Elaf Bank B.S.C. (c)

SHARI'A SUPERVISORY BOARD REPORT, REPORT OF THE BOARD OF DIRECTORS, INDEPENDENT AUDITORS' REPORT AND CONSOLIDATED FINANCIAL STATEMENTS

31 DECEMBER 2012

بنك إيلاف
ELAF BANK

To the Shareholders of ELAF Bank.

Assalam Alaykum Wa Rahmatul-Allah,

In compliance with the letter of appointment, we are required to submit the following report:

We have reviewed the principles and contracts relating to the transactions and applications introduced by ELAF Bank and its affiliates during **the year ending December 31, 2012.** We have also conducted our review to form an opinion as to whether ELAF Bank and its affiliates have complied with Shari'a rules and principles, and also with specific "fatwa" rulings, and guidelines issued by the Shari'a Supervisory Board.

We conducted our review directly, or through the Internal Shari'a Compliance Department, which included examining, on sample basis of each type of transactions, the relevant documentation and procedures adopted by ELAF Bank. We planned and performed our review so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that ELAF Bank and its affiliates have not violated Islamic Shari'a rules and principles.

Our responsibility is restricted to provide an independent opinion, based on our review of the operations of ELAF Bank and its affiliates, and report to you. The management of ELAF Bank is responsible to ensure that the financial institution conducts its business in accordance with Islamic Shari'a rules and principles.

Based on the above, the Shari'a Supervisory Board discloses the following opinion:

A) the contracts, transactions and dealings entered into by ELAF Bank and its affiliates during **the year ending December 31, 2012**, which we have reviewed, are in compliance with Islamic Shari'a rules and principles;

B) the allocation of profit and charging of losses relating to investment accounts conform to the basis that have been approved by the Shari'a Supervisory Board and in accordance with Islamic Shari'a rules and principles;

C) all earnings have been realized from sources or by means permitted by Islamic Shari'a rules and principles;

D) the calculation, and payment of Zakat is the responsibility of the shareholders.

We pray to Allah the Almighty to grant us all the success and straight-forwardness.

Dr. Abdul-Sattar Abou Ghuddah	Shaikh Adnan Alqattan	Shaikh Nizam Ya'aqubi
Shari'a Board Member	Shari'a Board member	Shari'a Board member

Kingdom of Bahrain , 12 /5/1434 Hijri , 24/3/2013 .

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INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF ELAF BANK B.S.C. (c)

We have audited the accompanying consolidated statement of financial position of Elaf Bank B.S.C. (c) ("the Bank") and its subsidiaries ("the Group") as of 31 December 2012, and the related consolidated statements of income, cash flows, changes in owners' equity and changes in off-balance sheet equity of investment accountholders for the year then ended. 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 Group'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 2012, the results of its operations, its cash flows, changes in owners' equity and changes in off-balance sheet equity of investment accountholders for the year then ended in accordance with the Financial Accounting Standards issued by AAOIFI.

Ernst & Young

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF ELAF BANK B.S.C. (c) (continued)

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 Report of the Board of Directors 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 ended 31 December 2012 that might have had a material adverse effect on the business of the Bank or on its financial position. Satisfactory explanations and information have been provided to us by 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 Group.

Ernst & Young

27 March 2013
Manama, Kingdom of Bahrain

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

At 31 December 2012

	Notes	*2012* *US$*	*2011* *US$*
ASSETS			
Cash and balances with banks	4	**12,986,997**	2,354,933
Due from financial institutions	5	**35,083,388**	14,206,052
Financing receivable	6	**13,698,448**	3,272,458
Musharaka financing	7	**1,902,720**	958,810
Receivable from ijarah investors	8	**14,800,849**	-
Investment in ijarah asset	9	**4,961,974**	7,650,409
ijarah muntahia bittamleek	10	**1,905,822**	-
Investments in securities	11	**232,067,260**	109,957,281
Investment in associates	12	**5,046,963**	3,444,085
Investment in real estate	13	**38,441,871**	15,842,773
Development properties	14	**16,173,111**	-
Non-current asset held for sale	15	**1,326,260**	-
Fixed assets	16	**433,070**	1,566,186
Other assets	17	**3,938,566**	1,704,978
TOTAL ASSETS		**382,767,299**	160,957,965
LIABILITIES, EQUITY OF INVESTMENT ACCOUNT HOLDERS AND OWNER'S EQUITY			
Liabilities			
Due to financial institutions	18	**39,036,923**	4,543,500
Due to non financial institutions	19	**435,408**	-
Other liabilities	20	**15,641,883**	1,646,066
Total liabilities		**55,114,214**	6,189,566
EQUITY OF INVESTMENT ACCOUNTHOLDERS	21	**1,263,633**	-
OWNERS' EQUITY			
Share capital	22	**300,000,000**	200,000,000
Share premium	22	**16,385,368**	-
Statutory reserve	22	**676,313**	676,313
Accumulated losses	22	**-**	(45,011,717)
Investment fair value reserves	22	**796,081**	(896,197)
General reserve	22	**4,618,036**	-
Equity attributable to parent's shareholders		**322,475,798**	154,768,399
Non-controlling interest		**3,913,654**	-
Total owners' equity		**326,389,452**	154,768,399
TOTAL LIABILITIES, EQUITY OF INVESTMENT ACCOUNT HOLDERS AND OWNER'S EQUITY		**382,767,299**	160,957,965
OFF BALANCE SHEET:			
EQUITY OF INVESTMENT ACCOUNT HOLDERS		**111,994,905**	-
COMMITMENTS	34	**14,277,462**	3,266,472

Paul Mercer
Chairman

Mohamed Al Adsani
Vice Chairman

The attached notes 1 to 38 form part of these consolidated financial statements.

Elaf Bank B.S.C. (c)

CONSOLIDATED STATEMENT OF INCOME

For the year ended 31 December 2012

	Notes	2012 US$	2011 US$
INCOME			
Profit from Islamic financing	23	**2,575,200**	2,781,574
Profit on Islamic financing		**(170,704)**	(59,333)
Net income from Islamic financing		**2,404,496**	2,722,241
Income from investment in securities	24	**9,263,830**	6,979,459
Income from investment banking services		**218,760**	20,000
Other income - net		**6,208**	67,047
Total income		**11,893,294**	9,788,747
EXPENSES			
Staff cost	25	**4,280,076**	5,130,200
Depreciation and amortisation	26	**1,268,853**	1,110,599
Other expenses	27	**3,577,206**	2,829,350
Total expenses		**9,126,135**	9,070,149
NET INCOME BEFORE ACQUISITION EXPENSES, PROVISION AND IMPAIRMENT		**2,767,159**	718,598
Provision and impairment	28	**(6,621,795)**	(4,888,684)
Acquisition expenses	29	**(8,515,611)**	-
NET LOSS FOR THE YEAR		**(12,370,247)**	(4,170,086)

P. l. Mercer

Paul Mercer
Chairman

Mohamed Al Adsani
Vice Chairman

The attached notes 1 to 38 form part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended 31 December 2012

	Notes	*2012 US$*	*2011 US$*
OPERATING ACTIVITIES			
Net loss for the year		**(12,370,247)**	(4,170,086)
Adjustment for non cash items:			
Depreciation and amortisation	26	**1,268,853**	1,110,599
Fixed assets write off	27	**765,320**	-
Gain on sale of investments	24	**(3,642,144)**	(852,707)
Gain on amalgamation	3	**(32,524)**	-
Gain on sale of fixed assets		**(17,560)**	-
Net amortisation of discount and premium		**(594,762)**	(1,433,016)
Impairment and provision	28	**6,621,795**	4,888,684
Operating profit (loss) before changes in operating assets and liabilities		**(8,001,269)**	(456,526)
Changes in operating assets and liabilities:			
Financing receivable		**1,946,072**	11,829,650
Musharaka financing		**(75,951)**	(965,834)
Ijarah muntahia bittamleek		**(1,905,822)**	-
Other assets		**(462,267)**	(275,628)
Other liabilities		**7,212,176**	869,312
Net cash (used in) from operating activities		**(1,287,061)**	11,000,974
INVESTMENT ACTIVITIES			
Purchase of investment in securities		**(91,788,574)**	(48,385,029)
Proceeds from sale of investment in securities		**94,190,008**	38,682,496
Purchase of fixed assets		**(88,091)**	(598,262)
Proceeds from sale of fixed assets		**17,560**	-
Net cash from (used in) investing activities		**2,330,903**	(10,300,795)
FINANCING ACTIVITY			
Due to financial institutions		**9,484,438**	4,543,500
Net cash from financing activity		**9,484,438**	4,543,500
NET INCREASE IN CASH AND CASH EQUIVALENTS		**10,528,280**	5,243,679
Cash and cash equivalents at 1 January		**16,560,985**	11,317,306
Cash and cash equivalents received on amalgamation		**16,444,807**	-
CASH AND CASH EQUIVALENTS AT 31 DECEMBER		**43,534,072**	16,560,985
CASH AND CASH EQUIVALENTS COMPRISE:			
Cash and balances with banks	4	**12,986,997**	2,354,933
Due from financial institutions with original maturity of 90 days or less	5	**30,547,075**	14,206,052
		43,534,072	16,560,985

The attached notes 1 to 38 form part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN OWNERS' EQUITY

For the year ended 31 December 2012

	Notes	*Share capital US$*	*Share premium US$*	*Statutory reserve US$*	*Accumulated losses US$*	*Investment fair value reserve US$*	*General reserve US$*	*Total US$*	*Non-controlling interest US$*	*Total owners' equity US$*
Balance at 1 January 2012		200,000,000	-	676,313	(45,011,717)	(896,197)	-	154,768,399	-	154,768,399
Reduction of share capital	22.a	(62,000,000)	-	-	45,011,717	-	16,988,283	-	-	-
Issue of shares	22.b	162,000,000	16,385,368	-	-	-	-	178,385,368	-	178,385,368
Net loss for the year		-	-	-	(12,370,247)	-	-	(12,370,247)	-	(12,370,247)
Transfer to general reserve	22.a	-	-	-	12,370,247	-	(12,370,247)	-	-	-
Acquisition of non-controlling interests		-	-	-	-	-	-	-	3,913,654	3,913,654
Cumulative changes in fair values		-	-	-	-	367,776	-	367,776	-	367,776
Transfer to statement of income on imapirment	28.b	-	-	-	-	1,324,502	-	1,324,502	-	1,324,502
Balance at 31 December 2012		**300,000,000**	**16,385,368**	**676,313**	**-**	**796,081**	**4,618,036**	**322,475,798**	**3,913,654**	**326,389,452**
Balance at 1 January 2011		200,000,000	-	676,313	(40,841,631)	(1,201,823)	-	158,632,859	-	158,632,859
Net loss for the year		-	-	-	(4,170,086)	-	-	(4,170,086)	-	(4,170,086)
Cumulative changes in fair values		-	-	-	-	305,626	-	305,626	-	305,626
Balance at 31 December 2011		200,000,000	-	676,313	(45,011,717)	(896,197)	-	154,768,399	-	154,768,399

