



# SUCCESS THROUGH PARTNERSHIP

Annual Report 2009



بنك الاستثمار الدولي  
INTERNATIONAL INVESTMENT BANK

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بِسْمِ اللَّهِ الرَّحْمَنِ الرَّحِيمِ

﴿قُلْ إِنْ رَبِّي يَبْسُطُ الرِّزْقَ لِمَنْ يَشَاءُ مِنْ عِبَادِهِ وَيَقْدِرُ لَهُ  
وَمَا أَنْفَقْتُمْ مِنْ شَيْءٍ فَهُوَ يُخْلِفُهُ وَهُوَ خَيْرُ الرَّازِقِينَ﴾

صَدَقَ اللَّهُ الْعَظِيمُ

# PROFILE

## Profile

International Investment Bank B.S.C. (c) (IIB) was incorporated as an Islamic investment bank on 6 October 2003, under commercial registration number 51867 as a Bahrain Joint Stock Company (closed). Operating under an Islamic wholesale banking licence issued by the Central Bank of Bahrain, IIB commenced investment activities on 13 October 2003.

IIB has an authorized capital of US\$ 200 million and its paid-up capital was increased during 2007 from US\$ 43 million to US\$ 110 million, through a combined rights issue and private placement issue. The Bank's shareholders are high net worth individuals, business houses and institutions from the GCC states.

The core business activities of the Bank include investing on its own account and investment, underwriting and placement in real estate and private equity in conformity with Islamic Shari'ah. It aims to offer its clients an internationally diversified range of investments generated through its network of strategic partnerships.

### **Vision**

To be a regional leader in private equity investments and real estate investments mainly through the provision and management of high-quality, globally-diversified investment offerings in accordance with the principles of Islamic Shari'ah; to maximize shareholder value; to generate superior risk-adjusted returns for clients; to provide excellent career opportunities to all employees and to deal fairly with all stakeholders.

### **Mission**

To originate, manage and ultimately exit from a well-diversified range of innovative investment products in association with leading international strategic partners; to provide high-quality advisory services to clients; to operate in accordance with the highest standards of corporate governance, risk management, due diligence and ethical standards; and to attract and retain the best-qualified employees available.

# SIX YEAR FINANCIAL SUMMARY

	2009	2008	2007	2006	2005	2004
<b>Earnings (US\$ millions)</b>						
Total income	6.3	34.9	31.1	24.6	12.4	4.2
Total expenses	8.9	16.6	13.2	11.1	5.4	3.4
Operating profit (loss)	(2.6)	18.3	17.9	13.5	7.0	0.8
Share of profit (loss) of associate	(0.1)	(4.1)	3.2	-	-	-
Impairment losses and provisions	(25.2)	(0.7)	-	-	-	-
Net income	(27.9)	13.5	21.1	13.5	7.0	0.8
Dividend (%) – cumulative 40%	-	7.0	15.0	10.0	8.0	-

<b>Financial Position (US\$ millions)</b>						
Total assets	179.5	218.7	257.3	94.5	63.4	44.4
Cash and due from financial institutions	57.7	120.5	215.1	62.7	27.2	28.0
Investments	68.3	62.9	36.4	16.4	13.7	14.1
Due to financial institutions	-	-	-	20.0	-	-
Equity	176.5	210.7	216.4	61.4	50.8	43.8

## Financial Ratios

<b>Profitability</b>						
Return on average equity (%)	(14.4)	6.3	15.2	24.1	14.8	1.8
Return on average assets (%)	(14.0)	5.7	12.0	17.1	13.0	1.8
Earnings per share (cents)	(25)	12	19	31	16	2
Cost-to-income ratio (%)	141.3	47.6	42.4	45.1	43.5	81

## Capital

Capital adequacy Ratio (regulatory minimum 12%)	59	87	126	134	101	200
Equity/total assets (%)	98.3	96.3	84.1	65.0	80.1	98.6

## Liquidity and Other

Investments/total assets (%)	38.1	28.8	14.1	17.4	21.6	31.8
Liquid assets/total assets (%)	32.1	55.1	83.6	66.3	42.9	63.1
Assets under management (US\$ millions)	422.8	414.0	348.0	181.7	117.6	41.6
Number of employees (at year end)	47	50	55	40	20	17

# SUMMARY OF PRINCIPAL INVESTMENT STRUCTURINGS 2004-2009

Year	Investment Description	Location	Private Equity (US\$ millions)	Other Funds # (US\$ millions)	Total Transaction Size (US\$ millions)	
1	2004	Property fund **	Bahrain	18.6	18.5	37.1
2	2004	Independent power producer ***	China	23.0	267.0	290.0
3	2005	Housing development company	Bahrain	22.6	0.6	23.2
4	2005	Income generating property *	UK	14.8	290.6	305.4
5	2005	Tower development *	Dubai	20.5	73.6	94.1
6	2005	Islamic investment bank	UK	19.8	448.0	467.8
7	2005	Paper manufacturing company	Abu Dhabi	12.0	35.1	47.1
8	2006	Income generating properties	France	50.8	68.7	119.5
9	2006	Real estate development company	Saudi Arabia	21.0	85.8	106.8
10	2006	Office tower development	Dubai	25.0	75.2	100.2
11	2007	Steel reinforcement bar manufacturing plant	Bahrain	13.0	28.4	41.4
12	2007	Income generating properties	Germany	99.3	133.7	233.0
13	2007	Real estate investment company	Saudi Arabia	2.7	10.7	13.4
14	2007/8	Mixed use tower development	Abu Dhabi	65.0	132.4	197.4
15	2007/8	Commercial bank	Azerbaijan	26.0	20.8	46.8
16	2008	Automobile dealership company	Tunisia	36.0	30.0	66.0
17	2008	Sugar manufacturing company	Bahrain	20.5	136.1	156.6
18	2009	Tower/shopping centre development	Bosnia	33.7	124.1	157.8
19	2009	Affordable housing development	Saudi Arabia	31.8	466.8	498.6
<b>Totals</b>				<b>556.1</b>	<b>2,446.1</b>	<b>3,002.2</b>

\* Investment realized in 2006

\*\* Partial exits in 2006, 2007 and 2009

\*\*\* Investment realized in 2007

# Comprises partners' contributions, borrowings and equity from IPO.

## Sector Summary

Sector	Private Equity Raised (US\$ millions)	Other Funds (US\$ millions)	Total Transaction Size (US\$ millions)	
1	Real estate income generating	164.9	493.0	657.9
2	Real estate development	197.0	957.9	1,154.9
3	Private equity	175.6	976.7	1,152.3
4	Property fund	18.6	18.5	37.1
<b>Totals</b>		<b>556.1</b>	<b>2,446.1</b>	<b>3,002.2</b>

## Principal Bankers and Professional Advisors

**Principal Bankers** : Ahli United Bank, Bahrain,  
Union National Bank, UAE

**External Auditors** : Ernst & Young, Bahrain

**External Legal Counsel** : Qays H. Zu'bi, Bahrain

# BOARD OF DIRECTORS' REPORT



A handwritten signature in black ink, appearing to be 'Saeed Abdul Jalil Al Fahim'.

**Saeed Abdul Jalil Al Fahim,**  
Chairman

## **Dear Shareholders,**

In line with our expectations stated in the 2008 Annual Report, 2009 has proven to be a difficult year for the world economy and financial markets. Only recently, there appear to be early signs that indicate a “reluctant” easing of the unfavourable conditions that have prevailed in the last two years.

At the highest level of analysis, it appears that economic conditions in Asia are heading for a gradual improvement whereas those for the western markets, particularly Europe, continue to remain weak and volatile.

Whilst developments in Asia have contributed to a better-than-average economic climate all other major economic regions continue to demonstrate metrics below their long term averages. At best, many experts assess the current economic situation as less unfavorable than it was in 2008 and for most of 2009. Although a recovery is on the way, the trajectory, robustness, and speed of such recovery are defiantly uncertain.

Closer to home, in the backdrop of the above sentiment, demand from regional investors for higher yielding, longer maturity offerings in real estate and private equity, the primary business proposition of your Bank, has not returned to the levels previously experienced. In addition, regional banks continue to be highly cautious in their financing of especially real estate development and private equity projects, as they continue to suffer from a lack of liquidity.

Having said that, I am pleased to state that notwithstanding a “first ever” loss since inception your Bank has weathered the year 2009 much better than many of its peers and other financial institutions in the region by following basic and prudent investment and liquidity management strategies.

## Investing Strategy

We stated in our last report that "IIB will continue to opt for the ultra-cautious investment philosophy of 2008 and focus on very selective investment purchases, capital preservation and maintenance of the existing portfolio. We are ready to invest from our deal "pipeline" in the right opportunities at attractive valuations."

In keeping with our strategy above, your Bank closely monitored the market and invested in only two transactions that we believe will offer investors superior risk adjusted returns. These two investments are currently in the process of being offered to our investors. In addition, IIB has selectively invested in listed regional equities and has profitably exited in one case, while retaining the shares in other investments until share prices increase.

## Portfolio Exits

I am also pleased to state that despite the difficult conditions of 2009, your Bank has secured the full exit of Bahrain Property Fund, one of its very first real estate initiatives, to be executed in the first quarter of 2010. The Fund, upon exit, is expected to have delivered current returns and total returns as predicated at the time of the offering to investors. Apart from the full exit of this investment, the Bank is actively pursuing the exit of some of its other investments. Although negotiations are ongoing, we would like to emphasize that preservation of investors' capital continues to be the highest priority of the Bank; the payment of current returns in the context of the current economic conditions, are of secondary priority.

## Current Portfolio

Your Bank conducted an extensive evaluation of its investment offerings of the previous years with the view to assessing if any of the investments have impaired, i.e., experienced valuation losses that are unlikely to recover in the near future. I am pleased to report that out of the 18 investments offered to investors over the last 6 years, only one investment, accounting for only 3.8% of the total offerings to date, has experienced an impairment and these impairments have been appropriately recorded in the Income Statement for 2009 in compliance with the relevant accounting standards.

## Liquidity Management Strategy

As you very well know, liquidity is necessary to ensure that an institution can meet its obligations as they fall due and to enable it to take advantage of market opportunities to purchase assets at advantageous prices, and at the same time, manage its operational cash flow requirements. I am pleased to confirm that your Bank's asset and capital positions demonstrate core strength, with 31% of Total Assets represented by murabaha short-dated placements with banks and a further 8% invested in regional listed equities, thereby maintaining 39% of the Total Assets in liquid and semi-liquid form.

IIB continues to, as stated earlier, place capital protection at the centre of its liquidity management policy. Thus, IIB has chosen to retain most of its liquidity in low-risk murabaha placements with financially sound regional banks. The maximum tenor has usually been one month, but in some cases has been extended to a maximum of 6 months in order to secure higher profit yields during a period of extremely low profit rates.

As in 2008, IIB chose to rely solely on internal funding through its shareholders' equity and consequently did not resort to any bank borrowings. This decision has yielded results in the form of balance sheet stability and IIB, accordingly, has always been a "lender" to its portfolio companies. In addition, IIB had no significant commitments, no off-balance sheet exposures and no derivatives or Collateralized Debt Obligations (CDO) positions at any time in 2009.

## 2009 Financial Performance

IIB has incurred a Net Loss for the year of US\$27.9 million compared to a Net Profit of US\$13.5 million in 2008, being the first ever loss in its history of 6 years. There are three major contributing factors to the loss: (1) investment banking fees were US\$20.6 million (91%)

lower due to fewer investments being placed with investors; (2) unrealized impairment losses on available for sale investments of US\$21.4 million, including one listed equity in Abu Dhabi that has declined in value by over US\$20.0 million or 61% in 2009; and (3) provisions of US\$3.8 million against possible future losses on investments and receivables. Conversely, total expenses are US\$7.7 million (46%) lower than in 2008 and are consistent with the reduced investment activity.

The Capital Adequacy Ratio at 31 December 2009 of 59% is about 5 times the minimum requirement of 12% mandated by the Central Bank of Bahrain. This demonstrates a strong and prudent approach by the Bank in managing its capital and allows for ample headroom to acquire future risk assets from a regulatory capital standpoint.

## 2009 Investment Offerings

During 2009, the sixth year of full operations, IIB has concluded the sell down of the 14.3% stake, carried over from 2008, in the first sugar plant to be constructed in the Kingdom of Bahrain.

From a review of numerous proposals received during 2009 that constitute the deal "pipeline", the Bank has structured, as stated earlier, only two investment transactions, underscoring its strategy of investing in only very carefully selected transactions.

1. During the third quarter of 2009, construction work has commenced on IIB's recently acquired project to develop a state-of-the-art "commercial" real estate complex in Bosnia and Herzegovina.
2. Secondly, the Bank has invested in the fourth quarter of 2009 in a well-positioned "residential" project in Saudi Arabia to build affordable homes for middle-income Saudis.

Both transactions are in the stage of obtaining final regulatory approvals from the Central Bank of Bahrain to be offered to investors in 2010. In addition, several deals have been evaluated for possible product launches in the second half of 2010 but are subject to the return of favorable market conditions and completion of the detailed due diligence thereon.

## Outlook: 2010 & Beyond

Global confidence from investors in the financial markets in general continues to remain weak and the management of liquidity and solvency on a day-to-day basis for many financial institutions continues to be challenging and is their number one priority. In this market environment, IIB will maintain high levels of liquidity to be ready to invest from the deal "pipeline" in the right opportunities at attractive valuations. We expect 2010 to be another challenging year for the investment banking sector.

## Shareholders' Dividends and Zakah

Following the Net Loss for the year, the Board has recommended that no dividend is paid for the year. As in the previous years, shareholders will directly pay their respective Zakah on their equity investments in the Bank.

## Board Membership

There were no changes during 2009.

## Appreciation

I take this opportunity to sincerely thank all shareholders for their continued confidence and trust in the Bank since its inception. I would also like to thank all my colleagues on the Board of Directors for their co-operation and guidance during the year, our management team and staff for their dedication and hard work, and finally the Central Bank of Bahrain and the Ministry of Industry and Commerce for their regulatory advice and support.

Our "Vision Statement" encompasses the commitments to "maximize shareholder value and to generate superior risk-adjusted returns for clients" and we will be striving towards this goal in 2010 and beyond.

# CORPORATE GOVERNANCE

The Board of Directors is responsible for the overall governance of the Bank through continuous review and adherence to international best practice and standards. The Board determines the Bank's strategy, provides direction to the Executive Management, ensures that the control framework is functioning in accordance with best practice and monitors Executive Management's performance.

## Board of Directors

The Board meets regularly throughout the year in order to control strategic, financial, operational, internal control and compliance issues. It currently comprises nine non-executive directors and one executive director.

## Board Members

The Board of Directors comprised the following members as at 31 December 2009:

### 1. HE. Saeed Abdul Jalil Al Fahim

Chairman

Chairman of Al Fahim Group, UAE; President of Sh. Khalifa Excellence Award (Abu Dhabi Chamber of Commerce and Industry); Chairman of Mubarak & Brothers Property & Financial Investment - Abu Dhabi; Former Deputy President of Abu Dhabi Chamber of Commerce and Industry; Former Member of Board of National Bank of Abu Dhabi; Former Member of Board of United Arab Bank.

### 2. Mr. Ahmed Salem Bugshan

Vice Chairman

Chief Executive Officer - Saudi Industrial Projects Co.(Pepsi-Cola), Saudi Arabia ; Chairman - Saudi Steel Profile Mfg. Co. Ltd., Saudi Arabia; Chairman - Savoy Sharm El Sheikh Hotel, Egypt; Board Member - Tirana Tourism Investment Cairo, Egypt.

### 3. Mr. Aamer Abdul Jalil Al Fahim

Director

Managing Director - Al Fahim Group, UAE; Board Member - Al Wathba Insurance Company; Member - Federal National Council, UAE; Board Member - Abu Dhabi Chamber of Commerce and Industry; Board Member - Al Qudra Holdings; Board Member – Marriage Fund; Board Member – Abu Dhabi University Board of Trustees; Board Member- Al Rayan Investments; Chairman - Aradi Properties P.J.S.C.

### 4. Mr. Ebrahim Eshaq Abdulrahman

Director

Chairman, Union Gulf Investment Co. S.P.C.; Managing Director , Investment and Trading (Gulf) Enterprises, B.S.C.(C) Bahrain; Director, Bahrain Car Parks Co. B.S.C.; Director, United Gulf Investment Corporation B.S.C.; Founder Shareholder and former Managing Director, Bank of Bahrain and Kuwait.

### 5. Mr. Abdul Wahab Mohammed Al Wazzan

Director

Chairman of Kuwait Real Estate Bank; Vice Chairman of National International Holding Company; Deputy Treasurer – Kuwait Chamber of Commerce & Industry; Former Minister of Commerce & Industry, Kuwait; Former Minister of Social Affairs & Labour, Kuwait; Former Chairman of Social Development Office, Kuwait.

