Basel II Pillar III Quantitative Disclosures
As at 30 June 2014

Ithmaar Bank B.S.C
Basel II Pillar III Quantitative Disclosures at 30 June 2014

INDEX

S. No.	Description	Page No.
1	Background	3
2	Basel II Framework	3
3	Methodology	3
4	Approaches adopted for determining regulatory capital requirements	4
5	Group structure	4
6	Consolidated Capital Structure for capital adequacy purpose	5
7	Disclosure of the regulatory capital requirements for credit risk under standardized approach	6
8	Gross credit exposures	7
9	Geographical distribution of credit exposures	8
10	Industrial distribution of credit exposures	9
11	Maturity breakdown of credit exposures	10
12	Related-party balances under credit exposure	11
13	Past due and impaired financings and related provisions for impairment	12
14	Past due and impaired financings by geographical areas	13
15	Details of credit facilities outstanding that have been restructured during the six month period ended 30 June 2014	13
16	Credit exposures which are covered by eligible financial collateral	13
17	Disclosure of regulatory capital requirements for market risk under the standardized approach	14
18	Disclosure of regulatory capital requirements for operational risk under the basic indicator approach	14
19	Tier one capital ratios and Total capital ratios	14
20	Equity positions in Banking book	15
21	Gross income from Mudaraba and profit paid to Unrestricted Investment Accountholders (URIA)	15
22	Movement in Profit Equalization Reserve and Provisions – URIA	16
23	Gross return from Restricted Investment Accounts (RIA)	17
24	Average declared rate of return on General Mudaraba deposits	17
25	Profit rate risk	17
26	Currency risk	18
27	Performance ratios	18
28	Liquidity rations	18
29	Legal contingencies and compliance	18

1. Background

The Public Disclosure (PD) module of the Central Bank of Bahrain (CBB) rulebook was introduced with effect from January 2008. The disclosures in this report are in addition to the disclosures set out in the Group's interim condensed consolidated financial statements for the six month period ended 30 June 2014, presented in accordance with Financial Accounting Standards (FAS) issued by the Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI). These disclosures are mainly related to compliance with the Basel II Pillar III Quantitative disclosure requirements and should be read in conjunction with the Group's interim condensed consolidated financial information for the six month period ended 30 June 2014.

2. Basel II Framework

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

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

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

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

3. Methodology

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

- Line by line consolidation is performed for the risk exposures and eligible capital of all the subsidiaries within the Group with the exception of Ithmaar's banking subsidiaries incorporated outside Kingdom of Bahrain which are operating under Basel II compliant jurisdictions, where full aggregation is performed of the risk weighted exposures and eligible capital as required under Prudential Consolidation and Deduction module (PCD).
- Pro-rata aggregation of risk weighted exposures and eligible capital of Ithmaar's significant investments (20% – 50%) in banking and other financial entities as required under PCD module.

4. Approaches adopted for determining regulatory capital requirements

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

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

5. Group Structure

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

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

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

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

6. Consolidated Capital Structure for capital adequacy purpose

A	**Tier 1 Capital**	
	Issued and fully paid-up ordinary capital	727,541
	Reserves	
	General reserves	56,725
	Statutory reserve	38,090
	Share Premium	149,614
	Others	(21,912)
	Accumulated losses	(412,681)
	Minority interest in the equity of subsidiaries	75,157
	Aggregation	185,996
	Sub-Total	**798,530**
	Regulatory deductions:	
	Goodwill	(13,329)
	Loss for the period	(4,645)
	Total Tier 1 capital before PCD deductions	**780,556**
B	**Tier 2 Capital**	
	General Provision	15,224
	Profit Equalization Reserves	5,069
	Investment risk reserve	1,604
	Unrealized gains arising from fair valuations (45%)	20,852
	Aggregation	29,257
	Total Tier 2 capital before PCD deductions	**72,006**
C	**Total Available Capital (A+B)**	**852,562**
D	**General deductions from Tier 1 & 2 under PCD Module**	
	Deduction of unconsolidated financial subsidiaries which are aggregated or deducted	(99,634)
	Deduction of unconsolidated financial associates which are aggregated or deducted	(4,557)
	Excess over maximum permitted large exposure limit	(85,363)
	Total Deductible Items	**(189,554)**
E	**Total Eligible Capital (C-D)**	**663,008**