The attached notes 1 to 38 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 2012

	Cash *USD '000*	*Marketable equity securities portfolio* *USD '000*	*Unlisted securities portfolio* *USD '000*	*Real estate portfolio* *USD '000*	*Total* *USD '000*
Balance at 1 January 2012	-	-	-	-	-
Additions by amalgamation (note 3)	1,263,634	1,756,161	66,250,381	42,724,729	111,994,905
Balance at 31 December 2012	**1,263,634**	**1,756,161**	**66,250,381**	**42,724,729**	**111,994,905**

On 31 December 2012, via letter no. EDBS/KH/337/2012, CBB approved the legal amalgamation of Capivest and CMH operations into the Bank in respect to which the net identifiable assets of CMH and Capivest as of 31 December 2012 were assumed by the Bank along with the off-balance sheet equity of investment accountholders.

1 INCORPORATION AND ACTIVITIES

Elaf Bank B.S.C. (c) ("the Bank"), is a closed shareholding company incorporated in the Kingdom of Bahrain on 12 June 2007 under commercial registration (CR) number 65549. The Bank operates as an Islamic Wholesale Investment Bank under a license issued by the Central Bank of Bahrain ("the CBB"). The Bank's registered office is Zamil Tower, 6th Floor, Al Khalifa Avenue, Block 305, Manama, Kingdom of Bahrain.

During the year, the shareholders of the Bank approved the merger of the Bank with Capivest B.S.C (c) (Capivest) and Capital Management House B.S.C. (CMH) where Capivest and CMH operations were amalgamated into the Bank's operations to form the Merged Entity in accordance with Article 312 (a) (1) of the Bahrain Commercial Companies Law. The merger was approved by the CBB and the Ministry of Industry and Commerce on 13 September 2012 and 11 October 2012 respectively subject to a 90 days no objection period. On 31 December 2012, via letter no. EDBS/KH/337/2012, CBB approved the legal amalgamation of Capivest and CMH operations into the Bank in respect to which the assets of CMH and Capivest as of 31 December 2012 were takenover and liabilites of CMH and Capivest as of 31 December 2012 were assumed by the Bank along with the off-balance sheet equity of investment accountholders. As a consideration for the above amalgamation the Bank issued 162,000 thousand shares to the shareholders of Capivest and CMH for a shareholding of 23% and 31% respectively in the merged entity. This transaction is considered as acquisition of CMH and Capivest by the Bank and has been accounted for accordingly. As the acquisition took place on the last day of the financial year of the Bank (31 December 2012), the statement of financial position has been consolidated and there is no impact on the statement of income due to the acquisition of CMH and Capivest by the Bank.

The Bank's activities are regulated by the CBB and supervised by a Shari'a Supervisory Board whose role is defined in the Bank's Memorandum and Articles of Association.

The principal activities of the Bank and its subsidiaries ("the Group") include investment advisory services and investment transactions, which comply with Islamic rules and principles according to the opinion of the Bank's Shari'a Supervisory Board.

The Bank carries out its business activities through its head office in the Kingdom of Bahrain and its branch in Malaysia. The branch was granted a license to perform Islamic banking business on 15 June 2011 under Islamic Banking Act 1983.

These consolidated financial statements were authorised for issue in accordance with a resolution of the Board of Directors on 27 March 2013.

2 ACCOUNTING POLICIES

2.1 Basis of preparation

The consolidated financial statements have been prepared on a historical cost basis, except for equity-type instruments at fair value through statement of income, equity-type instruments through equity, investment in real estate and non-current asset held for sale that have been measured at fair value. The consolidated financial statements are presented in United States Dollars, being the functional and reporting currency of the Group. All values are rounded to the nearest US Dollar unless otherwise indicated.

Statement of Compliance

The consolidated financial statements are prepared in accordance with the Financial Accounting Standards (FAS) issued by the Accounting and Auditing Organisation for Islamic Financial Institutions ("the AAOIFI"), the Shari'a Rules and Principles as determined by the Shari'a Supervisory Board of the Group, the Bahrain Commercial Companies Law, the CBB and Financial Institutions Law, and the CBB regulations (as contained in Volume 2 and applicable provisions of Volume 6 of CBB rulebook) and directives. In accordance with the requirements of AAOIFI, for matters which are not covered by the AAOIFI standards including "Interim Financial Reporting," the Group uses the relevant International Financial Reporting Standards ("the IFRS") issued by International Accounting Standards Board ("the IASB").

2 ACCOUNTING POLICIES (continued)

2.1 Basis of preparation (continued)

Basis of consolidation
The consolidated financial statements comprise the financial statements of the Bank and its subsidiaries as at and for the year ended 31 December each year. 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 profits and losses resulting from intra-group transactions are eliminated in full.

Subsidiaries are fully consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date that 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.

Special Purpose Vehicles (SPVs) for holding investments which are intended to be marketed within twelve months from their acquisition to portfolio customers are not consolidated in the financial statements and are presented as "Non-current assets held for sale".

Non-controlling interest represents the portion of net income and net assets not held, directly or indirectly, 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 parent shareholders' equity.

The following are the principal subsidiaries of the Bank, which are consolidated in these consolidated financial statements:

Company		*Activities*	*Year of incorporation*	*Country of incorporation*	*Ownership 2012*	*Ownership 2011*
	Subsidiaries					
1	Elaf Bahrain Real Estate Company B.S.C. (c)	Subsidiary to purchase and sale all kinds of real estate properties	2008	Kingdom of Bahrain	100%	100%
2	Elaf Corporate Services Limited	Subsidiary to manage its affiliated companies	2008	British Virgin Islands	100%	100%
3	Sokouk Exchange Centre – Tadawul Holding W.L.L.	Subsidiary to manage its affiliated companies	2008	Kingdom of Bahrain	100%	100%
4	Tamkeen Investment Company B.S.C. (c)	Subsidiary to administer Management Incentive Program ("MIP").	2008	Kingdom of Bahrain	100%	-
5	Suffun Bahrain W.L.L. **	SPV for an associated company investment.	2010	Kingdom of Bahrain	100%	-
6	Suffun Investment Company *	SPV for investors investment in an associated company	2010	Cayman Island	100%	-

2 ACCOUNTING POLICIES (continued)

2.1 Basis of preparation (continued)

	Company	*Activities*	*Year of incorporation*	*Country of incorporation*	*Ownership 2012*	*Ownership 2011*
7	GCC Balanced Growth Fund Company B.S.C.(c)	SPV for GCC Balanced Growth Fund	2010	Kingdom of Bahrain	100%	-
8	Medical Management Group SPC	SPV to Investment in health care	2005	Kingdom of Bahrain	100%	-
9	Omavest Holding W.L.L.	SPV to Investment in various projects	2009	Kingdom of Bahrain	100%	-
10	Capivest Real Estate Fund	SPV to Investment in various projects	2010	Kingdom of Bahrain	100%	-
11	Sakan Development Company Limited	SPV to Investment in real estate	2006	Cayman Island	70.91%	-

* Subsidiary not operational at 31 December 2012.
** Subsidiary is held as "Non-current assets held for sale"

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

a. Cash and cash equivalent
Cash and cash equivalents as referred to in the consolidated statement of cash flows comprise cash and balances with banks and amounts due from financial institutions with original maturities of 90 days or less.

b. Due from financial institutions
Commodity murabaha receivables
Commodity murabaha receivables are sales on deferred terms. The Group arranges a murabaha transaction by buying a commodity (which represents the object of the murabaha) and then resells this commodity to a Murabeh (beneficiary) after computing a margin of profit over cost. The sale price (cost plus the profit margin) is repaid in instalments by the Murabeh over the agreed period.

These are stated net of deferred profits, and provision for doubtful debts, if any. The Group considers the promise made by the purchase orderer in a Murabaha contract as obligatory.

Mudaraba investments
Mudaraba investments are stated at the fair value of consideration given less impairment, if any.

A Mudaraba investment is a partnership where the Group ("Rabbalmal") gives money to another ("Mudarib") for investing in a commercial enterprise for a definite period of time.

Mudaraba capital provided by the Group at inception in kind (if other than cash) is measured at the fair value of the assets. If the valuation of assets results in a difference between fair value and book value, such difference is recognized as profit or loss to the group.

In case Mudaraba capital is lost or damaged prior to the inception of work without misconduct or negligence on the part of the mudarib, then such losses are deducted from mudaraba capital and are treated as a loss to the Group. In the case of termination or liquidation, the unpaid portion by the mudarib is recognized as receivable due from the mudarib.

2 ACCOUNTING POLICIES (continued)

c. Financing receivables

Financing receivables are stated at cost net of deferred profit and provision for impairment, if any. The Group considers the promise made by the purchase orderer in a financingcontract as obligatory. Specific provisions are created for impairment where losses are expected to arise on non-performing contracts. The receivables are written off when they are considered to be uncollectible to reduce all impaired financing receivables to their expected realisable values.

d. Musharaka financing

Musharaka is a form of capital partnership. These are stated at the fair value of consideration given less any impairment. Musharaka capital provided by the Group at inception in kind (if other than cash) is measured at the fair value of the assets. If the valuation of assets results in difference between fair value and book value, such difference is recognized as profit or loss to the Group.

e. Investment in ijarah assets and ijarah muntahia bittamleek

These are initially recorded at cost including initial direct costs. 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. These assets are stated at cost less accumulated depreciation.

