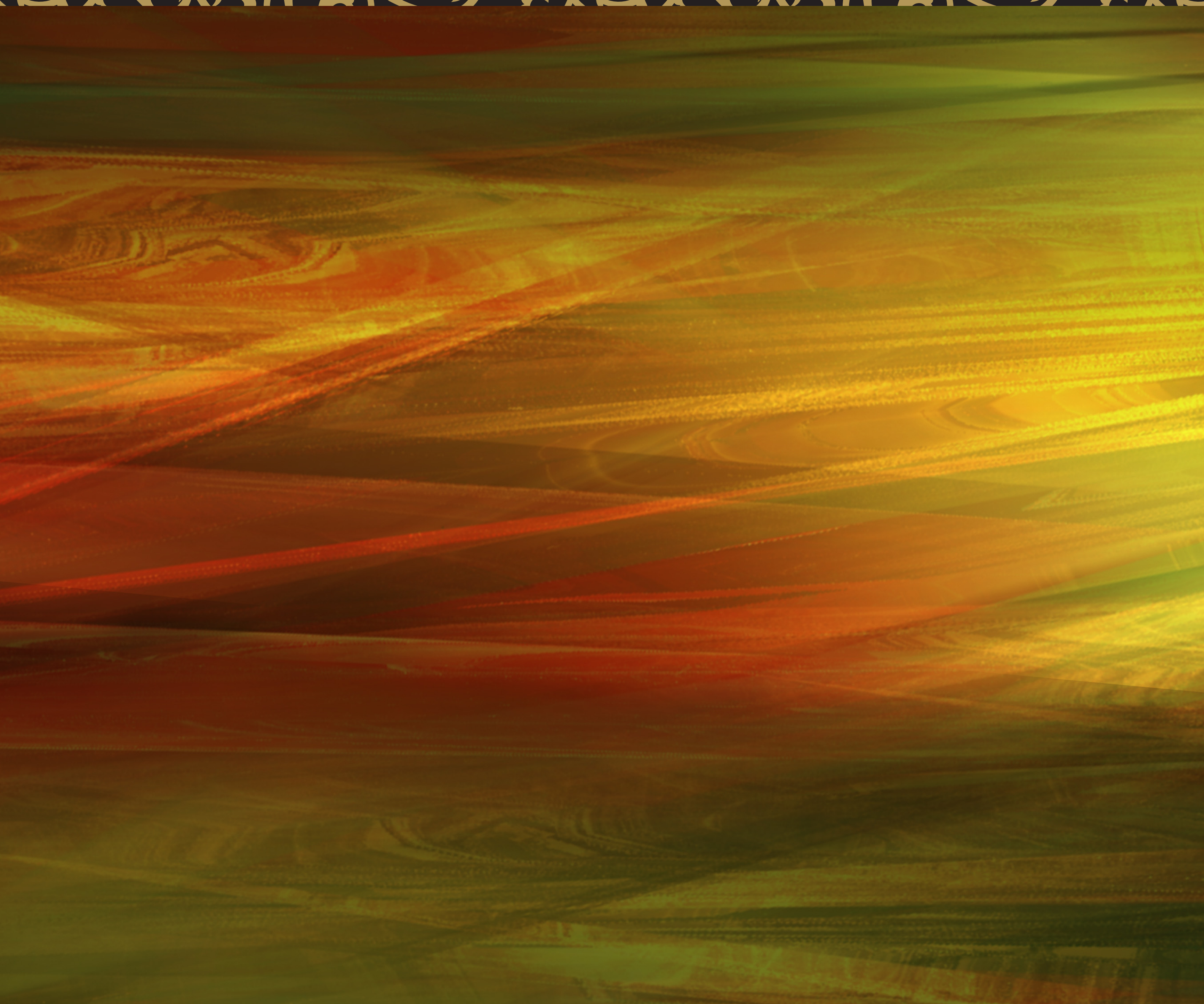
بنك الإثمار
Ithmaar Bank

ANNUAL REPORT '07

Strength in Unity



The Ithmaar banking group is a global financial services powerhouse whose flagship subsidiaries and associates include Shamil Bank, Solidarity, Faisal Private Bank (Switzerland), Faysal Bank Limited (Pakistan), First Leasing Bank and Ithmaar Development Company.

The Annual Reports of the group's different entities for this year showcase the concept of **'Strength in Unity'**. The different companies, while unique and pioneering in their respective fields, together are components of a bigger picture, a bigger enterprise ... the Ithmaar banking group.

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Vision, Mission & Values

Our Vision

- To be the benchmark international investment bank from the Middle East; and,
- With our subsidiaries and associates, to be the premier global Islamic financial services group.

Our Mission

- While being an exemplary corporate citizen and employer, to deliver superior returns to our shareholders.
- To provide excellent group services and value to our multilateral, governmental, corporate, financial, institutional and high net worth clients, through a wide range of Islamic financial services. These include: investments, asset management, commercial and private banking, private equity, public and private issue of securities, mergers and acquisitions advice, takaful, equipment leasing, and real estate development.

Our Values

- Expertise
- Innovation
- Transparency
- Sophistication
- International focus

Financial Highlights

	2007	(Restated) 2006	2005	2004	2003
Net profit **($ million)**	188.3	181.1	37.6	22.1	14.2
Net profit attributable to shareholders **($ million)**	102.8	167.6	36.5	22.1	13.8
Total equity **($ million)**	1,284.4	1,123.7	252.8	219.3	67
Total equity attributable to shareholders **($ million)**	1,087.8	792.1	247.4	214.5	62.4
Net book value per share **($)***	0.51	0.56	1.65	1.43	2.08
Earnings per share **(cents)***	5.79	11.10	24	18	–
Total assets **($ million)**	4,078.8	3,318.8	442	435	409
Funds under management **($ million)**	1,723.8	1,059.9	1,500	1,100	1,000
Return on average equity **(%)**	15.64	26.31	15.8	16	–
Return on average paid in capital **(%)**	23.07	66.55	24.4	18.4	–
Cost to operating income **(%)**	41.10	42.10	69	79	96
Cash dividends **($ million)**	53.7	47.5	20	10	–
Dividends per share **(cents)**	2.50	3.38	13.3	6.7	–
Capital adequacy **(%)**	25.79	29.52	36.8	37.3	32.5

* The 2007 and 2006 numbers reflect the four for one share split.

Chairman's Message

On behalf of the Board of Directors, it gives me great pleasure to present the annual report of Ithmaar Bank and its consolidated subsidiaries, associates and joint ventures for the period ended 31 December 2007. This was the first full year of operations of the Bank as a publicly-traded company, following its successful IPO in March 2006 and subsequent listing on the Bahrain Stock Exchange.

In what can best be described as a year of synergistic momentum, I am delighted to report that Ithmaar Bank posted an exceptional performance during 2007. This was marked by sound strategic progress, strong financial results, excellent business achievements, and significant organisational developments.

Ithmaar Bank heads a regional banking and financial services group, with a global outlook that comprises 17 subsidiaries, associates and joint ventures. For the purpose of this report, however, I will be focusing on the flagship institutions that make up the Ithmaar banking group, which either constitute the group's principal revenue generating streams, or offer optimum potential for growth. These are Ithmaar Bank, Shamil Bank, Faysal Bank Limited, Faisal Private Bank, Solidarity, First Leasing Bank, and Ithmaar Development Company, all of which are leaders in their respective fields.

Their combined activities, covering investment, private, retail, and commercial banking, private equity, Islamic insurance and assurance, equipment leasing, and real estate development, form a unique 360 degrees value chain that embraces the entire spectrum of banking and financial services. The group aims to leverage the synergies inherent in this consolidated base, to become the premier global financial services institution offering Sharia-compliant products and services. In pursuit of this challenging vision, we are committed to setting a new regional benchmark for personal and professional integrity, transparency and disclosure, and stakeholder value.

A key strategic development during the year was Ithmaar Bank's acquisition of the remaining 40 per cent stake in Shamil Bank which was publicly held. Shamil now becomes a wholly-owned subsidiary, further strengthening the synergy between the two institutions, whose activities have always complemented each other perfectly.

Ithmaar Bank posted a strong financial performance in 2007, full details of which are covered by subsequent sections of this annual report. The Bank's subsidiaries and associates all contributed significantly to the overall financial results. Summaries of their financial, business and operational achievements are included later in this annual report, so I will just mention some of the key highlights here.

Ithmaar Bank launched a number of innovative private equity transactions and strategic investments, and also initiated plans to establish an investment bank in the Kingdom of Saudi Arabia.

Shamil Bank posted record results, launched new retail, commercial and investment banking products, opened two new branches, and implemented a new core banking system.

Faisal Private Bank in Switzerland continued to expand its products and services, launching new investment vehicles focusing on attractive opportunities such as real estate in Eastern Europe and alternative energy. It has also increased its staffing levels and is working towards opening a representative office in Malaysia.

Faysal Bank Limited in Pakistan performed strongly in 2007, outpacing market growth in both deposits and advances, and adding 30 new branches and 31 new ATMs during the year.

Solidarity embarked upon a capital-raising and restructuring exercise, introduced new insurance solutions and continued its strategy of geographic expansion.

First Leasing Bank achieved its first year of profitability, further diversified its asset base, and made good progress in its plans to establish a presence in Qatar, Oman and the UAE.

Ithmaar Development Company announced details of three major development projects in the Kingdom of Bahrain, including the $1.6 billion Dilmunia, a groundbreaking 'health island' concept, and the $1.5 billion Aljazayer Beach Resort, which will give Bahrain a world class leisure facility and public beach.

Khalid Abdulla-Janahi
CHAIRMAN

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I am convinced that, above all else, it is the quality of our people that will ultimately determine the continued success of the Bank.

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As you are aware, we have always been a firm believer that banking is all about people. This is why Ithmaar Bank places such emphasis on attracting, developing and retaining the best people in the business. We practice what we preach, providing equal opportunities for advancement in a challenging work environment, where everyone, regardless of background or status, is encouraged to contribute and make a difference.

Our corporate culture embraces the values of leadership, professionalism, integrity and honesty, while recognising and rewarding performance. I am convinced that, above all else, it is the quality of our people that will ultimately determine the continued success of the Bank.

The importance we place on people is reflected in our approach to corporate social responsibility, of which the Ithmaar Education and Training Fund constitutes a main activity. In 2007, we continued to provide private education opportunities, locally and abroad, for under-privileged students across the Muslim world. A full report on the Fund's achievements to date appears later in this annual report.

Looking ahead, the momentous achievements across all areas of our operations during 2007 have provided strong impetus for the Bank's continued growth and development. As a result, we are better equipped than ever before to take advantage of new and exciting business opportunities in the Islamic banking and financial services sector across the Middle East, North Africa and South East Asia (MENASA) regions, where we will continue to strengthen our presence.

We are committed to maximising shareholder value, and to become the 'first choice' institution for employees, investors and clients. We will be distinguished not only by our products and services, but also by the way we operate, totally above board, with complete transparency and integrity, and in accordance with ethical best practice.

Finally, I would like to welcome Ithmaar Bank CEO Michael P. Lee and Kenneth Borda, who were appointed to the Board during the year. Their considerable international experience and industry expertise will be of immense value in helping to guide the future direction of the Bank.

I also congratulate Michael on a successful first year at the head of the Bank's Executive Management team. Since his appointment as CEO, he has worked diligently to attract the brightest banking talents the industry has to offer, and the fruits of his labours are yet to be fully realised.

I also take this opportunity to thank my fellow board members across the group, our shareholders, investors and clients, and the regulatory authorities of all countries in which we operate, for their support and guidance during the year.

Above all, I express my sincere appreciation to our people – the management and staff of our subsidiaries, associates and joint ventures around the world – for their loyalty and dedication, and for helping to make 2007 such a successful year for Ithmaar Bank.

Khalid Abdulla-Janahi

CHAIRMAN

CEO'S Statement

Ithmaar Bank achieved significant milestones during 2007 in building its direct institutional business capabilities. Rising income generated from the Bank's direct business activities complemented the continued growth of its subsidiaries and associates.

Ithmaar Bank achieved a consolidated record net profit of $188.3 million for 2007. Operating income increased by 173 per cent to $339.5 million. The significant contributors to the increased net profit were income from investments in financings of $181.4 million, income from investment property of $92.7 million and fees and commissions of $52.5 million. Distributions to investment account holders increased to $145.5 million, consistent with increased revenues. The net profit for 2007 of $188.3 million increased by 4 per cent over the 2006 net profit of $181.1 million. However, the 2006 results included a one-off gain of $105.5 million from the sale of a subsidiary, Islamic Investment Company of the Gulf (Bahamas) Limited. Excluding this non-recurring item, net profit for 2007 actually increased by 149 per cent, which is most encouraging, indicating that the Bank is well on its way towards achieving its long-term financial goals.

At the end of the year, total assets were a record $4.1 billion, up 23 per cent from 2006. Shareholders' equity rose by 37 per cent, from $792 million to $1.1 billion, and total equity increased by 14 per cent, from $1.1 billion to $1.3 billion. Funds under management increased by 63 per cent, from $1.1 billion to $1.7 billion. Return on average equity remained strong, at 15.6 per cent, and the cost to operating income ratio remained within industry norms, at 41 per cent.

In the light of this marked progress, the Board of Directors is recommending a cash dividend distribution of 2.5 cents per share (amounting to $53.74 million). This is in addition to the issue of 288 million bonus shares approved at the Extraordinary General Meeting held on 29 November 2007.

The Bank's shares on the Bahrain Stock Exchange performed strongly during 2007, and were one of the most liquid stocks in terms of trading volume.

A key development for Ithmaar Bank last year was its acquisition, through a share exchange, of the remaining 40 per cent in Shamil Bank which was publicly held, with Shamil Bank becoming a wholly owned, delisted subsidiary. Shamil Bank's commercial and investment banking operations are complementary to those of Ithmaar Bank's operations, and the acquisition of the Shamil Bank minority interest was another important step towards consolidating the Ithmaar banking group's businesses. We have already witnessed early signs of increased synergy, through Shamil Bank's recent collaborations with another Ithmaar subsidiary, Swiss-based Faisal Private Bank, in the offering of investment fund products. We are also, following the acquisition, reviewing the opportunities for combining some support services that are provided in-house within the Ithmaar banking group.

The Bank's private equity funds business made excellent progress in 2007. The Aldar Private Equity Fund, co-launched in 2007 with Shamil Bank and Islamic Investment Company of the Gulf, achieved its first closing of $200 million in November 2007. The Fund is designed to provide investors with access globally to alternative asset investments: it may invest in real estate, the general private equity sector, and Sharia-compliant hedge funds, with a special emphasis on the MENASA region.

The Infrastructure & Growth Capital Fund (IGCF), which is co-sponsored by Ithmaar Bank, alongside Abraaj Capital and Deutsche Bank, and which is managed by Abraaj Capital, reached its targeted size of $2 billion at its final closing in December 2007. IGCF is now the largest ever private equity fund focused on the Middle East, North Africa and South East Asia (MENASA) region, and the fund has already made several investments, one of which has already been sold, with the consideration being in the form of listed shares.

Michael P. Lee
CEO & MEMBER OF THE BOARD

"Ithmaar Bank and its subsidiaries achieved a record net profit of **$188.3 million** for 2007."

A successful private placement by Ithmaar Bank raised $185 million for Dilmunia Development Fund I LP. The funds raised are being deployed in purchasing the land and investing in the initial infrastructure works for the new $1.6 billion Dilmunia 'health island' project, which is spearheaded by Ithmaar Bank's subsidiary, Ithmaar Development Company. Reclamation work on the project is imminent, which work will enable the project to enter its next phase, when plots will be sold to investors for development. Dilmunia is set to revolutionise health care in the Kingdom of Bahrain, turning it into a regional centre for health tourism.

Meanwhile, a private placement offering to selective investors successfully raised $70 million for Ithmaar Bank's takaful associated company, Solidarity, with the result that its paid-up capital increased from $150 million to $220 million. This will facilitate the creation of two new entities, Solidarity Family Takaful and Solidarity General Takaful, both falling under the umbrella of a new holding company, Solidarity Group, and emanating from two business divisions within the existing Solidarity structure. The capital raising and new organisational structure will strengthen Solidarity's position as a leader in providing insurance solutions globally; and will allow for further strategic alliances, better performance accountability and higher efficiency, as well a more defined specialisation of business lines.

Key strategic developments in 2007 include the Bank's 23 per cent participation in the planned establishment of Ithraa Capital in the Kingdom of Saudi Arabia, subject to the approval of the Saudi Arabian Capital Markets Authority. This new investment bank will enable the Bank to capitalise upon the significant potential for investment banking activities in the large and highly liquid Saudi Arabian market.

During 2007, Ithmaar Bank met the capital call for the balance of its equity investment in Hong Kong-based CITIC International Assets Management Limited (CIAM), which focuses on real estate and other investments in the People's Republic of China.

Ithmaar Bank's key organisational achievements during 2007 include developing a strong support infrastructure. The Bank's business divisions are now supported by professional back office functions, including Human Resources, Information Technology, Financial Control, Operations, Administration and PR & Corporate Communications. As indicated above, following the acquisition of the Shamil Bank minority interest, opportunities for consolidating some support functions within the Ithmaar banking group are being explored.

During 2007, Ithmaar Bank was successful in attracting additional professionals to fill senior roles within the organisation. These include Managing Directors for Islamic Finance & Financial Institutions, and for Mergers & Acquisitions. We also appointed an Executive Director to be responsible for fund and other placements within the Private Equity Group, and another Executive Director for fund structuring and monitoring within the same Group, as well as a Chief Financial Officer (in charge of planning, managing and directing the consolidated financial accounting and reporting of the Bank and its subsidiaries and associates). In 2008, a Managing Director for the Private Equity Group has joined our team.

We are continuing to create multinational managerial and professional teams that balance international experience with regional understanding. Several more senior appointments will be made this year as the Bank continues to diversify its investment banking, private equity and capital markets business.

Our 2008 direct business development will concentrate on closing and managing various private equity funds and other proprietary initiatives which are already in process. Now that we have established the Islamic Finance & Financial Institutions Division, there will also be the prospect of raising complementary financing related to equity placements, enhancing the Bank's current fee income, which is also expected to be reinforced by the recent creation of the Mergers & Acquisitions Division.

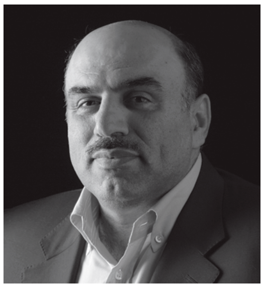
2008 will also be a very active year for Ithmaar Development Company, as it begins to implement its $3.3 billion projects portfolio. Projects include the above-mentioned Dilmunia project, the $1.5 billion Aljazayer Beach Resort and a chain of family-oriented hotels, the first of which will be located off the Kingdom of Bahrain's up-and-coming Seef District. While these developments are all located within Bahrain, Ithmaar Development Company is also planning other substantial projects elsewhere within the MENA region, and beyond.

From all angles – strategic, financial and operational – 2007 was an important foundation year for the Bank's direct business development, with the promising achievements during the year underlining the professionalism and dedication of our people. I take this opportunity to offer them my sincere thanks and appreciation for their invaluable contributions to our performance.

Ithmaar Bank has entered 2008 with additional confidence and strength, ready to achieve further milestones in the year ahead towards accomplishing our vision to be the benchmark international investment bank, operating globally from the Middle East.

Michael P. Lee

CEO & MEMBER OF THE BOARD



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Board of Directors

The Board presently has twelve directors, including six independent directors. The number of directors on the Board is established by the Bank's Memorandum and Articles of Association. The Board of Directors is headed by a Chairman, who is considered to be an independent director in accordance with the Central Bank of Bahrain's guidelines and international best practice.

As of 31 December, 2007, the Board of Directors comprised:

Khalid Abdulla-Janahi

CHAIRMAN

Mr. Janahi is the Group Chief Executive of Dar Al-Maal Al-Islami (DMI) and Chairman of Solidarity, Faisal Private Bank (Switzerland), DMI Administrative Services and Islamic Investment Company of the Gulf (Bahamas). He is also a Member of the Board of Shamil Bank and Faisal Islamic Bank of Egypt. Mr. Janahi is a Member of the Board of the Centre for International Business and Management (CIBAM), University of Cambridge, UK. A Fellow of the Institute of Chartered Accountants in England and Wales, Mr. Janahi holds a degree in Computer Science and Accountancy from the University of Manchester, UK.

Tunku Dato' Ya'acob Bin Tunku Abdullah

Prince Ya'acob is the Deputy Chairman of MAA Holdings Berhad (Malaysia), which he joined in 1999. Prior to his current position, Prince Ya'acob worked for 19 years for Malaysian Assurance Alliance Berhad, where his last position was as Chairman. He also worked at Price Waterhouse London (UK) and Malaysia, where he held the position of Assistant Manager in their offices in Kuala Lumpur. Prince Ya'acob holds a Bachelor of Science degree with Honours from the City University in London and is a Fellow of the Institute of Chartered Accountants of England and Wales.

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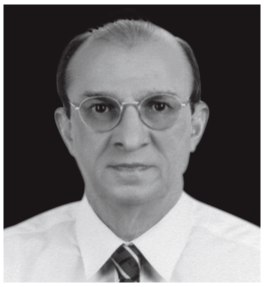

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1. Khalid Abdulla-Janahi **2.** Tunku Dato' Ya'acob Bin Tunku Abdullah
3. Abdelhameed Abou Moussa **4.** Mohamed Bin Saif Al Mezrouei **5.** Farook Bengali
6. Kenneth C. Borda **7.** Shaikh Mohammed Youseef El Khereiji

Abdelhameed Abou Moussa

Mr. Abou Moussa is the Governor of Faisal Islamic Bank of Egypt, which he joined in 1977. Prior to his current position, Mr. Abou Moussa worked in the Central Bank of Egypt for 16 years. He holds a Bachelor of Science in Accounting and a Diploma in Finance from Cairo University in Egypt, and a Diploma in Banking Economics from Lwegi Boconi University in Milano, Italy. He is a Member of the coordinating council that determines the monetary and fiscal policy objectives of the Egyptian economy.

Mohamed Bin Saif Al Mezrouei

Mr. Al Mezrouei is the Chief Executive Officer of the UAE Offsets Group. He joined the group in 1994 as a project manager and was appointed Deputy Chairman in 1996 and Member of the Board in early 2000. Prior to joining the group he was the Human Resources Manager of Abu Dhabi National Oil Company (ADNOC) for eight years. Mr. Al Mezrouei is also a Member of the Board of Mubadala Development Company and Chairman of the National Central Cooling Company (Tabreed). He also serves on the Board of Directors of other prominent entities such as Dolphin Energy Limited, Abu Dhabi Tourism Authority, Abu Dhabi Water & Electricity Authority, Al Ain Zoo, the Emirates Media Incorporation and Tourism & Development Investment Company. Mr. Al Mezrouei has a degree in Business Administration from the Laverne University in the US.

Farook Bengali

Mr. Bengali is a Member of the Board of Shamil Bank. He is the former President and Chief Executive Officer of Faysal Bank Limited (FBL). Prior to joining FBL in 1996, Mr. Bengali worked for almost 30 years for Standard Chartered Bank, Pakistan where his last position was Chief Executive, with overall responsibility for the operations of the Bank and its branches throughout the country. Mr. Bengali is a Fellow of the Chartered Institute of Bankers, UK and of the Institute of Bankers in Pakistan and holds Masters in both Economics and Law.

Kenneth C. Borda

Mr. Borda was formerly the Chief Executive Officer of Deutsche Bank AG, Middle East and North Africa. He retired in April of 2007. He had also acted as Chairman of Deutsche Bank Asia Pacific (excluding Japan). During an 18 year career with Deutsche Bank, he held several key management posts, including Regional CEO Asia Pacific, based in Hong Kong, and CEO Australia and New Zealand, based in Sydney. Mr. Borda was a Board Member of SFE Corporation (the listed national futures exchange in Australia) for more than five years until its acquisition by Australian Stock Exchange Limited in July 2006. In February 2007, he joined the Board of Ithmaar, as well as the boards of both Fullerton Funds Management, the asset management arm of Temasek, in Singapore, and the Australian oil and gas exploration and production company, Santos Limited.

Shaikh Mohammed Youseef El Khereiji

Shaikh Mohammed comes from one of the leading merchant families in the Kingdom of Saudi Arabia. He studied in Switzerland and the United Kingdom and graduated with an MBA in Marketing and Finance. He started his career as a consultant and financial adviser for, inter alia, Prudential Bache and BNP Paribas in Geneva. He is currently Chairman of Global Investment and Marketing SA (Geneva) and Creative Investment and Marketing SA. He is Chief Financial Officer of El Khereiji Group, Chairman of SAGE Capital Management Group in Bahrain and of Marriott European Hotel Operating Co. Ltd. Shaikh Mohammed is also Honorary Chairman of the Swiss Red Cross and is an active contributor to many charitable entities. He holds many other prominent executive board positions in Europe and the Middle East.

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Shaikha Hissah Bint Saad Al-Sabah

Shaikha Hissah is the President of the Council of Arab Businesswomen. She has had a long history in the Kuwait Government and private voluntary service, including: Department of Medical Services, Research and Development, Military Hospital, Ministry of Defence, State of Kuwait; Adviser, Defence Minister's Office, State of Kuwait; Chairperson of the Narcotics Control Committee; Kuwait Volunteers Women Society; Kuwait Businesswomen Committee; Arab African Women's Council; Honorary Chairperson, Arab Federation of Non-Government Societies for Addiction Prevention; Deputy Chairperson, Kuwait Narcotics Control Committee; and Member, National Committee for Narcotics Control and International Council of Alcohol and Addiction. Shaikha Hissah studied Public Administration and Political Science at the American University of Beirut, Lebanon.

Khalil Nooruddin

Mr. Nooruddin was the Director of the Bahrain Institute of Banking and Finance until he resigned in 2007. Prior to assuming that assignment in 2004, Mr. Nooruddin worked for 20 years as a corporate and investment banker. His last assignment in this field was with Investcorp Bank, where he served as a Member of the firm's Management Committee for 10 years. Before Investcorp, he served as a corporate banker with Chase Manhattan Bank in Bahrain and as an investment banking professional with Chase Investors Management Corporation and UBS Asset Management in London and Zurich. Before his banking career, he worked as an operations research analyst with Bahrain Petroleum Company (Bapco) in Bahrain and Caltex Petroleum Corporation in New York. Mr. Nooruddin is a Chartered Financial Analyst and holds a Master of Science in Quantitative Analysis from Stern Business School, New York University and a Bachelor of Science in Systems Engineering from the University of Petroleum and Minerals, Kingdom of Saudi Arabia. He is an active member of several civil and professional societies in the Kingdom of Bahrain.

Ziad Hasan Rawashdeh

Mr. Rawashdeh is a Board Member of Shamil Bank, Solidarity and Faisal Islamic Bank of Egypt. He is the Group Chief Operating Officer of DMI and Vice Chairman of Faisal Private Bank SA (Switzerland). He is also Chairman or a Board Member of several other DMI Group subsidiaries. Previous positions include Chief Executive Officer of Faisal Private Bank SA (Switzerland) and Managing Director of Islamic Investment Company of the Gulf (IICG), as well as several key positions within the DMI Group and at other financial institutions. A Fellow of the Arab Institute for Banking and Financial Studies, Mr. Rawashdeh holds a BSc in Economics.

