Basel II Pillar III Quantitative Disclosures
At 30 June 2012

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1. Background

The Public Disclosure (PD) module of the Central Bank of Bahrain (CBB) rulebook was introduced with effect from January 2008. The disclosures in this report are in addition to the disclosures set out in the Group's interim condensed consolidated financial information for the six month period ended 30 June 2012, presented in accordance with Financial Accounting Standards (FAS) issued by the Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI). These disclosures are mainly related to compliance with the Basel II Pillar III Quantitative disclosure requirements and should be read in conjunction with the Group's interim condensed consolidated financial information for the six month period ended 30 June 2012.

2. Basel II Framework

CBB has issued Basel II guidelines for the implementation of Basel II capital adequacy framework for Banks incorporated in the Kingdom of Bahrain.

The Basel II framework provides a risk based approach for calculation of regulatory capital. The Basel II framework is expected to strengthen the risk management practices across the financial institutions.

The Basel II framework is based on three pillars as follows:-

- Pillar I: Minimum capital requirements including calculation of the capital adequacy ratio
- Pillar II: Supervisory review process which includes the Internal Capital Adequacy Assessment Process
- Pillar III: Market discipline which includes the disclosure of risk management and capital adequacy information.

3. Methodology

As per the requirements of CBB's Basel II capital adequacy framework, the method for calculating the consolidated capital adequacy ratio for the Group is summarized as follows:

- Line by line consolidation is performed for the risk exposures and eligible capital of all the subsidiaries within the Group with the exception of Ithmaar's banking subsidiaries incorporated outside Kingdom of Bahrain which are operating under Basel II compliant jurisdictions, where full aggregation is performed of the risk weighted exposures and eligible capital as required under Prudential Consolidation and Deduction module (PCD).

- Pro-rata aggregation of risk weighted exposures and eligible capital of Ithmaar's significant investments (20% – 50%) in banking and other financial entities as required under PCD module.

4. Approaches adopted for determining regulatory capital requirements

The approach adopted for determining regulatory capital requirements under CBB's Basel II guidelines is summarised as follows:

Credit Risk	Standardised approach
Market Risk	Standardised approach
Operational Risk	Basic Indicator approach

5. Group Structure

The Group's interim condensed consolidated financial information are prepared and published on a full consolidation basis, with all subsidiaries being consolidated in accordance with AAOIFI. However, the CBB's consolidated capital adequacy methodology accommodates both line-by-line and aggregation forms of consolidation.

Line by line consolidation is performed for the risk exposures and eligible capital of all the subsidiaries within the Group except for the following:

Subsidiary	Country of Incorporation	Ownership	Approach
Faysal Bank Limited	Pakistan	66.6 per cent	Full Aggregation

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6. Consolidated Capital Structure for capital adequacy purpose

A	**Tier 1 Capital**	
	Issued and fully paid-up ordinary capital	670,863
	Reserves	
	General reserves	56,725
	Statutory reserve	38,090
	Share Premium	149,614
	Others	(24,164)
	Accumulated losses	(273,604)
	Minority interest in the equity of subsidiaries	111,987
	Aggregation	209,360
	Sub-Total	938,871
	Regulatory deductions:	
	Goodwill	(79,963)
	Loss for the period	(5,392)
	Total Tier 1 capital before PCD deductions	**853,516**
B	**Tier 2 Capital**	
	General Provision	27,786
	Profit Equalization Reserves	21,352
	Unrealized gains arising from fair valuations (45%)	7,533
	Aggregation	48,323
	Total Tier 2 capital before PCD deductions	**104,994**
C	**Total Available Capital (A+B)**	**958,510**
D	**General deductions from Tier 1 & 2 under PCD Module**	
	Deduction of unconsolidated financial subsidiaries which are aggregated or deducted	(99,635)
	Deduction of unconsolidated financial associates which are aggregated or deducted	(45,081)
	Excess over maximum permitted large exposure limit	(61,034)
	Total Deductible Items	**(205,750)**
E	**Total Eligible Capital (C-D)**	**752,760**