Depreciation is calculated using the straight-line method on Ijarah muntahia bittamleek assets at rates calculated to write off the cost of each asset over its lease term. For Ijarah assets, the depreciation is calculated using the straight-line method, at rates calculated to write off the cost of the assets over its estimated useful life.

f. Investments in securities

Investments comprise equity-type instruments at fair value through statement of income, equity-type instruments at fair value through equity and debt-type instruments at amortised cost.

Investments are recognised on the acquisition date at their fair value plus transaction costs, except for "investments at fair value through statement of income". Transaction costs relating to "investments at fair value through statement of income" are charged to the consolidated statement of income when incurred.

Equity-type instruments at fair value through statement of income

This includes instruments held for the purpose of generating profits from the short term market fluctuations. These are initially recognised at cost, being the fair value of the consideration given excluding acquisition costs. These are subsequently re-measured at fair value. All related realised and unrealised gains or losses are included in the consolidated statement of income.

All other investments are initially recognised at cost, being the fair value of the consideration given including transaction costs.

Equity-type instruments at fair value through equity

These include all equity-type instruments that are not fair valued through statement of income. Subsequent to acquisition, these are re-measured at fair value with unrealised gains or losses recognised directly in owners' equity under "Investment fair value reserve" until the investment is derecognised or determined to be impaired at which time the cumulative gain or loss previously recorded in owners' equity is recognised in consolidated statement of income.

Instruments which do not have a quoted market price or other appropriate methods from which to derive reliable fair values are stated at cost less impairment.

The losses arising from impairing fair value through equity investments are recycled in the consolidated statement of income in "provision for impairment" and removed from the cumulative changes in fair value reserve. Subsequent increases in the fair value of investments at fair value through equity are not reversed through the consolidated statement of income.

2 ACCOUNTING POLICIES (continued)

2.2 Summary of significant accounting policies (continued)

f. Investments in securities (continued)

Debt-type instruments at amortised cost
These are managed on a contractual yield basis and are not held for trading and has not been designated at fair value through statement of income are classified as debt-type instruments at amortised cost. Such investments are carried at amortised cost, less provision for impairment in value. Amortised cost is calculated by taking into account any premium or discount on acquisition. Any gain or loss on such investment is recognised in the consolidated statement of income, when the investment is de-recognised or impaired.

g. Investment in associates
The Group's investment in its associates is accounted for under the equity method of accounting. 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. Where there has been a change recognised directly in the equity of the associate. The Group recognises its share of any changes and discloses this when applicable, in the statement of changes in owners' equity. Goodwill relating to an associate is included in the carrying amount of the investment and is not amortised. The consolidated statement of income reflects the Group's share of the results of operations of the associate. If the Group's share of losses exceeds its interest in an associate, the Group's carrying amount is reduced to nil and recognition of further losses is discontinued except to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of the associate. Profits and losses resulting from transactions between the Group and the associate are eliminated to the extent of the interest in the associate.

h. Investment in real estate
All properties held for rental or for capital appreciation purposes, or both, are classified as investment in real estate. These are initially recognised at cost and subsequently re-measured at fair value with the resulting unrealized gains being recognised in the consolidated statement of changes in owners' equity under investment fair value reserves. Unrealized losses are recognised in equity to the extent of the available balance. In case cumulative losses exceed the available balance under equity, the excess is recognised in the consolidated statement of income under "provision for impairment".

i. Development properties
Properties constructed and held for sale are classified as development properties. Unsold properties are stated at the lower of cost or net realisable value. The cost of development properties includes the cost of land and other related expenditure which are capitalised as and when activities that are necessary to get the properties ready for sale are in progress. Net realisable value represents the estimated selling price less costs to be incurred in selling the property.

j. Non-current assets held for sale
Subsidiaries/associates acquired with a view to subsequent disposal within 12 months are classified as non current assets "held-for-sale" when the sale is highly probable. Related assets and liabilities of the subsidiary/associate are shown separately on the consolidated statement of financial position as "Assets held-for-sale" and "Liabilities relating to assets held-for-sale". Assets that are classified as held-for-sale are measured at the lower of carrying amount or fair value less costs to sell. Any resulting impairment loss reduces the carrying amount of the assets. Assets that are classified as held-for-sale are not depreciated. Any impairment loss is recognised in the consolidated statement of income for any initial and subsequent write down of these assets to fair value, less costs to sell. A gain for any subsequent increase in the fair value, less costs to sell, is recognised to the extent that it is not in excess of the cumulative impairment loss that was previously recognised.

2 ACCOUNTING POLICIES (continued)

2.2 Summary of significant accounting policies (continued)

k. Fixed assets

Fixed assets are stated at cost, net of accumulated depreciation and impairment, if any. The cost of additions and major improvements are capitalised; maintenance and repairs are charged to the consolidated statement of income as incurred. Gains or losses on disposal are reflected in other income. Depreciation is provided on the straight-line basis over the estimated useful lives of the assets.

The calculation of depreciation and amortisation is on the following basis:

• Leasehold improvements	10 years *
• Computer hardware and software	3 years
• Furniture and fixture	5 years
• Office and electric equipment	5 years
• Motor vehicles	4 years

* The calculation of depreciation on leasehold improvements is calculated over the life of lease if less than 10 years.

l. Fair values

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

(i) For investments that are traded in organised financial markets, fair value is determined by reference to the quoted market bid prices prevailing on the consolidated statement of financial position date.

(ii) For unquoted investments, fair value is determined by reference to recent significant 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 the current market value of similar investments or applying relevant valuation techniques including net present value of estimated future cash flows, comparison to similar instruments for which market observable prices exist and other relevant valuation models.

(iii) For investments that have fixed or determinable cash flows, fair value is based on the net present value of estimated future cash flows determined by the Group using current profit rates for investments with similar terms and risk characteristics.

(iv) Investments which cannot be remeasured to fair value using any of the above techniques are carried at cost, less provision for impairment.

m. Business combination

Business combinations are accounted for using the purchase method of accounting. This involves recognising identifiable assets and liabilities (including contingent liabilities) 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 discount on acquisition is recognised directly in the consolidated statement of income in the year of acquisition.

n. Impairment of financial assets

The Group assesses at each financial position date whether there is objective evidence that a financial asset is impaired. In the case of equity-type instruments at fair value through equity, a significant or prolonged decline in the fair value of the security below its cost is considered in determining whether the assets are impaired. If any such evidence exists for equity-type instruments at fair value through equity, the cumulative loss (measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in consolidated statement of income) is removed from owners' equity and recognised in the consolidated statement of income. Impairment losses recognised in the consolidated statement of income on equity instruments are not subsequently reversed through the consolidated statement of income.

2 ACCOUNTING POLICIES (continued)

2.2 Summary of significant accounting policies (continued)

n. Impairment of financial assets (continued)

Impairment losses on financing receivables and debt-type instruments at amortised cost are measured as the difference between the carrying amount of the financial asset and the present value of estimated cash flows discounted at the assets' original effective profit rate. Losses, if any, are recognised in the consolidated statement of income and reflected in an allowance account against murabaha receivables and debt-type instruments at amortised cost. When a subsequent event causes the amount of impairment loss to decrease, the impairment loss is reversed through the consolidated statement of income.

o. Due to financial institutions

These comprise placements received in the form of wakala and murabaha contracts. These are carried at their amortised cost.

p. Equity of investment account holders

Equity of investment account holders are carried at fair value of consideration received plus accrued profits less amounts settled.

Total income pertaining to investment account holders is allocated to individual investment accounts on their daily weighted average balances.

q. Foreign currency transactions

Functional and presentation currency

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

Transactions and balances

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

Group companies

The Group companies' functional currencies are either denominated in US Dollars or currencies, which are effectively pegged to the US Dollar, and hence, the translation of financial statements of the group entities that have a functional currency different from the presentation currency do not result in exchange difference.

r. Revenue recognition

Profit from Islamic financing

Income from murabaha receivable is recognised when the income is quantifiable and contractually determined at the commencement of the contract, the income is recognised proportionately over the period of the contract.

Income on mudaraba is recognised when the right to receive payment is established or on distribution by the mudarib, where as losses are charged to income on declaration by the mudarib.

Income on musharaka financing is recognised when the right to receive payment is established. Income related to accounts that are 90 days overdue is excluded from the consolidated statement of income.

2 ACCOUNTING POLICIES (continued)

2.2 Summary of significant accounting policies (continued)

r. Revenue recognition (continued)

Income from investments
Income from debt-type instruments at amortised cost (investment in Sukuk) is recognised on a time-apportioned basis using the effective profit method.

Dividend income from equity-type instruments at fair value through equity is recognised when the right to receive is established. This is usually the ex-dividend date for equity securities.

Income from investment banking services
Income from investment banking services is recognised when the service is provided and income is earned. This is usually when the Group has performed all significant acts in relations to the service being rendered and it is highly probable that the economic benefits from the transaction will flow to the Group.

Other income
Other income on investments is recognised when the right to receive payment is established.

s. Employee's end of service benefits
Provision is made for leaving indemnity payable under the Bahraini Labour Law applicable to non-Bahraini employees' accumulated periods of service at the financial position date. Moreover provision for indemnity payable is also made for Bahraini employees.

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.

The Group provides end of service benefits to its expatriate employees. Entitlement to these benefits is based upon the employees final salary and length of service, subject to completion of a minimum service period. The expected costs of these benefits are accrued over the period of employment.

t. Provisions
A provision is recognised in the consolidated statement of financial position when the Group has a legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation.

u. Dividends
Dividends to shareholders are recognised as a liability when it is approved by the shareholders.

v. Off balance sheet equity of investment account holders
This represents funds received by the Group 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 and are not included in the consolidated statement of financial position since the Group does not have the right to use or dispose these assets.

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

x. Fiduciary assets
The Group provides fiduciary services that result in holding or investing of assets on behalf of its employees. Assets held in a fiduciary capacity are not reported in the consolidated financial statements, as they are not the asset of the Group.

y. Social responsibility
The Group discharges its social responsibilities through donations to charitable causes and organization.

2 ACCOUNTING POLICIES (continued)

2.2 Summary of significant accounting policies (continued)

z. 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.

