

## INVESTORS BANK B.S.C. (c)

### FINANCIAL STATEMENTS 31 DECEMBER 2007

|                         |   |   |
|-------------------------|---|---|
| Commercial registration | : | 39646 (registered with Central Bank of Bahrain as a wholesale Islamic investment bank).   |
| Registered Office       | : | Al Salam Building<br>Diplomatic Area<br>PO Box 11818<br>Manama,<br>Kingdom of Bahrain   |
| Directors               | : | Mr. Sami Al Bader, <i>Chairman</i><br>Mr. Abdul Mohsen Al Othman, <i>Vice Chairman</i> (until 10 June 2007)<br>Mr. Ghassan Fahad Al-Sultan<br>Mr. Bader Sulaiman Al Jarrallah (until 10 June 2007)<br>Mr. Ahmed Shabeeb Al Dhaheri<br>Sheikh Bander Bin Fahad Al Fehaid (until 10 June 2007)<br>Mr. Isa Abdulla Al-Mannai (from 10 June 2007)<br>Dr. Abdulaziz Al Bader (from 10 June 2007) |
| Auditors                | : | KPMG  |

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**Financial statements**

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**Chairman's Report  
for the year ended 31 December 2007  
all amounts are expressed in US Dollars unless otherwise stated**

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Praise be to Allah and peace and blessing be upon the Messenger

Dear shareholders,

On behalf of my colleagues, members of the Board of Directors I am pleased to present to you the annual report on the activities of the Bank for the financial year ended 31 December 2007.

The world economies witnessed a noticeable slow down during 2007, particularly, in the United States of America where the most severe financial turmoil is concentrated. There was a slow down in activity in countries from Western Europe also during the last quarter of 2007.

At the same time, the overall inflation increased across the globe constantly driven by the increase in food and energy prices. In advanced economies, basic inflation moved upwards during 2007 despite the slow down in growth. In the emerging markets, the rise in overall inflation was more acute under the strong effect of the rise in demand and increase in the weight of energy and food stuff in particular, in consumer goods baskets.

The boom in basic commodities markets continued despite the slow down in global activity. Strong demand from emerging economies, which constituted a major part of increase in the consumption of basic commodities during the recent years, was one of the driving forces for the increase in the prices of basic food products.

The real estate mortgage markets crisis appeared in August 2007 in the United States of American high risk sub-prime market and its effect unexpectedly extended to cause extensive damage to markets and vital institution in the international financial system.

The subsequent fallouts lead to the reduction in liquidity in the inter-bank dealing which substantially affected the capital adequacy of major international central banks. This led, also, to the demise and bankruptcy of several international banks. Fear of credit risk extended beyond the high risk real estate mortgage sector. Share prices dropped with the increase in indications of economic weakness. The level of volatility in the equity and currency market continued.

The turmoil which hit the markets has affected the foreign exchange markets also. The rate of exchange for the US Dollar was further reduced compared to the level reached in mid 2007 as a result of the reduction in investments in American bonds and shares which was due to the drop in the level of confidence in the liquidity of these securities and their return.

In comparison with the foregoing and generally economic performance in the Gulf region during last year was robust. This is due to the increase in oil prices which lead to the realization of the highest level of liquidity ever achieved. This enabled the GCC countries to realise financial returns estimated at USD 240 Billion.

Despite the fall in oil prices, noticed during the recent months, such fall in the prices did not have major adverse implications during 2007 on the oil sector as was expected, in comparison with the other economic sectors, known as the non-oil sectors.

Despite all these developments in the oil and non-oil sectors the region is inevitably expected to face pressure with regard to the inflation resulting from increase in the price of food, raw material and rentals. Accordingly, it is expected that the rate of inflation in the countries of the region will exceed 3%.

Generally, the reasons behind inflation are referred to international factors relating to the pegging of the Bahrain Dinar to the US Dollar since the main corresponding effect for the reduction in the value of the US Dollar is the increase in the value of the Euro, Yen and other currencies such as the Canadian Dollar and the currencies of certain emerging markets. Add to this, the effect of the increase in operational cost in oil exporting countries and the increase in the global international demand for oil. In addition also to regional and national factors represented by the growth of local and gross production and the enhancement of government expenditure.

**Chairman's Report  
for the year ended 31 December 2007****all amounts are expressed in US Dollars unless otherwise stated (continued)**

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In addition to the problem of the Bahrain Dinar being pegged to the US Dollar, there is also the problem relating to the fallouts of the increase in the value of crude oil in international markets generally. This in turn would mean increase in the value of operational costs, and accordingly, increase in the value of goods produced and exported by certain countries.

Bahrain economy witnessed a remarkable growth during 2006. This growth continued during 2007 where the rate of growth reached 13.1% based on current prices and 7.1% based on fixed prices. Despite the effect of oil prices on the rate of economic growth achieved by Bahrain, the non-oil sector has noticeably contributed to the realisation of high growth rates in previous years where statistics indicate that the rate of growth in this sector was 9% during the year 2007 compared to 8% in 2006.

Dear shareholders,

The strategic initiatives and distinguished steps taken by the Bank 2007 in the business side, the modernization of the infrastructure through the restructuring of certain positions and the improvement of the working environment through the appointment of new calibres, the use of specialised firms in the formulation of a clear working strategy for the Bank, opening of new communication channels with the countries of the region and the activation of the Bank role in its cooperation with the other companies of the Group, will have its clear effect on the results, which will be achieved, Inshallah, during the coming period.

The Bank has moved to its new headquarters in the Seef District in the building, named the "Seef Star". The Bank plans to own 50% of the total built area jointly with International Takaful Company during the coming period.

With respect to the financial position of the Bank for the financial year ended 31 December 2007, the Bank has booked losses amounting to USD 10,260,855 (Ten million two hundred sixty thousand and eight hundred fifty five US Dollars).

Dear shareholders,

We assure that the steps taken by the Bank in 2007 will have their fruits during the coming period, bearing in mind that the Bank has taken into consideration all recommendations proposed by the Central Bank of Bahrain. In spite of all this we do realise that the future challenges will be numerous but we, as members of the Board of Directors, are quite confident that we have the ability to face them, thanks to God's Grace, the work of the senior management and the new team which undertakes the leadership in the working arena, in addition to the continuous training of the Bank staff and the implementation of modern technology information in the Bank.

In conclusion, I wish to express our gratitude and appreciation to His Majesty King Hamed Bin Isa Al Khalifa, the King of Bahrain, to his highness Sheikh Khalifa Bin Salman Al Khalifa, the Prime Minister and His Highness Sheikh Salman Bin Hamed Al Khalifa, the Crown Prince and Commander-in-Chief of the Bahrain Defence Force, to Government of the Kingdom of Bahrain, the Minister of Industry and Commerce, the Central Bank of Bahrain, the Bahrain Stock Exchange for their vision, guidance and continuous support for the establishment of a distinguished Islamic Banking Centre in the Kingdom. Gratitude is also extended to the Shariah Supervisory Board for their support and valuable guidance, to our investors and to our members of staff: executives and employees who stand behind the success achieved.



Sami Al Bader  
Chairman

21 April 2008

**In the Name of Allah, The Beneficent, The Merciful**

**SHARI'A BOARD'S REPORT**

**To the Shareholders of Investors Bank**

Assalam Alaikum Wa Rahmat Allah Wa Baraketuh

In compliance with the letter of appointment, we are required to submit the following report: We have reviewed the principles and the contracts relating to the transactions and applications introduced by the Investors Bank during the period ended 31/12/2007.

We have also conducted our review to form an opinion as to whether Bank has complied with Shari'a Rules and principles and also with the specific fatwas, rulings and guidelines issued by us.

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

We conducted our review which included examining, on a test basis of each type of transaction, the relevant documentation and procedures adopted by the 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 the Bank has not violated Islamic Shari'a Rules and Principles.

**In our opinion:**

- (1) the contracts, transactions and dealings entered into by the Bank during the year ended 31/12/2007 that we have reviewed are in compliance with the Islamic Shari'a Rules and Principles;
- (2) the allocation of profit and charging of losses relating to investment accounts conform to the basis that had been approved by us in accordance with Islamic Shari'a Rules and Principles;
- (3) the calculation of Zakah is in compliance with Islamic Shari'a Rules and principles.