(Expressed in thousands of United States Dollars unless otherwise stated)

7. Disclosure of the regulatory capital requirements for credit risk under standardized approach

Exposure funded by Self Finance

	Risk weighted assets	Capital requirement
Claims on Other Sovereign	55,623	6,675
Banks	157,872	18,945
Corporate Portfolio	416,526	49,983
Investments in Securities	848,688	101,843
Holding of Real estate	1,159,125	139,095
Regulatory Retail	3,221	387
Residential Mortgage	32,071	3,849
Past due financings	54,260	6,511
Other assets	228,778	27,453
Aggregation	1,668,642	200,237
Total	**4,624,806**	**554,978**

Exposure funded by Unrestricted Investment Accounts (URIA)

	Risk weighted assets	Capital requirement
Corporate Portfolio	101,982	12,238
Equity portfolio	28,937	3,472
Holding of Real estate	49,682	5,962
Regulatory Retail	125,262	15,031
Past due financings	17,866	2,144
Total	**323,729**	**38,847**

(Expressed in thousands of United States Dollars unless otherwise stated)

8. Gross credit exposures:

	Gross credit exposure	Average gross credit exposure
Credit risk exposure relating to on balance sheet assets are as follows:		
Cash, balances with banks and central banks	420,240	399,471
Commodity placements with banks, financial and other institutions	466,866	485,540
Murabaha and other financing	3,104,649	2,918,837
Musharaka financing	35,601	39,060
Investments	2,342,906	2,444,827
Other assets	301,900	302,925
Fixed assets	132,799	132,604
Intangible assets	247,902	252,881
Total on balance sheet credit exposure	**7,052,863**	**6,976,145**
Credit risk exposure relating to off balance sheet items are as follows:		
Financial guarantees and irrevocable letters of credit	806,543	828,661
Financing commitments, Undrawn facilities and other credit related liabilities	2,319,157	2,292,932
Total off balance sheet credit exposure	**3,125,700**	**3,121,593**
Total credit exposure	**10,178,563**	**10,097,738**
Total credit exposure financed by URIA	**1,650,331**	**1,582,845**
Total credit exposure financed by URIA (%)	**16%**	**16%**

Average gross credit exposures have been calculated based on the average of balances outstanding during the six month period ended 30 June 2012.

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9. Geographical distribution of credit exposures:

	Asia/ Pacific	Middle East	Europe	North America	Others	Total
On-balance sheet items						
Cash, balances with banks and central banks	224,709	138,131	44,484	12,916	-	420,240
Commodity placements with banks, financial and other institutions	-	311,955	154,911	-	-	466,866
Murabaha and other financing	1,860,004	950,896	213,615	10	80,124	3,104,649
Musharaka financing	35,601	-	-	-	-	35,601
Investments	963,157	1,186,242	146,084	38,621	8,802	2,342,906
Other assets	144,986	99,956	36,759	20,194	5	301,900
Fixed assets	61,522	70,739	538	-	-	132,799
Intangible assets	28,145	215,419	4,338	-	-	247,902
Total on balance sheet items	**3,318,124**	**2,973,338**	**600,729**	**71,741**	**88,931**	**7,052,863**
Off balance sheet items	**2,514,971**	**542,330**	**39,089**	**7,186**	**22,124**	**3,125,700**
Total credit exposure	**5,833,095**	**3,515,668**	**639,818**	**78,927**	**111,055**	**10,178,563**

The Group uses the geographical location of the credit exposures as the basis to allocate to the respective geographical region as shown above.