Classification of investments

Real estate investments acquired to earn rentals or for capital appreciation are classified as investment properties.

Management decides on acquisition of an investment whether it should be classified as an equity-type instrument at fair value through statement of income, an equity-type instrument at fair value through a equity or debt-type instrument at amortised cost.

Fair value of unquoted investments at fair value through equity

Where the fair value of the Group's investment portfolio cannot be derived from an organised market, they are determined using a variety of valuation techniques that include the use of mathematical models. The inputs to these models are derived from observable market data where possible, but where observable market data is not available, judgment by management is required to establish fair values. The judgments include consideration of comparable assets, discount rates and the assumptions used to forecast cash flows.

Fair value of investment in real estate

The fair value of investment in real estate is determined by independent real estate valuation experts. The determination of the fair value of such assets requires the use of judgment based on estimates by independent valuation experts that are based on local market conditions existing at the date of the statement of financial position.

Impairment

The Group treats investments classified as fair value through equity as impaired when there has been a significant or prolonged decline in the fair value below its cost or where other objective evidence of impairment exists. The determination of what is "significant" or "prolonged" requires considerable judgment. In making this judgment, the Group evaluates, among other factors, normal volatility in share price and duration and the extent to which the fair value of quoted equities is less than its cost and the future cash flows and the discount factors for unquoted equities.

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

2 ACCOUNTING POLICIES (continued)

2.2 Summary of significant accounting policies (continued)

aa. Derecognition
A financial asset (or, where applicable a part of a financial asset or part of a Group of similar financial assets) is derecognised when:

(i) the right to receive cash flows from the asset have expired;
(ii) 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
(iii) 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 asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

A financial liability is derecognised when the obligation specified in the contract is discharged, cancelled or expired.

bb. 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.

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

dd. Shari'a supervisory board
The Group's business activities are subject to the supervision of a Shari'a supervisory board consisting of three members appointed by the general assembly.

3 BUSSINESS COMBINATION

During the year, the shareholders of the Bank approved the merger of the Bank with Capivest and CMH where Capivest and CMH operations were amalgamated into the Bank's operations to form the Merged Entity in accordance with Article 312 (a) (1) of the Bahrain Commercial Companies Law.

The merger was approved by the CBB and the Ministry of Industry and Commerce on 13 September 2012 and 11 October 2012 respectively subject to a 90 days no objection period. On 31 December 2012, via letter no. EDBS/KH/337/2012, CBB approved the legal amalgamation of Capivest and CMH operations into the Bank in respect to which the assets of CMH and Capivest as of 31 December 2012 were takenover and liabilites of CMH and Capivest as of 31 December 2012 were assumed by the Bank along with the off-balance sheet equity of investment accountholders. As a consideration for the above amalgamation the Bank issued 162,000 thousand shares to the shareholders of Capivest and CMH for a shareholding of 23% and 31% respectively in the merged entity. This transaction is considered as acquisition of CMH and Capivest by the Bank and has been accounted for accordingly.

The following table sets out the net assets acquired and gain arising from the amalgamation:

	US$
Shares issued on amalgamation at fair value	**178,385,368**
Net identifiable assets at fair value	
Capivest	**84,250,410**
CMH	**94,167,482**
	178,417,892
Gain arising on amalgamation	**32,524**

3 BUSSINESS COMBINATION (continued)

Assets acquired and liabilities assumed

The fair value of the identifiable assets and liabilities of Capivest and CMH as at the merger date 31 December 2012 were as follows:

	Capivest US$	*CMH US$*	*Total US$*
Assets			
Cash and balances with banks	7,674,533	1,392,088	9,066,621
Due from financial institutions	5,650,499	6,264,000	11,914,499
Financing receivable	12,372,062	-	12,372,062
Musharaka financing	-	916,916	916,916
Receivable from ijara investors	14,800,849	-	14,800,849
Investment in securities	42,623,515	80,627,365	123,250,880
Investment in associate	1,602,878	-	1,602,878
Investment in real estate	17,193,261	5,405,837	22,599,098
Development properties	16,173,111	-	16,173,111
Non current asset held for sale	-	1,326,260	1,326,260
Fixed assets	28,098	-	28,098
Other assets	1,501,442	270,499	1,771,941
Total assets	119,620,248	96,202,965	215,823,213
Liabilities			
Due to financial institutions	25,008,985	-	25,008,985
Due to non financial institutions	435,408	-	435,408
Other liabilities	6,011,791	771,850	6,783,641
Total liabilities	31,456,184	771,850	32,228,034
Equity of investment accountholders	-	1,263,633	1,263,633
Non-controlling interest	3,913,654	-	3,913,654
Total identifiable net assets at fair value	84,250,410	94,167,482	178,417,892

If the acquisition had taken place at the beginning of the year, revenue contributed would have been US$ 5,500 thousand and the loss of the Group would have increased by US$ 28,913 thousand.

4 CASH AND BALANCES WITH BANKS

	2012 US$	*2011 US$*
Cash	**7,542**	2,723
Balances with banks	**12,979,455**	2,352,210
	12,986,997	2,354,933

5 DUE FROM FINANCIAL INSTITUTIONS

	2012 US$	*2011 US$*
Mudaraba investments	**27,445,106**	14,206,052
Wakala investments	**2,000,014**	-
Commodity murabaha	**5,640,268**	-
	35,085,388	14,206,052
Less: Deferred profits	**(2,000)**	-
	35,083,388	14,206,052

5 DUE FROM FINANCIAL INSTITUTIONS (continued)

Mudaraba investments include US$ 1,264 thousands representing investments on behalf of Equity of Investment Accountholders.

As at 31 December 2012, CMH had a wakala investment of US$ 2,000 thousand which was fully provided for and transferred to the Bank at its net book value being it's fair value. (note 3)

The original maturity of commodity murabahas receivables and mudaraba investments are as follows:

	2012	*2011*
	US$	*US$*
Original maturity of 90 days or less	**30,547,075**	14,206,052
Original maturity of more than 90 days	**4,536,313**	-
	35,083,388	14,206,052

6 FINANCING RECEIVABLE

	2012	*2011*
	US$	*US$*
Murabaha receivables	**14,044,503**	3,852,268
Less: Deferred profits	**(346,055)**	(579,810)
	13,698,448	3,272,458

As at 31 December 2012, Capivest had financing receivables of US$ 1,323 thousand which were fully provided for and transferred to the Bank at its net book value being it's fair value. (note 3)

There were no past due nor impaired financing receivables as of 31 December 2012 (2011: Nil).

7 MUSHARAKA FINANCING

	2012	*2011*
	US$	*US$*
Musharaka financing	**1,958,701**	965,834
Less: Provision for impairment (note 28)	**(55,981)**	(7,024)
	1,902,720	958,810

An amount of US$ 82 thousand of musharaka financing was impaired as of 31 December 2012 (2011: Nil).

8 RECEIVABLES FROM IJARA INVESTORS

Receivables from Ijara investors represent balances due from investors who participated in the Group's Ijara series products. The balance outstanding as of 31 December 2012 relates to amounts due from Ijara 9 investors of US$ 11,408 thousand and Ijara 6 investors of US$ 3,393 thousand which will be settled in accordance with the Ijara product structures. As of 31 December 2012, these receivables were neither past due nor impaired.

9 INVESTMENT IN IJARAH ASSETS

	2012 US$	*2011 US$*
Cost:		
At 1 January	**8,616,025**	8,616,025
At 31 December	**8,616,025**	8,616,025
Depreciation:		
At 1 January	**965,616**	570,803
Charge for the year	**784,868**	394,813
At 31 December	**1,750,484**	965,616
Less: Provision for impairment (note 28)	**(1,903,567)**	-
Net book value:		
As at 31 December	**4,961,974**	7,650,409

The amount of future Ijarah instalments receivable as of 31 December 2012 is US$ 1,638 thousand (2011: US$ 1,940 thousand).

10 IJARA MUNTAHIA BITTAMLEEK

	2012 US$	*2011 US$*
Equipment		
Cost:		
At 1 January	**-**	-
Addition for the year	**2,500,000**	-
At 31 December	**2,500,000**	-
Depreciation:		
At 1 January	**-**	-
Charge for the year	**594,178**	-
At 31 December	**594,178**	-
Net book value:		
As at 31 December	**1,905,822**	-

11 INVESTMENT IN SECURITIES

At 31 December 2012	*Amortised Cost US$*	*Fair value through equity US$*	*Fair value through statement of income US$*	*Total US$*
Debt type				
Quoted sukuk	**72,752,595**	**-**	**-**	**72,752,595**
Equity type				
Quoted shares	**-**	**13,665,212**	**-**	**13,665,212**
Unquoted shares	**-**	**128,645,865**	**20,347,737**	**148,993,602**
Less: Impairment (note 28)	**(371,342)**	**(2,972,807)**	**-**	**(3,344,149)**
	72,381,253	**139,338,270**	**20,347,737**	**232,067,260**

11 INVESTMENT IN SECURITIES (continued)

At 31 December 2011	*Amortised Cost US$*	*Fair value through equity US$*	*Fair value through statement of income US$*	*Total US$*
Debt type				
Quoted sukuk	58,720,579	-	-	58,720,579
Unquoted sukuk	16,791,279	-	-	16,791,279
Equity type				
Quoted shares	-	4,411,988	-	4,411,988
Unquoted shares	-	30,954,402	-	30,954,402
Less: Impairment (note 28)	-	(920,967)	-	(920,967)
	75,511,858	34,445,423	-	109,957,281

12 INVESTMENT IN ASSOCIATES

	2012 US$	*2011 US$*
At 1 January	**3,444,085**	3,444,085
Additions by amalgamation (note 3)	**1,602,878**	-
	5,046,963	3,444,085

Investment in associates comprise the following:

Name	***Country of incorporation***	***% holding***
Ali Iskandar Al Ansari and Partners W.L.L. *	State of Qatar	35%
Aqari Real Estate Company B.S.C. (c)	Kingdom of Bahrain	31.88%
Alpha Lease and Finance Holding Company B.S.C. (c) **	Kingdom of Bahrain	30%
Apex Real Estate Company B.S.C.(c) *	Kingdom of Bahrain	30%

* These associates are fully provided for and the financial information below does not include their financial information.
** The financial information below includes the information based on 30 September 2012 unaudited management accounts for this associate.