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

Wassalam Alaikum Wa Rahmat Allah Wa Barakatuh.

9<sup>th</sup> Rabia II, 1429 Hijri corresponding to 15<sup>th</sup> April 2008.

**SHARI'A BOARD**



Shaikh Dr. Abdul Sattar A. Karim Abu Ghuddah  
Chairman of the Board



Shaikh Dr. Ali Mohieddin Al Quradaghi  
Member



Shaikh Nedham Mohammed Saleh Yaqoobi  
Member

**KPMG Fakhro**  
**Audit**  
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**REPORT OF THE AUDITORS TO THE SHAREHOLDERS**  
**INVESTORS BANK B.S.C. (c)**

Manama, Kingdom of Bahrain

21 April 2008

We have audited the accompanying balance sheet of Investors Bank B.S.C. (c) ("the Bank") as at 31 December 2007 and the related statements of income, changes in equity, cash flows, changes in restricted investment accounts and sources and uses of charity fund for the year then ended.

**Respective responsibilities of directors and auditors**

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

**Basis of opinion**

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

**Opinion**

In our opinion, the financial statements give a true and fair view of the financial position of the Bank as at 31 December 2007, the results of its operations, the changes in its equity and its cash flows for the year then ended, in accordance with Sharia'a rules and principles as determined by the Sharia'a Supervisory Board of the Bank and Financial Accounting Standards issued by the Accounting and Auditing Organization for Islamic Institutions.




**BALANCE SHEET**  
**as at 31 December 2007**

US\$

|   | Note  | 2007               | 2006               |
|---|-------|--------------------|--------------------|
| <b>ASSETS</b>                                     |       |                    |                    |
| Cash and cash equivalents                         | 3     | 9,631,572          | 383,182            |
| Trading investments                               | 4,20  | 29,727,074         | 39,293,867         |
| Available-for-sale investments                    | 5,20  | 20,735,571         | 21,586,476         |
| Murabaha receivables                              | 20    | 3,243,848          | 4,925,048          |
| Receivable from Mudarib                           | 20    | 11,896,174         | -                  |
| Mudaraba investment                               | 20    | 4,500,000          | 21,931,034         |
| Receivables from sale of investments              | 20    | 29,860,901         | 30,268,197         |
| Deferred payment sale receivables                 | 20,25 | 3,680,203          | 3,680,203          |
| Investment property                               | 8     | 13,838,620         | 18,331,295         |
| Other assets                                      | 6     | 8,310,384          | 7,541,592          |
| Equipment   | 7     | 1,631,225          | 83,339             |
| <b>Total assets</b>                               |       | <b>137,055,572</b> | <b>148,024,233</b> |
| <b>LIABILITIES AND EQUITY</b>                     |       |                    |                    |
| <b>Liabilities</b>                                |       |                    |                    |
| Due to a financial institution                    | 25    | 3,670,202          | 3,670,202          |
| Due to related parties                            | 20    | 3,229,064          | 3,527,079          |
| Other liabilities                                 |       | 291,232            | 250,118            |
| <b>Total liabilities</b>                          |       | <b>7,190,498</b>   | <b>7,447,399</b>   |
| <b>Equity</b>                                     |       |                    |                    |
| Share capital                                     | 9     | 80,000,000         | 80,000,000         |
| Statutory reserve                                 |       | 7,409,515          | 7,409,515          |
| Available-for-sale investments fair value reserve |       | 10,263,817         | 10,714,722         |
| Retained earnings                                 |       | 32,191,742         | 42,452,597         |
| <b>Total equity (page 7)</b>                      |       | <b>129,865,074</b> | <b>140,576,834</b> |
| <b>Total liabilities and equity</b>               |       | <b>137,055,572</b> | <b>148,024,233</b> |
| <b>OFF-BALANCE SHEET ITEMS</b>                    |       |                    |                    |
| Restricted investment accounts (page 10)          |       | <b>16,708,037</b>  | <b>16,157,031</b>  |

The financial statements, which consist of pages 5 to 30, were approved by the Board of directors on 21 April 2008 and signed on its behalf by:



\_\_\_\_\_  
 Sami Al Bader  
 Chairman



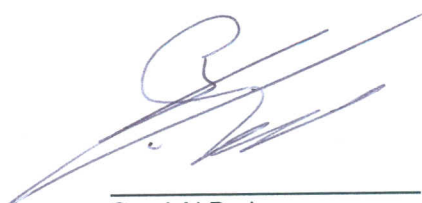
\_\_\_\_\_  
 Isa Abdulla Al-Mannai  
 Director

The accompanying notes 1 to 25 form an integral part of these financial statements.

**INCOME STATEMENT**  
**for the year ended 31 December 2007**

US\$

|   | Note  | 2007                | 2006              |
|---|-------|---------------------|-------------------|
| Income from trading investments                     | 10,20 | 771,937             | 8,044,351         |
| Income from available-for-sale investments          | 11,20 | 412,579             | 4,553,698         |
| Fair value losses on trading investments            | 4     | (9,566,793)         | (6,473,546)       |
| Fair value losses on available-for-sale investments |       | -                   | (20,409)          |
| Placement fee                                       | 20    | -                   | 2,000,000         |
| Underwriting fee                                    | 12,20 | -                   | 3,631,208         |
| Income from Mudaraba investment                     | 20    | 79,377              | 3,363,395         |
| Income from investment property, net                | 13    | 1,257,051           | -                 |
| Other income  |       | 2,028,155           | 343,557           |
| <b>Total net income</b>                             |       | <b>(5,017,694)</b>  | <b>15,442,254</b> |
| Staff cost  | 14    | 1,444,954           | 2,304,929         |
| Administrative and general expenses                 | 15    | 1,039,510           | 1,745,356         |
| Impairment allowance                                | 16    | 2,712,594           | -                 |
| Depreciation  |       | 46,103              | 53,681            |
| <b>Total expenses</b>                               |       | <b>5,243,161</b>    | <b>4,103,966</b>  |
| <b>(Loss) / profit for the year</b>                 |       | <b>(10,260,855)</b> | <b>11,338,288</b> |



Sami Al Bader  
Chairman



Isa Abdulla Al-Mannai  
Director

The accompanying notes 1 to 25 form an integral part of these financial statements.



**STATEMENT OF CHANGES IN EQUITY**  
for the year ended 31 December 2007

US\$

| 2007  | Share Capital     | Share premium | Statutory reserve | AFS Investments fair value reserve | General reserve | Retained earnings   | Total               |
|---|-------------------|---------------|-------------------|------------------------------------|-----------------|---------------------|---------------------|
| Balance at 1 January 2007                   | 80,000,000        | -             | 7,409,515         | 10,714,722                         | -               | 42,452,597          | 140,576,834         |
| Fair value losses during the year           | -                 | -             | -                 | (450,905)                          | -               | -                   | (450,905)           |
| Net loss recognised directly in equity      | -                 | -             | -                 | (450,905)                          | -               | -                   | (450,905)           |
| Net loss for the year                       | -                 | -             | -                 | -                                  | -               | (10,260,855)        | (10,260,855)        |
| <b>Total recognised income and expenses</b> | -                 | -             | -                 | <b>(450,905)</b>                   | -               | <b>(10,260,855)</b> | <b>(10,711,760)</b> |
| <b>At 31 December 2007</b>                  | <b>80,000,000</b> | -             | <b>7,409,515</b>  | <b>10,263,817</b>                  | -               | <b>32,191,742</b>   | <b>129,865,074</b>  |

The accompanying notes 1 to 25 form an integral part of these financial statements.

