10 YEAR Anniversary 2002-2012

Annual Report 2011

www.kfh.bh

Bringing Banking to Life

2011

بيت التمويل الكويتي
Kuwait Finance House
Bahrain B.S.C.(c) البحرين ش.م.ب (م)
Licensed as an Islamic Retail Bank by the Central Bank of Bahrain

His Royal Highness
Prince Khalifa bin Salman
Al Khalifa
The Prime Minister

His Majesty
King Hamad bin Isa
Al Khalifa
The King of the Kingdom of Bahrain

His Royal Highness
Prince Salman bin Hamad
Al Khalifa
The Crown Prince and Deputy
Supreme Commander

Best Islamic Bank in Bahrain
Islamic Finance News Awards 2011
KFH-Group

Best Mobile Application
Bahrain eContent Award 2011
KFH-Bahrain

Best Investment Product
Banker Middle East '11
Baytik Industrial Oasis

Best Investment Product
Banker Middle East '10
Menatelecom

Best Islamic Covered Card
Banker Middle East '10
Baytik Ijara

Best Islamic Wealth Management
Islamic Business & Finance Awards '09
Priority Banking

Best Project Finance House
Banker Middle East Industry Awards '08
Corporate Finance

Best Retail Brand
World Islamic Banking Conference Awards '08
KFH Group

Best New Product
Islamic Business & Finance Awards '08
Priority Banking

Best New Product
Islamic Business & Finance Awards '07
Durrat Al Bahrain

Kuwait Finance House-Bahrain

Annual Report 2011

Contents

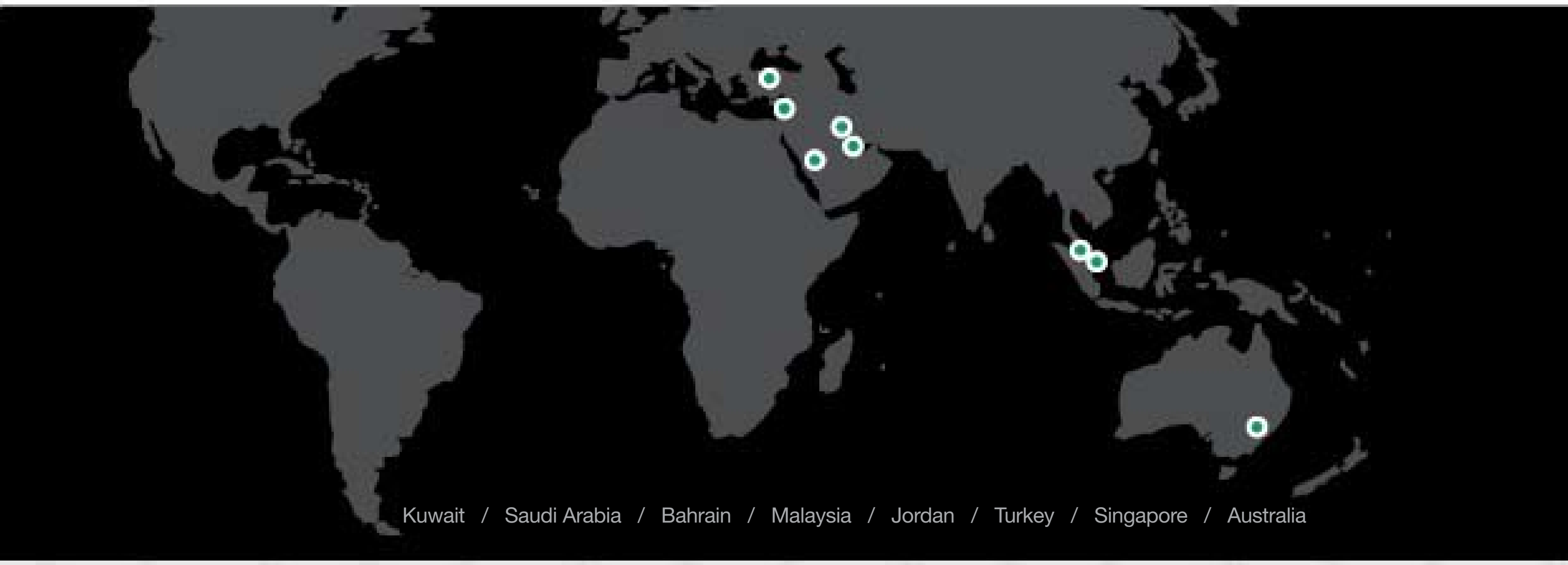
Bringing Banking to Life

Vision

At KFH-Bahrain we believe that banking is not just about money. For us it is something that can improve people's lives. Whether we are providing commercial and investment banking services or financial products for consumers, we start by understanding our customers and their needs. With an emphasis on innovation, we aim to provide cutting edge Islamic banking solutions while staying faithful to Shari'a principles, with a view to enhancing the lives of our customers.

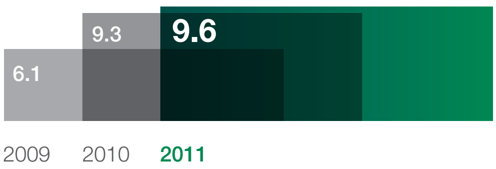
Mission

It is our mission to "Bring Banking to Life" by focusing on innovation, thinking outside the box and insisting on excellence in everything we do. This includes the development and provision of a wide range of integrated products and services in perfect harmony with Shari'a principles. Our mission and our commitment are backed by a robust financial position and a long and proven heritage of ingenuity, innovation and integrity.

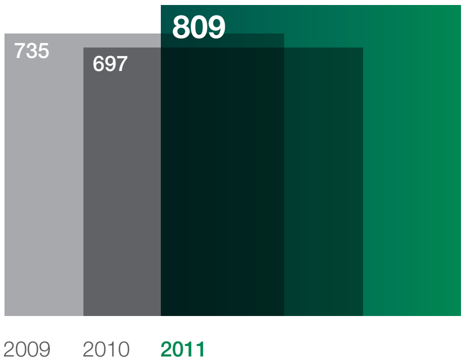


3 Year Highlights

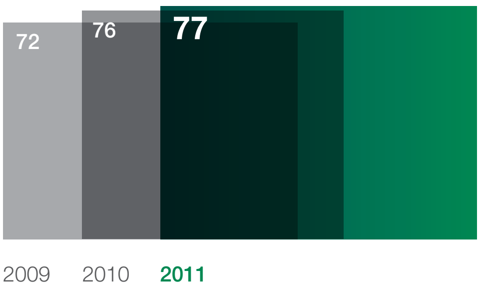
Net Income
BD Million



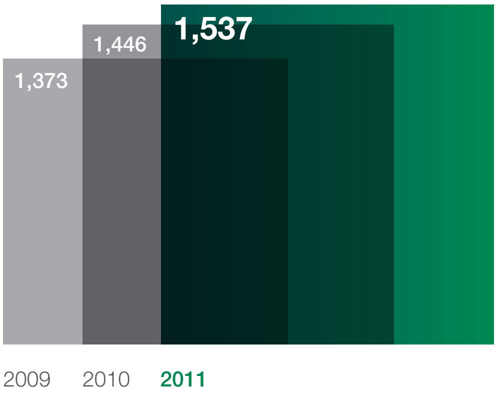
Customers Deposits
BD Million



Operating Income
BD Million



Total Assets
BD Million



Profile

Kuwait Finance House-Bahrain ("KFH-Bahrain"or the "Bank"), is a leading provider of Islamic retail commercial and investment banking services. Established in 2002 as a wholly owned subsidiary of Kuwait Finance House-Kuwait, a global industry leader, KFH-Bahrain specialises in conceptualising the development and introduction of innovative, Shari'a compliant banking and investment products.

KFH-Bahrain enjoys a reputation as a performance-driven, results-oriented institution, combining global investment strategies with the provision of popular retail products and services. KFH-Bahrain has made major advances and experienced considerable growth in the last few years, allowing it to further develop its products and services and provide outstanding investment opportunities for its customers.

At the forefront of the investment and finance sectors, KFH-Bahrain has developed a series of successful projects and made further investments in diverse sectors of the economy.

KFH-Bahrain is continuing its strategy of innovation and change and is committed to setting new standards for Islamic banking and finance. Such a strategy will reaffirm KFH-Bahrain's status as a market leader, enhancing its continued contribution to the economic growth and social development of the Kingdom of Bahrain.

Bader A. M. Al-Mukhaizeem
Chairman

Chairman's Statement

Dear Ladies and Gentlemen,

In the name of Allah, the Beneficent, the Merciful, Prayers and Peace Be Upon the Last Prophet and Messenger Mohammed.

It is my pleasure to present the annual report of KFH-Bahrain for the year ended 31st December 2011. In what has been an eventful and challenging year in terms of continued global economic uncertainty and major social political upheaval in the Arab World, I am pleased to report that, by the Grace of Allah the Almighty, 2011 was a successful year for KFH-Bahrain with the Bank improving on its position in 2010 and posting solid financial results.

Financial Results

The Bank's financial results for 2011 show continued solid steady growth. Operating income for the year increased by BD 1.3 million as compared to 2010 to reach BD 77million. Net operating income for the year increased by BD 0.9 million to reach BD 50.9 million due to the combined impact of increased revenue and reduced cost of funds. Net income for the year increased by BD 0.3 million, an increase of 3% from 2010, to reach BD 9.6 million. Total assets of the Bank reached BD 1.54 billion, an increase of BD 90.7million from 2010.

Adherence to Islamic principles

On behalf of the Bank's board of directors I would like to recognize the excellent work of our Shari'a Fatwa and Supervisory Board comprising of well respected scholars Shaikh Dr. Ajeel Jasem Al-Nashmi (Chairman), Shaikh Dr. Khalid Mathkour Al-Makhkour (Member) and Shaikh Dr. Mohammed Abdul Razaq Al-Tabtabaee (Member) who worked tirelessly to ensure the Bank's products and processes adhere to Islamic principles. Significant contributions in 2011 were the supervision of Sharia awareness sessions to employees and the publication of a Zakat calculation guide.

Risk, governance and compliance

The Bank continually examines its approach to risk, governance and compliance and in 2011 the Bank enhanced its economic capital planning and stress test models and improved its reporting of key risk indicators so that the Bank's management and board can better assess, monitor and manage the various risks the Bank is exposed to.

Customer satisfaction - a priority

In 2011 we added to and improved our retail product line with the introduction of a new mobile banking service, upgraded our SMS banking service, extended products available under the Ijara Card and launched a KFH-Bahrain cardholder discount program, all in an effort to improve our service. In addition we opened a new branch and we continued to improve our IT infrastructure and processes so as to deliver a more accessible and efficient service to our customers.

Community Service

At a time of national difficulty we consider it the role and duty of the Bank to encourage harmony and in this regard we made an extra effort to instill harmony in the country through our work to support the community. We continued to support the Islamic banking sector in Bahrain with our enhanced sponsorship of the Annual Conference of Accounting and Auditing Organization of Islamic Financial Institutions (AAOIFI) and the World Islamic Banking Conference. The Bank also supported a number of key educational initiatives such as the Injaz entrepreneurship and the Shaikha Hessa e-learning classroom concept under the banner "Inspiring Young Minds"

Recognition

I am pleased to report that we were honored with Best Mobile Application-Bahrain e-Content Award 2011 for KFH-Bahrain and Best Investment Product-Bankers Middle East 2011 for Baytik Industrial Oasis.

Thanks

On behalf of the Bank's Board of Directors and Executive Management, I would like to thank his Majesty King Hamad Bin Isa Al Khalifa, His Royal Highness Prince Khalifa Bin Salman Al Khalifa, the Prime Minister, and His Royal Highness Prince Salman Bin Hamad Al Khalifa, the Crown Prince and Deputy Supreme Commander. I would also like to extend our sincere appreciation to the Government of Bahrain and the Central Bank of Bahrain for their valuable direction.

In conclusion, I would like to thank our esteemed stakeholders for their support, our customers and business partners for their trust and loyalty, and the management and staff for their continued dedication and high professional standards which was evident when employees ensured the smooth running of the Bank notwithstanding difficult conditions requiring the Bank to activate its business continuity plan.

Bader Abdul Muhsen Al-Mukhaizeem
Chairman

In 2011 we added to and improved our retail product line with the introduction of a new mobile banking service, upgraded our SMS banking service, extended products available under the Ijara Card and launched a KFH-Bahrain cardholder discount programme, all in an effort to improve our service.

Abdulhakeem Yaqoub Alkhayyat
Managing Director & CEO

Managing Director and CEO's Statement

Dear Ladies and Gentlemen,

In the name of Allah, the Beneficent, the Merciful, Prayers and Peace be Upon the Last Prophet and Messenger Muhammad.

I am pleased to report that despite geo-political developments in the MENA region and the ongoing crisis in the Eurozone 2011 was another positive year for the Bank. In a year Bahrain has not seen the like before, we continued to improve our profitability and enhance our services and product offering. With thanks to Allah the Almighty and the support of our Chairman, the Board of Directors, management and staff, we posted healthy financial results and continued meeting our objectives of steadily growing the Bank.

Retail & Corporate Banking

On the retail side of our business we witnessed good growth achieved by virtue of an enhanced product offering and improved delivery channels and in 2012 we will be looking for further enhancements and improvements. With regard to corporate, we became more atuned and responsive to those clients who experienced difficulties meeting their payment obligations and were able to assist customers at the relevant time allowing them to weather the period of difficulty. Our retail and corporate banking portfolio comprises 39% of our total assets and is a reliable source of steady profits for ourselves and our investment account holders.

Debt Capital Markets & Investment Banking

Regarding our investments, we have successfully sold a number of our non-core investment assets and actively worked on developing our strategic real estate projects Durrat Al Bahrain and Diyar Al Muharraq. In tune with the needs of the country, our focus in Diyar Al Muharraq has been the provision of much needed affordable homes which we are steadily moving towards. Our investee company Menatelecom is a leading telecommunications provider in Bahrain and we are pleased to report it has now obtained 72,870 subscribers. Our DCM team has been active securing new banking lines, growing the Sukuk portfolio and devising new product lines and hope to launch an innovative short term financial institution investment product in 2012.

Shari'a Fatwa and Supervisory Board

I would like to deliver my sincere thanks to our Shari'a Fatwa and Supervisory Board under the guidance of their chairman Shaikh Dr. Ajeel Jasem Al-Nashmi. The Shari'a Fatwa and Supervisory Board has provided welcome guidance to our Shari'a department and this has resulted in increased awareness of Islamic values at the Bank.

Information Technology

2011 was a very productive year for the Bank in terms of IT infrastructure. We continued to significantly improve our IT capability and this is evident in the enhancements in our e-banking services. In parallel we completed the rebuilding of our data production centre and the expansion of our disaster recovery site so that our IT infrastructure is more efficient and resilient which should in turn provide our customers with faster processing.

Outlook

Given the unexpected events of 2011 it is difficult to predict with any certainty as to how the MENA economies will perform in 2012. Having said that, given the resources of the region and the resilient nature of the people, I do expect growth and we will position the Bank so that it can support such growth.

In the short term I certainly see opportunities to grow the retail side of our business as we improve our service in terms of accessibility by introducing and enhancing e-banking channels as well as new product lines.

Appreciation

In conclusion, I would like to express my sincere thanks and gratitude to the Chairman and members of the Board for their continued guidance and support and I would especially like to thank the Bank's staff for their dedication and hard work throughout 2011 which was never more illustrated than in the extra special efforts to provide a comprehensive and uninterrupted banking service to our customers during the height of the difficulties in Bahrain.

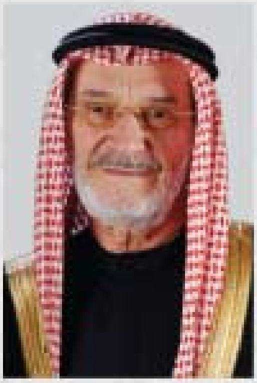
Abdulhakeem Yaqoub Alkhayyat
Managing Director & Chief Executive Officer

2011 was a very productive year for the Bank in terms of IT infrastructure. We continued to significantly improve our IT capability and this is evident in the enhancements in our e-banking services.

[redacted]

Board of Directors

Bader Abdul Muhsen Al-Mukhaizeem
Chairman



Mohammed Bin AlShaikh Ishaq
Vice Chairman

Mohammed Sulaiman Al Omar
Board Member

Abdulhakeem Yaqoub Alkhayyat
Managing Director & CEO

Yaqoob Yousef Majed
Board Member

Adel Ahmed Al Banwan
Board Member

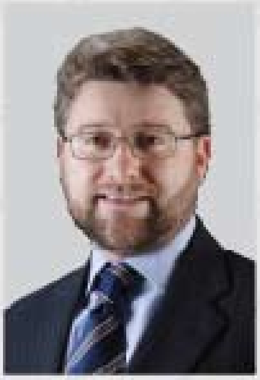
[redacted]

Abdul Razak Jawahery
Executive Manager

Ahmad Saeed
Executive Manager

Khalid Al Maarafi
Executive Manager

Lilian Le Falher
Executive Manager



Paul Mercer
Executive Manager

Sattam Algosaibi
Executive Manager

Executive Management

Hisham Al-Moayyed
Senior Manager - Real Estate

Isa Al Duwaishan
Senior Manager - Shari'a

Yousif Al-Hammadi
Senior Manager - Financial Control & Administration

Raed Ajawi
Manager - Internal Audit

Department Senior Management

Investment Portfolio

The last few years have been challenging years for the entire investment banking industry. As some of our investments were not completely immune to the crisis, we have spent these years to realize maximum return on such investments and increase operational efficiency within our portfolio assets.

The last few years have been challenging years for the entire investment banking industry. As some of our investments were not completely immune to the crisis, we have spent these years to realize maximum return on such investments and increase operational efficiency within our portfolio assets. We have been able to rebalance our portfolio and streamline the underlying businesses. Our Investment team strengthened the post-acquisition monitoring process and enhanced governance controls within our portfolio companies. These efforts have resulted in growth in the performance of our investments.

Real Estate Investments

We have continued our execution of real estate projects in the Kingdom of Bahrain and the MENA region. Our support to real estate projects, whether directly undertaken by us or through strategic partnerships, enabled these projects to weather the difficult market conditions witnessed during the previous period. Our portfolio includes several distinguished projects such as Diyar Al Muharraq, Durrat Al Bahrain and Ishbiliya Village.

In 2011, we continued our financial and management support for existing large scale real estate development projects and completed major development phases within a planned timeframe and budget. Steady progress was made towards the pre-development phase of some of the new projects and these are being monitored closely.

Corporate Investments

We continue to focus on the realization of non-core investments and stabilization of the investments which carry strong long term prospects. These investments will be managed and / or restructured (where required) and, through organic growth, an exit will be achieved. We have made the strategic decision not to invest in any new deals until the volatility in the financial and capital markets has subsided. However, we continuously evaluate this strategy including pursuing investment advisory / asset management activity.

Banking Group

The consumer banking and finance services provided by KFH–Bahrain combine a broad range of innovative products and services with exceptional client care. Our products and financing facilities are developed with the aim of providing for the long term needs of clients in the local market.

Bahrain World Trade Centre Branch

Manama Branch

East Riffa Branch

Automall Sitra Branch

Muharraq Branch

Adliya Branch

Automall Exhibition Road Branch

West Riffa Branch

Isa Town Branch

Our Branches

The consumer banking and finance services provided by KFH–Bahrain combine a broad range of innovative products and services with exceptional customer care. Our products and financing facilities are developed with the aim of providing for the long term and continous growing needs of clients in the local market. Our growth is driven by the determination to continuously improve our service quality, while thinking innovatively and striving to deliver superior Islamic Shari'a compliant products remain at the core of all we do.