Graham Roderick Walker

Mr. Walker is the Finance Director of Ithmaar Bank and the Group Head of Finance and Risk Management of DMI. Prior to joining DMI in 2000, Mr. Walker held various senior management positions with several major international financial institutions, including HSBC, Standard Chartered Bank and Foreign & Colonial Management Limited. He has wide ranging experience in banking and financial services. He is a Member of the Institute of Chartered Accountants of Scotland.


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8. Shaikha Hissah Bint Saad Al-Sabah **9.** Khalil Nooruddin **10.** Ziad Hasan Rawashdeh
11. Graham Roderick Walker **12.** Michael P. Lee

Michael P. Lee

CEO & MEMBER OF THE BOARD

Mr. Lee has over 35 years of experience as an international investment banker serving multilateral, governmental, corporate, financial institutional and high net worth clients. In his earlier career, with assignments based in London, Hong Kong and New York, he served investment banking clients in West and Eastern Europe, Africa, Asia Pacific, North and South America. Immediately prior to joining Ithmaar, he was Deputy Chairman and Managing Director of Emerging Markets Partnership (Bahrain) BSC(c), the general partner and manager of the $730.5 million Islamic Development Bank (IDB) Infrastructure Fund. This pioneering and successful regional private equity fund, headquartered in Bahrain and investing in private sector infrastructure in the Muslim world, was co-founded by IDB, DMI and EMP. After graduate training at Chase Manhattan Bank, Mr. Lee started his investment banking career at Merrill Lynch in 1973, spending over 10 years in London, Hong Kong and New York in commercial and investment banking, and general management. From 1979-81, he was Director of Corporate Development, Merrill Lynch International & Co., New York and, from 1981-84, he headed Merrill Lynch's international investment banking group responsible for financial institutions/private placements, becoming a Managing Director of Merrill Lynch-White Weld Capital Markets Group. From 1984-88, Mr. Lee was the Chief Executive Officer of Dean Witter Capital Markets International Ltd., London, covering capital markets and investment banking, and was also a Managing Director-Corporate Finance of Dean Witter Reynolds Inc., New York. In 1992, Mr. Lee became a senior adviser at Bahrain's Ministry of Finance & National Economy, providing inter alia strategic advice on the development and regulation of the Bahrain International Financial Centre and on investments. He has now lived in Bahrain for 16 years. Mr. Lee holds an MA (Honours) degree in Philosophy, Politics and Economics from the University of Oxford.

MEETINGS

In accordance with its Articles of Association, the Board of directors meets at least four times a year and the Board expects each director to attend at least 50 per cent of all Board meetings and meetings of committees on which they serve.

Executive Management

STANDING: (left to right) Maysan Al-Maskati, Nayla Asgharali, Michael McKinlay, Michael P. Lee, Scott A. Creswell and Andrew Pocock

SITTING: (left to right) Jassim A. K. Salman, Masood Tyabji, Ahmed Abdul Rahim, Ravindra Khot, Salman bin Ahmad Al Khalifa and Mohammad Ali

Missing from the picture: Mohammad Khan Hoti and Carolyn Prowse

Michael P. Lee

CEO & MEMBER OF THE BOARD

Please see Mr. Lee's biographical details in the Board of Directors section.

Salman bin Ahmad Al Khalifa

MANAGING DIRECTOR, GROUP BUSINESS DEVELOPMENT

Prior to joining the Bank, Salman held a range of positions within the private and public sectors, both regionally and internationally. He previously served as Director of Banking Services at the Central Bank of Bahrain (formerly the Bahrain Monetary Agency) and has held the position of Vice Chairman of the International Islamic Financial Market, one of the core infrastructure institutions of the Islamic Banking and Finance Industry. During his tenures at Barclays Capital and Bear Stearns in London, Salman managed a range of investment banking relationships and marketed various securities and structured products to Middle East markets. Salman has a Bachelor of Science in Finance from the American University, Washington DC.

Andrew Pocock

MANAGING DIRECTOR, PRIVATE EQUITY

Mr. Pocock joined Ithmaar Bank in January, 2008, bringing extensive experience in private equity, and in international investment and commercial banking acquired from varied assignments in Europe, the Americas, the Far East and the Middle East. During his career, Mr. Pocock has been an Executive Director of a leading international merchant bank, Samuel Montagu and Co. in London (now part of HSBC Group); undertook advisory assignments for the World Bank; and headed the European business from London of Gulf International Bank (GIB), from 1994 to 2000, when he was appointed GIB's Head of Banking in Bahrain.

... Andrew Pocock

Subsequently, as a senior investment Director with Emerging Markets Partnership (Bahrain), Mr. Pocock was responsible for some of the large, successful investments in the $730.5 million Islamic Development Bank Infrastructure Fund. Prior to his current appointment, Mr. Pocock served at Gulf One Investment Bank where, as Managing Director, Infrastructure, he was the architect of a number of private equity infrastructure initiatives.

Mr. Pocock began his career with Bank of London & South America, serving in Peru and Uruguay, followed by several years with J Henry Schroder Wagg & Co, London-based merchant bankers, and with Scandinavian Bank - in London, Hong Kong, Singapore, and in Bahrain where, from 1978-1980, he was Regional CEO and Head of the OBU Branch.

Carolyn Prowse

MANAGING DIRECTOR, MERGERS & ACQUISITIONS

An Oxford University graduate, Ms. Prowse spent 10 years at British Airways Plc, most recently as Senior Manager, Investments & Joint Ventures, and was based in London. Her responsibilities included reviewing, structuring and negotiating all types of corporate transactions, including acquisitions, disposals, mergers, joint ventures and alliances. A British national, Ms. Prowse also played a key role in restructuring parts of the BA Group in her 10 years there. Prior to BA, Ms. Prowse worked for LEK LLP, a consulting firm specialising in corporate strategy, mergers and acquisitions and privatisations, where her work included the privatisation of the UK railways. At Ithmaar Bank, apart from Mergers & Acquisitions, she also has investment banking responsibility for the transportation sector.

Mohammad Khan Hoti

MANAGING DIRECTOR, GENERAL INVESTMENT BANKING

Prior to joining Ithmaar Bank, Mr. Hoti was the General Manager, Investment Banking of Faysal Bank Limited, which he joined in 1996. He has wide experience of both commercial and investment banking and has held senior positions in Pakistan and the Middle East with US and regional banks. Mr. Hoti holds an MBA from UCLA Graduate School of Management and a BSc in Economics and Management from New York University.

Masood Tyabji

MANAGING DIRECTOR, ISLAMIC FINANCE AND FINANCIAL INSTITUTIONS

With 16 years of experience in the banking industry, Mr. Tyabji has broad experience in leading Islamic finance business lines at international banks. Over the years, he has both overseen and been personally involved in structuring, closing and distributing complex transactions, including many pioneering Sharia-compliant financings. Mr Tyabji has long-established relationships with major corporations, financial institutions, GCC corporate families and key Sharia scholars in the region. Immediately prior to joining the Bank, he was Head of Islamic Banking at Gulf International Bank (GIB), where he scaled GIB's Islamic Banking business to league table levels within the GCC. Before that Mr Tyabji worked for HSBC and Citibank at various locations, where he worked on a number of groundbreaking Islamic financing transactions. A long-time Gulf resident, he holds a Master of Business Administration from the University of Karachi.

Ahmed Abdul Rahim

MANAGING DIRECTOR, GROUP SUPPORT

A veteran of Bahrain's banking industry, Mr. Abdul Rahim joined Ithmaar Bank in March 2007 following a successful stint at its subsidiary Shamil Bank, where he was General Manager, Support Group since June 2006. Coming under his direct supervision at Ithmaar Bank are Financial Control, IT & Operations, Human Resources and PR & Corporate Communications. Mr. Abdul Rahim had previously worked for 28 years for National Bank of Bahrain at various executive levels, including as Manager FX and Funding, Chief Internal Auditor and finally Assistant General Manager, Corporate Services. He holds an MBA from the University of Glamorgan, Wales (UK), and is an Associate in Financial Accounting from the Institute of Financial Accountants, London (UK). He also holds an Executive Management Diploma from University of Bahrain and an Advance Banking Diploma from the Bahrain Institute of Banking and Finance.

Mohammad Ali

GROUP CHIEF AUDITOR

Mr. Ali joined Ithmaar Bank as Group Chief Internal Auditor in August 2007. Prior to that, he worked for DMI Administrative Services in Geneva, Switzerland for ten years as Director, Internal Audit, responsible for overseeing the auditing activities of the group companies in Switzerland, Saudi Arabia, Bahrain and Pakistan. Mr. Ali has international audit experience having worked as an Audit Manager for Bank of Credit in the US and a Contract Specialist for the multinational construction company Bechtel in Saudi Arabia. He was a Senior Manager for Audit at the Hub Power Company (HUBCO) in Pakistan before joining Al-Faysal Investment Bank in Pakistan as Executive Vice-President, Audit. He holds an MBA from Western Illinois University and is a Member of the American Institute of Certified Public Accountants (AICPA).

Scott A. Creswell

GENERAL COUNSEL & COMPANY SECRETARY

Mr. Creswell joined DMI Switzerland in 1986, and for ten years was senior legal counsel in the legal department. Since 1997, he has been based in Bahrain and is currently the head of the legal department at Ithmaar Bank. Prior to joining DMI, Mr. Creswell practised law in Chicago, Illinois and is currently admitted to practise before a number of courts, including the Illinois Supreme Court and the United States Supreme Court.

Ravindra Khot

GROUP CHIEF FINANCIAL OFFICER

Mr. Khot is in charge of consolidated financial, regulatory and management reporting, as well as the annual budget process. He is also responsible for provision of proactive and key support in the Bank's development strategy and business plan, management decision-making, liquidity planning and oversight of the performance management, strategies and budgets. Mr. Khot has 21 years of experience in investment banking and the financial services industry. Prior to joining Ithmaar, he held the position of Vice President, Financial Administration at TAIB Bank. His other key positions include Senior Manager, Financial Services at PricewaterhouseCoopers and Principal Consultant, Consulting at i-flex Solutions. He started his professional career in 1986 with Price Waterhouse. During his career, he has been responsible for overseas assignments in the US, Latin America, the Middle East and India. He is a Fellow of the Institute of Chartered Accountants of India.

Maysan Al-Maskati

EXECUTIVE DIRECTOR, PRIVATE EQUITY

Mr. Al-Maskati began his investment banking career in 1998 at leading international private equity specialist Emerging Markets Partnership (EMP), whose Bahrain subsidiary is the General Partner and Manager of the $730.5 million Islamic Development Bank (IDB) Infrastructure Fund. This pioneering regional private equity fund, headquartered in the Kingdom of Bahrain and investing in private sector infrastructure, was co-founded by IDB, Dar Al-Maal Al-Islami (DMI) Trust and EMP. During his tenure with EMP, Mr. Al-Maskati was actively involved, alongside senior management, in both closing the fund and in making large investments in the power and petrochemical sectors, and also contributed to effecting investments in other sectors. Prior to joining Ithmaar Bank, Mr. Al-Maskati worked at Gulf One Investment Bank as Vice President, Infrastructure, and Masar Advisory as Private Equity Director. Mr. Al Maskati holds a BSc in Industrial and Manufacturing Systems Engineering from Kansas State University, US.

Michael McKinlay

EXECUTIVE DIRECTOR, PRIVATE EQUITY

Prior to joining Ithmaar Bank, Mr. McKinlay founded and led Stormberg Partners WLL, a GCC based advisory firm directed at the Chairmen and CEOs of leading family groups in the region. Before that, Mr. McKinlay had spent 15 years in wealth management 'start ups', working inter alia for Credit Suisse and HSBC, establishing operations in the Kingdom of Saudi Arabia, Switzerland, Jersey and the UAE. He also served 10 years as a transactional commercial banker with what is now JP Morgan in positions of country leadership. Mr. McKinlay has 20 years of experience in the GCC dealing with investors in a range of asset classes. He has an MBA from Cranfield School of Management and is an Alumnus of the London Business School's Investment Management Programme.

Jassim Abdul Karim Salman

EXECUTIVE DIRECTOR, IT & OPERATIONS

Mr. Salman has experience in both business and technical disciplines. Before joining Ithmaar Bank, he was a Senior Advisor on IT & Operations to the Director General of the Dubai Financial Markets (DFM). He also contributed to the Bahrain Capital Market industry, with extensive responsibilities for the planning and operations of the Bahrain Central Securities Depository, the management of Advanced Trading, Clearing and Settlement systems, as well as the practical management of IT functions at the Bahrain Stock Exchange. Other areas of experience include 15 years in banking, electrical and electronic engineering and telecommunications. Mr. Salman holds a Higher National Diploma in Electrical and Electronic Engineering from the Derby Lonsdale University in Derby, UK.

Nayla A. Asgharali

DIRECTOR, COMPLIANCE

Ms. Asgharali joined Ithmaar Bank in February 2007. Prior to joining the Bank, Ms. Asgharali was the Head of Compliance, MLRO & Head of Operational Risk at Bank Muscat International and Head of Internal Audit at Futurebank. She has also worked for the Bahrain Saudi Bank, as a senior officer in the Internal Audit department. Before joining the Central Bank of Bahrain in 2004 as Bank Analyst in the Banking Supervision Directorate, she worked at Ernst & Young as an internal auditor for three years. Ms. Asgharali is a Certified Financial Services Auditor (CFSA) and a Certified Internal Auditor (CIA), with experience in carrying out risk based audits, control evaluation and setting up and managing internal audit functions. Ms. Asgharali has a Bachelor of Science from the University of Bahrain and is a Certified Anti-Money Laundering Specialist (CAMS).

Management Review of Operations

This review covers Ithmaar Bank's operational progress during 2007. The Bank's core business activities are underwriting (equity and other financings), private equity (structuring, participation and portfolio management), advisory services (capital markets, mergers and acquisitions), project financing, investments and asset management.

Ithmaar Bank made remarkable progress during the year, with emphasis being placed upon building the Bank's institutional capability, securing new business, and building its brand image – all in pursuit of its vision of being the benchmark international investment bank operating globally from the Middle East.

The Bank is seeking to be a leading 'regional architect' and manager of new private equity funds, whether for funds wholly managed by Ithmaar Bank, or for funds co-managed with other world class investment specialists. It is also further extending its network of relationships with both institutional investors and leading investment banks around the world. In 2007, the Bank established a strong pipeline of future business, and it is now in proactive discussions with regional and other institutional clients pursuing alternative investment opportunities, as well as with clients who are contemplating mergers and acquisitions, or who may be raising equity or other financing in 2008/9.

Group Consolidation

ACQUISITION OF SHAMIL BANK

In 2007, Ithmaar Bank acquired the 40 per cent minority interest in Shamil Bank which was publicly held, thereby making Shamil a 100 per cent subsidiary. The Extraordinary General Meetings (EGMs) of Ithmaar Bank and Shamil Bank were held on 29 November 2007. Two independent firms were engaged to perform valuations for Ithmaar Bank and Shamil Bank. The share exchange proposal, of 12 shares of Ithmaar Bank for 10 shares of Shamil Bank held by the remaining 40 per cent Shamil Bank minority interest, was approved by both of the EGMs. Accordingly, Ithmaar Bank issued 446.5 million new Ithmaar Bank shares to Shamil Bank minority shareholders. The Ithmaar Bank EGM also approved the issue of 288 million bonus shares to existing Ithmaar Bank shareholders (as at 28 November 2007).

Private Equity Group

The private equity activities of Ithmaar Bank during 2007 encompassed direct investments, the development and launching of funds, and an active role in the placing of proprietary and third party investments.

ALDAR PRIVATE EQUITY FUND

Launched in 2007 by Ithmaar Bank, together with Shamil Bank and Islamic Investment Company of the Gulf (Bahamas), this Sharia-compliant fund achieved its first closing target of $200 million in November 2007. Aldar Private Equity Fund, which has five initial investors, provides investors with access to alternative asset investments globally, covering real estate, the general private equity sector, and Sharia-compliant hedge funds, with a special emphasis on the high growth region of the Middle East, North Africa and South East Asia (MENASA).

INFRASTRUCTURE & GROWTH CAPITAL FUND (IGCF)

Ithmaar Bank is a co-sponsor of IGCF, alongside Abraaj Capital and Deutsche Bank. The Bank holds a 24.5 per cent interest in the IGCF General Partner. IGCF, which is managed by Abraaj Capital, reached the targeted $2 billion fund size at the final closing in December 2007. IGCF is now the largest ever private equity fund focused on the Middle East, North Africa and South East Asia (MENASA) region. The predominant focus of IGCF is to take majority or minority stakes in infrastructure projects and growth capital investment opportunities, and to participate in large scale privatisations and buyouts. Sector focus includes utilities, petrochemicals, oil and gas, industrials, transportation, ports, and social infrastructure, such as education and healthcare.

IGCF made several significant investments during 2007, including the acquisition of Egyptian Fertilisers Company – the largest private equity-led leveraged buyout in the history of the MENA region: in February, 2008, it was announced that the fund has sold this investment, with the consideration being in the form of listed shares.

CITIC INTERNATIONAL ASSETS MANAGEMENT LTD

CITIC International Assets Management Ltd (CIAM) is part of the CITIC Group, a diversified conglomerate wholly owned by the State Council of the People's Republic of China. In 2007, Ithmaar's total investment in CITIC was increased to $61 million, from $24 million in 2006, and the Bank now owns 20 per cent of both the voting and equity capital of the company. CIAM's principal activity is to invest in companies and projects in China, both for its own account and on behalf of clients. Established in 2002 to specialise in distressed asset management, the current portfolio of CIAM includes direct investments in real estate, high technology, health, retail and industrial projects.

PRIVATE PLACEMENTS

Following organisational realignment during the year, equity placement for funds and private equity transactions became the responsibility of a Private Placement Division within the Private Equity Group. Successful placements raised equity capital for Ithmaar's target client groups. These included selective third party world class alternative asset managers, such as an Australasian private equity fund manager which mandated Ithmaar to assist with the placement of a new buy-out fund, predominantly to be placed with the fund manager's own Australasia investment clients: Ithmaar introduced to the fund selective investors from the Middle East and Asia. Other successful equity placements have also been concluded for private equity funds where Ithmaar is the general partner, or a shareholder in the fund's general partner, as well as for client enterprises, such as the 2007 equity underwriting and placement which raised the paid-up capital for the 33 per cent Ithmaar affiliate, Solidarity, from $150 million to $220 million. Looking ahead, the Division will broaden its target investor footprint, specifically in the key markets where Ithmaar wishes to reach new investors. In 2008, the Division will increase its headcount, and broaden the range of investment offerings to existing and target investors, in line with Ithmaar's aspirations to be the benchmark international investment bank, operating globally from the Middle East .

> The Bank is seeking to be a leading 'regional architect' and manager of new private equity funds.

NEW DEVELOPMENTS

Ithmaar Bank's Private Equity Group's investment business will concentrate in the near term on the development, launch and management of various sector-specific investment funds and vehicles, in some cases in partnership with prestigious international partners. Some of these initiatives will address global opportunities in assets that are not widely addressed by the private equity investment community. Private equity business is expected to make an important contribution to Ithmaar's financial performance, and the cadre of professional staff required to implement these initiatives is being expanded through the recruitment of additional experienced private equity practitioners.

Group Business Development

With emphasis on strengthening Ithmaar Bank's regional and global client reach, some reorganisation was effected towards the end of the year. A Group Business Development function is now being headed by Managing Director, Shaikh Salman bin Ahmad Al Khalifa, working in close association with the Chairman and with the CEO & Member of the Board. The mandate is to help develop and maintain group level senior relationships with selective supranationals, governments, financial institutions, corporates and high net worth individuals.

Ithmaar Bank's private banking products are now being offered through Shamil Bank's Private Banking Division and Faisal Private Bank, a first step towards the cross-fertilisation of the business development activities of the Ithmaar banking group.

Ithmaar Bank will continue to strengthen its business, especially in the Middle East, North Africa, and South East Asia (MENASA) region, with sectoral focus on energy, natural resources and related industries, real estate, leisure, healthcare, financial institutions, transportation, telecommunications and information technology.

Investment Banking Group (IBG)

During 2007, IBG was formed, initially to include the three divisions, General Investment Banking, Mergers & Acquisitions and Islamic Finance & Financial Institutions. All in all, IBG is involved in an array of M&A, private placement, equity and complementary financing capital market activity and general advisory mandates catering to both intra-group and external clients. IBG and its predecessor, the Investments Department, led private equity placements for First Leasing Bank and Solidarity, respectively increasing the capital of the former from $11 million to circa $100 million, and the latter from $150 million to $220 million. The Mergers & Acquisitions Division, established in August 2007, offers advice on all types of corporate transactions, including acquisitions, divestitures, joint ventures and strategic alliances. The Islamic Finance & Financial Institutions Division, armed with the additional responsibility of developing asset-backed funds, expects to be launching its first such offering during the course of 2008.

Ithmaar Development Company

Ithmaar Development Company is an Ithmaar Bank subsidiary, which was established to manage and execute major development projects, including real estate, infrastructure, resorts, hotels, medical facilities and commercial centres. The core activities of Ithmaar Development Company include management and development of property, development management services and facility management services. The Company's current real estate portfolio comprises three innovative projects in the Kingdom of Bahrain, with estimated value of $3.3 billion, which are outlined below.

DILMUNIA

This innovative $1.6 billion project will provide international-standard health and wellness facilities, set in a resort-style environment on a man-made island in north-east Bahrain. Dilmunia will include specialist centres for diagnostics, nutrition, diabetes, aesthetic surgery, women and children, sports medicine and alternative medicine. This 'health island' will feature deluxe spas, boutique hotels, residential clusters, commercial facilities and recreational amenities. Ithmaar Bank raised $185 million for Dilmunia Development Fund I LP in 2007, which will finance the purchase of land and invest in the initial infrastructure works for the project. In the next phase, plots will be sold to investors for development.

HOTELS COMPANY

Ithmaar Development Company plans to establish a chain of luxury Sharia-compliant hotels within and outside of the GCC region. The first project will be a $175 million property, comprising a hotel tower and office tower, located off Bahrain's attractive Seef District.

ALJAZAYER BEACH RESORT

This $1.5 billion project will develop Aljazayer beach, located in southwest Bahrain, into a luxury leisure and family tourism and entertainment facility. The Resort will include public and private beaches, two hotels, a marina, a theme park and water park, a cultural centre, commercial district, residential units and beach chalets.

Human Resources, IT and other organisational developments

Throughout 2007, Ithmaar Bank invested heavily in developing a robust organisational infrastructure to support its ambitious plans for business expansion. The Bank further strengthened its corporate governance, risk management, internal controls, and policies and procedures. In addition, progress was made in developing key support functions, such as Human Resources (HR), Information Technology (IT), Financial Controls, Operations, Administration and PR & Corporate Communications.

Besides recruitment, key HR achievements include the development of an HR policy, a succession plan, job descriptions, a performance appraisal system and a training requirements analysis, together with the implementation of an HR system covering payroll, personal information, and online internal documentation.

The Bank recognises the crucial role that IT plays in supporting its current business activities and expansion plans. Accordingly, the implementation of an advanced IT infrastructure commenced during the year, with an estimated cost of $1.5 million for the first year. This coincided with the relocation of the Bank to new premises in the Seef District.

Subsidiaries & Associates Overview

Shamil Bank

Shamil Bank is a leading Islamic commercial and investment bank based in Bahrain. The Bank provides a diverse range of Sharia-compliant products and services that cater to the financing and investment needs of individuals and institutions.

Strategically, the acquisition by Ithmaar Bank of the remaining 40 per cent of Shamil Bank shares, which were publicly held, further strengthened the synergy between the two institutions, whose activities have always complemented each other.

Shamil Bank performed well during 2007, posting a net profit of $73.5 million, while its contribution to Ithmaar's profits stood at $46 million, a $25.2 million jump compared to last year. Total assets rose 40 per cent to $1 billion, from $780 million at the close of 2006. Total funds under management increased to $782 million from $755 million.

With the opening of two new branches and the installation of three additional ATMs during 2007, the Bank's network now comprises nine branches and 18 ATMs across the Kingdom of Bahrain. In addition, a marketing agreement was signed with Ithmaar Bank associate Solidarity to sell its car insurance products as a value-added feature to the Shamil Car Finance campaign. New commercial banking products launched during the year include an innovative car financing package, and the Nibrass Financing Scheme for small-to-medium enterprises (SMEs), which is a groundbreaking joint initiative with the Kingdom's Labour Fund.

The Bank launched three new investment funds during the year: the capital-protected Shamil Navigator Modaraba, with exposure to two profiles of diversified assets comprising global Islamic equities and commodities; the $90 million Shamil Bosphorus Modaraba that will invest in residential and mixed-use real estate developments in Turkey; and Aldar Fund, which provides investors with access to alternative asset investments globally.

In addition, the Bank successfully implemented its new core banking system in 2007. This has resulted in improved business processes, reduced costs and greater responsiveness to customers.

www.shamilbank.net

Faisal Private Bank (FPB)

FPB, a wholly owned subsidiary of Ithmaar Bank since 29 November, 2007, posted a net profit of $6.7 million. Its contribution to Ithmaar Bank's profits stood at $5.7 million, an increase of $5.1 million as compared to last year.

Total assets stood at $134.6 million, compared to $80.7 million at the end of 2006. Total funds under management increased to $441.2 million, up from $304.5 million as at the end of 2006.

In the last year, FPB continued its focus on expanding its services and products through the launch of products such as a Real Estate fund focusing on Eastern Europe, and an alternative energy investment vehicle through a company called Solara. In 2007, FPB also began actively planning, at an early stage, the opening of a representative office in Malaysia. As a part of its growth plan, FPB increased its staffing levels and completed the implementation of two new IT systems; Apsys and Microsoft CRM.

To create more awareness of the bank and to support the new generation, FPB became the official sponsor of the GP2 Asia Series race driver Romain Grosjean, a member of Team ART GRAND Prix.

www.faisalfinance.com

Faisal Private Bank

Faysal Bank Limited (FBL)

The net profit of FBL, in which Ithmaar now has 65.7 per cent equity interest since 29 November 2007, rose to $57.9 million, while its contribution to Ithmaar Bank's profits stood at $31.6 million, an increase of $21.6 million as compared to last year. Total assets increased to $2.3 billion, up from $1.9 billion as at the end of 2006.

FBL expanded its network, adding 30 new branches and 31 new ATMs during the year. FBL now has 105 branches and 81 ATMs across Pakistan. The Bank continued to do well in 2007, beating market growth in both deposits and advances.

www.faysalbank.com

FAYSAL BANK

Solidarity Group

Solidarity is one of the largest takaful (Islamic insurance) companies in the world. The Company provides General and Family takaful products and services which comply with the principles of the Islamic Sharia, around the globe.

Solidarity, in which Ithmaar Bank holds 33.8 per cent equity interest as at 31 December, 2007, posted a net profit of $7 million, as compared to $5.4 million for 2006. Gross revenue for 2007 was at $20.5 million, up from $16 million during 2006.

The significant strategic progress, record financial performance and strong operational achievements by Solidarity in 2007 illustrate that the Company has entered a new and exciting phase in its development. The increase in paid up capital to $220 million has provided added impetus to the Company's strategy of growing its presence in its home markets, and into previously untapped foreign markets, through investments in new ventures and acquisitions. As a result of successful geographic expansion initiatives during 2007, Solidarity now has a presence, either existing or in progress, in seven countries around the world.