**STATEMENT OF CHANGES IN EQUITY**  
for the year ended 31 December 2007

US\$

| 2006  | Share Capital | Share premium | Statutory reserve | AFS Investments fair value reserve | General reserve | Retained earnings | Total       |
|---|---------------|---------------|-------------------|------------------------------------|-----------------|-------------------|-------------|
| Balance at 1 January 2006                                   | 50,000,000    | 13,746,334    | 6,275,686         | 11,813,378                         | 479,382         | 48,712,422        | 131,027,202 |
| Fair value gains during the year                            | -             | -             | -                 | 3,116,399                          | -               | -                 | 3,116,399   |
| Transfer to income statement on disposal of AFS investments | -             | -             | -                 | (4,215,055)                        | -               | -                 | (4,215,055) |
| Net income recognised directly in equity                    | -             | -             | -                 | (1,098,656)                        | -               | -                 | (1,098,656) |
| Net profit for the year                                     | -             | -             | -                 | -                                  | -               | 11,338,288        | 11,338,288  |
| Total recognised income and expenses                        | -             | -             | -                 | (1,098,656)                        | -               | 11,338,288        | 10,239,632  |
| Issue of bonus shares                                       | 30,000,000    | (13,746,334)  | -                 | -                                  | (479,382)       | (15,774,284)      | -           |
| Charity contribution declared (for 2005)                    | -             | -             | -                 | -                                  | -               | (200,000)         | (200,000)   |
| Board remuneration declared (for 2005)                      | -             | -             | -                 | -                                  | -               | (490,000)         | (490,000)   |
| Transfer to statutory reserve                               | -             | -             | 1,133,829         | -                                  | -               | (1,133,829)       | -           |
| At 31 December 2006   | 80,000,000    | -             | 7,409,515         | 10,714,722                         | -               | 42,452,597        | 140,576,834 |

The accompanying notes 1 to 25 form an integral part of these financial statements.

**STATEMENT OF CASH FLOWS**  
**for the year ended 31 December 2007**

US\$

|  | 2007               | 2006               |
|--|--------------------|--------------------|
| <b>OPERATING ACTIVITIES</b>                                  |                    |                    |
| Management and advisory fees received                        | -                  | 1,759              |
| Dividends received   | -                  | 270,592            |
| Placement fees received                                      | 2,000,000          | -                  |
| Underwriting fees received                                   | 3,631,836          | -                  |
| Advances for purchase of available-for-sale investments      | -                  | (1,167,134)        |
| Income from Murabaha contracts received                      | 129,130            | 26,926             |
| Purchase of available-for-sale investments                   | -                  | (33,491)           |
| Proceeds from sale of available-for-sale investments         | 2,006,527          | 57,842             |
| Proceeds from sale of trading investments                    | -                  | 9,861,671          |
| Arrangement fee paid on sale of trading investments          | -                  | (406,667)          |
| Receipts from deferred payment sale                          | -                  | 500,000            |
| Payments for operating expenses                              | (2,606,368)        | (2,771,659)        |
| Payments to the Managing Director (note 14)                  | -                  | (1,000,000)        |
| Board remuneration paid                                      | -                  | (490,000)          |
| Employee Qard Hasan and advances, net                        | 84,403             | (33,636)           |
| Others   | 21,028             | (50,857)           |
| <b>Cash flows from operating activities</b>                  | <b>5,266,556</b>   | <b>4,765,346</b>   |
| <b>INVESTING ACTIVITIES</b>                                  |                    |                    |
| Purchase of equipment  | (1,551,262)        | (4,780)            |
| Proceeds from disposal of equipment                          | -                  | 998                |
| <b>Cash flows from investing activities</b>                  | <b>(1,551,262)</b> | <b>(3,782)</b>     |
| <b>FINANCING ACTIVITIES</b>                                  |                    |                    |
| Mudaraba investment  | (4,500,000)        | -                  |
| Mudaraba investment income                                   | 79,377             | -                  |
| Murabaha financing   | -                  | (4,650,000)        |
| Receipt from Mudaraba investments                            | 10,034,860         | -                  |
| Cash paid to charitable organisations, net (page 12)         | (81,141)           | (85,026)           |
| <b>Cash flows from financing activities</b>                  | <b>5,533,096</b>   | <b>(4,735,026)</b> |
| <b>Net increase in cash and cash equivalents</b>             | <b>9,248,390</b>   | <b>26,538</b>      |
| Cash and cash equivalents at beginning of the year           | 383,182            | 356,644            |
| <b>Cash and cash equivalents at end of the year (note 3)</b> | <b>9,631,572</b>   | <b>383,182</b>     |

The accompanying notes 1 to 25 form an integral part of these financial statements.

**STATEMENT OF CHANGES IN RESTRICTED INVESTMENT ACCOUNTS**  
for the year ended 31 December 2007

US\$

| 2007  | Balance at 1 January 2007 |                                       | Movements during the year           |                      |                                      |                                    |   | Balance at 31 December 2007 |                                       |                   |
|---|---------------------------|---------------------------------------|-------------------------------------|----------------------|--------------------------------------|------------------------------------|---|-----------------------------|---------------------------------------|-------------------|
|   | No of units<br>(000)      | Average<br>value per<br>share<br>US\$ | Investment/<br>(withdrawal)<br>US\$ | Revaluations<br>US\$ | Investment<br>profit/ (loss)<br>US\$ | Bank's fees<br>as an agent<br>US\$ | Administra-<br>tion<br>expenses<br>US\$ | No of units<br>(000)        | Average<br>value per<br>share<br>US\$ | Total<br>US\$     |
| Murabaha with Lotus Air<br>Ltd  | -                         | -                                     | -                                   | -                    | -                                    | -                                  | -                                       | -                           | -                                     | 317,689           |
| Investments in International<br>Investment Group K.S.C.C.<br>(note 2 below) | 12,887                    | 0.44                                  | -                                   | -                    | -                                    | -                                  | -                                       | 12,887                      | 0.44                                  | 5,670,202         |
| Portfolio managed by the<br>Bank  | 2,940                     | 3.46                                  | -                                   | 551,006              | -                                    | -                                  | -                                       | 2,940                       | 3.65                                  | 10,720,146        |
|   |                           |                                       |                                     | <b>551,006</b>       |                                      |                                    |   |                             |                                       | <b>16,157,031</b> |
|   |                           |                                       |                                     |                      |                                      |                                    |   |                             |                                       | <b>16,708,037</b> |

1 Restricted investment accounts represent amounts received from and transactions entered on behalf of related parties. The restricted investment accounts at 31 December 2007 are carried net of a provision for impairment amounting to US\$ 282,311 (2006: US\$ 282,311).

2 On the instructions of a restricted investment account holder, a related party, the Bank has entered into a deferred payment purchase agreement with a financial institution to acquire shares of International Investment Group K.S.C.C ('IIG'). The Bank then entered into a deferred payment sale agreement with the restricted investment account holder for sale of the these shares. However, due to a legal dispute with the financial institution, the Bank could not effect the transfer of the IIG shares to the restricted investment account holder (note 25).

The accompanying notes 1 to 25 form an integral part of these financial statements.

**STATEMENT OF CHANGES IN RESTRICTED INVESTMENT ACCOUNTS  
for the year ended 31 December 2007**

US\$

|  | Balance at 1 January 2006 |                              | Movements during the year     |                   |                                |                              |                              | Balance at 31 December 2006 |                              |            |
|--|---------------------------|------------------------------|-------------------------------|-------------------|--------------------------------|------------------------------|------------------------------|-----------------------------|------------------------------|------------|
|  | No of units (000)         | Average value per share US\$ | Investment/ (withdrawal) US\$ | Revaluations US\$ | Investment profit/ (loss) US\$ | Bank's fees as an agent US\$ | Administration expenses US\$ | No of units (000)           | Average value per share US\$ | Total US\$ |
| Murabaha with Lotus Air Ltd Shares in Bahrain Family Leisure Company BSC Investments in International Investment Group K.S.C.C. (note 2 below) | -                         | -                            | -                             | -                 | -                              | -                            | -                            | -                           | -                            | 317,689    |
| Portfolio managed by the Bank  | 2,385                     | 0.30                         | (631,640)                     | (107,544)         | 31,631                         | (977)                        | -                            | -                           | -                            | 708,530    |
|  | 12,887                    | 0.44                         | -                             | -                 | -                              | -                            | -                            | 12,887                      | 0.44                         | 5,670,202  |
|  | 2,940                     | 3.42                         | -                             | 101,336           | -                              | -                            | -                            | 2,940                       | 3.46                         | 10,169,140 |
|  |                           |                              | (631,640)                     | (6,208)           | 31,631                         | (977)                        | -                            |                             |                              | 16,157,031 |

- 1 Restricted investment accounts represent amounts received from and transactions entered on behalf of related parties. The restricted investment accounts at 31 December 2006 are carried net of a provision for impairment amounting to US\$ 282,311 (2004: US\$ 282,311).
- 2 On the instructions of a restricted investment account holder, a related party, the Bank has entered into a deferred payment purchase agreement with a financial institution to acquire shares of International Investment Group K.S.C.C ('IIG'). The Bank then entered into a deferred payment sale agreement with the restricted investment account holder for sale of the these shares. However, due to a legal dispute with the financial institution, the Bank could not effect the transfer of the IIG shares to the restricted investment account holder (note 25).