KFH-Bahrain provides a 'one-stop-shop' for our clients' banking and financing requirements through our growing network of branches and ATMs. The opening of the Isa Town branch has increased the branch network to 9 branches across the Kingdom.

New services and innovative products are constantly being introduced for the benefit of our customers. These range from technology and service enhancements that provide greater access to information and funds, both locally and internationally, to the launch of our unique, never-before-seen products. We have demonstrated a constant pattern of growth with our electronic services throughout the year with the introduction of the online banking service and real-time cash and cheque deposit ATM Machines and an upgrade of both the telephone banking and customized SMS notification services.

At the beginning of the year, the KFH iPhone and Blackberry application was launched and later awarded the Bahrain eContent Award 2011 in the eBanking Category. The first of its kind application is in-line with the Bank's vision of making the experience with KFH-Bahrain as simple and as convenient as possible by using a wide range of communication channels through state of the art technologies.

Our Baytik Ijara card, winner of Banker Middle East Awards 2010 for the "Best Islamic covered card", is the world's first Islamic financing card that allows cardholders to acquire durable goods on a 'lease-to-own' basis. In additon, cardholders may benefit from a discount offered by participating outlets in the Baytik Ijara Shopper's Guide. This financing facility has been developed further to provide exclusive finance schemes such as Student Finance and financing the purchase of jewelry.

A unique 25 year home financing scheme is another example of the innovative products offered by KFH-Bahrain. With an exclusive offer targeting Ishbiliya Village, Durrat Al Bahrain and a number of development and residential projects, we have set a new standard in consumer finance.

The first Islamic chipped credit card – a Shari'a compliant offering with many benefits, introduced in 2007 in association with Visa – was enthusiastically received and continues its impressive growth. Cardholders enjoy a revolving credit facility without incurring interest but instead pay a low annual service charge.

KFH Automall showrooms are considered to be the largest in Bahrain to date and are located in Sitra and Exhibition Road. Each showroom provides a unique automotive and marine shopping experience, while also benefitting from a fully-fledged KFH-Bahrain branch within its facility, KFH Automalls provide customers with the convenience of a 'one-stop-shop' service for the lowest profit rate financing, insurance, registration and other add-ons, all under one roof.

Our Corporate Finance department at KFH-Bahrain has continued to maintain its solid track record.

We aim to support new and established companies to achieve their business growth objectives through providing tailor-made financing solutions to meet our clients' needs. Our Corporate Finance department provide Shari'a compliant financing instruments, service and advice. These include: Murabaha, Ijara and Istisna'a, as well as Commodity and Convertible Murabaha facilities.

We provide services across various sectors, including:

- Project financing
- Real estate financing
- Working capital financing
- Trade financing

Furthermore, the Corporate Finance department is currently in the process of launching a new product, in partnership with Tamkeen, aimed at providing financing solutions for Small and Medium Enterprises (SMEs). SMEs will be able to obtain easy financing at low subsidized profit rates. This will support the business growth of SMEs and take their organizations to better levels of production and profitability.

Our Corporate Finance department aims to maximize the business potential of its client base in order to further enhance existing client relationships and reinforce their confidence in KFH-Bahrain. Moreover, we continue to provide an exceptional quality of service and expert advice to both new and established companies in private and public sectors.

Corporate Finance

KFH-Bahrain's Treasury & Capital Markets department is active in the institutional banking and wholesale markets through its Treasury, Capital Markets, and Product Structuring functions.

The department offers customized institutional banking solutions to financial institutions, sovereign and quasi-sovereign entities, and large corporates.

Treasury

The primary function of Treasury is to efficiently manage liquidity and capital across the Bank. In this capacity, Treasury is responsible for handling interbank activities (assets & liabilities) and foreign exchange.

Capital Markets

Capital Markets is involved in Sukuk issuance mandates for institutions accessing financial markets. Additionally it is mandated with managing the Bank's sukuk portfolio. Capital Markets also participates in syndication activities regionally.

Product Structuring

In addition to its Treasury, Sukuk and Financing activities, the department's mission includes the development of services in the fields of liquidity management, investment solutions and financial tools intended for different types of investors and parties.

Treasury & Capital Markets

KFH Bahrain's approach to risk governance

At KFH-Bahrain, we believe that a robust and well implemented risk management framework is essential in protecting the interests of our stakeholders and translating our banking processes into tangible results. To achieve this, we developed a framework and culture which is proactive in the management of risk throughout the full life cycle of a financial transaction and in our operating circumstances.

The Board of Directors (BoD) are responsible for managing risk in the Bank. They do this through setting the risk appetite in the form of a comprehensive limit structure and aligning business and risk strategies to achieve overall risk adjusted returns. The Board level Risk Governance and Compliance Committee (RGCC) meets regularly to oversee the the bank-wide implementation of the BoD approved strategies, policies, and the risk appetite. Senior Management through the Risk Management - Asset Liability Committee develops and implements appropriate risk and business processes to monitor and manage risk within the parameters set by the BoD.

The Risk Management Department helps the management Risk Committee, RGCC and BoD, through the use of comprehensive Risk Management Dashboards, to take sound business and operating decisions. To develop such capabilities, review and enhancement of the Risk Management Infrastructure are paramount. The Bank has in last few years put in tremendous efforts to improve, monitor and gather quality data into systems and formats which give a timely and accurate picture of the risk profile. Sophisticated and prudent models are developed and refined periodically to allow measurement of risk taken and also project the likely impact of various factors in the Bank's business and operating goals. The models such as internal scoring systems, stress test program and the Internal Capital Adequacy and Assessment Program (ICAAP) have become valuable decision tools in the Bank.

KFH-Bahrain recognises that good policies are not enough and it is only through creation of a sound risk culture that risk can be contained and managed. To achieve this, all staff are educated in basic risk management principles and departmental procedures are integrated with the Bank's risk management processes. The Bank has put in place a Risk and Control Self Assessment ("RCSA") framework which ensures that risk taking activities are owned, understood and properly mitigated continuously by the risk taker itself. Several layers of check and

Risk Management

balances are implemented in the Bank's processes. Business units are the first line of defence against risk in their activities whereas the Risk Management Department provides tools and framework for business and support units, while Internal Audit provides independent oversight over all the banking processes. To further assure regulators and internal stakeholders that risk measurement tools and models are realistic in assessing risk, the Bank has all its internal models validated by an external consultant.

The Bank, in response to new evolving best practices, regulations and risks emanating from the global economic crisis, periodically revises its internal policies and processes to ensure compliance with latest directives and to ensure that they are appropriate to the level of complexity and breadth of our business and the economic landscape in which we operate. The Bank conducts various impact studies to assure its stakeholders that the Bank is appropriately prepared to comply with new regulations such as those from the Basel III, IFSB and CBB guidelines. Further, in the context of global and regional risks, the Bank ensured that its contingency plans such as those for liquidity and capital are relevant and implementable. Ability to provide services to our customers at all times has become very important in this uncertain time. The Bank has implemented and tested Disaster Recovery and Business Continuity programs.

The Bank is constantly seeking to improve its policies, processes and methodologies to reflect the latest and the best in international risk management practice. For more detailed information on Risk Management in the Bank, please refer to the Public Disclosure.

We at KFH-Bahrain are committed to adopting the highest international standards, regulatory requirements and global best practices in corporate governance. KFH-Bahrain has established a strong corporate governance framework that is designed to protect the interests of all stakeholders, ensure compliance with regulatory requirements and enhance organisational efficiency.

We have established a robust organizational structure that clearly segregates functions and responsibilities, and reflects a division of roles and responsibilities of the Board of Directors and Management. Clear mandates exist for the Board, Chairman of the Board, Board Committees, Managing Director and Chief Executive Officer, the entire Management, and Senior Management Committees.

Responsibilities

The Board of Directors are accountable to the shareholders for the creation and delivery of strong sustainable financial performance and long term sustainable shareholder value by providing effective governance over the Bank's affairs. The Board determines the strategic objectives and policies of KFH-Bahrain to deliver long term value and provide overall strategic direction within a framework of rewards, incentives and controls.

The Chairman is responsible for leading the Board, ensuring its effectiveness and monitoring its performance. The Board currently has four committees: the Audit Committee, the Risk, Governance & Compliance Committee; the Executive Committee; and the Nomination and Remuneration Committee. Each committee has specific terms of reference that define its scope, powers and responsibilities.

Information about the Board structure, the managerial structure, the qualifications and experience of each Board Member, the qualification and experience of the Chairman, the Managing Director and Chief Executive Officer and the Executive Managers are provided in Public Disclosure (enclosed to this Annual Report).

The remuneration/incentive structure of the Managing Director and the Chief Executive Officer, Board Members and Shari'a Board Members is discussed at Board level. Remuneration of the Managing Director and the Chief Executive Officer and Board Members is approved in the AGM.

Corporate Governance Charter

We have developed a Corporate Governance Charter that provides the basis for promoting high standards of corporate governance in KFH-Bahrain. It sets out high level guidelines and lays the foundation for our overall corporate governance system. It outlines the key elements of an effective corporate governance framework and

Corporate Governance

describes the roles and responsibilities of the Board of Directors in its review, approval and monitoring of the Bank's strategy and financial performance. It also contains the terms of reference for all the Board and Senior Management Committees.

Code of Conduct

The Bank has developed a Code of Conduct that covers the principles, policies and laws that govern the Bank's activities. The Code also addresses:

- Responsibility of Approved Persons to:
  - ensure confidentiality of information
  - ensure independent decision making
  - ensure that their conduct in general is in the best interests of the Bank
- Prohibition against the use of insider information
- Polices to prohibit conflicts of interest.

Compliance

KFH-Bahrain is committed to conducting its business in a Shari'a compliant manner, to delivering its strategic and operational objectives with the highest professional and ethical standards and to complying fully with the spirit and letter of any applicable regulatory requirements, Kingdom of Bahrain legislation, code of best practice promoted by industry associations and internal codes of conduct.

In this context, and in compliance with the Central Bank of Bahrain requirements, we have established an independent Compliance Department that is responsible for ensuring the appropriate implementation of the Compliance Framework, and adherence to the Compliance Policies documented in the Board-approved Compliance Manual. The Compliance Framework is established to help us efficiently realise our goals while complying with applicable laws, rules and regulations.

The primary purpose of the Compliance Manual is to establish a strong compliance culture within KFH-Bahrain by giving us a framework of policies and guidelines to which we must adhere to ensure appropriate management of Compliance Risk and to fulfill our duties relating to regulatory requirements. It also ensures that we adhere to all applicable regulations, and that any violations are identified and corrected on a timely basis. The Manual provides the basis for the creation of our Compliance Function Infrastructure, facilitating the optimisation of shareholder value. By implementing these guidelines we will be able to monitor and control Compliance Risk more effectively.

The Board of Directors has the overall responsibility for ensuring that all activities of KFH-Bahrain are conducted in full compliance with applicable laws and regulations.

The Board has approved the Compliance Manual. The Manual shall be reviewed as and when there is a significant change in KFH-Bahrain's business model or regulatory requirements. Manual review ensures that it is in line with our current practices or any other changes introduced by the CBB and other regulatory authorities that may have an impact on the Compliance Function.

We have also adopted Compliance Procedures which allow us to appropriately manage compliance risk and discharge our responsibilities relating to regulatory authorities. The objective of the procedures is to ensure that:

- All regulatory requirements are adequately complied with;
- Potential non-compliance is detected, reported and rectified in a timely manner; and
- Non-compliances are reported to the appropriate statutory body and internally to the Managing Director & Chief Executive Officer and Risk, Governance and Compliance Committee.

Disclosures

A Public Disclosure Policy has been developed as part of our commitment to the highest standards of transparency and fairness in disclosing information for the benefit of all stakeholders. The Public Disclosure Policy provides the approach adopted towards managing and controlling the process of public disclosure of financial and non-financial communication to shareholders and customers, ensuring that the information disseminated complies with the CBB directives and is accurate, complete and fairly presents KFH-Bahrain's financial position and results of operations in all material respects within regulatory-stipulated timelines. The purpose of the policy is to assist the Board, Senior Management and relevant departments to understand their roles and responsibilities in the Disclosure Process. We are committed to disclosing information to the public in a manner consistent with guidelines provided by the Central Bank of Bahrain, and in line with Basel II Pillar III requirements.

Anti-Money Laundering

We have adopted detailed policies and procedures in line with the Central Bank of Bahrain's directives to combat money laundering, financing of terrorism and other financial crimes. Detailed procedures are included upon account opening and through customer due diligence, as well as in internal and external reporting, staff training and record keeping. It helps all members of management and staff to understand:

- The legal requirements and the different penalties for non-compliance;
- What the Bank requires of all members of management and staff; and
- How to recognise money laundering and the action one must take.

It is a firm policy of KFH-Bahrain not to allow itself to be directly or indirectly used by any elements for unlawful activities. From our perspective, the prevention of money laundering, financing of terrorism and other financial crimes has three objectives:

- Ethical – taking part in the fight against crime;
- Professional – ensuring that we are not involved in recycling the proceeds of crime that could call into question the Bank's reputation and integrity; and
- Legal – complying with Bahrain legislation and regulations that impose a series of specific obligations on financial institutions and their employees.

We have appointed a Money Laundering Reporting Officer and a Deputy Money Laundering Officer pursuant to the provisions of the CBB rulebook volume 2 who are responsible for ensuring the appropriate implementation of and adherence to the AML Policies and Procedures as approved by the Board.

Corporate Communication Strategies

We maintain an effective communication strategy by means of deploying a board approved Corporate Communication Manual that enables both the Board and Management to communicate effectively with stakeholders and the general public. Main communication channels include the annual report, public disclosure, corporate website and corporate brochure, and regular announcements in the appropriate local press.

The Communications Policy has been approved by the Board. This Policy ensures the disclosure of all relevant information to stakeholders on a timely basis in and the provision of at least the last three years of financial data on KFH-Bahrain's website.

We have a Corporate Communication Department which is responsible for communicating new product information through various channels of communication which includes websites, direct mailers, electronic mail and local media.

The department supports the Compliance Officer on any communication required to our investors and customers. The Corporate Communication Department has assisted, where required, with all business units of KFH-Bahrain in support of their awareness programmes or marketing of new products and services for the year 2011.

The department has assisted throughout the year with its various social functions and charitable contributions. These are highlighted in the Corporate Social Responsibility section of the Annual Report.

Consumer / Investor Awareness Programmes

We employ a range of communication channels to reach consumers and investors to create awareness of our products, services and investments.

Communication channels for consumers normally adopt an integrated approach, depending on the level of exposure and awareness required. This can include mass media, publishing advertisements in the press and magazine publications, billboards, lamp posts, LED display boards, direct mail, SMS messaging and emails. The external communication programme is supported by in-branch communication including: roll-ups, banners, posters, leaflets, flyers, brochures, danglers and online media via the KFH-Bahrain website, Call Center and eBanking site.

Communication to investors is predominantly via Private Placement Memorandums and Investor Reports. We also communicate our investments via our website. All other investment communication is directly via our Investment Placement Team as part of its investor relations programmes.

Complaints and Feedback

We have appointed a Complaints Officer to manage customer complaints and ensure that all complaints are properly addressed and issues are solved in a timely manner. After receiving a complaint, the Complaints Officer internally addresses the complaint to the concerned department for their response. After analysing the responses of the concerned department the Complaints Officer finds a suitable solution and communicates it to the complainant. There are various channels in place to assist in receiving feedback/complaints from customers including our website and suggestion boxes at each of our branches.

Other Disclosures

The information relating to transactions with related parties is reported in KFH-Bahrain's Financial Statements.

Page 92 of the Financial Statements provides the information on systems and controls employed by KFH-Bahrain to ensure Shari'a compliance, which includes information on any non-Shari'a compliant earnings and expenditures, and the manner in which they were disposed of, as well as KFH-Bahrain's annual zakat contributions.

As a concerned corporate citizen and a leading Bahrain-based Islamic financial institution, we are committed to contributing towards the social well-being of the Bahraini local community. We are also dedicated to supporting the business and economic development of the Kingdom, in-line with the principles of Shari'a and ethical approach to business.

Throughout 2011, KFH-Bahrain continued to implement a comprehensive corporate social responsibility (CSR) programme comprising of financial and practical support for a range of charitable, educational, medical, cultural, sporting and social organizations and other deserving causes. We also participated in and sponsored a number of major initiatives and events aimed at supporting Islamic banking and finance with a view to contributing towards the further development of business and the economy. Some examples of our CSR activities during the year are as follows:

Developing Tomorrow's Sporting Champions

- Sponsored the Manama Club Bankers' Cup.
- Sponsored the Sh Nasser's 5th Football Championship.
- Sponsored the Sh Nasser Royal Endurance Championship.
- Sponsored the Busaiteen Sports and Cultural Club.
- Sponsored the Bahrain Football Association.
- Sponsored the Bahrain Golf Association.

Supporting Islamic Banking and Finance

- AAOIFI – World Bank Annual Conference.
- Platinum Sponsor of the Annual Conference of the Accounting and Auditing Organisation of Islamic Financial Institutions (AAOIFI) in Bahrain.
- Gold Strategic Partners and Gala Dinner Hosts of The World Islamic Banking Conference.

Promoting Health, Education and Leadership

- Sponsor of the Sophia Antipolis Mentorship Programme Graduation Ceremony.
- Sponsor of the 10th International Entrepreneurship Forum 2011.
- Sponsor of Young Arab Leaders Forum.
- Sponsor Shaikha Hessa Girls' School e-learning classrooms
- Sponsor BDF Royal Medical Services – Laser Device

Corporate Social Responsibility

Shari'a Board Report

In the Name of Allah Most Gracious Most Merciful
Praise be to Allah, and may peace and blessings be upon our Prophet Muhammad, his family and companions.

To the shareholders of Kuwait Finance House-Bahrain:

Peace, mercy and blessings of God upon you:

According to the letter of assignment, we present the following report.

We have reviewed the products used and the contracts relating to transactions, applications and practices made by the Kuwait Finance House - Bahrain during the period ending by December 31, 2011. We have also made due diligence to express our opinion regarding whether Kuwait Finance House - Bahrain has committed to the principles and rules of the Shari'a, as well as our advisory opinions, decisions and directives.

Responsibility of Management:
The Management is responsible for making ensure that Kuwait Finance House - Bahrain operates in accordance with the provisions and principles of Islamic Law, while our responsibility is restricted and confined to expression of an independent opinion based on our observations of the Bank's operations, as well as preparations of a report for you.

Scope of work of the Fatwa and Shari'a Supervisory Board:
We have reviewed and adopted forms of contracts and agreements. We also reviewed various processes relating to all transactions of Kuwait Finance House - Bahrain, with shareholders, investors and others. We have selected random samples of such transactions according to the Annual Shari'a Auditing Plan covering all departments, as well as the periodic reports filed by the Head of Shari'a Department regarding the audit operations, field visits, the operations and application of Fatwas and decisions issued by the Board.

We have planned and implemented our task with the aim of obtaining all the information and explanations which we considered necessary to provide us with sufficient evidence to give reasonable assurance that Kuwait Finance House - Bahrain did not violate the provisions of the rules and principles of Islamic Shari'a.

Opinion of the Board:

a) The reviewed contracts and transactions entered into by the Kuwait Finance House - Bahrain during the period ending by 31/12/2011, were in accordance with the rules and principles of Islamic Shari'a.

b) The distribution of profits and loading of losses on the investment accounts were in line with the base adopted and approved by us according to the rules and principles of Islamic Law.

c) All the gains made from Haram (prohibited by Islam Shari'a rules) sources or methods have been set aside in a separate account and spent on charitable purposes.

d) Zakat was calculated in accordance with the rules of Islamic Shari'a.

