,483	-	-	88,483
Other liabilities	33	7,066	-	6,717	13,816	2,389	-	16,205
Total liabilities	68,098	130,166	38,682	8,531	245,477	2,389	-	247,866
Commitments	3,292	362	362	1,601	5,617	2,373	-	7,990
Net liquidity gap	12,586	(68,405)	(7,412)	66,814	3,583	85,452	138,141	227,176
Net cumulative gap	12,586	(55,819)	(63,231)	3,583	3,583	89,035	227,176	

29. SEGMENT INFORMATION

Operating segments are reported in accordance with internal reporting provided to Executive Management (the chief operating decision-maker), which is responsible for allocating resources to the reportable segments and assesses its performance. All operating segments used by the Group meet the definition of a reportable segment under FAS 22.

During the year, the Group has changed its reportable segments as a result of the recent restructuring of its business and in-line with the current internal reporting to the Chief Operating decision-maker for segment measurement and monitoring. Currently, the Group is organised into business units based on their nature of operations and services and has three reportable operating segments which are as follows:

Investment Banking & Alkhair Capital Menkul Degerler A.S

The Group's Investment banking business is engaged in transaction origination and structuring, investment, placement to third-party investors, restructuring and managing portfolio companies. This segment focuses on stable companies, historically revenue-generating with positive profitability, requiring growth capital or partial exits. The segment focuses on specific sectors and geographies, whilst avoiding start-ups, venture capital, and greenfield investments. The segment targets businesses in the oil & gas services; industrial services; building materials; logistics; and agri-business; specifically in the MENA region including Turkey.

Alkhair Capital Menkul Degerler A.S originates Shari'ah compliant PE transactions, especially proprietary deals from direct contacts with a wide range of local sources. The Turkey office also provides a post-investment management services (post management until successful exit, advisory for an IPO or trade sale) to co-investors.

The business manages the Bank's Global Private Equity Fund. It also sources and manages investments on behalf of the Bank's Strategic Acquisition Fund.

Alkhair International Islamic Bank Malaysia Berhad

Alkhair International Islamic Bank Malaysia Berhad was established in 2004 to source investment opportunities in the Far East and monitor the performance of the acquired companies on behalf of the Bank and investors and to establish distribution channels for the Group.

Alkhair Capital Saudi Arabia

Alkhair Capital Saudi Arabia was incorporated in March 2009 and registered with Capital Markets Authority. Its principal activities are Asset Management, Corporate Finance & Investment banking and Brokerage.

Information regarding the results of each reportable segment is included below. Inter-segment pricing is determined on an arm's length basis. Management monitors the operating results of its business units separately for the purpose of making decisions about resource allocation and performance assessment.

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29. SEGMENT INFORMATION (continued)

	For the year ended 31 December 2012				
	Investment Banking & Alkhair Capital Menkul Degerler A.S	Alkhair International Islamic Bank Malaysia Berhad	Alkhair Capital Saudi Arabia	Inter-company	Total
External revenue					
Net finance expense	(2,457)	3,385	-	-	928
Income from investment securities	(11,707)	1,031	-	-	(10,676)
Fees and commission	2,229	1,145	380	-	3,754
Share of profit of equity-accounted investees	10,575	-	-	-	10,575
Other income	685	24	-	-	709
Inter-segment income	(3,267)	317	2,950	-	-
Total income	(3,942)	5,902	3,330	**-**	5,290
Total operating expenses	(32,483)	(4,479)	(7,536)	-	(44,498)
Reversal of impairment	1,350	(250)	-	-	1,100
Income from assets held for sale and discontinued operations	64	-	-	-	64
Provision for tax	-	-	(1,719)	-	(1,719)
(Loss) / profit for the year	(35,011)	1,173	(5,925)	**-**	(39,763)
Equity-accounted investees	106,006	-	-	-	106,006
Capital expenditure	255	-	20	-	275
Segment assets	272,538	185,567	70,099	(86,049)	442,155
Segment liabilities	167,888	156,990	7,446	(86,049)	246,275

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29. SEGMENT INFORMATION (continued)

	For the year ended 31 December 2011				
	Investment Banking & Alkhair Capital Menkul Degerler A.S	Alkhair International Islamic Bank Malaysia Berhad	Alkhair Capital Saudi Arabia	Inter-company	Total
External revenue					
Net finance expense	(2,401)	2,805	-	65	469
Income from investment securities	7,112	1,153	-	-	8,265
Fees and commission	8,564	216	-	(65)	8,715
Share of profit of equity-accounted investees	6,444	-	-		6,444
Other income	2,226	(35)	-		2,191
Inter-segment income	(2,921)	-	2,921		-
Total income	19,024	4,139	2,921	-	26,084
Total operating expenses	(31,386)	(3,317)	(6,919)	-	(41,622)
Reversal of impairment	4,010	-	-	-	4,010
Income from assets held for sale and discontinued operations	14,497	-	-	-	14,497
Provision for tax	-	-	(1,800)	-	(1,800)
Profit / (loss) for the year	6,145	822	(5,798)	-	1,169
Equity-accounted investees	114,952	-	-	-	114,952
Capital expenditure	86	5	(25)	-	66
Segment assets	308,054	190,577	73,589	(89,188)	483,032
Segment liabilities	169,347	162,372	5,011	(88,864)	247,866

The comparative segment reporting for the previous year has been restated and disclosed based on the current reportable segments.