Summarised financial information of associates:

	2012 US$	*2011 US$*
Total assets	**44,759,183**	21,160,250
Total liabilities	**14,506,911**	3,053,690

13 INVESTMENT IN REAL ESTATE

	2012 US$	*2011 US$*
At 1 January	**15,842,773**	19,803,466
Addition by amalgamation (note 3)	**22,599,098**	-
Less: Provision for impairment (note 28)	-	(3,960,693)
	38,441,871	15,842,773

14 DEVELOPMENT PROPERTIES

	2012 US$	*2011 US$*
Land	**5,943,959**	-
Development Cost	**10,229,152**	-
	16,173,111	-

15 NON-CURRENT ASSETS HELD FOR SALE

	2012 US$	*2011 US$*
Suffun Bahrain W.L.L.	**1,326,260**	-
	1,326,260	-

The Bank's total commitment under Suffun Bahrain W.L.L. ("Suffun") is US$ 11,406 thousand is included under uncalled capital commitments (note 33). Suffun continues to be designated as held for sale as the Bank is actively seeking to sell a majority stake in this investment to the investors.

16 FIXED ASSETS

	Lease hold improvements US$	***Computer hardware and software US$***	***Furniture and equipment US$***	***Vehicles US$***	***Total US$***
Cost:					
At 1 January 2011	1,115,707	1,588,653	236,119	150,716	3,091,195
Additions	302,941	295,321	-	-	598,262
At 31 December 2011	1,418,648	1,883,974	236,119	150,716	3,689,457
Additions	-	18,922	69,169	-	88,091
Additions by amalgamation (note 3)	-	28,098	-	-	28,098
Disposal	-	-	-	(83,872)	(83,872)
Less: Write off (note 27)	(1,115,707)	(1,789,597)	(236,119)	-	(3,141,423)
At 31 December 2012	**302,941**	**141,397**	**69,169**	**66,844**	**580,351**
Depreciation and amortisation:					
At 1 January 2011	230,772	910,474	129,260	136,979	1,407,485
Charge for the year	111,571	543,497	46,981	13,737	715,786
At 31 December 2011	342,343	1,453,971	176,241	150,716	2,123,271
Charge for the year	141,851	287,891	54,243	-	483,985
Disposal	-	-	-	(83,872)	(83,872)
Less: Write off (note 27)	(453,913)	(1,700,858)	(221,332)	-	(2,376,103)
At 31 December 2012	**30,281**	**41,004**	**9,152**	**66,844**	**147,281**
Net book balues:					
At 31 December 2012	**272,660**	**100,393**	**60,017**	**-**	**433,070**
At 31 December 2011	1,076,305	430,003	59,878	-	1,566,186

17 OTHER ASSETS

	2012 US$	2011 US$
Sales proceeds receivables	**1,302,935**	-
Prepaid expenses	**307,087**	190,866
Income receivable	**1,159,201**	1,315,168
Ijarah receivable	**630,133**	-
Staff receivable	**61,432**	11,514
Others	**477,778**	187,430
	3,938,566	1,704,978

18 DUE TO FINANCIAL INSTITUTIONS

	2012 US$	2011 US$
Murabaha payable	**21,355,038**	-
Wakala payable	**17,681,885**	4,543,500
	39,036,923	4,543,500

19 DUE TO NON FINANCIAL INSTITUTIONS

These mainly represent funds received from investors to be invested in entities to be set up or promoted by the Group.

20 OTHER LIABILITIES

	2012 US$	2011 US$
Acquisition payables	**8,017,873**	-
Provision for employee benefits	**1,609,222**	789,121
Due to Ijara investors	**1,073,424**	-
Directors' fee accrual	**520,823**	538,482
Accounts payables	**442,595**	121,991
Bonus accruals	**268,786**	-
Others	**3,709,160**	196,472
	15,641,883	1,646,066

21 EQUITY OF INVESTMENT ACCOUNT HOLDERS

Equity of investment account holders are funds of investees held by the Bank which it can invest as it deems appropriate without restriction as to where, how and for what purpose the funds are invested. These accounts are payable on demand and the account holder has the right to withdraw or transfer funds without penalty.

The Bank provides these accounts as an added service to investees who have idle cash and does not market these accounts as a product. Therefore, it is not the practice of the Bank to guarantee the preservation of capital or competitive rate of return through the creation of profit equalization reserves or investment risk reserves. As a result, the Bank has minimal displaced commercial risk.

These funds are invested in short term interbank placements with reputed financial institutions, thus making allowance for short-term liquidity requirements as well as reducing risk for the investment account holders. The funds are invested and managed in accordance with Shari'ah principles.

Profit paid to the investment account holders is based on the profit earned by the profit bearing assets.

22 OWNERS' EQUITY

(i) Share capital	***2012*** ***US$***	*2011* *US$*
Authorized:		
500,000,000 (2011: 500,000,000) ordinary shares at US$ 1 per share	**500,000,000**	500,000,000
Issued, subscribed and paid up capital:		
At beginning of year:		
200,000,000 (2011: 200,000,000) shares at US$ 1 per share	**200,000,000**	200,000,000
Reduction of share capital 62,000,000 shares (2011:nil)	**(62,000,000)**	-
Issued during the period :		
162,000,000 (2011:nil) ordinary shares of US$ 1 each	**162,000,000**	-
Issued and paid up share capital at end of the year:		
300,000,000 (2011: 200,000,000) ordinary shares of US$ 1 each	**300,000,000**	200,000,000

Following resolutions passed by the shareholders of the Bank at the Extraordinary General Meeting (EGM) held during the year and in compliance with the guidance of Ministry of Industry and Commerce:

22.a Reduced the issued and paid up share capital from US$ 200,000 thousand to US$ 138,000 thousand by offsetting accumulated losses of US$ 45,012 thousand that resulted in a general reserve of US$ 16,988 thousand. Further, current year losses of US$ 12,370 thousand were offset against the general reseve which is subject to necessary regulatory approvals and will be submitted for formal approval at the Annual General Meeting. This resulted in a general reserve of US$ 4,618 thousand as of 31 December 2012.

22.b Issued additional 162,000 thousand ordinary shares amounting to US$ 162,000 thousand at a value of US$ 1 per share including a premium of 0.1011 per share (US$ 16,385 thousand).

Additional information on shareholding pattern

(a) Names and nationalities of the major shareholders and the number of shares in which they have an interest of 5% or more of outstanding shares as of 31 December:

		2012	
	Country of incorporation	***% of holding***	***Share capital***
Aref Investment Group	Kuwait	**28.52%**	**85,560,000**
Kuwait Investment Company	Kuwait	**7.69%**	**23,072,427**
Gulf Investment House	Kuwait	**5.79%**	**17,357,403**

		2011	
	Country of incorporation	*% of holding*	*Share capital*
Aref Investment Group	Kuwait	62.00%	124,000,000
Kuwait Investment Company	Kuwait	11.86%	23,720,000
Sokouk Holding Company	Kuwait	10.64%	21,280,000
Qatar Islamic Bank	Qatar	10.00%	20,000,000
Islamic Corporation for the Development of the Private Sector	Saudi Arabia	5.00%	10,000,000

22 OWNERS' EQUITY (continued)

(b) Distribution schedule of equity shares, setting out the number of holders and percentage in the following categories as of 31 December:

Categories	**2012** Number of shares	Number of shareholders	% of total outstanding shares
Less than 5%	174,010,170	133	58.00%
5% up to less than 10%	40,429,830	2	13.48%
20% up to less than 50%	85,560,000	1	28.52%
	300,000,000	**136**	**100.00%**

Categories	*2011* Number of shares	Number of shareholders	% of total outstanding shares
Less than 5%	1,000,000	1	0.50%
5% up to less than 10%	10,000,000	1	5.00%
10% up to less than 20%	65,000,000	3	32.50%
More than 50%	124,000,000	1	62.00%
	200,000,000	6	100.00%

(ii) 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 and following the approval of CBB. (note:22.b)

(iii) Reserves

Statutory reserve

In accordance with the Bahrain Commercial Companies Law and the Bank's articles of association, 10% of the net profit for the year is transferred to the statutory reserve until such time as the reserve reaches 50% of the Bank's paid-up share capital. The reserve is not distributable except in such circumstances as stipulated in the Bahrain Commercial Companies Law and following the approval of the CBB. No transfer has been made for the current year as the Bank incurred losses of US$ 12,370 thousand (2011: US$ 4,170 thousand).

Investments fair value reserve

This represents cumulative unrealized fair value changes on investments and the net foreign exchange gain (loss) arising from translating the investments carried at fair value other than the investments carried at fair value through profit and loss. This reserve is transferred to the consolidated statement of income upon sale or impairment of the investments.