The Board approves the report based on the reviewed periodic reports filed by the Shari'a Department Management.

The Board thanks the top management, departments and staff for their good cooperation with it and their commitment to its decisions. The Board pray to God Almighty to bring them success.

May God's mercy and blessings upon you. Report date: 12-1-2012

Sheikh Dr. / Ajeel bin Jassem Al Nashmi	**Dr. Sheikh / Khalid bin Madhkoor Al Madhkoor**	**Dr. Sheikh / Mohammed Abdul Razak Tabtabai**
Chairman	Member	Member

Independent Auditors' Report

to the Shareholders of Kuwait Finance House (Bahrain) B.S.C. (c)

We have audited the accompanying consolidated statement of financial position of Kuwait Finance House (Bahrain) B.S.C. (c) [the "Bank"] and its subsidiaries [together the "Group"] as of 31 December 2011, and the related consolidated statements of income, cash flows, changes in owners' equity, and changes in off-balance sheet equity of investment account holders for the year then ended and a summary of significant accounting policies and other explanatory information. These consolidated financial statements and the Group's undertaking to operate in accordance with Islamic Shari'a Rules and Principles are the responsibility of the Bank's Board of Directors. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with Auditing Standards for Islamic Financial Institutions issued by the Accounting and Auditing Organisation for Islamic Financial Institutions ["AAOIFI"]. 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 consolidated financial statements presentation. We believe that our audit provides a reasonable basis for our opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as of 31 December 2011, the results of its operations, its cash flows, changes in equity and changes in off-balance sheet equity of investment account holders for the year then ended in accordance with the Financial Accounting Standards issued by AAOIFI.

Other Matters

As required by the Bahrain Commercial Companies Law and the Central Bank of Bahrain (CBB) Rule Book (Volume 2), we report that:

a) the Bank has maintained proper accounting records and the consolidated financial statements are in agreement therewith; and

b) the financial information contained in the directors' 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 and 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. The Bank has also complied with the Islamic Shari'a Rules and Principles as determined by the Shari'a Supervisory Board of the Bank.

Ernst + Young

7TH February 2012
Manama, Kingdom of Bahrain

Consolidated Financial Statements

Consolidated Statement of Financial Position

At 31 December 2011

	Note	2011 BD 000	2010 BD 000
ASSETS			
Cash and balances with banks and Central Bank of Bahrain	6	**48,230**	38,968
Murabaha and due from banks	7	**102,212**	51,370
Financing contracts with customers	8	**601,225**	640,391
Investments	9	**285,821**	257,340
Investment in joint ventures and associates	10	**123,217**	85,994
Investment properties	11	**152,315**	143,073
Receivables, prepayments and other assets	12	**152,247**	158,331
Goodwill and intangibles	13	**27,764**	28,644
Premises and equipment		**44,323**	42,561
TOTAL ASSETS		**1,537,354**	1,446,672
LIABILITIES, EQUITY OF INVESTMENT ACCOUNT HOLDERS, AND OWNERS' EQUITY			
LIABILITIES			
Customers' current accounts		**73,802**	55,780
Murabaha and due to banks	14	**213,441**	246,406
Murabaha and due to non-banks		**290,688**	187,785
Other liabilities	16	**41,025**	44,067
Subordinated murabaha payable	17	**100,186**	99,423
		719,142	633,461
EQUITY OF INVESTMENT ACCOUNT HOLDERS	18	**445,288**	452,963
OWNERS' EQUITY			
Equity attributable to shareholders of the parent			
Share capital	19	**177,140**	177,140
Share premium	19	**71,403**	71,403
Statutory reserve	19	**14,312**	13,353
General reserve	19	**28,236**	28,236
Available for sale reserve	19	**333**	(4,784)
Investment revaluation reserve	19	**43,661**	43,473
Foreign currency translation reserve	19	**(1,440)**	(1,446)
Retained earnings	19	**16,640**	8,201
		350,285	335,576
Non-controlling stakeholders		**22,639**	24,672
		372,924	360,248
TOTAL LIABILITIES, EQUITY OF INVESTMENT ACCOUNT HOLDERS AND OWNERS' EQUITY		**1,537,354**	1,446,672
OFF BALANCE SHEET:			
EQUITY OF INVESTMENT ACCOUNT HOLDERS		**56,553**	87,031
COMMITMENTS AND CONTINGENT ITEMS	21	**43,665**	44,850

Bader Abdul Muhsen Al-Mukhaizeem
Chairman of the
Board of Directors

Abdulhakeem Yaqoub Alkhayyat
Managing Director and
Chief Executive Officer

The attached notes 1 to 39 form part of these consolidated financial statements.

Consolidated Statement of Income

For the year ended 31 December 2011

	Note	2011 BD 000	2010 BD 000
Income from retail and corporate banking activities	22	**45,421**	49,616
Income from investment activities	23	**24,951**	19,115
Share of loss of joint ventures and associates	10	**(5,833)**	(3,163)
Other income	25	**12,469**	10,103
Operating income		**77,008**	75,671
Return on equity of investment account holders, net of mudarib share	18	**(12,124)**	(13,299)
Profit on murabaha and due to banks, murabaha and due to			
non-banks and subordinated murabaha payable	28	**(14,023)**	(12,380)
Net operating income		**50,861**	49,992
Staff costs		**14,630**	13,930
Depreciation		**7,263**	9,357
Provisions	26	**4,095**	512
Other expenses	27	**18,061**	18,775
Total operating expenses		**44,049**	42,574
Net income before adjustment for non-controlling stakeholders		**6,812**	7,418
Adjustment attributable to non-controlling stakeholders		**2,774**	1,907
NET INCOME ATTRIBUTABLE TO SHAREHOLDERS OF THE PARENT		**9,586**	9,325

The attached notes 1 to 39 form part of these consolidated financial statements.

Consolidated Statement of Changes in Owners' Equity

For the year ended 31 December 2011

	Attributable to shareholders of the parent										
	Share capital BD 000	Share premium BD 000	Statutory reserve BD 000	General reserve BD 000	Available for sale reserve BD 000	Investment revaluation reserve BD 000	Foreign currency translation reserve BD 000	Retained earnings BD 000	Total BD 000	Non-controlling stakeholders BD 000	Total owners' equity BD 000
Balance at 1 January 2011	177,140	71,403	13,353	28,236	(4,784)	43,473	(1,446)	8,201	335,576	24,672	360,248
Net income for the year	-	-	-	-	-	-	-	9,586	9,586	(2,774)	6,812
Other comprehensive income for the year (note 20)	-	-	-	-	5,117	-	6	-	5,123	-	5,123
Total comprehensive income for the year	-	-	-	-	5,117	-	6	9,586	14,709	(2,774)	11,935
Net transfer to investment revaluation reserve	-	-	-	-	-	188	-	(188)	-	-	-
Transfer to statutory reserve	-	-	959	-	-	-	-	(959)	-	-	-
Net movement in share of non - controlling stakeholders	-	-	-	-	-	-	-	-	-	741	741
Balance at 31 December 2011	**177,140**	**71,403**	**14,312**	**28,236**	**333**	**43,661**	**(1,440)**	**16,640**	**350,285**	**22,639**	**372,924**
Balance at 1 January 2010	177,140	71,403	12,420	28,236	(5,984)	37,043	(1,688)	6,239	324,809	26,305	351,114
Change due to FAS 25 (note 9)	-	-	-	-	-	7,351	-	(7,351)	-	-	-
Net income for the year	-	-	-	-	-	-	-	9,325	9,325	(1,907)	7,418
Other comprehensive income for the year (note 20)	-	-	-	-	1,200	-	242	-	1,442	-	1,442
Total comprehensive income for the year	-	-	-	-	1,200	-	242	9,325	10,767	(1,907)	8,860
Net transfer from investment revaluation reserve	-	-	-	-	-	(921)	-	921	-	-	-
Transfer to statutory reserve	-	-	933	-	-	-	-	(933)	-	-	-
Net movement in share of non - controlling stakeholders	-	-	-	-	-	-	-	-	-	274	274
Balance at 31 December 2010	177,140	71,403	13,353	28,236	(4,784)	43,473	(1,446)	8,201	335,576	24,672	360,248

The attached notes 1 to 39 form part of these consolidated financial statements.

Consolidated Statement of Cash Flows

For the year ended 31 December 2011

	Note	2011 BD 000	2010 BD 000
OPERATING ACTIVITIES			
Net income before adjustment for non-controlling stakeholders		**6,812**	7,418
Adjustments for:			
Share of loss of joint ventures and associates	10	**5,833**	3,163
Depreciation		**7,263**	9,357
Provisions	26	**4,095**	512
Net unrealised gain on investments	23	**(10,651)**	(2,406)
Loss (gain) on sale of investments	23	**2,240**	(14,294)
Net unrealised gain on investment properties	23	**(1,129)**	-
Net gain on sale of investment properties	23	**(11,916)**	(65)
Operating income before changes in operating assets and liabilities		**2,547**	3,685
Changes in operating assets and liabilities:			
Mandatory reserve with Central Bank of Bahrain	6	**(6,055)**	610
Financing contracts with customers		**38,765**	17,845
Receivables, prepayments and other assets		**(3,573)**	(28,853)
Murabaha and due to banks		**(32,202)**	93,668
Murabaha and due to non-banks		**102,903**	3,837
Customers' current accounts		**18,022**	3,625
Other liabilities		**(3,042)**	11,333
Net cash from operating activities		**117,365**	105,750
INVESTING ACTIVITIES			
Purchase of investments		**(42,895)**	(41,591)
Proceeds from sale / maturity of investments		**35,894**	20,364
Purchase of investments in joint ventures	10	**(40,211)**	(3,855)
Purchase / construction of investment properties	11	**(5,752)**	(5,472)
Proceeds from sale of investment properties		**8,608**	415
Purchase of equipment		**(12,026)**	(4,330)
Net cash used in investing activities		**(56,382)**	(34,469)
FINANCING ACTIVITIES			
Net movement in equity of investment account holders		**(7,675)**	(46,330)
Net movement in share of non - controlling stakeholders		**741**	274
Net cash used in financing activities		**(6,934)**	(46,056)
NET INCREASE IN CASH AND CASH EQUIVALENTS		**54,049**	25,225
Cash and cash equivalents at 1 January		**66,718**	41,493
CASH AND CASH EQUIVALENTS AT 31 DECEMBER	29	**120,767**	66,718

The attached notes 1 to 39 form part of these consolidated financial statements.

Consolidated Statement of Changes in Off-Balance Sheet Equity of Investment Account Holders

For the year ended 31 December 2011

	Balance at 1 January 2011 BD 000	Additional Investments BD 000	Gross Income BD 000	Mudarib Share BD 000	Withdrawals / distributions BD 000	Balance at 31 December 2011 BD 000
Murabaha contracts	**84,584**	**56,985**	**5,944**	**(568)**	**(91,370)**	**55,575**
Ijarah Muntahia Bittamleek contracts	**2,447**	**-**	**107**	**(24)**	**(1,552)**	**978**
	87,031	**56,985**	**6,051**	**(592)**	**(92,922)**	**56,553**

	Balance at 1 January 2010 BD 000	Additional Investments BD 000	Gross Income BD 000	Mudarib Share BD 000	Withdrawals / distributions BD 000	Balance at 31 December 2010 BD 000
Murabaha contracts	68,897	80,328	5,533	(377)	(69,797)	84,584
Ijarah Muntahia Bittamleek contracts	5,299	-	372	(88)	(3,136)	2,447
	74,196	80,328	5,905	(465)	(72,933)	87,031

The attached notes 1 to 39 form part of these consolidated financial statements.

1 CORPORATE INFORMATION

Kuwait Finance House (Bahrain) B.S.C. (c) ["the Bank"] is a closed joint stock company incorporated in the Kingdom of Bahrain on 22 January 2002 under the Bahrain Commercial Companies Law No. 21/2001 and is registered with the Ministry of Industry and Commerce under commercial registration (CR) number 48128. The Bank is regulated and supervised by the Central Bank of Bahrain (the "CBB") and has an Islamic retail banking license. The Bank operates under Islamic principles and in accordance with all the relevant regulatory guidelines for Islamic banks issued by the CBB. The address of the Bank's registered office is Bahrain World Trade Centre, West Tower, Isa Al Kabeer Avenue, Manama 316, P.O. Box 2066, Manama, Kingdom of Bahrain.

The Bank offers a full range of Islamic banking services and products. The activities of the Bank include accepting Shari'a money placements/deposits, managing Shari'a profit sharing investment accounts, offering Shari'a financing contracts, dealing in Shari'a compliant financial instruments as principal/agent, managing Shari'a compliant financial instruments and other activities permitted under the CBB's Regulated Islamic Banking Services as defined in the licensing framework.

The Bank is a subsidiary of Kuwait Finance House K.S.C. (the "ultimate parent"), a public company incorporated in the State of Kuwait and listed at the Kuwait Stock Exchange. The ultimate parent is regulated and supervised by the Central Bank of Kuwait. The Bank's Shari'a Supervisory Board is entrusted to ensure the Group's adherence to Shari'a rules and principles in its transactions and activities.

The Bank and its subsidiaries (together the "Group") operate in the Kingdom of Bahrain, Hashemite Kingdom of Jordan and the United Kingdom. The activities of the Bank's key subsidiaries are mentioned in note 4.

The Bank has nine branches (2010: nine), all operating in the Kingdom of Bahrain.

The consolidated financial statements were authorised for issue in accordance with a resolution of the Board of Directors passed on 7 February 2012.

2 BASIS OF PREPARATION

The consolidated financial statements have been prepared under the historical cost basis, except for investments and investment properties that have been measured at fair value. The consolidated financial statements are presented in Bahraini Dinars ("BD") which is the functional currency of the Bank. All the values are rounded to the nearest BD thousand, unless otherwise indicated.

Statement of Compliance

The consolidated financial statements of the Group have been prepared in accordance with the Financial Accounting Standards ("FAS") issued by the Accounting and Auditing Organization for Islamic Financial Institutions ("AAOIFI"), the Shari'a rules and principles as determined by the Shari'a Supervisory Board of the Bank, the Bahrain Commercial Companies Law, Central Bank of Bahrain ("CBB") and the Financial Institutions Law, the CBB Rule Book (Volume 2 and applicable provisions of Volume 6) and CBB directives. In accordance with the requirement of AAOIFI, for matters not covered by FAS, the Group uses the relevant International Financial Reporting Standards ("IFRS") issued by the International Accounting Standards Board ("IASB").

Basis of consolidation

The consolidated financial statements comprise the financial statements of the Bank and its subsidiaries as at 31 December 2011. The financial statements of the subsidiaries are prepared for the same reporting year as the Bank, using consistent accounting policies.

All intra-group balances, transactions, income and expenses and unrealised gains and losses resulting from intra-group transactions are eliminated in full.

Subsidiaries are fully consolidated from the date on which control is transferred to the Group and continue to be consolidated until the date when such control ceases. Control is achieved where the Group has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The results of subsidiaries acquired or disposed of during the year, if any, are included in the consolidated statement of income from the date of acquisition or up to the date of disposal, as appropriate.

Share of non-controlling stakeholders represents the portion of profit or loss and net assets not held by the Group and are presented separately in the consolidated statement of income and within owners' equity in the consolidated statement of financial position, separately from the equity attributable to shareholders of the parent.

3 ACCOUNTING POLICIES

3.1 Significant accounting judgments and estimates

The preparation of the Group's financial statements requires management to make judgments, estimates and assumptions that affect the amounts reported in the consolidated financial statements. The most significant uses of judgments and estimates are as follows:

Going concern

The Group'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 the foreseeable future. Furthermore, the Board of Directors is not aware of any material uncertainties that may cast significant doubt upon the Group's ability to continue as a going concern. Therefore, the consolidated financial statements continue to be prepared on a going concern basis.

Fair value of unquoted equity securities and investment properties

Fair value is determined for each investment individually in accordance with the valuation policies set out in note 3.3.23. Where the fair values of the Group's unquoted equity securities cannot be derived from an active market, they are derived using a variety of valuation techniques. Judgment by management is required to establish fair values through the use of appropriate valuation models, consideration of comparable assets, discount rates and the assumptions used to forecast cash flows.

Investment properties and investments in real estate projects are carried at fair value as determined by independent real estate valuation experts. The determination of the fair value for such assets requires the use of judgment and estimates by the independent valuation experts that are based on local market conditions existing at the date of the statement of financial position.

Impairment provisions against financing contracts with customers

The Group reviews its financing contracts at each reporting date to assess whether an impairment provision should be recorded in the consolidated financial statements. In particular, judgment by management is required in the estimation of the amount and timing of future cash flows when determining the level of provision required. Such estimates are based on assumptions about factors involving varying degrees of judgment and uncertainty and actual results may differ resulting in future changes to the provisions.

In addition to specific provisions against individually significant financing contracts, the Group also makes a collective impairment provision against exposures which, although not specifically identified as requiring a specific provision, have a greater risk of default than when originally granted. This takes into consideration, factors such as any deterioration in country risk, industry, and technological obsolescence, as well as identified structural weaknesses or deterioration in cash flows.

Impairment of investments at fair value through equity

The Group treats investments carried at fair value through equity as impaired when there is a significant or prolonged decline in the fair value below its cost or where other objective evidence of impairment exists. The determination of what is 'significant' or 'prolonged' requires judgment. The Group evaluates factors, such as the historical share price volatility for comparable quoted equities and future cash flows and the discount factors for comparable unquoted equities.

Liquidity

The Group manages its liquidity through consideration of the maturity profile of its assets and liabilities which is set out in the liquidity risk disclosures in Note 34. This requires judgment when determining the maturity of assets and liabilities with no specific maturities.

3.2 Adoption of new and amended standards and interpretations

The accounting policies are consistent with those of the previous year except for the following new and amended IFRS, FAS and IFRIC interpretations effective as of 1 January 2011:

- IAS 24 Related Party Transactions (amendment)
- IFRS 7 Financial Instruments: Disclosures (amendment)
- IAS 32 Financial Instruments: Presentation (amendment)
- FAS 25 Investment in sukuk, shares and similar instruments

3 ACCOUNTING POLICIES (continued)

The adoption of the standards or interpretations is described below:

IAS 24 Related Party Transactions (Amendment)
The IASB has issued an amendment to IAS 24 that clarifies the identification of related party relationships, particularly in relation to significant influence or joint controls. The new definitions emphasise a symmetrical view on related party relationship as well as clarifying in which circumstances persons and key management personnel affect related party relationship of an entity. Secondly, the amendment introduces an exemption from the general related party disclosure requirements for transactions with a government and entities that are controlled, jointly controlled or significantly influenced by the same government as the reporting entity. The adoption of the amendment did not have any impact on the financial position or performance of the Group.

IFRS 7 Financial instruments: Disclosures (amendment)
These amendments introduced new disclosure requirements for transfers of financial assets, including disclosures for:

- financial assets that are not derecognised in their entirety; and
- financial assets that are derecognised in their entirety but for which the entity retains continuing involvement.

The amendment has had no effect on the disclosures made by the Group as the Group has not issued these types of instruments.

IAS 32 Financial Instruments: Presentation (Amendment)
The amendment alters the definition of a financial liability in IAS 32 to enable entities to classify rights issues and certain options or warrants as equity instruments. The amendment is applicable if the rights are given prorate to all of the existing owners of the same class of an entity's non-derivative equity instruments, to acquire a fixed number of the entity's own equity instruments for a fixed amount in any currency. The amendment has had no effect on the financial position or performance of the Group as the Group has not issued these type of instruments.