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10. Industrial distribution of credit exposures:

	Banks and financial institutions	Trading and manufacturing	Property and construction	Services	Private Individuals	Textile	Others	Total
On-balance sheet items								
Cash, balances with banks and central banks	299,998	-	-	120,239	-	-	3	420,240
Commodity placements with banks, financial and other institutions	466,866	-	-	-	-	-	-	466,866
Murabaha and other financing	273,537	1,042,479	121,900	602,332	569,657	8,950	485,794	3,104,649
Musharaka financing	316	12,611	-	1,443	5,137	1,808	14,286	35,601
Investments	1,496,968	63,761	641,329	89,080	8,370	3,389	40,009	2,342,906
Other assets	206,321	98	45,502	16,099	33,880	-	-	301,900
Fixed assets	63,651	-	69,148	-	-	-	-	132,799
Intangible assets	247,902	-	-	-	-	-	-	247,902
Total on balance sheet items	**3,055,559**	**1,118,949**	**877,879**	**829,193**	**617,044**	**14,147**	**540,092**	**7,052,863**
Off balance sheet items	**1,224,421**	**1,312,418**	**52,956**	**140,101**	**54,060**	**28,514**	**313,230**	**3,125,700**
Total credit exposure	**4,279,980**	**2,431,367**	**930,835**	**969,294**	**671,104**	**42,661**	**853,322**	**10,178,563**

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11. Maturity breakdown of credit exposures:

	Up to 1 Month	1-3 Months	3-12 Months	1-5 Years	5-10 Years	10-20 Years	Over 20 Years	Total
On-balance sheet items								
Cash, balances with banks and central banks	415,239	-	5,001	-	-	-	-	420,240
Commodity placements with banks, financial and other institutions	375,760	-	91,106	-	-	-	-	466,866
Murabaha and other financing	427,808	532,783	729,141	967,942	396,765	50,210	-	3,104,649
Musharaka financing	-	-	-	13,695	21,906	-	-	35,601
Investments	38,926	19,896	400,937	645,609	967,701	-	269,837	2,342,906
Other assets	107,637	3,905	50,666	79,659	60,033	-	-	301,900
Fixed assets	-	-	-	66,984	65,815	-	-	132,799
Intangible assets	-	-	-	280	-	247,622	-	247,902
Total on balance sheet items	**1,365,370**	**556,584**	**1,276,851**	**1,774,169**	**1,512,220**	**297,832**	**269,837**	**7,052,863**
Off balance sheet items	**562,654**	**324,390**	**1,142,279**	**1,025,001**	**59,767**	**11,609**	**-**	**3,125,700**
Total credit exposure	**1,928,024**	**880,974**	**2,419,130**	**2,799,170**	**1,571,987**	**309,441**	**269,837**	**10,178,563**

12. Related-party balances under credit exposure:

A number of banking transactions are entered into with related parties in the normal course of business. The related party balances included under credit exposure at 30 June 2012 were as follows:

Affiliated companies	434,939
Directors & key management	13,071
Total	**448,010**

Concentration of risk to individual counterparties where the credit exposure is in excess of the 15% individual obligor limit:

Non-banks	161,487
Total	**161,487**

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13. Past due and impaired financings and related provisions for impairment:

	Gross exposure	Impairment provisions	Net exposure
Analysis by industry			
Manufacturing	254,934	143,690	111,244
Agriculture	12,448	4,515	7,933
Construction	20,841	5,719	15,122
Finance	18,926	3,629	15,297
Trade	117,024	46,926	70,098
Personal	75,525	38,029	37,496
Real estate	45,080	23,658	21,422
Technology and telecommunications	650	318	332
Transportation	5,828	2,475	3,353
Other sectors	17,908	10,837	7,071
Total	**569,164**	**279,796**	**289,368**
Ageing analysis			
Over 3 months up to 1 year	79,524	12,531	66,993
Over 1 year up to 3 years	152,752	65,512	87,240
Over 3 years	336,888	201,753	135,135
Total	**569,164**	**279,796**	**289,368**

Movement in impairment provisions	Relating to owners	Relating to unrestricted investment accounts	Total
At 1 January 2012	233,555	47,235	280,790
Charge for the period	13,191	3,264	16,455
Write back during the period	(10,224)	-	(10,224)
Utilized during the period	(504)	-	(504)
Exchange differences	(6,721)	-	(6,721)
At 30 June 2012	**229,297**	**50,499**	**279,796**