### 6. Mr. Fahad Fouad Bubshait

Director

CEO - Bareeka Ltd; Chairman - Audeo Maxima Holdings, UAE; Former Chairman - BubbleDeck Middle East LLC, UAE; Foreign Investments Advisor to Mr. Fouad Abdulla Fouad, President of Abdulla Fouad Holding Co. Ltd ; Former General Manager - Abdulla Fouad Holding Co. Ltd.

### 7. Mr. Ali Haider Suliman Al Haider

Director

Vice Chairman & Shareholder of Suliman & Brothers Co W.L.L.; Board Member of Qatar German Medical Co.; Board Member of Salam Bounian; Partner in Al Safa Trading Company; Shareholder of Sulian Hajj Haider & Sons.

### 8. Mr. Ali Hashim Sadiq Hashim

Director

President & CEO - Gulf United Investment, KSA; Chairman - Gulf Packaging Systems; KSA, Board Member - Middle East Telecom (METCO), KSA; Partner & Board Member - Arabian Gulf Manufacturer (AGM), Jeddah, KSA; Chairman - Prime Plastic Products (3P), Jeddah, KSA; President - Tahweel Investment, Ras Al-Khaimah, UAE; Chairman - Rawasy Al Khaleej Plastic Ind. Sharjah, UAE; Vice Chairman & CEO - Gulf Manufacturer (GM), Egypt; Board Member - Safra Petrochemical, Jeddah.

### 9. Dr. Bader Ibrahim Mohammad Bin Saedan

Director

General Manager – Al Saedan Real Estate Co , Saudi Arabia; Chairman - Saudi Maintenance Made Simple (SMMS), KSA; Board Member – Commodore International, U.K; Board Member—Saudi Tunisian Real Estate Co., Tunisia; Board Member – Mawten R.E. Co., Saudi Arabia; Member of the R. E. Committee – Riyadh Chamber of Commerce & Industry.

### 10. Mr. Aabed Al-Zeera

Director and Chief Executive Officer

Chief Executive Officer, IIB; Director, European Islamic Investment Bank Plc, United Kingdom; Vice-Chairman of AmrahBank, Azerbaijan; Director of several companies of IIB.



**1. HE. Saeed Abdul Jalil Al Fahim,**  
Chairman



**2. Mr. Ahmed Salem Bugshan,**  
Vice Chairman



**3. Mr. Aamer Abdul Jalil Al Fahim,**  
Director



**4. Mr. Ebrahim Eshaq  
Abdulrahman,** Director



**5. Mr. Abdul Wahab Mohammed  
Al Wazzan,** Director



**6. Mr. Fahad Fouad Bubshait,**  
Director



**7. Mr. Ali Haider Suliman  
Al Haider,** Director



**8. Mr. Ali Hashim Sadiq Hashim,**  
Director



**9. Dr. Bader Ibrahim Mohammad  
Bin Saedan,** Director



**10. Mr. Aabed Al-Zeera,** Director  
and Chief Executive Officer

# CORPORATE GOVERNANCE

## Board Committees

The Board has established four sub-committees and a Shari'ah Supervisory Board comprising expert, independent scholars to assist the Board in expeditiously and effectively discharging its responsibilities. This committee structure ensures appropriate oversight by the Board of Directors while permitting efficient day-to-day management of the Bank. The members and summary terms of reference are as follows:

### Executive Committee

**Mr. Aamer Abdul Jalil Al Fahim (Chairman)**  
**Mr. Ebrahim Eshaq Abdulrahman, Member**  
**Mr. Ali Hashim Sadiq Hashim, Member**  
**Dr. Bader Ibrahim Mohammad Bin Saedan, Member**

Assists the Board to review the Bank's strategy, annual budget and forecasts, risk policies and management committees' activities and actions.

### Audit Committee

**Mr. Abdul Wahab Mohammed Al-Wazzan (Chairman)**  
**Mr. Ali Haider Suliman Al Haider, Member**  
**Mr. Fahad Fouad Bubshait, Member**

Assists the Board to review the integrity of the financial statements, compliance with legal and regulatory requirements, the Bank's internal audit function and the independent auditor's qualifications, independence and performance.

### Nominations Committee

**Mr. Ahmed Salem Bugshan (Chairman)**  
**Mr. Aamer Abdul Jalil Al Fahim, Member**  
**Mr. Ali Hashim Sadiq Hashim, Member**

Assists the Board to assess candidates and to recommend Board and management appointments.

### Remuneration Committee

**Mr. Ali Hashim Sadiq Hashim (Chairman)**  
**Mr. Aamer Abdul Jalil Al Fahim, Member**  
**Mr. Ahmed Salem Bugshan, Member**

Assists the Board to establish and update the remuneration policies and procedures including the level of remuneration paid to executive management.

## Independent Shari'ah Supervisory Board

Being an Islamic Bank, IIB's Shari'ah Supervisory Board regularly reviews all investment products and business activities to ensure compliance with the Islamic Shari'ah principles, approves the Bank's financial statements and participates with management in the development of suitable investment products and services.

IIB's Shari'ah Supervisory Board comprises three prominent GCC Islamic scholars who provide the Bank with pragmatic Islamic opinions. Brief biographies are as follows:

### Sheikh Nizam Yaquby

Sh. Yaquby is a member of the Islamic supervisory board of several Islamic institutions, including the Central Bank of Bahrain, AAIOFI, Islamic Rating Agency, IIFM and Dow Jones Islamic Index. His work has appeared in the following publications: *Risalah Fi al-Tawbah*, *Qurrat al-'Ainayn fi Fada il Birr al-Walidayn*, *Irshad al-'Uqala'ila Hukun al-Qira'h min al-Mushaf fi al-Salah*, *Tahqia al-Amal fi Ikhraj Zakat al-Fitr bi al-Mal*.

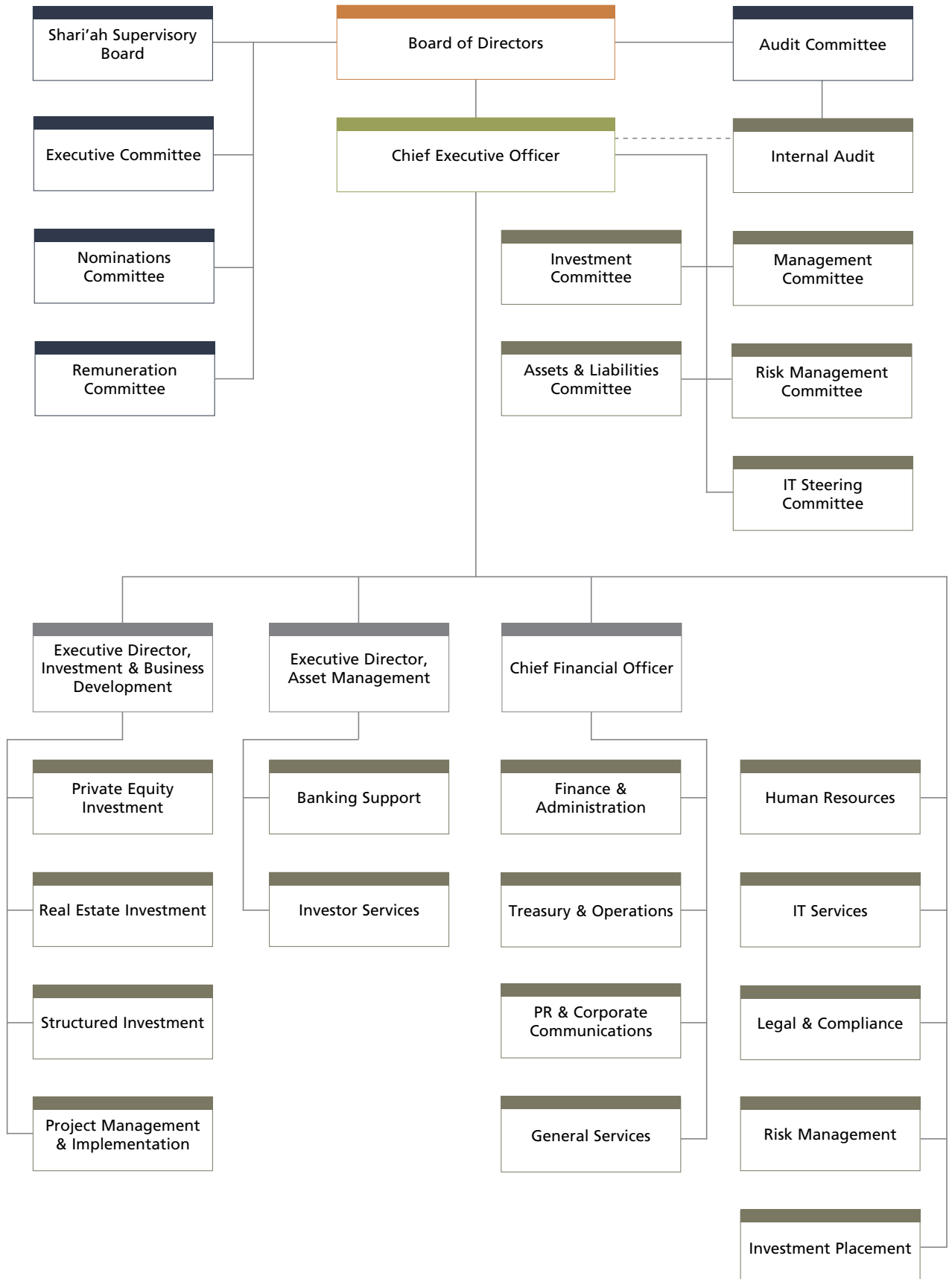
### Sheikh Abdul Sattar Abu Ghuddah

Sh. Abu Ghuddah holds a Ph.D. in Islamic law and comparative Fiqh from Al Azhar University Cairo, Egypt. He has taught at various institutes, including Imam Al Da'awa Institute (Riyadh), Religious Institute (Kuwait) and the Shari'ah College of the Law Faculty at Kuwait University.

### Sheikh Osama Mohammed Saad Bahar

Sh. Al Bahar holds a Bachelor's degree in Islamic Shari'ah and was an Associate Lecturer at the BIBF, Bahrain. He is a member of the Shari'ah Board of the National Investor Fund of Abu Dhabi and is a Shari'ah Advisor to Khaleej Finance and Investments. From 1994 to 2005, he was manager of the Shari'ah department at Shamil Bank, Bahrain. Since 2005, Sh. Osama has been Shari'ah compliance officer at ABC Islamic Bank, Bahrain and is currently Head of Shari'ah Compliance at First Energy Bank, Bahrain.

## Organizational Structure



# CORPORATE GOVERNANCE

## Investment and Business Development

The department is responsible for the investment and business development activities including origination, structuring and execution of investment programs and activities, obtaining the required internal and regulatory approvals and evaluating investments in quoted and unquoted equities. It develops investments and asset allocation strategies / activities and completes the detailed due diligence and documentation in conjunction with consultants, partners, accounting firms and law firms.

It also develops strategic relationships and performs the detailed evaluation of potential divestments.

## Asset Management

The department monitors the Bank's investments in private companies, real estate income generating properties and real estate development projects including effective record keeping relative to each investment to ensure efficient monitoring, cash inflow maximization and exit planning of investments.

It works closely with project sponsors to optimize the overall project implementation timetable; maximize project costs; and deliver project quality in order to ensure that planned project returns are achieved. The department arranges Shari'ah compliant corporate finance for projects designed to leverage equity funding, maximize free cash flows to equity and ROE. It executes planned exits in a timely and methodical manner to deliver investor returns.

In addition, it is responsible for investor reporting and relations including the preparation of periodic investment status reports.

## Investment Placement

The department is responsible for advising investors and placing IIB's investment offerings with sophisticated investors. Whilst mandated with the responsibility of maximizing investment placement, the department ensures that every investment placed with investors is consistent with the investment objectives and risk tolerance of investors. Moreover, in order to achieve best practice governance within the framework of the ethical and regulatory requirements of the Central Bank of Bahrain, investments are placed with only those investors who have provided the detailed "Know Your Customer" (KYC) documents and have otherwise complied with all legal formalities associated with the placement of each investment.

## Support, Administration & Internal Controls

The business departments and executive management of the Bank are supported by a network of well structured and staffed departments, as follows:

- Financial Control Department, including Treasury, Operations and General Services
- Legal & Compliance Department
- Risk Management Department
- Information Technology Department
- Internal Audit Department
- Human Resources & Administration Department
- Corporate Communications Department

The Bank's operations and transactions are subjected to commensurate controls, checks and balances and segregation of duties to ensure that each transaction is originated, approved, executed and accounted for in conformity with not only Shari'ah standards but also best practice.

For example, to ensure strong segregation of duties, the Bank's operations are structured to ensure that no employee can originate, execute and account for a transaction. At least two individuals are involved in each transaction, including two signatories on every funds transfer. Each transfer is approved and executed in accordance with "Levels of Authority" approved by the Board of Directors.

Department Heads report to the Chief Executive Officer and the Head of Risk Management has a reporting "dotted line" to the Chairman of the Board Audit Committee to ensure objectivity and independence from executive management. Likewise, the Director, Internal Audit reports to the Chairman of the Board Audit Committee with a reporting "dotted line" to the Chief Executive Officer. The duties of all staff are clearly defined in detailed job descriptions which are reviewed from time to time to ensure conformity with the current requirements of the business.

Being an Islamic bank, IIB must ensure that all its activities are in compliance with Shari'ah principles. Compliance is achieved through the adoption of policies and procedures that are Shari'ah compliant, through regular discussions with members of the Shari'ah Supervisory Board who review the documentation relating to the Bank's transactions. Consultants perform regular reviews of its activities and have confirmed that the Bank is Shari'ah compliant. During the year the Bank has donated all non - Shari'ah compliant earnings to charity.

## Compensation & Incentive Structures

The Directors receive an annual fee that is approved at the subsequent Annual General Meeting, plus reimbursement of their travel and accommodation expenses in connection with attending Board meetings. The members of the Shari'ah Supervisory Board receive a flat fee that the Board of Directors approves annually, plus a fee for each meeting attended and reimbursement of their actual travel and accommodation expenses. Executive management's salaries are set annually by the Remuneration Committee and the Chief Executive Officer agrees the annual salaries of all other employees. All staff are eligible to participate in the discretionary annual bonus pool which is awarded on the basis of achievement of both corporate and individual goals. Other benefits are payable to employees in line with normal industry practice and are approved in aggregate by the Board of Directors. An allocation for a staff stock option scheme was approved by the General Assembly. The details of the scheme are still under study.

## Executive Management

### Management Committees

The Board has established five management committees, namely the Management Committee, Investment Committee, Risk Management Committee, Assets & Liabilities Committee and IT Steering Committee. These committees comprise senior management and heads of departments who are best qualified to make decisions on such issues as funding, asset utilization, IT, investment purchase/sale and management of all types of risk, including market, credit, liquidity and operational risks.

### Management Committee

**Mr. Aabed Al-Zeera (Chairman)**  
**Mr. Mohamed Hadi Mejai, Member**  
**Mr. Michael Ross-McCall, Member**  
**Mr. Subhash Jalan, Member**

Monitors the execution of the strategic business plan, provides a forum to assimilate viewpoints and adopt best practices in the management of the Bank and provides guidelines to carry out the day-to-day affairs of the Bank, within the overall approved procedures laid down by the Board.

### Investment Committee

**Mr. Aabed Al-Zeera (Chairman)**  
**Mr. Mohamed Hadi Mejai, Member**  
**Mr. Subhash Jalan, Member**

Manages the investment portfolio, makes recommendations on proposed investments and exits and approves the final share allocation to investors.

## Risk Management Committee

**Mr. Michael Ross-McCall (Chairman)**  
**Mr. Mohamed Hadi Mejai, Member**  
**Mr. Mazar Jalal, Member**  
**Mr. Ninan Varkey, Member**

Performs a risk review of new business deals to be underwritten by IIB, performs an annual review of existing business deals underwritten by IIB and monitors all types of risks faced by IIB including market, credit and operational risks.

## Assets & Liabilities Committee

**Mr. Subhash Jalan (Chairman)**  
**Mr. Michael Ross-McCall, Member**  
**Ms. Haleema Ebrahim, Member**  
**Mr. Ninan Varkey, Member**  
**Mr. Fadi Al-Qassim, Member**

Manages liquidity, the profit rate risk inherent in the Bank's asset and liability portfolio, capital adequacy and ensures the mix of assets and liabilities is appropriate.

## I.T. Steering Committee

**Mr. Michael Ross-McCall (Chairman)**  
**Mr. Mohamed Hadi Mejai, Member**  
**Mr. Subhash Jalan, Member**  
**Mr. Said Itani, Member**

Ensures a first class IT and communication service to users, supervises projects to select and implement new systems, provides IT strategic direction and ensures that a bank-wide disaster recovery plan is prepared and implemented.