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

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

Exposure funded by Self Finance

	Risk weighted assets	Capital requirement
Claims on sovereign	84,491	10,139
Banks	122,566	14,708
Corporate portfolio	426,549	51,186
Investments in securities	1,039,979	124,797
Holding of real estate	856,111	102,733
Regulatory retail	1,680	202
Past due financings	135,910	16,309
Other assets	197,475	23,697
Aggregation	1,453,844	174,461
Total	**4,318,605**	**518,232**

Exposure funded by Unrestricted Investment Accounts (URIA)

	Risk weighted assets	Capital requirement
Corporate portfolio	83,866	10,064
Equity portfolio	19,097	2,292
Holding of real estate	20,331	2,440
Regulatory retail	175,347	21,042
Past due financings	77,168	9,260
Total	**375,809**	**45,098**

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

8. Gross credit exposures:

	Gross credit exposure	Average gross credit exposure
Credit risk exposure relating to on balance sheet assets are as follows:		
Cash and balances with banks and central banks	668,199	631,935
Commodity and other placements with banks, financial and other institutions	383,352	440,837
Murabaha and other financings	3,306,155	3,229,900
Musharaka financing	75,238	68,670
Investments	2,563,377	2,525,438
Other assets	295,802	281,497
Fixed assets	118,699	116,932
Intangible assets	223,829	223,687
Total on balance sheet credit exposure	**7,634,651**	**7,518,896**
Credit risk exposure relating to off balance sheet items are as follows:		
Financial guarantees and irrevocable letters of credit	858,470	905,223
Financing commitments, Undrawn facilities and other credit related liabilities	2,378,249	2,515,945
Total off balance sheet credit exposure	**3,236,719**	**3,421,168**
Total credit exposure	**10,871,370**	**10,940,064**
Total credit exposure financed by URIA	**2,013,236**	**2,021,123**
Total credit exposure financed by URIA (%)	**18.52%**	**18.47%**

Average gross credit exposures have been calculated based on the average of balances outstanding during the six month period ended 30 June 2014.

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

9. Geographical distribution of credit exposures:

	Asia/ Pacific	Middle East	Europe	North America	Others	Total
On-balance sheet items						
Cash and balances with banks and central banks	288,737	205,924	132,229	41,309	-	668,199
Commodity and other placements with banks, financial and other institutions	-	347,045	28,754	-	7,553	383,352
Murabaha and other financings	1,793,626	1,169,361	226,342	128	116,698	3,306,155
Musharaka financing	75,238	-	-	-	-	75,238
Investments	1,259,283	1,127,677	147,747	28,670	-	2,563,377
Other assets	156,840	84,894	37,220	16,843	5	295,802
Fixed assets	58,564	60,067	68	-	-	118,699
Intangible assets	24,186	195,584	4,059	-	-	223,829
Total on balance sheet items	**3,656,474**	**3,190,552**	**576,419**	**86,950**	**124,256**	**7,634,651**
Off balance sheet items	**2,539,403**	**661,860**	**27,926**	**-**	**7,530**	**3,236,719**
Total credit exposure	**6,195,877**	**3,852,412**	**604,345**	**86,950**	**131,786**	**10,871,370**

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

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

10. Industrial distribution of credit exposures:

	Banks and financial institutions	Trading and manufacturing	Property and construction	Services	Private Individuals	Textile	Others	Total
On-balance sheet items								
Cash and balances with banks and central banks	668,199	-	-	-	-	-	-	668,199
Commodity and other placements with banks, financial and other institutions	383,352	-	-	-	-	-	-	383,352
Murabaha and other financings	424,071	1,251,789	197,589	193,046	838,382	113,730	287,548	3,306,155
Musharaka financing	-	30,066	-	29,558	12,524	920	2,170	75,238
Investments	1,678,694	170,289	574,910	108,714	28,721	-	2,049	2,563,377
Other assets	201,357	15,988	32,132	7,421	35,634	36	3,234	295,802
Fixed assets	60,341	-	58,358	-	-	-	-	118,699
Intangible assets	223,829	-	-	-	-	-	-	223,829
Total on balance sheet items	**3,639,843**	**1,468,132**	**862,989**	**338,739**	**915,261**	**114,686**	**295,001**	**7,634,651**
Off balance sheet items	**780,612**	**1,267,327**	**424,718**	**130,196**	**193,132**	**37,351**	**403,383**	**3,236,719**
Total credit exposure	**4,420,455**	**2,735,459**	**1,287,707**	**468,935**	**1,108,393**	**152,037**	**698,384**	**10,871,370**