The proposed evolution of Solidarity's corporate structure into a holding company structure will provide a strong platform for future business growth and strategic expansion. The new structure will enable Solidarity to enhance the inherent synergies between different parts of the Company, as well as improving economies of scale through corporate shared services.

Solidarity's strong business performance during the year was highlighted by new product introductions, widened distribution channels, enhanced levels of customer service, and a continued investment in technology. New products include the launch of SOLIDFoundation home finance (mortgage) protection, the Corporate Savings Scheme Takaful Policy, and Directors' and Officers' Liability cover, the latter in collaboration with Chubb.

New distribution channels were developed through the signing of marketing agreements with Shamil Bank, Sakana and the ARG Group. The Company opened two new Customer Care Centres at Seef Mall and KFH AutoMall, and also introduced a new 24x7 Motor Claims Call Centre, with a toll-free number, in order to provide enhanced levels of customer service.

www.solidarity.cc

First Leasing Bank (FLB)

FLB is the first bank in the GCC dedicated to the introduction and expansion of high quality equipment leasing in the region. The Bank offers finance and operating leasing solutions for the industrial, manufacturing, medical, printing and publishing, telecommunications, IT, transportation and marine industries, among others.

FLB, in which Ithmaar Bank holds a 21.3 per cent equity interest, posted a net profit of $4.5 million in 2007. Total assets increased to $102 million, from $98 million as at the end of 2006. Total operating income increased by more than four times to $7.8 million, compared to $1.4 million during 2006.

The record achievements of First Leasing Bank (FLB) in 2007 underline the Bank's successful development from its early seed years to a new phase of growth and profitability. The increase in FLB's capital to $100 million at the end of 2006 provided a significant boost to the business activities of the Bank during 2007. Key developments included arranging higher ticket transactions for larger corporate clients, expanding the asset base and finalising plans to establish a presence in new regional markets.

With the ability to take on higher exposures, the average transaction size rose almost five-fold during the year, with many larger deals now ranging between $5 and $10 million. These were arranged by inviting other financial institutions to participate in the deal on a club basis, or by FLB underwriting the deal and then selling down to other institutions.

With its move into new sectors, the Bank successfully expanded its portfolio with more varied assets, including 'green' technology, printing presses, and manufacturing process equipment for the first time. FLB is also looking at a variety of investments with which to balance its portfolio further. These include some specific, almost boutique-type, real estate investments and small projects, but based on concepts more consistent with equipment leasing. An example would be not only leasing the equipment inside a warehouse, but also financing the warehouse itself.

The Bank's current main markets are Bahrain, Kuwait and UAE, but due to the injection of new capital, the Bank is planning to expand into Qatar and Oman, operating either singly or through a local partner, and also to open an office in the UAE. Discussions have also started with a number of interested parties about a joint venture in Saudi Arabia.

www.1stleasingbank.com

بنك الإجارة الأول
FIRST LEASING BANK

Ithmaar Development Company

Ithmaar Development Company, which commenced its operations during 2007, posted a net profit of $34 million. The Company is the developer and manager of Ithmaar Bank's infrastructure development projects and other high quality real estate and tourism-related ventures. Ithmaar Development Company also intends to provide real estate consultancy services and facility management services, among others. The company's current $3.3 billion projects portfolio mainly includes three major projects in the Kingdom of Bahrain, which it is developing and executing in partnership with other entities.

DILMUNIA HEALTH ISLAND

The $1.6 billion Health Island Project (Dilmunia) entails the creation of international-standard health and wellness facilities in a resort-style environment. Dilmunia, which will be constructed on a 125-hectare man-made island on the North Eastern coast of Bahrain, will include state-of-the-art diagnostic centres and facilities catering to nutrition and diabetes, plastic surgery and aesthetic medicine, women's and children's health, alternative medicine and sports medicine. Dilmunia will also include deluxe spas and boutique hotels, as well as residential clusters, commercial facilities and recreational amenities.

HOTEL & OFFICE TOWER PROJECT

The $175 million Hotel/Office Tower Project, comprising a hotel tower, serviced apartments and an office tower, is located in the Seef District of Manama. The 150-room hotel, with 50 serviced apartments, will be a luxurious family-oriented Sharia-compliant facility, which is intended to be the first of a chain of such hotels to be developed in the region. The Tower Project will also provide 10,000 square metres of office space.

ALJAZAYER BEACH RESORT

The $1.5 billion Aljazayer Beach Resort project involves the creation of a world class leisure and family tourism and entertainment facility on the southwestern coast of Bahrain. The facilities will include public beaches, several hotels, marinas, a theme park, a water park, a cultural centre, an entertainment district, a commercial district, residential units and chalets. Aljazayer is being developed in partnership with the Government of Bahrain on a long-term lease basis.

www.ithmaarbank.com

Corporate Governance

The Bank is committed to upholding the highest standards of corporate governance, which it regards as a key factor in ensuring fairness for all stakeholders and achieving organisational efficiency. During 2007, the Board conducted a thorough review of the Bank's high level policies for corporate governance, internal controls, risk management and compliance, in accordance with the latest regulations and guidelines issued by the Central Bank of Bahrain (CBB). The Board's adherence to best corporate governance practices is underlined by various principles, such as integrity, transparency, independence, accountability, responsibility, fairness and social responsibility.

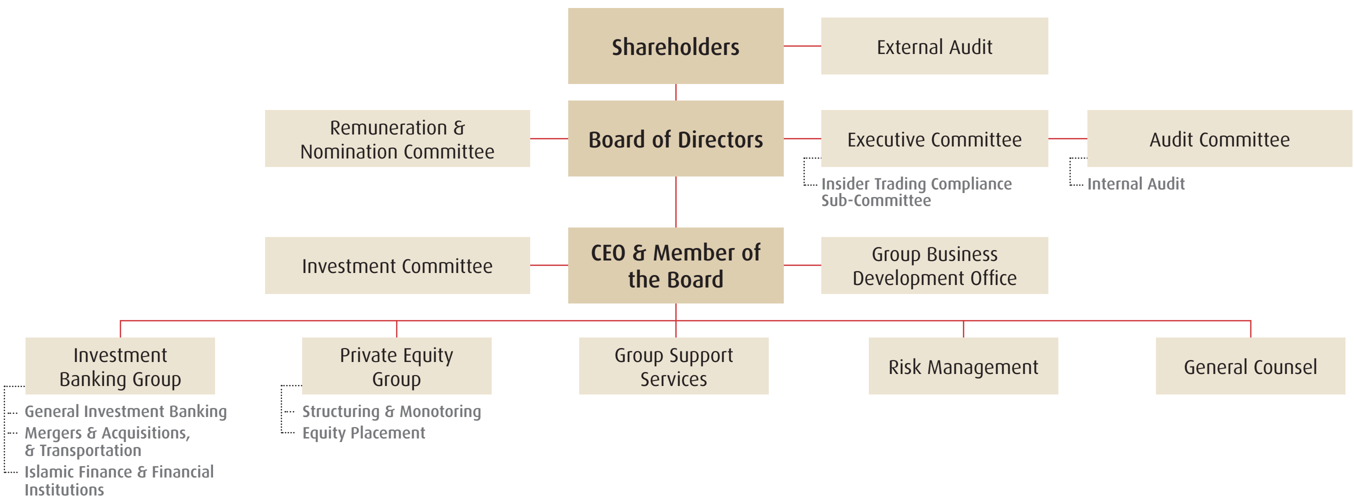
Moreover, the Bank's Corporate Governance Policies are designed to lay a solid foundation for management and oversight, promote ethical and responsible decision making, safeguard integrity in financial reporting, make timely and balanced disclosures, respect the rights of shareholders, recognise and manage risk, encourage enhanced performance, remunerate fairly and responsibly, and recognise the legitimate interest of stakeholders.

Shareholders' Rights

Recognising the importance of shareholders, Ithmaar Bank treats all its shareholders equally and fairly in line with the guidelines of regulatory agencies. Basic legitimate rights of shareholders include the right to participate in shareholders' meetings, the right to appoint other persons as a proxy for participating in and voting at meetings, and the right to participate in the election or disqualification of a director, individually. Their rights also include voting on the appointment of independent auditors, and voting for other businesses of the Bank, such as increases in or reduction of capital, the right to receive dividend payments, as well as the right to give opinions and the right to enquire during shareholders' meeting.

Bank Administration

The Bank is administered by the Board of Directors, committees of the Board, and the Executive Management.



BANK ADMINISTRATIVE CHART

> ... integrity, transparency, independence, accountability, responsibility, fairness and social responsibility.

Board's Responsibilities

The Board of Directors is accountable to the shareholders for setting the broad policy guidelines and strategic direction, and the creation and delivery of strong sustainable financial performance and long-term shareholder value. The Chairman is responsible for leading the Board, ensuring its effectiveness, monitoring the performance and supporting the Executive Management. The Board's role includes the task of monitoring management in such a manner as to ensure that appropriate policies and processes are in place, that they are operating effectively, and that the Bank is meeting its plans and budget targets.

Term

Each director is elected for a three-year term, renewable at annual general meetings of the shareholders of the Bank.

Board Committees

The Board of Directors may, from time to time, establish committees as it considers necessary or appropriate to assist it in carrying out its responsibilities. The Board has established the following committees and has adopted charters setting out the matters relevant to their composition, responsibilities and administration.

EXECUTIVE COMMITTEE

The main objective of this committee is to provide oversight of the Bank's strategic planning, approve transactions for which the Board has delegated authority to the committee within the parameters of the Limits of Authority, to make recommendations to the Board regarding transactions not falling within the Limits of Authority of the Executive Committee, and to evaluate the Bank's financial strategies and policies.

Khalid Abdulla-Janahi
CHAIRMAN

Graham R. Walker
MEMBER

Michael P. Lee
MEMBER

AUDIT COMMITTEE

The Audit Committee comprises three members from the Board of Directors and operates under the terms of reference set forth in a formal charter. The Audit Committee assists the Board through review of the Bank's financial information, internal controls, risk management processes and internal audit functions. The committee also oversees the Internal Audit function and evaluates the performance of the Bank's external auditors. In addition, the Committee is charged with ensuring the Bank's compliance with applicable laws and regulations.

Ziad H. Rawashdeh
CHAIRMAN

Abdelhameed Abou Moussa
MEMBER

Khalil Nooruddin
MEMBER

REMUNERATION & NOMINATION COMMITTEE

The main objective of this committee is to assist the Board in the effective discharge of its responsibilities in relation to the remuneration of directors and performance of the Board, ensure the appropriate Board composition, ensure appropriate nomination of directors to the Board and provide a formal forum for communication between the Board and the Bank's management on Human Resource issues.

Tunku Dato' Ya'acob Bin Tunku Abdullah
CHAIRMAN

Mohamed Bin Saif Al Mezrouei
MEMBER

Shaikha Hissah Bint Saad Al-Sabah
MEMBER

INSIDER TRADING COMPLIANCE SUB-COMMITTEE (OF THE EXECUTIVE COMMITTEE)

This committee is established by the Executive Committee and its main objective is to undertake the responsibility of ensuring that the Bank complies with the Insider's Regulatory Guidelines and to review and investigate any matter within the scope of this Charter, and to make recommendations to the Executive Committee in relation thereto.

Graham R. Walker
CHAIRMAN

Nayla Asgharali
MEMBER

Jassim A. Karim Salman
MEMBER

EXECUTIVE MANAGEMENT

Management is responsible for operating the Bank in an effective, ethical and legal manner, designed to produce value for the Bank's shareholders consistent with the Bank's policies and standards. The Chief Executive Officer is appointed by and reports to the Board of Directors. Senior management is responsible for implementing the Board's strategic directions, and understanding the Bank's income-producing activities and material risks faced by the Bank.

INVESTMENT COMMITTEE (MANAGEMENT)

The main objective of this Committee is to review, approve and ratify all investments within its authority, review risk management reports, and resolve all credit-related issues.

Michael P. Lee
CHAIRMAN

Shaikh Salman bin Ahmad Al Khalifa
MEMBER

Carolyn Prowse
MEMBER

Mohamed Khan Hoti
MEMBER

Masood Tyabji
MEMBER

Scott A. Creswell
MEMBER

Board and Management Conduct

CONFIDENTIALITY OF INFORMATION

In order to facilitate open discussion, the Board believes that maintaining confidentiality of the Bank's information and Board and committee deliberations are critical.

CONFLICTS OF INTEREST

Directors avoid any action, position or interest that conflicts with an interest of the Bank, or gives the appearance of a conflict. The Bank annually solicits information from directors in order to monitor potential conflicts of interest and directors are expected to be mindful of their fiduciary obligations to the Bank. In the event of a situation involving a potential conflict of interest, directors are encouraged to seek advice from the Bank's Compliance Officer.

CODE OF BUSINESS CONDUCT AND ETHICS

The Bank's Code of Business Conduct and Ethics applies to members of the Board, as well as Executive Management, officers, employees, agents, consultants, and others, when they are representing or acting for the Bank. The Board of Directors, as well as officers and employees, act ethically at all times and acknowledge their adherence to the Bank's policies. Any waiver of the Code of Business Conduct and Ethics for a director or executive officer may be granted only by the Board or the appropriate Board committee, and must be promptly disclosed to the stockholders.

COMMUNICATION WITH SHAREHOLDERS

The Bank conducts all communications with its stakeholders in a professional, honest, transparent, understandable, accurate and timely manner. Main communications channels include an annual report, quarterly publications of financial results, a corporate website and regular announcements in the appropriate local media.

Internal Audit

The Bank's internal audit function monitors compliance with the policies and procedures and effectiveness of internal controls. The work of internal audit is focused on the areas of risk assigned through a risk assessment approach.

The internal audit function reports directly to the Audit Committee of the Board of Directors. The internal audit conducts its work independently of the Bank's senior management, in accordance with the internal audit plan approved by the Audit Committee.

Compliance

In accordance with the directives of the Central Bank of Bahrain, the Bank appointed a Compliance Officer, who also acts as a Money Laundering Reporting Officer (MLRO). The Compliance Officer acts as central coordinator for the group in respect of all matters relating to the CBB's regulatory reporting and other requirements, the Bahrain Stock Exchange and the Ministry of Industry and Commerce.

The compliance function covers the broad areas of corporate governance, adherence to best practices, code of conduct, conflict of interest, adherence to the IFRS, compliance with Basel II and other issues. Each of Ithmaar's operating subsidiaries has appointed local compliance officers to ensure adherence to local requirements and regulatory issues. It is the duty of the MLRO in each subsidiary to ensure that sufficient evidence is obtained in all cases to enable the identity of every client to be satisfactorily established, failing which monies cannot be transferred, and to report any suspicions concerning a customer or account to their relevant regulator and senior management.

The MLRO is also responsible for establishing and maintaining appropriate and effective systems, controls and records to ensure compliance with regulatory obligations in regard to money laundering.

This responsibility of the Compliance Officer also includes the issue and implementation of policy and procedural manuals to all subsidiaries throughout the group, arranging in-house and external training for relevant officers and submission of group reports to the Board & the CBB.

"Our association with the Ithmaar Education and Training Fund has allowed us to provide higher quality education to the orphans under our care. It has allowed needy pupils to get the same opportunities that are available to those who come from wealthy ones. These scholarships are changing these students' lives for the better, offering them hope for a better future. We are very grateful to Ithmaar Bank for its important contribution to our efforts."

HASAN JASSIM ZUWAYED
SECRETARY GENERAL, ROYAL CHARITY ORGANISATION

Corporate Social Responsibility

As a concerned corporate citizen, Ithmaar Bank has an enduring commitment to contribute to the social and economic betterment of society. To support this commitment, the Bank has developed a wide-embracing programme of corporate social responsibility activities.

These include considerable financial contributions to a range of charitable, educational, social, cultural and sporting organisations and events; plus widespread sponsorship of conferences, seminars and initiatives, which support the growth of the Islamic banking industry, and further enhance the status of its home country, the Kingdom of Bahrain, as the leading financial centre in the Middle East.

In particular, two highly-acclaimed endeavours – the 'Ithmaar Education and Training Fund' and 'ITHMAAR GROUP Yalla Bahrain!' – illustrate the level of investment and commitment, as well as the variety and scope of activities.

ITHMAAR EDUCATION AND TRAINING FUND

Ithmaar Bank believes that education and training is a key foundation for sustainable economic growth, especially for emerging and developing nations. Accordingly, in 2007, the Bank's shareholders approved the establishment of the 'Ithmaar Education and Training Fund' with an appropriation of $4.2 million from profits for the year ended 2006.

The Fund comprises three distinct but interrelated elements. First, in coordination with the Kingdom of Bahrain's Royal Charity Association, Ithmaar Bank annually sponsors six needy orphan students to attend private schools in Bahrain, for 11 years, from Grades 2 to 12.

"We are pleased to be able to offer world class education to promising students from around the world with the support of the Ithmaar Education and Training Fund. Our partnership with Ithmaar Bank has allowed us to offer Masters degree programmes to students who would otherwise have difficulty in pursuing their education and achieving their true potential. The percent of students at the MSc level from overseas is greater than that from the UK, giving LSE the widest international spread of any university in the world. These scholarships from Ithmaar Bank help make that possible."

HOWARD DAVIES
DIRECTOR, LONDON SCHOOL OF ECONOMICS

This will mean that there will be a total of 66 students enrolled in the programme by its eleventh year. Also, in collaboration with Ahlia University, the Bank provides undergraduate degree courses for ten orphan students every year in Bahrain. The total number of students at any time from the fourth year onward will be 40. Thirdly, in an arrangement with the London School of Economics, Ithmaar Bank funds post-graduate education for promising young needy students from across the Muslim world. The first group of students is already pursuing courses at the univeristy.

EXEMPLARY EMPLOYER

Ithmaar Bank is widely considered an employer of choice, both within the banking industry and the GCC in general. Its recognition as a preferred employer has given it the competitive advantage of being able to attract and retain high quality staff for both senior and junior positions. The Bank has policies in place that reward strong performance with promotions, financial incentives and equal opportunities for all, regardless of background, sex or nationality.

In addition to the above-mentioned Ithmaar Education and Training Fund, the Bank also supports bright young talents through an annual internship programme, which it launched in 2007. It also lends the expertise of its staff to educational initiatives aiming to develop the talents of future generations through training programmes such as those offered by inJAz Bahrain to public and private high school students.

SUPPORT FOR ORPHANS

In addition to the above-mention educational initiatives, Ithmaar Bank, from time to time, organises and sponsors activities for orphans in the Kingdom of Bahrain. Among these was the purchase of 120 tickets to the Formula One race at the Bahrain International Circuit for orphans from the Royal Charity Association. The youngsters also had lunch with the Blades pilots and crew at the Bahrain International Airport. The Blades were in Bahrain for the Blades in Bahrain aerobatic display, which the Ithmaar banking group sponsored.

ITHMAAR GROUP YALLA BAHRAIN!

Ithmaar Bank is the title sponsor of this unique six-week programme, which is an annual event that aims to drum up support ahead of the annual Formula One Grand Prix. The 'Yalla Bahrain!' calender, which the Ithmaar banking group is supporting for the second year in a row, includes artistic, sporting and family-oriented events which benefit the community and stimulates economic activity in the Kingdom.

Risk Management

The essence of effective risk management is to achieve a balance between business profits and risk appetite. The risk management framework establishes the parameters within which such balance is to be achieved through the definition of the Bank's key risk management principles, covering credit, market, operational and reputation risks. It also defines the role and responsibilities of the Board of Directors, Risk Management and senior management.

Ithmaar's risk management framework considers leading practices including the COSO (Committee of Sponsoring Organisations of the Treadway Commission) principles. Risk management, as well as internal audit, plays an important high level role in ensuring that the standards are maintained. Risk management is an evolutionary process and the Bank recognises the need to continually evaluate, improve and adjust the components of its risk management process.

CAPITAL MANAGEMENT

The Bank's objectives when managing capital, which is a broader concept than the 'equity' on the face of balance sheets, are:

i) To comply with the capital requirements set by the regulators of the banking jurisdictions where the group operates;

ii) To safeguard the Bank's ability to continue as a going concern so that it can continue to provide returns for shareholders and benefits for other stakeholders; and

iii) To maintain a strong capital base to support the development of its business.

This involves a coordinated effort by the business divisions, Risk Management and Financial Control.

CREDIT RISK

Ithmaar manages its credit risk, including risk arising from its private equity investments, by implementing its robust policies and procedures with respect to identification, measurement, mitigation and control. Credit risks are monitored on a revolving basis and are subject to at least an annual or more frequent review. The Bank also monitors the credit ratings of its financial counterparties through ratings provided by Standard and Poor's, Moody's, Fitch or Capital Intelligence.

MARKET RISK

Ithmaar undertakes exposures which are subject to market risks and separates exposures to market risk into either trading or non-trading portfolios. Ithmaar's market risk exposure comprises non-trading portfolios; they primarily consist of foreign exchange and equity risks arising from the Bank's available-for-sale investments.

The market risks arising from trading activities are monitored by and regular reports are submitted to management.

OPERATIONAL RISK

Ithmaar's approach to operational risk includes emphasis on automation of processes and implementing effective internal controls. The Bank is further enhancing its operational risk framework to include the mapping of business processes with major risks and associated internal controls. This also includes identifying and managing the key risk indicators and implementing a robust business continuity plan.

REPUTATION RISK

Sound corporate governance is a cornerstone in managing reputation risk. The Bank has introduced a formal "corporate governance policy" and a "code of ethics and business conduct" for members of the Board, Management and staff. This code will help to build a professional atmosphere; integrity and ethical behaviour that will also help prevent reputation risks from crystallising. All material breaches have to be reported to senior management and the Board and will lead to appropriate consequences.

BASEL II

As part of the requirements of the Central Bank of Bahrain, the Bank is subject to the Basel II capital adequacy framework, Pillar 1 - Minimum Capital Requirements, effective January 2008. The Bank has developed and implemented a detailed project plan to ensure that Central Bank of Bahrain timelines are met. The Pillar 1 deals with maintenance of regulatory capital calculated for three major components of risk that a bank faces: credit risk, operational risk and market risk.

The Bank has adopted the following approach for capital adequacy measurement:

- Standardised approach for credit risk
- Basic indicator approach for operational risk
- Standardised approach for market risk

Report of the Directors

FOR THE YEAR ENDED 31 DECEMBER 2007

The Directors submit their report dealing with the activities of Ithmaar Bank BSC (the "Bank") for the year ended 31 December 2007, together with the audited consolidated financial statements of the Bank and its subsidiaries ("the Group") for the year then ended.

PRINCIPAL ACTIVITIES

The principal activities of the Bank and its subsidiaries (collectively the "Group") are a wide range of financial services, including investment, commercial and private banking, private equity, public and private issue of securities, mergers and acquisitions advice, takaful, equipment leasing and real estate development.

FINANCIAL POSITION AND RESULTS

The financial position of the Group as at 31 December 2007, together with the consolidated statements of income, changes in equity and cash flows for the year then ended is set out in the accompanying consolidated financial statements.

The Group has reported a net profit of $188.3 million for 2007, as compared to a net profit of $181.1 million for 2006. Total assets amounted to $4,078 million (31 December 2006: $3,319 million). Funds under management amounted to $1,724 million (31 December 2006: $1,060 million)

CORPORATE GOVERNANCE, RISK MANAGEMENT AND COMPLIANCE

During 2007, the Bank has further strengthened its corporate governance, risk management and compliance frameworks. The Board strength increased from ten to twelve members.

The Bank has also made significant progress in the implementation of Basel II which is effective from 1st January 2008.

CAPITAL AND CAPITAL ADEQUACY

During the year the Bank increased its authorised capital from $500 million to $1,000 million and its paid up capital from $360 million to $543.6 million. The increase in the authorised, issued and paid up share capital has been duly approved by the shareholders and the Central Bank of Bahrain.

The Bank's consolidated risk asset ratio under Basel I as at 31 December 2007 was 25.79 per cent (2006: 29.52 per cent) as compared to a minimum regulatory requirement of 12 per cent. The Bank's risk weighted assets and eligible capital are set out in Note 38 to the accompanying consolidated financial statements. The Bank monitors adequacy of capital at all times.

DIVIDEND

The Directors propose to recommend at the Annual General Meeting a dividend of $53.7 million (2.5 cents per share) for the year ended 31 December 2007.

A dividend for 2006 amounting to $47.5 million (13.5 cents per share equivalent to 3.375 cents per share after the four for one share split) was approved and paid in 2007.

DIRECTORS

The following are the Directors of the Bank as at 31 December 2007:

Mr. Khalid Abdulla-Janahi
(CHAIRMAN)

Tunku Dato' Ya'acob Bin Tunku Abdullah

Mr. Abdel Hamid Abo Moussa

Mr. Mohamed Bin Saif Al Mezrouei

Mr. Farook Bengali

Mr. Kenneth C. Borda
(WITH EFFECT FROM 26 FEBRUARY 2007)

Mr. Mohammed Youseef El-Khereiji

Sheikha Hissah Bint Saad Al-Sabah

Mr. Khalil Nooruddin

Mr. Ziad Hasan Rawashdeh

Mr. Graham Roderick Walker

Mr. Michael P. Lee
(WITH EFFECT FROM 3 SEPTEMBER 2007)

Directors and the Executive Management held 66,195,706 shares in the Bank as at 31 December 2007 (2006: 4,929,866 shares before four for one share split). Directors' fees in respect of 2007 amounted to $1,108,500 (2006: $806,500).

AUDITORS

The auditors, PricewaterhouseCoopers, have expressed their willingness to be reappointed as auditors of the Bank for the year ending 31 December 2008.

By order of the Board of Directors

Khalid Abdulla-Janahi
CHAIRMAN

24 February 2008

Financial Statements

… INDEX TO THE FINANCIAL STATEMENTS

Independent Auditor's Report

TO THE SHAREHOLDERS OF ITHMAAR BANK B.S.C.

REPORT ON THE FINANCIAL STATEMENTS

We have audited the accompanying consolidated financial statements of Ithmaar Bank B.S.C. (the "Bank") and its subsidiaries (together, the "Group"), which comprise the consolidated balance sheet as at 31 December 2007 and the consolidated income statement, consolidated statement of changes in equity and consolidated cash flow statement for the year then ended and a summary of significant accounting policies and other explanatory notes.

MANAGEMENT'S RESPONSIBILITY FOR THE FINANCIAL STATEMENTS

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

AUDITOR'S RESPONSIBILITY

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those Standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error.

In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

OPINION

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Group as at 31 December 2007, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

MATTERS OF EMPHASIS

Without qualifying our opinion, we draw attention to Note 47 in the consolidated financial statements which indicates that the previously issued financial statements for the year ended 31 December 2006 on which we issued an audit report dated 26 February 2007, have been revised and reissued. As explained in Note 47, these revisions were to reflect the recognition of intangibles arising from the acquisition of Shamil Bank of Bahrain B.S.C. on a gross basis as opposed to net of minority interests as previously reported.

REPORT ON REGULATORY REQUIREMENTS

Further, as required by the Bahrain Commercial Companies Law ("BCCL") and the Central Bank of Bahrain Law ("CBBL") , we report that we have obtained all the information that we considered necessary for the purpose of our audit; the Bank has maintained proper books of account and the consolidated financial statements and the financial information contained in the Directors' report are in agreement therewith; and nothing has come to our attention which causes us to believe that the Bank has breached any of the applicable provisions of the BCCL, the CBBL, the terms of its banking license or its Memorandum and Articles of Association which would materially affect its activities or its financial position as at 31 December 2007.