FAS 25 Investment in sukuk, shares and similar instruments
FAS 25 sets out principles for recognition, measurement, presentation and disclosure of investment in sukuk, shares and other investments that exhibit the characteristics of debt and equity instruments. The adoption of FAS 25 had an effect on the classification and measurement of the Group's financial assets as explained in note 9.

3.3 Summary of significant accounting policies
The significant accounting policies adopted in the preparation of the consolidated financial statements are set out below:

3.3.1 Foreign currency translation
The consolidated financial statements are presented in Bahraini Dinars, which is Group's presentation currency. Each entity in the Group determines its own functional currency and items included in the financial statements of each entity are measured using that functional currency.

(i) Transactions and balances
Transactions in foreign currencies are initially recorded in the functional currency using the rate of exchange prevailing at the date of the transaction.

Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the date of statement of financial position. All differences are taken to the consolidated statement of income with the exception of all monetary items that provide an effective protection for a net investment in a foreign operation. These are recognised in other comprehensive income until the disposal of the net investment, at which time they are recognised in the consolidated statement of income.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial recognition. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value is determined. Exchange gains and losses on non-monetary items classified as "fair value through statement of income" are taken to the consolidated statement on income and for items classified as "fair value through equity" such differences are taken to the consolidated statement of comprehensive income. Any goodwill arising on the acquisition of a foreign operation and any fair value adjustments to the carrying amounts of assets and liabilities arising on the acquisition are treated as assets and liabilities of the foreign operations and translated at closing rate.

3 ACCOUNTING POLICIES (continued)

(ii) Group companies
As at the reporting date, the assets and liabilities of subsidiaries are translated into the Group's presentation currency (Bahraini Dinars) at the rate of exchange prevailing at the date of statement of financial position, and their statements of income are translated at the weighted average exchange rates for the year. Exchange differences arising on translation are recognised in other comprehensive income. On disposal of a foreign subsidiary, the cumulative amount recognised in other comprehensive income relating to that particular foreign subsidiary is recognised in the consolidated statement of income in 'Other operating expenses' or 'Other income'.

3.3.2 Financial instruments - Initial recognition and subsequent measurement

Date of recognition
All financial assets and liabilities are initially recognised on the trade date, i.e. the date that the Group becomes a party to the contractual provisions of the instrument.

Initial measurement of financial instruments
The classification of financial instruments at initial recognition depends on the purpose and the management's intention for which the financial instruments were acquired and their characteristics. All financial instruments are measured initially at their fair value plus transaction costs, except in the case of financial assets recorded at fair value through statement of income.

(i) Murabaha receivables from banks
These are international commodity murabaha transactions. The Bank arranges a murabaha transaction by buying a commodity (which represents the object of the murabaha) and then resells this commodity to the beneficiary murabeh (after computing a profit margin). The sale price (cost plus the profit margin) is paid either lump sum at maturity or in installments by the murabeh over the agreed period.

Murabaha receivables from banks are stated net of deferred profits and provision for impairment, if any.

(ii) Financing contracts with customers

(a) Murabaha
Murabaha represents the sale of goods at cost plus an agreed profit. Murabaha receivables consist of deferred sales transaction agreements and are stated net of deferred profits, any amounts written off and provision for impairment, if any. Promise made in the murabaha to the purchase orderer is not obligatory upon the customer.

(b) Ijarah Muntahia Bittamleek
Ijarah Muntahia Bittamleek mainly comprise of land and buildings and certain other assets. Ijarah Muntahia Bittamleek is a lease whereby the legal title of the leased asset passes to the lessee at the end of the ijarah (lease term), provided that all ijarah installments are settled.

Assets under Ijarah Muntahia Bittamleek are depreciated at rates calculated to write off the cost of each asset over its useful life to its residual value.

(c) Musharaka
Musharaka contracts represents a partnership between the Bank and a customer whereby each party contributes to the capital in equal or varying proportions to establish a new project or share in an existing one, and whereby each of the parties becomes an owner of the capital on a permanent or declining basis and shall have a share of profits or losses. These are stated at the fair value of consideration given less any amounts written off and provision for impairment, if any.

(iii) Investments
Investments are classified as follows:

- Investments at fair value through statement of income
- Investments at fair value through equity
- Investments at amortised cost

3 ACCOUNTING POLICIES (continued)

(a) Investments at fair value through statement of income
Investments at fair value through statement of income include investments designated upon initial recognition as investments at fair value through statement of income.

In addition to the above, the Group utilises the exemption available to associates and joint ventures as per IAS 28, IAS 31 and FAS 24 as applicable to venture capital organisations and classifies such investments as "investments at fair value through statement of income". Financial assets carried at fair value through statement of income are recognised at fair value, with transaction costs recognised in the consolidated statement of income.

Investments classified as 'at fair value through statement of income' are subsequently measured at fair value. The unrealised gains and losses arising from the remeasurement to fair value are included in the consolidated statement of income.

(b) Investments at fair value through equity
Investments at fair value through equity are those which are designated as such or are not classified as carried at fair value through statement of income or at amortised cost. These include investments in equity securities and managed funds.

After initial measurement, investments at fair value through equity are subsequently measured at fair value. Unrealised gains and losses are recognised in statement of comprehensive income and then transferred to the 'available for sale reserve' in the consolidated statement of changes in equity. When the investment is disposed of or determined to be impaired, the cumulative gain or loss, previously transferred to the available for sale reserve, is recognised in the consolidated statement of income. Where the Group holds more than one investment in the same security they are deemed to be disposed off on a weighted average basis. Profit earned whilst holding investments at fair value through equity is reported as 'Income from investment activities' using the effective profit rate method.

(c) Investments at amortised cost
Non-derivative financial assets with fixed or determinable payments and fixed maturities are classified as such when the Group has the positive intention and ability to hold them to maturity. After initial measurement, these investments are measured at amortised cost using the effective profit rate (EPR), less impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the EPR. The EPR amortisation is included in the consolidated statement of income. The losses arising from impairment are recognised in the consolidated statement of income under 'provisions'.

(iv) Murabaha and due to banks
This represents funds received from banks on the principles of murabaha contracts and are stated at fair value of consideration received less amounts settled.

(v) Murabaha and due to non banks
These are stated at fair value of consideration received less amounts settled.

(vi) Equity of investment account holders
Equity of investment account holders is invested in murabaha and due from banks, sukuk and financing contracts with customers. No priority is granted to any party for the purpose of distribution of profits. According to the terms of acceptance of the investment account holders funds, 100% of these funds are invested after deductions of mandatory reserve and sufficient operational cash requirements.

Equity of investment account holders is carried at fair value of consideration received less amounts settled. Expenses are allocated to investment accounts in proportion of average equity of investment account holders to total average assets of the Bank.

Income is allocated proportionately between equity of investment account holders and owners' equity on the basis of the average balances outstanding during the year and share of the funds invested.

3 ACCOUNTING POLICIES (continued)

3.3.3 Derecognition of financial assets and financial liabilities

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

- the rights to receive cash flows from the asset have expired; or

- the Group retains the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a "pass-through" arrangement; or

- the Group has transferred its rights to receive cash flows from the asset and either: (a) has transferred substantially all the risks and rewards of the assets, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

When the Group has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Group's continuing involvement in the asset.

(ii) Financial liabilities
A financial liability is derecognised when the obligation specified in the contract is discharged, cancelled or expired.

3.3.4 Impairment of financial assets

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

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

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

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

Financing contracts together with the associated provisions are written off when there is no realistic prospect of future recovery and collateral has been realised or has been transferred to the Group. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognised, the previously recognised impairment loss is increased or reduced in the consolidated statement of income.

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

3 ACCOUNTING POLICIES (continued)

(ii) Investments at fair value through equity
For investments at fair value through equity, the Group assesses at each reporting date whether there is objective evidence that an investment or a group of investments is impaired.

In the case of equity investments classified as "fair value through equity", objective evidence would include a significant or prolonged decline in the fair value of the investment below its cost. Where there is evidence of impairment, the cumulative loss measured as the difference between the acquisition cost and the current fair value less any impairment loss on that investment previously recognised in the consolidated statement of comprehensive income is removed from 'available for sale reserve' and recognised in the consolidated statement of income. Impairment losses on equity investments are not reversed through the consolidated statement of income; increases in their fair value subsequent to impairment are recognised directly in equity.

(iii) Restructured financing contracts with customers
Where possible the Group seeks to restructure financing contracts rather than taking possession of the collaterals. This may involve extending the payment arrangements and the agreement of new conditions. Once the terms have been renegotiated, any impairment is measured using the effective profit rate before the modification of terms of the financing contract and the financing is no longer considered past due. Management continuously reviews restructured financing contracts to ensure that all criteria met and that future payments are likely to occur. The financing contracts continue to be subject to an individual or collective impairment assessment.

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

3.3.6 Land and development costs
Land and development costs consist of cost of land being developed for sale in the ordinary course of business and costs incurred in bringing such land to its saleable condition and is stated at the lower of cost and net realisable value.

Net realisable value is based on estimated selling price less any further costs expected to be incurred on completion and sale.

3.3.7 Recognition of income and expense

(i) Income recognition

(a) Murabaha
Where the income is quantifiable and contractually determined at the commencement of the contract, income is recognised on a time-apportioned basis over the period of the contract based on the principal amounts outstanding. Accrual of income is suspended when the Group believes that the recovery of these amounts may be doubtful.

(b) Ijarah Muntahia Bittamleek
Ijarah income is recognised on a time-apportioned basis, net of depreciation, over the lease term. Accrual of income is suspended when the Group believes that the recovery of these amounts may be doubtful.

(c) Musharaka
Income on musharaka contracts is recognised when the right to receive payment is established or on distribution by the musharek.

(d) Dividends
Dividends from investments in equity securities are recognised when the right to receive the payment is established.

(e) Fees and commission income
Fees and commission income is recognised when earned.

(f) Sale of property under development
Where property is under development and agreement has been reached to sell such property when construction is complete, the Group considers whether the contract comprises:

- contract to construct a property; or
- contract for the sale of a completed property.

3 ACCOUNTING POLICIES (continued)

Where a contract is judged to be for the construction of a property, revenue is recognised using the percentage of completion method as construction progresses. The percentage of work complete is measured based on the costs incurred up until the end of the reporting period as a proportion of total costs expected to be incurred.

Where the contract is judged to be for the sale of a completed property, revenue is recognised when the significant risks and rewards of ownership of the property are transferred to the buyer.

(g) Service income
Revenue from rendering of services is recognised when the services are rendered.

(h) Revenue from sale of goods
Revenue from sales of goods is recognised when the significant risks and rewards of ownership of the goods have passed to the buyer and the amount of revenue can be measured reliably.

i) Group's share as a mudarib
The Group's share as a mudarib for managing the equity of investment account holders is accrued based on the terms and conditions of the related mudaraba agreements whereas, for off balance sheet equity of investment accounts, mudarib share is recognized when distributed.

(ii) Expense recognition

(a) Profit on murabaha payables (banks and non banks)
Profit on these is accrued on a time-apportioned basis over the period of the contract based on the principal amounts outstanding.

(b) Return on equity of investment account holders
Return on equity of investment account holders is based on the income generated from jointly financed assets after deducting mudarib share and is accrued based on the terms and conditions of the underlying mudaraba agreement. Investors' share of income represents income generated from assets financed by investment account holders net off allocated administrative expenses and provisions. The Group's share of profit is deducted from the investors' share of income before distribution to investors.

3.3.8 Investment in associates
An associate is an entity in which the Group has significant influence and which is neither a subsidiary nor a joint venture.

Under the equity method, the investment in the associate is carried in the consolidated statement of financial position at cost plus post acquisition changes in the Group's share of net assets of the associate. Goodwill relating to an associate is included in the carrying amount of the investment and is not amortised nor individually tested for impairment.

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

The consolidated statement of income reflects the share of the results of operations of the associate. Where there has been an income or expense recognised in the other comprehensive income of the associate, the Group recognises its share of any such income or expense, when applicable, in the consolidated statement of comprehensive income. Gains and losses resulting from transactions between the Group and the associate are eliminated to the extent of stake in the associate.

The reporting dates of the associates and the Group are identical and the associates' accounting policies conform to those used by the Group for like transactions and events in similar circumstances.

Upon loss of significant influence over the associate, the Group measures and recognises any retaining investment at its fair value. Any difference between the carrying amount of the associate upon loss of significant influence and the fair value of the retaining investment and proceeds from disposal is recognised in the consolidated statement of income.

3 ACCOUNTING POLICIES (continued)

3.3.9 Investment in joint ventures

The Group has arrangements with other parties which represent joint ventures. These take the form of agreements to share control.

Where the joint venture is established through a stake in a company (a jointly controlled entity), the Group recognises its stake in the entity's assets and liabilities using the equity method of accounting. Under the equity method, the investment in a joint venture is carried in the statement of financial position at cost plus post acquisition changes in the Group's share of its net assets, less distributions received and less impairment in value of individual investments.

3.3.10 Investment properties

Properties held to earn rental income, for capital appreciation or both are classified as investment properties. 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 date of the consolidated statement of financial position. The Group engages independent valuation specialists to determine fair value as at the year end.

Gains or losses arising from changes in the fair values of investment properties are included in the consolidated statement of income in 'Income from investment activities' in the year in which they arise and in case of gains these are appropriated to the investment revaluation reserve in the consolidated statement of changes in equity in accordance with the requirements of AAOIFI. When the investment property is disposed of, the cumulative gain previously transferred to the investment revaluation reserve, is transferred to retained earnings.

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

Transfers are made to investment properties when, and only when, there is a change in use, evidenced by the end of owner occupation or commencement of an operating lease. Transfers are made from investment properties when, and only when, there is a change in use, evidenced by commencement of owner occupation or commencement of development with a view to sale.

3.3.11 Premises and equipment

Premises and equipment are stated at cost excluding the costs of day-to-day servicing, less accumulated depreciation and accumulated impairment in value, if any.

Depreciation is calculated using the straight-line method to write down the cost of premises and equipment to their residual values over their estimated useful lives. Land is not depreciated. The estimated useful lives are as follows:

	Years
Premises	20
Equipment	3 - 7
Motor vehicles and office furniture	2 - 5

An item of premises and equipment is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is recognised in the consolidated statement of income in the year the asset is derecognised.

3.3.12 Business combinations and goodwill

Business combinations are accounted for using the purchase method of accounting. This involves recognising identifiable assets (including previously unrecognised intangible assets) and liabilities (including contingent liabilities and excluding future restructuring) of the acquired business at fair value. Any excess of the cost of acquisition over the fair values of the identifiable net assets acquired is recognised as goodwill. If the cost of acquisition is less than the fair values of the identifiable net assets acquired, the gain on acquisition is recognised directly as income in the consolidated statement of income in the year of acquisition.

3 ACCOUNTING POLICIES (continued)

Goodwill acquired in a business combination is initially measured at cost being the excess of the cost of the business combination over the Group's stake in the net fair value of the identifiable assets, liabilities and contingent liabilities acquired. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill is reviewed for impairment, annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired.

When subsidiaries are sold, the difference between the selling price and the net assets plus cumulative translation differences and related goodwill is recognised in the consolidated statement of income.

3.3.13 Intangible assets

Intangible assets include the value of license rights. Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is their fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less accumulated amortisation and any accumulated impairment losses.

Intangible assets with finite useful lives are amortised over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset maybe impaired. The amortisation period and the amortisation method are reviewed at least at each financial year end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are accounted for by changing the amortisation period or method, as appropriate, and treated as changes in accounting estimates. The amortisation expense on intangible assets with finite useful lives is recognised in the consolidated statement of income. Amortisation of license rights is calculated using the straight-line method to write down the cost of intangible assets to their residual values over its estimated useful life of 10 to 15 years.

3.3.14 Impairment of non financial assets

The Group assesses at each reporting date or more frequently whether there is an indication that a non financial asset may be impaired. If any such indication exists, or when annual impairment testing for an asset is required, the Group makes an estimate of the asset's recoverable amount. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount.

For assets excluding goodwill, an assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If any such indication exists, the recoverable amount is estimated. A previously recognised impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised. If that is the case, the carrying amount of the asset is increased to its recoverable amount. Impairment losses relating to goodwill cannot be reversed for subsequent increase in its recoverable amount in future periods.

3.3.15 Financial guarantees

In the ordinary course of business, the Group provides financial guarantees, consisting of letters of credit, guarantees and acceptances. Financial guarantees are initially recorded in the consolidated statement of financial position at fair value in 'other liabilities' being the premium received. Subsequent to initial recognition, the Group's liability under each guarantee is measured at the higher of the amortised premium and the best estimate of expenditure required to settle any financial obligation arising as a result of the guarantee.

Any increase in the liability relating to financial guarantees is recognised in the consolidated statement of income under 'provisions'. The premium received is recognised in the consolidated statement of income on a straight line basis over the life of the guarantee.

3.3.16 Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) arising from 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 obligation.

3 ACCOUNTING POLICIES (continued)

3.3.17 Segment reporting
Operating segments are reported in a manner consistent with the internal reporting provided to the Chief Operating Decision Maker (CODM). CODM is a person or group that allocates resources to and assesses the performance of the operating segments of the entity. The Group has determined the Managing Director and Chief Executive Officer as its CODM.

3.3.18 Cash and cash equivalents
Cash and cash equivalents comprise of cash and balances with banks and the Central Bank of Bahrain (excluding mandatory reserve) and murabaha and due from banks with original maturity of 90 days or less.

3.3.19 Employees' end of service benefits
Provision is made for leaving indemnity payable under the Bahraini Labor Law applicable to non-Bahraini employees' accumulated periods of service at the consolidated statement of financial position date.

Bahraini employees of the Group are covered by contributions made to the Social Insurance Organisation ("SIO") as a percentage of the employees' salaries. The Group's obligations are limited to these contributions, which are expensed when due. For Bahrainis with basic salaries above a certain threshold, the Bank recognises leaving indemnity in line with the requirements of SIO.

3.3.20 Off balance sheet equity of investment account holders
Off balance sheet equity of investment account holders represents funds received by the Bank on the basis of mudaraba to be invested in specified products as directed by the investment account holders. The assets funded by these funds are managed in a fiduciary capacity by the Bank for which the Bank earns mudarib share. These assets are not included in the consolidated statement of financial position as the Group does not have the right to use or dispose of them except within the conditions laid down in the underlying mudaraba contract.

3.3.21 Earnings prohibited by Shari'a
The Group is committed to avoid recognising any income generated from non-Islamic sources. Accordingly, all non-Islamic income is transferred to charity.

3.3.22 Inventories
Inventories are carried at the lower of cost and net realisable value. When inventories become old or obsolete, an estimate is made of their net realisable value. For individually significant amounts this estimation is performed on an individual basis. Amounts which are not individually significant, but which are old or obsolete, are assessed collectively and an allowance applied according to the inventory type and the degree of ageing or obsolescence, based on historical selling prices.

3.3.23 Fair value of financial instruments
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.

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

- For investments that are traded in organised financial markets, fair value is determined by reference to the quoted market price prevailing on the date of consolidated statement of financial position;

- For private equity investments, fair value is determined using recent buy or sell transactions with third parties that are either completed or are in progress. Where no recent significant transactions have been completed or are in progress, fair value is determined by reference to valuation models, including net present value of estimated future cash flows, and based on earnings before financing cost, tax, depreciation and amortization ("EBITDA") multiples;

- For equity investments which are primarily set up to invest in real estate, fair value is determined by revaluing the underlying real estate properties of these companies based on the valuation performed by independent valuers; and

- Investments in funds, unit trusts, or similar investment entities are carried at the latest net asset valuation provided by the fund administrators.