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

11. Maturity breakdown of credit exposures:

	Up to 1 Month	1-3 Months	3-12 Months	1-5 Years	5-10 Years	10-20 Years	Over 20 Years	Total
On-balance sheet items								
Cash and balances with banks and central banks	668,199	-	-	-	-	-	-	668,199
Commodity and other placements with banks, financial and other institutions	240,827	113,771	28,754	-	-	-	-	383,352
Murabaha and other financings	285,799	647,109	579,943	1,046,880	690,851	33,833	21,740	3,306,155
Musharaka financing	11,917	15,129	21,421	21,537	487	4,747	-	75,238
Investments	338,060	494,552	365,606	491,175	66,244	22,662	785,078	2,563,377
Other assets	116,251	14,964	121,321	16,539	8,945	7,890	9,892	295,802
Fixed assets	1,225	52	2,257	17,492	7,263	22,628	67,782	118,699
Intangible assets	-	-	-	7,293	15,858	155,477	45,201	223,829
Total on balance sheet items	**1,662,278**	**1,285,577**	**1,119,302**	**1,600,916**	**789,648**	**247,237**	**929,693**	**7,634,651**
Off balance sheet items	**651,635**	**620,470**	**446,282**	**1,480,615**	**37,717**	**-**	**-**	**3,236,719**
Total credit exposure	**2,313,913**	**1,906,047**	**1,565,584**	**3,081,531**	**827,365**	**247,237**	**929,693**	**10,871,370**

12. Related-party balances under credit exposure

A number of banking transactions are entered into with related parties in the normal course of business. The related party balances included under credit exposure at 30 June 2014 were as follows:

Affiliated companies	452,694
Directors & key management	12,934
Total	**465,628**

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

Non-banks	158,682
Total	**158,682**

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

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

	Gross exposure	Impairment provisions	Net exposure
Analysis by industry			
Manufacturing	254,302	191,475	62,827
Agriculture	16,536	6,233	10,303
Construction	90,623	21,788	68,835
Finance	2,143	1,581	562
Trade	206,371	57,361	149,010
Personal	81,642	16,560	65,082
Real estate	33,064	20,774	12,290
Technology and telecommunications	504	34	470
Transportation	2,276	1,255	1,021
Other sectors	63,377	45,395	17,982
Total	**750,838**	**362,456**	**388,382**
Ageing analysis			
Over 3 months up to 1 year	186,562	8,793	177,769
Over 1 year up to 3 years	106,838	14,634	92,204
Over 3 years	457,438	339,029	118,409
Total	**750,838**	**362,456**	**388,382**

Movement in impairment provisions	**Relating to owners**	**Relating to unrestricted investment accounts**	**Total**
At 1 January 2014	264,114	67,186	331,300
Charge for the period	15,672	5,216	20,888
Write back during the period	(6,350)	-	(6,350)
Utilized during the period	-	(374)	(374)
Exchange differences	16,992	-	16,992
At 30 June 2014	**290,428**	**72,028**	**362,456**

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

14. Past due and impaired financings by geographical areas:

Analysis by Geography	Gross exposure	Impairment Provisions	Net exposure
Asia / Pacific	355,857	236,981	118,876
Middle East	385,391	120,469	264,922
Europe	9,590	5,006	4,584
Total	**750,838**	**362,456**	**388,382**

15. Details of credit facilities outstanding that have been restructured during the six month period ended 30 June 2014:

Restructured financings during the six month period ended 30 June 2014 aggregated to $7.6 million. This restructuring had an impact of $1.3 million on present earnings during the six month period ended 30 June 2014. Further, this restructuring is expected to have positive impact of $0.5 million on the Group’s future earnings in 2014. Extension of maturity dates was the basic nature of concessions given to all the restructured facilities.