## Chairman and Executive Managers

### H.E. Saeed Abdul Jalil Al Fahim, Chairman

H.E. Saeed Al Fahim is the Chairman of Al Fahim Group, one of the most successful group of companies in the UAE operating chiefly in the automotive dealership, hospitality and hotel, oil and gas, real estate and insurance sectors. He obtained a degree in Business Administration from Bowling Green University, USA and Shendi University in Sudan has awarded him an Honorary Doctorate in Business Administration in appreciation of his distinguished contribution to Sudan's rural development. He holds a number of company directorships.

# CORPORATE GOVERNANCE

## **Abed Al-Zeera, Chief Executive Officer**

Mr. Al-Zeera oversees the Executive Management team and chairs the Management Committee. He holds an OND in Business Studies from a UK body and has almost thirty years of international banking experience with major financial institutions in the Kingdom of Bahrain and the United Arab Emirates. They include American Express Banking Corporation, Arab Banking Corporation (ABC), Standard Chartered Bank and First Islamic Investment Bank (now Arcapita). He was instrumental in setting up ABC's Representative Office in Abu Dhabi in 1996, where he served as Vice President and Chief Representative.

Mr. Al-Zeera was one of the key promoters of IIB who, together with the Al Fahim Group, conceived and successfully set up the Bank. He is a board member of several companies of IIB and is a Non-Executive Director of European Islamic Investment Bank Plc, London, where he chairs the Board Executive Committee. He is also Vice-Chairman of AmrahBank in Azerbaijan.

## **Mohamed Hadi Mejai, Executive Director**

Mr. Mejai heads Investment and Business Development. Prior to joining IIB in 2005, he spent several years with the Islamic Development Bank Group and affiliated investment companies and funds in the Kingdom of Saudi Arabia and UAE. He started his banking career in UK. Mr. Mejai's track record is mainly in acquisition structuring, monitoring and placement of investments. He holds a Masters of Science from the University of London, UK and completed his executive education at the Theseus International Institute, France, and the London Business School, UK. He is trilingual Arabic, French and English.

## **Michael Ross-McCall, Chief Financial Officer**

Mr. Ross-McCall heads Finance and Administration with additional responsibility for Treasury, Operations, General Services and Corporate Communications. He holds a Law Degree from Edinburgh University and is a member of The Institute of Chartered Accountants of Scotland. Following several years' employment with Ernst & Young and Price Waterhouse, he has over 20 years' experience in the banking sector, including senior positions at Wells Fargo Bank, Bank of Bahrain & Kuwait and Bahraini Saudi Bank.

## **Subhash Jalan, Executive Director**

Mr. Jalan heads Asset Management. He is a CFA charter holder, a member of the Institute of Chartered Accountants of India and holds the CISA (Certified Information System Auditor) qualification from USA. He has substantial investment experience in private equity including venture capital funds, buyout funds, direct equity, mezzanine funds and real estate investments. His previous work experience includes Vice President for manufacturing projects at Gulf Investment Corporation in Kuwait, Group Investment Manager at M H Alshaya Co. in Kuwait and Senior Investment Officer at Industrial Bank of Kuwait.

## **Other Senior Officers**

### **Ninan Varkey, Head - Risk Management**

Mr. Varkey holds a degree in Commerce and is a member of the Institute of Chartered Accountants of India. He carries over 20 years of experience in the financial services industry. He has held positions as President of Cochin Stock Exchange, India and Vice-President of leading financial services companies in India. He headed the risk management function at the commodity derivative business of Infrastructure Leasing Finance-Investsmart, India before joining IIB.

### **Ali Redha, Director, Internal Audit**

Mr. Redha is a member of the American Institute of Certified Public Accountants (AICPA). He has over 13 years of experience in auditing and banking at KPMG, Daar Al-Maal Al-Islami (DMI Group), Shamil Bank, Ithmaar Bank and Bahraini Saudi Bank. He joined IIB in 2005 in order to establish the internal audit department and reports to the Chairman of the Board Audit Committee.

### **Hakan Gunay, Director**

Mr. Gunay holds a B.Sc. degree in management from the Middle East Technical University in Turkey and obtained his MBA from Cass Business School, City University, London as a British Council Chevening Scholar. He started his career at the Export Credit Bank of Turkey and worked in Turkey and Belgium for companies operating in the energy sector. He also worked at the Islamic Corporation for the Development of the Private Sector, part of the Islamic Development Bank Group, in Saudi Arabia. He has more than 17 years of experience in the appraisal, development and financing of mainly industrial and infrastructure projects in Europe, the Middle East, Africa and Central Asia.

### **Said Itani, Head - IT**

Mr. Itani has more than 25 years' experience in the IT sector, latterly in Saudi Arabia and Bahrain. From 1995 to 2002 he was IT Division Manager at Bank Al-Jazira in Jeddah and from 2002 to 2006 he was Head of IT, Security and Property at UBS-Noriba Bank in Bahrain.

### **Ghizlane Rahali, Associate - Corporate Communications and PR**

Ms. Rahali obtained a B.Sc. degree in International Business Administration and Marketing from Old Dominion University, USA. She is responsible for IIB's Corporate Communications Department that includes media relations, PR, sponsorships and corporate publications. Prior to that, she was a sponsorship manager at the Bahrain International Circuit responsible for handling the sponsorship of several large regional companies and banks.

## Communications Strategy

A summary of the Bank's quarterly and annual financial statements is published in local and regional newspapers.

The Bank maintains a website [www.iib-bahrain.com](http://www.iib-bahrain.com) which contains the last five years of annual financial data as at 31 December, together with summary financial data covering the interim quarterly financial statements. It also contains a profile of the Bank, details of the principal products and services, profiles of the senior managers and regular press releases concerning investment transactions and other developments.

Inquiries are made to the relevant departments as follows:

Investments and partnerships: [invest@iib-bahrain.com](mailto:invest@iib-bahrain.com)

Existing Investors inquiries: [portfolio@iib-bahrain.com](mailto:portfolio@iib-bahrain.com)

New investors: [placement@iib-bahrain.com](mailto:placement@iib-bahrain.com)

Financials and annual performance: [enquiries@iib-bahrain.com](mailto:enquiries@iib-bahrain.com)

The Bank's Asset Management Department has assigned a designated individual to maintain a log of the client queries / complaints. A brief of client inquiry / complaint is prepared and forwarded to the concerned Asset Manager, who prepares a draft response. Brief is then forwarded to the Head of Asset Management who approves the response, which is then forwarded to the client. An entry is made in the log of queries / complaints that query is being entertained.

## Additional Governance Controls

The Board has approved a number of policies, which are communicated to management and all staff. These cover subjects including risk management, anti-money laundering, ethical behaviours, personal conduct, financial control, human resources and business continuity.

Corporate governance is also supported by the ongoing reviews performed by the Internal Audit Department and the External Auditors. The reviews confirm that the policies and internal control procedures conform to practice and are being fully complied with by management and staff.

## Charitable Contributions

The Bank made contributions and donations to Bahraini charities in 2009 aggregating to US\$ 100,000 (2008: US\$ 300,000). The beneficiaries comprised local charity funds registered with the Ministry of Social Development and needy families who received coupons to purchase foodstuffs and basic electrical appliances.

## CHIEF EXECUTIVE OFFICER'S REVIEW OF OPERATIONS



A handwritten signature in black ink, appearing to read 'Aabed Al-Zeera', enclosed within a simple black oval outline.

**Aabed Al-Zeera**  
Chief Executive Officer

Since the inception of International Investment Bank (IIB), the Bank's strategy has been to structure and offer to clients a range of attractive investment opportunities in the manufacturing, financial, energy, and real estate sectors in various regions.

As stated by Mr. Chairman, 2009 was indeed a very challenging year for the investment banking sector due mainly to continuing weak investor appetite for new investment offerings and the non-availability of debt financing, which typically accounts for a significant portion of the capital structure of most investment offerings.

Comprising an operating loss of US\$ 2.6 million and unrealized impairment losses and provisions on four investments and one receivable of US\$ 25.3 million, IIB has reported a net loss of US\$ 27.9 million for 2009, the first since its inception in 2003. Notwithstanding such loss, the Bank's balance sheet continues to remain strong with good liquidity and the absence of borrowings and off balance sheet exposures. In addition, we are confident that we have adopted a prudent approach to impairment provisioning and believe, based on current global market conditions, that no significant future provisions will become necessary.

## Deal Flow

Supported by its network of strategic and financial partners, the Bank's Investment & Business Development Department carried out an initial review on many investment opportunities in private equity and real estate in the GCC region, North Africa and Europe from which few were selected for further in-depth analysis. The Department continues to develop a pipeline of investment opportunities that are currently at various stages of due diligence. IIB intends to provide to its investors a steady flow of top quality investments during 2010 and beyond.

## Deal Sell-Down

During the first quarter of 2009, the Bank completed the sale to investors of its remaining shares in IIB Sugar, representing a 14.3% equity stake in the sugar refinery. To be built in the Kingdom of Bahrain at an estimated cost of US\$157 million, IIB Sugar will be the first of its kind in the Kingdom and the third in the GCC. The refinery, which is expected to be operational in two years, will manufacture white sugar to be marketed in the Middle East and European markets.

## Asset Management

After an investment has been placed with investors, the Bank's Asset Management Department assumes responsibility for the management of the investment. With over US\$ 2.5 billion of total assets under supervision, the Department is responsible for oversight of each investment in order that the underlying assets are managed effectively during the holding period and exited profitably at the end of the planned investment time horizons.

In 2009, a difficult year on all counts, the department worked very closely with investment sponsors to ensure that the value of each investment is preserved. No exit was effected in 2009 but we expect at least one will be completed during 2010.

The Department also manages the Bank's proprietary investment portfolio. All prospective purchases and sales are evaluated by the Bank's Investment & Business Development Department in detail and a recommendation submitted via the Risk Management Committee to the Investment Committee and the Board Executive Committee, in accordance with the approval mandates.

## Core Banking System

I am pleased to report that the iMAL core banking system supplied by Path Solutions has been successfully implemented during 2009 on time and within budget. Under the close supervision of the Bank's Information Technology Steering Committee, the implementation has automated a number of key processes, including accounting, financial control and treasury. The iMAL represents a major commitment which will support IIB's long-term growth and development.

## Disaster Recovery Centre (DRC)

During the fourth quarter, IIB entered into a commitment to lease an office suite in the Kingdom Tower in Hoorā, Kingdom of Bahrain, located several kilometers from the Bank's head office in the Almoayyed Tower in Seef District. A fully functioning back-up office comprising furniture, computers and communication equipment, the DRC can accommodate key staff members who would require an immediate location in the event that the head office is unavailable for operations. A new server has also been installed in the DRC to back up the servers in the IT Department located in the head office, on a real-time basis.

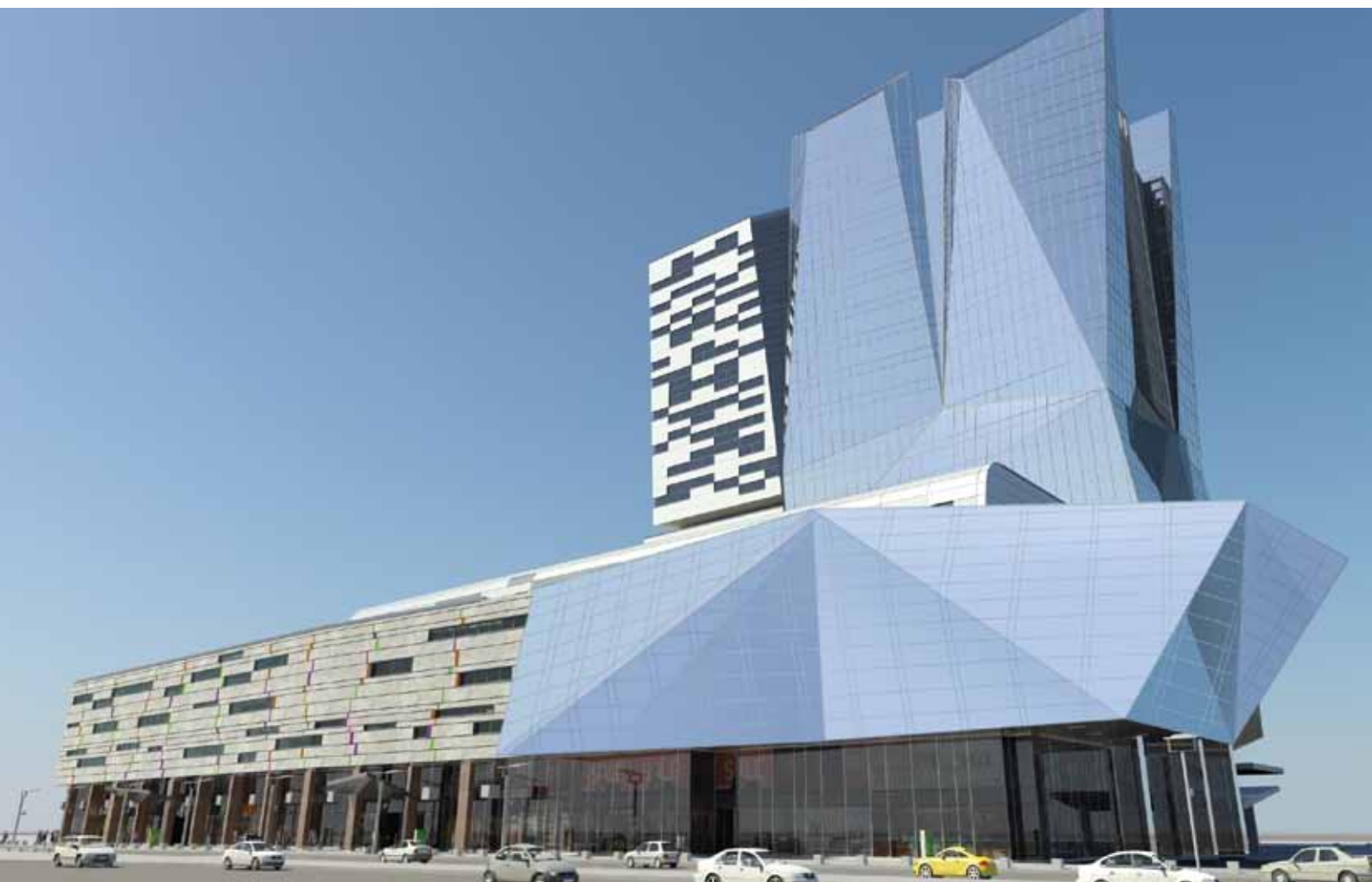
## Investor Relations

During 2008, enhancements were introduced through improvements to systems, procedures and processes supported by enhanced computer applications. The full benefit of these changes has been realized during 2009. Each investor has a designated Placement Executive who visits the investor on a regular basis and upon specific requests from time to time. The executive is supported by a coordinator based in Bahrain who acts as the liaison point between the investor and the executive.

## Corporate Events

I am pleased to state that for the second year, IIB has sponsored a stand at the World Islamic Banking Conference (WIBC) that was held in November 2009 at the Gulf Convention Centre, Kingdom of Bahrain. Launched in 1994, the WIBC is the world's largest and most influential gathering of Islamic finance leaders, attracting a large audience of bankers, consultants and investors in the region.

## PRINCIPAL TRANSACTIONS IN 2009



Sarajevo City Center (Artist Impression)

### Istethmary Sarajevo City Center - 1 Limited

IIB has invested, on behalf of its investors, in a project to construct a real estate complex comprising a hotel tower, commercial office tower, a shopping mall and entertainment center in Sarajevo, Bosnia and Herzegovina (Eastern Europe). The complex will be developed on a 10,585 square metre plot of land in Marijin Dvor, the most affluent area in central Sarajevo, opposite to the Parliament Building and the biggest office towers in Sarajevo that are owned by Kuwait Investment Authority and the Government of Bosnia and Herzegovina.

The Project offers investors the opportunity to invest in an untapped market. In Europe, there is a growing interest to invest in Eastern European countries as they are offering attractive yields and a competitive investment climate.

The Project shall be the first of its kind in the country, being of a similar design to the mega malls of the West and the Middle East. When completed, the Project shall cater to varied needs of consumers/visitors, aiming to achieve its objectives of providing world class hotel, office space, shopping and entertainment facilities encompassing a unique atmosphere.

To date, significant progress has been made on the Project execution side.

According to market experts and local real estate agents, property and land prices in Sarajevo have increased almost ten-fold since 1996. The unique topography of Sarajevo plays a role particularly in the increase of prices of land, as the availability of plots suitable for large scale real estate projects is extremely limited in the city center. Property and land prices are also expected to get a further boost from the prospect of Bosnia and Herzegovina joining the European Union ("EU"), similar to other Eastern European countries which have recently joined the EU.