General reserve

This represents the reserve arising on the reduction of the Bank's share capital from US$ 2,000 thousand to US$ 138,000 thousand. (note:22.a)

23 PROFIT FROM ISLAMIC FINANCING

	2012* *US$	*2011* *US$*
Income from mudaraba financing	**520,740**	440,787
Income from musharaka financing	**84,657**	8,156
Income from murabaha receivables	**387,391**	919,796
Income from ijarah asset	**1,580,195**	1,412,835
Wakala income	**2,217**	-
	2,575,200	2,781,574

24 INCOME FROM INVESTMENT IN SECURITIES

	2012 *US$*	*2011* *US$*
Profit earned on debt-type instruments at amortised cost	**5,493,534**	5,956,514
Dividends on equity-type instruments at fair value through equity	**128,152**	170,238
Gain on disposal of debt-type instruments at amortised cost	**2,522,533**	852,707
Gain on disposal of investments at fair value through equity	**1,119,611**	-
	9,263,830	6,979,459

25 STAFF COST

	2012 *US$*	*2011* *US$*
Salaries and benefits	**3,302,159**	3,944,154
Social insurance expenses	**114,928**	165,342
Other staff expenses	**862,989**	1,020,704
	4,280,076	5,130,200

26 DEPRECIATION AND AMORTISATION

	2012 *US$*	*2011* *US$*
Depreciation and amortisation - fixed assets (note 16)	**483,985**	715,786
Depreciation - investment in ijarah asset (note 9)	**784,868**	394,813
	1,268,853	1,110,599

27 OTHER EXPENSES

	2012 *US$*	*2011* *US$*
Professional expenses	**411,091**	221,215
Travel and accommodation	**152,076**	371,544
Premises Cost	**751,997**	691,267
Fixed assets write off (note 16)	**765,320**	-
Directors remuneration	**343,785**	451,668
Board of directors sitting fee and expenses	**180,764**	155,098
Other administrative expenses	**972,173**	938,558
	3,577,206	2,829,350

28 PROVISION FOR IMPAIRMENT

(a) The following table shows the movement of provision for impairment during the year ended 31 December:

	Musharaka financing US$	***Investment* in ijarah assets US$**	**2012 Total US$**	*Musharaka financing US$*	*Investment in ijarah assets US$*	*2011 Total US$*
Provision at beginning of the year	7,024	-	7,024	-	-	-
Charged during the year	49,577	1,903,567	1,953,144	7,024	-	7,024
Foreign exchange translation	(620)	-	-	-	-	-
Provision at end of the year	**55,981**	**1,903,567**	**1,960,168**	7,024	-	7,024
Notes	**7**	**9**		7	9	

(b) The following table shows the provision and impairment charge during the year ended 31 December:

	2012 US$	*2011 US$*
Musharaka financing	**49,577**	7,024
Investment in ijarah asset	**1,903,567**	-
Investment in real estate (note 13)	-	3,960,693
Investments in securities		
Impairment (note 11)	**3,344,149**	920,967
Transfer from investment fair value reserve	**1,324,502**	-
	6,621,795	4,888,684

29 ACQUISITION EXPENSES

	2012 US$	*2011 US$*
Merger expenses	**5,615,611**	-
Redundancy expenses*	**2,900,000**	-
	8,515,611	-

* During the year, the shareholders of the Bank approved the merger of the Bank with Capivest and CMH, where the Board of Directors of the Bank has decided to reduce the workforce of the Group, in relation to which an amount of US$ 2,900 thousand was provided at the year end.

30 SEGMENT INFORMATION

a) Geographic sector

The geographical distribution of the Group's assets and liabilities is as follows:

2012	***Middle East US$***	***Europe US$***	***Africa US$***	***South East Asia US$***	***Total US$***
Assets					
Cash and balances with banks	8,770,393	4,182,524	-	34,080	12,986,997
Due from financial institutions	35,083,388	-	-	-	35,083,388
Financing receivable	12,372,062	1,326,386	-	-	13,698,448
Musharaka financing	916,916	-	-	985,804	1,902,720
Receivable from Ijarah investors	14,800,849	-	-	-	14,800,849
Investment in ijarah asset	-	-	-	4,961,974	4,961,974
Ijarah muntahia bittamleek	-	-	-	1,905,822	1,905,822
Investments in securities	180,471,731	34,870,121	16,725,408	-	232,067,260
Investment in associates	5,046,963	-	-	-	5,046,963
Investment in real estate	38,441,871	-	-	-	38,441,871
Development properties	16,173,111	-	-	-	16,173,111
Non-current asset held for sale	1,326,260	-	-	-	1,326,260
Fixed assets	433,070	-	-	-	433,070
Other assets	2,958,842	45,515	133,808	800,401	3,938,566
Total assets	**316,795,456**	**40,424,546**	**16,859,216**	**8,688,081**	**382,767,299**
Liabilities					
Due to financial institutions	25,008,985	-	-	14,027,938	39,036,923
Due to non financial institutions	435,408	-	-	-	435,408
Other liabilities	15,579,539	-	62,344	-	15,641,883
Total liabilities	**41,023,932**	**-**	**62,344**	**14,027,938**	**55,114,214**
Equity of investment accountholders	**125,836**	**-**	**1,137,797**	**-**	**1,263,633**

2011	*Middle East US$*	*Europe US$*	*Africa US$*	*South East Asia US$*	*Total US$*
Assets					
Cash and balances with banks	2,354,933	-	-	-	2,354,933
Due from financial institutions	14,206,052	-	-	-	14,206,052
Financing receivable		3,272,458			3,272,458
Musharaka financing	-	-	-	958,810	958,810
Investment in ijarah asset	-	-	-	7,650,409	7,650,409
Investments in securities	67,057,576	22,762,166	20,137,539	-	109,957,281
Investment in associates	3,444,085	-	-	-	3,444,085
Investment in real estate	15,842,773	-	-	-	15,842,773
Fixed assets	1,566,186	-	-	-	1,566,186
Other assets	1,704,978	-	-	-	1,704,978
Total assets	106,176,583	26,034,624	20,137,539	8,609,219	160,957,965
Liabilities					
Due to financial institutions	-	-	-	4,543,500	4,543,500
Other liabilities	1,646,066	-	-	-	1,646,066
Total liabilities	1,646,066	-	-	4,543,500	6,189,566

30 SEGMENTAL ANALYSIS (continued)

b) Industry sector

The industrial distribution of the Group's assets and liabilities is as follows:

2012	*Trading and manufacturing US$*	*Banks and financial institutions US$*	*Real Estate US$*	*Others US$*	*Total US$*
Assets					
Cash and balances with banks	-	12,986,997	-	-	12,986,997
Due from financial institutions	-	35,083,388	-	-	35,083,388
Financing receivable	-	-	1,326,386	12,372,062	13,698,448
Musharaka financing	-	985,804	-	916,916	1,902,720
Receivable from Ijarah investors	-	-	-	14,800,849	14,800,849
Investment in ijarah asset	-	-	-	4,961,974	4,961,974
Ijarah muntahia bittamleek	-	-	-	1,905,822	1,905,822
Investments in securities	15,695,096	82,000,945	91,654,476	42,716,743	232,067,260
Investment in associates	-	3,444,085	1,602,878	-	5,046,963
Investment in real estate	-	-	38,441,871	-	38,441,871
Development properties	-	-	16,173,111	-	16,173,111
Non-current asset held for sale	-	-	-	1,326,260	1,326,260
Fixed assets	-	-	-	433,070	433,070
Other assets	12,819	421,706	689,210	2,814,831	3,938,566
Total assets	**15,707,915**	**134,922,925**	**149,887,932**	**82,248,527**	**382,767,299**
Liabilities					
Due to financial institutions	-	39,036,923	-	-	39,036,923
Due to non financial institutions	268,679	-	-	166,729	435,408
Other liabilities	247,834	163,192	300,275	14,930,582	15,641,883
Total liabilities	**516,513**	**39,200,115**	**300,275**	**15,097,311**	**55,114,214**
Equity of investment accountholders	**1,137,797**	**-**	**-**	**125,836**	**1,263,633**

2011	*Trading and manufacturing US$*	*Banks and financial institutions US$*	*Real Estate US$*	*Others US$*	*Total US$*
Assets					
Cash and balances with banks	-	2,354,933	-	-	2,354,933
Due from financial institutions	-	14,206,052	-	-	14,206,052
Murabaha receivable			3,272,458		3,272,458
Musharaka financing	-	958,810	-	-	958,810
Investment in ijarah asset	-	-	-	7,650,409	7,650,409
Investments in securities	16,791,279	45,788,251	31,911,805	15,465,946	109,957,281
Investment in associates	-	3,444,085	-	-	3,444,085
Investment in real estate	-	-	15,842,773	-	15,842,773
Fixed assets	-	-	-	1,566,186	1,566,186
Other assets	-	-	-	1,704,978	1,704,978
Total assets	16,791,279	66,752,131	51,027,036	26,387,519	160,957,965
Liabilities					
Due to financial institutions	-	4,543,500	-	-	4,543,500
Other liabilities	-	-	-	1,646,066	1,646,066
Total liabilities	-	4,543,500	-	1,646,066	6,189,566

The Group's revenue and expenses are reviewed at a Group level and therefore no separate operating segment results and other disclosures are provided in these consolidated financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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31 RELATED PARTY BALANCES AND TRANSACTIONS

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence or joint control over the other party in making financial and operating decisions. Related parties comprise major shareholders, directors, shari'a supervisory board and executive management of the Group and/or entities over which they excercise control and/or significant influence.

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

	Associated companies US$	***Directors/ key management personnel Shari'a board members US$***	***Major shareholders / entities in which directors are interested US$***	***2012 US$***	*Associated companies US$*	*Directors/ key management personnel Shari'a board members US$*	*Major shareholders / entities in which directors are interested US$*	*2011 US$*
Assets								
Cash and balances with banks	-	-	5,911,922	5,911,922	-	-	1,990	1,990
Due from financial institutions	-	-	5,650,499	5,650,499	-	-	-	-
Investments in securities	-	25,723,626	12,286,966	38,010,592	-	-	9,500,000	9,500,000
Investment in associates	5,046,963	-	-	5,046,963	3,444,085	-	-	3,444,085
Other assets	-	78,818	1,061	79,879	-	-	-	-
	5,046,963	25,802,444	23,850,448	54,699,855	3,444,085	-	9,501,990	12,946,075
Liabilities								
Due to financial institutions	-	-	13,242,584	13,242,584	-	-	-	-
Due to non financial institutions	-	-	250,004	250,004	-	-	-	-
Other liabilities	79,576	2,166,890	5,336,519	7,582,985	-	700,648	-	700,648
	79,576	2,166,890	18,829,107	21,075,573	-	700,648	-	700,648
Equity of investment accountholders	-	1,137,797	-	1,137,797	-	-	-	-
Commitments	-	11,405,836	-	11,405,836	-	-	-	-

31 RELATED PARTY BALANCES AND TRANSACTIONS (continued)

	Associated companies US$	***Directors/ key management personnel Shari'a board members US$***	***Major shareholders / entities in which directors are interested US$***	***2012 US$***	*Associated companies US$*	*Directors/ key management personnel Shari'a board members US$*	*Major shareholders / entities in which directors are interested US$*	*2011 US$*
Income								
Income from investment in securities	-	-	382,591	382,591	-	-	226,152	226,152
Expenses								
Staff cost	-	2,446,452	-	2,446,452	-	3,382,758	-	3,382,758
Other expenses	-	670,198	-	670,198	-	579,394	-	579,394
Acquisition expenses	-	-	5,615,611	5,615,611				

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

	2012 US$	*2011 US$*
Short term employee benefits	**2,080,153**	2,990,969
Long term employee benefits	**366,299**	391,789

Director's remuneration, sitting fee and expenses for the year ended 31 December 2012 amounted to US$ 525 thousand (2011: US$ 607 thousand).