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

Exposure funded by Self Finance

	Gross Exposure	Eligible Financial Collateral
Corporate portfolio	1,555,116	199,592
Retail Portfolio	276,484	36,720
Past due financings	173,497	9,473
Total	**2,005,098**	**245,785**

Exposure funded by Unrestricted Investment Accounts

	Gross Exposure	Eligible Financial Collateral
Corporate portfolio	334,767	55,215
Retail Portfolio	780,007	688
Past due financings	201,450	22,051
Total	**1,316,224**	**77,954**

Counterparty Credit Risk (CCR)

	Gross Positive Fair Value of Contracts	Netting Benefit	Credit Risk Mitigation	Net Value Exposure at Default	Risk Weighted Assets
Profit Rate Contracts	2,171	-	-	2,171	2,171
Foreign Exchange Contracts	4,239	-	-	4,239	2,242
Total	**6,410**	**-**	**-**	**6,410**	**4,413**

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

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

	Risk weighted assets			Capital requirement		
	30 June 2014	**Maximum Value**	**Minimum Value**	**30 June 2014**	**Maximum Value**	**Minimum Value**
Foreign exchange risk	145,789	145,789	145,592	17,495	17,495	17,471
Aggregation						
Foreign exchange risk	4,746	4,746	13,951	570	570	1,674
Profit Rate Risk (Trading Book)	27,792	27,792	9,785	3,335	3,335	1,174
Equity Position Risk	40,698	40,698	36,934	4,884	4,884	4,432
Commodity Risk	-	-	-	-	-	-
Total	**219,025**	**219,025**	**206,263**	**26,283**	**26,283**	**24,752**

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

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

The alpha coefficient has been set at 15% under CBB Basel II guidelines. The capital requirement for operational risk at 30 June 2014 aggregated to $53.1 million.

19. Tier one capital ratios and Total capital ratios:

	Tier One Capital Ratio	**Total Capital Ratio**
Ithmaar consolidated	11.03%	12.38%
Significant Bank subsidiaries whose regulatory capital amounts to over 5% of group consolidated regulatory capital whether on a stand-alone or sub-consolidated basis are as follows:		
Faysal Bank Limited	10.30%	11.92%

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

20. Equity position in Banking book

At 30 June 2014, the Group's investment securities aggregated to $1,377 million. Out of the total investment securities, $49.4 million were listed investment securities and the remaining $1,327.6 million represented unlisted investment securities.

Cumulative realized income from sale of investment securities during the six month period ended 30 June 2014 amounted to $1.4 million. Total unrealized income recognized in the consolidated statement of changes in owners' equity amounted to $1.1 million.

At 30 June 2014, capital requirements using standardized approach aggregated to $51.1 million for listed investment securities and $77.3 million for unlisted investment securities excluding capital charge of investment securities classified as real estate holdings.

21. Gross income from Mudaraba and profit paid to Unrestricted Investment Accountholders:

	30 June		**31 December**				
	2014	**2013**	**2013**	**2012**	**2011**	**2010**	**2009**
Income from unrestricted investment accounts	51,742	49,790	100,796	93,207	67,926	61,546	48,836
Less: return to unrestricted investment accounts	(42,406)	(37,684)	(77,133)	(70,785)	(65,019)	(56,395)	(44,796)
Group's share of income from unrestricted investment accounts as a Mudarib	**9,336**	**12,106**	**23,663**	**22,422**	**2,907**	**5,151**	**4,040**

For the six month period ended 30 June 2014 the return to unrestricted investment accountholders based on the average balance outstanding during six month period stood at 7.12%. The Group's share of income from unrestricted investment account (Mudarib) including management fee for the six month period ended 30 June 2014 as a percentage of gross income from unrestricted investment accounts stood at 36.08%.