The project is dependent on securing € 48.0 million of bank financing and discussions are in progress with several local banks.



Al Fareeda City (Artist Impression)

### Istethmary Al Fareeda Investments Limited

IIB has invested with its partners to complete the Al Fareeda City project comprising affordable housing units, commercial space and service amenities, over an area of circa 1.02 million square metres strategically located north of Jeddah in the Dhahban area in the Kingdom of Saudi Arabia (KSA). The Project is proposed to be completed over 36 months at an overall cost of about SAR 1.91 billion (US\$ 500 million) and will comprise 2,085 villas (categorized into five blocks of varying design sizes), 42,661 square metres of commercial area, service areas (including sports centre, green oasis, walkway, mosque, market area) and community support including police station, fire station, school and hospital.

Saudi Arabia is currently one of the strongest performing real estate markets in the MENA region. It is expected that Saudi Arabia shall be one of the first markets to recover from an improvement in the global market conditions.

Much of the current activity in the Saudi residential market has been targeted at the luxury end of the market and remains unaffordable to middle income households.

The key growth drivers for the KSA real estate and construction market include:

- Fastest population growth rate amongst the Arab countries.
- Around 60% population between the working age of 15-64 years.

- Strong real estate demand fundamentals increasing attractiveness for both domestic as well as foreign investors.
- Availability of low cost financing from KSA banks and financial institutions.
- Strong government focus on increased infrastructure spending.
- Estimated implementation of planned investments under public-private partnerships mostly in infrastructure could exceed US\$ 300 billion by the year 2012.
- Initiation of a new mortgage financing law that allows lenders to repossess the property should the borrower be in default on his commitments.

According to the Saudi Government estimates, about 200,000 housing units per year are required to cater to the growing demand for affordable housing in the country. A young, fast growing and rapidly urbanizing population has been instrumental in projecting that the Kingdom could face a shortfall of as many as 1 million dwellings by 2014. KSA being one of the largest construction markets in the Middle East is estimated to have total real estate investments of around US\$ 300 billion, which is expected to cross the US\$ 400 billion mark in 2010.

Subject to obtaining final regulatory approval, the Bank intends to sell down both investments to its investors during the first half of 2010.

## Overview

During 2009, the Bank has recorded a net loss of US\$ 27.9 million, compared to net income of US\$ 13.5 million during 2008, being the first annual loss in IIB's 6-year history. Total assets at year-end 2009 aggregate to US\$ 179.5 million and include cash and cash equivalents of US\$ 57.7 million.

Total equity at 31 December 2009 is US\$ 176.5 million.

Assets under management have increased during the year to US\$ 422.8 million at the end of 2009.

The Capital Adequacy Ratio at 31 December 2009 is 59% versus the minimum required by the Central Bank of Bahrain of 12%. The significantly higher level of Capital Adequacy is consistent with the strategy of prudence during the current and forecast uncertain and subdued economic conditions.

## Income

The Bank's total income for 2009 is US\$ 6.3 million compared with US\$ 35.0 million in 2008 and mainly comprises investment banking fees together with income on due from financial institutions.

Investment banking fees of US\$ 2.1 million are generated from the structuring, underwriting and placement of new investments, despite the difficult market conditions and from management fees earned on prior year transactions. In 2008, IIB concluded the sell down of two investment offerings that were carried over from 2007, fully sold down one transaction that was structured during the year and partly sold down another transaction.

In 2009, the Bank completed the sale to investors of the remaining available shares in the deal carried over from 2008, being a stake in a green-field sugar plant to be constructed in the Kingdom of Bahrain.

Income on due from financial institutions, being the profit on commodity murabaha deposits, is US\$ 2.6 million versus US\$ 5.3 million in 2008. The reduction reflects the higher average funds placed at a higher average profit rate during 2008, partly offset by higher profit earned in 2009 on facilities granted to several of IIB's investee companies.

The gain on sale of investments in 2009 of US\$ 0.2 million relates to the sale of a short-term shareholding in a GCC-listed company. Dividend income in 2009 of US\$ 0.7 million has been received from both IIB's investee companies and regionally listed equities. Other income of US\$ 0.7 million comprises the profit on a short-term financing provided to a non-related third party. There were no unrealised fair value gains on GCC-listed shares held for trading during the year, compared with gains of US\$ 5.5 million in 2008.

The Bank has booked its share of a loss in one UAE-based associate company engaged in real estate investments of US\$ 0.1 million (2008: loss US\$ 4.1 million).

## Expenses

Total expenses in 2009 aggregate to US\$ 8.9 million, a decrease of US\$ 7.7 million (46%) compared to 2008. Staff compensation and benefits decreased by 48% to US\$ 5.0 million as a result of a smaller average number of employees and lower transaction-based benefits. Deal expenses including travel, legal fees and professional fees have also decreased significantly in 2009, as detailed due diligence costs were incurred on a smaller number of potential investment transactions. Non-deal related expenses, in particular business travel, professional fees and media/advertising costs are substantially lower in 2009 in line with the reduced business activity, but partly offset by higher IT costs relating to the core banking system that went-live during 2009.

## Impairment losses and provisions

IIB has booked unrealised impairment losses in 2009 of US\$ 21.4 million (2008: US\$ 0.7 million) in respect of two quoted investments and one unquoted investment, including US\$ 20.0 million that relates to one listed investment on a GCC exchange. The Bank has also raised general provisions of US\$ 3.8 million (2008: nil) against an unlisted investment located in the GCC and a receivable located in Europe, as a measure of prudence against possible future losses.

## Assets

Cash and cash equivalents at year-end 2009 are US\$ 57.7 million and represent 32% of total assets. These comprise cash, balances with banks and due from financial institutions comprising commodity murabaha placements with financially sound banks rated A- or higher and located in the GCC region. With the addition of investments in quoted equities, liquid assets aggregate to US\$ 73.5 million or 41% of total assets.

Receivables at 31 December 2009 of US\$ 51.1 million mainly comprise three items. Short-term Shari'ah-compliant financing facilities of US\$ 8.1 million (net of general provisions) have been granted to two investee companies to assist with working capital requirements. Secondly, the Bank paid a deposit in 2008 to participate in a real estate project located in the Kingdom of Saudi Arabia. The project has subsequently been aborted and IIB has agreed to receive repayment of the remaining balance of US\$ 11.8 million over a period of 18 months. Finally, IIB has purchased for US\$ 27.7 million in 2009 a share in a real estate development project on behalf of its investors in the Kingdom of Saudi Arabia that is intended to provide affordable housing to Saudi nationals.

Investments have decreased in 2009 by a net US\$ 19.6 million to US\$ 37.4 million. IIB purchased shares valued at US\$ 1.7 million at 31 December 2009 in a listed company in the GCC and sold most of its remaining shares in one IIB investee company valued at US\$ 0.6 million. The remainder of the reduction is due to net unrealised fair value and impairment write-downs.

Assets classified as held for sale comprise a payment in 2009 of US\$ 26.9 million to secure a stake on behalf of its investors in a real estate development in Sarajevo, Bosnia and Herzegovina. Subject to obtaining the final regulatory approvals, IIB intends to sell down most of this investment to its investors. Investment in associate at the end of 2009 represents a 27.32% shareholding of US\$ 4.0 million in a company established in the UAE to purchase land for investment purposes. Due to market conditions, there is no longer an intention to develop the plot of land located in the Business Bay district of Dubai, which is now in the process of being sold.

Other assets of US\$ 0.4 million mainly comprise prepaid expenses, advance payments for equipment and sundry receivables. Equipment has increased in 2009 to US\$ 2.0 million mainly as a result of capitalizing the cost of the core banking system that was implemented during the year.

Reflecting the unfavorable market conditions, assets under management have increased by a modest 2.1% to US\$ 422.8 million.

## Liabilities and Equity

There are no borrowings on the balance sheet at the year end and no reverse murabaha liabilities classified as due to financial institutions since January 2007. Other liabilities of US\$ 3.0 million mainly comprise accrued expenses, payables to investors and payables to suppliers.

Equity has reduced by US\$ 34.2 million to US\$ 176.5 million at the 2009 year end. The reduction is comprised of the net loss for the year of US\$ 27.9 million and the payment of the 7% dividend of net US\$ 7.5 million for 2008, offset by net fair value and foreign currency translation gains on investments of US\$ 1.2 million.

# CAPITAL STRUCTURE

## Capital Base

The Bank's capital base comprises of Tier 1 capital which includes nominal share capital, share premium, statutory reserve, retained earnings, current year net income, unrealised gross losses arising from fair valuing equity securities less the cost of treasury shares, plus Tier 2 capital which consists of part of the unrealised gains arising from fair valuing equities less the aggregate amounts that exceed the regulatory large exposures limit.

The issued and paid up share capital of the Bank was US\$ 109,995,797 at 31 December 2008 and 2009, comprising of 109,995,797 shares of US\$ 1 each.

The Bank's regulatory capital base of US\$ 173.9 million as at 31 December 2009 comprises Tier 1 capital of US\$ 174.3 million and Tier 2 capital of –US\$ 0.4 million as disclosed in note 21 of the financial statements.

## Capital Adequacy

The purpose of capital management is to ensure the efficient utilization of capital in relation to business requirements and growth, risk profile and shareholders' returns. But the primary concern is capital protection from loss.

The Bank manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of its activities. In order to maintain or adjust the capital structure, the Bank may issue ordinary shares, buy back ordinary shares or adjust the amount of dividend payment to shareholders. No changes have been made in the objectives, policies and processes from the previous years.

As compared to the minimum Capital Adequacy Ratio ("CAR") of 12% prescribed by Central Bank of Bahrain (CBB), the Bank's ratio at year-end 2009 is 59%, being almost five times the minimum ratio of 12%. Last year, the CAR ratio of the Bank using Basel II requirements was 87% as against the minimum required ratio of 12%.

The ratio is derived from guidelines issued by CBB which are compatible with the "Basel II" Accord issued by the Basel Committee on Banking Supervision. The CAR measures total qualifying capital held by an institution in relation to its risk-weighted assets. In common with other banks incorporated in Bahrain, IIB commenced the ongoing measurement of its capital adequacy under the "Basel II" rules from 1 January 2008. Please refer to note 21 Capital Management in the attached financial statements.

Given the Capital Adequacy Ratio of the Bank as at 31 December 2009, it has ample capacity to record additional investments and still meet the minimum capital adequacy requirement of 12%. However, it plans to continue its conservative approach to liquidity and only modest investment purchases are planned for 2010.

## Profile of Risk-weighted Assets and Capital Charge

The Bank has adopted the "Standardized" approach for credit risk and market risk and "Basic Indicator" approach for operational risk for regulatory reporting purposes. IIB's risk-weighted capital requirements for credit, market and operational risks as at 31 December 2009 are as follows:

### a) Credit Risk

The descriptions of the counterparty classes along with the risk weights to be used to derive the risk weighted assets are:

#### Cash and Balances with banks and Due from financial institutions

Cash has a nil risk weighting. Claims on banks are risk weighted based on the ratings assigned to them by external rating agencies but short term claims on locally incorporated banks (whether rated or unrated) are assigned a risk weighting of 20% where such claims have an original maturity of three months or less and are denominated and funded in either Bahraini Dinars or US Dollars. Claims on banks outside Bahrain with a credit rating of A+ to A- are assigned a 50% risk weighting.

Credit exposures and risk weighted assets are disclosed as follows:

US\$ '000	Gross credit exposure	Risk weighted assets	Capital requirement
Claims on banks –			
Murabahas	57,674	26,255	3,151

#### Receivables

Receivables have a risk weighting of 100%. These include funding provided to two unrated entities on a corporate murabaha basis that is repayable within 12 months. The following are the gross credit exposures and risk weights assigned for capital adequacy purposes:

US\$ '000	Gross credit exposure	Risk weighted assets	Capital requirement
Due from investee companies –			
Murabahas	8,346	8,346	1,002

## Investments

Investments listed on a recognised stock exchange attract a risk weighting of 100%. Unlisted investments have a 150% risk weighting and holdings of real estate are assigned a risk weighting of 200%. Credit exposure and risk weighted assets considered for Capital Adequacy Ratio calculations comprising of banking book exposures are disclosed as follows:

US\$ '000	Gross credit exposure	Risk weighted assets	Capital requirement
Investment in listed equities	16,798	16,798	2,016
Investment in un-listed equities	50,267	98,547	11,826
<b>Total</b>	<b>67,065</b>	<b>115,345</b>	<b>13,842</b>

The gross credit exposure is all funded exposure and is entirely funded by capital. The Bank holds no cash collateral or eligible guarantees to mitigate credit risk. Since the year end position is representative of the risk positions of the Bank during the period, average gross exposures are not disclosed separately.

The realised gains net of losses arising from investment sales or liquidations during 2009 were US\$ 0.2 million (2008: US\$ 0.7 million). The total net unrealised gains recognised in equity for 2009 aggregated to US\$ 1.2 million (2008: loss US\$ 2.5 million).

## b) Market Risk

The Bank's capital charge in respect of market risk in accordance with the Standardized approach is as follows:

US\$ '000	Risk weighted assets	Year end capital requirement
Foreign exchange risk	43,638	5,237
<b>Total market risk</b>	<b>43,638</b>	<b>5,237</b>

IIB has no exposure to profit rate risk, equity position risk or options risk, as Bank does not maintain any trading book. However, equity price and profit rate risk has been disclosed in note 20.4 of the financial statements in accordance with International Financial Reporting Standard (IFRS) 7.

## c) Operational Risk

In accordance with the Basic Indicator approach methodology, the capital charge is computed by multiplying the latest three-year average gross income by a pre-defined beta factor as follows:

US\$ '000	Risk weighted assets	Capital requirement
Based on 2006-8 average gross income	55,596	6,671
<b>Total operational risk</b>	<b>55,596</b>	<b>6,671</b>

## Capital Management

The Bank aims to maintain sufficient capital to enable it to pursue strategies that build long-term shareholder value, whilst always exceeding minimum regulatory ratio requirements. In addition, it maintains capital as a buffer for unexpected losses and seeks to maximize the annual return on capital.

To assist it to implement an effective capital management framework, the Bank has implemented an internal capital adequacy assessment process (ICAAP). The purpose of the ICAAP framework is to document the ongoing assessment of the Bank's overall capital adequacy in relation to its risk profile and its capital management strategy. The ICAAP outlines the Bank's risk strategy, capital objectives, methodology and assumptions used to measure internal capital.

# RISK MANAGEMENT

The Board of Directors is charged with the overall responsibility for risk management. It approves and periodically reviews the risk policies and strategy of the Bank. It is assisted by the Executive Committee, Management Committee, Investment Committee and Audit Committee.

The Risk Management Committee has the overall responsibility for establishing the risk framework and strategy, principles, policies and limits. It is responsible for the fundamental risk issues and manages and monitors relevant risk decisions. The Risk Management Department is responsible for implementing the appropriate risk management strategy and methodology for the Bank. It ensures that risks do not exceed the approved limits. The Risk Management Department also carries out internal capital adequacy assessments to determine the adequacy of overall capital in relation to the Bank's risk profile and formulates the strategy for maintaining the capital levels. The capital provides the Bank with a cushion to absorb losses without endangering client funds.

The various risks to which the Bank is exposed and the principal risk management techniques are summarized below. Further information on risk management is contained in Note 20 to the Financial Statements.

## 1. Credit Risk

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. The principle business of the Bank is Investment Banking. The process of managing the credit risk starts at the origination of the investment activity and compliance with investment criteria, guidelines and policies. The Bank manages credit risk by setting limits for individual counterparties, countries, regions and industry sectors. Limits are authorized by the Board of Directors based on management's recommendations, monitored by the Risk Management Department and reviewed regularly by the Risk Management Committee. Details of maximum exposure to credit risk by balance sheet components, geographical region, industry sector and credit rating are contained in Note 20.2 to the Financial Statements in accordance with the requirements of International Financial Reporting Standard (IFRS) 7.

Information disclosed in the annual report in respect of geographical region, industry sector and credit rating is prepared in accordance with the requirement of Prudential Information Report for Islamic Banks as at 31 December 2009. We believe the disclosures to be reasonably representative of the position during 2009 as there has been no significant fluctuation in the level of credit risk assets.

### Credit risk concentrations and thresholds

Protection against excessive credit risk is through country, industry and counterparty threshold limits. Single name concentrations are monitored on an individual basis. Under the CBB's single obligor regulations, banks incorporated in Bahrain are required to obtain the CBB's approval for any planned exposure to a single counterparty exceeding 15% of the capital base.

As at 31 December 2009, the Bank's exposure in excess of 15% of the obligor limit to an individual counterparty is shown below:

US\$ '000	C.A.R Limit (15%)	On balance sheet exposure	Off balance sheet exposure	Total exposure	Deducted amount
Counterparty A	26,367	26,880	-	26,880	(513)
Counterparty B	26,367	27,737	-	27,737	(1,370)

### Excessive risk concentration

Bank policies and procedures include specific guidelines to focus on country and counterparty limits and maintaining a diversified portfolio.