3 ACCOUNTING POLICIES (continued)

3.3.24 Taxation

There is no tax on corporate income in the Kingdom of Bahrain. Taxation on overseas operations is provided for in accordance with the fiscal regulations of the respective countries in which the Group operates and is included in the accompanying consolidated statement of income under “other operating expenses”.

3.4 Standards issued but not yet effective

Standards issued but not yet effective up to the date of issuance of the Group’s consolidated financial statements are listed below. This listing of standards and interpretations issued are those that the Group reasonably expects to have an impact on disclosures, financial position or performance when applied at a future date. The Group intends to adopt these standards when they become effective.

IAS 1 Financial Statement Presentation

The amendments becomes effective for annual periods beginning on or after 1 July 2012 and require that an entity present separately, the items of other comprehensive income that would be reclassified (or recycled) to profit or loss in the future if certain conditions are met (for example, upon derecognition or settlement), from those that would never be reclassified to profit or loss. The amendment affects presentation only, therefore, will have no impact on the Group’s financial position or performance.

IAS 27 Separate Financial Statements (as revised in 2011)

IAS 27 (2011) supersedes IAS 27 (2008). As a consequence of the new IFRS 10 and IFRS 12, IAS 27 (2011) carries forward the existing accounting and disclosure requirements for separate financial statements, with some minor clarifications.

IAS 27 (2011) is effective for annual periods beginning on or after 1 January 2013 and earlier application is permitted. The Group does not present separate financial statements.

IAS 28 Investments in Associates and Joint Ventures (as revised in 2011)

IAS 28 (2011) supersedes IAS 28 (2008). As a consequence of the new IFRS 11 and IFRS 12, IAS 28 has been renamed IAS 28 Investments in Associates and Joint Ventures, and describes the application of the equity method to investments in joint ventures in addition to associates.

IAS 28 (2011) is effective for annual periods beginning on or after 1 January 2013 and earlier application is permitted. The Group is currently assessing the full impact of this revised standard.

IFRS 9 Financial Instruments: Classification and Measurement

IFRS 9 as issued reflects the first phase of the IASB’s work on the replacement of IAS 39 and applies to classification and measurement of financial assets and financial liabilities as defined in IAS 39.

It replaces the parts of IAS 39 that relate to the classification and measurement of financial instruments. IFRS 9 requires financial assets to be classified into two measurement categories: those measured as at fair value and those measured at amortised cost. The determination is made at initial recognition. The classification depends on the entity’s business model for managing its financial instruments and the contractual cash flow characteristics of the instrument.

For financial liabilities, the standard retains most of the IAS 39 requirements. The main change is that, in cases where the fair value option is taken for financial liabilities, the part of a fair value change due to an entity’s own credit risk is recorded in other comprehensive income rather than the income statement, unless this creates an accounting mismatch.

It also includes those paragraphs of IAS 39 dealing with how to measure fair value and accounting for derivatives embedded in a contract that contains a host that is not a financial asset, as well as the requirements of IFRIC 9 Reassessment of Embedded Derivatives.

The IASB issued amendments to IFRS 9 that defer the mandatory effective date from 1 January 2013 to 1 January 2015 with early application continuing to be permitted. In subsequent phases, the IASB will address hedge accounting and impairment of financial assets.

The Group will quantify the effect of adoption of this Standard, in conjunction with the other phases, when issued, to present a comprehensive picture.

3 ACCOUNTING POLICIES (continued)

IFRS 10 Consolidated Financial Statements
IFRS 10 introduces a new approach to determining which investees should be consolidated and provides a single consolidation model that identifies control as the basis for consolidation for all types of entities.

An investor controls an investee when:

- it is exposed or has rights to variable returns from its involvement with that investee;
- it has the ability to affect those returns through its power over that investee; and
- there is a link between power and returns.

Control is re-assessed as facts and circumstances change.

IFRS 10 replaces IAS 27 Consolidated and Separate Financial Statements and SIC-12 Consolidation - Special Purpose Entities. IFRS 10 is effective for annual periods beginning on or after 1 January 2013 and earlier application is permitted. The Group is currently assessing the full impact of this new standard.

IFRS 11 Joint Arrangements
IFRS 11 establishes principles for the financial reporting by parties to a joint arrangement and improves on IAS 31 by establishing principles that are applicable to the accounting for all joint arrangements.

IFRS 11 classifies Joint arrangements into two types – Joint operations and Joint ventures; and defines joint control as the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities (i.e. activities that significantly affect the returns of the arrangement) require the unanimous consent of the parties sharing control.

IFRS 11 supersedes IAS 31 Interests in Joint Ventures and SIC-13 Jointly Controlled Entities – Non-monetary Contributions by Venturers. IFRS 11 is effective for annual periods beginning on or after 1 January 2013 and earlier application is permitted. The Group is currently assessing the full impact of this new standard.

IFRS 12 Disclosure of Involvement with Other Entities
IFRS 12 combines, enhances and replaces the disclosure requirements for subsidiaries, joint arrangements, associates and unconsolidated structured entities. As a consequence of these new IFRSs, the IASB also issued amended and retitled IAS 27 Separate Financial Statements and IAS 28 Investments in Associates and Joint Ventures.

IFRS 12 aims to provide information to enable users to evaluate:

- the nature of, and risks associated with, an entity's interests in other entities; and
- the effect of those interests on the entity's financial position, financial performance and cash flows.

IFRS 12 is effective for annual periods beginning on or after 1 January 2013 and earlier application is permitted. The Group is currently assessing the full impact of this new standard.

IFRS 13 Fair Value Measurement
IFRS 13 replaces the fair value measurement guidance contained in individual IFRSs with a single source of fair value measurement guidance. It defines fair value, establishes a framework for measuring fair value and sets out disclosure requirements for fair value measurements. It explains how to measure fair value when it is required or permitted by other IFRSs. IFRS 13 does not extend the use of fair value accounting but provide guidance on how it should be applied where its use is already required or permitted by other standards within IFRSs.

IFRS 13 is effective for annual periods beginning on or after 1 January 2013 and earlier application is permitted. The Group is currently assessing the full impact of this new standard.

4 INVESTMENT IN SUBSIDIARIES

Key subsidiaries, all of which have 31 December as their year end, are listed below. There is no change in the percentage holding of the subsidiaries during the year, except as mentioned in note 4.1.

Subsidiary	Activities	Year of incorporation	Country of incorporation	Ownership %
Miracle Graphics Company W.L.L.	The company is engaged in the business of ordinary photography, printing and publishing.	2003	Kingdom of Bahrain	70.00
Al-Enma House for Real Estate B.S.C. (c)	The company is engaged in property management of commercial, industrial and residential buildings and the provision of security services to buildings and facilities.	2003	Kingdom of Bahrain	59.28
Bayan Group for Property Investments W.L.L.	The principal activity of the company is to buy, sell and lease properties and to undertake joint ventures with other companies engaged in similar activities.	2004	Kingdom of Bahrain	100.00
Al Kindi Pharmaceutical Industries (Public Shareholding Company)	The company is engaged in the manufacture of drugs in all their pharmaceutical dosage forms and the manufacturing of semi-pharmaceutical products specialised for skin care and cosmetics.	1997	Hashemite Kingdom of Jordan	82.20
Kuwait Finance House - Jordan and its subsidiaries	The company and its subsidiaries are engaged in investment advisory and investments in private equities and real estate development.	2007	Hashemite Kingdom of Jordan	100.00
Ishbiliya Village W.L.L.	The principal activity of the company is to invest in and develop real estate projects and consequently buying, selling and marketing of such properties.	2005	Kingdom of Bahrain	73.72
Motherwell Bridge Limited (Note 4.1)	The Company is engaged in design, engineering, construction management and manpower management of engineering projects principally in the oil, gas, petrochemical and steel industries.	2008	United Kingdom	79.14
Mena Telecom W.L.L.	The company is a licensed telecommunications company.	2003	Kingdom of Bahrain	100.00

4.1 - The percentage holding has changed from 85.1% at 31 December 2010 due to restructuring of Motherwell Bridge Limited.

Notes to the Consolidated Financial Statements

For the year ended 31 December 2011

5 CLASSIFICATION OF FINANCIAL INSTRUMENTS BY MEASUREMENT BASIS

The Group's financial instruments have been classified in accordance with their measurement basis as follows:

	Financial assets at fair value through statement of income BD 000	Financial assets at fair value through equity BD 000	Financial assets at amortised cost BD 000	Financial assets at cost/ amortised cost BD 000	Financial liabilities at cost/ amortised cost BD 000	Total 2011 BD 000
ASSETS						
Cash and balances with banks and Central Bank of Bahrain	-	-	-	48,230	-	48,230
Murabaha and due from banks	-	-	-	102,212	-	102,212
Financing contracts with customers	-	-	-	601,225	-	601,225
Investments	209,208	14,535	62,078	-	-	285,821
Receivables	-	-	-	56,947	-	56,947
	209,208	14,535	62,078	808,614	-	1,094,435
LIABILITIES AND EQUITY OF INVESTMENT ACCOUNT HOLDERS						
Customers' current accounts	-	-	-	-	73,802	73,802
Murabaha and due to banks	-	-	-	-	213,441	213,441
Murabaha and due to non-banks	-	-	-	-	290,688	290,688
Other liabilities	-	-	-	-	41,025	41,025
Subordinated murabaha payable	-	-	-	-	100,186	100,186
Equity of investment account holders	-	-	-	-	445,288	445,288
	-	-	-	-	1,164,430	1,164,430

	Financial assets at fair value through statement of income BD 000	Financial assets at fair value through equity BD 000	Financial assets at amortised cost BD 000	Financial assets at cost/ amortised cost BD 000	Financial liabilities at cost/ amortised cost BD 000	Total 2010 BD 000
ASSETS						
Cash and balances with banks and Central Bank of Bahrain	-	-	-	38,968	-	38,968
Murabaha and due from banks	-	-	-	51,370	-	51,370
Financing contracts with customers	-	-	-	640,391	-	640,391
Investments	172,217	31,451	53,672	-	-	257,340
Receivables	-	-	-	56,985	-	56,985
	172,217	31,451	53,672	787,714	-	1,045,054
LIABILITIES AND EQUITY OF INVESTMENT ACCOUNT HOLDERS						
Customers' current accounts	-	-	-	-	55,780	55,780
Murabaha and due to banks	-	-	-	-	246,406	246,406
Murabaha and due to non-banks	-	-	-	-	187,785	187,785
Other liabilities	-	-	-	-	44,067	44,067
Subordinated murabaha payable	-	-	-	-	99,423	99,423
Equity of investment account holders	-	-	-	-	452,963	452,963
	-	-	-	-	1,086,424	1,086,424

6 CASH AND BALANCES WITH BANKS AND CENTRAL BANK OF BAHRAIN

		2011 BD 000	2010 BD 000
Cash		4,547	3,755
Balances with banks		10,378	9,383
Balance with Central Bank of Bahrain		3,630	2,210
CBB mandatory reserve	6.1	29,675	23,620
	6.2	48,230	38,968

6.1 This mandatory reserve is not available for use in the Group's day to day operations.

6.2 This balance includes BD 24,698 thousand (2010: BD 23,399 thousand) financed by investment account holders' funds.

7 MURABAHA AND DUE FROM BANKS

	2011 BD 000	2010 BD 000
Murabaha and due from banks	102,230	51,373
Deferred profits	(18)	(3)
	102,212	51,370

The above amounts are entirely financed through investment account holders' funds. These carry profit rates ranging from 0.30% to 0.85% per annum (2010: 0.25% to 0.60% per annum).

8 FINANCING CONTRACTS WITH CUSTOMERS

	Self financed		Financed through investment account holders' funds		Total	
	2011 BD 000	2010 BD 000	2011 BD 000	2010 BD 000	2011 BD 000	2010 BD 000
Murabaha	248,361	213,330	162,997	222,148	411,358	435,478
Deferred profits	(29,378)	(16,448)	(19,242)	(17,078)	(48,620)	(33,526)
Provisions	(1,671)	(1,807)	(1,037)	-	(2,708)	(1,807)
	217,312	195,075	142,718	205,070	360,030	400,145
Ijarah Muntahia Bittamleek (Note 8.1)	129,023	113,539	113,581	119,452	242,604	232,991
Musharaka	10,334	18,998	-	-	10,334	18,998
	356,669	327,612	256,299	324,522	612,968	652,134
Collective impairment					(11,743)	(11,743)
					601,225	640,391

8 FINANCING CONTRACTS WITH CUSTOMERS (continued)

8.1 These mainly comprise of land and building and are presented net of accumulated depreciation amounting to BD 54,303 thousand (2010: BD 83,334 thousand).

8.2 The gross amount of financings individually determined to be impaired, before deducting any individually assessed impairment provision is BD 5,170 thousand (2010: BD 2,591 thousand).

8.3 Included in the above is an amount of BD 41,867 thousand (BD 44,194 thousand) which is past due for more than 90 days and non performing. This exposure is sufficiently collateralized and the repayment prospects of these remain favourable hence no provision is required against this exposure.

8.4 During the year, the Bank took possession of properties with a carrying value of BD 1,623 thousand. These have been classified under investment properties.

The following is a reconciliation of the individual and collective impairment provisions for losses on financing contracts with customers:

	Specific impairment 2011 BD 000	**Collective impairment 2011 BD 000**	**Total 2011 BD 000**	Specific impairment 2010 BD 000	Collective impairment 2010 BD 000	Total 2010 BD 000
At 1 January	**1,807**	**11,743**	**13,550**	1,183	11,855	13,038
Charge for the year	**1,066**	**-**	**1,066**	408	104	512
Reversals for the year	**(165)**	**-**	**(165)**	-	-	-
Provision for the year *	**901**	**-**	**901**	408	104	512
Transfers	**-**	**-**	**-**	216	(216)	-
At 31 December	**2,708**	**11,743**	**14,451**	1,807	11,743	13,550

* This amount includes provision against investment murabahas amounting to BD 500 thousand (2010: BD Nil).

9 INVESTMENTS

The Group's investments are classified as follows:

		2011 BD 000	2010 BD 000
Investments at fair value through statement of income	9.1	**209,208**	172,217
Investments at fair value through equity	9.2	**14,535**	31,451
Investments at amortised cost	9.3	**62,078**	53,672
		285,821	257,340

9.1 Carried at fair value through statement of income		
Designated upon initial recognition at fair value through statement of income:		
Unquoted equity securities	**200,553**	160,814
Managed funds - at Net Asset Value	**8,655**	11,403
	209,208	172,217

9.2 Carried at fair value through equity		
Quoted equity securities	**6,389**	7,356
Unquoted equity securities	**1,219**	856
Managed fund - at Net Asset Value	**6,927**	23,239
	14,535	31,451

9 INVESTMENTS (continued)

The movement of investments carried at fair value through equity during the year is as follows:

	2011 BD 000	2010 BD 000
At 1 January	31,451	9,295
Acquisitions	1,049	23,213
Transfers	7,307	-
Fair value changes	(2,023)	(1,057)
Disposal	(23,249)	-
At 31 December	14,535	31,451

	2011 BD 000	2010 BD 000
9.3 Carried at amortised cost		
Quoted sukuk		
Government *	2,262	2,527
Others *	14,703	11,726
Unquoted sukuk		
Government *	11,070	9,185
Others *	34,043	30,234
	62,078	53,672

* As at 31 December 2010 and 2011, investment in sukuk is entirely financed through equity of investment account holders' funds. All other investments are self financed.

The adoption of FAS 25 during the year had an effect on the classification and measurement of the Group's financial assets. As a result of the application of this new standard, the classification of the investment portfolio was revisited and changes were made in these classifications in line with FAS 25. Sukuk amounting to BD 53,672 thousand have been reclassified from 'fair value through equity' to 'amortised cost'. The fair value loss that would have recognised in the consolidated statement of comprehensive income under 'available for sale reserve' during the year if the Group had not reclassified the investments from 'fair value through equity' to 'amortised cost' is BD 6 thousand. Further, cumulative unrealised fair value gains relating to investments carried at fair value through statement of income amounting to BD 3,524 thousand were reclassified from investment revaluation reserve to retained earnings.

9.4 Composition of investment portfolio

The industry and geographic composition of the Group's investment portfolio is as follows:

	Middle East BD 000	Others BD 000	Total 2011 BD 000	Total 2010 BD 000
Real estate development	224,132	-	224,132	192,676
Banking and financial services	45,389	1,245	46,634	46,878
Others	352	14,703	15,055	17,786
	269,873	15,948	285,821	257,340

9 INVESTMENTS (continued)

9.5 Reclassification of investments

During the year ended 31 December 2008, the Group reclassified certain of its held for trading equity investments to available for sale. The investments were reclassified to reflect the change in Group's intention to hold the said investments for foreseeable future rather than exit or trade in the short term as allowed under amendments to IAS 39 and IFRS 7, "Reclassification of Financial Assets".

As at 31 December 2011, the carrying and fair value of reclassified investments is BD 6,389 thousand (31 December 2010: BD 7,356 thousand). During the year, the Group recognised impairment losses of BD 3,694 thousand (2010: BD Nil) against these investments in the consolidated statement of income. In the previous year, fair value losses on these investments taken to the consolidated statement of comprehensive income amounted to BD 1,599 thousand.

10 INVESTMENT IN JOINT VENTURES AND ASSOCIATES

The Group has the following joint ventures and associates as at 31 December 2011:

Name of the entity	Nature of business	Country of incorporation	Holding
Joint Ventures			
Diyar Homes Company W.L.L	Real estate development, project management and the buying and selling of properties.	Kingdom of Bahrain	50.0%
Durrat Khaleej Al Bahrain B.S.C.(c)	Development of Durrat Al Bahrain project with a view of sale of land, residential and commercial properties.	Kingdom of Bahrain	50.0%
Associates			
Deera Investment and Real Estate Development Company	Real estate project development and property management.	Hashemite Kingdom of Jordan	28.0%
Energy Central B.S.C.(c)	Providing district cooling, sea water desalination, waste water treatment and related services.	Kingdom of Bahrain	33.5%
Seef Properties B.S.C	Engaged in the real estate development and operation sector.	Kingdom of Bahrain	15.5%

Durrat Khaleej al Bahrain B.S.C (c) and Diyar Homes Company W.L.L. are jointly controlled entities whereby the venturers have an arrangement that establishes joint control over the economic activities of these entities. The Group recognises its stake in the joint ventures using the equity method of accounting.

Although the group holds less than 20% of the equity shares of Seef Properties B.S.C, the group exercises significant influence by virtue of its contractual right to appoint three directors to the board of directors of the company and has the power to participate in the financial and operating policy decisions.

10 INVESTMENT IN JOINT VENTURES AND ASSOCIATES (continued)

The following table illustrates the summarised financial information of joint ventures and associates:

	2011 BD 000	2010 BD 000
Current assets	**212,258**	233,015
Non current assets	**226,126**	150,749
Current liabilities	**(106,845)**	(44,352)
Non current liabilities	**(22,517)**	(103,095)
Total net assets	**309,022**	236,317

Total revenue and net income of joint venture and associates for the year:

	2011 BD 000	2010 BD 000
Revenues	**28,050**	16,312
Net loss	**(9,366)**	(474)

The movement of the Group's investment in joint ventures and associates is as follows:

	2011 BD 000	2010 BD 000
At 1 January	**85,994**	77,569
Investment during the year	**40,211**	3,855
Transfer from investments at fair value through statement of income	**-**	10,227
Share of recycling of investments at fair value through equity revaluation	**3,363**	-
Share of fair value changes on investments at fair value through equity	**-**	313
Share of results of associates	**(5,833)**	(3,163)
Other movements	**(518)**	(2,807)
At 31 December	**123,217**	85,994

The quoted value of the investment in associates for which quoted prices are available is BD 10,228 thousand (2010 : BD 12,908 thousand). However, the quoted price does not represent the fair value as the shares are not actively traded. The fair value based on internal models approximates their carrying value.