The accompanying notes 1 to 25 form an integral part of these financial statements.

**STATEMENT OF SOURCES AND USES OF CHARITY FUND**  
**for the year ended 31 December 2007**

US\$

|  | <b>2007</b>     | 2006    |
|--|-----------------|---------|
| <b>Sources of charity fund</b>                   |                 |         |
| Contributions by the Bank                        | -               | 200,000 |
| Non-Islamic income                               | 553             | 235     |
| <b>Total sources</b>                             | <b>553</b>      | 200,235 |
| <b>Uses of charity fund</b>                      |                 |         |
| Contributions to charitable organisations        | 81,141          | 85,026  |
| <b>Total uses</b>                                | <b>81,141</b>   | 85,026  |
| <b>(Deficit) / excess of sources over uses</b>   | <b>(80,588)</b> | 115,209 |
| Undistributed charity fund at 1 January          | 115,209         | -       |
| <b>Undistributed charity fund at 31 December</b> | <b>34,621</b>   | 115,209 |

The accompanying notes 1 to 25 form an integral part of these financial statements.

**NOTES TO THE FINANCIAL STATEMENTS**  
**for the year ended 31 December 2007**

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**1 INCORPORATION AND ACTIVITIES**

Investors Bank B.S.C. (C) (the "Bank") was established in the Kingdom of Bahrain as an exempt company on 26 October 1997 and operates under an investment banking license granted by the Central Bank of Bahrain (the "CBB"). The Bank commenced commercial operations on 15 June 1998. The legal status of the Bank was changed to a closed Bahraini joint stock company on 3 July 2005.

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

The principal activities of the Bank include investment banking and financial activities, investment transactions, participating in equity investments in projects in conformity with the Islamic Shari'a. The Bank may, in particular, carry on the following business activities:

- (a) Providing investment account facilities;
- (b) Accepting restricted or unrestricted investment funds commingling the same with those of the Bank and investing them in accordance with the Shari'a;
- (c) Managing the investment of third party funds as an agent for a fixed fee or as a Mudarib and any other banking activities not contravening the provisions of the Shari'a;
- (d) Industrial, commercial and agricultural business activities, either directly or through companies which the Bank may establish, or in which the Bank may acquire shares; and
- (e) Purchasing, leasing and constructing buildings, and the renting thereof.

**2 SIGNIFICANT ACCOUNTING POLICIES****(a) Statement of compliance**

The financial statements have been prepared in accordance with Financial Accounting Standards ("FAS") issued by the Accounting and Auditing Organisation for Islamic Financial Institutions.

**(b) Basis of preparation**

The financial statements are presented in US Dollars, being the principal currency of the Bank's operations. They are prepared on the historical cost basis modified by measurement at fair value of trading investments and creation available-for-sale investments.

The accounting policies have been consistently applied by the Bank and are consistent with those used in the previous year.

The preparation of financial statements in conformity with FAS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Bank's accounting policies. The areas involving a high degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements as set out in note 24.

**(c) Revenue recognition**

**Income from investment advisory services** is recognised when the Bank has performed all significant acts relating to the advisory service being rendered and it is highly probable that economic benefits from the transaction will flow to the Bank.

**Underwriting fees** is recognised as income when earned.

**Placement fees** are recognised as income when earned.

**Income from Murabaha contracts** are recognised on a time-apportioned basis over the period of the contract.

**NOTES TO THE FINANCIAL STATEMENTS**  
**for the year ended 31 December 2007**

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2 *Significant accounting policies (continued)*(c) *Revenue recognition (continued)*

Income from **deferred payment sale contracts** are recognised on a time-apportioned basis over the period of the contract.

Income from **Mudaraba contracts** are recognised when the Mudarib declares profits.

Income from investments (**dividend income**) is recognised when the right to receive is established.

(d) **Mudaraba investments**

Mudaraba investments are stated at cost less provision for impairment.

(e) **Trading and available-for-sale investments****(i) Classification**

Held-for-trading investments are financial assets which are held principally for the purpose of generating a profit from short-term fluctuations in price or dealer's margin or where a pattern of short-term profit taking exists or is part of a portfolio for which there is evidence of a recent actual pattern of short-term profit taking. These comprise investments in quoted shares.

Available-for-sale investments are financial assets that are not held-for-trading purposes, or held-to-maturity. These include investments in quoted and unquoted shares and managed funds.

**(ii) Recognition**

Held-for-trading and available-for-sale investments are recognised/derecognised by the Bank on Trade i.e. the date the bank commits to purchase/sell the investments.

**(iii) Measurement**

Held-for-trading investments are measured initially at cost being fair value. Transaction costs are charged as expense. Subsequent to initial recognition, Held-for trading investments are re-measured to fair value and the resulting unrealised gains or losses are recognised in the income statement in the year in which they arise.

Available-for-sale investments are measured initially at cost being fair value including transaction costs. Subsequent to initial recognition available-for-sale investments are re-measured to fair value and the resulting fair value gains or losses are recognised in an "investment fair value reserve" as a separate component in the equity provided that unrealised losses are recognised in equity to the extent of the available balance. In case losses exceed the available balance, the unrealised losses are recognised in the income statement under "fair value losses on investments". In case there are unrealised losses that have been previously recognised in the income statement, then the unrealised gains for the year are recognised to the extent of previously recognised losses in the income statement. Any excess of such gains over previously recognised losses is taken to the "Investments fair value reserve".

Fair value for quoted investments is their market bid price in an active market. Investments for which there is no quoted market price or other appropriate methods from which to derive fair values, are stated at cost less impairment allowances, if any. Fair value for unquoted managed funds is the fund's net assets value as determined by the fund manager.



**NOTES TO THE FINANCIAL STATEMENTS**  
**for the year ended 31 December 2007**

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- (f) **Deferred payment sale receivables**  
Receivables arising from deferred payment sale are recognised at the time of contracting and stated at their cost less impairment allowances.
- (g) **Equipment**  
Equipment are stated at cost, net of accumulated depreciation. Depreciation is computed using the straight-line method to write-off the cost of the assets over their estimated useful lives ranging from 3 to 5 years.
- (h) **Investment property**  
Investment property is stated at cost less impairment.
- (i) **Impairment**  
The carrying amount of the Bank's assets are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated. An impairment loss is recognised whenever the carrying amount of an asset exceeds its estimated recoverable amount. Impairment losses are recognised in the income statement. Impairment losses are reversed only if there is an indication that the impairment loss may no longer exist and there has been a change in the estimates used to determine the recoverable amount.
- (j) **Earnings prohibited by Shari'a**  
The Bank is committed to avoid recognising any income generated from non-Islamic sources. Accordingly, all non-Islamic income is credited to a charity account where the Bank uses these funds for charitable means. Movements in non-Islamic funds are shown in the statement of sources and uses of charity fund.
- (k) **Restricted investment accounts**  
Restricted investment accounts represents assets held in trust or in a fiduciary capacity by the Bank for the benefit of the investment accounts holders. The restricted investment accounts are exclusively restricted for investment in specified projects as directed by the investments account holders.  
  
Restricted investments in quoted securities are valued at their market bid price. Restricted investments in securities for which there are no quoted market price or other appropriate methods from which to derive fair values, are stated at cost less impairment allowances, if any.
- (l) **Transactions and balances in foreign currencies**  
Transactions in foreign currencies are translated at the exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date, are translated at the exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in the income statement. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated to the reporting currency at the exchange rates ruling at the dates that the values are determined.