PricewaterhouseCoopers

MANAMA, KINGDOM OF BAHRAIN
24 February 2008

CONSOLIDATED BALANCE SHEET

as at 31 December 2007

(Expressed in thousands of United States Dollars)

	Notes	2007	2006 (Restated)
ASSETS			
Cash and cash equivalents	6	575,304	619,977
Due from banks		16,172	1,900
Trading securities		-	394
Investments in financings	7, 8, 9	1,882,028	1,635,035
Investment securities	10	638,579	403,090
Investment property	12	213,067	67,766
Accounts receivable	13	101,856	65,902
Investments in associates	14	194,549	152,520
Property, plant and equipment	15	130,930	30,701
Intangible assets	16	326,304	339,314
Non-current assets held for sale	17	-	2,156
Total assets		**4,078,789**	**3,318,755**
LIABILITIES			
Customer current accounts	18	569,239	383,704
Customer investment accounts	19	1,368,904	1,051,871
Due to banks		394,025	535,967
Other borrowings	20, 22	123,239	-
Accounts payable	21	269,438	177,865
Current tax payable		9,175	9,623
Deferred tax liability	23	60,372	36,070
Total liabilities		**2,794,392**	**2,195,100**
EQUITY			
Capital and reserves attributable to the Bank's equity holders			
Share capital	33	537,474	353,525
Reserves	34	550,334	438,568
		1,087,808	**792,093**
Minority interests	32	**196,589**	**331,562**
Total equity		**1,284,397**	**1,123,655**
Total equity and liabilities		**4,078,789**	**3,318,755**
Funds under management	39	**1,723,814**	**1,059,937**

These consolidated financial statements were approved for issue by the Board of Directors on 24 February 2008 and signed on their behalf by:

Khalid Abdulla-Janahi
Chairman

Michael P. Lee
CEO and Director

Graham R. Walker
Director

The notes on pages 51 to 114 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF INCOME

as at 31 December 2007

(Expressed in thousands of United States Dollars)

	Notes	2007	2006 (Restated)
INCOME			
Income from short term deposits		43,429	23,144
Income from investments in financings	24	181,354	56,631
Fee and commission income	25	52,481	27,729
Fund management and services	39	19,524	43,283
Gains/(losses) from investment securities	10	44,737	(1,201)
Income from investment property	26	92,731	14,405
Net trading income	27	7,517	1,587
Dividend income	28	27,242	825
Gain on sale of associated company	42	15,001	4,613
Other income		954	1,215
		484,970	172,231
Distribution to investment account holders		(145,495)	(47,984)
Operating income		339,475	124,247
EXPENSES			
Staff costs	29	(74,312)	(28,066)
General and administrative expenses	30	(48,440)	(17,319)
Depreciation and amortisation	15,16	(20,542)	(6,823)
Exchange gain/(loss)		3,782	(100)
Total expenses		(139,512)	(52,308)
Gain on sale of subsidiary	42	-	105,541
Operating profit		199,963	177,480
Share of profit of associated companies	14	8,353	15,695
Profit before income taxes		208,316	193,175
Taxes	31	(20,006)	(12,125)
Profit after income taxes		**188,310**	**181,050**
Attributable to:			
Equity holders of the Bank		102,755	167,558
Minority interests	32	85,555	13,492
		188,310	**181,050**
Basic/diluted earnings per share	37	**US cts 5.79**	**US cts 11.10**

These consolidated financial statements were approved for issue by the Board of Directors on 24 February 2008 and signed on their behalf by:

Khalid Abdulla-Janahi	Michael P. Lee	Graham R. Walker
Chairman	CEO and Director	Director

The notes on pages 51 to 114 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

as at 31 December 2006

(Expressed in thousands of United States Dollars)

	Notes	Attributable to the Bank's equity holders								Minority interests	Total equity
		Share capital	Share premium	Statutory reserve	General reserve	Fair value reserve	Currency translation	Retained earnings	Total reserves		
At 1 January 2006		150,000	-	8,778	13,503	24,678	(7,756)	58,156	97,359	5,418	252,777
Issue of new shares	33	210,000	187,500						187,500		397,500
Treasury shares acquired	33	(6,475)	(6,510)						(6,510)		(12,985)
Share issue expenses			(14,672)		826				(13,846)		(13,846)
Share based payments			1,029						1,029		1,029
Net profit for the year								167,558	167,558	13,492	181,050
Dividend paid	36							(20,000)	(20,000)	(13,839)	(33,839)
Change of ownership interest in subsidiary					(3,910)	(184)	(235)	(1,322)	(5,651)	328,668	323,017
Revaluation of associate following acquisition of controlling interest					34,244				34,244		34,244
Movement in fair value of available-for-sale investments						(614)			(614)	(1,224)	(1,838)
Movement in deferred tax available-for-sale investments						(2)			(2)	(1)	(3)
Movement in fair value of associated companies					1,381	(5,546)			(4,165)	(21)	(4,186)
Associated companies sold						(2,212)	3,211		999		999
Available-for-sale investments sold						31			31	2	33
Foreign currency translation adjustment							636		636	(933)	(297)
Transfer to statutory reserve				16,820				(16,820)			
At 31 December 2006 (restated)		**353,525**	**167,347**	**25,598**	**46,044**	**16,151**	**(4,144)**	**187,572**	**438,568**	**331,562**	**1,123,655**

The notes on pages 51 to 114 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

as at 31 December 2007

(Expressed in thousands of United States Dollars)

		Attributable to the Bank's equity holders									
	Notes	Share capital	Share premium	Statutory reserve	General reserve	Fair value reserve	Currency translation	Retained earnings	Total reserves	Minority interests	Total equity
At 1 January 2007		353,525	167,347	25,598	46,044	16,151	(4,144)	187,572	438,568	331,562	1,123,655
Issue of bonus shares	33	72,000	(72,000)						(72,000)		
Issue of new shares	42	111,625	312,550						312,550	(230,288)	193,887
Goodwill on acquisition of minority interest	42		(193,887)						(193,887)		(193,887)
Treasury shares acquired	33	(12,857)	(12,933)						(12,933)		(25,790)
Treasury shares sold		13,181	14,949						14,949		28,130
Net profit for the year								102,755	102,755	85,555	188,310
Dividend paid	36							(47,520)	(47,520)	(21,812)	(69,332)
Minority interests relating to new subsidiaries										13,954	13,954
Movement in fair value of available-for-sale investments	10					27,234			27,234	24,745	51,979
Movement in deferred tax relating to available-for-sale investments						(7,120)			(7,120)	(3,851)	(10,971)
Movements in fair value of associated companies						(2,603)			(2,603)		(2,603)
Available-for-sale investments sold						(5,587)			(5,587)	(2,662)	(8,249)
Foreign currency translation adjustment						(905)	1,065	(27)	133	(614)	(481)
Transfer to general reserve					22,283			(22,283)			
Transfer to statutory reserve				10,275				(10,275)			
Appropriation to Ithmaar Education and Training Fund								(4,205)	(4,205)		(4,205)
At 31 December 2007		**537,474**	**216,026**	**35,873**	**68,327**	**27,170**	**(3,079)**	**206,017**	**550,334**	**196,589**	**1,284,397**

The notes on pages 51 to 114 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

as at 31 December 2007

(Expressed in thousands of United States Dollars)

	Notes	2007	2006 (Restated)
CASH FLOWS FROM OPERATING ACTIVITIES			
Profit before taxes and minority interests		208,316	193,175
Adjustments for:			
Share based payments		5,321	1,029
Depreciation and amortisation	15,16	20,542	6,823
Changes in fair value of investment property	12	(36,033)	(13,205)
Gain on sale of subsidiary	42	-	(105,541)
Income from associated companies	14	(8,353)	(20,308)
Operating profit before changes in operating assets and liabilities		189,793	61,973
(Increase) in due from banks		(14,273)	(1,840)
Net decrease/(increase) of trading securities		394	(196)
(Increase) in investments in financings		(246,993)	(182,048)
(Increase)/decrease of investment securities		(183,694)	166,700
(Increase)/decrease in accounts receivable		(35,928)	74,177
Increase/(decrease) in accounts payable, excluding taxes		80,286	(28,432)
Increase/(decrease) in investment accounts		362,359	(176,640)
Taxes (paid)/refunded		(6,549)	1,435
Net cash provided by/(used in) operating activities		**145,395**	**(84,871)**
CASH FLOWS FROM INVESTING ACTIVITIES			
Cash inflow on sale of a subsidiary	42	-	134,376
Cash inflow on purchase of a subsidiary	42	-	22,447
Cash inflow on conversion of associate to subsidiary	42	-	233,899
Dividends from associated companies	14	1,169	4,596
Investments in associated companies	14	(52,158)	(71,551)
Sale of associated companies	14	17,042	18,521
Purchase of investment property	12	(236,722)	(7,910)
Sale of investment property	12	130,329	7,720
Purchase of property, plant and equipment and intangibles		(105,699)	(14,949)
Sale of property, plant and equipment and intangibles		-	11,015
Net cash (used in)/provided by investing activities		**(246,039)**	**338,164**

The notes on pages 51 to 114 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

as at 31 December 2007

(Expressed in thousands of United States Dollars)

	Notes	2007	2006 (Restated)
CASH FLOWS FROM FINANCING ACTIVITIES			
Other borrowings	22	123,239	-
Treasury shares purchased	33	(25,790)	(12,985)
Treasury shares sold	33	28,130	-
Dividends paid	36	(47,520)	(20,000)
Dividends paid to minority shareholders of subsidiaries		(21,812)	(13,839)
Proceeds from issuance of shares	33,35	-	397,500
Proceeds from issuance of shares in subsidiaries		-	1,435
Share issue expenses paid	33,35	-	(14,672)
Net cash provided by financing activities		**56,247**	**337,439**
Foreign currency translation adjustments		(276)	3,709
Net (decrease)/increase in cash and cash equivalents		**(44,673)**	**594,441**
Cash and cash equivalents at beginning of year		619,977	25,536
Cash and cash equivalents at end of year		**575,304**	**619,977**

The notes on pages 51 to 114 form an integral part of these consolidated financial statements.

1. FORMATION AND ACTIVITIES

Ithmaar Bank B.S.C. (the "Bank") was incorporated in the Kingdom of Bahrain on 13 August 1984 and is an investment bank regulated by the Central Bank of Bahrain. The Bank has its registered office at Addax Tower, 10th floor, Building 1006, Road 2813, Al Seef District 428, Manama, Kingdom of Bahrain.

The principal activities of the Bank and its subsidiaries (collectively the "Group") are a wide range of financial services, including investment, commercial and private banking, private equity, public and private issue of securities, mergers and acquisitions advice, takaful, equipment leasing and real estate development. The management of Islamic modarabas which are similar to investment funds are not consolidated in the accompanying consolidated financial statements because they represent funds invested by clients without recourse to the Group. Accordingly, they are included in off-balance sheet accounts as disclosed in note 39.

During the first six months of 2006, the Bank's issued share capital was increased to $360 million. Public trading of Ithmaar Bank B.S.C. shares (ITHMR) began on the Bahrain Stock Exchange on 4 June 2006.

In November 2007, the Bank acquired the remaining 40% share holding in Shamil Bank of Bahrain ("Shamil Bank") through a share exchange by issuing 446,499,970 shares to the Shamil Bank minority shareholders. Twelve ordinary shares of the Bank were exchanged for every ten ordinary shares in Shamil Bank. The Bank also issued 288,000,000 bonus shares to the existing shareholders before the share exchange. The paid up capital of the Bank now stands at $543.6 million, while the authorised capital is $1 billion.

2. ACCOUNTING POLICIES

The principal accounting policies adopted in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

Basis of preparation

The consolidated financial statements of the Group are prepared in accordance with and comply with International Financial Reporting Standards (IFRS). The consolidated financial statements are prepared under the historical cost convention as modified by the revaluation of available-for-sale financial assets, financial assets and financial liabilities held at fair value through profit or loss and investment property.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in note 4.

Impact of New Accounting Pronouncements: International Financial Reporting Standards

Standards, interpretations and amendments to published standards effective from 1 January 2007

The following new standards, interpretations and amendments are relevant to the Group and therefore, mandatory for accounting period with effect from 1 January 2007:

IFRS 7 - Financial Instruments: Disclosures, and a complementary amendment to IAS 1, Presentation of Financial Statements – Capital Disclosures: IFRS 7 introduces new disclosures to improve the information about financial instruments. It requires the disclosure of qualitative and quantitative information about exposure to risks arising from financial instruments, including specified minimum disclosures about credit risk, liquidity risk and market risk, including sensitivity analysis to market risk. It replaces IAS 30, Disclosures in the Financial Statements of Banks and Similar Financial Institutions, and disclosure requirements in IAS 32, Financial Instruments: Disclosure and Presentation. The amendment to IAS 1 introduces disclosures about the level of an entity's capital and how it manages capital. The Group has adopted IFRS 7 and the amendment to IAS 1 from 1 January 2007.

The following interpretations to existing standards have been published that are mandatory for the Group's accounting periods beginning on or after 1 May 2006 or later periods but are not relevant

2 ACCOUNTING POLICIES (continued)

for the Group's operations: (a) IFRIC 7 - Applying the Restatement Approach under IAS 29, Financial Reporting in Hyperinflationary Economies and IFRIC 9 -Reassessment of Embedded Derivatives.

IFRIC 8 - Scope of IFRS 2: IFRIC 8 requires consideration of transactions involving the issuance of equity instruments – where the identifiable consideration received is less than the fair value of the equity instruments issued – to establish whether or not they fall within the scope of IFRS 2. The Group has applied IFRIC 8 from 1 January 2007, but there is no impact on the Group's accounts.

IFRIC 10 - Interim Financial Reporting and Impairment: IFRIC 10 prohibits the impairment losses recognised in an interim period on goodwill, investments in equity instruments and investments in financial assets carried at cost to be reversed at a subsequent balance sheet date. The Group has applied IFRIC 10 from 1 January 2007, but there is no impact on the Group's accounts.

New accounting standards and IFRIC interpretations that are not yet effective

The following new standards, interpretations and amendments to existing standards have been published that are mandatory for the Group's accounting periods beginning on or after 1 January 2008 or later periods but that the Group has not early adopted:

IAS 1 (amended), 'Presentation of financial statements' (effective from 1 January 2009). It primarily affects the presentation of owner changes in equity and of comprehensive income. It does not change the recognition, measurement or disclosures of specific transactions and other events required by other IFRSs.

IAS 23 (amended), 'Borrowing costs' (effective from 1 January 2009). It requires an entity to capitalise borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset (one that takes a substantial period of time to get ready for use or sale) as part of the cost of that asset. The option of immediately expensing those borrowing costs will be removed.

IAS 27 (amended) (effective for accounting periods beginning on or after 1 July 2009) requires the effects of all transactions with non-controlling interests to be recorded in equity if there is no change in control. They will no longer result in goodwill or gains and losses. The standard also specifies the accounting when control is lost. Any remaining interest in the entity is remeasured to fair value and a gain or loss is recognised in profit or loss. In addition, total comprehensive income must be attributed to the owners of the parent and to the non-controlling interests even if this results in the non-controlling interests having a deficit balance. These changes will impact the accounting for future transactions with non-controlling interest formerly minority interest.

IFRS 2 (amended) (effective for accounting periods beginning on or after 1 January 2009) deals with two matters. It clarifies that vesting conditions can be service conditions and performance conditions only. Other features of share-based payment are not vesting conditions. It also specifies that all cancellations, whether by the entity or by other parties, should receive the same accounting treatment.

IFRS 3 (revised), 'Business combinations' requires significant changes in the application of the acquisition method to business combinations. All payments to purchase a business are to be recorded at fair value at the acquisition date, with some contingent payments subsequently remeasured at fair value through profit or loss. Goodwill may be calculated based on the parent's share of net assets or it may also include goodwill related to the minority interest. All transaction costs will be expensed. The standard is applicable to business combinations occurring in accounting periods beginning on or after 1 July 2009, with earlier application permitted. The change may have a significant impact on the accounting for future business combinations.

IFRS 8, 'Operating segments ' (effective from 1 January 2009). IFRS 8 replaces IAS 14 and aligns segment reporting with the requirements of the US standard SFAS 131, 'Disclosures about segments of an enterprise and related information'. The new standard requires a 'management approach', under which segment information is presented on the same basis as that used for internal reporting purposes.

2 ACCOUNTING POLICIES (continued)

This new standard may impact the manner in which the segments are reported such as the number of reportable segments and measures to be reported. The change may also require management to reallocate goodwill to the newly identified operating segments.

IFRIC 11, 'IFRS 2 – Group and treasury share transactions' (effective for periods beginning on or after 1 March 2007); IFRIC 11 provides guidance on whether share-based transactions involving treasury shares or involving group entities (for example options over a parent's shares) should be accounted for as equity-settled or cash-settled share-based payment transactions in the stand-alone accounts of the parent and group companies. This interpretation does not have an impact on the group's financial statements.

IFRIC 12, 'Service concession arrangements' (effective from 1 January 2008). IFRIC 12 applies to contractual arrangements whereby a private sector operator participates in the development, financing, operation and maintenance of infrastructure for public sector services.

IFRIC 13, 'Customer loyalty programmes' (effective from 1 July 2008). IFRIC 13 clarifies that where goods or services are sold together with a customer loyalty incentive (for example, loyalty points or free products), the arrangement is a multiple-element arrangement and the consideration receivable from the customer is allocated between the components of the arrangement using fair values.

IFRIC 14, 'IAS 19 – The limit on a defined benefit asset, minimum funding requirements and their interaction' (effective from 1 January 2008). IFRIC 14 provides guidance on assessing the limit in IAS 19 on the amount of the surplus that can be recognised as an asset. It also explains how the pension asset or liability may be affected by a statutory or contractual minimum funding requirement.

Consolidation

(a) Subsidiaries

Subsidiaries are all entities (including special purpose entities) over which the Group has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date on which control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the consolidated statement of income.

Intercompany transactions, balances and unrealised gains on transactions between group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Subsidiaries' accounting policies have been changed where necessary to ensure consistency with the policies adopted by the Group.

Costs associated with the restructuring of a subsidiary as a part of the acquisition or subsequent to the acquisition are included in the consolidated statement of income upon the date of commitment.

(b) Associates

Associates are all entities over which the Group has significant influence but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights. Investments in associates are

2 ACCOUNTING POLICIES (continued)

accounted for by the equity method of accounting and are initially recognised at cost. The Group's investment in associates includes goodwill (net of any accumulated impairment loss) identified on acquisition.

The Group's share of its associates' post-acquisition profits or losses is recognised in the consolidated statement of income, and its share of post-acquisition movements in reserves is recognised in reserves. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment. When the Group's share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the associate.

Unrealised gains on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounts for associated companies have been restated to conform with Group accounting policies, if necessary, except as otherwise disclosed.

(c) Transactions and minority interests

The Group applies a policy of treating transactions with minority interests as transactions with parties external to the Group. Disposals to minority interests result in gains and losses for the Group that are recorded in the income statement. Purchases from minority interests result in goodwill, being the difference between any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary.

Acquisition of minority interest is accounted using the Economic Entity Method. Under the Economic Entity Method, the purchase of a minority interest is a transaction with a shareholder. As such, any excess consideration over the Group's share of net assets is recorded in equity.

Segment reporting

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing products or services within a particular economic environment that is subject to risks and returns that are different from those segments operating in other economic environments.

Foreign currency translation

(a) Functional and presentation currency

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

(b) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the statement of income, except where hedge accounting is applied.

Translation differences on non-monetary items, such as equities held at fair value through profit or loss, are reported as part of their fair value gain or loss. Translation differences on non-monetary items, such as equities classified as available-for-sale financial assets, are included in the fair value reserve in equity.

(c) Group companies

The results and financial position of all group entities (none of which has the currency of a hyperinflationary economy) that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

(i) assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;

(ii) income and expenses for each statement of income are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the

2 ACCOUNTING POLICIES (continued)

rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions);

(iii) and all resulting exchange differences are recognised as a separate component of equity (cumulative translation adjustment).

Exchange differences arising from the translation of the net investment in foreign entities, and of borrowings and other currency instruments designated as hedges of such investments, are taken to shareholders' equity on consolidation. When a foreign operation is sold, such exchange differences are recognised in the consolidated statement of income as part of the gain or loss on sale.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate.

Derivative financial instruments and hedging

Derivative financial instruments including foreign exchange contracts, equity options and equity futures are initially recognised in the consolidated balance sheet at fair value and subsequently remeasured at their fair value. Fair values are obtained from quoted market prices in active markets, discounted cash flow models, and options pricing models as appropriate. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

Changes in the fair value of derivatives held for trading are included in net trading income.

On the date a derivative contract is entered into, the Group designates derivatives as either (a) a hedge of fair value of a recognised asset or liability (fair value hedge); or (b) a hedge of highly probable future cash flows attributable to a recognised asset or liability, a forecast transaction or a firm commitment (cash flow hedge). At present the Group does not hedge future cash flows. Hedge accounting is used for derivatives provided certain criteria are met.

The Group's criteria for a derivative instrument to be accounted for as a hedge include:

(a) Formal documentation of the hedging instrument, hedged item, hedging objective, strategy and relationship is prepared before hedge accounting is applied; (b) the hedge is documented showing that it is expected to be highly effective in offsetting the risk in the hedged item through out the reporting period; and (c) the hedge is highly effective on an ongoing basis.

Changes in the fair value of the effective portions of derivatives that are designated and qualify as fair value hedges and that prove to be highly effective in relation to hedged risk, are recorded in the consolidated statement of income, along with the corresponding change in fair value of the hedged asset or liability that is attributable to that specific hedged risk.

If the fair value hedge no longer meets the criteria for hedge accounting, an adjustment to the carrying amount of a hedged financial instrument is amortised in the consolidated statement of income over the period to maturity. The adjustment to the carrying amount of a hedged equity security remains in retained earnings until the disposal of the equity security.

Certain derivative transactions, while providing effective economic hedges under the Group's risk management policies, do not qualify for hedge accounting under the specific rules in IAS 39 and are therefore treated as derivatives held for trading with fair value gains and losses reported in the consolidated statement of income.

Income from investments and investments in financings

Income from investments and investments in financings, which is both contractually determined and quantifiable at the commencement of the transaction, is accrued on the effective return method basis over the period of the transaction. Where income is not contractually determined or quantifiable, it is recognised when reasonably certain of realisation or when realised. Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, income is thereafter recognised using the rate of return used to discount the future cash flows for the purpose of measuring the impairment loss.

2 ACCOUNTING POLICIES (continued)

Fees and commission income

Fees and commissions are generally recognised as income when earned. Origination fees on financings which are probable of being drawn down, are deferred and recognised over the term of the financing as an adjustment to the effective yield. Structuring fees, commission and fees arising from negotiating or participating in the negotiation of a transaction for a third party, are recognised on completion of the underlying transaction.

Asset management fees related to investment funds are recognised rateably over the period the service is provided and are recorded in fund management and services income.

Management advisory and technical service fees are recognised based on applicable service contracts usually on a time-apportionate basis and are recorded in other income.

Distribution to investment account holders

The expense charged to the consolidated statement of income as a distribution to investment account holders represents the share of the Group's income from all sources which is due to customers of the Group under contractual arrangements in force.

Sale and repurchase agreements

Securities sold subject to a linked repurchase agreement are recognised as trading or investment securities and the counterparty liability is included in customer investment accounts. The difference in the sale and repurchase value is accrued over the period of the contract and recorded as expense in the consolidated statement of income.

Securities purchased under agreements to resell are recorded as investments in financings. The difference between the contracted price and the resale price is amortised over the period of the contract and is recognised as income in the consolidated statement of income.

Obligations for the return of securities or for forward sales, which are a part of the repurchase agreements, are recognised as commitments as disclosed in note 43.

Financial Assets

The Group classifies its financial assets into the following categories: financial assets at fair value through profit or loss; loans and receivables; held-to-maturity investments and available-for-sale financial assets. The classification of investments is determined at initial recognition. Financial assets are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss (refer to details below). Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or when the Group has transferred substantially all risks and rewards of ownership.

(a) Financial assets at fair value through profit or loss

This category includes financial assets held for trading, including trading securities, and those designated at fair value through profit or loss at inception. A financial asset is classified in this category if acquired principally for the purpose of selling in the short term or if so designated by management. Derivatives are also categorised as held for trading unless qualifying for hedge accounting.

Financial assets at fair value through profit and loss are initially recognised at fair value (which excludes transaction costs) and subsequently carried at fair value based on quoted bid prices. All related realised and unrealised gains and losses are included in net trading income in the period in which they arise. Dividends declared are included in dividend income.

All purchases and sales of financial assets held for trading and at fair value through profit and loss that require delivery within the time frame established by regulation or market convention ('regular way' purchases and sales) are recognised at trade date, which is the date that the Group commits to purchase or sell the asset.

(b) Loans and receivables

Loans and receivables, which include investments in financings, are non-derivative financial assets with fixed or determinable payments that are not quoted

2 ACCOUNTING POLICIES (continued)

in an active market other than: (a) those that the Group intends to sell immediately or in the short term, which are classified as held for trading, and those that the entity upon initial recognition designates as at fair value through profit or loss; (b) those that the entity upon initial recognition designates as available for sale; or (c) those for which the holder may not recover substantially all of its initial investment, other than because of credit deterioration. In general, they arise when the Group provides money, goods or services directly to a debtor with no intention of trading the receivable and also includes purchased loans and receivables that are not quoted in an active market. Loans and receivables are carried at amortised cost using the effective yield method. All loans are recognised when cash is advanced to the customer.

(c) Held-to-maturity

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities and there is the intent and the ability to hold them to maturity. If more than an insignificant amount of held-to-maturity assets is sold, the entire category will be considered tainted and reclassified as available-for-sale.

Held-to-maturity investments are carried at amortised cost using the effective yield method, less any provision for impairment.

(d) Available-for-sale

Available-for-sale investments are those intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in exchange rates, equity prices or other market rates. All regular way purchases and sales of investment securities are recognised at trade date, which is the date that the entity commits to purchase or sell the asset.

Available-for-sale investments are initially recognised at fair value (which includes transaction costs) and subsequently carried at fair value. The fair values of quoted investments in active markets are based on current bid prices. If the market for a financial asset is not active or the asset is an unlisted security, the Group establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants.

Unrealised gains and losses arising from changes in the fair value of securities classified as available-for-sale are recognised in equity. When the securities are disposed of or impaired, the related accumulated fair value adjustments are included in the consolidated statement of income as gains or losses from investment securities. Dividends declared are included in dividend income.

Changes in the fair value of monetary securities denominated in a foreign currency and classified as available for sale are analysed between translation differences resulting from changes in amortised cost of the security and other changes in the carrying amount of the security. The translation differences on monetary securities are recognised in profit or loss; translation differences on non monetary securities are recognised in equity. Changes in the fair value of monetary and non-monetary securities classified as available for sale are recognised in equity.

Impairment of Financial Assets

The Group assesses at each balance sheet date whether there is objective evidence that a financial asset or group of financial assets is impaired.

(a) Assets carried at amortised cost

A financial asset or a group of financial assets is impaired if and only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset and that event has an impact on the estimated future cash flows of the asset that can be reliably estimated. If there is objective evidence that an impairment loss on loans and receivables or held-to-maturity investments carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of expected future cash flows discounted at the financial instrument's original effective rate of return, including any amounts recoverable from guarantees and collateral, and recognised in the consolidated statement of income.