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14. Past due and impaired financings by geographical areas:

Analysis by Geography	Gross exposure	Impairment Provisions	Net exposure
Asia / Pacific	378,411	203,666	174,745
Middle East	159,593	57,599	101,994
Europe	31,160	18,531	12,629
Total	**569,164**	**279,796**	**289,368**

15. Details of credit facilities outstanding that have been restructured during the six month period ended 30 June 2012:

Restructured financings during the six month period ended 30 June 2012 aggregated to $58 million. This restructuring had an impact of $1.4 million on present earnings during the six month period ended 30 June 2012. Further, this restructuring is expected to have positive impact of $5.3 million on the Group's future earnings. Extension of maturity dates was the basic nature of concessions given to all the restructured facilities.

16. Credit exposures which are covered by eligible financial collateral:

Exposure funded by Self Finance

	Gross Exposure	Eligible Financial Collateral
Corporate portfolio	1,573,961	33,086
Banks	51,620	432
Retail	236,885	32,208
Public Sector Entities	88,892	12
Past due financings	161,327	16,078
Total	**2,112,685**	**81,816**

Exposure funded by Unrestricted Investment Accounts

	Gross Exposure	Eligible Financial Collateral
Corporate portfolio	411,028	67,036
Past due financings	65,337	20,332
Total	**476,365**	**87,368**

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17. Disclosure of regulatory capital requirements for market risk under the standardized approach:

	Risk weighted assets			Capital requirement		
	30 June 2012	Maximum Value	Minimum Value	30 June 2012	Maximum Value	Minimum Value
Foreign exchange risk	133,336	146,141	133,336	16,000	17,537	16,000
Aggregation	116,425	160,128	116,425	13,971	19,215	13,971
Total	**249,761**	**306,269**	**249,761**	**29,971**	**36,752**	**29,971**

18. Disclosure of regulatory capital requirements for operational risk under the basic indicator approach:

For regulatory reporting, the capital requirement for operational risk is calculated based on basic indicator approach. According to this approach, the Bank's average gross income over the preceding three financial years is multiplied by a fixed alpha coefficient.

The alpha coefficient has been set at 15% under CBB Basel II guidelines. The capital requirement for operational risk at 30 June 2012 aggregated to $49.61 million.

19. Tier one capital ratios and Total capital ratios:

	Tier One Capital Ratio	Total Capital Ratio
Ithmaar consolidated	11.54%	13.41%
Significant Bank subsidiaries whose regulatory capital amounts to over 5% of group consolidated regulatory capital whether on a stand-alone or sub-consolidated basis are as follows:		
Faysal Bank Limited	8.48%	10.87%

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20. Equity position in Banking book

At 30 June 2012, the Group's investment securities aggregated to $1,013.9 million. Out of the total investment securities, $79.4 million were listed investment securities and the remaining $934.5 million represented unlisted investment securities.

Cumulative realized losses from sale of investment securities during six month period ended amounted to $3 million. Total unrealized gains recognized in the interim condensed consolidated statement of changes in owners' equity amounted to $8.7 million.

At 30 June 2012, capital requirements using standardized approach aggregated to $44.5 million for listed investment securities and $60.8 million for unlisted investment securities before aggregation/pro-rata aggregation of investments in Banking and other financial entities.

21. Gross income from Mudaraba and profit paid to Investment Account Holders:

	30 June		31 December					
	2012	**2011**	**2011**	**2010**	**2009**	**2008**	**2007**	**2006**
Income from unrestricted investment accounts	44,811	31,476	67,926	61,546	48,835	50,033	54,500	71,893
Less: return to unrestricted investment accounts	(35,519)	(29,322)	(65,018)	(56,395)	(44,796)	(37,868)	(44,781)	(46,073)
Group's share of income from unrestricted investment accounts as a Mudarib	**9,292**	**2,154**	**2,908**	**5,151**	**4,039**	**12,165**	**9,719**	**25,820**

For the six month period ended 30 June 2012 the return to unrestricted investment account holders based on the average balance outstanding during the six month period stood at 4.8%. The Group's share of income from unrestricted investment account (Mudarib) including management fee six month period ended 30 June 2012 as a percentage of gross income from unrestricted investment accounts stood at 20.7%.