### Geographical distribution of exposures

The geographical distribution of exposures, impaired assets and the related impairment provisions are analyzed as follows:

US\$ '000	Gross funded credit exposure	Impaired securities	Provision against securities
Bahrain	30,424	-	-
Europe	43,498	1,368	2,000
Other Gulf Cooperation Council (GCC) countries	103,033	20,034	1,772
Africa	1,753	-	-
Asia	768	-	-
<b>Total</b>	<b>179,476</b>	<b>21,402</b>	<b>3,772</b>

The impaired security is reflected at fair value based on the relevant closing stock market price as at 31 December 2009. The criteria used to allocate exposures to particular geographical areas is the country to which the funds were transferred.

### Industrial sector analysis of the exposures

The industrial sector analysis of exposures, impaired assets and the related impairment provisions is as follows:

US\$ '000	Gross funded credit exposure	Impaired securities	Provision against securities
Real estate – development	63,201	-	1,772
Real estate – income generating	11,933	-	-
Banking and financial institutions	59,494	317	-
Insurance	820	1,051	-
Manufacturing	16,483	20,034	-
Automotive	1,754	-	-
Others	25,791	-	2,000
<b>Total</b>	<b>179,476</b>	<b>21,402</b>	<b>3,772</b>

The Bank has no unfunded exposures as at 31 December 2009.

## Large exposures

The Bank follows the CBB's guidelines with respect to definition and measurement of large exposures at the consolidated level as stipulated in the CBB Rulebook for Islamic Banks.

The following are the large exposures of US\$ 1,000,000 and over as of 31 December 2009:

	Large exposure (banks) US\$ '000	% of exposure to equity		Large exposure (non-banks) US\$ '000	% of exposure to equity
Bank A	49,066	27.8%	Counterparty A	27,737	15.7%
Bank B	6,041	3.4%	Counterparty B	26,880	15.2%
Bank C	1,339	0.8%	Counterparty C	12,732	7.2%
			Counterparty D	11,775	6.7%
			Counterparty E	8,196	4.6%
			Counterparty F	4,648	2.6%
			Counterparty G	3,987	2.3%
			Counterparty H	3,528	2.0%
			Counterparty I	3,045	1.7%
			Counterparty J	2,960	1.7%
			Counterparty K	1,987	1.1%
			Counterparty L	1,740	1.0%
			Counterparty M	1,393	0.8%
			Counterparty N	1,343	0.8%
			Counterparty O	1,324	0.8%
			Counterparty P	1,123	0.6%

## Maturity analysis of funded exposures

Residual contractual maturity of the Bank's major types of funded credit exposures based on expected maturities is as follows:

US\$ '000	Within 1 month	1-3 months	3-6 months	6-12 months	Total within 12 months	1-5 years	Total over 12 months	Total
Cash	2	-	-	-	2	-	-	2
Claims on banks	57,674	-	-	-	57,674	-	-	57,674
Investment in quoted equities	-	-	-	-	-	15,831	15,831	15,831
Investment in unquoted equities	-	-	-	-	-	21,582	21,582	21,582
Assets classified as held for sale	-	-	26,880	-	26,880	-	-	26,880
Investment in associate	-	-	-	3,987	3,987	-	-	3,987
Receivables	5,216	4,308	4,125	6,555	20,204	30,920	30,920	51,124
Other assets & equipment	207	131	51	34	423	1,973	1,973	2,396
	<b>63,099</b>	<b>4,439</b>	<b>31,056</b>	<b>10,576</b>	<b>109,170</b>	<b>70,306</b>	<b>70,306</b>	<b>179,476</b>

## Exposure by external credit rating

The Bank uses ratings issued by Standard & Poor's, Moody's, Capital Intelligence and Fitch to derive the risk weightings under the CBB's Basel 2 capital adequacy framework. Where ratings vary between rating agencies, the highest rating from the lowest two ratings is used to represent the rating for regulatory capital adequacy purposes. The following are gross credit risk exposures considered for Capital Adequacy Ratio calculations comprising of banking book exposures.

US\$ '000	Gross credit exposure	Rated exposure	Unrated exposure
Cash and claims on banks	57,676	56,970	706
Equity portfolio	68,280	-	68,280
Other exposures	53,520	-	53,520
<b>Total</b>	<b>179,476</b>	<b>56,970</b>	<b>122,506</b>

## Intra-group transactions including exposures to related parties

Related parties represent associated companies, major shareholders, directors and key management personnel of the Bank and entities controlled, jointly controlled or significantly influenced by such parties. Pricing policies and terms of these transactions are on an arm's length basis and are identical to those applicable to transactions with all other parties.

## Exposures to related parties

US\$ '000	Gross credit exposure
Claims on shareholders	6,052
Claims on associates	3,987
Claims on investee companies	2,716
Claims on directors	-
<b>Total</b>	<b>12,755</b>

## Liabilities to related parties

US\$ '000	Gross liability
Deposits payable to shareholders	2,489
<b>Total</b>	<b>2,489</b>

## Impairment of assets

An assessment is made at each balance sheet date to determine whether there is objective evidence that a specific financial asset or group of financial assets may be impaired. If such evidence exists, an impairment loss is recognised in the statement of income. Evidence of impairment may include indications that the investee company is experiencing significant financial difficulty, default or delinquency in profit or principal payments, the probability that it will enter bankruptcy or other financial

# RISK MANAGEMENT

re-organisation and that there is a measurable decrease in the estimated future cash flows such as changes in arrears or economic conditions that correlate with defaults.

## Impairment is determined as follows:

- a) for assets carried at amortized cost, impairment is based on the present value of estimated future cash flows discounted at the original effective profit rate;
- b) for assets carried at fair value, impairment is the difference between cost and fair value; and
- c) for assets carried at cost, impairment is based on the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset.

## Impairment losses on financial assets

On a quarterly basis, the Bank assesses whether any provision for impairment should be recorded in the statement of income. Considerable judgement by management is required in the estimation of the amount and timing of future cash flows when determining the level of provision required. Such estimates are necessarily based on assumptions about several factors involving varying degrees of judgement and uncertainty and actual results may differ resulting in future changes in such provisions.

## 2. Liquidity Risk

Liquidity risk is the risk that the Bank will be unable to meet its payment obligations when they fall due under both normal and stress circumstances. The Assets & Liabilities Committee (ALCO) monitors future cash flows and liquidity required for working capital and investment acquisition. The Bank's investments generally have a long-term maturity and hence, as a matter of policy, the long-term investments are funded from IIB's own capital. The Bank maintains significant cash and cash equivalent balances and also has access to geographically diversified funding sources, although no deposit liabilities or long-term funding by external counterparties were booked during 2009. The ratio of liquid assets (defined as cash, balances with banks, due from financial institutions and quoted investments) to total assets at 31 December 2009 is 41%. Details of liquidity risk and funding management are contained in Note 20.3 to the Financial Statements.

The Bank groups all assets and liabilities into specific maturity time buckets and monitors the mismatches between the inflows and outflows against approved limits. The maturity analysis of assets and liabilities based on expected recovery or settlement dates is contained in Note 19 to the Financial Statements.

## 3. Market Risk

Market risk is the risk to earnings resulting from adverse movements in foreign currency rates, profit rate yield curves and equity prices. The Bank has no significant concentration of market risk and does not have a trading portfolio of equities or foreign currencies. It is exposed to market risk from currency rate fluctuations on its foreign currency denominated assets and liabilities.

To enable effective monitoring and managing of exposures, all market risks associated with the Bank's investments are managed and monitored using basic sensitivity analyses reflecting such factors as volatility, liquidity and concentration. The investments in unquoted equities, comprising the Bank's retentions in its investment offerings and selective participations in private placements, are generally illiquid without a ready market to effect an exit.

Note 20.4 to the Financial Statements details the Bank's exposure to equity price risk, foreign currency risk and profit rate risk.

## 4. Operational Risk

Operational Risk is the risk of direct or indirect loss resulting from breaches in internal controls, processing errors, inadequate information systems, fraud, or external events. Its impact can be in the form of a financial loss, loss of reputation or loss of competitive position. Operational risk is inherent in all business activities and can never be eliminated entirely but can only be mitigated or minimized. The Bank minimizes its exposure to such risk by ensuring that appropriate management control mechanisms, infrastructure, systems, internal controls and human resources are in place. IIB has developed an operational risk framework, reviewed by experienced external consultants, that provides for identification, measurement, monitoring and control of potential risk events. A number of processes are used throughout the Bank including risk and control self-assessments, key risk indicators (KRIs), event management, new product review / approval procedures and business continuity plans.

In addition, Internal Audit Department issues regular reports including an annual organization-wide risk assessment and the external auditors make recommendations on internal controls and processes. Business units are responsible for managing the operational risks relevant to their activities, supported by a disaster recovery program covering computer backup, data recovery and business continuity.

Head of Risk Management maintains a risk register for capturing loss event data and events. On a quarterly basis matters logged are discussed with the departmental heads. During the current year no significant loss events occurred.

## 5. Legal Risk

Legal Risk is the risk arising from the potential that unenforceable contracts, lawsuits, or adverse judgements can disrupt or otherwise adversely affect the operations of the Bank. It has professional service arrangements with well-established local and international law firms. The policies and procedures of the Bank ensure that investments are made, funds are transferred, contracts are entered into, legal agreements are signed and any other binding arrangement is executed only after a rigorous legal due diligence has been performed either by the Legal & Compliance Department or external legal counsel. IIB fully complied with all applicable laws and regulations during the year ended 31 December 2009 and accordingly was not subject to any penalties for non-compliance.

## **Chief Executive Officer**

**Abed Al- Zeera**, Chief Executive Officer (CEO)  
**Anne Uson**, Executive Secretary

## **Investment & Business Development**

**Mohamed Hadi Mejai**, Executive Director  
**Hakan Gunay**, Director  
**Fadi Al-Qassim**, Project Manager  
**Suad Emad Almoayyed**, Associate  
**Mohammed Maher Mannai**, Associate  
**Atif Naveed**, Associate  
**Marieta Cano**, Executive Secretary

## **Investment Placement**

**Alyas Al-Meftah**, Director  
**Daaij Al-Khalifa**, Principal  
**Fawzan Al-Naser**, Principal  
**Jassim Al-Shaikh**, Principal  
**Bashar Al-Shaikh**, Principal  
**Omar Shaheen**, Principal  
**Salah Hasan Habib**, Associate,  
**Mohammed Juma Habib**, Associate  
**Nawar Al-Alawi**, Coordinator  
**Mohammed Ebrahim Janahi**, Coordinator  
**Mona Mahmood Ghuloom**, Coordinator  
**Bushra A.Hassan Al-Madhi**, Coordinator

## **Asset Management**

**Subhash Jalan**, Executive Director  
**Murtaza Ghulam**, Principal  
**Mazar Jalal**, Principal  
**Fatima Al Aradi**, Investors Relations Officer  
**Sadaf Gill**, Analyst  
**Mahmood Al-Qassab**, Coordinator  
**Ruby Castro**, Executive Secretary

## **Finance and Administration**

**Michael Ross-McCall**, Chief Financial Officer (CFO)  
**Augustine Peter**, Principal  
**Haleema Ebrahim**, Associate - Treasury  
**Prerna Khandelwal**, Accountant  
**Ghizlane Rahali**, Associate - Corporate Communications & PR  
**Hussain Ali Jassim**, General Services Supervisor  
**Khulood Farhan**, Receptionist & General Secretary

## **Information Technology**

**Said Itani**, Head  
**Sayed Hussein Mahdi**, Associate  
**Hassan Abbas**, Officer

## **Risk Management**

**Ninan Varkey**, Head

## **Internal Audit**

**Ali Redha**, Director

## **Human Resources**

**Sawsan Al-Ansari**, Consultant

# SHARI'AH SUPERVISORY BOARD REPORT

To the Shareholders of International Investment Bank B.S.C. (c)

## **Asslam Alaikum Wa Rahmat Allah Wa Barakatuh**

In compliance with the terms of our letter of appointment, we are required to report as follows:

We have reviewed the principles and contracts relating to the transactions conducted by International Investment Bank B.S.C. (c) (the "Bank") during the course of the year ending December 31, 2009. Our review was conducted in order to judge whether the Bank followed the principles of the Islamic Shari'ah, specific fatwas, and guidelines issued by the Shari'ah Supervisory Board. The Bank's management is responsible for ensuring that its operations are carried out in compliance with our rulings. It is our responsibility to present an independent view of the Bank's operations and to communicate it to the shareholders.

Our review included a detailed analysis of each type of transaction with its relevant documentation and procedures adopted by the Bank.

The review was planned and performed so as to obtain all necessary information and explanations to provide sufficient evidence proving that the Bank has not violated any rules and principles of the Islamic Shari'ah.

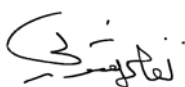
### **In our opinion:**

- The Bank's contracts, transactions and deals for the year ending December 31, 2009 are in compliance with the rules and principles of the Islamic Shari'ah.
- The Bank's allocation of profit and charging of losses relating to investment accounts are in compliance with the rules and principles of the Islamic Shari'ah.

- Earnings that have been realized from sources that are non-Shari'ah compliant were donated to charity.
- The Bank's calculation of Zakat is in compliance with the rules and principles of the Islamic Shari'ah.

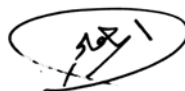
We beseech the Almighty to grant us excellence and success.

Wassalam Alaikum Wa Rahmat Allah Wa Barakatuh



**Sheikh Nizam Yaquby**

Chairman, Shari'ah Supervisory Board



**Sheikh Osama Bahar**

Member, Shari'ah Supervisory Board

8 Rabia 1431  
22 February 2010



# Financial Statements 2009

# INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS

## **Independent Auditors' Report to the Shareholders of International Investment Bank B.S.C. (c)**

We have audited the accompanying financial statements of International Investment Bank B.S.C. (c) ["the Bank"] which comprise the balance sheet as at 31 December 2009 and the statements of income, cash flows and changes in equity for the year then ended, and a summary of significant accounting policies and other explanatory notes.

### **Board of Directors' Responsibility for the Financial Statements**

The Board of Directors is responsible for the preparation and fair presentation of these financial statements in accordance with Financial Accounting Standards issued by the Accounting and Auditing Organisation for Islamic Financial Institutions ["AAOIFI"]. This responsibility includes: designing, implementing and maintaining internal controls relevant to the preparation and fair presentation of the 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. In addition, the Board of Directors is responsible for the Bank's undertaking to operate in accordance with Islamic Shari'a rules and principles.

### **Auditors' Responsibility**

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with both Auditing Standards for Islamic Financial Institutions issued by the AAOIFI and International Standards on Auditing. Those standards require that we comply with relevant ethical requirements and plan and perform the audit to obtain reasonable assurance as to 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 auditors' judgement, 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 controls relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate for the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal controls. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the Board of Directors, as well as evaluating the overall presentation of the financial statements.

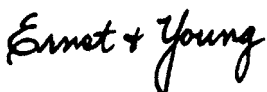
We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### **Opinion**

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Bank as of 31 December 2009 and its financial performance and its cash flows for the year then ended in accordance with Financial Accounting Standards issued by the AAOIFI and the Islamic Shari'a rules and principles as determined by the Shari'a Supervisory Board of the Bank.

### **Other Regulatory Matters**

We confirm that, in our opinion, proper accounting records have been kept by the Bank and the financial statements, and the contents of the report of the Board of Directors relating to these financial statements, are in agreement therewith. We further report, to the best of our knowledge and belief, that no violations of the Bahrain Commercial Companies Law, nor of the Central Bank of Bahrain and Financial Institutions Law, nor of the Memorandum and Articles of Association of the Bank have occurred during the year ended 31 December 2009 that might have had a material adverse effect on the business of the Bank or on its financial position, and that the Bank has complied with the terms of its banking license.