**NOTES TO THE FINANCIAL STATEMENTS**  
**for the year ended 31 December 2007**

US\$

2 *Significant accounting policies (continued)***(m) Cash and cash equivalents**

Cash and cash equivalents comprise cash and balances with financial institutions and short-term highly liquid assets (commodity Murabahas), with maturities of three months or less when acquired, which are subject to insignificant risk of changes in fair value and are used by the Bank in the management of its short-term commitments

**3 CASH AND CASH EQUIVALENTS**

|                                | <b>2007<br/>US\$</b> | <b>2006<br/>US\$</b> |
|--------------------------------|----------------------|----------------------|
| Cash on hand                   | 1,326                | 1,326                |
| Cash at banks                  | 1,778,918            | 381,856              |
| Short term Commodity Murabaha: |                      |                      |
| Gross                          | 7,856,537            | -                    |
| Deferred profit                | (5,209)              | -                    |
| Carrying amount                | 7,851,328            | -                    |
|                                | <b>9,631,572</b>     | <b>383,182</b>       |

**4 TRADING INVESTMENTS**

|  | <b>2007<br/>US\$</b> | <b>2006<br/>US\$</b> |
|--|----------------------|----------------------|
| At 1 January                             | 39,293,867           | 70,354,102           |
| Purchases during the year                | -                    | 4,200,000            |
| Sales during the year, at carrying value | -                    | (28,786,689)         |
| Fair value losses during the year        | (9,566,793)          | (6,473,546)          |
| <b>At 31 December</b>                    | <b>29,727,074</b>    | <b>39,293,867</b>    |

At 31 December 2007, investments with a carrying value of US\$ NIL (2006: US\$ 39,293,867) were held in the name of related parties as portfolio managers for the Bank.

**5 AVAILABLE-FOR-SALE INVESTMENTS**

|   | <b>2007<br/>US\$</b> | <b>2006<br/>US\$</b> |
|---|----------------------|----------------------|
| At 1 January                                | 21,586,476           | 22,797,020           |
| Purchases during the year                   | -                    | 748,925              |
| Sales during the year, at carrying value    | -                    | (5,055,455)          |
| Fair value (losses) / gains during the year | (450,905)            | 3,095,986            |
| Impairment loss                             | (400,000)            | -                    |
| <b>At 31 December</b>                       | <b>20,735,571</b>    | <b>21,586,476</b>    |

**NOTES TO THE FINANCIAL STATEMENTS**  
**for the year ended 31 December 2007**

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## 5 Available-for-sale investments (continued)

Available-for -sale investments comprise:

|                                     | <b>2007<br/>US\$</b> | <b>2006<br/>US\$</b> |
|-------------------------------------|----------------------|----------------------|
| <b>Investment in shares</b>         |                      |                      |
| i) Quoted – at fair value           | 19,762,462           | 20,263,384           |
| ii) unquoted – at cost              | 1,486,430            | 1,447,658            |
| <b>Investments in managed funds</b> | <b>868,779</b>       | <b>857,534</b>       |
|                                     | <b>22,117,671</b>    | <b>22,568,576</b>    |
| Less: provision for impairment      | (1,382,100)          | (982,100)            |
|                                     | <b>20,735,571</b>    | <b>21,586,476</b>    |

Impairment allowance on available for sale investments

|                                      | <b>2007<br/>US\$</b> | <b>2006<br/>US\$</b> |
|--------------------------------------|----------------------|----------------------|
| Opening balance                      | 982,100              | 982,100              |
| Additional provision during the year | 400,000              | -                    |
| Closing balance                      | <b>1,382,100</b>     | <b>982,100</b>       |

Material available-for-sale investments as at current year end are as follows:

|                                    | Country of<br>incorporation | %<br>ownership | Nature of main activities                              |
|------------------------------------|-----------------------------|----------------|--|
| <b>Quoted shares at fair value</b> |                             |                |  |
| Bahrain Islamic Bank BSC           | Bahrain                     | 1.45           | Commercial banking in accordance with Islamic Shari'a. |
| Takaful International BSC          | Bahrain                     | 18.03          | Takaful – insurance according to the Islamic Shari'a.  |

At 31 December 2007, investments with carrying value of US\$ 11,854,788 (2006: US\$ 12,348,738) were held in the name of a financial institution and pledged as collateral against amounts due to the financial institution (note 25). Also, investments with carrying value of US\$ 6,435,709 (2006: US\$ 6,435,709) were pledged as collateral against amounts due to a related party.

**NOTES TO THE FINANCIAL STATEMENTS**  
**for the year ended 31 December 2007**

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**6 OTHER ASSETS**

|  | <b>2007<br/>US\$</b> | <b>2006<br/>US\$</b> |
|--|----------------------|----------------------|
| Current account with related parties (note 20)       | 5,666,486            | 2,256                |
| Statutory deposit with CBB                           | 13,263               | 13,263               |
| Underwriting fee receivable                          | -                    | 3,631,836            |
| Placement fee receivable                             | -                    | 2,000,000            |
| Management and advisory fees receivable              | 71,701               | 93,300               |
| Prepaid expenses                                     | 179,502              | 157,190              |
| Qard Hassan  | 56,016               | 140,419              |
| Advance towards purchase of AFS investment (note 20) | 454,114              | 451,772              |
| Others   | 2,677,837            | 1,451,556            |
|  | <b>9,118,919</b>     | <b>7,941,592</b>     |
| Less: impairment allowances                          | (808,535)            | (400,000)            |
|  | <b>8,310,384</b>     | <b>7,541,592</b>     |

## Impairment allowance on other assets

|                                      | <b>2007<br/>US\$</b> | <b>2006<br/>US\$</b> |
|--------------------------------------|----------------------|----------------------|
| Opening balance                      | 400,000              | 400,000              |
| Additional provision during the year | 408,535              | -                    |
| Closing balance                      | <b>808,535</b>       | <b>400,000</b>       |

**7 EQUIPMENT**

|  | <b>Office<br/>equipment<br/>&amp; furniture</b> | <b>Fixtures</b>  | <b>Motor<br/>vehicles</b> | <b>2007<br/>Total<br/>US\$</b> | <b>2006<br/>Total<br/>US\$</b> |
|--|---|------------------|---------------------------|--------------------------------|--------------------------------|
| <b>Cost</b>                              |   |                  |                           |                                |                                |
| At 1 January                             | 341,606   | 184,879          | 58,045                    | 584,530                        | 604,273                        |
| Additions                                | 533,271   | 1,060,717        | -                         | 1,593,988                      | 4,780                          |
| Disposals                                | -   | -                | -                         | -                              | (24,524)                       |
| <b>At 31 December</b>                    | <b>874,877</b>                                  | <b>1,245,596</b> | <b>58,045</b>             | <b>2,178,518</b>               | <b>584,529</b>                 |
| <b>Depreciation</b>                      |   |                  |                           |                                |                                |
| At 1 January                             | 284,386   | 184,879          | 31,925                    | 501,190                        | 471,833                        |
| Charge for the period                    | 34,494  | -                | 11,609                    | 46,103                         | 53,681                         |
| Disposals                                | -   | -                | -                         | -                              | (24,324)                       |
| <b>At 31 December</b>                    | <b>318,880</b>                                  | <b>184,879</b>   | <b>43,534</b>             | <b>547,293</b>                 | <b>501,190</b>                 |
| <b>Net book value<br/>at 31 December</b> | <b>555,997</b>                                  | <b>1,060,717</b> | <b>14,511</b>             | <b>1,631,225</b>               | <b>83,339</b>                  |

**NOTES TO THE FINANCIAL STATEMENTS**  
for the year ended 31 December 2007

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**8 INVESTMENT PROPERTY**

Investment property represents the Bank's share in a building in a Sharjah jointly owned with a related party. The building is registered in the name of the related party.

**9 EQUITY**

Authorised:

303,030,303 ordinary shares of US\$ 0.33 each

Issued and fully paid up:

242,424,242 shares of US\$ 0.33 each

|  | 2007        | 2006        |
|--|-------------|-------------|
|  | 100,000,000 | 100,000,000 |
|  | 80,000,000  | 80,000,000  |

**Share premium**

Share premium represents the net amount received in excess of the par value of share capital and this amount is not distributable to shareholders, except in the circumstances stipulated by the law.

**Statutory reserve**

In accordance with the requirements of the Bahrain Commercial Companies Law 2001, 10% of the net profit for the year is transferred to a statutory reserve until such time as the reserve represents 50% of the paid up capital. This reserve is not available for distribution.