11 INVESTMENT PROPERTIES

	2011 BD 000	2010 BD 000
Cost		
At 1 January	**120,867**	114,714
Additions	**16,619**	5,472
Disposals	**(13,063)**	(497)
Transfer from other assets	**5,500**	1,178
At 31 December	**129,923**	120,867
Fair value adjustment		
At 1 January	**22,206**	22,206
Net unrealised gain on investment properties	**1,129**	-
Relating to disposals	**(943)**	-
At 31 December	**22,392**	22,206
Total	**152,315**	143,073

Investment properties, held in the Kingdom of Bahrain, at 31 December consists of the following:

	2011 BD 000	2010 BD 000
Buildings	**61,762**	55,464
Lands	**90,553**	87,609
	152,315	143,073

Rental income included in the consolidated statement of income from investment properties amounted to BD 389 thousand (2010: BD 502 thousand).

Investment properties is stated at fair value which has been determined based on valuations performed by independent valuers, with recent experience in the location and category of the properties being fair valued, at dates close to 31 December 2011 and 31 December 2010. The fair values have been determined based on recent transactions in the market, the independent valuers' knowledge and professional judgement.

Investment properties includes the Bank's share of BD 353 thousand (2010: BD 353 thousand) which are jointly owned with third parties and are subject to normal conditions applicable to joint ownership.

12 RECEIVABLES, PREPAYMENTS AND OTHER ASSETS

		2011 BD 000	2010 BD 000
Land and development cost	12.1	**92,527**	97,131
Performance and management fees receivable (Note 12.2 & 30)		**9,042**	21,161
Project expenses receivable		**4,248**	1,708
Inventories		**986**	2,618
Profit receivable		**1,616**	1,662
Trade receivables of subsidiaries		**14,066**	12,132
Prepaid expenses		**1,787**	1,597
Advance for purchase of investment		**-**	6,718
Receivables relating to sale / liquidation of investments		**17,728**	2,814
Receivables from corporate customers		**7,471**	7,439
Other assets		**2,776**	3,351
		152,247	158,331

12 RECEIVABLES, PREPAYMENTS AND OTHER ASSETS (continued)

12.1 Land and development costs

	2011 BD 000	2010 BD 000
Land	**44,968**	53,367
Development costs	**47,559**	43,764
	92,527	97,131

These development costs represent construction, consultancy and profit paid on murabaha financing, capitalised relating to various real estate projects being undertaken by the Group.

12.2 Performance and management fees receivable

Included in this balance is BD 7,928 thousand (2010: BD 19,225 thousand) receivable from a related party.

13 GOODWILL AND INTANGIBLES

	Goodwill 2011 BD 000	Intangibles 2011 BD 000	Total 2011 BD 000	Goodwill 2010 BD 000	Intangibles 2010 BD 000	Total 2010 BD 000
Cost:						
At 1 January	**25,911**	**4,989**	**30,900**	26,727	-	26,727
Additions	**-**	**-**	**-**	-	-	-
Transfer from assets of disposal group classified as held for sale	**-**	**-**	**-**	-	4,989	4,989
Other movements	**(744)**	**-**	**(744)**	(816)	-	(816)
At 31 December	**25,167**	**4,989**	**30,156**	25,911	4,989	30,900
Amorisation and impairment:						
At 1 January	**1,555**	**701**	**2,256**	1,555	-	1,555
Amortisation charge for the year	**-**	**136**	**136**	-	383	383
Transfer from assets of disposal group classified as held for sale	**-**	**-**	**-**	-	318	318
At 31 December	**1,555**	**837**	**2,392**	1,555	701	2,256
Net book value:						
At 1 January	**24,356**	**4,288**	**28,644**	25,172	-	25,172
At 31 December	**23,612**	**4,152**	**27,764**	24,356	4,288	28,644

The carrying amount of goodwill is attributable to the following subsidiaries, which are treated as cash generating units:

	2011 BD 000	2010 BD 000
Miracle Graphics Company W.L.L.	**800**	800
Motherwell Bridge Limited	**22,812**	23,556
	23,612	24,356

13 GOODWILL AND INTANGIBLES (continued

Key assumptions used in estimating recoverable amounts of cash-generating units
The recoverable amount of each cash generating unit's goodwill is based on value in use calculations using cash flow projections from financial budgets approved by senior management, extrapolated for nine years. The discount rate of 11.9% (2010: 12.7%) has been applied to cash flow projections, which represents weighted average cost of capital adjusted for appropriate risk premium for these cash generating units. The key assumptions used in estimating recoverable amounts of cash generating units were sensitised to test the resilience of value in use calculations. On this basis, management believes that reasonable changes in key assumptions used to determine the recoverable amount of the Group's cash generating units will not result in an impairment.

14 MURABAHA AND DUE TO BANKS

	2011 BD 000	2010 BD 000
Murabaha payable to banks	**157,330**	101,518
Due to banks	**56,111**	144,888
	213,441	246,406

15 FUNDS UNDER MANAGEMENT

At 31 December 2011, clients' funds managed in a fiduciary capacity amounted to BD 84,128 thousand (2010: BD 106,371 thousand).

16 OTHER LIABILITIES

	2011 BD 000	2010 BD 000
Payable against purchase of investment properties (Note 30)	**-**	3,981
Pay orders issued not presented	**1,177**	2,819
Payable on account of financing contracts	**439**	1,297
Staff related accruals	**3,568**	3,466
Profit payable on account of murabaha and due to banks and non-banks	**2,275**	2,216
Profit payable on equity of investment account holders	**2,243**	2,167
Trade payables of subsidiaries	**27,961**	24,088
Due to investors	**500**	2,029
Others	**2,862**	2,004
	41,025	44,067

17 SUBORDINATED MURABAHA PAYABLE

The subordinated murabaha payable carries a profit equivalent to a rate of 2% over the six month Kuwait Inter Bank Offer Rate (KIBOR). The facility has been approved by CBB to be recognised as Tier II capital and is unsecured and sub-ordinate to the claim of all creditors, including equity of investment account holders. This facility will expire in 2019 but can be terminated at the option of the Bank after third quarter of 2014, subject to the prior approval of the CBB.

During the year, an amount of BD 3,053 thousand (2010: BD 3,138 thousand) has been charged to the consolidated statement of income in respect of subordinated murabaha payable.

18 EQUITY OF INVESTMENT ACCOUNT HOLDERS

The mudarib share on investment accounts ranges from 20% to 40% (2010: 20% to 40%) depending on the investment period and in the case of saving accounts, where there is no restriction on cash withdrawal, the mudarib share ranges from 50% to 60% (2010: 50% to 60%). Mudarib share for the year ended 31 December 2011 amounted to BD 2,048 thousand (2010: BD 5,300 thousand) and is included within financing income from retail and corporate banking activities. The rate of return to investment account holders, as at 31 December 2011 and 2010, for various types of Investment Accounts, denominated in BD and USD, is as follows:

	2011 Rate of return %	2010 Rate of return %
Investment Accounts - Denominated in BHD		
Saving Account	**0.50**	1.00
VIP Saving Account	**0.60**	1.25
One Month Investment Account	**2.50**	2.80
Three Months Investment Account	**3.00**	3.40
Six Months Investment Account	**3.25**	3.60
One Year Investment Account	**3.75**	4.20
Investment Accounts - Denominated in USD		
Saving Account	**0.25**	1.00
VIP Saving Account	**0.35**	1.25
One Month Investment Account	**1.78**	2.80
Three Months Investment Account	**2.08**	3.40
Six Months Investment Account	**2.22**	3.60
One Year Investment Account	**2.37**	4.20

18.1 Investment Accounts by type	2011 BD 000	2010 BD 000
Saving Accounts	**33,357**	27,708
VIP Saving Accounts	**21,590**	16,264
One Month Investment Accounts	**123,032**	139,475
Three Months Investment Accounts	**169,671**	182,469
Six Months Investment Accounts	**50,199**	40,827
One Year Investment Accounts	**47,439**	46,220
	445,288	452,963

19 SHARE CAPITAL AND RESERVES

Share capital

		2011 BD 000	2010 BD 000
Authorised:			
3,500,000 thousand (2010: 3,500,000 thousand) ordinary shares of BD 0.1 each		**350,000**	350,000
Issued and fully paid up:			
As at the beginning and end of the year 1,771,405 thousand (2010: 1,771,405 thousand) shares	19.1	**177,140**	177,140

19.1 Out of the issued and paid up capital, 120,456 thousand shares (2010: 120,456 thousand shares) of BD 0.1 (2010: BD 0.1) are held under Employee Share Ownership Plan. The Bank is in the process of amending its Memorandum and Articles of Association to reflect the paid up share capital of BD 177,140 thousand.

Nature and purpose of reserves

Share premium
Amounts collected in excess of the par value of the issued share capital during any new issue of shares, net of issue expenses, are treated as share premium. This amount is not available for distribution, but can be utilised as stipulated by the Bahrain Commercial Companies Law.

Statutory reserve
As required by Bahrain Commercial Companies Law ("BCCL") and the Bank's articles of association, 10% of the net income for the year has been transferred to the statutory reserve. However, as allowed under BCCL the Bank may resolve to discontinue such annual transfers when the reserve totals 50% of paid up share capital. The reserve is not distributable except in such circumstances as stipulated in the BCCL and following the approval of the CBB.

General reserve
The general reserve is established in accordance with the articles of association of the Group and is distributable following a resolution of shareholders at a general meeting and the approval of CBB. The Group may transfer any amount to the general reserve, as approved by the shareholders at a general meeting, out of the net income for the year after appropriating statutory reserve.

Available for sale reserve
Unrealised gains and losses resulting from investments carried at fair value through equity, if not determined to be impaired, recorded in the 'available for sale' reserve and not available for distribution. Upon disposal of such assets, the related cumulative gains or losses are transferred to retained earnings and become available for distribution.

Investment revaluation reserve
Unrealised gains or losses on 'investment properties' and certain 'investments carried at fair value through statement of income' as deemed appropriate by the management, recorded in the consolidated statement of income are appropriated to the 'investment revaluation reserve' in equity and are not available for distribution. Upon disposal of such assets, the related cumulative gains or losses are transferred to retained earnings and become available for distribution.

Foreign currency transaction reserve
The foreign currency translation reserve is used to record exchange differences arising from the translation of the financial statements of foreign subsidiaries.

Retained Earnings
Retained earnings is the cumulative amount of annual earnings not paid out as dividends. Included in retained earnings is a non-distributable reserve amounting to BD 1,523 thousand (2010: BD 1,524 thousand) relating to subsidiaries of the Bank.

20 TOTAL COMPREHENSIVE INCOME ATTRIBUTABLE TO SHAREHOLDERS OF THE PARENT

	2011 BD 000	2010 BD 000
Net income before adjustment for non-controlling stakeholders	6,812	7,418
Other comprehensive income:		
Fair value adjustments against available for sale investments	1,754	887
Net movement in foreign currency translation reserve	6	242
Share of other comprehensive income of joint venture	3,363	313
Total other comprehensive income for the year	5,123	1,442
Total comprehensive income for the year	11,935	8,860
Adjustment attributable to non-controlling stakeholders	2,774	1,907
	14,709	10,767

21 COMMITMENTS AND CONTINGENT ITEMS

	2011 BD 000	2010 BD 000
Contingent liabilities:		
Letters of credit	13,567	12,778
Guarantees	12,125	14,904
	25,692	27,682
Irrevocable commitments to extend credit:		
Original term to maturity of one year or less	8,223	16,942
Investment commitment	9,750	226
	43,665	44,850

Operating lease commitments

At 31 December 2011, the Group had commitments in respect of non cancellable operating leases amounting to BD 5,240 thousand (2010: BD 7,697 thousand) relating to leasehold premises. Of the commitments in respect of operating leases, BD 1,550 thousand (2010: BD 1,476 thousand) are due within one year, BD 3,690 thousand (2010: BD 3,977 thousand) are due in one to five years and the remaining over five years.

Construction commitments

At 31 December 2011, the Group had commitments in respect of construction contracts amounting to BD 7,789 thousand (2010: BD 5,837 thousand).

22 INCOME FROM RETAIL AND CORPORATE BANKING ACTIVITIES

		2011 BD 000	2010 BD 000
Income from Murabaha		**25,391**	27,840
Income from Ijarah Muntahia Bittamleek	22.1	**17,810**	18,531
Income from Musharaka		**540**	1,519
Income from Murabaha with banks		**487**	183
Financing income from retail and corporate banking activities		**44,228**	48,073
Mudarib share from off balance sheet equity of investment account holders		**592**	465
Fees and commission income		**601**	1,078
		45,421	49,616

22.1 This is presented net of depreciation on Ijarah Muntahia Bittamleek assets amounting to BD 71,983 thousand (2010: BD 30,954 thousand).

23 INCOME FROM INVESTMENT ACTIVITIES

	2011 BD 000	2010 BD 000
Net unrealised gain on investments	**10,651**	2,406
(Loss) gain on sale of investments	**(2,240)**	14,294
Net unrealised gain on investment properties	**1,129**	-
Net gain on sale of investment properties	**11,916**	65
Performance and management fees	**478**	271
Dividend income	**144**	436
Income from sukuk	**2,511**	1,956
Other income (loss)	**362**	(313)
	24,951	19,115

24 INCOME AND EXPENSE RELATING TO FINANCING CONTRACTS AND SUKUKS

	2011 BD 000	2010 BD 000
Financing income from retail and corporate banking activities	**44,228**	48,073
Income from sukuk	**2,511**	1,956
	46,739	50,029
Less: Profit on murabaha and due to banks, murabaha and due to non-banks and subordinated murabaha payable	**14,023**	12,380
Less: Return on equity of investment account holders, net of mudarib share	**12,124**	13,299
	26,147	25,679
	20,592	24,350

25 OTHER INCOME

This amount comprises revenue arising from subsidiaries of the Bank through the sale of goods, rendering of services, and the sale of real estate properties net of directly attributable expenses.

26 PROVISIONS

	2011 BD 000	2010 BD 000
Provisions against financing contracts with customers	401	512
Impairment loss on investments	3,694	-
	4,095	512

27 OTHER EXPENSES

	2011 BD 000	2010 BD 000
Business development	1,421	1,254
Technology and communication	2,342	5,314
Legal, consulting and outsourcing	1,404	1,565
Premises - rentals and maintenance	2,482	3,613
Administration, selling and others	10,412	7,029
	18,061	18,775

28 PROFIT ON MURABAHA AND DUE TO BANKS, MURABAHA AND DUE TO NON-BANKS AND SUBORDINATED MURABAHA PAYABLE

	2011 BD 000	2010 BD 000
Murabaha and due to banks	3,729	3,072
Murabaha and due to non-banks	7,241	6,170
Subordinated murabaha payable (Note 17)	3,053	3,138
	14,023	12,380

29 CASH AND CASH EQUIVALENTS

Cash and cash equivalents for the purpose of consolidated statement of cash flows comprise of the following amounts:

	2011 BD 000	2010 BD 000
Cash	4,547	3,755
Balances with banks	10,378	9,383
Balances with CBB excluding mandatory reserve deposit	3,630	2,210
Murabaha and due from banks with original maturity of less than ninety days	102,212	51,370
	120,767	66,718

30 RELATED PARTY DISCLOSURES

Related parties represent associated companies, the parent and its major shareholders, directors and key management personnel of the Bank, the Bank's Shari'a Supervisory Board and entities controlled, jointly controlled or significantly influenced by such parties. Transactions with related parties arise from the ordinary course of business. Pricing policies and terms of these transactions are approved by the Group's management. Outstanding balances at the year end are unsecured. For the year ended 31 December 2011, the Group has not made any provision related to amounts owed by related parties (2010: Nil).

The following table provides the total amount of transactions that have been entered into with related parties for the relevant financial year:

	Associated companies BD 000	Parent company BD 000	Directors and key management personnel BD 000	Other related parties BD 000	2011 BD 000	2010 BD 000
Murabaha and due from banks	-	26,400	-	-	26,400	10,077
Financing contracts with customers	3,543	-	22,483	78,182	104,208	97,136
Performance and management fees receivable (Note 12)	7,928	-	-	1,263	9,191	21,161
Project expenses receivable	-	-	-	58	58	58
Other receivables	-	-	-	-	-	19,856
Murabaha and due to banks	-	116,013	-	-	116,013	54,010
Murabaha and due to non-banks	-	-	-	86,969	86,969	55,637
Customers' current accounts	11,613	639	72	2,553	14,877	5,545
Payable against purchase of investment properties (Note 16)	-	-	-	-	-	3,981
Other liabilities	336	-	-	-	336	284
Subordinated murabaha payable	-	100,186	-	-	100,186	99,423
Equity of investment account holders	10,717	-	897	64,587	76,201	74,336
Letters of credit	20	-	-	6,698	6,718	6,718
Commitments to extend credit	500	-	-	2,355	2,855	2,355

The income and expenses in respect of related parties included in the consolidated financial statements are as follows:

	Associated companies BD 000	Parent company BD 000	Directors and key management personnel BD 000	Other related parties BD 000	2011 BD 000	2010 BD 000
Income from murabaha with banks	-	142	-	21	163	23
Income from financing contracts with customers	984	-	346	4,421	5,751	5,405
Performance and management fees (Note 23)	112	-	-	-	112	125
Profit on murabaha and due to banks	-	5,454	-	118	5,572	2,623
Profit on murabaha and due to non-banks	12	-	-	2,499	2,511	2,350
Profit on subordinated murabaha payable	-	3,053	-	-	3,053	3,138
Profit on equity investment account holders	1	-	3	1,983	1,987	2,367
Operating expenses	-	-	-	1,735	1,735	1,453

30 RELATED PARTY DISCLOSURES (continued)

Compensation of key management personnel, included in the consolidated statement of income, is as follows:

	2011 BD 000	2010 BD 000
Short term employee benefits	2,762	2,779
Long term employee benefits	134	128

Director's remuneration and attendance fee for the year ended 31st December 2011 amounted to BD 150 thousand and BD 557 thousand respectively (2010: BD 150 thousand and BD 557 thousand respectively).

31 SEGMENT INFORMATION

For management purposes, the Group is organised into the following segments.

Retail & Corporate Banking Group Principally engaged in Shari'a compliant profit sharing investment arrangements, providing Shari'a compliant financing contracts and other facilities to corporate, retail and institutional customers.

Investment Banking Group Principally engaged in investment banking activities, including private equity, real estate investments, treasury and other activities.

No operating segments have been aggregated to form the above reportable segments.

Management monitors the operating results of its segments separately for the purpose of making decisions about resource allocation and performance assessment. Segment performance is evaluated based on segment profit (as reported in internal management reports) which is measured using the same measurement principles as are used in the preparation of these consolidated financial statements.

Revenues of BD 12,227 thousand (2010: BD 9,535 thousand) were derived from a single external customer. These revenues related to the sale of investment banking assets.