32 SHARI'A SUPERVISORY BOARD

The Bank's Shari'a Supervisory Board consists of three Islamic scholars who review the Bank's compliance with general Shari'a principles and specific fatwas, rulings and guidelines issued. Their review includes examination of evidence relating to the documentation and procedures adopted by the Bank to ensure that its activities are conducted in accordance with Islamic Shari'a principles.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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33 MATURITY PROFILE

The maturity profile of the Group's assets and liabilities are based on contractual repayment arrangements. The contractual maturities of assets and liabilities have been determined on the basis of the remaining period at the financial position date to the contractual maturity date. The consolidated maturity profile at 31 December 2012 was as follows:

2012	*Up to 3 month US$*	*3 months to 1 year US$*	*1 to 5 years US$*	*5 to 10 years US$*	*No fixed maturity US$*	*Total US$*
Assets						
Cash and balances with banks	12,986,997	-	-	-	-	12,986,997
Due from financial institutions	30,547,075	4,536,313	-	-	-	35,083,388
Financing receivable	1,326,386	12,372,062	-	-	-	13,698,448
Musharaka financing	776,521	770,395	355,804	-	-	1,902,720
Receivable from Ijarah investors	-	11,407,546	-	-	3,393,303	14,800,849
Investment in ijarah asset	4,961,974	-	-	-	-	4,961,974
Ijarah muntahia bittamleek	-	30,822	1,875,000	-	-	1,905,822
Investments in securities	9,788,909	-	33,840,582	28,751,762	159,686,007	232,067,260
Investment in associates	-	-	-	-	5,046,963	5,046,963
Investment in real estate	-	-	-	-	38,441,871	38,441,871
Development properties	-	-	-	-	16,173,111	16,173,111
Non-current asset held for sale	-	1,326,260	-	-	-	1,326,260
Fixed assets	-	-	-	-	433,070	433,070
Other assets	1,968,864	1,054,610	355,729	-	559,363	3,938,566
Total assets	62,356,726	31,498,008	36,427,115	28,751,762	223,733,688	382,767,299
Liabilities						
Due to financial institutions	14,529,316	8,082,867	16,424,740	-	-	39,036,923
Due to non financial institutions	-	-	435,408	-	-	435,408
Other liabilities	11,058,014	1,838,591	1,920,580	86,934	737,764	15,641,883
Total liabilities	25,587,330	9,921,458	18,780,728	86,934	737,764	55,114,214
Equity of investment accountholders	1,263,634	-	-	-	-	1,263,634
Total liabilities and equity of investment accountholders	**26,850,964**	**9,921,458**	**18,780,728**	**86,934**	**737,764**	**56,377,848**
Net liquidity gap	**35,505,762**	**21,576,550**	**17,646,387**	**28,664,828**	**222,995,924**	**326,389,451**
Cumulative net liquidity gap	**35,505,762**	**57,082,312**	**74,728,699**	**103,393,527**	**326,389,451**	
Commitments	**6,344,051**	**7,876,023**	**57,388**	-	-	**14,277,462**

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33 MATURITY PROFILE (continued)

The consolidated maturity profile at 31 December 2011 was as follows:

2011	*Up to 3 month* US$	*3 months to 1 year* US$	*1 to 5 years* US$	*5 to 10 years* US$	*No fixed maturity* US$	*Restated Total* US$
Assets						
Cash and balances with banks	2,354,933	-	-	-	-	2,354,933
Due from financial institutions	14,206,052	-	-			14,206,052
Financing receivable	440,000	1,980,000	852,458			3,272,458
Musharaka financing	-	-	461,612	-	497,198	958,810
Investment in ijarah asset	280,628	1,132,204	6,237,577	-	-	7,650,409
Investments in securities	3,250,000	20,089,247	40,974,446	11,198,165	34,445,423	109,957,281
Investment in associates	-	-	-	-	3,444,085	3,444,085
Investment in real estate	-	-	-	-	15,842,773	15,842,773
Fixed assets	-	-	-	-	1,566,186	1,566,186
Other assets	-	1,588,575	-	-	116,403	1,704,978
Total assets	20,531,613	24,790,026	48,526,093	11,198,165	55,912,068	160,957,965
Liabilities						
Wakala payable	4,543,500	-	-	-	-	4,543,500
Other liabilities	-	1,646,066	-	-	-	1,646,066
Total liabilities	4,543,500	1,646,066	-	-	-	6,189,566
Net liquidity gap	15,988,113	23,143,960	48,526,093	11,198,165	55,912,068	154,768,399
Cumulative net liquidity gap	15,988,113	39,132,073	87,658,166	98,856,331	154,768,399	
Commitments	3,012,567	97,666	156,239	-	-	3,266,472

The Group does not have assets and liabilities with contractual maturities beyond 10 years.

34 COMMITMENTS

	2012 *US$*	*2011* *US$*
Uncalled capital commitments in respect of investment	**13,505,836**	-
Promise to purchase foreign currency commitment	**484,140**	-
Commitment realted to project developments	**132,626**	-
Commitment to finance	**-**	2,500,000
Operating lease commitments - expiring within one year	**97,472**	610,233
Operating lease commitments - expiring in one to three years	**57,388**	156,239
	14,277,462	3,266,472

35 RISK MANAGEMENT

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

- credit risk;
- liquidity risk;
- market risks;
- profit rate in banking book; and
- operational risk

The Group has a risk management and governance framework which is intended to integrate risk management in its strategic thinking and business practices.

Furthermore, the Group has taken several initiatives to implement a comprehensive Basel II framework. These initiatives involve steps to identify all the risk areas that it manages and has particularly strengthened its risk management policies and procedures.

This note presents information about the Group's exposure to each of the above risks, its objectives, policies and processes for measuring and managing risk.

Risk Management and Governance Structure

Board of Directors
The Board of Directors of the Group has overall responsibility for establishing the Group's approach to risk and ensuring that an effective risk management framework is in place. The Board approves and periodically reviews the risk management policies and strategies of the Group. The Bank's Board of Directors' structure constitute of 7 members as of 31 December 2012, however, this has increased to 10 after the amalgamation and during the Ordinary General Meeting dated 29 January 2013.

Audit Committee
The mandate of the Audit Committee requires it to assist the Board in fulfilling its statutory and fiduciary responsibilities with respect to internal controls, accounting policies, auditing and financial reporting practices. The committee is responsible to assist the Board in its oversight of (i) the integrity and reporting of the Group's quarterly and annual consolidated financial statements, (ii) compliance with legal and regulatory requirements; and (iii) the independence and performance of the Group's internal and external auditors. The Committee also reviews the activities and performance of the internal audit function.

35 RISK MANAGEMENT (continued)

Risk Management and Governance Structure (continued)

Risk Committee
The Risk Committee ("RC") is a sub-committee of the Board of Directors and assists the Board in fulfilling its oversight responsibilities with regards to the development of risk management framework across all spectrums of business and operational activities conducted by the Group. The mandate of this committee is to develop and implement risk management strategies and policies. The committee is also responsible for the assessment of the efficiency of overall risk management function of the Group and the compliance with regulatory requirements relating to risk management. The committee also ensures the transparency and timeliness of internal and external disclosures on risk matters.

Shari'a Supervisory Board
The Group's compliance with Shari'a principles is overseen by an external and independent Shari'a Supervisory Board, fully supported by the Group's internal Shari'a and other departments. The Shari'a department is responsible for ensuring that there is an ongoing process of reviewing and auditing for Shari'a compliance in accordance with AAOIFI standards for existing and new investments. The Shari'a Board ensures that all investments undertaken by the lines of business are structured in such a manner that investments comply strictly with Shari'a principles.

Asset and Liability Committee
The Asset and Liability Committee ("ALCO") establishes policy and objectives for the asset and liability management of the Group's statement of financial position in terms of structure, distribution, risk and return and its impact on profitability. It also monitors the cash flows, tenor and cost/yield profiles of assets and liabilities and evaluates the Group's balance sheet both from profit rate sensitivity and liquidity points of view, makes corrective adjustments based upon perceived trends and market conditions, monitors liquidity and foreign exchange exposures and positions.

Investment, Credit & Risk Committee
The Investment Credit & Risk Committee ("ICRC") comprises the CEO and the Heads of Risk Management, Investment Banking, Treasury Capital Markets and Legal & Compliance. In addition to facilitating the credit and investment decisions, the ICRC's mission is to establish and maintain a risk management framework throughout the Group to best manage Bank's shareholders and client interests. Its mandate is to identify, assess and measure risks arising from the Group's activities, and to define the appropriate course of action to mitigate or manage them.

Risk Management Department
The Risk Management Department ("RMD") is responsible for implementing and maintaining risk related policies & procedures to ensure an independent control processes. It provides oversight compliance with risk principles, policies and limits across the Group. The department 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 department also ensures complete capture of the risks in risk measurement and reporting systems.

Internal Audit
Internal Audit is responsible for carrying out a risk-based program of work designed to provide assurance that assets are being safeguarded. This involves ensuring that controls are in place and working effectively in accordance with Group policies and procedures as well as with laws and regulations. The work carried out by Internal Audit includes providing assurance on the effectiveness of the risk management functions as well as that of controls operated by the business units. The Audit Committee approves the annual audit plan and also receives regular reports of the results of audit work.

35 RISK MANAGEMENT (continued)

Risk Management and Reporting Structure

The Group identifies, measures, controls and monitors its material risks on a periodic basis. The Group has established relevant risk limit structures to quantify its risk appetite. RC reviews and recommends the limits, suggested by the ICRC to the Board which is ultimately responsible for the final approval of the limit. The monitoring and controlling of risks is managed through limits set by the ICRC. These limits reflect the business strategy and market environment of the Group as well as the level of risk that the Group is willing to accept.

The Risk Management Department presents reports to the Board of Directors through ICRC and RC. These reports include risk and investment review of Group's portfolio and its impact on Group's capital adequacy.