22 February 2010

Manama, Kingdom of Bahrain

# STATEMENT OF INCOME

For the year ended 31 December 2009

	Notes	2009 US\$'000	2008 US\$'000
<b>Income</b>			
Investment banking fees	3	2,120	22,725
Income on due from financial institutions	4	2,564	5,292
Unrealised loss on available for sale securities		-	(130)
Gain on sale of investments, net		198	729
Unrealised gain on financial assets fair valued through statement of income		-	145
Unrealised gain on financial assets held for trading		-	5,496
Dividend income		679	667
Other income		735	27
<b>TOTAL INCOME</b>		<b>6,296</b>	<b>34,951</b>
<b>Expenses</b>			
Corporate expenses		2,231	4,416
Deal acquisition expenses		1,959	4,778
Selling expenses		1,455	3,301
Asset management expenses		728	1,179
General and administration expenses	6	2,572	2,930
<b>TOTAL EXPENSES</b>		<b>8,945</b>	<b>16,604</b>
<b>OPERATING (LOSS) / INCOME</b>		<b>(2,649)</b>	<b>18,347</b>
Share of loss from associate	12	(77)	(4,096)
<b>NET (LOSS) / INCOME BEFORE IMPAIRMENT AND FOREIGN EXCHANGE LOSSES</b>		<b>(2,726)</b>	<b>14,251</b>
Impairment losses and provisions	9,10,12	(25,174)	(688)
Loss on foreign exchange		(3)	(45)
<b>NET (LOSS) / INCOME FOR THE YEAR</b>		<b>(27,903)</b>	<b>13,518</b>

The attached explanatory notes 1 to 25 form part of these financial statements

# BALANCE SHEET


At 31 December 2009

	Notes	2009 US\$'000	2008 US\$'000
<b>ASSETS</b>			
Cash and balances with banks	7	1,974	2,205
Due from financial institutions	8	55,702	118,268
Receivables	9	51,124	33,813
Investments	10	37,413	57,048
Assets classified as held for sale	11	26,880	-
Investment in associate	12	3,987	5,836
Other assets		423	595
Equipment		1,973	953
<b>TOTAL ASSETS</b>		<b>179,476</b>	<b>218,718</b>
<b>LIABILITIES AND EQUITY</b>			
Other liabilities	13	2,994	8,066
<b>TOTAL LIABILITIES</b>		<b>2,994</b>	<b>8,066</b>
<b>EQUITY</b>			
Share capital	14	109,996	109,996
Treasury shares	14	(6,798)	(6,798)
Share premium	14	72,050	72,050
Reserves	14	1,234	27,704
Proposed appropriations	15	-	7,700
<b>TOTAL EQUITY</b>		<b>176,482</b>	<b>210,652</b>
<b>TOTAL LIABILITIES AND EQUITY</b>		<b>179,476</b>	<b>218,718</b>

The financial statements were authorised for issue in accordance with a resolution of the Board of Directors on 22 February 2010.



**Saeed Abdul Jalil Al Fahim**  
Chairman



**Aabed Al Zeera**  
Chief Executive Officer

The attached explanatory notes 1 to 25 form part of these financial statements

# STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2009

	Reserves							Total reserves appropriations US\$ '000	Proposed appropriations US\$ '000	Total US\$ '000
	Share capital US\$ '000	Treasury shares US\$ '000	Share premium US\$ '000	Statutory reserve US\$ '000	Cumulative changes in fair value reserve US\$ '000	Foreign currency translation reserve US\$ '000	Accumulated deficit / retained earnings US\$ '000			
Balance at 1 January 2009	109,996	(6,798)	72,050	5,588	(2,320)	-	24,436	27,704	7,700	210,652
Income recognised directly in equity	-	-	-	-	367	856	-	1,223	-	1,223
Net loss for the year	-	-	-	-	-	-	(27,903)	(27,903)	-	(27,903)
Dividend paid	-	-	-	-	-	-	-	-	(7,490)	(7,490)
Transfer to retained earnings relating to treasury shares	-	-	-	-	-	-	210	210	(210)	-
Balance at 31 December 2009	109,996	(6,798)	72,050	5,588	(1,953)	856	(3,257)	1,234	-	176,482
Balance at 1 January 2008	109,996	(113)	71,867	4,236	67	-	20,115	24,418	10,226	216,394
Loss recognised directly in equity	-	-	-	-	(2,532)	-	-	(2,532)	-	(2,532)
Net income for the year	-	-	-	-	-	-	13,518	13,518	-	13,518
Transfer of fair value gain to reserve	-	-	-	-	145	-	(145)	-	-	-
Purchase of treasury shares at premium	-	(6,798)	-	-	-	-	-	-	-	(6,798)
Sale of treasury shares at premium	-	113	183	-	-	-	-	-	-	296
Dividend paid	-	-	-	-	-	-	-	-	-	-
Transfer to statutory reserve	-	-	-	1,352	-	-	(1,352)	-	(10,226)	(10,226)
Proposed appropriation (note 15)	-	-	-	-	-	-	(7,700)	(7,700)	7,700	-
Balance at 31 December 2008	109,996	(6,798)	72,050	5,588	(2,320)	-	24,436	27,704	7,700	210,652

The attached explanatory notes 1 to 25 form part of these financial statements

# STATEMENT OF CASH FLOWS

For The Year Ended 31 December 2009

	Notes	2009 US\$'000	2008 US\$'000
<b>OPERATING ACTIVITIES</b>			
Net (loss) / income for the year		(27,903)	13,518
Adjustments for:			
Depreciation	6	543	347
Unrealised gain on financial assets fair valued through statement of income		-	(145)
Unrealised gain on financial assets held for trading		-	(5,496)
Unrealised loss on available for sale securities		-	130
(Gain) on sale of investments, net		(198)	(729)
Share of loss from associate	12	77	4,096
Impairment losses and provisions	9,10,12	25,174	688
		(2,307)	12,409
Changes in operating assets and liabilities:			
Receivables		(19,311)	(29,845)
Other assets		172	226
Other liabilities		(5,072)	(32,607)
Purchase of investments		(35,416)	(45,901)
Proceeds from disposal of investments		8,190	18,652
Net cash used in operating activities		(53,744)	(77,066)
<b>INVESTING ACTIVITIES</b>			
Investment made in an associate		-	(311)
Purchase of equipment		(1,563)	(234)
Net cash used in investing activities		(1,563)	(545)
<b>FINANCING ACTIVITIES</b>			
Purchase of treasury shares	14	-	(6,798)
Proceeds from sale of treasury shares		-	296
Dividends paid		(7,490)	(10,478)
Net cash used in financing activities		(7,490)	(16,980)
<b>DECREASE IN CASH AND CASH EQUIVALENTS</b>		(62,797)	(94,591)
Cash and cash equivalents at beginning of the year		120,473	215,064
<b>CASH AND CASH EQUIVALENTS AT END OF THE YEAR</b>		57,676	120,473
Cash and cash equivalents comprise:			
Cash and balances with banks		1,974	2,205
Due from financial institutions		55,702	118,268
		57,676	120,473

The attached explanatory notes 1 to 25 form part of these financial statements

## 1. CORPORATE INFORMATION

International Investment Bank B.S.C. (c) ["the Bank"] operates under a Wholesale Islamic Banking License issued by the Central Bank of Bahrain ["the CBB"]. The core business activities of the Bank include investing on its own account and investment, underwriting and placement in real estate and private equity and corporate finance in conformity with Islamic Shari'a.

The Bank was incorporated on 6 October 2003, under commercial registration number 51867 as a Bahrain Joint Stock Company (closed). The Bank's registered office is at 37<sup>th</sup> floor Al Moayyed Tower, P.O. Box 11616, Manama, Kingdom of Bahrain.

## 2. ACCOUNTING POLICIES

### a) Basis of preparation

These financial statements have been prepared under the historical cost convention except as modified by the revaluation of investments carried at fair value through statement of income, held for trading and available for sale investment at fair value.

The financial statements are presented in United States Dollars ["US\$"] which is the Bank's functional currency.

### Statement of compliance

The financial statements of the Bank are prepared in accordance with Financial Accounting Standards issued by the Accounting and Auditing Organisation for Islamic Financial Institutions ["AAOIFI"], the Islamic Shari'a Rules and Principles as determined by the Shari'a Supervisory Board of the Bank, the Bahrain Commercial Companies Law and the Central Bank of Bahrain and Financial Institutions Law. For matters which are not covered by AAOIFI standards, the Bank uses the relevant International Financial Reporting Standards [the "IFRSs"].

During the current year the Bank has adopted to prepare financial statements in accordance with Financial Accounting Standards issued by AAOIFI only. Previously the Bank was applying both International Financial Reporting Standards and AAOIFI in preparing financial statements. Due to such a change in the adoption of accounting standards, investments previously carried at fair value through statement of income have been reclassified as "available for sale".

### b) Significant accounting judgments and estimates

In the process of applying the Bank's accounting policies, management has used its judgment and made estimates in determining the amounts recognised in the financial statements. The most significant judgments and estimates are as follows:

### Fair value

The determination of fair value is done for each investment individually in accordance with the valuation policies set out below:

- (i) For investments quoted in an active market, fair value is determined by reference to quoted market prices.
- (ii) For investments in units in funds, fair value is determined based on the latest net asset value provided by the fund manager.
- (iii) For unquoted investments, the Bank establishes fair value by using an appropriate valuation technique. Valuation techniques include using recent arm's length market transactions between knowledgeable willing parties, if available, and reference to recent valuation multiples of other comparable entities that are substantially the same.

### Classification of investments

Management decides on acquisition of an investment whether it should be classified as "held for trading" or "available for sale".

### Impairment of investments

The Bank treats available for sale investments as impaired when there has been a significant or prolonged decline in the fair value below its cost or where other objective evidence of impairment exists. The determination of what is "significant" or "prolonged" requires considerable judgment.

# NOTES TO THE FINANCIAL STATEMENTS

At 31 December 2009

## 2. ACCOUNTING POLICIES (continued)

### c) Summary of significant accounting policies

The principal accounting policies applied in the preparation of these financial statements are set out below:

#### i) Foreign currency translation

##### *Transactions and balances*

Transactions in foreign currencies are initially recorded in the functional currency at the rate of exchange prevailing at the date of the transaction.

Monetary assets and liabilities denominated in foreign currencies are translated into functional currency using rate of exchange prevailing at the balance sheet date. All differences are taken to 'Gain / (loss) on foreign exchange' in the statement of income.

Non-monetary items that are measured in terms of historical cost in foreign currency are translated using the exchange rates at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates prevailing at the date when the fair value was determined. Translation gains or losses on non-monetary items carried at fair value are included in equity as part of the fair value adjustment on investment available for sale.

#### ii) Financial instruments – initial recognition and subsequent measurement

Financial instruments comprise financial assets and financial liabilities.

Financial assets consist of cash and balances with banks, due from financial institutions, investments and other assets. Financial liabilities consist of other liabilities.

Incremental transaction costs associated with the acquisition of investments available for sale are included in the cost of such investments. Transaction cost incurred for investment held for trading is expensed out immediately.

##### *Initial recognition of financial instruments*

The classification of financial instruments at initial recognition depends on the purpose for which the financial instruments were acquired and their characteristics. All financial instruments are initially recognised at their cost being the fair value of the consideration given plus, in the case of financial assets and financial liabilities not held for trading, any directly attributable incremental costs of acquisition or issue.

##### *Due from financial institutions*

Due from financial institutions comprise of commodity murabaha receivables and are stated net of deferred profit and provision for impairment, if any.

Murabaha receivables are sales on deferred terms. The Bank arranges a murabaha transaction by buying a commodity (which represents the object of the murabaha) and then resells this commodity to the Murabeh (beneficiary) after computing a margin of profit over cost. The sale price (cost plus the profit margin) is repaid in installments by the Murabeh over the agreed period.

Mudaraba investments are partnerships where the Bank ("Rabb-ul-Maal") gives money to another ("Mudarib") for investing in a commercial enterprise for a definite period of time.

##### *Investments*

Investments are initially classified as "held for trading", "available for sale" or "held for sale".

After initial recognition, investments are remeasured to fair value as below:

##### *Held for trading*

Realised gains and losses, dividends and unrealised gains and losses arising from the re-measurement to fair value, are included in the statement of income.

##### *Available for sale*

Fair value changes are reported as a separate component of equity until the investment is derecognised, or the investment is determined to be impaired, at which time the cumulative change is included in the statement of income for the period. The losses arising from impairment of such investments are recognised in the statement of income and are excluded from the

statement of changes in equity. Investments whose fair value cannot be reliably measured are carried at cost less impairment losses, if any.

#### *Held for sale*

Assets are classified as held for sale if the carrying amount is to be recovered principally through a sale transaction planned to occur within 12 months, rather than through continuing use. Assets held for sale are measured at the lower of carrying amount or fair value less costs to sell.

#### iii) Derecognition of financial assets and financial liabilities

##### *Financial assets*

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is derecognised where:

- the right to receive cash flows from the asset has expired; or
- the Bank retains the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a "pass-through" arrangement; or
- the Bank has transferred its right to receive cash flows from the asset and either: (a) has transferred substantially all the risks and rewards of the assets, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

##### *Financial liabilities*

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

#### iv) Impairment of financial assets

An assessment is made at each balance sheet date to determine whether there is objective evidence that a specific financial asset or a group of financial assets may be impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that have occurred after the initial recognition of the asset. If such evidence exists, any impairment loss is recognised in statement of income.

#### *Investments*

In the case of equity investments classified as available for sale, objective evidence would include a significant or prolonged decline in the fair value of the investment below its cost. Where there is evidence of impairment, the cumulative loss (measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognised in the statement of income) is removed from equity and recognised in the statement of income. Impairment losses on equity investments are not reversed through the statement of income, increases in their fair value after impairment are recognised directly in equity.

#### v) Offsetting of financial instruments

Financial assets and financial liabilities are only offset and the net amounts reported in the balance sheet when there is a legally enforceable or religious right to set off the recognised amounts and the Bank intends to either settle these on a net basis, or intends to realise the asset and settle the liability simultaneously.

#### vi) Investment in associates

The Bank's investments in associates are accounted for using the equity method of accounting. An associate is an entity in which the Bank has significant influence and which is neither a subsidiary nor a joint venture represented by an interest between 20% and 50% in the voting capital.

Under the equity method, the investment in an associate is initially recognised at cost and adjusted thereafter for the post-acquisition changes in the Bank's share of net assets of the associate. The Bank recognises in the statement of income its share of the total recognised profit or loss of the associate from the date that influence or ownership effectively commences until the date that it effectively ceases. Distributions received from an associate reduce the carrying amount of the investment. Adjustments to the carrying amount may also be necessary for changes in the Bank's share in the associate arising from changes in its equity that have not been recognised in the associate's profit or loss. The Bank's share of those changes is recognised directly in equity. Profits and losses resulting from transactions with an associate are eliminated to the extent of the Bank's share in the associate.

The reporting dates of the associates and the Bank are identical and the associates' accounting policies conform to those used by the Bank for like transactions and events in similar circumstances.

# NOTES TO THE FINANCIAL STATEMENTS

At 31 December 2009

## 2. ACCOUNTING POLICIES (continued)

### c) Summary of significant accounting policies (continued)

#### vii) Equipment

All items of equipment are recorded at cost, less accumulated depreciation. Depreciation is provided on a straight line basis over the estimated useful lives of the equipment.

#### viii) Investment banking fees

Investment banking fees represent acquisition, structuring, placement, management and brokerage fees. The Bank earns acquisition, structuring, placement and brokerage fees during the acquisition and placement process for rendering services including: structuring of transactions, acquiring and leasing properties, placing with investors and arranging financing. These fees are recognised when earned, generally on receipt of cash and signed share purchase agreements by the Bank.

Management fees represent a recurring fee earned by the Bank for rendering management and administrative services. Management fees are recognised as and when services are rendered.

#### ix) Exit income

Exit income comprises performance fees representing the fee earned by the Bank for exceeding pre-determined hurdle rates. Exit income is recognised when a binding and definitive sale agreement or contract is signed.

#### x) Income on due from financial institutions

Income on due from financial institutions represents income from murabaha receivables. Murabaha income is recognised on a time apportioned basis over the period of the contract based on the principal amounts outstanding. Income that is over due by 90 days or more is excluded from the income of the year.

Murabaha income is recognised when it is quantifiable or when right to receive payment is established, whereas the losses are charged to income when advised by the Mudarib.

#### xi) Dividends

Dividends are recognised when the right to receive payment is established.

#### xii) Employees' end of service benefits

Provision is made for leaving indemnity payable under the Bahraini Labour Law applicable to non-Bahraini employees based upon accumulated periods of service at the balance sheet date.

Bahraini employees of the Bank are covered by contributions made to the General Organisation of Social Insurance Scheme (GOSI) as a percentage of the employees' salaries. The Bank's obligations are limited to these contributions, which are expensed when due.

#### xiii) Zakah

In accordance with its Articles of Association, the Bank is not required to pay Zakah on behalf of its shareholders.

#### xiv) Cash and cash equivalents

Cash and cash equivalents comprise cash and balances with banks and due from financial institutions with original maturities of three months or less.

#### xv) Fiduciary assets

Assets held in a fiduciary capacity are not reported in the balance sheet, as they are not the assets of the Bank.

#### xvi) Proposed dividend

Proposed dividends are included as part of equity and only recognised as liabilities when approved by the shareholders.

#### xvii) Provisions

Provisions are recognised when the Bank has a present obligation (legal or constructive) arising from a past event and the costs to settle the obligation are both probable and able to be reliably measured.