The following table presents revenue, net profit and total assets of the Group's segments for the year ended 31 December 2011:

	Retail & Corporate Banking Group BD 000	Investment Banking Group BD 000	Total BD 000
Revenue	42,425	34,583	77,008
Segment profit / (loss)	21,992	(12,406)	9,586
Segment assets	573,134	950,555	1,523,689
Unallocated assets			13,665
Total assets			1,537,354

The following table shows the distribution of the Group's net income and total assets by geographical segments, based on the location in which the transactions and assets are recorded, for the year ended 31 December 2011.

	Bahrain BD 000	Other countries BD 000	Total BD 000
Revenues	57,732	19,276	77,008
Segment assets	1,217,307	320,047	1,537,354

Other countries mainly represent State of Kuwait, Hashemite Kingdom of Jordan and United Kingdom.

31 SEGMENT INFORMATION (continued)

The following table presents revenue, net profit and total assets of the Group's segments for the year ended 31 December 2010:

	Retail & Corporate Banking Group BD 000	Investment Banking Group BD 000	Total BD 000
Revenue	47,349	28,322	75,671
Segment profit / (loss)	26,472	(17,147)	9,325
Segment assets	620,916	809,858	1,430,774
Unallocated assets			15,898
Total assets			1,446,672

The following table shows the distribution of the Group's net income and total assets by geographical segments, based on the location in which the transactions and assets are recorded, for the year ended 31 December 2010.

	Bahrain BD 000	Other countries BD 000	Total BD 000
Revenues	46,119	29,552	75,671
Segment assets	1,125,869	320,803	1,446,672

Other countries mainly represent State of Kuwait, Hashemite Kingdom of Jordan and United Kingdom.

32 FAIR VALUE OF FINANCIAL INSTRUMENTS

Financial instruments comprise of financial assets and financial liabilities. Financial assets consist of cash, balances with banks and Central Bank of Bahrain, murabaha and due from banks, financing contracts with customers, investments and receivables. Financial liabilities comprise of murabaha and due to banks, murabaha and due to non-banks, customers' current accounts, other liabilities, equity of investment account holders and subordinated murabaha payable.

At 31 December 2011 and 2010, the fair value of financial instruments approximate their carrying values.

Financial instruments recorded at fair value
The Group uses the following hierarchy for determining and disclosing the fair value of 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 market observable, either directly or indirectly; and

- Level 3: Technique which use inputs that have significant effect on the recorded fair value and are not based on observable market data.

32 FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

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

	Level 1 2011 BD 000	Level 2 2011 BD 000	Level 3 2011 BD 000	Total 2011 BD 000
Investments at fair value through statement of income				
Unquoted equity securities	-	-	200,553	200,553
Managed funds	-	5,290	3,365	8,655
Investments at fair value through equity				
Quoted equity securities	6,389	-	-	6,389
Unquoted equity securities	-	-	1,219	1,219
Managed fund	-	-	6,927	6,927
	6,389	5,290	212,064	223,743

	Level 1 2010 BD 000	Level 2 2010 BD 000	Level 3 2010 BD 000	Total 2010 BD 000
Investments at fair value through statement of income				
Quoted equity securities	-	-	-	-
Unquoted equity securities	-	-	160,814	160,814
Managed funds	-	5,830	5,573	11,403
Investments at fair value through equity				
Quoted equity securities	7,356	-	-	7,356
Unquoted equity securities	-	-	856	856
Managed fund	-	23,239	-	23,239
	7,356	29,069	167,243	203,668

During the year ended 31 December 2011, there were no transfers between Level 1 and Level 2 fair value measurements, and no transfers into and out of Level 3 fair value measurements.

The following table shows a reconciliation of the opening and closing amount of Level 3 financial assets which are recorded at fair value.

	Unquoted equity securities 2011 BD 000	Managed funds 2011 BD 000	Unquoted equity securities 2010 BD 000	Managed funds 2010 BD 000
Balance at 1 January	161,670	5,573	163,052	4,185
Investments made during the year	29,484	7,159	3,393	-
Unrealised fair value (loss) gain	11,691	(514)	1,142	1,637
Disposals / Redemptions during the year	(1,093)	(1,926)	(5,892)	-
Other movements	20	-	(25)	(249)
Balance at 31 December	201,772	10,292	161,670	5,573

32 FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

Impact on fair value of level 3 financial instruments measured at fair value of changes to key assumptions

	Carrying amount 2011 BD 000	Effect of reasonably possible alternative assumption 2011 BD 000	Carrying amount 2010 BD 000	Effect of reasonably possible alternative assumption 2010 BD 000
Investments at fair value through statement of income				
Unquoted equity securities	200,553	20,055	160,814	16,081
Managed funds	3,365	337	5,573	557
Investments at fair value through equity				
Unquoted equity securities	1,219	122	856	86
Managed fund	6,927	693	-	-
	212,064	21,207	167,243	16,724

In order to determine reasonably possible alternative assumptions the Group adjusted key unobservable models inputs as follows:

For equities, the Group adjusted the price earning ratio by increasing and decreasing the price earning ratio by 10 percent, which is considered by the Group to be within a range of reasonably possible alternatives based on the price earning ratios of companies with similar industry and risk profiles.

For managed funds, the Group values its investments based on a net asset value, which is determined by the fund manager. The Group adjusted the value of the funds to increase or decrease by ten percent, which is considered by the Group to be within a range of reasonably possible alternatives.

For investments in real estate, fair value is determined by reference to valuations by independent real estate valuation experts. The determination of the fair value of such assets is based on local market conditions existing at the date of the statement of financial position. The Group adjusted the value of these assets to increase or decrease by ten percent, which is considered by the Group to be within a range of reasonably possible alternatives.

33 MATURITY ANALYSIS OF ASSETS, LIABILITIES AND EQUITY OF INVESTMENT ACCOUNT HOLDERS

The table below shows an analysis of assets, liabilities and equity of investment account holders analysed according to when they are expected to be recovered or settled. Group's contractual undiscounted repayment obligations are disclosed in Note 34.3 'Risk Management - Liquidity Risk and Funding Management'.

	Up to one year			Over one year				
	Up to 3 months 2011 BD 000	3 months to 12 months 2011 BD 000	Subtotal upto 12 months 2011 BD 000	1 to 5 years 2011 BD 000	5 to 10 years 2011 BD 000	Over 10 years 2011 BD 000	Subtotal Over 1 year 2011 BD 000	Total 2011 BD 000
Assets								
Cash and balances with banks and Central Bank of Bahrain	17,678	4,615	22,293	7,698	4,481	13,758	25,937	48,230
Murabaha and due from banks	102,212	-	102,212	-	-	-	-	102,212
Financing contracts with customers	50,542	135,207	185,749	291,235	74,366	49,875	415,476	601,225
Investments	6,402	7,300	13,702	81,279	190,840	-	272,119	285,821
Investment in joint ventures and associates	-	-	-	123,217	-	-	123,217	123,217
Investment properties	-	-	-	25,000	127,315	-	152,315	152,315
Receivables, prepayments and other assets	14,819	130	14,949	137,183	115	-	137,298	152,247
Goodwill and intangibles	-	-	-	23,612	4,152	-	27,764	27,764
Premises and equipment	-	-	-	-	44,323	-	44,323	44,323
Total	191,653	147,252	338,905	689,224	445,592	63,633	1,198,449	1,537,354
Liabilities and equity of investment account holders								
Customers' current accounts	25,535	8,415	33,950	13,284	13,284	13,284	39,852	73,802
Murabaha and due to banks	39,616	32,568	72,184	141,257	-	-	141,257	213,441
Murabaha and due to non-banks	78,165	37,229	115,394	139,918	17,688	17,688	175,294	290,688
Other liabilities	7,857	3,454	11,311	29,714	-	-	29,714	41,025
Equity of investment account holders	120,289	75,009	195,298	83,330	83,330	83,330	249,990	445,288
Subordinated murabaha payable	-	-	-	-	100,186	-	100,186	100,186
Total	271,462	156,675	428,137	407,503	214,488	114,302	736,293	1,164,430
Net	(79,809)	(9,423)	(89,232)	281,721	231,104	(50,669)	462,156	372,924

33 MATURITY ANALYSIS OF ASSETS, LIABILITIES AND EQUITY OF INVESTMENT ACCOUNT HOLDERS (continued)

	Up to one year			Over one year				
	Up to 3 months 2010 BD 000	3 months to 12 months 2010 BD 000	Subtotal upto 12 months 2010 BD 000	1 to 5 years 2010 BD 000	5 to 10 years 2010 BD 000	Over 10 years 2010 BD 000	Subtotal Over 1 year 2010 BD 000	Total 2010 BD 000
Assets								
Cash and balances with banks and Central Bank of Bahrain	13,448	4,652	18,100	5,642	3,776	11,450	20,868	38,968
Murabaha and due from banks	51,263	107	51,370	-	-	-	-	51,370
Financing contracts with customers	51,749	247,759	299,508	251,101	76,480	13,302	340,883	640,391
Investments	7,356	44,193	51,549	147,994	57,797	-	205,791	257,340
Investment in joint ventures and associates	-	-	-	-	85,994	-	85,994	85,994
Investment properties	-	-	-	143,073	-	-	143,073	143,073
Receivables, prepayments and other assets	8,425	86	8,511	138,666	11,154	-	149,820	158,331
Goodwill and intangibles	-	-	-	-	-	28,644	28,644	28,644
Premises and equipment	-	-	-	-	-	42,561	42,561	42,561
Total	132,241	296,797	429,038	686,476	235,201	95,957	1,017,634	1,446,672
Liabilities and equity of investment account holders								
Customers' current accounts	20,081	6,415	26,496	9,762	9,760	9,762	29,284	55,780
Murabaha and due to banks	38,187	22,214	60,401	186,005	-	-	186,005	246,406
Murabaha and due to non-banks	53,871	22,973	76,844	88,618	11,162	11,161	110,941	187,785
Other liabilities	7,841	7,033	14,874	29,193	-	-	29,193	44,067
Equity of investment account holders	89,432	102,452	191,884	87,026	87,027	87,026	261,079	452,963
Subordinated murabaha payable	-	-	-	-	99,423	-	99,423	99,423
Total	209,412	161,087	370,499	400,604	207,372	107,949	715,925	1,086,424
Net	(77,171)	135,710	58,539	285,872	27,829	(11,992)	301,709	360,248

34 RISK MANAGEMENT

34.1 Introduction

Risk is inherent in the Group's activities but it is managed through a process of ongoing identification, measurement and monitoring of material risks. The Group manages its exposure to risks within the approved risk limits. The process of risk management is critical to the Group's continuing profitability and each business unit within the Group is accountable for the risk exposures relating to its responsibilities. The Group is mainly exposed to credit risk, liquidity risk and market risk, the latter being subdivided into trading and non-trading risks. The Group is also subject to prepayment risk and operating risk.

The independent risk control process does not include business risks such as changes in the environment, technology and industry. These are monitored through the Group's strategic planning process.

Risk management structure

The Board of Directors is ultimately responsible for identifying and controlling risks; however, there are separate independent bodies responsible for managing and monitoring risks.

Board of Directors

The Board of Directors is responsible for the overall risk management approach and for approving the risk strategies, policies and risk appetite of the Bank.

Risk, Governance and Compliance Committee (RGC Committee)

The RGC committee is appointed by the Board of Directors and comprise of four members, three of whom are non-executive directors and one is an independent member. The committee has the overall responsibility for the development of the risk strategy and implementing principles, frameworks, policies and limits. It is responsible for the fundamental risk issues and manages and monitors relevant risk decisions. The committee also decides the corporate governance structure and manages the compliance requirements of the Bank.

Audit Committee

The Audit Committee is appointed by the Board of Directors and comprise of four members, three of whom are non-executive directors and one is an independent member. The committee assists the Board in carrying out its responsibilities with respect to assessing the quality and integrity of financial reporting, the audit thereof, the soundness of the internal controls of the Bank, the measurement system of risk assessment and relating these to the Bank's capital, and the methods for monitoring compliance with laws, regulations and supervisory and internal policies.

Asset and Liability Committee (ALCO)

ALCO is the senior management committee responsible for maintaining oversight of the Bank's risk profile and governance aspects. It helps the RGC Committee in establishing the risk policies and strategies and monitors the risk appetite in terms of risk limits and reports. It also controls the risks by appropriate actions. ALCO establishes policy and objectives for the asset and liability management of the Bank in terms of structure, distribution, risk and return and its impact on profitability. It also monitors the cash flow, cost and yield profiles and tenor of assets and liabilities and evaluates both from profit rate sensitivity and liquidity points of view, makes corrective adjustments based upon perceived trends and market conditions and monitors liquidity, foreign exchange exposures and positions.

Shari'a Supervisory Board

The Bank's Shari'a Supervisory Board is entrusted with the responsibility of ensuring the Bank's adherence to Shari'a rules and principles in its transactions and activities.

Risk Management Group

The Risk Management Group is responsible for implementing and maintaining risk related procedures to ensure an independent control process. It also helps the ALCO in establishing risk strategies, policies and limits, across the Bank. The group is also responsible for the independent control of risks, including monitoring the risk of exposures against limits and the assessment of risks of new products and structured transactions. This group also ensures the complete capture of the risks in risk measurement and reporting systems and performs stress tests on the various portfolios of the Bank.

Treasury Department

The treasury department is responsible for managing the Bank's assets and liabilities and the overall financial structure. It is also primarily responsible for the funding and liquidity risks of the Bank.

34 RISK MANAGEMENT (continued)

Internal Audit
Independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It helps an organization to accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance process. Internal audit discusses the results of all assessments with management, and reports its findings and recommendations to the Audit Committee.

Compliance Department
The compliance department is responsible for managing all the compliance related issues with the external parties and regulators. It also monitors compliance with internal risk policies of the Bank.

Risk measurement and reporting systems
The Group identifies, measures, controls and monitors its material risks on a periodic basis. The Bank has established relevant risk limit structures to quantify its risk appetite. The Bank conducts stress testing under various scenarios for its material portfolios using statistical methods to assess the impact of such scenarios on its portfolio and regulatory capital.

Established risk limits reflect the business strategy and market environment in which the Bank operates as well as the level of risk that the Bank is willing to accept. In addition, the Bank monitors and measures the overall risk bearing capacity in relation to the aggregate risk exposures across its material risk types and activities.

Information compiled from all the businesses is examined and processed in order to analyse, control and identify risks at an early stage. This information is presented and explained to the Board of Directors, the RGC Committee and senior management. The report includes aggregate credit exposures, concentration limits, investment limits, foreign exchange exposures, profit rate limits, liquidity gaps and ratios and changes in Group's risk profile. On a periodic basis, detailed reporting of industry, customer and geographic risks takes place. Senior management assesses the appropriateness of the general allowance for credit losses on a quarterly basis. The Board of Directors receives the risk management report once in a quarter which is designed to provide all the necessary information to assess and conclude on the risks of the Group.

As part of the Risk Management's reporting framework, tailored risk reports are prepared and distributed in order to ensure that all business divisions have access to extensive, necessary and up-to-date information. Periodic briefing is given to the Managing Director and Chief Executive Officer and all other relevant members of the Bank on the utilisation of market limits, proprietary investments and liquidity and any other risk developments.

34.2 Credit Risk
Credit risk is the risk that the Group will incur a loss because its customers, clients or counterparties fail to discharge their contractual obligations. The Bank manages and controls its credit risk by setting limits on the amount of risk it is willing to accept for individual counterparties and for geographical and industry concentrations, and by monitoring exposures in relation to such limits.

The Bank has established a credit quality review process to provide early identification of possible changes in the creditworthiness of counterparties, including regular collateral revisions for corporate portfolio. Counterparty limits are established with the use of a credit risk classification system, which assigns each counterparty a risk rating. Risk ratings for corporate customers are subject to revision at the time of renewal of the corporate facility. The credit quality review process allows the Bank to assess the potential loss as a result of the risks to which it is exposed and take corrective action.

Credit-related commitments risk
The Bank makes available to its customers guarantees which may require that the Bank makes payments on their behalf. Such payments are collected from customers based on the terms of the letter of credit. They expose the Bank to risks similar to financing contracts and these are mitigated by the same control processes and policies.

Risk concentrations of the maximum exposure to credit risk without taking collateral
Concentrations arise when a number of counterparties are engaged in similar business activities, or activities in the same geographic region, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations indicate the relative sensitivity of the Bank's performance to developments affecting a particular industry or geographical location.

In order to avoid excessive concentrations of risk, the Bank's policies and procedures include specific guidelines to focus on maintaining a diversified portfolio. Identified concentrations of credit risks are controlled and managed accordingly.

34 RISK MANAGEMENT (continued)

The maximum credit exposure to any client or counterparty as of 31 December 2011 was BD 52,336 thousand (31 December 2010: BD 55,297 thousand).

Maximum exposure to credit risk without taking account of any collateral and other credit enhancements
The table below shows the maximum exposure to credit risk for the components of the statement of financial position. The maximum exposure is shown gross, before the effect of mitigation through the use of master netting and collateral agreements.

	Gross maximum exposure 2011 BD 000	Gross maximum exposure 2010 BD 000
Balances with banks	**10,378**	9,383
Murabaha and due from banks	**102,212**	51,370
Financing contracts with customers	**601,225**	640,391
Investments at amortised cost	**48,746**	53,672
Receivables	**56,947**	56,985
Total	**819,508**	811,801
Credit commitments and contingent items	**43,665**	44,850
Total credit risk exposure	**863,173**	856,651

Where financial instruments are recorded at fair value the amounts shown above represent the current credit risk exposure but not the maximum risk exposure that could arise in the future as a result of changes in values.

Risk concentrations of the maximum exposure to credit risk
The Group financial assets having credit risk, before taking into account any collateral held can be analysed by the following geographical regions:

	Middle East 2011 BD 000	North America 2011 BD 000	Europe 2011 BD 000	Other 2011 BD 000	Total 2011 BD 000
Balances with banks	6,157	2,172	2,010	39	10,378
Murabaha and due from banks	102,212	-	-	-	102,212
Financing contracts with customers	578,589	2,978	-	19,658	601,225
Investments at amortised cost	40,263	943	-	7,540	48,746
Receivables	53,262	-	3,685	-	56,947
Credit commitments and contingent tems	43,665	-	-	-	43,665
Total	824,148	6,093	5,695	27,237	863,173

34 RISK MANAGEMENT (continued)

	Middle East 2010 BD 000	North America 2010 BD 000	Europe 2010 BD 000	Other 2010 BD 000	Total 2010 BD 000
Balances with banks	4,948	2,662	1,713	60	9,383
Murabaha and due from banks	51,370	-	-	-	51,370
Financing contracts with customers	637,669	1,941	-	781	640,391
Investments at amortised cost	39,065	985	-	1,910	41,960
Receivables	52,428	-	4,492	65	56,985
Credit commitments and contingent items	42,914	-	1,710	226	44,850
Total	828,394	5,588	7,915	3,042	844,939

An industry sector analysis of the Group financial assets having credit risk, before taking into account collateral held or other credit enhancements, is as follows:

	Trading and manufacturing 2011 BD 000	**Banking and financial 2011 BD 000**	**Construction and real estate 2011 BD 000**	**Other 2011 BD 000**	**Total 2011 BD 000**
Balances with banks	**-**	**10,378**	**-**	**-**	**10,378**
Murabaha and due from banks	**-**	**102,212**	**-**	**-**	**102,212**
Financing contracts with customers	**68,054**	**22,366**	**391,102**	**119,703**	**601,225**
Held to maturity investments	**-**	**9,614**	**39,132**	**-**	**48,746**
Receivables	**4,611**	**-**	**33,339**	**18,997**	**56,947**
Credit commitments and contingent items	**25,692**	**-**	**17,973**	**-**	**43,665**
Total	**98,357**	**144,570**	**481,546**	**138,700**	**863,173**

	Trading and manufacturing 2010 BD 000	Banking and financial 2010 BD 000	Construction and real estate 2010 BD 000	Other 2010 BD 000	Total 2010 BD 000
Balances with banks	-	9,383	-	-	9,383
Murabaha and due from banks	-	51,370	-	-	51,370
Financing contracts with customers	67,221	76,805	381,089	115,276	640,391
Held to maturity investments	-	6,975	34,985	-	41,960
Receivables	-	-	22,477	34,508	56,985
Credit commitments and contingent items	30,814	226	12,100	1,710	44,850
Total	98,035	144,759	450,651	151,494	844,939

34 RISK MANAGEMENT (continued)

Collateral and other credit enhancements
The amount and type of collateral required depends on an assessment of the credit risk of the counterparty. Guidelines are implemented regarding the acceptability of types of collateral and valuation parameters.