2 ACCOUNTING POLICIES (continued)

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the previously recognised impairment loss is reversed through the consolidated statement of income.

In the case of Islamic financings to customers in countries where there is an increased risk of difficulties in servicing external debt, an assessment of the political and economic situation is made and additional country risk provisions may be established.

(b) Assets classified as available-for-sale

In the case of equity investments classified as available-for-sale, a significant or prolonged decline in the fair value of the security below their cost is considered in determining whether the assets are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss, measured as the difference between the acquisition cost and the current fair value less any impairment loss on that financial asset previously recognised, is removed from equity and recognised in the consolidated statement of income. If in subsequent periods the fair value of equity instruments increases, impairment losses previously recognised in the consolidated statement of income are not reversed but are recognised in equity as adjustments to fair value.

Impairment of non-financial assets

Assets that have an indefinite useful life are not subject to amortisation and are tested annually for impairment. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

Due from banks

Due from banks comprises mainly short term deposits in the form of parallel purchase and sale of currencies and commodities (PPSC), which are spot purchases of internationally traded currencies and commodities and a corresponding forward sale of the same. For the purpose of accounting, these are treated as term deposits and the return is recorded as income from investments in the statement of income.

Due from banks are included in the IAS39 category of "Financial Assets measured at Amortised Cost".

Intangible assets

(a) Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net identifiable assets of the acquired subsidiary/associate at the date of acquisition. Goodwill on acquisitions of associates is included in investments in associates. Goodwill is tested annually or more often if indicators exist for impairment and carried at cost less accumulated impairment losses. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is an asset's fair value less costs to sell. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

Goodwill is allocated to cash-generating units for the purpose of impairment testing.

(b) Computer software

Acquired computer software licenses are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortised on the basis of the expected useful lives (three to five years).

Costs associated with developing or maintaining computer software programs are recognised as an expense as incurred. Costs that are directly associated with the production of identifiable and unique software products controlled by the Group, and that will probably generate economic benefits exceeding costs beyond one year, are recognised as intangible assets. Direct costs include software development employee costs and an appropriate portion of relevant overheads.

2 ACCOUNTING POLICIES (continued)

Computer software development costs recognised as assets are amortised using the straight line method over their useful lives.

(c) Other acquired intangible assets

Other acquired intangible assets determined to have finite lives, such as core deposits and customer relationships, are amortised on a straight line basis over their estimated useful lives of up to twenty years. The original carrying amount of core deposits and customer relationships has been determined by independent appraisers, based on the interest differential on the expected deposit duration method.

Investment property

Investment property principally comprises office buildings and land which are held to earn rental income or for long-term capital appreciation or both. Investment property is carried at fair value, representing open market value determined annually by reference either to external valuers or to other independent valuation sources. Changes in fair values are recorded in the consolidated statement of income as part of other income. The Group does not classify operating leases as investment property.

Property, plant and equipment and depreciation

Property, plant and equipment are stated at historical cost less accumulated depreciation and impairment, except for land, which is shown at cost. Land is not depreciated. Cost includes expenditure that is directly attributable to the acquisition of the items.

Depreciation is calculated on the straight-line method to write off the cost of each asset over its estimated useful life as follows:

Buildings	50 years
Leasehold improvements	over the period of the lease
Furniture, equipment and motor vehicles	3-10 years

The Group depreciates freighter aircraft as the difference between the cost and its residual value, over the estimated holding period of this category of assets.

Depreciation is calculated separately for each significant part of an asset category. Where the carrying amount of an asset is greater than its estimated recoverable amount, it is written down immediately to its recoverable amount. The asset's residual value and useful life are reviewed, and adjusted if appropriate, at each balance sheet date.

Subsequent costs are included in the asset's carrying amount or are recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost can be measured reliably. All other repairs and renewals are charged to the consolidated statement of income during the financial period in which they are incurred.

Gains and losses on disposal of property, plant and equipment are determined by comparing proceeds with carrying amounts.

Leases

Total payments made under operating leases are charged to the consolidated statement of income on a straight-line basis over the period of the lease. When an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognised as an expense in the period in which termination takes place.

When a Group company is the lessee of property, plant and equipment and the Group has substantially all the risks and rewards of ownership, they are classified as finance leases. Finance leases are capitalised at the inception of the lease at the lower of the fair value of the leased property or the present value of the minimum lease payments. Each lease payment is allocated between the liability and finance charges so as to achieve a constant rate on the finance balance outstanding. The corresponding rental obligations, net of finance charges, are included in payables. The profit element of the finance cost is charged to the consolidated statement of income over the lease period. The asset acquired under finance leases is depreciated over the shorter of the useful life of the asset or the lease term.

When a Group company is the lessor and assets are held subject to a finance lease, the value of the lease

2 ACCOUNTING POLICIES (continued)

payments is recognised as a receivable. The difference between the gross receivable and the present value of the receivable is recognised as unearned finance income. Lease income is recognise over the term of the lease using the actuarial method.

Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events; it is more likely than not that an outflow of resources embodying economic benefits will be required to settle the obligation; and a reliable estimate of the amount of the obligation can be made. Provisions are measured at the present value of management's best estimate of the expenditure required to settle the present obligation at the balance sheet date.

Employee entitlements to annual leave and long service leave are recognised when they accrue to employees. A provision is made for the estimated liability for annual leave and long-service leave as a result of services rendered by employees up to the date of the consolidated balance sheet.

Non-current assets held for sale

The Group classifies a non-current asset (or disposal group) as held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use. A non-current asset must be available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such assets (or disposal groups). Its sale must be planned and committed and an active programme initiated to locate a buyer and complete the plan within one year. The asset (or disposal group) must be actively marketed for a price that is reasonable in relation to its current fair value.

A non-current asset held for sale is carried at the lower of its carrying amount and the fair value less costs to sell. Impairment losses are recognised through the consolidated statement of income for any initial or subsequent write down of the asset (or disposal group) to fair value less costs to sell. Subsequent gains in fair value less costs to sell are recognised to the extent they do not exceed the cumulative impairment losses previously recorded. A non-current asset is not depreciated while classified as held for sale or while part of a disposal group held for sale.

The Group separately classifies the non-current assets held for sale (or disposal group) in the consolidated balance sheet. Furthermore, all major classes of assets and liabilities are disclosed. Any cumulative income or expense is disclosed as a separate item within equity. Prior period amounts are not re-presented to reflect the classification of the assets (or disposal group) in the current period.

Non-current assets, which are to be abandoned, are not classified as held for sale and are reclassified as discontinued operations, to the extent they meet the requirements of discontinued operations in the paragraph which follows.

If a non-current asset (or disposal group) ceases to be classified as held for sale or as discontinued operations, the results of operations are reclassified and included in the consolidated statement of income from continuing operations for all periods presented.

Due to banks

Due to banks are included in the IAS 39 category of "Financial Liabilities measured at Amortised Cost".

Borrowings

Borrowings including Debt are recognised initially at fair value net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between proceeds net of transaction costs and the redemption value is recognised in the consolidated statement of income over the period of the borrowings using the effective return method.

Taxation

Taxes are provided and charged in the consolidated statement of income on the basis of the estimated tax expense payable currently and in future years, arising in respect of the results of current operations.

Deferred income taxes

Deferred income tax is provided, using the comprehensive liability method, for all temporary differences arising between the tax bases of assets and liabilities and their respective carrying values for financial reporting purposes. The amount of deferred taxes on these differences is determined using the provisions of local tax laws, including rates, and is

2 ACCOUNTING POLICIES (continued)

adjusted upon enactment of changes in these laws. Provision is made for potential taxes which could arise on the remittance of retained overseas earnings where there is a current intention to remit such earnings.

A deferred tax asset is recognised for all deductible temporary differences and carry forward of unused tax losses and tax credits to the extent that it is probable that future taxable profit will be available against which the deductible temporary differences and unused tax losses and tax credits can be utilised.

Deferred tax related to fair value re-measurement of investments available-for-sale which is charged or credited directly to the fair value reserve, is also credited or charged directly to the fair value reserve and is subsequently recognised in the consolidated statement of income together with the deferred gain or loss.

Deferred tax related to fair value remeasurement, which is charged or credited to the consolidated statement of income, is also charged or credited to the consolidated statement of income.

Retirement benefit plans

The Group operates a number of defined benefit and defined contribution pension plans throughout the world, the assets of which are generally held in separate trustee-administered funds. The pension plans are generally funded by payments from employees and by the relevant Group companies, taking into account the recommendations of independent qualified actuaries.

For defined benefit plans, the pension accounting costs are assessed using the projected unit credit method. Under this method, the cost of providing pensions is charged to the consolidated statement of income so as to spread the regular cost over the service lives of employees in accordance with the advice of qualified actuaries who carry out a valuation of the plans every year. The pension obligation is measured as the present value of the estimated future cash outflows using high standard corporate bond rates which have terms to maturity approximating the terms of the related liability. Actuarial gains and losses arising from experience adjustments, and changes in actuarial assumptions, in excess of the greater of 10% of the value of plan assets or 10% of the defined benefit obligation, are charged or credited to income over the employees' expected average remaining working lives.

The Group's contributions to defined contribution pension plans are charged in the consolidated statement of income in the year to which they relate.

Share capital

Incremental costs directly attributable to the issue of new shares or options or to the acquisition of a business are shown in equity as a deduction, net of tax, from the proceeds.

Dividends on share capital are recognised as an appropriation in equity in the period in which they are declared. Dividends for the year which are declared after the date of the statement of financial position are dealt with in note 36.

Share-based payments

The Bank has adopted IFRS 2 Share-based Payments with respect to shares issued to employees at below fair value. As a result, the Bank has charged the cost of such payment, being the difference between the deemed fair value of the shares and the proceeds received, to the consolidated statement of income and credited this amount to the share premium.

The Bank has implemented an incentive scheme whereby certain employees will be entitled to a cash payment, calculated by reference to the difference between the book value per share as at the grant date and the higher of the book value per share or the last traded price recorded on the Bahrain Stock Exchange as at the end of the vesting period, subject in either case to a maximum amount per share. The estimated liability under this incentive scheme is charged to staff costs over the vesting period.

Treasury shares

Where any Group company purchases the Bank's equity share capital (treasury shares), the consideration paid, including any directly attributable incremental costs is deducted from equity attributable to the Bank's equity holders until the shares are cancelled, reissued or disposed off. Where such shares are subsequently sold or reissued, any consideration received, net of any directly attributable incremental transaction costs is included in equity attributable to the Bank's equity holders.

2 ACCOUNTING POLICIES (continued)

Acceptances

Acceptances comprise undertakings by the Group to pay bills of exchange drawn on customers. The Group expects most acceptances to be settled simultaneously with the reimbursement from the customers. Acceptances are accounted for as off-balance sheet transactions and are disclosed as contingent liabilities and commitments.

Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition, including cash and non-restricted balances with central banks and amounts due from other banks.

Fiduciary activities

The Group through its banking subsidiaries provides fund management and advisory services to third parties which involve the Group making allocation and purchase and sale decisions in relation to a wide range of financial instruments. Those assets that are held in a fiduciary capacity are not included in these consolidated financial statements.

Income arising from fund management and advisory services comprises the revenues earned from the management of the funds in the modarabas accrued on the basis of the terms and conditions of the related management agreements. Funds under management represent amounts invested by clients and placed with funds managed by the Group.

3. FINANCIAL RISK MANAGEMENT

a. Strategy in using financial instruments

By its nature, the Group's activities are principally related to the use of financial instruments. The Group accepts investments from customers at varying rates of return and for various periods and seeks to earn above average profits by investing these funds in high quality assets. The Group seeks to increase these margins by consolidating short-term funds and investing for longer periods at higher return potential whilst maintaining sufficient liquidity to meet all claims that might fall due.

The Group also seeks to raise its profit margins by obtaining above average margins, net of provisions, through transactions with commercial and retail customers. Such exposures involve not just on-balance sheet Islamic financings but the Group also enters into Islamically acceptable guarantees and other commitments such as letters of credit and performance and other bonds.

The Group also trades in financial instruments where it takes positions in traded and over the counter instruments including derivatives to take advantage of short-term market movements in the equity and bond markets and in currency and profit rates. The individual subsidiary's Boards place trading limits on the level of exposure that can be taken in relation to both overnight and intra-day market positions. With the exception of specific hedging arrangements, foreign exchange and profit rate exposures associated with these derivatives are normally offset by entering into counterbalancing positions, thereby controlling the variability in the net cash amounts required to liquidate market positions.

The Group utilises the following derivative instruments for both hedging and non-hedging purposes:

(i) Currency forwards represent commitments to purchase foreign and domestic currency, including undelivered spot transactions; (ii) equity futures are contractual obligations to receive or sell shares on a future date at a specified price established in an organised financial market; and (iii) equity options are contractual agreements under which the seller (writer) grants the purchaser (holder) the right, but not the obligation, either to buy (a call option) or sell (a put option) at or by a set date or during a set period, a specific amount of shares at a predetermined price. In consideration for the assumption of the risk, the seller receives a premium from the purchaser. Options may be either exchange-traded or negotiated between the Group and a customer (over the counter).

b. Capital management

The Bank's objectives when managing capital, which is a broader concept than the 'equity' on the face of balance sheets, are:

(i) To comply with the capital requirements set by the regulators of the banking jurisdictions where the Group operates;

3 FINANCIAL RISK MANAGEMENT (continued)

(ii) To safeguard the Bank's ability to continue as a going concern so that it can continue to provide returns for shareholders and benefits for other stakeholders; and

(iii) To maintain a strong capital base to support the development of its business.

Capital adequacy and the use of regulatory capital are monitored regularly by the Bank's management, employing techniques based on the guidelines developed by the Basel Committee, as implemented by the Central Bank of Bahrain for supervisory purposes. The required information is filed with the Central Bank of Bahrain on a quarterly basis.

The Central Bank of Bahrain requires each bank or banking group to: (a) hold the minimum level of the regulatory capital and (b) maintain a ratio of total regulatory capital to the consolidated risk-weighted exposures (the 'Basel I ratio') at the agreed minimum of 12%. In addition, those individual banking subsidiaries or similar financial institutions not incorporated in the Kingdom of Bahrain are directly regulated and supervised by their local banking supervisor, whose requirements may differ from country to country.

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

(i) Tier 1 capital: share capital (net of the book value of any treasury shares), minority interests arising on consolidation from interests in permanent shareholders' equity, retained earnings and reserves created by appropriations of retained earnings. The book value of goodwill is deducted in arriving at Tier 1 capital; and

(ii) Tier 2 capital: qualifying subordinated loan capital, collective impairment allowances and qualifying asset revaluation reserves including unrealised gains arising on the fair valuation of equity instruments held as available for sale.

The risk-weighted assets are measured by means of a hierarchy of risk weights classified according to the nature of and reflecting an estimate of credit, market and other risks associated with each asset and counterparty, taking into account any eligible collateral or guarantees. A similar treatment is adopted for off-balance sheet exposure, with some adjustments to reflect the more contingent nature of the potential losses.

c. Risk management

The Group's activities expose it to a variety of financial risks and those activities involve the analysis, evaluation, acceptance and management of some degree of risk or combination of risks. The Group's aim is to achieve an appropriate balance between risk and return and minimise potential adverse effects on the Group's financial performance.

The Group's risk management policies are designed to identify and analyse these risks, to set appropriate risk limits and controls, and to monitor the risks and adherence to limits by means of reliable and up-to-date information systems. The Group regularly reviews its risk management policies and systems to reflect changes in markets, products and emerging best practice.

Risk management is carried out by individual entities within the Group under policies approved by their respective Boards of Directors. The Boards provide written principles for overall management, as well as written policies covering specific areas, such as market rate risk, credit risk, use of derivative financial instruments and non-derivative financial instruments. In addition, internal audit is responsible for the independent review of risk management and the control environment. The most important types of risk are credit risk, liquidity risk, market risk and other operational risk.

d. Credit risk

The Group takes on exposure to credit risk, which is the risk that a counterparty will cause a financial loss for the Group by failing to discharge an obligation. Credit exposures arise principally in lending activities that lead to loans and advances (including accounts receivables). There is also credit risk in off-balance sheet financial instruments, such as loan commitments. Credit risk management and control are carried out by credit risk management teams, which report to the Boards of Directors through risk management committees.

3 FINANCIAL RISK MANAGEMENT (continued)

Credit risk measurement

Loans and advances

The Group has well defined credit structures under which credit committees, comprising senior officers with required credit background, critically scrutinise and sanction financing. The Group's exposure to credit is measured on an individual counterparty basis, as well as by groups of counterparties that share similar attributes. To reduce the potential of risk concentration, credit limits are established and monitored in light of changing counterparty and market conditions. Besides financial, industry and transaction analysis, the credit evaluation also includes risk rating systems which gauge risk rating of all customers.

Risk limit control and mitigation policies

The Group manages limits and controls concentrations of credit risk wherever they are identified - in particular, to individual counterparties and groups, and to industries and countries.

The Group structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to geographical and industry segments. Such risks are monitored on a revolving basis and are subject to an annual or more frequent review, when considered necessary. Limits on the level of credit risk by industry sector and by country are approved by the Boards of Directors of Group entities.

The exposure to any one borrower including banks and brokers is further restricted by sub-limits covering on- and off-balance sheet exposures, and daily delivery risk limits in relation to trading items such as forward foreign exchange contracts. Actual exposures in relation to daily delivery risk limits are monitored on a daily basis, whereas other limits are monitored on a quarterly, semi annual or annual basis.

Exposure to credit risk is also managed through regular analysis of the ability of borrowers and potential borrowers to meet payment obligations and by changing these lending limits where appropriate.

Some other specific control and mitigation measures are outlined below.

(a) Collateral

The Group employs a range of policies and practices to mitigate credit risk. The most traditional of these is the taking of security for funds advances, which is common practice. The principal collateral types for loans and advances are:

(i) Mortgages over residential and commercial properties;

(ii) Charges over business assets such as premises, inventory and accounts receivable;

(iii) Charges and pledges over financial instruments such as debt securities and equities.

In order to minimise the credit loss the Group will seek immediate recovery or additional collateral from the counterparty as soon as impairment indicators are noticed for the relevant individual loans and advances.

Collateral held as security for financial assets other than loans and advances is determined by the nature of the instrument.

(b) Derivatives

The Group maintains control limits on net open derivative positions (i.e, the difference between purchase and sale contracts), by both amount and term. At any one time, the amount subject to credit risk is limited to the current fair value of instruments that are favourable to the Group (i.e., assets where their fair value is positive), which in relation to derivatives is only a small fraction of the contract, or notional values used to express the volume of instruments outstanding. This credit risk exposure is managed as part of the overall lending limits with customers, together with potential exposures from market movements. Collateral or other security is not usually obtained for credit risk exposures on these instruments, except where the Group requires margin deposits from counterparties.

Settlement risk arises in any situation where a payment in cash, securities or equities is made in the expectation of a corresponding receipt in cash, securities or equities. Daily settlement limits are established for each counterparty to cover the aggregate of all settlement risk arising from the Group's market transactions on any single day.

3 FINANCIAL RISK MANAGEMENT (continued)

(c) Credit-related commitments

The primary purpose of these instruments is to ensure that funds are available to a customer as required. Guarantees and standby letters of credit carry the same credit risk as loans. Documentary and commercial letters of credit – which are written undertakings by the Group on behalf of a customer authorising a third party to draw drafts on the Group up to a stipulated amount under specific terms and conditions – are collateralised by the underlying shipments of goods to which they relate and by other collaterals that are obtained in the normal course of business and therefore carry less risk than a direct loan.

Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. With respect to credit risk on commitments to extend credit, the Group is potentially exposed to loss in an amount equal to the total unused commitments, where these are not unconditionally cancellable. However, the likely amount of loss is less than the total unused commitments, as most commitments to extend credit are contingent upon customers maintaining specific credit standards. The Group monitors the term to maturity of credit commitments because longer-term commitments generally have a greater degree of credit risk than shorter-term commitments.

Impairment and provisioning policies

The internal rating systems referred to in "Credit Risk Measurement" focus more on credit-quality mapping from the inception of the lending and investment activities. In contrast, impairment provisions are recognised for financial reporting purposes only for losses that have been incurred at the balance sheet date based on objective evidence of impairment. Due to the different methodologies applied, the amount of incurred credit losses provided for in the financial statements are usually lower than the amount determined from the expected loss model that is used for internal operational management purposes.

The Group's internal rating tools and guidelines assist management to determine whether objective evidence of impairment exists under IAS 39 based on the following criteria set out by the Group:

(i) Delinquency in contractual payments of principal or return;

(ii) Cash flow difficulties experienced by the borrower (e.g., equity ratio, net income percentage of sales);

(iii) Breach of loan covenants or conditions;

(iv) Initiation of bankruptcy proceedings;

(v) Deterioration of the borrower's competitive position; and

(vi) Deterioration in the value of collateral;

The Group's policy requires the review of individual financial assets that are above materiality thresholds at least annually or more regularly when individual circumstances require. Impairment allowances on individually assessed accounts are determined by an evaluation of the incurred loss at balance sheet date on a case-by-case basis, and are applied to all individually significant accounts. The assessment normally encompasses collateral held (including re-confirmation of its enforceability) and the anticipated receipts for that individual account.

Collectively assessed impairment allowances are provided for: (i) portfolios of homogeneous assets that are individually below materiality thresholds; and (ii) losses that have been incurred but have not yet been identified, by using the available historical experience, experienced judgement and statistical techniques.

CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of United States Dollars)

3 FINANCIAL RISK MANAGEMENT (continued)

	Maximum exposure	
	2007	**2006**
Credit risk exposure relating to on-balance sheet assets are as follows:		
Due from banks	16,172	1,900
Investments in financings		
Corporate financing	1,112,567	943,482
Bank and other financial institutions	389,048	335,602
Agricultural financing	27,934	17,928
Consumer financing	255,704	253,634
Government/public financing	19,525	1,760
Other financing	77,250	82,629
Investment securities	638,579	403,090
Accounts receivable	101,856	65,902
Credit risk exposure relating to off-balance sheet items are as follows:		
Financial guarantees and irrevocable letters of credit	713,812	625,029
Financing commitments, undrawn facilities and other credit related liabilities	698,446	551,517
At 31 December	**4,050,893**	**3,282,473**

Restructuring activities include extended payment arrangements, approved external management plans, modification and deferral of payments. Following restructuring, a previously overdue customer account is reset to a normal status and managed together with other similar accounts. Restructuring policies and practices are based on indicators or criteria which, in the judgement of management, indicate that payment will most likely continue. These policies are kept under continuous review.

Renegotiated loans reported under corporate financing, that would otherwise be past due or impaired, amounted to $0.7 million at 31 December 2007 (2006: $6.1 million).

CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of United States Dollars)

3 FINANCIAL RISK MANAGEMENT (continued)

Concentration of assets and liabilities

Assets and liabilities of the Group are located in the following geographical regions and industry sectors:

Geographical regions

At 31 December 2007	Asia/ Pacific	Middle East	Europe	North America	Others	Total
Cash and cash equivalents	201,858	266,551	49,723	57,172		575,304
Due from banks		16,172				16,172
Investments in financings	1,535,871	68,287	262,072	15,798		1,882,028
Investment securities	532,894	59,208	10,535	35,942		638,579
Investment property	20,017	51,045	142,005			213,067
Accounts receivable	13,072	36,079	29,652	23,053		101,856
Investments in associates	62,720	131,812	17			194,549
Property, plant and equipment	36,999	51,524	41,842	565		130,930
Intangible assets	2,630	313,820	4,917	4,937		326,304
Total assets	**2,406,061**	**994,498**	**540,763**	**137,467**		**4,078,789**
Customer current accounts	306,912	239,357	21,779	475	716	569,239
Customer investment accounts	1,358,773	5,172	2,971	1,922	66	1,368,904
Due to banks	170,376	157,848	63,992	1,809		394,025
Other borrowings	16,397	79,842	27,000			123,239
Accounts payable	114,414	140,648	10,928	3,448		269,438
Current tax payable	8,829		339	7		9,175
Deferred tax liability	55,089		5,283			60,372
Total liabilities	**2,030,790**	**622,867**	**132,292**	**7,661**	**782**	**2,794,392**
Net on-balance sheet position	**375,271**	**371,631**	**408,471**	**129,806**	**(782)**	**1,284,397**
Contingent liabilities and commitments	**1,253,375**	**131,933**	**11,557**	**15,378**	**15**	**1,412,258**

At 31 December 2006						
Total assets	**1,936,985**	**640,228**	**636,450**	**105,092**		**3,318,755**
Total liabilities	**1,663,038**	**442,487**	**74,295**	**14,603**	**677**	**2,195,100**
Net on-balance sheet position	**273,947**	**197,741**	**562,155**	**90,489**	**(677)**	**1,123,655**
Contingent liabilities and commitments	**1,055,683**	**115,761**	**5,090**	**-**	**12**	**1,176,546**

CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of United States Dollars)

3 FINANCIAL RISK MANAGEMENT (continued)

Concentration of assets and liabilities (continued)

Industry sectors

At 31 December 2007	Banks and finance institutions	Trading and manufacturing	Property and construction	Services	Private individuals	Textile	Other	Total
Cash and cash equivalents	337,946		147,745	76,902			12,711	575,304
Due from banks	16,172							16,172
Investments in financings	376,655	263,442	199,367	419,222	114,882	300,365	208,095	1,882,028
Investment securities	542,002	14,848	50,424	2,748		884	27,673	638,579
Investment property	749		212,318					213,067
Accounts receivable	28,349	4,065	38,160	4,605	9,103		17,574	101,856
Investments in associates	153,231	1,652	39,666					194,549
Property, plant and equipment			88,865	41,500			565	130,930
Intangible assets	321,368						4,936	326,304
Total assets	**1,776,472**	**284,007**	**776,545**	**544,977**	**123,985**	**301,249**	**271,554**	**4,078,789**
Customer current accounts		77,027	45,505	82,949	286,282	9,270	68,206	569,239
Customer investment accounts	68,260	116,770	45,513	237,346	276,132	12,023	612,860	1,368,904
Due to banks	394,025							394,025
Other borrowings			53,050	70,189				123,239
Accounts payable	40,760	15,112	81,764	7,905	19,502	3,314	101,081	269,438
Current tax payable				9,175				9,175
Deferred tax liability			4,111	56,261				60,372
Total liabilities	**503,045**	**208,909**	**229,943**	**463,825**	**581,916**	**24,607**	**782,147**	**2,794,392**
Net on-balance sheet position	**1,273,427**	**75,098**	**546,602**	**81,152**	**(457,931)**	**276,642**	**(510,593)**	**1,284,397**
Contingent liabilities and commitments	**371,667**	**199,420**	**103,259**	**192,955**	**16,729**	**221,439**	**306,789**	**1,412,258**

At 31 December 2006	Banks and finance institutions	Trading and manufacturing	Property and construction	Services	Private individuals	Textile	Other	Total
Total assets	**1,655,568**	**286,745**	**267,670**	**307,610**	**339,470**	**224,601**	**237,091**	**3,318,755**
Total liabilities	**767,706**	**143,441**	**91,647**	**247,923**	**664,128**	**19,806**	**260,449**	**2,195,100**
Net on-balance sheet position	**887,862**	**143,304**	**176,023**	**59,687**	**(324,658)**	**204,795**	**(23,358)**	**1,123,655**
Contingent liabilities and commitments	**282,088**	**153,177**	**62,552**	**43,183**	**82,425**	**195,708**	**357,413**	**1,176,546**

(Expressed in thousands of United States Dollars)

3 FINANCIAL RISK MANAGEMENT (continued)

Investments in financings and receivables past due but not impaired

Investments in financings and receivables less than 90 days past due are not considered impaired, unless other information is available to indicate the contrary. The gross amount of investments in financings by class and receivables that were past due but not impaired were as follows:

2007	Investments in financings							
	Corporate financing	Banks and other financial institutions	Agricultural financing	Consumer financing	Government/ Public financing	Other financing	Other receivables	Total
Past due up to 30 days	88,315	1,053	1,193	2,057		53,880	2,368	148,866
Past due 30 – 60 days	86,276	206	265	43,228	50			130,025
Past due 60 – 90 days	90,484	100	411	34223				125,218
Past due greater than 90 days	568	125	1,683	4,941		133	4,943	12,393
Total	**265,643**	**1,484**	**3552**	**84,449**	**50**	**54,013**	**7,311**	**416,502**
Fair value of collateral	192,556	2,149	1,491	5,445				201,641

Included in the above $201.6 million collateral, is $200.9 million relating to financings of $91.1 million where the coverage of client exposure is 100% or greater; whereas $0.7 million relating to financings of $1.5 million, the coverage is less than 100%.