**General reserve**

General reserve represents appropriations from the Bank's net profit as approved by the shareholders and can only be distributed with the approval of the shareholders.

**10 INCOME FROM TRADING INVESTMENTS**

Dividend income

Income from sale of investments

|  | 2007<br>US\$   | 2006<br>US\$     |
|--|----------------|------------------|
|  | 771,937        | 1,412,454        |
|  | -              | 6,631,897        |
|  | <b>771,937</b> | <b>8,044,351</b> |

**11 INCOME FROM AVAILABLE-FOR-SALE INVESTMENTS**

Dividend income

Income from sale of investments

|  | 2007<br>US\$   | 2006<br>US\$     |
|--|----------------|------------------|
|  | 412,579        | 548,532          |
|  | -              | 4,005,166        |
|  | <b>412,579</b> | <b>4,553,698</b> |

**12 UNDERWRITING FEES**

This represents fees arising from underwriting the sale of shares of a related party. The underwriting exposure amounted to US\$ NIL (2006: US\$ 72.6 million). The Share were placed with investors before the year end.

**NOTES TO THE FINANCIAL STATEMENTS**  
for the year ended 31 December 2007

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**13 INCOME FROM INVESTMENT PROPERTY - NET**

|   | <b>2007<br/>US\$</b> | <b>2006<br/>US\$</b> |
|---|----------------------|----------------------|
| Gain on partial sale of investment property | 1,891,893            | -                    |
| Advertising and other expenses              | (634,842)            | -                    |
|   | <b>1,257,051</b>     | -                    |

**14 STAFF COST**

In 2006, staff costs included US\$ 1,000,000 paid to the Managing Director during the year as consideration for his services in earlier periods.

**15 ADMINISTRATIVE AND GENERAL EXPENSES**

|                                | <b>2007<br/>US\$</b> | <b>2006<br/>US\$</b> |
|--------------------------------|----------------------|----------------------|
| Consultancy and legal expenses | 364,139              | 584,781              |
| Rent                           | 164,945              | 91,432               |
| Advertising and promotion      | 80,162               | 113,986              |
| Professional fees              | 62,334               | 40,318               |
| License and registration       | 35,589               | 61,288               |
| Communication                  | 32,279               | 34,298               |
| Business development           | 52,608               | 96,532               |
| Brokerage fee                  | 6,256                | 407,075              |
| Others                         | 241,198              | 315,646              |
|                                | <b>1,039,510</b>     | <b>1,745,356</b>     |

**16 IMPAIRMENT ALLOWANCE**

|                                | <b>2007<br/>US\$</b> | <b>2006<br/>US\$</b> |
|--------------------------------|----------------------|----------------------|
| Murabaha receivables           | 1,904,059            | -                    |
| Available-for-sale investments | 400,000              | -                    |
| Other assets                   | 408,535              | -                    |
|                                | <b>2,712,594</b>     | -                    |

**17 ZAKAH**

Zakah is directly borne by the shareholders and, accordingly, no provision is made by the Bank for Zakah. The Bank computes the Zakah payable by the shareholder on the net invested funds method. The basis of computation is approved by the Shari'a Board and the amounts payable are notified to the shareholders.

**NOTES TO THE FINANCIAL STATEMENTS**  
for the year ended 31 December 2007

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**18 MATURITY PROFILE**

The maturity profile of the Bank's assets and liabilities is as follows:

| 2007                     |                    |                  |                    |                                |
|--------------------------|--------------------|------------------|--------------------|--------------------------------|
|                          | Assets             | Liabilities      | Net                | Restricted investment accounts |
| Up to 1 month            | 15,298,057         | 73,183           | 15,224,874         | -                              |
| From 1 month to 3 months | 50,406,865         | 3,283,852        | 47,123,013         | -                              |
| From 3 months to 1 year  | 60,830,942         | 3,739,842        | 57,091,100         | -                              |
| From 1 year to 3 years   | 8,873,534          | 93,621           | 8,779,913          | 16,708,037                     |
| Over 3 years             | 1,646,174          | -                | 1,646,174          | -                              |
|                          | <b>137,055,572</b> | <b>7,190,498</b> | <b>129,865,074</b> | <b>16,708,037</b>              |

| 2006                     |                    |                  |                    |                                |
|--------------------------|--------------------|------------------|--------------------|--------------------------------|
|                          | Assets             | Liabilities      | Net                | Restricted investment accounts |
| Up to 1 month            | 9,084,974          | 6,428            | 9,078,546          | -                              |
| From 1 month to 3 months | 57,930,531         | 338,936          | 57,591,595         | -                              |
| From 3 months to 1 year  | 58,398,879         | 7,040,620        | 51,358,259         | -                              |
| From 1 year to 3 years   | 22,513,248         | 61,415           | 22,451,833         | 16,157,031                     |
| Over 3 years             | 96,601             | -                | 96,601             | -                              |
|                          | <b>148,024,233</b> | <b>7,447,399</b> | <b>140,576,834</b> | <b>16,157,031</b>              |

**19 CONCENTRATION OF ASSETS AND LIABILITIES**

The Bank's assets and liabilities are distributed over the following industry sectors and geographical areas:

| 2007                             |                    |                  |                                |
|----------------------------------|--------------------|------------------|--------------------------------|
| Industry sectors                 | Assets             | Liabilities      | Restricted investment accounts |
| Banks and financial institutions | 64,718,861         | 6,899,266        | 5,670,202                      |
| Investment companies             | 16,271,870         | -                | 10,720,146                     |
| Others                           | 56,064,841         | 291,232          | 317,689                        |
|                                  | <b>137,055,572</b> | <b>7,190,498</b> | <b>16,708,037</b>              |

| 2006                             |                    |                  |                                |
|----------------------------------|--------------------|------------------|--------------------------------|
| Industry sectors                 | Assets             | Liabilities      | Restricted investment accounts |
| Banks and financial institutions | 69,712,613         | 6,899,265        | 5,670,202                      |
| Investment companies             | 13,562,592         | -                | 10,169,140                     |
| Others                           | 64,749,028         | 548,134          | 317,689                        |
|                                  | <b>148,024,233</b> | <b>7,447,399</b> | <b>16,157,031</b>              |

**NOTES TO THE FINANCIAL STATEMENTS**  
**for the year ended 31 December 2007**

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19 *Concentration of assets and liabilities (continued)*

**Geographical concentration**

All assets and liabilities of the Bank as at 31 December 2007 and 31 December 2006 are concentrated in the Middle East region.

**20 RELATED PARTY TRANSACTIONS AND BALANCES**

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial and operating decisions. Related parties also include directors and shareholders of the Bank and companies in which they have an ownership interest.

A significant portion of the Bank's income arises from transactions with related parties. Transactions with related parties are undertaken on terms agreed between the parties.

Significant balances with related parties at 31 December comprise:

|  | <b>2007</b><br><b>US\$</b> | <b>2006</b><br><b>US\$</b> |
|--|----------------------------|----------------------------|
| <b>Assets</b>  |                            |                            |
| Trading investments  | 29,727,074                 | 39,293,867                 |
| Available-for-sale investments                             | 8,313,197                  | 8,270,151                  |
| Murabaha receivables                                       | 3,243,848                  | 4,925,048                  |
| Mudaraba investments                                       | 4,500,000                  | 21,931,034                 |
| Receivables from sale of investments                       | 29,860,901                 | 30,268,197                 |
| Deferred payment sale receivables                          | 3,680,203                  | 3,680,203                  |
| Advance towards purchase of available-for-sale investments | 45,579                     | 451,772                    |
| Receivable from Mudarib                                    | 11,896,174                 | -                          |
| Current account with related parties                       | 5,666,486                  | 2,256                      |
| Dividend receivable  | 814,259                    | 987                        |
| Due from chairman  | 99,161                     | 59,302                     |
| Management and advisory fees receivable                    | 71,701                     | 133,037                    |
| <b>Liabilities</b>   |                            |                            |
| Murabaha payables  | 3,229,064                  | 3,229,064                  |
| Payables for expenses                                      | -                          | 298,015                    |

The Bank has investments in companies of certain shareholders. The carrying amounts of such investments at 31 December 2007 were US\$ 48,788 (2006: US\$ 55,759).