The main types of collateral obtained by the Bank are as follows:
- For commercial financing, lien over investment accounts, charges over real estate properties, inventory, trade receivables and unlisted equities; and
- For retail and consumer financing, lien over investment accounts, and mortgages over the related assets.

The Bank also obtains personal guarantees from companies owners for commercial financing obtained. Management monitors the market value of collateral, requests additional collateral in accordance with the underlying agreement, and monitors the market value of collateral obtained periodically during its review of the adequacy of the allowance for impairment losses.

Credit quality per class of financial assets
The credit quality of financial assets is managed by the Bank using internal credit gradings. These internal credit gradings are assigned to each individual borrower. They are defined as follows:

Good
Good credits' are those, which are performing, as the contract requires. There is no reason to suspect that the creditor's financial condition or collateral adequacy has depreciated in any way.

Substandard
Substandard credits are inadequately protected by the repayment capacity of the obligor or by the collateral pledged. They are characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected. Loss potential, while existing in the aggregate amount of substandard assets does not have to exist in individual assets classified substandard.

Doubtful / Loss (Individually impaired)
Doubtful credits have all the weaknesses inherent in a credit classified as substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable or improbable. The possibility of loss is extremely high, but because of certain important and reasonably specific pending factors which may work to the advantage and strengthening of the asset, its rating as an estimated loss is deferred until its more exact status may be determined. Total loss is expected for loss credits however in management's opinion recovery is a possibility, and hence write off is deferred.

Credit quality per class of financial assets

	Neither past due nor impaired				
	Good 2011 BD 000	Sub-standard 2011 BD 000	Past due but not impaired 2011 BD 000	Individually impaired 2011 BD 000	Total 2011 BD 000
Balances with banks	10,378	-	-	-	10,378
Murabaha and due from banks	102,212	-	-	-	102,212
Financing contracts with customers	461,516	23,855	125,135	5,170	615,676
Investments at amortised cost	48,746	-	-	-	48,746
Receivables	56,947	-	-	-	56,947
Total	679,799	23,855	125,135	5,170	833,959

34 RISK MANAGEMENT (continued)

	Neither past due nor impaired				
	Good 2010 BD 000	Sub-standard 2010 BD 000	Past due but not impaired 2010 BD 000	Individually impaired 2010 BD 000	Total 2010 BD 000
Balances with banks	9,383	-	-	-	9,383
Murabaha and due from banks	51,370	-	-	-	51,370
Financing contracts with customers	472,511	34,347	144,492	2,591	653,941
Investments at amortised cost	41,960	-	-	-	41,960
Receivables	56,985	-	-	-	56,985
Total	632,209	34,347	144,492	2,591	813,639

It is the Group's policy to maintain accurate and consistent risk ratings across the credit portfolio. This facilitates focused management of the applicable risks and the comparison of credit exposures across all lines of business, geographical regions and products. The rating system is supported by a variety of financial analytics, combined with processed market information to provide the main inputs for the measurement of counterparty risk. All internal risk ratings are tailored to the various categories and are derived in accordance with the Group's rating policy. The attributable risk ratings are assessed and updated regularly for corporate customers.

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

	Less than 30 days 2011 BD 000	**31 to 60 days 2011 BD 000**	**61 to 90 days 2011 BD 000**	**More than 90 days 2011 BD 000**	**Total 2011 BD 000**
Financing contracts with customers	**57,063**	**15,218**	**10,987**	**41,867**	**125,135**

	Less than 30 days 2010 BD 000	31 to 60 days 2010 BD 000	61 to 90 days 2010 BD 000	More than 90 days 2010 BD 000	Total 2010 BD 000
Financing contracts with customers	44,744	4,050	51,504	44,194	144,492

The estimated value of collateral held by the Bank against substandard and past due financing contracts amounts to BD 26,815 thousand and BD 384,040 thousand (2010: BD 32,279 thousand and BD 358,678 thousand) respectively. The utilisation of the above collaterals will be on a customer by customer basis and will be limited to the customer's total exposure.

Carrying amount by class of financial assets whose terms have been renegotiated

The outstanding amount of financing contracts with customers for which financing terms have been renegotiated (restructured facilities) amounted to BD 316,617 thousand (2010: BD 169,090 thousand) and these are secured with collateral amounting to BD 547,928 thousand (2010: BD 142,817 thousand). For restructured facilities amounting to BD 99,078 thousand (2010: BD 103,891 thousand) either six months or more have elapsed since the date of restructuring and the customers have made regular payments and on a timely basis or the deals have been settled. As a condition to restructuring, the Bank has received partial payment from customers and/or obtained additional collateral.

Included in the total amount of renegotiated facilities during the year is an amount relating to related parties of BD 29,426 thousand (2010: BD 16,950 thousand). These facilities are secured with collateral amounting to BD 6,937 (2010: BD 10,918 thousand).

34 RISK MANAGEMENT (continued)

Impairment assessment

The main considerations for impairment assessment include whether any payments of the principal or profit are overdue by more than 90 days or there are any known difficulties in the cash flows of counter parties, credit rating downgrades, or infringement of the original terms of the contract.

Individually assessed provisions

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

Collectively assessed provisions

Provisions are assessed collectively for losses on financing contracts that are not individually significant and for individually significant financing contract where there is not yet objective evidence of individual impairment. Provisions are evaluated on each reporting date with each portfolio subjected to a separate review.

The collective assessment takes account of impairment that is likely to be present in the portfolio even though there is not yet objective evidence of the impairment in an individual assessment. Impairment losses are estimated by taking into consideration of the following information: historical losses on the portfolio, current economic conditions, the approximate delay between the time a loss is likely to have been incurred and the time it will be identified as requiring an individually assessed impairment provision, and expected receipts and recoveries once impaired. Management is responsible for deciding the length of this period which can extend for as long as one year. The impairment provision is then reviewed as a part of the credit management framework to ensure alignment with the Group's overall policy.

Financial guarantees and letters of credit are assessed and provision made in a similar manner as for financing contracts.

34.3 Liquidity risk and funding management

Liquidity risk is the risk that the Group will be unable to meet its payment obligations when they fall due under normal and stress circumstances. To limit this risk, management arranges diversified funding sources in addition to its core deposit base, manages assets with liquidity in mind, and monitors future cash flows and liquidity on a daily basis. This incorporates an assessment of expected cash flows and the availability of high grade collateral which could be used to secure additional funding if required.

The Group maintains a portfolio of highly marketable and diverse assets that can be easily liquidated in the event of an unforeseen interruption of cash flow. The Group also has committed lines of credit that it can access to meet liquidity needs. In addition, the Bank maintains a mandatory reserve with the Central Bank of Bahrain equal to 5% of customer deposits denominated in Bahrain Dinars, excluding deposits from resident subsidiaries. The liquidity position is assessed and managed under a variety of scenarios, giving due consideration to stress factors relating to both the market in general and specifically to the Bank. The most important of these is to maintain limits on the ratio of liquid assets to customer liabilities. Liquid assets comprise of cash and balances with banks and Central Bank of Bahrain, Murabaha and due from banks, investment in quoted securities and liquid sukuk. Customer liabilities comprise of customers' current accounts, investment accounts and Murabaha and due to non banks. The ratios during the year were as follows:

	2011 **%**	2010 %
31 December	**21.87**	16.51
During the year: Average	**23.84**	14.79
Highest	**28.13**	16.97
Lowest	**17.77**	12.59

34 RISK MANAGEMENT (continued)

Analysis of financial liabilities and equity of investment account holders by remaining contractual maturities

The table below summarises the maturity profile of the Group's financial liabilities and equity of investment account holders at 31 December 2011 and 2010 based on contractual undiscounted repayment obligations. Maturity analysis of assets, liabilities and equity of investment account holders by expected maturities is disclosed in Note 33. Repayments which are subject to notice are treated as if notice were to be given immediately. However, the Group expects that many customers will not request repayment on the earliest date the Group could be required to pay and the table does not reflect the expected cash flows indicated by the Group's deposit retention history.

	On demand BD 000	Less than 3 months BD 000	3 to 12 months BD 000	1 to 5 years BD 000	Over 5 years BD 000	Total BD 000
At 31 December 2011						
Murabaha and due to banks	**9,017**	**120,132**	**79,127**	**6,748**	**-**	**215,024**
Murabaha and due to non-banks	**-**	**211,893**	**46,126**	**39,492**	**-**	**297,511**
Customers' current accounts	**73,802**	**-**	**-**	**-**	**-**	**73,802**
Other liabilities	**-**	**7,857**	**3,454**	**29,714**	**-**	**41,025**
Equity of investment account holders	**71,530**	**309,308**	**66,839**	**-**	**-**	**447,677**
Subordinated murabaha payable	**-**	**-**	**-**	**-**	**108,501**	**108,501**
Total undiscounted financial liabilities	**154,349**	**649,190**	**195,546**	**75,954**	**108,501**	**1,183,540**
At 31 December 2010						
Murabaha and due to banks	731	146,306	90,453	10,524	-	248,014
Murabaha and due to non-banks	-	155,307	12,153	21,820	-	189,280
Customers' current accounts	55,780	-	-	-	-	55,780
Other liabilities	-	7,841	7,033	24,395	4,798	44,067
Equity of investment account holders	43,972	345,823	65,818	-	-	455,613
Subordinated murabaha payable	-	-	-	-	101,096	101,096
Total undiscounted financial liabilities	100,483	655,277	175,457	56,739	105,894	1,093,850

Credit commitments and contingent items

These include commitments to enter into contracts which are designed to meet the requirements of the Group's customers. Commitments represent contractual commitments under murabaha, musharaka and ijarah muntahia bittamleek contracts. Commitments generally have fixed expiration dates, or other termination clauses. Since commitments may expire without being exercised, the total contract amounts do not necessarily represent future cash flow requirements.

Letters of credit and guarantees (including standby letters of credit) commit the Bank to make payments on behalf of customers contingent upon the failure of the customer to perform under the terms of the contract.

34 RISK MANAGEMENT (continued)

The table below shows the contractual expiry by maturity of the Group's credit commitments and contingent items.

	On demand BD 000	Less than 3 months BD 000	3 to 12 months BD 000	1 to 5 years BD 000	Total BD 000
At 31 December 2011					
Letters of credit	**2,441**	**-**	**11,126**	**-**	**13,567**
Guarantees	**-**	**12,125**	**-**	**-**	**12,125**
Irrevocable commitments to extend credit	**-**	**2,084**	**6,139**	**-**	**8,223**
Investment commitment	**-**	**-**	**7,750**	**2,000**	**9,750**
Total	**2,441**	**14,209**	**25,015**	**2,000**	**43,665**
At 31 December 2010					
Letters of credit	439	-	12,339	-	12,778
Guarantees	-	14,904	-	-	14,904
Irrevocable commitments to extend credit	-	1,846	15,087	9	16,942
Investment commitment	-	-	-	226	226
Total	439	16,750	27,426	235	44,850

The Group does not expect any material loss in respect of the above.

34.4 Market risk

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to changes in market variables such as profit rates, foreign exchange rates, and equity prices. The Group manages and monitors the positions using sensitivity analysis.

Profit rate risk

Profit rate risk arises from the possibility that changes in profit rates will affect future profitability or the fair values of financial instruments. The Bank measures the profit rate risk by measuring and managing the repricing gaps. It also performs sensitivity analysis.

The following table demonstrates the sensitivity to reasonably possible change in profit rates, with all other variables held constant of the Group's consolidated statement of income. The sensitivity of the consolidated statement of income is the effect of the assumed changes in profit rates on the consolidated net income for the year, based on the non-trading financial assets and financial liabilities held as at the date of statement of financial position.

The effect of decrease in basis points is expected to be equal and opposite to the effect of the increase shown.

	2011 BD 000	Change in basis points	Effect on net income for the year BD 000
ASSETS			
Murabaha and due from banks	**102,212**	**+25**	**256**
Financing contracts with customers	**242,604**	**+25**	**607**
Investments at amortised cost	**62,078**	**+25**	**155**
LIABILITIES AND EQUITY OF INVESTMENT ACCOUNT HOLDERS			
Murabaha and due to banks	**213,441**	**+25**	**534**
Murabaha and due to non-banks	**290,688**	**+25**	**727**
Subordinated murabaha payable	**100,186**	**+25**	**250**
Equity of investment account holders	**445,288**	**+25**	**1,113**
Total			**3,642**

34 RISK MANAGEMENT (continued)

	2010 BD 000	Change in basis points	Effect on net income for the year BD 000
ASSETS			
Murabaha and due from banks	51,370	+25	128
Financing contracts with customers	232,991	+25	582
Investments at amortised cost	53,672	+25	134
LIABILITIES AND EQUITY INVESTMENT ACCOUNT HOLDERS			
Murabaha and due to banks	246,406	+25	(616)
Murabaha and due to non-banks	187,785	+25	(469)
Subordinated murabaha payable	99,423	+25	(249)
Equity of investment account holders	452,963	+25	(1,132)
Total			(1,622)

Currency risk
Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Bank has established Value at Risk limit for foreign currency exposures. This limit is monitored on a regular basis by the Risk Management Group and reported to the ALCO.

The Group had the following significant net exposures denominated in foreign currencies as of 31 December:

	Equivalent long (short) 2011 BD '000	Equivalent long (short) 2010 BD '000
Currency		
NZD	**3**	614
KWD	**(183)**	(19,234)
JOR	**34,242**	29,714
GBP	**2,561**	(3,752)
EUR	**1,783**	(1,676)

The table below indicates the currencies to which the Group had significant exposure at 31 December on all its monetary assets and liabilities. The analysis calculates the effect of a reasonably possible movement of the currency rate against the Bahraini Dinar, with all other variables held constant, on the consolidated statement of income.

34 RISK MANAGEMENT (continued)

The effect of decreases in currency rate is expected to be equal and opposite to the effect of the increases shown.

	Change in currency rate %	Effect on profit 2011 BD 000	Effect on equity 2011 BD 000	Change in currency rate %	Effect on profit 2010 BD 000	Effect on equity 2010 BD 000
NZD	+20	1	-	+20	123	-
KWD	+20	(37)	-	+20	(3,847)	-
JOR	+20	6,848	-	+20	5,943	-
GBP	+20	512	-	+20	(750)	-
EUR	+20	357	-	+20	(335)	-
Total		7,681	-		1,134	-

Equity price risk

Equity price risk is the risk that the fair values of equities decrease as a result of changes in the levels of equity indices and the value of individual stocks. The equity price risk exposure arises from the Group's investment portfolio.

The effect on income and equity (as a result of a change in the fair value of equity instruments at 31 December 2011) due to a reasonably possible change (i.e. +10%) in the value of individual investments, with all other variables held constant, is BD 20,055 thousand and BD 761 thousand (2010: BD 27,222 thousand and BD 821 thousand) respectively. The effect of decrease in the value of individual investments is expected to be equal and opposite to the effect of the increase shown.

34.5 Prepayment risk

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

34.6 Investment property price risk

Investment property price risk is the risk that the fair values of investment properties decrease as a result of downfall in the real estate market. The investment property price risk exposure arises from Group's holding of investment properties (land and buildings).

The effect on income due to a reasonably possible change (i.e. +10%) in the value of individual investment properties, with all other variables held constant, is BD 23,120 thousand (2010: 21,461 thousand). The effect of decrease in the value of individual investment is expected to be equal and opposite to the effect of the increase shown.

34.7 Operational risk

Operational risk is the risk of loss arising from systems failure, human error, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to financial loss. The Group cannot expect to eliminate all operational risks, but through a control framework and by monitoring and responding to potential risks. The Bank has implemented Risks Controls and Self Assessment process (RCSA) whereby each of the units identifies risks in processes, key risk indicators and implemented controls. The key risk indicators values and actual incidents to the operational risk unit are reported to senior management for action. Controls include effective segregation of duties, access, authorisation and reconciliation procedures, staff education and assessment processes, including the use of internal audit.

35 CAPITAL MANAGEMENT

The Group maintains an actively managed capital base to cover risks inherent in the business. The adequacy of the Group's capital is monitored using, among other measures, the rules and ratios established by the Basel Committee on Banking Supervision ("BIS rules/ratios") and adopted by the Central Bank of Bahrain in supervising the Group. The Bank has also implemented the Internal Capital Adequacy and Assessment Plan (ICAAP) as per the CBB guidelines based on Pillar II recommendations of the Basel Committee. The Bank had identified the capital requirement for future five years based on the Bank's business strategy and the risk charges required for its significant risks including credit risk, market risk, profit rate risk, liquidity risk, investments risks and operational risks. The Board of Directors, on an annual basis, review and approve the ICAAP plan for both normal and stress conditions.

35 CAPITAL MANAGEMENT (continued)

The primary objectives of the Group's capital management are to ensure that the Group complies with externally imposed capital requirements and that the Group maintains healthy 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 the 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 capital securities. No changes were made in the objectives, policies and processes from the previous years.

Regulatory capital and risk-weighted assets
The regulatory capital and risk-weighted assets have been calculated in accordance with Basel II as adopted by the CBB.

		2011 BD 000	2010 BD 000
Tier 1 capital	35.1	**257,099**	215,597
Tier 2 capital	35.2	**60,249**	37,124
Total capital		**317,348**	252,721
Credit risk-weighted assets		**1,046,644**	1,004,564
Market risk-weighted assets		**42,133**	45,774
Operational risk-weighted assets		**122,055**	96,907
Total risk weighted assets		**1,210,832**	1,147,245
Capital adequacy ratio		**26.2%**	22.0%
Minimum requirement		**12.0%**	12.0%

35.1 Tier 1 capital comprises share capital, share premium, general reserve, statutory reserve and retained earnings, less unrealised loss arising from fair valuing equities net of deductions.

35.2 Tier 2 capital comprises subordinated murabaha payable, collective impairment provision and asset revaluation reserves net of deductions. Certain adjustments are made to AAOIFI-based results and reserves, as prescribed by the Central Bank of Bahrain.

36 EARNINGS AND EXPENSES PROHIBITED BY SHARI'A

The Group did not receive any significant income or incur significant expenses which were prohibited by the Shari'a.

37 SOCIAL RESPONSIBILITY

The Bank discharges its social responsibilities through donations to charitable causes and organisations approved by Shari'a Supervisory Board.

38 ZAKAH

In accordance with the instructions of the Shari'a Supervisory Board of the Bank, payment of Zakah is the responsibility of the shareholders of the Bank. Accordingly, no Zakah has been charged to these consolidated financial statements.

39 COMPARATIVE FIGURES

Certain of the prior year figures have been reclassified as explained in note 9. Such reclassification does not affect previously reported net income or shareholders' equity.

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