2006	Investments in financings							
	Corporate financing	Banks and other financial institutions	Agricultural financing	Consumer financing	Government/ Public financing	Other financing	Other receivables	Total
Past due up to 30 days	34,453		497	12,287			3,314	50,551
Past due 30 – 60 days	48,746		1,090	16,124		573		66,533
Past due 60 – 90 days	9,122		151	4,757				14,030
Past due greater than 90 days			336			9	653	998
Total	**92,321**		**2,074**	**33,168**		**582**	**3,967**	**132,112**
Fair value of collateral	154,916		2,204	44,362				201,482

Included in the above $201.5 million collateral, is $201.4 million relating to financings of $127.1 million where the coverage of client exposure is 100% or greater; whereas $0.1 million relating to financings of $0.1 million, the coverage is less than 100%.

Upon initial recognition of investments in financings, the fair value of collateral is based on valuation techniques commonly used for the corresponding assets. In subsequent periods, the fair value is updated by reference to market prices or indices of similar assets.

3 FINANCIAL RISK MANAGEMENT (continued)

e. Market risk

The Group takes on exposure to market risks, which is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risks arise from open positions in currency, equity, profit rate and other products, all of which are exposed to general and specific market movements and changes in the level of volatility of market rates or prices such as profit rates, credit spreads, foreign exchange rates and equity prices. The Group separates exposures to market risk into either trading or non-trading portfolios.

The market risks arising from trading and non-trading activities are monitored by individual entities within the Group. Regular reports are submitted to management.

Trading portfolios include those positions arising from market-making transactions where the Group acts as principal with clients or with the market. Non-trading portfolios primarily arise from the management of the entity's retail and commercial banking assets and liabilities. Non-trading portfolios also consist of foreign exchange and equity risks arising from the Group's available-for-sale investments.

(a) Foreign exchange risk

The Group takes on exposure to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The Boards of Directors of individual entities within the Group set limits on the level of exposure by currency and in aggregate for both overnight and intra-day positions, which are monitored daily.

(b) 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. Movement in the market profit rates may affect the earnings of the Group.

The profit rate exposure taken by the Group arises from investing in corporate, small medium enterprises, consumer financing, investment banking and interbank activities where variation in market profit rates may affect the profitability of the Group. The risk is managed by the management of individual entities. The profit rate dynamics are reviewed at regular intervals and repricing of assets and liabilities are adjusted to ensure that the spread of the subsidiary remains at an acceptable level.

The financings and deposits of the Group are broadly linked to the market variable rates and thus get automatically repriced on a periodic basis based on profit rate scenarios.

CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of United States Dollars)

3 FINANCIAL RISK MANAGEMENT (continued)

Price risk

The table below summarises the impact of increase/decrease of equity indices on the Group's post tax profit for the year and on other components of equity. The analysis is based on the assumptions that equity indices increased/decreased by 10% (2006: 10%) with all other variables held constant and all the Group's equity instruments moved according to the historical correlation with the indices.

	Impact on post-tax profits		Impact on other components of equity	
Index	**2007**	2006	**2007**	2006
Pakistan stock exchange (+/-10%)	-	35	15,009	14,328

Currency risk

Assuming that all other variables held constant, the impact of currency risk on the statement of income/equity based on reasonable shift is summarized below:

	USD/PKR	USD/EUR	USD/BHD	PKR/GBP
As at 31 December 2007				
Total currency exposure	379,341	34,923	75,011	213
Reasonable shift	2.26%	0.32%	0.35%	0.53%
Total effect on income	**8,573**	**112**	**263**	**1**

	USD/PKR	USD/EUR	USD/BHD	PKR/GBP
As at 31 December 2006				
Total currency exposure	204,599	31,940	25,350	66,385
Reasonable shift	3.6%	1.3%	0.9%	3.6%
Total effect on income	**7,366**	**415**	**228**	**2,390**

The basis for calculation of the reasonable shift is arrived at by comparing the foreign exchange spot rate at 31 December as compared to the one year forward rate at the same period.

CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of United States Dollars)

3 FINANCIAL RISK MANAGEMENT (continued)

Currency exposure

At 31 December 2007	United States Dollar	Pakistan Rupee	Swiss Franc	Bahrain Dinar	Euro	Other	Total
Cash and cash equivalents	314,348	131,684	11,564	88,845	4,778	24,085	575,304
Due from banks	9,465			6,707			16,172
Investments in financings	377,335	1,441,289	59	29,748	28,660	4,937	1,882,028
Investment securities	119,441	496,553	466	21	5,461	16,637	638,579
Investment property	48,015	20,017	41,670	45,889	51,623	5,853	213,067
Accounts receivable	50,984	12,692	4,460	512	20,613	12,595	101,856
Investments in associates	125,343	547				68,659	194,549
Property, plant and equipment	46,268	36,999	331	46,757	11	564	130,930
Intangible assets	317,314	2,630	858	565	1	4,936	326,304
Total assets	**1,408,513**	**2,142,411**	**59,408**	**219,044**	**111,147**	**138,266**	**4,078,789**
Customer current accounts	161,846	291,236	25	101,448	11,802	2,882	569,239
Customer investment accounts	116,879	1,237,902			2,881	11,242	1,368,904
Due to banks	231,476	156,622			3,092	2,835	394,025
Other borrowings	53,792	16,397		53,050			123,239
Accounts payable	47,154	113,624	4,110	100,664	211	3,675	269,438
Current tax payable	7	8,829	314		25		9,175
Deferred tax liability		55,089	5,283				60,372
Total liabilities	**611,154**	**1,879,699**	**9,732**	**255,162**	**18,011**	**20,634**	**2,794,392**
Net on-balance sheet position	**797,359**	**262,712**	**49,676**	**(36,118)**	**93,136**	**117,632**	**1,284,397**
Contingent liabilities and commitments	**452,782**	**800,170**	**5,022**	**30,965**	**88,479**	**34,840**	**1,412,258**
At 31 December 2006							
Total assets	**1,292,942**	**1,818,098**	**54,495**	**65,803**	**19,008**	**68,409**	**3,318,755**
Total liabilities	**489,518**	**1,585,592**	**11,251**	**89,555**	**4,784**	**14,400**	**2,195,100**
Net on-balance sheet position	**803,424**	**232,506**	**43,244**	**(23,752)**	**14,224**	**54,009**	**1,123,655**
Contingent liabilities and commitments	**358,336**	**731,745**	**3,442**	**8,407**	**33,243**	**41,373**	**1,176,546**

CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of United States Dollars)

3 FINANCIAL RISK MANAGEMENT (continued)

Profit rate risk

The table below summarises the Group's exposure to profit rate risks. It includes the Group's financial instruments at carrying amounts, categorised by the earlier of contractual repricing or maturity dates.

	Up to One month	One-three months	Three-twelve months	One-five years	Over five years	Non rate sensitive	Total
As at 31 December 2007							
Assets							
Cash and cash equivalents	296,230	29,151				249,923	575,304
Due from banks	6,707	9,465					16,172
Investment in financings	422,044	489,227	518,567	341,916	92,473	17,801	1,882,028
Investment securities available for sale	16,127	61,539	207,996	25,295	21,946	305,676	638,579
Other assets	129		8,614	27,792			36,535
Total financial assets	**741,237**	**589,382**	**735,177**	**395,003**	**114,419**	**573,400**	**3,148,618**
Liabilities							
Customer current accounts						569,239	569,239
Customer investment accounts	568,191	309,151	423,334	68,200	28		1,368,904
Due to banks	58,642	184,679	123,101	19,981	3,394	4,228	394,025
Other borrowings	27,000		42,934			53,305	123,239
Accounts payable		5,087				264,351	269,438
Total financial liabilities	**653,833**	**498,917**	**589,369**	**88,181**	**3,422**	**891,123**	**2,724,845**
Total repricing gap	**87,404**	**90,465**	**145,808**	**306,822**	**110,997**	**(317,723)**	**423,773**

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(Expressed in thousands of United States Dollars)

3 FINANCIAL RISK MANAGEMENT (continued)

	Up to One month	One-three months	Three-twelve months	One-five years	Over five years	Non rate sensitive	Total
As at 31 December 2006							
Assets							
Cash and cash equivalents	364,661	53,321				201,995	619,977
Due from banks		1,900					1,900
Investment in financings	165,876	574,434	708,010	113,209	65,624	7,882	1,635,035
Investment securities available for sale	51,892	60,930	35,852	36,267	31,768	186,381	403,090
Other assets		592	15,049	4,182			19,823
Total financial assets	**582,429**	**691,177**	**758,911**	**153,658**	**97,392**	**396,258**	**2,679,825**
Liabilities							
Customer current accounts						383,704	383,704
Customer investment accounts	512,693	249,465	237,206	52,507			1,051,871
Due to banks	85,612	240,099	206,105			4,151	535,967
Accounts payable		5,002				172,863	177,865
Total financial liabilities	**598,305**	**494,566**	**443,311**	**52,507**		**560,718**	**2,149,407**
Total repricing gap	**(15,876)**	**196,611**	**315,600**	**101,151**	**97,392**	**(164,460)**	**530,418**

	USD	PKR	GBP	BHD
As at 31 December 2007				
Total profit rate exposure	130,137	244,471	12,466	64,992
Reasonable shift	1.14%	1.35%	0.30%	0.58%
Total effect on income	**1,484**	**3,300**	**37**	**377**

	USD	PKR	GBP	BHD
As at 31 December 2006				
Total profit rate exposure	183,753	59,645	23,820	69,492
Reasonable shift	1.02%	0.32%	0.55%	1.65%
Total effect on income	**1,874**	**191**	**131**	**1,147**

The basis for calculation of the reasonable shift is arrived at by comparing the interbank lending rate at the beginning and the end of the year.

(Expressed in thousands of United States Dollars)

3 FINANCIAL RISK MANAGEMENT (continued)

f. Liquidity risk

Liquidity risk is the risk that the Group is unable to meet its payment obligations associated with its financial liabilities when they fall due and to replace funds when they are withdrawn. The consequence may be the failure to meet obligations to repay investors and counter parties and fulfil commitments to lend.

Liquidity risk management process

The Group's liquidity risk management process, as carried out within the Group and monitored by management in individual entities within the Group, includes:

(i) Day-to-day funding, managed by monitoring future cash flows to ensure that requirements can be met. This includes replenishment of funds as they mature or are borrowed by customers. The Group maintains an active presence in money markets to enable this to happen;

(ii) Maintaining a portfolio of highly marketable assets that can easily be liquidated as protection against any unforeseen interruption to cash flow;

(iii) Monitoring balance sheet liquidity ratios against internal and regulatory requirements; and

(iv) Managing the concentration and profile of debt maturities.

Monitoring and reporting of treasury and capital market maturities is done through monitoring of daily maturities. Similarly the overall liquidity maintenance is done through monthly maturity gap analysis at balance sheet level. Hence, monitoring and reporting takes the form of regular and periodic cash flow measurement and projections. The starting point for those projections is an analysis of the contractual maturity of the financial liabilities and the expected collection date of the financial assets.

The Group also monitors unmatched medium-term assets.

The table below presents the cash flows payable by the Group under financial liabilities by remaining contractual maturities at the balance sheet date. The amounts disclosed in the table are the contractual undiscounted cash flows, whereas the Group manages the inherent liquidity risk based on expected cash inflows.

	Up to One month	One-three months	Three-twelve months	One-five years	Over five years	Total
As at 31 December 2007						
Liabilities						
Customer current account	569,239					569,239
Customer investment account	568,695	319,180	442,264	79,771	2,337	1,412,247
Due to banks	63,373	186,781	128,078	19,981	3,394	401,607
Other borrowings	261	524	32,494	88,377	26,271	147,927
Accounts payable	129,792	21,734	23,316	94,678		269,520
Current tax payable	25	266	55		8,829	9,175
Deferred tax liability				1,172	59,200	60,372
Total liabilities liquidity risk	**1,331,385**	**528,485**	**626,207**	**283,979**	**100,031**	**2,870,087**
Total assets liquidity risk	**887,890**	**778,201**	**896,971**	**835,196**	**680,531**	**4,078,789**

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(Expressed in thousands of United States Dollars)

3 FINANCIAL RISK MANAGEMENT (continued)

	Up to One month	One-three months	Three-twelve months	One-five years	Over five years	Total
As at 31 December 2006						
Liabilities						
Customer current account	383,704					383,704
Customer investment account	492,424	274,669	253,131	59,892	14,508	1,094,624
Due to banks	66,993	119,062	369,164	22,825		578,044
Accounts payable	150,347	11,411	12,081	2,049	2,083	177,971
Current tax payable			394		9,229	9,623
Deferred tax liability			79	1,032	34,959	36,070
Total liabilities liquidity risk	**1,093,468**	**405,142**	**634,849**	**85,798**	**60,779**	**2,280,036**
Total assets liquidity risk	**722,422**	**828,478**	**378,204**	**651,664**	**737,987**	**3,318,755**

The table below presents the cash flows payable by the Group under off-balance sheet liabilities.

	No later than one year	One-five years	Over five years	Total
As at 31 December 2007				
Acceptances and Endorsements	38,922	1,193		40,115
Guarantees and irrevocable letters of credit	370,869	197,079	26,751	594,699
Performance bid bonds	13,321	8,034	1,801	23,156
Other contingent	428		55,414	55,842
Undrawn facilities and other commitments to finance	448,591			448,591
Operating lease commitments	28	132	516	676
Open foreign currency Positions	101,653			101,653
Repurchased and Resale transactions	147,526			147,526
Total off-balance sheet liabilities	**1,121,338**	**206,438**	**84,482**	**1,412,258**

(Expressed in thousands of United States Dollars)

3 FINANCIAL RISK MANAGEMENT (continued)

	No later than one year	One-five years	Over five years	Total
As at 31 December 2006				
Acceptances and endorsements	58,715	2,587		61,302
Guarantees and irrevocable letters of credit	366,823	95,106	32,857	494,786
Performance bid bonds	9,652	2,084		11,736
Other contingent liabilities	989		964	1,953
Undrawn facilities and other commitments to finance	364,228	68,362		432,590
Operating lease commitments		51	521	572
Open foreign currency positions	54,681			54,681
Repurchase and resale transactions	118,926			118,926
Total off-balance sheet liabilities	**974,014**	**168,190**	**34,342**	**1,176,546**

Unrepresentative data

The quantitative data required for IFRS 7 disclosures encompassing market, credit and liquidity risks for the year ended 31 December 2006 was representative of the Group risk profile at that date and is determined by Group management to be representative for future periods. For the period prior to 15 August 2006, this data is not considered representative due to Group acquisitions and disposals (note 42).

Funding approach

Sources of liquidity are regularly reviewed to maintain a wide diversification by currency, geography, provider, product and term.

Assets available to meet liabilities and to cover outstanding loan commitments include cash and bank balances; loans and advances to banks; and loans and advances to customers. In the normal course of business, a proportion of customer loans contractually repayable within one year will be extended. In addition, assets have been pledged to secure liabilities. The Group would also be able to meet unexpected net cash outflows by selling securities and accessing additional funding sources such as undrawn facilities.

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES

The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities, income and expenses. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below:

Impairment of investments in financings

The Group reviews its investments in financings to assess impairment at least on a quarterly basis. In determining whether an impairment loss should be recorded in the consolidated statement of income, judgements are made as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows. This evidence may include observable data indicating that there has been an adverse change in the payment status of a borrower, or national or local economic

4 CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES (continued)

conditions that correlate with defaults on assets. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

Fair value and impairment of available-for-sale equity investments

The Group may from time to time hold investments in financial instruments that are not quoted in active markets. Fair values of such instruments are determined using valuation techniques. Where valuation techniques are used to determine fair values, they are validated and periodically reviewed by Group management.

The Group determines that available-for-sale equity 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. In making this judgment, the Group evaluates among other factors, the normal volatility in share price. In addition, impairment may be appropriate when there is evidence of a deterioration in the financial health of the investee, industry and sector performance, changes in technology, and operational and financing cash flows.

On occasion the Group may hold investments whose fair value cannot be reliably measured. In those instances, full disclosure with a description of the investment, the carrying value and an explanation of why fair value cannot be measured reliably are included in the notes to the financial statements.

Income taxes

The Group is subject to income taxes in some jurisdictions. Estimates are required in determining the provision for income taxes. There are some transactions and calculations for which the ultimate tax determination is uncertain. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences impact the income tax and deferred tax provisions in the period in which such determination is made.

Estimated impairment of goodwill

The Group tests annually whether goodwill has suffered any impairment, in accordance with the accounting policy stated in note 2. The recoverable amounts of cash-generating units have been determined based on estimated future cash flows and comparisons with market multiples. These calculations require the use of estimates, which are subject to judgement. Changes in the underlying assumptions may impact the reported numbers.

Pension obligations

The most significant assumptions the Group has to make in connection with the actuarial calculation of pension obligations and pension expenses affect the discount rate, the expected annual rate of compensation increase, the expected employee turnover rate, the expected average remaining working life, the expected annual adjustments to pensions and the expected annual return on plan assets. These assumptions are subject to review by the Group. A change in any of these key assumptions may have a significant impact on the projected benefit obligations, funding requirements and periodic pension cost.

5. SEGMENTS

a) Business segments

The Group and its associates are organised on a worldwide basis into the following business segments:

(i) retail banking incorporates private banking services, private customer current accounts, savings, deposits, investment savings products, custody, credit and debit cards, consumer loans and mortgages;

(ii) insurance includes life assurance, general insurance and reinsurance activities;

(iii) asset management encompasses managing clients' assets on either a fiduciary or trustee basis, carrying out securities trading operations, distributing mutual funds, granting documentary credit and other financings and holding deposits on behalf of clients.

(iv) corporate management comprises those activities of a supporting nature to the Group such as legal, financial control, audit and risk management, and the promotion of investment financing activities.

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(Expressed in thousands of United States Dollars)

5 SEGMENTS (continued)

Transactions between the business segments are on normal commercial terms and conditions.

For the year ended 31 December 2007

	Retail Banking	Insurance	Asset Mgmt	Corporate Mgmt	Elimination	Group
External income	321,389		22,571	126,009		469,969
Income from other segments			375	28,233	(28,608)	
Gain on sale of associated company	15,001					15,001
Total income	**336,390**		**22,946**	**154,242**	**(28,608)**	**484,970**
Distribution to investment account holders	(141,375)		(2,002)	(2,118)		(145,495)
Operating income	**195,015**		**20,944**	**152,124**	**(28,608)**	**339,475**
Operating expense	(85,205)		(10,014)	(44,293)		(139,512)
Operating profit	**109,810**		**10,930**	**107,831**	**(28,608)**	**199,963**
Share of net profit in associated companies	2,296	2,621	1,954	1,482		8,353
Profit before tax	112,106	2,621	12,884	109,313	(28,608)	208,316
Tax expense	(18,338)		(685)	(983)		(20,006)
Profit for the year	93,768	2,621	12,199	108,330	(28,608)	188,310
Minority interests	(40,001)		(974)	(44,580)		(85,555)
Profit after minority interests	**53,767**	**2,621**	**11,225**	**63,750**	**(28,608)**	**102,755**

At 31 December 2007

	Retail Banking	Insurance	Asset Mgmt	Corporate Mgmt	Elimination	Group
Segment assets	3,363,152		152,220	368,868		3,884,240
Investments in associated companies	18,571	83,154	61,337	31,487		194,549
Segment liabilities	2,670,790		50,939	72,663		2,794,392
Other segment items						
Depreciation	5,921		160	701		6,782
Amortisation of intangibles	13,073		107	580		13,760

CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of United States Dollars)

5 SEGMENTS (continued)

For the year ended 31 December 2006 (restated)

	Retail Banking	Insurance	Asset Mgmt	Corporate Mgmt	Elimination	Group
External income	102,801		39,988	24,829		167,618
Income from other segments			638	4,920	(5,558)	
Gain on sale of associated companies				4,613		4,613
Total income	**102,801**		**40,626**	**34,362**	**(5,558)**	**172,231**
Distribution to investment account holders	(46,343)		(971)	(670)		(47,984)
Operating income	56,458		39,655	33,692	(5,558)	124,247
Operating expense	(22,236)		(17,795)	(12,277)		(52,308)
Gain on sale of subsidiary				105,541		105,541
Operating profit	34,222		21,860	126,956	(5,558)	177,480
Share of profits/(losses) in associated companies	12,880	2,080	866	(131)		15,695
Profit before tax	47,102	2,080	22,726	126,825	(5,558)	193,175
Tax expense	(9,728)		(704)	(1,693)		(12,125)
Profit for the year	37,374	2,080	22,022	125,132	(5,558)	181,050
Minority interests	(13,065)		(427)			(13,492)
Profit after minority interests	**24,309**	**2,080**	**21,595**	**125,132**	**(5,558)**	**167,558**

At 31 December 2006 (restated)

	Retail Banking	Insurance	Asset Mgmt	Corporate Mgmt	Elimination	Group
Segment assets	2,685,535		103,884	376,816		3,166,235
Investments in associated companies	35,653	62,368	24,103	30,396		152,520
Segment liabilities	2,074,530		32,808	87,762		2,195,100
Other segment items						
Depreciation	1,578		342	95		2,015
Amortisation of intangibles	4,796		11	1		4,808

b) Geographical segments

A geographical segment is engaged in providing products and services within a particular economic environment that are subject to risks and returns that are different from those of segments operating in other economic environments. The Group is organised in five geographical segments which are Bahrain, Asia, other Middle East, Pakistan and Europe.

CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of United States Dollars)

5 SEGMENTS (continued)

The analysis below is based on legal vehicles.

For the year ended 31 December 2007

	Bahrain	Other Asia	Other Middle East	Pakistan	Europe	Group
Total income	209,680			237,500	22,789	469,969
Gain on sale of associated company	15,001					15,001
	224,681			237,500	22,789	484,970
Distribution to investment account holders	(20,916)			(122,577)	(2,002)	(145,495)
Operating income	203,765			114,923	20,787	339,475
Share of net profit in associated companies	5,717	1,954	523	159		8,353
Profit before tax	137,811	1,954	523	69,148	(1,120)	208,316
Tax expense	(960)			(17,720)	(1,326)	(20,006)
Profit for the year	136,851	1,954	523	51,428	(2,446)	188,310
Minority interests	(61,635)			(22,946)	(974)	(85,555)
Profit after minority interests	**75,216**	**1,954**	**523**	**28,482**	**(3,420)**	**102,755**

At 31 December 2007

	Bahrain	Other Asia	Other Middle East	Pakistan	Europe	Group
Segment assets	1,285,983			2,314,455	283,802	3,884,240
Investments in associated companies	124,539	61,324	8,139	547		194,549
Segment liabilities	708,868			2,028,536	56,988	2,794,392

NOTES

CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of United States Dollars)

5 SEGMENTS (continued)

For the year ended 31 December 2006 (restated)

	Bahrain	Other Asia	Other Middle East	Pakistan	Europe	Group
Total income	44,521		28,060	78,635	16,402	167,618
Gain on sale of associated company	4,613					4,613
	49,134		28,060	78,635	16,402	172,231
Distribution to investment account holders	(7,601)			(39,412)	(971)	(47,984)
Operating income	41,533		28,060	39,223	15,431	124,247
Gain on sale of subsidiary	105,541					105,541
Share of net profit in associated companies	4,229		535	10,065	866	15,695
Profit before tax	144,587		15,064	34,164	(640)	193,175
Tax expense	(1,412)			(8,900)	(1,813)	(12,125)
Profit for the year	143,175		15,064	25,264	(2,453)	181,050
Minority interests	(3,521)			(9,544)	(427)	(13,492)
Profit after minority interests	**139,654**		**15,064**	**15,720**	**(2,880)**	**167,558**

At 31 December 2006 (restated)

	Bahrain	Other Asia	Other Middle East	Pakistan	Europe	Group
Segment assets	1,051,741		(11,233)	1,891,729	233,998	3,166,235
Investments in associated companies	115,049	24,090	8,006	5,375		152,520
Segment liabilities	489,214			1,666,831	39,055	2,195,100

6. CASH AND CASH EQUIVALENTS

	2007	2006
Cash on hand	37,155	20,340
Cash at central banks – statutory reserve	83,899	64,512
Cash at central banks – current account	76,835	84,599
Cash at other banks	377,415	450,526
Total	**575,304**	**619,977**

(Expressed in thousands of United States Dollars)

7. INVESTMENTS IN FINANCINGS

Investments in financings are included in the IAS 39 category of "Loans and Receivables".

	2007	2006
Investments in financings	1,688,868	1,462,900
Financings subject to finance leases	260,257	233,347
Provision for impairment	(67,097)	(61,212)
Total	**1,882,028**	**1,635,035**

Financings subject to finance leases

	2007		
	Gross investment in finance leases receivable	Unearned future finance income on finance leases	Net investment in finance leases
Not later than one year	111,538	(24,419)	87,119
Later than one year and not later than five years	205,178	(32,542)	172,636
Later than five years	551	(49)	502
Total	**317,267**	**(57,010)**	**260,257**

The allowance for uncollectible finance lease receivables included in the provision for impairment amounted to $7.6 million at 31 December 2007.

Financings subject to finance leases

	2006		
	Gross investment in finance leases receivable	Unearned future finance income on finance leases	Net investment in finance leases
Not later than one year	74,095	(22,803)	51,292
Later than one year and not later than five years	214,892	(32,837)	182,055
Total	**288,987**	**(55,640)**	**233,347**

The allowance for uncollectible finance lease receivables included in the provision for impairment amounted to $5.6 million at 31 December 2006.

CONSOLIDATED FINANCIAL STATEMENTS

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8. COLLATERAL RECEIVED AND REPLEDGED

Assets held as collateral against advances to financial institutions

	Fair value amount	
	2007	**2006**
Assets available to be repledged with obligation to return	98,116	86,540
	98,116	**86,540**

At 31 December 2007 total collateral in the form of real estate was sold without obligation to return in the amount of $1.9 million (2006: $1.7 million).