**NOTES TO THE FINANCIAL STATEMENTS**  
**for the year ended 31 December 2007**

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20 *Related party transactions and balances (continued)*

Significant transactions with related parties include:

|  | <b>2007</b><br><b>US\$</b> | <b>2006</b><br><b>US\$</b> |
|--|----------------------------|----------------------------|
| <b>Income</b>                              |                            |                            |
| Income from trading investments            | 771,937                    | 2,577,974                  |
| Income from available-for-sale investments | 955                        | 4,206,958                  |
| Placement fees                             | -                          | 2,000,000                  |
| Underwriting fees                          | -                          | 3,631,208                  |
| Fair value losses on trading investments   | (9,566,793)                | (6,473,546)                |
| Income from Mudaraba investment            | 79,377                     | 3,363,395                  |
| Income from Murabaha receivables           | 222,858                    | 275,048                    |
| Other income                               | -                          | 977                        |
| <b>Expenses</b>                            |                            |                            |
| Impairment provision                       | 2,312,594                  | -                          |
| Remuneration to the Managing Director      | -                          | 1,000,000                  |
| Arrangement expenses                       | -                          | 203,333                    |

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

|  | <b>2007</b><br><b>US\$</b> | <b>2006</b><br><b>US\$</b> |
|--|----------------------------|----------------------------|
| Salaries and other short-term benefits | 168,572                    | 226,549                    |
| Post employment benefits               | 3,820                      | 9,450                      |
| Directors' remuneration                | -                          | 490,000                    |
| Payment to the Managing Director       | -                          | 1,000,000                  |

**21 Proposed appropriations**

The Board of Directors doesn't propose any appropriation for the year. For 2006, the board of directors decided not seek regulatory approval for the proposed directors' remuneration of US\$ 150,000.

**NOTES TO THE FINANCIAL STATEMENTS**  
**for the year ended 31 December 2007**

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**22 RISK MANAGEMENT**

The Bank is exposed to the credit risk, liquidity risk and market risk during the course of its business along with other operation risks.

The Bank's Board of Directors has the overall responsibility for the establishment and oversight of the Bank's risk management framework. The Board has established an Executive Committee, which is responsible for developing and monitoring bank's operations and policies across various functions including the risk management policies. The Executive Committee consists of three non-executive directors of the Bank along with the Chief Executive Officer (CEO) as an attendee. The Executive Committee reviews and approves the CEO's recommendations for investment strategies, investment proposals, various products and services and where deemed necessary, also refers decisions to the Board of Directors. Although the Bank currently has no separate Risk Management Committee (commensurate with its activities), the Head of Risk Management assists with the overall management of the Bank's risks.

The Bank's Audit Committee is responsible for monitoring compliance with the risk management policies and procedures, and for reviewing the adequacy of the risk management framework in relation to the risks faced by the Bank. The Audit Committee is assisted in these functions by Internal Audit function. Internal Audit undertakes both regular and ad-hoc reviews of risk management controls and procedures, the results of which are reported to the Audit Committee. The Bank is in the process of updating the charter of the audit committee of the Board to include responsibilities for overall risk management approach, risk strategy and policies of the Bank as part of the Basel II implementation plan.

The Bank has an internal risk management function to provide independent review, monitoring and control of the various risks faced by the Bank. It works closely with the executive management and other business and control functions. Various operating departments (the business units and the support functions) own the risks.

The Bank with the help of external consultants is in the process of updating its business strategy and plan. As part of this exercise the Bank will establish exposure limits, commensurate to its new business strategy and market environment as well as set levels of risk the Bank is willing to accept in relation to its available capital.

**a) Credit risk**

Credit risk is the risk that a counterparty to a financial transaction does not discharge its obligations on due dates and cause the other party to incur a financial loss.

The Bank's credit risk arises mainly from cash and balances with banks, Murabaha receivables, Mudaraba investment, receivable from sale of investments, available-for-sale investments, deferred payment sale receivables and other assets.

The Bank has an Asset Management department, which is responsible for origination of investment / credit proposals and post sanction review and monitoring. The Bank's Risk Management Department (RMD) works alongside the investment originators at all stages of the deal cycle, up to exit and provides an independent review.

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22 *Risk Management (continued)*a) *Credit risk (continued)*

Bank has initiated steps to ensure adequate segregation of duties so that the RMD will independently deal with:

- Formulating investment and credit policies in consultation with business units, covering credit assessment, risk reporting, documentary and legal procedures, and compliance with relevant regulatory requirements.
- Establishing the authorization structure for the approval and renewal of investment and credit facilities. Authorization limits are currently allocated to Executive committee and Board of Directors.
- Reviewing and assessing investment and credit risk.
- Limiting concentrations of exposure to counterparties, geographies and industries and product types.
- Developing and maintaining the Bank's risk grading in order to categorise exposures according to the degree of risk of financial loss faced and to focus management on the attendant risks. The current risk grading framework consists of two broad grades "Unimpaired" and "Impaired", reflecting risk of default and the availability of collateral or other credit risk mitigation. Risk is assessed on an individual basis for each investment / receivable and is reviewed at least once a year.
- Reviewing compliance of business units with agreed exposure limits, including those for selected industries, country risk and product types.

The Bank ensures that liquid assets like cash is placed with Islamic financial institutions based on an appropriate credit evaluation. Deferred payment sale receivable is due from a related party. Majority of other assets represents current accounts with related parties.

The Bank's maximum exposure to credit risk at 31 December was as follows:

|  | <b>2007</b>       | 2006              |
|--|-------------------|-------------------|
|  | <b>US\$</b>       | US\$              |
| Cash and cash equivalents              | 9,631,572         | 383,182           |
| Available-for-sale investments         | 20,735,571        | 21,586,476        |
| Murabaha receivables                   | 3,243,848         | 4,925,048         |
| Mudaraba investment                    | 4,500,000         | 21,931,034        |
| Receivable from Mudarib                | 11,896,174        | -                 |
| Receivable from sale of investments    | 29,860,901        | 30,268,197        |
| Deferred payment sale receivables      | 3,680,203         | 3,680,203         |
| Other assets                           | 8,130,881         | 7,384,402         |
| <b>Maximum exposure to credit risk</b> | <b>91,679,150</b> | <b>90,158,542</b> |

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22 *Risk Management (continued)*

a) *Credit risk (continued)*

Analysis of Bank's exposure to credit risk:

| Descriptions<br>2007                                       | Cash &<br>cash<br>equivalents | Available-<br>for-sale<br>investments | Murabaha<br>receivables | Mudaraba<br>investment | Receivables<br>from sale of<br>investments | Deferred<br>payment<br>sale<br>receivables | Other<br>financial<br>assets | Total<br>US\$     |
|--|-------------------------------|---------------------------------------|-------------------------|------------------------|--|--|------------------------------|-------------------|
| Neither past<br>due nor<br>impaired:<br>Carrying<br>amount | 9,631,572                     | 20,735,571                            | -                       | 4,500,000              | -  | -  | 5,882,190                    | 40,749,333        |
| Past due but<br>not impaired:                              |                               |                                       |                         |                        |  |  |                              |                   |
| 30 – 60 days   | -                             | -                                     | -                       | -                      | -  | -  | -                            | -                 |
| 60 – 90 days   | -                             | -                                     | -                       | -                      | -  | -  | 814,258                      | 814,258           |
| 90 – 180 days  | -                             | -                                     | -                       | -                      | -  | -  | -                            | -                 |
| Over 180 days  | -                             | -                                     | -                       | -                      | 29,860,901                                 | 3,680,203                                  | 12,855,607                   | 46,396,711        |
| Carrying<br>amount - Past<br>due but not<br>impaired       | -                             | -                                     | -                       | -                      | 29,860,901                                 | 3,680,203                                  | 13,669,865                   | 47,210,969        |
| Individually<br>impaired:                                  |                               |                                       |                         |                        |  |  |                              |                   |
| Gross amount   | -                             | 1,382,100                             | 5,147,907               | -                      | -  | -  | 1,283,535                    | 7,813,542         |
| Allowance for<br>impairment                                | -                             | (1,382,100)                           | (1,904,059)             | -                      | -  | -  | (808,535)                    | (4,094,694)       |
| Carrying<br>Amount -<br>Individually<br>impaired           | -                             | -                                     | 3,243,848               | -                      | -  | -  | 475,000                      | 3,718,848         |
| <b>Carrying<br/>Amount</b>                                 | <b>9,631,572</b>              | <b>20,735,571</b>                     | <b>3,243,848</b>        | <b>4,500,000</b>       | <b>29,860,901</b>                          | <b>3,680,203</b>                           | <b>20,027,055</b>            | <b>91,679,150</b> |