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29. SEGMENT INFORMATION (continued)

Geographic segment information:
The Group operates in five geographic markets: Bahrain, Other Middle East, North America, Asia Pacific and Europe. The following tables show the distribution of the Group's total income and non-current assets by geographical segments .

31 December 2012	Bahrain	Other Middle East	North America	Asia Pacific	Europe	Total
Total income	1,877	(2,091)	-	4,229	1,275	5,290
Net loss	(25,801)	(11,346)	(237)	(500)	(1,879)	(39,763)
Non-current assets *	18,934	377	-	365	307	19,983

31 December 2011	Bahrain	Other Middle East	North America	Asia Pacific	Europe	Total
Total income	2,288	14,086	1,976	3,031	4,703	26,084
Net income/(loss)	(20,635)	5,345	15,388	(602)	1,673	1,169
Non-current assets *	22,112	457	-	556	64	23,189

** includes equipment and investment property*

30. SHARI'AH SUPERVISORY BOARD
The Bank's Shari'ah Supervisory Board consists of six Islamic scholars who review that the Bank is compliant with general Shari'ah principles and specific fatwas, rulings and guidelines issued. Their review includes examination of evidence relating to the documentation and procedures adopted by the Bank to ensure that its activities are conducted in accordance with Islamic Shari'ah principles.

31. EARNINGS AND EXPENSES PROHIBITED BY SHARI'AH
The Group did not receive any significant income or incur significant expenses that were prohibited by the Shari'ah.

32. SOCIAL RESPONSIBILITIES
The Group discharges its social responsibilities through donations to good faith charity funds.

33. ZAKAH
The Bank is not obliged to pay Zakah. Payment of Zakah is the responsibility of the shareholders of the Bank. Zakah payable by shareholders on their holdings in the Bank is calculated on the basis of a method prescribed by the Bank's Shari'ah Supervisory Board. Zakah payable by the shareholders in respect of the year ended 31 December 2012 was US$ 0.0283 cents per share (2011: US$ 0.0220 cents per share).

34. CAPITAL MANAGEMENT

The Central Bank of Bahrain (CBB) sets and monitors capital requirements for the Bank as a whole. In implementing current capital requirements CBB requires the Bank to maintain a prescribed ratio of total capital to total risk-weighted assets. CBB capital adequacy regulations are based on the principles of Basel II and IFSB capital adequacy guidelines.

The Bank's regulatory capital is analysed into two tiers:

- *Tier 1 capital*, includes ordinary share capital, disclosed reserves including share premium, general reserves, legal / statutory reserve as well as retained earnings after deductions for goodwill and other regulatory adjustments relating to items that are included in equity but are treated differently for capital adequacy purposes.

- *Tier 2 capital*, includes interim retained profits reviewed by the auditors and an allowed portion profit equalisation reserve (PER) and investment risk reserves (IRR). As per CBB, the PER & IRR can be up to a maximum amount equal to the capital charge pertaining to 30% of the risk weighted assets financed by unrestricted investment accounts.

Certain limits are applied to elements of the capital base in line with regulatory requirements. Tier 1 capital should represent at least half of the total eligible capital, i.e., Tier 2 capital is limited to 100% of Tier 1 capital. The limit on Tier 2 capital is based on the amount of Tier 1 capital after all deductions of investments pursuant to Prudential Consolidation and Deduction Requirements (PCD) Module of the CBB. The PCD Module sets out the regulatory rules for prudential consolidation, pro-rata consolidation or deduction where the own controlling or significant minority stakes in regulated financial entities, insurance entities and have significant exposures to investment in commercial entities. It also sets out the framework for the prudential deductions from capital for various instances including exposures to counterparties exceeding the large exposure limits as set out by CBB.

Banking operations are categorised as either trading book or banking book, and risk-weighted assets are determined according to specified requirements that seek to reflect the varying levels of risk attached to assets and off-balance sheet exposures.

The primary objectives of the Group's capital management are to ensure that the Group complies with regulatory capital requirements and that the Group maintains adequate capital ratios in order to support its business and to maximise shareholders' value.

The Group manages its capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of its activities. In order to maintain or adjust the capital structure, the Group may adjust the amount of dividend payment to shareholders, return capital to shareholders or issue new capital. No changes were made in the objectives, policies and processes from the previous years.

The Group has adopted the standardised approach for credit risk and market risk and basic indicator approach for operational risk regulatory capital computation purposes under the CBB capital adequacy framework. The Group does not have Basel II permissible credit risk mitigants against any of its credit exposures.

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34. CAPITAL MANAGEMENT (continued)

The Group's capital adequacy ratio, calculated in accordance with the capital adequacy rules determined by the Central Bank of Bahrain, is as follows:

	2012	2011
Regulatory capital base:		
Tier 1 capital	91,515	122,960
Tier 2 capital	-	-
Total regulatory capital	**91,515**	122,960
Risk-weighted assets	**405,597**	568,630
Tier 1 capital adequacy ratio	22.56%	21.62%
Total capital adequacy ratio	22.56%	21.62%

The Group has complied with the externally imposed capital requirements set by the regulator for its consolidated capital adequacy ratio throughout the year.

Capital allocation

The allocation of capital between specific operations and activities is primarily driven by regulatory requirements. The Bank's capital management policy seeks to maximise return on risk adjusted while satisfying all the regulatory requirements. The Bank's policy on capital allocation is subject to regular review by the Board.

35. COMPARATIVES

Certain prior period amounts have been regrouped to conform to current year's presentation. Such regrouping did not affect previously reported profit or equity.