At 31 December 2007 assets available to be repledged with obligation to return include the following:

	2007	**2006**
Market treasury bills	41,246	53,092
Pakistan investment bonds	35,468	10,570
Shares	21,402	22,878
Total	**98,116**	**86,540**

Repossessed collateral

The Group obtained assets by taking possession of collateral held as follows:

Nature of assets	Carrying amount	Balance sheet classification
2007		
Motor Vehicle	700	Investment in financing
Land	4,905	Property, plant and equipment
Total	**5,605**	
2006		
Motor vehicles	321	Investments in financings
Land	575	Non current assets held for sale
Land	425	Property, plant and equipment
Total	**1,321**	

Repossessed properties are sold as soon as practicable, with the proceeds used to reduce the outstanding indebtedness.

(Expressed in thousands of United States Dollars)

9. ALLOWANCE ACCOUNT FROM CREDIT LOSSES

Allowance for impairment

Reconciliation of allowance account for losses on investments in financings by class and receivables is as follows:

2007	Investments in financings							
	Corporate financing	Banks and other financial institutions	Agricultural financing	Consumer financing	Government/ Public financing	Other financing	Other receivables	Total
Balance at 1 January	57,595		30	3,373		214	84	61,296
Provision for impairment	2,319		1,676	12,496			99	16,590
Amounts recovered	(282)							(282)
Reversal of impairment provision	(7,837)		(13)	(1,141)				(8,991)
Foreign exchange	(1,039)		(32)	(262)			(3)	(1,336)
Balance at 31 December	**50,756**		**1,661**	**14,466**		**214**	**180**	**67,277**

Included in the above table are individual loan impairments and respective collateral as follows:

2007	Investments in financings							
	Corporate financing	Banks and other financial institutions	Agricultural financing	Consumer financing	Government/ Public financing	Other financing	Other receivables	Total
Individually impaired loans	49,834		1,661	13,662			214	65,371
Fair value of collateral	476,340	1,070	4,140	155,536	1,211			638,297

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9 ALLOWANCE ACCOUNT FROM CREDIT LOSSES (continued)

2006	Investments in financings							
	Corporate financing	Banks and other financial institutions	Agricultural financing	Consumer financing	Government/ Public financing	Other financing	Other receivables	Total
Balance at 1 January							1,110	1,110
Subsidiary acquistions	68,712			3,017			86	71,815
Subsidiary disposals							(552)	(552)
Provision for impairment	6,659		30	10,842		214		17,745
Amounts recovered	(11,861)			(9,672)				(21,533)
Reversal of impairment provision	(5,106)			(771)			(558)	(6,435)
Foreign exchange	(809)			(43)			(2)	(854)
Balance at 31 December	**57,595**		**30**	**3,373**		**214**	**84**	**61,296**

Included in the above table are individual loan impairments and respective collateral as follows:

2006	Investments in financings							
	Corporate financing	Banks and other financial institutions	Agricultural financing	Consumer financing	Government/ Public financing	Other financing	Other receivables	Total
Individually impaired loans	55,952		30	3,373		214	84	59,653
Fair value of collateral	94,718		552	7,542		21		102,833

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10. INVESTMENT SECURITIES

	2007	2006
Investment securities available-for-sale		
Investment securities – at fair value		
– Listed	208,614	192,258
– Unlisted	429,965	210,832
Total	**638,579**	**403,090**

Gains/(losses) from investment securities

	2007	2006
Derecognition of available-for-sale assets	44,739	388
Impairment provision	(2)	(1,589)
Total	**44,737**	**(1,201)**

The movement in investment securities may be summarised as follows:

	2007	2006
At 1 January	403,090	35,553
Subsidiary acquisitions		541,501
Additions	467,595	43,147
Disposals	(278,048)	(209,742)
Net gains/(losses) from changes in fair value	51,979	(999)
Exchange differences	(6,035)	(4,781)
Provision for impairment	(2)	(1,589)
At 31 December	**638,579**	**403,090**

11. FAIR VALUE OF FINANCIAL INSTRUMENTS

Financial instruments measured at fair value

The fair values of quoted investments in active markets are based on current bid prices. If there is no active market for a financial asset, the Group establishes fair value using valuation techniques. These include the use of recent arm's length transactions, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants. No amount was recognised in the consolidated statement of income for the change in fair value estimated using a valuation technique (2006: $Nil).

(Expressed in thousands of United States Dollars)

11 FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

The table below summarises the carrying amounts and fair values of those financial assets and liabilities not presented on the Group's balance sheet at their fair value.

	Carrying amount		Fair value	
	2007	2006	**2007**	2006
Financial assets				
Investments in financings				
Corporate financing	1,076,378	930,771	1,007,202	906,602
Banks and other financial institutions	156,864	106,326	154,645	103,724
Agricultural financing	28,011	17,928	29,768	16,773
Consumer financing	249,442	246,479	319,528	247,362
Government / Public financing	19,525			19,361
Other financing	5,650	14,265	5,776	13,725
Unlisted investments securities available-for-sale	496,553	346,399	496,553	349,537
Financial liabilities				
Customer investment accounts				
Private individuals	326,286	498,149	324,454	494,710
Financial institutions	63,194	72,889	62,839	72,386
Corporate institutions	974,357	404,817	968,885	402,022
Due to banks	162,157	247,401	162,079	247,370
Other borrowings	16,397		16,362	

Due from banks

Due from banks includes inter-bank placements and items in the course of collection.

Investments in financings

Investments in financings are net of provisions for impairment. The estimated fair value of investments in financings represents the discounted amount of estimated future cash flows expected to be received. Expected cash flows are discounted at current market rates to determine fair value.

Due to banks and customers

The estimated fair value of deposits with no stated maturity, which includes non-interest bearing deposits, is the amount repayable on demand.

Other borrowings

The aggregate fair values are calculated based on quoted market prices. For those notes where quoted market prices are not available, a discounted cash flow model is used based on a current yield curve appropriate for the remaining term to maturity.

Fair value

In the opinion of Group management, the fair value of those financial instruments which are measured at amortised cost in the consolidated balance sheet and not listed above are not significantly different from their carrying values since assets and liabilities are either short-term in nature or in the case of customer financing and deposits, are linked to market variable rates and hence are being regularly repriced.

(Expressed in thousands of United States Dollars)

12. INVESTMENT PROPERTY

	2007	2006
At 1 January	67,766	43,769
Subsidiary acquisitions	-	8,208
Additions	236,722	7,910
Disposals	(130,329)	(7,720)
Fair value gains during the year	36,033	13,205
Net exchange differences	2,875	2,394
At 31 December	**213,067**	**67,766**

Rental income from investment property amounting to $1.9 million (2006: $1.2 million) has been included in the consolidated statement of income under income from investment property. Direct operating expenses (including repairs and maintenance) arising from investment property that generated rental income amounted to $0.75 million (2006: $0.7 million). Direct operating expenses (including repairs and maintenance) arising from investment property that did not generate rental income amounted to $0.1 million (2006: $0.1 million). Such expenses have been included in the consolidated statement of income under general and administrative expenses.

Investment property under operating leases

The Group leases out part of its investment property under operating leases. The leases are for terms of one to five years. There were no contingent rents in 2007 (2006: $Nil).

The future aggregate minimum rentals receivable under non cancellable operating leases are as follows:

	2007	2006
Not later than one year	940	1,286
Later than one year and not later than five years	1,694	1,789
	2,634	**3,075**

13. ACCOUNTS RECEIVABLE

	2007	2006
Accounts receivable	67,926	28,804
Provision for impairment	(180)	(84)
Funds under management	24,528	30,859
Receivables from affiliated companies (note 41)	4,400	6,128
Receivables from associated companies (note 41)	4,666	40
Derivative financial instruments	516	155
	101,856	**65,902**

Included in accounts receivable are prepayments in the amount of $10.5 million (2006: $6.6 million) and loans to employees and directors of $7.8 million (2006: $7.3 million). The remaining balance relates primarily to fees, deposits and other receivables.

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13 ACCOUNTS RECEIVABLE (continued)

Included in the receivable from funds under management at 31 December 2007 is $16.8 million (2006: $9.3 million) in bridge financings made to real estate development funds which are sponsored by a subsidiary of the Group. Bridge financings are generally short-term in nature. The balance represents profit sharing, management fees and other fees and expenses due from clients.

Derivative financial instruments

	2007	
	Notional Amount	Fair value
Foreign exchange derivatives held for trading: Currency forwards sold	29,235	516

	2006	
	Notional Amount	Fair value
Foreign exchange derivatives held for trading: Currency forwards sold	114,006	155

14. INVESTMENTS IN ASSOCIATES

	2007	2006
At 1 January	152,520	157,451
Subsidiary acquisitions (note 42)	-	28,631
Conversion to subsidiaries through acquisition of controlling interest (note 42)	-	(90,916)
Share of results before tax	8,558	18,590
Share of tax	(205)	(2,895)
Dividends paid	(1,169)	(4,596)
Share of fair value gains	(103)	(5,193)
Additions (note 42)	52,158	71,549
Disposals (note 42)	(17,042)	(18,521)
Exchange differences	(168)	(1,580)
At 31 December	**194,549**	**152,520**

(Expressed in thousands of United States Dollars)

14 INVESTMENTS IN ASSOCIATES (continued)

The summarised financial information of the Group's principal associates is as follows:

Name and Country of incorporation	Assets	Liabilities	Revenue	Profit/ (loss)	Published price quotation	% owned Voting	% owned Economic
2007							
Unlisted:							
Solidarity Company BSC (c) (Bahrain)	341,285	82,808	20,448	7,010		34	34
First Leasing Bank B.S.C. (Closed) (Bahrain)	102,341	1,558	7,801	4,499		21	21
Citic International Assets Management Limited (Hong Kong)	312,298	10,768	20,781	13,634		20	20
Sanpak Engineering (Pakistan)	11,171	5,960	1,727	637		31	31
*Islamic Company for Production, Printing and Packing Materials "Icopack" (Egypt)	18,885	11,787	14,102	809		23	23
*Misr Company for Packing Materials "Egywrap" (Egypt)	20,303	17,536	27,982	1,274		23	23
Sakana Holistic Housing Solutions B.S.C. (Closed) (Bahrain)	43,170	11,223	1,000	(788)		50	50
Faysal Asset Management Limited (Pakistan)	1,924	72	1,451	528		30	30

For some of the associates, published information is not available for 31 December 2007 and therefore the income and profit and loss have been arrived at by using the 2006 audited financial statements and projecting that for 2007. For presentation purposes, the assets and liabilities for these associates, however, represent the amounts as audited at 31 December 2006.

(Expressed in thousands of United States Dollars)

14 INVESTMENTS IN ASSOCIATES (continued)

Name and Country of incorporation	Assets	Liabilities	Revenue	Profit/ (loss)	Published price quotation	% owned Voting	% owned Economic
2006							
Listed:							
Meezan Bank Limited (Pakistan)	764,447	696,344	28,940	10,221	19.55 PKR	26	15
Faysal Income & Growth Fund (Pakistan)	21,430	47	2,428	2,168	106.46 PKR	23	12
Unlisted:							
Solidarity Company BSC (c) (Bahrain)	203,642	43,267	15,150	5,354		40	40
First Leasing Bank B.S.C. (Closed) (Bahrain)	99,222	2,214	1,454	(252)		21	21
Citic International Assets Management Limited (Hong Kong)	211,002	18,059	7,424	4,825		20	13
Sanpak Engineering (Pakistan)	11,697	6,796	2,854	1,606		31	18
*Islamic Company for Production, Printing and Packing Materials "Icopack" (Egypt)	16,997	7,210	11,333	925		23	23
*Misr Company for Packing Materials "Egywrap" (Egypt)	35,583	19,448	30,712	1,302		23	23
Sakana Holistic Housing Solutions B.S.C. (Closed) (Bahrain)	6,631	-	-	-		50	30
Faysal Asset Management Limited (Pakistan)	1,407	57	1,420	460		30	15

* For some of the associates, published information is not available for 31 December 2006 and therefore the income and profit and loss have been arrived at by using the 2005 audited financial statements and projecting that for 2006. For presentation purposes, the assets and liabilities for these associates, however, represent the amounts as audited at 31 December 2005.

PKR Pakistan Rupee

Included in investment in associates at 31 December 2007 is $3.7 million (2006: $3.7 million) of goodwill. The movement is as follows:

	2007	2006
At 1 January	3,665	17,548
Additions	-	1,677
Disposal of associated company	-	(15,560)
At 31 December	**3,665**	**3,665**

(Expressed in thousands of United States Dollars)

15. PROPERTY, PLANT AND EQUIPMENT

	Land and buildings	Leasehold property, furniture, equipment, aircrafts and motor vehicles	Total
Cost			
At 1 January 2007	7,152	42,811	49,963
Additions	52,009	53,904	105,913
Transfer from non-current assets held for sale	2,194	35	2,229
Disposals	(297)	(1,333)	(1,630)
Currency effect	(307)	(336)	(643)
At 31 December 2007	**60,751**	**95,081**	**155,832**
Depreciation			
At 1 January 2007	992	18,270	19,262
Charge for the year	202	6,580	6,782
Transfer from non-current assets held for sale	109	2	111
Disposals	(3)	(1,102)	(1,105)
Currency effect	(68)	(80)	(148)
At 31 December 2007	**1,232**	**23,670**	**24,902**
Net book value			
At 31 December 2007	**59,519**	**71,411**	**130,930**
Cost			
At 1 January 2006	1,620	4,841	6,461
Subsidiary acquisitions	18,037	27,832	45,869
Additions	252	10,175	10,427
Disposals	(12,432)	-	(12,432)
Currency effect	(325)	(37)	(362)
At 31 December 2006	**7,152**	**42,811**	**49,963**
Depreciation			
At 1 January 2006	387	3,740	4,127
Subsidiary acquisitions	922	13,048	13,970
Charge for the year	(142)	2,157	2,015
Disposals	(147)	(736)	(883)
Currency effect	(28)	61	33
At 31 December 2006	**992**	**18,270**	**19,262**
Net book value			
At 31 December 2006	**6,160**	**24,541**	**30,701**

Land and buildings at 31 December 2007 include cost of land aggregating to $56.8 million (2006: $4.7 million).

Leasehold property at 31 December 2007 aggregated $18.9 million (2006: $15.7 million), less accumulated depreciation of $4.9 million (2006: $2.9 million).

Equipment and motor vehicles at 31 December 2007 included $0.1 million (2006: $0.2 million) at net carrying cost subject to finance leases.

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16. INTANGIBLE ASSETS

	Goodwill	Customer relations	Core deposits	Other*	Total
Year ended 31 December 2007					
Opening net book amount	97,836	82,139	152,631	6,708	339,314
Additions	1,463			6,080	7,543
Disposals	(6,754)				(6,754)
Foreign exchange				(39)	(39)
Amortisation charge		(4,185)	(7,777)	(1,798)	(13,760)
Closing net book amount	**92,545**	**77,954**	**144,854**	**10,951**	**326,304**
At 31 December 2007					
Cost	92,545	83,709	155,547	14,220	346,021
Accumulated amortisation		(5,755)	(10,693)	(3,269)	(19,717)
Net book amount	**92,545**	**77,954**	**144,854**	**10,951**	**326,304**
Year ended 31 December 2006 (restated)					
Opening net book amount				531	531
Acquisition of subsidiaries (note 42)	97,836	83,709	155,547	2,916	340,008
Additions				4,340	4,340
Disposals				(740)	(740)
Foreign exchange				(17)	(17)
Amortisation charge		(1,570)	(2,916)	(322)	(4,808)
Closing net book amount	**97,836**	**82,139**	**152,631**	**6,708**	**339,314**
At 31 December 2006 (restated)					
Cost	97,836	83,709	155,547	8,179	345,271
Accumulated amortisation		(1,570)	(2,916)	(1,471)	(5,957)
Net book amount	**97,836**	**82,139**	**152,631**	**6,708**	**339,314**

The carrying amount of goodwill has been allocated to cash-generating units as follows:

	2007	2006
Shamil Bank of Bahrain B.S.C.	66,070	66,070
Faysal Bank Limited	21,760	21,760
Faisal Private Bank (Switzerland) S.A.	3,252	3,252
Enqii Holdings Plc	1,463	-
Meezan Bank Limited	-	6,754
	92,545	**97,836**

No other intangible assets with indefinite lives have been allocated to those cash-generating units. The recoverable amounts of the units have been determined based on their fair values less costs to sell. The fair values of Faysal Bank Limited and Meezan Bank Limited have been determined by reference to quoted market prices. In 2006, the fair values of Shamil Bank of Bahrain B.S.C. and Faisal Private Bank (Switzerland) S.A. were determined by independent appraisals using a combination of comparable market multiples, including price earnings ratios, price to book ratios and percentages of funds under management.

* Other intangible assets included $5.4 million at 31 December 2007 (2006: $4.0 million) of computer software related to core banking systems, which is being amortised over five years.

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17. NON-CURRENT ASSETS HELD FOR SALE

As at 31 December 2006, $2.2 million related to property located in Pakistan, which had been identified to be sold by the management of Faysal Bank Limited. As at 31 December 2007, this property is reclassified as Property, plant and equipment.

18. CUSTOMER CURRENT ACCOUNTS

	2007	2006
Individuals	168,032	161,887
Financial institutions	78,407	15,056
Corporate institutions	322,800	206,761
	569,239	**383,704**

19. CUSTOMER INVESTMENT ACCOUNTS

	2007	2006
Individuals	326,286	498,149
Financial institutions	68,261	127,808
Corporate institutions	974,357	425,914
	1,368,904	**1,051,871**

20. COLLATERALISED BORROWINGS

Financial assets pledged to secure liabilities:

At 31 December 2007, there were collateralized borrowings in aggregate $28.5 million (2006: $8.0 million).

Assets which are pledged as collateral are conducted under terms that are usual and customary to standard lending and securities borrowing and lending activities.

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21. ACCOUNTS PAYABLE

	2007	2006
Accounts payable and other provisions	38,667	15,107
Advance received from customers	68,965	-
Demand drafts	38,859	80,940
Accruals	45,402	20,443
Security deposits on consumer leases	59,236	45,957
Funds under management	8,479	5,576
Payables to affiliated companies (note 41)	4,496	2,494
Payables to associated companies (note 41)	1,930	-
Derivative financial instruments	343	293
Payables to directors	15	468
Deferred income	2,920	6,346
Finance lease liabilities	126	241
	269,438	**177,865**

Liabilities against assets subject to finance leases comprise:

	2007		
	Minimum lease payments	Financial charges for future periods	Principal outstanding
Not later than one year	63	(4)	59
Later than one year and not later than five years	67		67
	130	**(4)**	**126**

Liabilities against assets subject to finance leases comprise:

	2006		
	Minimum lease payments	Financial charges for future periods	Principal outstanding
Not later than one year	106	(12)	94
Later than one year and not later than five years	153	(6)	147
	259	**(18)**	**241**

Derivative Financial Instruments

	2007	
	Contractual amount	Fair value
Foreign exchange derivatives held for trading:		
Currency forwards purchased	51,021	343

	2006	
	Contractual amount	Fair value
Foreign exchange derivatives held for trading:		
Currency forwards purchased	170,140	293

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22. OTHER BORROWINGS

	2007	2006
Term finance	16,397	-
Other debts	106,842	-
	123,239	**-**

Term finance represents seven-year floating rate unsecured term finance certificates issued by a subsidiary.

Other debts include short-term borrowings by subsidiaries amounting to US$ 79 million and term finance for aircrafts amounting to US$ 27 million.

23. DEFERRED TAX

	2007	2006
At January	36,070	3,087
Subsidiary acquisition	-	24,724
Income statement charge	13,718	8,273
Investment security fair value measurement	10,971	3
Exchange differences	(387)	(17)
At 31 December	**60,372**	**36,070**
Deferred tax liabilities on provisions and tax losses carried forward	(7,063)	(3,270)
Deferred tax (liability) / asset on available-for-sale investments	(9,639)	1,355
Deferred tax liability on leasing transactions	(38,387)	(29,229)
	(55,089)	**(31,144)**

The Group had no deferred tax assets in 2007 (2006: $1.4 million) and a deferred tax liability of $55.1 million (2006: $32.5 million). For balance sheet presentation purposes, the deferred tax assets and the deferred tax liability have been offset, since both arose in the same tax jurisdiction.

Deferred tax liability on the revaluation of investment property at fair value	(4,111)	(3,894)
Deferred tax liability on provisions	(1,172)	(1,032)
	(5,283)	**(4,926)**

24. INCOME FROM INVESTMENTS IN FINANCINGS

	2007	2006
Income from investments in financings	188,854	68,499
Provision for impairment	(7500)	(17,745)
Reversal of provision for impairment	-	5,877
	181,354	**56,631**

(Expressed in thousands of United States Dollars)

25. FEE AND COMMISSION INCOME

	2007	2006
Arrangement fees	20,710	3,308
Financing fees	6,849	2,364
Structuring fees and commissions	2,533	2,821
Document credit fees	2,634	1,300
Other fees	15,405	7,087
Selling commission	-	1,362
Fees from affiliated companies	-	5,522
Fees from associated companies	4,350	3,965
	52,481	**27,729**

26. INCOME FROM INVESTMENT PROPERTY

	2007	2006
Rental income from investment property	1,947	1,201
Gain on revaluation of investment property	35,891	11,989
Realised gain on sale of investment property	54,893	1,215
	92,731	**14,405**

27. NET TRADING INCOME

	2007	2006
Income from foreign exchange trading	6,950	1,612
Gains on trading securities	567	21
(Loss) on revaluation of trading securities	-	(46)
	7,517	**1,587**

Foreign exchange trading includes gains and losses from spot and forward contracts translated foreign currency assets and liabilities.

28. DIVIDEND INCOME

	2007	2006
Investment securities available-for-sale	27,242	825

29. STAFF COSTS

	2007	2006
Salaries and other benefits	65,585	23,613
Share based payments (note 41)	5,321	1,029
Social security and other statutory costs	2,500	1,989
Post retirement benefits (note 40)	906	1,435
	74,312	**28,066**

Other benefits include housing allowance, home leave, relocation expense, medical and health expense, training, severance costs and end of service benefit costs.

(Expressed in thousands of United States Dollars)

30. GENERAL AND ADMINISTRATIVE EXPENSES

	2007	2006
Office expenses	20,539	7,297
Professional fees	15,997	8,597
Others	11,904	1,425
	48,440	**17,319**

31. TAXES

	2007	2006
Current taxes	6,288	3,852
Deferred taxes	13,718	8,273
	20,006	**12,125**

The expected income tax expense for the Group is an aggregate of individual amounts representing the mix of profits and losses and the applicable tax rates in each jurisdiction. Consequently, the effective tax rate on consolidated income may vary from year to year, according to the source of earnings. Most affiliates of the Group operate in tax free jurisdictions.

Reconciliation between the reported income tax and the amount computed, using the weighted average of applicable domestic corporate tax rates, is as follows:

	2007	2006
Net accounting profit	220,919	195,895
Weighted average applicable domestic corporate tax rate	13%	6.8%
Weighted average applicable domestic corporate tax	28,737	13,382
Effect of revenue taxed at a different rate than domestic corporate tax rate	(8,731)	(1,257)
Effective tax	**20,006**	**12,125**

The Bank operates in certain countries which have tax regimes, but for which no provision for income tax has been recorded in these consolidated financial statements. It is believed that the Bank's potential tax liability arising in respect of its operations in those countries is remote at the present time.

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32. MINORITY INTERESTS

The consolidated financial statements include 100% of the assets, liabilities and earnings of subsidiaries. The ownership interests of the other shareholders in the subsidiaries are called minority interests.

The following table summarises the minority shareholders' interests in the equity of consolidated subsidiaries.

		2007		2006 (Restated)
	Minority %		Minority %	
Faysal Bank Limited	34.28	136,885	49	160,898
Health Island B.S.C (c)	50.00	58,322		
Enqii Holdings Plc	7.75	742		
Ithmaar Aviation Lease One (Dublin) Ltd.	5.00	640		
Shamil Bank of Bahrain B.S.C.			40	167,477
Faisal Private Bank (Switzerland) S.A.			21	1,938
Faisal Finance (Jersey) Limited			5	1,249
		196,589		**331,562**

Minority interests in the consolidated statement of income of $85.5 million (2006: $13.5 million) represent the minority shareholders' share of the earnings of these subsidiaries for the respective years.

33. SHARE CAPITAL

	Number of shares (thousands)	Share capital
Issued		
At 1 January 2006	150,000	150,000
Shares issued	210,000	210,000
Treasury shares acquired (net)	(6,475)	(6,475)
At 31 December 2006	**353,525**	**353,525**
Four for one share split	1,414,100	353,525
Treasury shares purchased	(51,428)	(12,857)
Treasury shares sold	52,724	13,181
Bonus issue	288,000	72,000
New shares issued	446,500	111,625
At 31 December 2007	**2,149,896**	**537,474**

On 19 March 2007, a four for one share split increased the total authorised number of shares of 500 million with a nominal value of $1.00 per share to 2,000 million with a nominal value of $0.25 per share. As a result, the total number of issued shares of 360 million increased to 1,440 million shares. During the EGM held on 29 November 2007, the authorised share capital was increased to 4,000,000,000 shares with a nominal value of $0.25 per share, totalling $1,000 million. All issued shares are fully paid.

33 SHARE CAPITAL (continued)

The Bank owned 24,603,264 of its own shares at 31 December 2007 (2006: 25,900,444). The shares were acquired through various purchases and sales during the year on the Bahrain Stock Exchange for a net consideration of $2.3 million. The nominal value of the shares acquired amounting to $0.3 million has been included in share capital and the balance of the consideration has been included in the share premium. The shares are held as Treasury shares and the Bank has the right to reissue these shares at a later date.

In November 2007, the Bank acquired the remaining 40 per cent share holding in Shamil Bank of Bahrain B.S.C ("Shamil Bank") through a share exchange by issuing 446,499,970 new shares to the minority shareholders. Twelve ordinary shares of the Bank were exchanged for every ten ordinary shares in Shamil Bank. The Bank also issued 288,000,000 bonus shares to the existing shareholders before the share exchange.

34. RESERVES

Statutory reserves

In accordance with the requirements of the Bahrain Commercial Companies Law, an amount of at least 10% of the Bank's net income for the year is transferred to a statutory reserve until such time as that reserve represents 50% of the paid up share capital of the Bank. The reserve can be utilised for payment of dividends up to 5% of the issued and fully paid up share capital.

Retained earnings

Consolidated retained earnings include the following reserves of the subsidiaries – statutory reserve amounting $12.1 million (2006: $4.9 million) and fiduciary reserve amounting $8.1 million (2006: $5.8 million). Consolidated retained earnings also include subsidiary profits amounting to $20.4 million which is not available for distribution due to applicable local regulations.

35. PRIVATE PLACEMENT AND INITIAL PUBLIC OFFERING

In December 2005, the Bank offered 50,000,000 new shares through a fully underwritten issue to existing unit holders and certain employees of Dar Al-Maal Al-Islami Trust through a private placement. This offer was subsequently increased to 60,000,000 shares. These shares were offered at $1.00 per share and were on allotment subject to the same rights and obligations as were applicable to other shares in the Bank apart from the entitlement to dividends in respect of the year ended 31 December 2005. The shares offered through the private placement were allotted on the closing when the Bank received the proceeds on 9 April 2006.

On 19 February 2006, the Bank offered 150,000,000 new shares through an initial public offering at a price of $2.25 per share. Following the successful completion of both the private placement and the initial public offering, the Bank's issued and paid up capital was increased to $360 million.