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22 *Risk Management (continued)*a) *Credit risk (continued)*

| Descriptions                                | Cash & cash equivalents | Available-for-sale investments | Murabaha receivables | Mudaraba investment | Receivables from sale of investments | Deferred payment sale receivables | Other financial assets | Total US\$  |
|---|-------------------------|--------------------------------|----------------------|---------------------|--------------------------------------|-----------------------------------|------------------------|-------------|
| 2006  |                         |                                |                      |                     |                                      |                                   |                        |             |
| Neither past due nor impaired:              |                         |                                |                      |                     |                                      |                                   |                        |             |
| Carrying amount                             | 383,182                 | 21,186,476                     | -                    | 21,931,034          | 30,268,197                           | -                                 | 6,909,402              | 80,678,291  |
| Past due but not impaired:                  |                         |                                |                      |                     |                                      |                                   |                        |             |
| 30 – 60 days                                | -                       | -                              | -                    | -                   | -                                    | -                                 | -                      | -           |
| 60 – 90 days                                | -                       | -                              | 4,925,048            | -                   | -                                    | -                                 | -                      | 4,925,048   |
| 90 – 180 days                               | -                       | -                              | -                    | -                   | -                                    | -                                 | -                      | -           |
| Over 180 days                               | -                       | -                              | -                    | -                   | -                                    | 3,680,203                         | -                      | 3,680,203   |
| Carrying amount - Past due but not impaired | -                       | -                              | 4,925,048            | -                   | -                                    | 3,680,203                         | -                      | 8,605,251   |
| Individually impaired:                      |                         |                                |                      |                     |                                      |                                   |                        |             |
| Gross amount                                | -                       | 1,382,100                      | -                    | -                   | -                                    | -                                 | 875,000                | 2,257,100   |
| Allowance for impairment                    | -                       | (982,100)                      | -                    | -                   | -                                    | -                                 | (400,000)              | (1,382,100) |
| Carrying Amount - Individually impaired     | -                       | 400,000                        | -                    | -                   | -                                    | -                                 | 475,000                | 875,000     |
| Carrying Amount                             | 383,182                 | 21,586,476                     | 4,925,048            | 21,931,034          | 30,268,197                           | 3,680,203                         | 7,384,402              | 90,158,542  |

The impairment provision created on impaired assets is based on the management's assessment of the expected realisations and considers the time value of the money. Specific impairments are identified by the Bank based on the various specific factors, which include financial health of the investee and expected cash flows.

Financial assets, which are past due but not impaired are primarily with related parties and are considered to be low risk as these are not disputed and are being negotiated among the group companies for settlement by way of exchange with other investment grade assets.

Concentration 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 affected by changes in economic, political or other conditions. The Bank seeks to manage its concentration risk by establishing geographic and industry wise concentration limits. Presently, all of the Bank's assets are, however, in GCC region as this has strategic fit with Bank's overall business approach and also the current market imperatives. The sectoral distribution of assets and liabilities is in note 19.

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22 *Risk Management (continued)***b) Liquidity risk**

Liquidity risk is defined as the risk that funds will not be available to meet liabilities as they fall due.

It is the Bank's policy to keep a significant part of its assets in liquid assets such as trading and available-for-sale investments.

The short-term liabilities of the bank mainly represent short-term Murabaha payables to financial institutions, which are secured by pledge of certain investments and are normally rolled over on maturity. The Bank is in the process of establishing an Asset Liability Committee (ALCO), which will set policies and procedures for liquidity management. For maturity profile of assets and liabilities please refer to note 18.

**c) Profit rate risk**

Profit rate risk arises due to different timing of re-pricing of the Company's assets and liabilities. The Bank's exposure to profit rate risk is limited to cash and cash equivalents and Murabaha receivables. The Bank does not have significant profit rate risk sensitivity due to the short-term nature of its cash and cash equivalents and due to maturity of the Murabaha receivables.

**d) Currency risk**

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

The Bank had the following net foreign currency exposures as at 31 December:

| Currency                    | 2007            | 2006            |
|-----------------------------|-----------------|-----------------|
|                             | US\$ Equivalent | US\$ Equivalent |
| Bahraini Dinar              | 48,103,181      | 42,956,751      |
| Kuwaiti Dinar               | 61,448,035      | 74,189,669      |
| United Arab Emirates Dirham | 13,838,620      | 18,331,295      |

## Sensitivity Analysis:

The following table demonstrate the sensitivity to a reasonable possible change in foreign exchange rates, with all other variables held constant, of the Bank's income statement based on the balance sheet position as of 31 December:

| Currency      | 5% decrease |           | 5% increase |             |
|---------------|-------------|-----------|-------------|-------------|
|               | 2007        | 2006      | 2007        | 2006        |
| Kuwaiti Dinar | 3,234,107   | 3,904,719 | (2,926,097) | (3,532,841) |

**e) Equity price risk**

Equity price risk is the risk that Corporations quoted equity investments will depreciate in value due to movements in the quoted equity prices. The Bank does not have an active trading book. All but one equity investments are either available-for-sale and are marked to market. The Bank has only one of its investments marked as trading Investment exposure to which is significant compared with Bank's capital. The Bank monitors the price movement of this investment on a daily basis and intends to reduce the exposure to more conservative level in the near future.

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22 *Risk Management (continued)*e) *Equity price risk (continued)***Sensitivity Analysis:**

The following table demonstrate the sensitivity to a reasonable possible change in equity prices, with all other variables held constant, of the Bank's income statement or equity based on the balance sheet position as of 31 December:

| Particulars                      | 5% decrease |             | 5% increase |           |
|----------------------------------|-------------|-------------|-------------|-----------|
|                                  | 2007        | 2006        | 2007        | 2006      |
| Available-for-sale investments - | (988,123)   | (1,013,024) | 988,123     | 1,013,024 |
| Trading investments              | (1,486,354) | (1,964,693) | 1,486,354   | 1,964,693 |

**23 FAIR VALUE**

Fair value is an amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. Differences can therefore arise between the book values under the historical cost method and fair value estimates.

Other than certain available-for-sale investments carried at cost of US\$ 754,330 (2006:US\$ 715,558), the estimated fair values of the Bank's other financial instruments are not significantly different from their book values.

**24 CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES**

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

**Impairment of available-for-sale investments**

The Bank determines that available-for-sale investments are impaired when there has been a significant or prolonged decline in the fair value below its cost. This determination of what is significant or prolonged requires judgment. Where fair values are not readily available and the investments are carried at cost, the recoverable amount of such investment is estimated to test for impairment. In making this judgment, the Bank evaluates among other factors, evidence of a deterioration in the financial health of the investee, industry and sector performance, changes in technology, and operational and financing cash flows.

**25 LITIGATION AND CLAIMS**

In 2004, the bank entered into a sale and purchase agreement with a local financial institution to purchase shares of a related party on behalf of another related party. The net amount due to the financial institution was US\$ 3,670,202. In accordance with the terms of the agreement, the bank pledged certain of its investments with a carrying value of US\$ 11,854,788 as at 31 December 2007. Subsequently, the agreement was terminated by the financial institution due to disputes with the bank and as a result, the pledged investments have been retained by the financial institution. In the opinion of the bank's lawyers and management, the agreement was wrongfully terminated and following the financial institution's refusal to settle the matter amicably, the Bank has filed a legal case in the Bahrain courts against the financial institution for wrongful possession of investments. As a result, the court has taken custody of the shares under dispute. The related party on whose behalf the transactions was entered has provided a manager's cheque for an equal amount which has been deposited with the court. This amount is included under Deferred payment sale receivables.

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25 *Litigation and claims (continued)*

The related party on whose behalf the transaction was entered into has also agreed to reimburse the bank for legal expenses and any losses arising on final settlement with the financial institution. Accordingly, in the opinion of the directors, no provision is required to be made in the financial statements against the investments pledged with the financial institution or for contingent claims that might arise on final settlement.