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. A periodic briefing is given to the Chief Executive Officer and all other relevant members of the Group on the utilization of market limits, proprietary investments and liquidity, plus any other risk developments.

(a) Credit Risk

Credit risk is the risk that the Group will incur a loss because its customers, clients or counterparties failed to discharge their contractual obligations. Being a wholesale investment bank, the Group is involved in investment advisory services and investment transactions which comply with Islamic rules and principles according to the opinion of the Shari'a Board. Credit risk arises largely through short-term placements of excess cash through Mudaraba contracts in a conservative manner.

The Group 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. Counterparty limits are established with the use of a credit risk classification system, which assigns each counterparty a risk rating. Risk ratings are subject to revision at the time of renewal of the facility.

Investment risk is a major component of the Group's overall risk profile. The Group seeks to manage its investment risks through each stage of the investment process, including deal sourcing, acquisition, post investment monitoring.

The Board has delegated responsibility for the management of investment and credit risk to its ICRC. ICRC is the highest management-level authority on all investment exposures. The overall role of ICRC is to facilitate the investment business of the Group in the most effective and efficient manner within the risk guidelines specified by the Board or its designated RC. Prior to funding an investment, and regardless of its size, the ICRC provides an independent assessment of the opportunity, highlighting key risks prior to commitment.

Day-to-day management of the Group's investments is overseen by Investment Banking and Treasury Capital Markets Division. Additionally, the ALCO reviews all investments from the perspective of the Group's financial position.

The RMD regularly monitors the level of risk within the investment portfolio to ensure that appropriate level of economic capital is maintained. This process ensures that the required risk capital is below the available equity, which results in a positive equity cushion. The RMD ensures that Elaf maintains appropriate asset diversification by geography, industry and investment type.

35 RISK MANAGEMENT (continued)

(a) Credit Risk (continued)

Maximum exposure to credit risk
The table below shows the gross maximum exposure to credit risk for the components of the consolidated statement of financial position. The figures represent gross exposure net of any provision for impairment, without taking into account any collateral held and other credit mitigants.

	Maximum exposure	
	2012	*2011*
	US$	*US$*
Balances with banks	**12,979,455**	2,352,210
Due from financial institutions	**35,083,388**	14,206,052
Financing receivable	**13,698,448**	3,272,458
Musharaka financing	**1,902,720**	958,810
Receivable from Ijarah investors	**14,800,849**	-
Investments in securities	**72,381,253**	75,511,858
Other assets	**3,631,479**	1,514,112
	154,477,592	97,815,500

Concentration risk
Concentration of risk arises when a number of counterparties are engaged in similar economic 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 effected by changes in economic, political or other conditions. The Group seeks to manage the concentration of risk by establishing and constantly monitoring geographic and industry wise concentration. The Group seeks to manage its concentration risk by establishing geographic and industry wise concentration limits. The geographic and industry wise distribution of assets and liabilities are set out in note 30.

(b) Liquidity risk
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.

The main action to manage the Group's liquidity is through the adherence to limits on liquidity mismatches. These include the limits of the cumulative excess of maturing liabilities over assets in the short-term and limits on dependence on short-dated funds.

Treasury department is overall responsible for ensuring that the limits enacted are adhered to, on a day-to-day basis and managing excess liquidity of the Group through short term placements and investments. Treasury maintains a constant communication with the banks which have extended a committed short term financing line to the Group. The Treasury provides a monthly report to the ALCO regarding the dependability and reliability of these banks. Treasury also monitors the market conditions and generates watch reports which would monitor the spreads and the volatilities of the asset prices and as such the exogenous liquidity risk the Group is exposed to.

The asset and liability maturity profile shown in note 33 is based on management's assessment of the Group's right and ability to liquidate these instruments based on their underlying liquidity characteristics.

35 RISK MANAGEMENT (continued)

(c) Market Risk

Market risk is the risk that changes in market prices, such as profit rates, equity prices, foreign exchange rates and commodity prices will affect the Group's income or the value of its holdings of financial instruments. Market risk comprises equity position risk, profit rate risk, commodities risk, currency risk and other price risk.

The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk.

The Group does not have a trading portfolio and hence is not exposed to market risk in relation to such instruments. The Group is not exposed to commodities or price risk as there is no commodity holding either in the banking or trading book. Market risk for the Group arises only on account of its foreign exchange exposure in the banking book.

The Group manages its market risk exposures by evaluating each new product and activity with respect to the market risk introduced by it.

Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. Most of the transactions completed by the Group are in US Dollars. However, in the normal course of business certain non-trading monetary assets and liabilities are in other currencies and give rise to currency risk.

Positions are monitored regularly to ensure that they are maintained within established limits and guidelines. The Group is not exposed to any significant currency risk.

Equity price risk

Equity price risk is the risk that the fair value of equity investments decreases as a result of fluctuations in the respective stock market indices. The Bank has investments at fair value through equity quoted on stock exchanges. Based on the values at 31 December 2012, a change in the quoted price of plus or minus 5% would change the value of these investments by plus or minus US$ 683 thousand (2011: US$ 221 thousand) with a corresponding increase or decrease in equity, except in case of impairment which will result in loss being taken to consolidated statement of income.

The Bank also has unquoted investments carried at fair value using either net asset value or valuations from independent valuers. Based on the values at 31 December 2012, a change in the valuation of 5% would change the value of these investments by plus or minus US$ 6,284 thousand (2010: US$ 1,502 thousand) with a corresponding increase or decrease in equity, except in case of further decline on impaired investments which will result in loss being taken to consolidated statement of income.

Prepayment risk

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

35 RISK MANAGEMENT (continued)

(c) Market Risk (continued)

(d) Profit rate risk in banking book

Profit rate risk is the potential impact of the mismatch between the rate of return on assets and the expected rate of return of the sources of finance. The table below analyses the Group's profit rate risk exposure on non-trading financial assets and liabilities. The Group's assets and liabilities are included at carrying amount and categorised based on contractual repayment arrangements:

2012	***Up to 3 Month US$***	***3 months to 1 year US$***	***1 to 5 years US$***	***Above 5 Years US$***	***Total US$***
Assets					
Due from financial institutions	30,547,075	4,536,313	-	-	35,083,388
Financing receivable	1,326,386	12,372,062	-	-	13,698,448
Investments in securities	9,788,909	-	33,840,582	28,751,762	72,381,253
Total profit rate sensitive assets	41,662,370	16,908,375	33,840,582	28,751,762	121,163,089
Liabilities					
Due to financial institutions	14,529,316	8,082,867	16,424,740	-	39,036,923
Total profit rate sensitive liabilities	14,529,316	8,082,867	16,424,740	-	39,036,923
Profit rate sensitivity gap	**27,133,054**	**8,825,508**	**17,415,842**	**28,751,762**	**82,126,166**

2011	*Up to 3 Month US$*	*3 months to 1 year US$*	*1 to 5 years US$*	*Above 5 Years US$*	*Total US$*
Assets					
Due from financial institutions	14,206,052	-	-	-	14,206,052
Financing receivable	440,000	1,980,000	852,458		3,272,458
Investments in securities	3,250,000	20,089,247	40,974,446	11,198,165	75,511,858
Total profit rate sensitive assets	17,896,052	22,069,247	41,826,904	11,198,165	92,990,368
Liabilities					
Due to financial institutions	4,543,500	-	-	-	4,543,500
Total profit rate sensitive liabilities	4,543,500	-	-	-	4,543,500
Profit rate sensitivity gap	13,352,552	22,069,247	41,826,904	11,198,165	88,446,868

The sensitivity of the Group's consolidated statement of income to a 200 basis points parallel increase (decrease) in market profit rates (assuming no asymmetrical movement in yield curves and a constant statement of financial position) on floating rate non trading financial assets and liabilities, would be an increase (decrease) of profit by US$ 345 thousand (2011:US$ 655 thousand).

(e) Operational Risk

Operational risk is the risk of loss arising from inadequate or failed internal processes, people and systems or from external events, whether intentional, unintentional or natural. It is an inherent risk faced by all business and covers a large number of operational risk events including business interruption and systems failures, internal and external fraud, employment practices and workplace safety, customer and business practices, transaction execution and process management, and damage to physical assets.

The Group cannot expect to eliminate all operational risks, but through a control framework and by monitoring and responding to potential risks, the Group is able to manage the risks. Controls include effective segregation of duties, access, authorization and reconciliation procedures, staff education and assessment processes, including the use of internal audit.

35 RISK MANAGEMENT (continued)

(e) Operational Risk (continued)

Risk and Control Self Assessment ("RCSA") is an annual exercise as per Bank's policy and is a requirement by Central Bank of Bahrain based on Basel II principles related to operational risk management. During the year 2012 the Group decided to postpone the RCSA exercise to 2013 due to the merger process.

The Group has developed a Disaster Recovery and Business Continuity Plan ("DR&BCP") to enable the Group to survive a disaster and to reestablish normal business operations. The DR&BCP will enable the Group to minimize interruptions to business service operations, resume critical operations within a specified time after a disaster, minimize financial loss due to disruptions, limit the severity of the disruption, expedite the restoration of services and maintain a positive public image of the Bank.

36 FAIR VALUE OF FINANCIAL INSTRUMENTS

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

Level 1: quoted (unadjusted) prices in active markets for identical assets;
Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly; and

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

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

2012	***Level 1 US$***	***Level 2 US$***	***Level 3 US$***	***Total US$***
Quoted shares	**13,665,212**	**-**	**-**	**13,665,212**
Unquoted shares	**-**	**-**	**146,020,795**	**146,020,795**
	13,665,212	**-**	**146,020,795**	**159,686,007**

2011	*Level 1 US$*	*Level 2 US$*	*Level 3 US$*	*Total US$*
Quoted shares	4,411,988	-	-	4,411,988
Unquoted shares	-	-	30,033,435	30,033,435
	4,411,988	-	30,033,435	34,445,423

37 EARNINGS PROHIBITED BY SHARI'A

Earnings prohibited by Shari'a, if earned are set aside for charitable purposes or otherwise dealt with in accordance with directions of the Shari'a supervisory Board.

38 COMPARATIVES

Certain prior year amounts have been regrouped to conform to the current year's presentation. Such reclassification did not affect previously reported consolidated statement of income or consolidated owners' equity.