Expenses amounting to $0.9 million had been incurred in connection with the private placement and the initial public offering at 31 December 2005. Of this amount, $0.1 million was recognised in the consolidated statement of profit and loss and $0.8 million was charged directly to equity. Additional expenses amounting to $14.7 million have been incurred during 2006, which have been charged directly to equity.

Certain employees subscribed for shares in the Bank in the private placement. The benefit received by these employees amounted to $1.0 million, representing the difference between the deemed fair value of the shares and the subscription price, which has been recognised as an expense in the consolidated statement of income in 2006.

36. PROPOSED DIVIDEND

The Directors propose to recommend at the Annual General Meeting a dividend of $53.7 million (2.5 cents per share) for the year ended 31 December 2007.

A dividend for 2006 amounting to $47.5 million (13.5 cents per share equivalent to 3.375 cents per share after the four for one share split) was approved and paid in 2007. A dividend for 2005 amounting to $20.0 million (13.0 cents per share) was approved and paid in 2006.

(Expressed in thousands of United States Dollars)

37. BASIC/DILUTED EARNINGS PER SHARE

Basic/diluted earnings per share is calculated by dividing the net income attributable to shareholders by the weighted average number of issued and fully paid up ordinary shares during the year.

	2007	2006 (Restated)
Net income attributable to shareholders	102,755	167,558
Weighted average number of issued and fully paid up ordinary shares ('000)	1,773,972	1,510,180
Basic/diluted earnings per share	**US cts 5.79**	**US cts 11.10**

38. CAPITAL MANAGEMENT

The table below summarises the composition of regulatory capital and the ratios of the Bank for the years ended 31 December 2006 and 2007. During those two years, the Bank complied with all of the externally imposed capital requirements to which it is subject.

	2007	2006
Tier 1 capital		
Share capital (net of treasury shares)	537,474	353,525
Share premium	216,026	167,347
General reserves	68,327	46,044
Statutory reserve	25,598	8,778
Retained earnings	113,538	36,834
Minority interests	196,589	331,562
Less: Goodwill	(92,545)	(97,836)
Total qualifying Tier 1 capital	**1,065,007**	**846,254**
Tier 2 capital		
Revaluation reserve – available-for-sale investments	12,226	7,268
Net profit for the current year	102,755	167,558
Currency translation adjustment	(3,078)	(4,144)
Total qualifying Tier 2 capital	**111,903**	**170,682**
Less: other regulatory requirements	**(194,768)**	**(194,821)**
Total regulatory capital	**982,142**	**822,115**
Risk-weighted assets:		
On-balance sheet	3,180,882	2,193,271
Off-balance sheet	627,017	591,494
Total risk-weighted assets	**3,807,899**	**2,784,765**
Basel I ratio	**25.79%**	**29.52%**

(Expressed in thousands of United States Dollars)

39. FUNDS UNDER MANAGEMENT

Funds under management aggregated $1.7 billion (2006: $1.1 billion) and represented amounts invested by clients and placed with funds managed by the Group. These funds are invested without recourse to the Group. The Group earned fees of approximately $19.5 million associated with such funds in 2007 (2006: $43.3 million).

At 31 December 2007, the Group had amounts due to funds under management of $6.7 million (2006: $5.0 million) and due from funds under management of $110.6 million (2006: $310.4 million).

40. RETIREMENT BENEFIT PLANS

Substantially all employees of the Group's European incorporated subsidiaries are covered either by insured or state pension plans. In accordance with local practice, no pension plans exist in certain countries in which the Group operates.

The Group's principal retirement benefit plans are in Switzerland and are defined benefit plans. The assets of the funded plans are held in separate trustee administered funds. These plans are valued by independent actuaries every year using the projected unit credit method.

The assumptions used in the actuarial valuations for 2007 and 2006 are the best estimates of the main parameters influencing the pension liability and are detailed as follows:

	2007	2006
	%	%
Standard financial cost rate	2.85	2.70
Expected long-term rates of return on plan assets	3.80	3.70
Rate of increase in compensation	2.00	2.00
Rate of increase in pension	0.00	0.00
The funded status of the Group's pension plans is as follows:		
Projected benefits obligations	(49,458)	(42,911)
Plan assets at fair values	48,327	41,375
Funded status	(1,131)	(1,536)
Unrecognised actuarial losses	(2)	(2)
Liability in the balance sheet	(1,133)	(1,538)
Net periodic pension cost consists of the following:		
Service costs	1,706	2,081
Financial costs	1,285	1,245
Expected return on assets	(1,607)	(1,454)
Total cost	1,384	1,872
Employee contributions	(478)	(437)
Net periodic pension cost	906	1,435
Movement in the liability recognised in the balance sheet:		
At 1 January	1,538	940
Acquisition of subsidiary	-	392
Exchange differences	575	543
Net periodic pension cost	906	1,435
Employer contributions	(1,886)	(1,772)
At 31 December	**1,133**	**1,538**

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40 RETIREMENT BENEFIT PLANS (continued)

The movement in the defined benefit obligation over the year is as follows:

	2007	2006
Beginning of the year	42,911	32,676
Acquisition of subsidiary	-	9,684
Service costs	1,706	2,081
Financial costs	1,285	1,245
Employee contributions	478	437
Actuarial (gain)	-	(2,168)
Benefits paid	(219)	(3,843)
Premiums paid	(483)	(452)
Exchange differences	3,780	3,251
End of year	**49,458**	**42,911**

The movement in the fair value of plan assets of the year is as follows:

	2007	2006
Beginning of the year	41,375	29,006
Acquisition of subsidiary	-	8,400
Expected return on plan assets	1,607	1,454
Actuarial gain	-	1,736
Employer contributions	1,886	1,772
Employee contributions	478	437
Benefits paid	(219)	(3,843)
Premiums paid	(483)	(452)
Exchange differences	3,683	2,865
End of year	**48,327**	**41,375**
Actual return on plan assets	1,607	3,141

The expected return on plan assets is determined by considering the expected returns available on the assets underlying the current investment policy. Expected returns on fixed rate investments are based upon gross redemption yields as at the balance sheet date. Expected returns on equity and property investments reflect long-term real rates of return experienced in the respective markets. The expected return for each asset class was weighted based on the target asset allocation to develop the expected long-term rate of return on assets assumption for the portfolio.

Expected contributions to post employment benefit plans for the year ending 31 December 2008 is $1.8 million (2007: $1.6 million).

As at 31 December	2007	2006	2005	2004
Present value of defined benefit obligation	49,458	42,911	32,676	31,627
Fair value of plan assets	48,327	41,375	29,006	29,165
Deficit	1,131	1,536	3,671	2,461
Experience adjustments on plan assets		(1,736)	(1,682)	788
Experience adjustments on plan liabilities		(2,168)	3,280	(615)

(Expressed in thousands of United States Dollars)

41. RELATED PARTY TRANSACTIONS AND BALANCES

A number of transactions are entered into with related parties in the normal course of business. These include loans, current and investment accounts. Transactions and balances disclosed as with associated companies are those with companies in which the Bank owns 20% to 50% of the voting rights and over which it exerts significant influence, but does not have control. Transactions with other related parties, who consist of Dar Al-Maal Al-Islami Trust and its subsidiaries other than the Bank, are disclosed as affiliated companies. The volumes of related party transactions, outstanding balances at the year end, and relating income and expense for the year are as follows.

a) Loans to key management personnel

	2007	2006
Loans		
Loans outstanding at 1 January	967	2,043
Loan repayments during the year	(268)	(1,180)
Foreign exchange	34	104
Loans outstanding at 31 December	**733**	**967**

No provisions have been recognised in respect of loans given to related parties (2006: Nil).

The loans advanced to key management personnel bear no return, are unsecured and are repayable over varying periods up to 2011.

b) Loans to employees

All employees of the Group are entitled to receive employee loans on favourable terms not equivalent to those of transactions made on an arm's length basis. Included in accounts receivable are amounts due from employees at 31 December 2007 of $7.8 million (2006: $7.3 million).

c) Current and investments accounts

	Associated companies		Affiliated companies	
Year ended	**2007**	2006	**2007**	2006
Amounts payable to:				
Solidarity Company B.S.C. (c)		21,097		
Dar Al-Maal Al-Islami Trust				
DMI Services N.V.			4,920	80
Islamic Investment Company				
of the Gulf (Bahamas) Limited	1,930		45	27
Gulf Company for Financial Investments			2,509	2,445
First Leasing Bank B.S.C. (Closed)		50,022		

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41 RELATED PARTY TRANSACTIONS AND BALANCES (continued)

	Associated companies		Affiliated companies	
Year ended	**2007**	2006	**2007**	2006
Amounts receivable from:				
Solidarity Company BSC (c)	4,600	28		
Meezan Bank Limited		12		
DMI Services N.V.			14,067	15,580
Dar Al-Maal Al-Islami Trust			196,768	197,822
Islamic Investment Company of the Gulf (Bahamas) Limited			10,268	10,009
Faysal Bahamas Limited				26
Gulf Company for Financial Investments				5
Egyptian Company for Business and Trade			829	817
Expense on current and investment accounts				
Faisal Private Bank (Switzerland) S.A.*		194		
Faysal Bank Limited*		47		
Shamil Bank Bahrain B.S.C.*				165
Dar Al-Maal Al-Islami Trust				171
Gulf Company for Financial Investments			63	60
Solidarity Company BSC (c)	112	648		
First Leasing Bank B.S.C.(Closed)	887	22		
Islamic Investment Company of the Gulf (Bahamas) Limited			209	
d) Other revenue				
Faisal Private Bank (Switzerland) S.A.*		80		
Faysal Bank Limited*		406		
Dar Al-Maal Al-Islami Trust			12,539	6,166
DMI Services N.V.			5,648	8,395
Shamil Bank Bahrain B.S.C.*				1,715
Islamic Investment Company of the Gulf (Bahamas) Limited			463	736
First Leasing Bank B.S.C. (Closed)		3,797		
Sakana Holistic Housing Solutions B.S.C (Closed).	69			
Faysal Asset Management Limited (Pakistan)	59			
Solidarity Company BSC (c)	4,350			

* 2006 transactions represent the period from 1 January to 15 August

The fees paid by DMI Services N.V. represented the recovery of certain costs incurred on its behalf by a subsidiary company which were included as a reduction of staff costs and administrative expenses. In 2006, the revenue from Shamil Bank of Bahrain represents principally investment income received less advisory fees paid to it in connection with the initial public offering of the Bank's shares (note 35).

Details of other related party transactions during the year are contained in note 43 below.

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41 RELATED PARTY TRANSACTIONS AND BALANCES (continued)

	2007	2006
e) Key management compensation		
Salaries and other benefits	16,431	14,396
Share based payments	4,257	1,029
Post-employment benefits	1,477	822
	22,165	**16,247**

f) Directors' remuneration

The total remuneration of the Board of Directors in 2007 amounted to $1.1 million (2006: $0.8 million).

g) Indemnity

Dar Al-Maal Al-Islami Trust has provided indemnities up to $3.5 million (2006: $3.5 million) in respect of any shortfall on the carrying values which may be realised on certain investments held by subsidiaries.

42. ACQUISITIONS AND DISPOSALS (RESTATED)

Acquisition of subsidiaries

During 2007, the Extra Ordinary General Meeting of the Bank held on 29 November 2007 approved the acquisition of the remaining 40 % shareholding in Shamil Bank through a share exchange by issuing 446,499,970 shares of the Bank to the minority shareholders of Shamil Bank. Twelve ordinary shares of the Bank were exchanged for every ten ordinary shares in Shamil Bank. The purchase consideration for acquisition of minority interest amounted to $424.2 million. The resultant Goodwill of $193.9 million was accounted under the Economic Entity method in equity against the Share Premium arising from this acquisition amounting to US$312.6 million.

On 15 August 2006 the Bank had purchased on the Bahrain Stock Exchange 136,979,173 shares, representing 60% of the issued share capital of Shamil Bank at a price of $2.93 per share from Dar Al-Maal Al-Islami Trust. The total consideration amounted to $401.3 million. The Bank indirectly acquired a controlling interest in Faisal Private Bank (Switzerland) S.A. (formerly Faisal Finance (Switzerland) S.A.) and a controlling interest in Faysal Bank Limited, Pakistan. Further the Bank increased its ownership of Faisal Finance (Jersey) Limited.

The Group had assessed the fair values of the acquired companies' tangible and intangible assets, liabilities and contingent liabilities. The acquired companies have been consolidated with effect from the date of acquisition and the excess of consideration over the fair value of the net assets acquired amounting to $97.8 million has been included under goodwill.

Purchase consideration	401,349
Fair value of net assets acquired	(303,513)
Goodwill (note 16)	**97,836**

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42 ACQUISITIONS AND DISPOSALS (continued)

The following table provides a comparison of the fair value and carrying amounts of the assets acquired and liabilities assumed with respect of acquisition. The table below takes into consideration the fair valuation of net assets:

	2006	
	Fair value	Acquirees' carrying amount
Assets		
Cash and cash equivalents	423,796	423,796
Investments	44,076	44,076
Investments in financings	199,362	199,362
Investment securities	86,811	86,811
Investment property	10,157	10,157
Accounts receivable	113,061	113,061
Investments in associates	154,256	118,061
Property, plant and equipment	4,347	4,347
Customer related intangible assets	55,819	-
Core deposit intangible assets	65,357	-
Other intangible assets	2,914	-
Other assets	1,340	1,340
Total assets acquired	**1,161,296**	**1,001,011**
Liabilities		
Investment accounts	(151,739)	(151,739)
Due to banks	(307,891)	(307,891)
Accounts payable	(180,666)	(180,666)
Other liabilities	(965)	(965)
Total liabilities assumed	**(641,261)**	**(641,261)**
Net assets	520,035	359,750
Minority Interests	(216,522)	-
Net assets acquired	**303,513**	**-**
Cash and cash equivalents transferred		423,796
Purchase consideration settled in cash		401,349
Cash inflow on acquisition		**22,447**

The indirect acquisition of Faysal Bank Limited (FBL), Pakistan, increased the cash inflow by $233.9 million. The profit of Shamil Bank since the acquisition date included in the Bank's consolidated statement of income for the twelve month period ended 31 December 2006 amounted to $12.8 million. If the acquisition had occurred on 1 January 2006, the consolidated profit after taxes for the twelve months ended 31 December 2006 would have been $220.9 million.

(Expressed in thousands of United States Dollars)

42 ACQUISITIONS AND DISPOSALS (continued)

2006 indirect acquisition of equity method investee

As noted above, as a result of the Shamil Bank acquisition, Ithmaar Bank also acquired a controlling interest in FBL, a previously equity accounted investee, increasing its ownership interest from 29% to 51%. The indirect acquisition triggered a revaluation of the historical investment on the basis of the fair value of the net assets of the investee at the time control was acquired. This revaluation which amounted to $34.2 million was recorded through equity. At the same time, of the amount relating to the acquisition of associates amounting to $154.3 million noted above, $128.6 million has been allocated to individual line items, reflecting the consolidation of FBL. A detailed overview of the impact of the indirect acquisition of FBL in the Bank's consolidated financial statements is included below:

	2006 Fair value
Assets	
Cash and cash equivalents	209,267
Investments	943
Investments in financings	1,143,813
Investment securities	469,638
Accounts receivable	32,709
Investments in associates	4,835
Property, plant and equipment	29,973
Customer related intangible assets	27,890
Core deposit intangible assets	90,190
Other intangible assets	1,857
Other assets	1,644
Total assets acquired	**2,012,759**
Liabilities	
Investment accounts	(1,311,851)
Due to banks	(259,557)
Accounts payable	(69,501)
Other liabilities	(29,853)
Total liabilities assumed	**(1,670,762)**
Net assets	341,997
Minority interests	(167,647)
Net assets acquired	**174,350**

Disposal of subsidiaries

On 15 August 2006 the Bank sold 100% of the share capital in Islamic Investment Company of the Gulf (Bahamas) Limited to Dar Al-Maal Al-Islami Trust for a total consideration of $150.0 million.

This transaction resulted in a gain on sale of a subsidiary of $105.5 million which is included in the consolidated statement of income.

(Expressed in thousands of United States Dollars)

42 ACQUISITIONS AND DISPOSALS (continued)

Included in the sale were the following wholly-owned subsidiaries of Islamic Investment Company of the Gulf (Bahamas) Limited:

Subsidiary	Country of Incorporation
Islamic Investment Company of the Gulf (Sharjah)	United Arab Emirates
Gulf Company for Financial Investments S.A.E.	Egypt
Egyptian Company for Business and Trade S.A.E.	Egypt
Faysal Bahamas Limited	Bahamas

The details of the assets and liabilities sold are as follows:

Cash and cash equivalents	15,624
Investments	16,160
Trading securities	208
Investments in financings	8,811
Investment securities	33,754
Investment property	1,948
Accounts receivable	26,907
Property, plant and equipment	2,471
Other assets	740
Investments from off balance sheet funds	(29,795)
Accounts payable	(31,565)
Total assets and liabilities sold	**45,263**
Cash and cash equivalents transferred	15,624
Sale consideration settled in cash	150,000
Cash inflow on disposal	**134,376**

Acquisition of associates

On 30 November 2007, the Bank subscribed further $17.99 million for an additional 14,394,677 shares in the capital of Solidarity Company BSC (c) at a premium of $0.25 per share. On 20 June 2006, the Bank had subscribed $20.0 million for an additional 20 million shares in the capital of Solidarity Company BSC (c) at par.

On 22 February 2006 the Bank acquired 2,250,000 shares in First Leasing Bank B.S.C. (Closed) for a total consideration of $2.4 million. On 28 December 2006 the Bank subscribed for a further 19,073,810 new shares at a price of $1.05 per share amounting to $20.0 million. At 31 December 2006 the Bank owned 21,323,810 shares, representing 21.3% of the total issued share capital of First Leasing Bank B.S.C. (Closed).

On 28 December 2006 the Bank acquired 124,816,636 shares in Citic International Assets Management Limited for a total consideration of Hong Kong dollars 131.4 million ($16.9 million). On the same date the Bank subscribed for a further 318,716,898 new shares at a total cost of Hong Kong dollars 335.2 million, of which Hong Kong dollars 55.3 million ($7.1 million) was payable on initial subscription. The balance amount $ 36.1 million (Hong Kong dollars 279.9 million) was paid on 7 November 2007. At 31 December 2007 the Bank was entitled to a voting and equity interest of 20% (2006: 20% and 12.5% respectively).

(Expressed in thousands of United States Dollars)

42 ACQUISITIONS AND DISPOSALS (continued)

Disposal of associates

In June 2007, Shamil Bank of Bahrain B.S.C. disposed of 19% of its investment in Meezan Bank Limited to an unrelated party for a total consideration of $37.8 million. The gain on disposal recognised in the consolidated statement of income amounted to $15.0 million, representing the difference between the consideration and the carrying value, including unrealised fair value and foreign exchange reserves, net of the proportional goodwill recorded upon the acquisition of Shamil Bank of Bahrain. Following this transaction, the Group's interest was reduced to 7% and the remaining investment is recorded as an investment security available-for-sale.

During April 2007, one of the Group's subsidiaries reclassified a $4.9 million investment in Faysal Income and Growth Fund (Pakistan) from an associated company to investment securities available-for-sale.

In June 2006, the Bank disposed of 7.5% of its investment in Faisal Islamic Bank of Egypt to Dar Al-Maal Al-Islami Trust for a consideration of $18.8 million. The consideration for this transaction was determined by an agreed fair value for settlement in September 2006. The gain on disposal amounting to $4.6 million, representing the difference between the consideration and the carrying value of $14.2 million, has been recognised in the consolidated statement of income in 2006. Following this transaction, the Group's interest in FIBE was reduced to 2.4% which was subsequently disposed of as part of the sale of Islamic Investment Company of the Gulf (Bahamas) Limited referred to above.

43. CONTINGENT LIABILITIES AND COMMITMENTS

Contingent liabilities	**2007**	2006
Acceptances and endorsements	40,115	61,302
Guarantees and irrevocable letters of credit	617,855	508,865
Customer claims	55,842	54,862
	713,812	**625,029**

DMI Administrative Services SA had at 31 December 2007 a potential contingent liability not exceeding $1.1 million (2006: $1.0 million) in respect of its retirement benefit plan in the event that the plan assets attributable to individual members ultimately fall below their contractual entitlements.

Sanpak Engineering carried at 31 December 2007 contingent liabilities of $2.8 million (2006: $1.8 million), of which the Group's share was $0.87 million (2006: $0.3 million). These related to letters of credit issued as part of their normal business activities.

Solidarity has at 31 December 2007 a letter of guarantee for $16 million (2006: $26.7 million), of which the Group's share is $5.4 million (2006: $10.7 million), from the National Commercial Bank of Saudi Arabia for the proposed incorporation of a subsidiary in the Kingdom of Saudi Arabia.

Meezan Bank Limited carried at 31 December 2006 contingent liabilities of $694.0 million, of which the Group's share was $104.1 million. These related to guarantees, letters of credit and other financing commitments made as part of their normal banking operations.

(Expressed in thousands of United States Dollars)

43 CONTINGENT LIABILITIES AND COMMITMENTS (continued)

Commitments	2007	2006
Undrawn facilities, financing lines and other commitments to finance	698,446	551,517

As at 31 December 2006, the Bank had a commitment of Hong Kong dollars 279.9 million ($36.0 million) to pay the balance of the subscription monies due on the issue of 318,716,898 new shares in Citic International Assets Management Limited subject to calls being made by the directors over a period not exceeding two years from 28 December 2006. This amount was paid during the year ended 31 December 2007.

On 21 September 2006 the Bank entered into an agreement to sell 7,500,000 shares in Solidarity Company B.S.C. (c) in exchange for $7.5 million. On the same date Islamic Investment Company of the Gulf (Bahamas) Limited agreed with the Bank that it would arrange to transfer 7,500,000 shares in Solidarity Company B.S.C. (c) to the purchaser under the agreement upon receipt of $7.5 million from the Bank. The transaction underlying the agreement was completed on 5 February 2007 when both the shares and the funds were transferred.

Operating lease commitments

Commitments for operating leases include IT hardware, cars and office equipment.
The future minimum lease payments under non cancellable operating leases are as follows:

Not later than one year	193	240
Later than one year and not later than five years	484	332
	677	**572**

Significant net open foreign currency position		
Trading	**101,653**	**54,681**

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44. CURRENT AND NON-CURRENT ASSETS AND LIABILITIES

At 31 December 2007	Current	Non-current	Total
Cash and cash equivalents	575,291	13	575,304
Due from banks	16,172	-	16,172
Investments in financings	1,349,614	532,414	1,882,028
Investment securities	458,966	179,613	638,579
Investment property	48,711	164,356	213,067
Accounts receivable	61,294	40,562	101,856
Investments in associates	-	194,549	194,549
Property, plant and equipment	48,078	82,852	130,930
Intangible assets	4,937	321,367	326,304
Total assets	**2,563,063**	**1,515,726**	**4,078,789**
Customer current accounts	569,239	-	569,239
Customer investment accounts	1,300,676	68,228	1,368,904
Due to banks	370,650	23,375	394,025
Other borrowings	27,262	95,977	123,239
Accounts payable	174,761	94,677	269,438
Current tax payable	346	8,829	9,175
Deferred tax liability	-	60,372	60,372
Total liabilities	**2,442,934**	**351,458**	**2,794,392**
Net assets	**120,129**	**1,164,268**	**1,284,397**

At 31 December 2006			
Total assets	**1,929,104**	**1,389,651**	**3,318,755**
Total liabilities	**2,093,253**	**101,847**	**2,195,100**
Net assets	**(164,149)**	**1,287,804**	**1,123,655**

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45. SUBSIDIARIES

A listing of the Group's principal subsidiaries as at 31 December 2007 is as follows:

	% owned		Country of
	Voting	Economic	Incorporation
Shamil Bank of Bahrain B.S.C.	100	100	Kingdom of Bahrain
Faysal Bank Limited	65.72	65.72	Pakistan
Faisal Private Bank (Switzerland) S.A.	100	100	Switzerland
Faisal Finance (Jersey) Limited	100	100	Jersey
Cantara (Switzerland) S.A.	100	100	Switzerland
DMI Administrative Services S.A.	100	100	Switzerland
DMI (Jersey) Limited	100	100	Jersey
MFAI (Jersey) Limited	100	100	Jersey
Faisal Finance (Luxembourg) S.A.	100	100	Luxembourg
Faisal Finance (Netherlands Antilles) NV	100	100	Netherlands Antilles
Rayten Holdings Limited	100	100	Jersey
Ithmaar Development Company Limited	100	100	Kingdom of Bahrain
Health Island BSC (C)	50	50	Kingdom of Bahrain

46. RESTATEMENT OF PREVIOUSLY ISSUED FINANCIAL STATEMENTS

Certain changes have been incorporated in previously issued financial statements for the twelve months ended 31 December 2006 which were presented to the Annual General Meeting held on 14 March 2007. These figures have been restated to reflect the recognition of intangibles arising from the acquisition of Shamil Bank on a gross basis as opposed to net of minority interests as previously reported. The effects of the restatements are:

	Previously Reported	Restated	Adjustment Increase/(decrease)
December 2006			
Consolidated Statement of Income			
Depreciation and amortisation	4,103	6,823	2,720
Profit after income taxes	183,770	181,050	(2,720)
Attributable to:			
Equity holders of the Bank	168,200	167,558	(642)
Minority interests	15,570	13,492	(2,078)
Consolidated Balance Sheet			
Intangible assets	200,497	339,314	138,817
Total assets	3,179,938	3,318,755	138,817
Reserves	404,966	438,568	33,602
Minority interests	226,347	331,562	105,215
Total equity	984,838	1,123,655	138,817

Our People

Abdulla Nooraldin Al Khateeb
Abdulla Salman Al Ghatam
Abdulrehman Abdulla
Ahmed Abdulrahim
Ali Jama Muse
Andrew L.I. Pocock
Asfar Amanullah
Ayoob Yusuf Abdulla Mohamed Alawadhi
Bassim S. Sharafeldin
Carolyn Anne Prowse
Dana Aqeel Mahmood Raees
Dheya Ali Al-Sheker
Esraa Abdulhameed Haji Al Janahi
Estherkine Clara Pinto
Fadheela Ali Hasan Khamis
Fahad Isa Ali Alqadhi
Farhan-ul-Haq Siddiqui
Husain Abdali Yaqoob Yusuf
Jassim A.K. Salman
Katarzyna Anna Kubica
Karim Sehnaoui
Khalil Mohamed Qambar Qasim
Luis Maronese
Lulwa Y. Al Jassim
Maha Tareq Saleh Khaled Al Aujan
Maysan Al-Maskati
Masood Naseem Tyabji
Michael Anthony McKinlay
Michael P. Lee
Mohammad Ali
Mohammad Khan Hoti
Nada Ahmed Ali Al AAli
Nayla Mohamed Aslam Asgharali
Ravindra Khot
Salem Ali Salem
Saqib Mahmood Mustafa
Sara Khaled Juma
Sarah Mahmood Ahmadi
Sathyavijaya Rao Nirikhi
Scott A. Creswell
Salman bin Ahmad Al Khalifa
Shereen Ali
Syed Altaf Azim Syed Ali Imam
Syed Muhammad Shabbir Shah
Syed Shahzad Bukhari
Tariq Khonji
Yaqoob Yusuf Hasan Mohamed
Yara Abdulridha Abdulla Faraj
Zahra Hasan

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