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

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

	30 June		31 December				
	2014	**2013**	**2013**	**2012**	**2011**	**2010**	**2009**
Profit Equalization Reserve							
As at 1 January	2,546	10,061	10,061	18,607	8,154	3,099	3,645
Net addition	2,523	2,636	5,183	5,443	10,453	6,011	-
Transfer to impairment provisions	-	(6,694)	(12,698)	(13,989)	-	-	-
Net utilization	-	-	-	-	-	(956)	(546)
Closing balance	**5,069**	**6,003**	**2,546**	**10,061**	**18,607**	**8,154**	**3,099**
Amount appropriated as a percentage of gross profit	5%	5%	5%	6%	15%	10%	-
Provisions							
As at 1 January	105,743	88,363	88,363	68,854	69,767	64,427	46,562
Net addition	5,216	3,239	6,496	6,406	1,456	5,464	17,865
Transfer from Profit Equalization Reserve	-	6,694	12,698	13,989	-	-	-
Net utilization	(374)	(1,673)	(1,814)	(886)	-	(124)	-
Reclassification	-	-	-	-	(2,369)	-	-
Closing balance	**110,585**	**96,623**	**105,743**	**88,363**	**68,854**	**69,767**	**64,427**

At 30 June 2014, the ratio of profit equalization reserve and provisions to equity of unrestricted investment accountholders stood at 0.26% and 5.6% respectively.

At 30 June 2014, the ratio of financings to URIA stood at 64.9%.

At 30 June 2014, the Investment Risk Reserve (IRR) amounted to $1.6 million.

The following table summarizes the breakdown of URIA and impairment provisions

	30 June		31 December				
	2014	**2013**	**2013**	**2012**	**2011**	**2010**	**2009**
URIA : Banks	41,606	40,405	119,655	35,178	58,260	83,584	83,581
URIA : Non-Banks	1,924,017	1,761,298	1,865,814	1,715,944	1,418,374	1,112,379	899,430
Provisions : Banks	2,341	2,167	6,373	1,775	2,717	4,876	5,478
Provisions : Non-Banks	108,244	94,456	99,370	86,588	66,137	64,891	58,949

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

23. Gross return from Restricted Investment Accounts (RIA)

	30 June		31 December				
	2014	2013	2013	2012	2011	2010	2009
Gross income / (expense)	(161)	385	4,279	268	2,408	7,523	5,544
Mudarib fee	108	257	599	809	2,814	12,249	17,952

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

	30 June		31 December				
	2014	2013	2013	2012	2011	2010	2009
	Percentage						
7 Days	0.23	0.25	0.25	0.25	0.30	0.50	0.50
30 Days	1.21	1.67	1.49	1.90	2.31	3.00	3.17
90 Days	1.71	2.17	1.99	2.48	2.90	3.25	3.25
180 Days	2.21	2.67	2.49	2.90	3.25	3.50	3.50
360 Days	2.66	3.17	2.97	3.40	3.50	3.70	3.63

25. Profit rate risk:

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

	USD	EUR	PKR	BD	AED
Total profit rate exposure	494,669	129,550	158,177	1,007,943	280,978
Rate shock (assumed) (+/-)	0.05%	0.02%	0.25%	0.25%	0.37%
Total estimated impact (+/-)	**247**	**26**	**395**	**2,520**	**1,040**

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

26. Currency risk:

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

The significant net foreign currency positions at 30 June 2014 were as follows:

	Long/(Short)
Pakistani Rupee	98,693
Euro	(118,917)
United States Dollars	104,932
Polish Zloty	64,686
UAE Dirham	(283,289)
Hong Kong Dollar	68,833

27. Performance ratios:

	30 June		31 December				
	2014	2013	2013	2012	2011	2010	2009
Return on average assets	0.05%	-0.21%	-1.08%	-0.38%	-0.91%	-2.18%	-4.13%
Return on average Shareholders' equity	-0.04%	-2.50%	-14.34%	-5.23%	-10.20%	-21.99%	-30.26%
Cost to operating income Ratio	87.54%	97.72%	97.60%	85.38%	121.71%	72.06%	139.31%

28. Liquidity ratios

	30 June		31 December				
	2014	2013	2013	2012	2011	2010	2009
Liquid assets to total assets	13.77%	13.03%	14.78%	13.74%	12.80%	13.48%	17.02%
Short term assets to short term liabilities	61.15%	49.67%	66.97%	56.98%	63.80%	63.44%	83.39%

29. Legal contingencies and compliance:

At 30 June 2014, the Group had contingent liabilities towards customer and other claims aggregating to $391.2 million. The management is of the view that these claims are not likely to result into potential liabilities. During the six month period ended 30 June 2014, the Bank paid penalty of $16.3 thousand imposed by the CBB due to delay in compliance of regulatory submission requirement.