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22. Movement in Profit Equalization Reserve and Provisions – URIA:

	30 June		31 December					
	2012	2011	2011	2010	2009	2008	2007	2006
Profit Equalization Reserve								
As at 1 January	18,609	8,155	8,155	3,099	3,645	2,072	764	4,795
Net addition	2,743	3,986	10,454	6,012	-	1,573	1,308	-
Net utilization	-	-	-	(956)	(546)	-	-	(4,031)
As at period ended	**21,352**	**12,141**	**18,609**	**8,155**	**3,099**	**3,645**	**2,072**	**764**
Amount appropriated as a percentage of gross profit	6%	13%	15%	10%	-	3%	2%	-
Provisions								
As at 1 January	68,855	69,766	69,766	64,428	46,563	38,334	37,906	27,310
Net addition	3,264	879	1,457	5,465	17,865	8,229	428	10,596
Net utilization	-	-	-	(127)	-	-	-	-
Reclassification	-	-	(2,368)	-	-	-	-	-
As at period ended	**72,119**	**70,645**	**68,855**	**69,766**	**64,428**	**46,563**	**38,334**	**37,906**

At 30 June 2012, the ratio of profit equalization reserve and provisions to equity of unrestricted investment account holders stood at 1% and 5% respectively.

At 30 June 2012, the ratio of financings to URIA stood at 63%.

23. Average declared rate of return on General Mudaraba deposits:

	30 June		31 December					
	2012	2011	2011	2010	2009	2008	2007	2006
	Percentage							
7 Days	0.25	0.25	0.30	0.50	0.50	0.52	0.75	0.75
30 Days	2.00	2.25	2.31	3.00	3.17	3.26	4.25	4.02
90 Days	2.67	2.80	2.90	3.25	3.25	3.27	4.50	4.27
180 Days	3.00	3.25	3.25	3.50	3.50	3.51	4.70	4.52
360 Days	3.50	3.50	3.50	3.70	3.63	3.68	4.95	4.77

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24. Profit rate risk:

Profit rate risk is the risk that the value of the financial instrument will fluctuate due to changes in the market profit rates.

	USD	PKR	EUR	BHD
Total profit rate exposure	289,365	815,199	414,592	137,811
Rate shock (assumed) (+/-)	2%	2%	2%	2%
Total estimated impact (+/-)	**5,787**	**16,304**	**8,292**	**2,756**

25. Currency risk:

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. Substantial portion of the Group's assets and liabilities are denominated in US Dollars, Bahraini Dinars and Pakistan Rupee. Bahraini Dinars and Saudi Riyal are pegged to US Dollars and as such currency risk is minimal.

The significant net foreign currency positions at 30 June 2012 were as follows:

	Long/(Short)
Euro	(55,579)
UAE Dirham	(299,514)
Hong Kong Dollar	66,111
Saudi Riyal	13,428
Polish Zloty	55,497
Egyptian Pound	9,114

26. Performance Ratios:

	30 June		31 December					
	2012	**2011**	**2011**	**2010**	**2009**	**2008**	**2007**	**2006**
Return on average assets *	0.04%	0.24%	-0.91%	-2.18%	-4.13%	1.80%	5.09%	9.63%
Return on average Shareholders' equity *	0.20%	1.32%	-10.20%	-21.99%	-30.26%	2.20%	10.93%	32.24%
Cost to operating income Ratio *	93.36%	104.62%	121.71%	72.06%	139.31%	51.51%	41.27%	42.10%

*Years 2011, 2010 and 2009 are based on the AAOIFI framework, while 2008 and earlier are based on IFRS.

27. Legal contingencies and compliance:

At 30 June 2012, the Group had contingent liabilities towards customer claims aggregating to $392.6 million. The management is of the view that these claims are not likely to result into potential liabilities.