#### xviii) Treasury shares

Own equity instruments which are acquired (treasury shares) are deducted from equity. No gain or loss is recognised in the statement of income on the purchase and sale of the Bank's own equity instruments. No dividends are paid on treasury shares.

# NOTES TO THE FINANCIAL STATEMENTS

At 31 December 2009

## 3. INVESTMENT BANKING FEES

	2009 US\$'000	2008 US\$'000
Acquisition, structuring and placement fees	1,406	21,789
Management fees	714	936
	2,120	22,725

## 4. INCOME ON DUE FROM FINANCIAL INSTITUTIONS

	2009 US\$'000	2008 US\$'000
Profit on commodity murabaha	2,555	4,952
Income from murabaha receivables from investee companies	9	340
	2,564	5,292

## 5. STAFF COSTS

	2009 US\$'000	2008 US\$'000
Salaries and other staff related costs	4,578	9,307
End of service benefits	435	313
	5,013	9,620

The Bank classifies its expenses based on function and hence the staff cost has been allocated to Corporate, Deal acquisition, Selling and Asset Management functions.

## 6. GENERAL AND ADMINISTRATION EXPENSES

	2009 US\$'000	2008 US\$'000
Depreciation	543	347
Rent and maintenance	446	497
Legal and professional	349	514
Directors' remuneration	300	500
Printing and advertisement	235	273
Donations	100	300
Shari'a committee	75	119
Communication	60	106
Others	464	274
	2,572	2,930

## 7. CASH AND BALANCES WITH BANKS

	2009 US\$'000	2008 US\$'000
Cash on hand	2	2
Balances with banks	1,972	2,203
	1,974	2,205

# NOTES TO THE FINANCIAL STATEMENTS

At 31 December 2009

## 8. DUE FROM FINANCIAL INSTITUTIONS

	2009 US\$'000	2008 US\$'000
Commodity murabaha	55,713	118,394
Deferred income	(11)	(126)
	55,702	118,268

## 9. RECEIVABLES

	Notes	2009 US\$'000	2008 US\$'000
Advance paid for a deal	9.1	27,736	-
Receivables and prepayments	9.2	15,041	25,679
Due from investee companies	9.3	8,347	8,134
		51,124	33,813

### 9.1 Advance paid for a deal

The Bank has made an advance payment towards a future real estate related project in the Kingdom of Saudi Arabia. The legal formalities including preparation of the private placement memorandum and regulatory approvals of this project are still in progress.

### 9.2 Receivables and prepayments

	2009 US\$'000	2008 US\$'000
Management fee receivables	1,449	940
Receivable from investee companies	1,287	3,258
Other receivables	12,305	21,481
	15,041	25,679

Included in "Other receivables" is an amount of US\$ 11.77 million (31 December 2008: US\$ 20.62 million) due on account of an abandoned real estate investment project in the Kingdom of Saudi Arabia. During the year, the Bank has entered into an agreement with the counter party for the repayment of amount over a period of fifteen months ending 30 July 2010. The Bank will receive quarterly installment with a profit rate of 6.33% per annum on the outstanding amount. Out of the total amount outstanding, US\$ 1.24 million has been received subsequent to the year end.

### 9.3 Due from investee companies

	2009 US\$'000	2008 US\$'000
Commodity murabaha receivables	10,974	8,344
Deferred profit	(627)	(210)
	10,347	8,134
Provision	(2,000)	-
	8,347	8,134

# NOTES TO THE FINANCIAL STATEMENTS

At 31 December 2009

## 10. INVESTMENTS

The Bank has investments in various equity instruments, which are as under:

	Notes	2009 US\$'000	2008 US\$'000
<i>Carried at fair value through statement of income</i>			
Quoted		-	705
Held for trading			
Quoted		-	32,765
Available for sale			
Quoted		15,831	1,356
Unquoted	10.1	21,582	22,222
		37,413	57,048
<b>Impairment on available for sale investments</b>			
Quoted	10.2	20,351	688
Unquoted		1,051	-
		21,402	688

10.1 Included in unquoted investment above is an equity stake of 18% (2008: 18%) in EWAAN Capital, an asset management company which is being established in the Kingdom of Saudi Arabia. EWAAN Capital had not commenced its operations as at 31 December 2009.

10.2 Effective from 1 January 2009, the Bank has changed its intention regarding investment categorised as held for trading since the Bank no longer wishes to realise short term gains from market price movements and intends to hold this investment as strategic in nature. Therefore investment has been reclassified as "Available for sale (AFS)" with effect from 1 January 2009 at fair value. Subsequent to reclassification, the fair value gains or losses are recognised in statement of changes in equity except in case of losses arising from impairment or derecognition of investment which are recognised in statement of income.

The quoted investment reclassified was carried at US\$ 32.77 million at 1 January 2009. The carrying value of quoted investment at 31 December 2009 is US\$ 12.73 million. During the year, the Bank has provided US\$ 20.03 million as impairment loss against the said investment.

## 11. ASSETS HELD FOR SALE

During the year 2009, the Bank established Istethmary Sarajevo City Centre-I Limited "the Company", a special purpose vehicle incorporated in Cayman Islands, which holds 100% equity stake in Istethmary Sarajevo City Centre-II Limited, a special purpose vehicle incorporated in Cayman Islands, which owns indirectly equity stake of 28.31% in Magros Veletrgovia d.d. Total assets and liabilities of the Company amounted to US\$ 28.67 million and nil (2008: nil) respectively and the non-controlling interest amounts to US\$ 1.79 million (2008: nil).

## 12. INVESTMENT IN ASSOCIATE

	2009 US\$'000	2008 US\$'000
Opening balance	5,836	12,288
Add: Investment made during the year	-	311
Less: Share of loss from associate	(77)	(4,096)
Less: Sale of investment	-	(266)
Less: Investment reclassified as available for sale	-	(2,401)
	5,759	5,836
Provision	(1,772)	-
	3,987	5,836

# NOTES TO THE FINANCIAL STATEMENTS

At 31 December 2009

## 12. INVESTMENT IN ASSOCIATE (continued)

The Bank holds an investment in IIB UAE Investments Limited ("IIB-UAE"), a special purpose vehicle incorporated in Cayman Islands with limited liability. IIB Bay Tower Investment Limited, a subsidiary of IIB UAE Investments Limited, was established to own 65% of Bay Development Properties Limited. As on the balance sheet date, the Bank holds 27.32% (2008:27.32%) equity stake in IIB UAE.

The following table summarises financial information of the Bank's investment in associate:

	2009 US\$'000	2008 US\$'000
Associates' balance sheet		
Assets	32,611	49,598
Liabilities	(119)	(16,636)
Net assets	32,492	32,962
Share of loss from associate	(77)	(4,096)

During 2007, Bay Development Properties Limited ("the Company"), in which IIB UAE Investments Limited owns approximately 65% equity, had entered into a conditional sale/purchase agreement with a buyer to sell the investment property. Later on the Company had terminated this sale/purchase agreement on the basis that the buyer had failed to fulfill his contractual obligation. The buyer has commenced a court action against the Company for i) the appointment of a receiver to preserve the property, ii) specific performance of the sale/purchase agreement and iii) the sum of AED 124 million (US\$ 33.77 million), being the amount agreed for the plot of land pursuant to the sale/purchase agreement.

During 2008, the Court of First Instance and the Court of Appeal awarded the buyer with specific performance of the sale/purchase agreement but not the other reliefs sought by the buyer. The Company had appealed the Court of Appeal's decision to the Court of Cassation.

During 2009, the Court of Cassation dismissed the Company's appeal and affirmed the judgement of the Court of First Instance awarding specific performance of the sale/purchase agreement. The Company made an application to the Court of Cassation to rule that the order for specific performance of the sale/purchase agreement includes payment by the buyer to the Company of the balance of the purchase price stipulated in the sale/purchase agreement which was dismissed by the court.

Dubai Courts issued a notice to the parties of judgement awarding specific performance of the sale/purchase agreement to the buyer. Further, Dubai Properties issued a letter stating that they do not object to the transfer of the plot to the buyer and accordingly Dubai Land Department issued a title deed to the buyer.

The Company filed a complaint with the Dubai Land Department which has lead to a restrictive covenant stating that the plot can not be disposed of in any way, pending further notice from the Land Department.

The Company has made an application to the Dubai Court of Appeal requesting that the court reconsider the judgement that it rendered in 2008 on the basis that the buyer made fraudulent representations to the court. As at the reporting date the Court has not delivered its decision on the application.

The Company is also suing the buyer, Dubai Properties and Business Bay L.L.C. before the Dubai Court of First Instance (Case No. 111/2009) essentially for payment of the balance of the purchase price provided under the sale/purchase agreement. The amount claimed from the buyer as unpaid balance of the purchase price consists of the AED 17.44 million (US\$ 4.75 million) plus AED 60.31 million (US\$ 16.42 million) made up of three cheques which the buyer handed to the Company as payment but that the bank refused to cash in because the cheques were at least six months old by the time the Company presented them for payment. In the same case, the Company is also seeking payment of AED 26.16 million (US\$ 7.12 million) from Dubai Properties and Business Bay L.L.C. alleging that this is an overpayment made by or on behalf of the counterclaim against the Company seeking AED 250 million (US\$ 68.07 million) as compensation for alleged damages suffered by the buyer as a result of the Company's refusal to transfer ownership of the plot. As at the reporting date the Court has not delivered its decision on the application.

# NOTES TO THE FINANCIAL STATEMENTS

At 31 December 2009

In addition to the two cases above, the Company has filed a complaint against the buyer's Principal, with the Dubai police authorities, the complaint is based on the three cheques amounting to AED 60.31 million (US\$ 16.42 millions).

At the reporting date, the legal title of the land is held in the name of the buyer. The sale and transfer of investment property is restricted by the Dubai Land Department pending further notice from the Land Department.

## 13. OTHER LIABILITIES

	2009 US\$'000	2008 US\$'000
Payable to investors	2,489	2,577
Brokerage payable	-	2,823
Accrued expenses	394	2,265
Other payables	111	401
	2,994	8,066

Other payables include earnings prohibited by Shari'a to be utilised exclusively for charitable purposes and amounts to US\$ 9 thousand (2008: nil).

## 14. EQUITY

	2009 US\$'000	2008 US\$'000
Share capital		
Authorised: 200,000,000 ordinary shares of US\$ 1 each	200,000	200,000
Issued and fully paid:		
109,996,000 ordinary shares (2008: 109,996,000) of US\$ 1 each	109,996	109,996

### Treasury Shares

	2009		2008	
	Number of shares'000	Value US\$'000	Number of shares'000	Value US\$'000
At 1 January	3,000	6,798	100	113
Purchase of treasury shares during the year	-	-	3,000	6,798
Sale of treasury shares during the year	-	-	(100)	(113)
At 31 December	3,000	6,798	3,000	6,798

In the year 2008, the Bank sold 0.10 million treasury shares at a cost of US\$ 0.11 million, for a total sale price of US\$ 0.30 million. The Bank also purchased 3 million shares of its own equity from one of the investors at a total cost of US\$ 6.79 million. There has been no sale or purchase of treasury shares in the current year.

### Share premium

Amounts collected in excess of the par value of the issued share capital, net of share issue expenses, are treated as share premium. This amount is not available for distribution, but can be utilised as stipulated in the Bahrain Commercial Companies Law.

# NOTES TO THE FINANCIAL STATEMENTS

At 31 December 2009

## 14. EQUITY (continued)

### Statutory reserve

The statutory reserve has been created in accordance with the Bahrain Commercial Companies Law. The Bank transfers 10% of its annual profits to its statutory reserve till such time as the reserve equals 50% of the issued share capital of the Bank. The reserve is not available for distribution, except in circumstances as stipulated in the Bahrain Commercial Companies Law and following the approval of the Central Bank of Bahrain. As the Bank made a loss during the year, no transfers have been made during the year.

### Cumulative changes in fair value reserve

This represents unrealised fair valuation gains or losses on available for sale investments. This reserve is distributable upon value realisation, which takes place at the time of actual exit or derecognition.

### Foreign currency translation reserve

The foreign currency translation reserve is used to record exchange differences arising from the translation of the non-monetary items denominated in foreign currencies.

## 15. PROPOSED APPROPRIATIONS

The Board of Directors of the Bank has not proposed any cash dividend (2008: 7%), owing to the fact that the Bank has incurred an operating loss in the year.

## 16. ASSETS UNDER MANAGEMENT

Total assets under management as at 31 December 2009 were:

	2009 US\$ '000	2008 US\$ '000
Proprietary	68,280	62,884
Client	354,470	351,131
	422,750	414,015

Proprietary assets are included in the balance sheet, while clients' assets, which are managed in fiduciary capacity without recourse to the Bank, are not included in the balance sheet.

## 17. TRANSACTIONS WITH RELATED PARTIES

Related parties comprise major shareholders, directors, key management personnel and Shari'a Supervisory Board of the Bank and entities controlled, jointly controlled or significantly influenced by them.

The significant balances with related parties were as follows:

	Shareholders/ directors US\$ '000	Others US\$ '000	Total 2009 US\$ '000	2008 US\$ '000
<b>Assets</b>				
Investment	6,052	1,981	8,033	10,267
Investment in associates	-	3,987	3,987	5,836
Receivable from investee companies	-	735	735	147
<b>Liabilities</b>				
Other liabilities	2,489	-	2,489	2,577

The Directors believe that no provision is required in respect of balances due from related parties.

# NOTES TO THE FINANCIAL STATEMENTS

At 31 December 2009

Transactions with related parties included in the statement of income were as follows:

	Shareholders/ directors US\$ '000	Others US\$ '000	Total 2009 US\$ '000	2008 US\$ '000
<b>Income</b>				
Investment banking fees	-	76	76	1,732
Unrealised gain on items fair valued through statement of income	-	-	-	145
Share of loss from associate	-	(77)	(77)	(4,096)
Provision (note 12)	-	(1,772)	(1,772)	-
Dividend income	-	30	30	48
<b>Expenses</b>				
Directors' remuneration	300	-	300	500
Shari'a Supervisory Board remuneration	-	70	70	119

Compensation of key management personnel was as follows:

	2009 US\$'000	2008 US\$'000
Short term employee benefits	3,020	5,896
End of service benefits	204	121
	3,224	6,017

Investments amounting to US\$ 15.13 million (2008: US\$ 35.17 million) are held in the name of related parties on behalf of the Bank.

## 18. COMMITMENTS

	Notes	2009 US\$'000	2008 US\$'000
Operating lease	18.1	335	968

18.1 At 31 December 2009, the Bank has commitments of non-cancelable operating leases of US\$ 0.33 million (2008: US\$ 0.72 million) relating to leasehold premises. Of the commitments, US\$ 0.23 million (2008: US\$ 0.39 million) expire within one year and the remaining expire within one to two years.

# NOTES TO THE FINANCIAL STATEMENTS

At 31 December 2009

## 19. MATURITY ANALYSIS OF ASSETS AND LIABILITIES

The table below shows an analysis of financial assets and liabilities analysed according to when they are expected to be recovered or settled. See Note 20.3 "Liquidity risk and funding management" for the Bank's contractual undiscounted repayment obligations.

	Up to 3 months US\$ '000	3 to 12 months US\$ '000	Subtotal less than 12 months US\$ '000	1 to 3 years US\$ '000	Undated US\$ '000	Total US\$ '000
<b>ASSETS</b>						
Cash and balances with banks	1,974	-	1,974	-	-	1,974
Due from financial institutions	55,702	-	55,702	-	-	55,702
Receivables	9,524	12,681	22,205	3,183	-	25,388
Investments	-	589	589	64,560	-	65,149
Investment in associates	-	-	-	3,987	-	3,987
Other assets	338	85	423	-	-	423
Equipment	-	-	-	-	1,973	1,973
Assets classified as held for sale	-	26,880	26,880	-	-	26,880
<b>Total assets</b>	<b>67,538</b>	<b>40,235</b>	<b>107,773</b>	<b>71,730</b>	<b>1,973</b>	<b>181,476</b>
<b>LIABILITIES</b>						
Other liabilities	1,627	1,138	2,765	229	-	2,994
<b>Total liabilities</b>	<b>1,627</b>	<b>1,138</b>	<b>2,765</b>	<b>229</b>	<b>-</b>	<b>2,994</b>
<b>Net gap</b>	<b>65,911</b>	<b>39,097</b>	<b>105,008</b>	<b>71,501</b>	<b>1,973</b>	<b>178,482</b>

The maturity profile of assets and liabilities as at 31 December 2008 based on contractual undiscounted repayment obligations is as follows.

	Up to 3 months US\$ '000	3 to 12 months US\$ '000	Subtotal less than 12 months US\$ '000	1 to 3 years US\$ '000	Undated US\$ '000	Total US\$ '000
<b>ASSETS</b>						
Cash and balances with banks	2,205	-	2,205	-	-	2,205
Due from financial institutions	118,268	-	118,268	-	-	118,268
Receivables	-	8,134	8,134	25,679	-	33,813
Investments	-	-	-	57,048	-	57,048
Investment in associates	-	-	-	5,836	-	5,836
Other assets	405	190	595	-	-	595
Equipment	-	-	-	-	953	953
<b>Total assets</b>	<b>120,878</b>	<b>8,324</b>	<b>129,202</b>	<b>88,563</b>	<b>953</b>	<b>218,718</b>
<b>LIABILITIES</b>						
Other liabilities	1,399	1,178	2,577	5,489	-	8,066
<b>Total liabilities</b>	<b>1,399</b>	<b>1,178</b>	<b>2,577</b>	<b>5,489</b>	<b>-</b>	<b>8,066</b>
<b>Net gap</b>	<b>119,479</b>	<b>7,146</b>	<b>126,625</b>	<b>83,074</b>	<b>953</b>	<b>210,652</b>

## 20. RISK MANAGEMENT

### 20.1 Introduction

Risk is inherent in the Bank's investing activities and is managed through a process of ongoing identification, measurement and monitoring, subject to risk limits and other controls. This process of risk management is critical to the Bank's continuing profitability and each individual within the Bank is accountable for the risk exposures relating to his or her responsibilities. The main risks to which the Bank is exposed are credit risk, liquidity risk, market risk and operational risk.

#### a) Risk management structure

##### *Board of Directors*

The Board of Directors is responsible for the overall risk management approach and for approving the risk strategies and principles.

##### *Shari'a Supervisory Board*

The Shari'a Supervisory Board reviews the principles and contracts relating to the transactions conducted by the Bank to judge whether it followed the principles of the Islamic Shari'a, specific fatwas and guidelines issued by the Board.

##### *Executive Committee*

The Executive Committee of the Board considers and approves requests to purchase and sell individual investments up to the limit imposed by the Board.

##### *Investment Committee*

Potential deals are presented to the Investment Committee and Risk Management Committee for consideration and those worthy of further evaluation are forwarded to the Executive Committee for initial approval to incur detailed due diligence expenditure.

##### *Risk Management Committee*

The Risk Management Committee has the overall responsibility for establishing the risk strategy and implementing principles, frameworks, policies and limits. It is responsible for the fundamental risk issues and manages and monitors relevant risk decisions.

##### *Risk Management Department*

The Risk Management Department is responsible for implementing the appropriate risk management strategy and methodology for the Bank. It ensures that there are adequate control procedures in place such that the risks exposed to are within the approved limits.

##### *Assets & Liabilities Committee*

The Assets & Liabilities Committee is responsible for monitoring liquidity risk, profit rate risk, foreign currency limits/exposures, capital adequacy and the overall asset/liability mix.

##### *Audit Committee*

The Audit Committee is appointed by the Board of Directors and consists of three non-executive Board members. The Audit Committee assists the Board in carrying out its responsibilities with respect to assessing the quality and integrity of financial reporting and risk management, the audit thereof, the soundness of the internal controls of the Bank, the measurement system of risk assessment and relating these to the Bank's capital, and the methods for monitoring compliance with laws, regulations and supervisory and internal policies.

##### *Internal Audit*

Risk management processes throughout the Bank are audited at least annually by the Internal Audit Department, based on the risk-based audit plan approved by the Audit Committee. Audit staff examine both the adequacy of the procedures and the Bank's compliance with the procedures. Internal Audit discusses the results of all assessments with management, then reports its findings and recommendations to the Audit Committee.

# NOTES TO THE FINANCIAL STATEMENTS

At 31 December 2009

## 20. RISK MANAGEMENT (continued)

### 20.1 Introduction (continued)

#### b) Risk measurement and reporting systems

Currently, the Bank's assets mainly comprise cash and balances with banks, due from financial institutions and investments. Balances with banks and due from financial institutions represent deposits with GCC incorporated banks with investment grade credit ratings. Investments comprise mainly retentions in the Bank's investment offerings, which are unquoted and illiquid.

Monitoring and controlling risks is primarily performed based on limits approved by the Board. These limits reflect the business strategy and market environment of the Bank as well as the level of risk that it is willing to accept, with additional emphasis on selected industries. The Bank also monitors and measures the overall risk-bearing capacity in relation to the aggregate risk exposure across all risk types and activities.

#### c) Excessive risk concentration

Concentrations arise when a number of counterparties are engaged in similar business activities, or activities in the same geographical region, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations indicate the relative sensitivity of the Bank's performance to developments affecting a particular industry or geographical location.

In order to avoid excessive concentrations of risk, the Bank's policies and procedures include guidelines to maintain a diversified portfolio. Identified concentrations of credit risks are controlled and managed accordingly.

### 20.2 Credit risk

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. The Bank manages credit risk by setting limits for individual counterparties. Counterparty limits are set by the Board of Directors, monitored by the Risk Management Department and reviewed regularly.

#### a) Risk concentrations of the maximum exposure to credit risk

Concentration of risk is managed by client/counterparty. The maximum credit exposure to any client or counterparty as of 31 December 2009 was US\$ 49.1 million (2008: US\$ 55.8 million).

l) The table below shows the maximum exposure to credit risk for the balance sheet components. There is no significant use of master netting and collateral agreements.

	Notes	Gross maximum exposure 2009 US\$ '000	Gross maximum exposure 2008 US\$ '000
Credit risk items:			
Balances with banks	7	1,972	2,203
Due from financial institutions	8	55,702	118,268
Receivables	9	51,124	33,813
Other assets		423	595
<b>Total Credit Risk Exposure</b>		<b>109,221</b>	<b>154,879</b>

ll) The analysis by geographical region of the Bank's financial assets having credit risk exposure as at 31 December 2009 is as follows:

	Banking activities US\$ '000	Others US\$ '000	Total US\$ '000
Geographical region:			
Bahrain	8,609	44,327	52,936
Europe	-	8,349	8,349
Other Gulf Cooperation Council (GCC) countries	49,066	728	49,794
Africa	-	50	50
Asia	-	92	92
	<b>57,675</b>	<b>53,546</b>	<b>111,221</b>

# NOTES TO THE FINANCIAL STATEMENTS

At 31 December 2009

The analysis by geographical region of the Bank's financial assets having credit risk exposure as at 31 December 2008 is as follows:

	Banking activities US\$ '000	Others US\$ '000	Total US\$ '000
Geographical region:			
Bahrain	120,471	24,287	144,758
Europe	-	8,792	8,792
Other Gulf Cooperation Council (GCC) countries	-	1,187	1,187
Africa	-	100	100
Asia	-	42	42
	120,471	34,408	154,879

III) The industry sector analysis of the Bank's financial assets having credit risk exposure as at 31 December 2009 is as follows:

	Banking activities US\$ '000	Others US\$ '000	Total US\$ '000
Industry sector:			
Real estate	-	38,224	38,224
Banking and financial institutions	57,675	92	57,767
Manufacturing	-	2,847	2,847
Automotive	-	50	50
Others	-	12,333	12,333
	57,675	53,546	111,221

The industry sector analysis of the Bank's financial assets having credit risk exposure as at 31 December 2008 is as follows:

	Banking activities US\$ '000	Others US\$ '000	Total US\$ '000
Industry sector:			
Real estate	-	30,700	30,700
Banking and financial institutions	120,471	1,718	122,189
Manufacturing	-	437	437
Automotive	-	100	100
Others	-	1,453	1,453
	120,471	34,408	154,879

b) Credit quality per class of financial assets

The credit rating analysis of the Bank's financial assets having credit risk exposure as at 31 December 2009 is as follows:

	Banking activities US\$ '000	Others US\$ '000	Total US\$ '000
Credit rating:			
A+ (by Fitch)	7,903	-	7,903
A- (by Fitch)	49,066	-	49,066
Unrated	706	53,546	54,252
	57,675	53,546	111,221

# NOTES TO THE FINANCIAL STATEMENTS

At 31 December 2009

## 20. RISK MANAGEMENT (continued)

### 20.2 Credit risk (continued)

#### b) Credit quality per class of financial assets (continued)

The credit rating analysis of the Bank's financial assets having credit risk exposure as at 31 December 2008 is as follows:

	Banking activities US\$ '000	Others US\$ '000	Total US\$ '000
Credit rating:			
A+ (by Fitch)	105,945	-	105,945
A- (by Fitch)	4,374	-	4,374
Unrated	10,152	34,408	44,560
	120,471	34,408	154,879

### 20.3 Liquidity risk and funding management

Liquidity risk is the risk that the Bank will be unable to meet its payment obligations when they fall due under normal and stress circumstances. It monitors future cash flows and liquidity required for working capital and investment acquisition on a quarterly basis and maintains significant cash and cash equivalent balances.

l) The table below summarises the maturity profile of the Bank's financial liabilities at 31 December 2009 based on contractual undiscounted repayment obligations. Note 19 (Maturity analysis of assets and liabilities) shows the expected maturities of these liabilities.

	On demand US\$ '000	Less than 3 months US\$ '000	3 months to 1 year US\$ '000	1 to 5 years US\$ '000	Total US\$ '000
Other liabilities	-	1,627	1,138	229	2,994
Total undiscounted financial liabilities	-	1,627	1,138	229	2,994

The table below summarises the maturity profile of the Bank's financial liabilities at 31 December 2008 based on contractual undiscounted repayment obligations.

	On demand US\$ '000	Less than 3 months US\$ '000	3 months to 1 year US\$ '000	1 to 5 years US\$ '000	Total US\$ '000
Other liabilities	-	1,399	1,178	5,489	8,066
Total undiscounted financial liabilities	-	1,399	1,178	5,489	8,066

### 20.4 Market risk

Market risk is the risk to earnings resulting from adverse movements in foreign currency rates, profit rate yield curves and equity prices. To enable effective monitoring and managing of exposures, all market risks associated with the Bank's investments are managed and monitored using basic sensitivity analyses.

#### a) Equity price risk

Equity price risk is the risk that the fair value of equity investments decreases as a result of fluctuations in the respective stock market indices. As at 31 December 2009, the Bank had available for sale investments listed on overseas stock exchanges. Based on the values at 31 December 2009, a change in the quoted price of plus or minus 10% would change the value of these investments by plus or minus US\$ 1.58 million (2008: US\$ 3.56 million) with a corresponding increase or decrease in equity, except in case where impairment loss accrued which will result in decrease being taken to statement of income.

The Bank also has unquoted investments carried at fair value using either net asset value or valuation from independent valuer. Based on the values at 31 December 2009, a change in the valuation of 10% would change the value of these investments by plus or minus US\$ 2.56 million (2008: US\$ 2.14 million) with a corresponding increase or decrease in equity.

# NOTES TO THE FINANCIAL STATEMENTS

At 31 December 2009

## b) Foreign currency risk

Foreign currency risk is the risk that the value of a financial instrument will fluctuate due to adverse changes in foreign currency rates. Certain investments and other financial assets and liabilities are in other currencies and give rise to foreign currency risk.

Positions are monitored on a quarterly basis to ensure they are maintained within established limits. The Bank's exposure in foreign currencies consists of exposures from banking activities, as it does not have a trading book in foreign currencies.

The Bahraini Dinar (BHD), Saudi Riyal (SAR) and UAE Dirham (AED) are pegged to the US Dollar and resultantly positions in these currencies are not considered to represent currency risk. The Bank had the following foreign currency exposures at 31 December 2009:

	Assets US\$ '000	Liabilities US\$ '000	Net US\$ '000
Euro	38,919	-	38,919
Pound Sterling	1,499	-	1,499
Kuwaiti Dinar	701	-	701
Others	2,523	-	2,523
	43,642	-	43,642

The Bank had the following foreign currency exposures at 31 December 2008:

	Assets US\$ '000	Liabilities US\$ '000	Net US\$ '000
Euro	9,453	212	9,241
Pound Sterling	2,328	-	2,328
Kuwaiti Dinar	738	-	738
Others	521	-	521
	13,040	212	12,828

## Sensitivity Analysis

The following table demonstrates the sensitivity of the statement of income to a reasonable possible movement of the currency rates against the US Dollar (functional and reporting currency) based on the above positions as on 31 December, with all other variables held constant.

	Change in exchange rate (+/-) %	2009 Effect on net income (+/-) US\$ '000	2008 Effect on net income (+/-) US\$ '000
Euro	10%	2,997	44
Kuwaiti Dinars	10%	32	34

## c) Profit rate risk

Profit rate risk arises from the possibility that changes in profit rates will affect future cash flows or the fair values of the financial instruments. The Bank currently has limited exposure to profit rate risk. The Bank's assets that are exposed to profit rate risk comprise of due from financial institutions and have repricing dates no longer than three months. During 2009, a +/- 0.25% change in the profit rate, with all other variables constant, would have resulted in a +/- US\$ 0.23 million (2008: +/- 0.25% resulted in US\$ 0.29 million) impact on the statement of income.

# NOTES TO THE FINANCIAL STATEMENTS

At 31 December 2009

## 21. CAPITAL MANAGEMENT

The Bank maintains an actively managed capital base to cover risks inherent in the business. The adequacy of the Bank's capital is monitored using, among other measures, the rules and ratios established by the Basel Committee on Banking Supervision as adopted by the Central Bank of Bahrain.

The primary objectives of the Bank's capital management are to ensure that the Bank complies with regulatory capital requirements and that the Bank maintains healthy capital ratios in order to support its business and to maximise shareholders' value. During the past year, the Bank has complied in full with all its externally imposed capital requirements.

The Bank manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of its activities. In order to maintain or adjust the capital structure, the Bank may adjust the amount of dividend payment to shareholders, return capital to shareholders or issue new capital. No changes were made in the objectives, policies and processes from the previous years.

Basel II as adopted by CBB became applicable from 1 January 2009. For the purposes of comparison, the proforma capital position as at 31 December 2009, regulatory capital and risk weighted assets have been recalculated in accordance with the Basel II.

	Notes	Basel II 2009 US\$ '000	Basel II 2008 US\$ '000
Regulatory capital base:			
Tier 1 capital	21.1	173,896	200,348
Total regulatory capital		173,896	200,348
Risk weighted assets	21.2	292,982	229,318
Total capital adequacy ratio		59%	87%
Minimum regulatory ratio		12%	12%

### 21.1 Tier 1 Capital

	Basel II 2009 US\$ '000	Basel II 2008 US\$ '000
Share capital	109,996	109,996
Treasury shares	(6,798)	(6,798)
Share premium	72,050	72,050
Statutory reserve	5,588	5,588
Cumulative changes in fair value reserve	(2,373)	(2,736)
Retained earnings	(3,257)	24,436
Core Tier 1 Capital	175,206	202,536
Deductions	(942)	(1,161)
Tier 1 Capital before adjustments for negative balance of Tier 2	174,264	201,375
Negative balance of Tier 2	(368)	(1,027)
Tier 1 Capital net of negative Tier 2 Capital	173,896	200,348

Tier 1 capital comprises: share capital; share premium; statutory reserve; foreign currency translation reserve and retained earnings, including current year profit. Tier 2 capital comprises of positive fair value reserves minus capital deduction for large exposure.

# NOTES TO THE FINANCIAL STATEMENTS

At 31 December 2009

## 21.2 Risk weighted assets

	Basel II 2009 US\$ '000	Basel II 2008 US\$ '000
Credit risk weight assets	193,748	159,206
Market risk weight assets	43,638	14,516
Operational risk weight assets	55,596	55,596
	292,982	229,318

### Credit risk-weighted assets

The Bank uses the standardized approach, which requires banks to use external credit ratings to combine them into categories to which standardized risk weightings are applied. For regulatory purposes, credit risk-weighted assets include investments and receivables.

### Market risk-weighted assets

The Bank does not maintain a trading book and, as a result, market risk-weighted assets result from the net foreign currency positions of the Bank.

### Operational risk-weighted assets

In calculating operational risk-weighted assets, the Bank uses the basic indicator approach which calculates operational risk-weighted assets as a proportion of the average of three years' revenues.

## 22. FAIR VALUE OF FINANCIAL INSTRUMENTS

### Determination of fair value and fair value hierarchy

The Bank uses the following hierarchy for determining and disclosing fair value of financial assets and liabilities:

Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities;

Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly; and

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

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

	2009			
	Level1 US\$'000	Level2 US\$'000	Level3 US\$'000	Total US\$'000
Non-trading investments				
Quoted	15,831	-	-	15,831
Unquoted	-	15,972	5,610	21,582
	15,831	15,972	5,610	37,413

There has been no transfers from level 1 and level 2 to level 3 during the year 2009.

# NOTES TO THE FINANCIAL STATEMENTS

At 31 December 2009

## 22. FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

### Financial instruments recorded at fair value

The following is a description of the determination of fair value of financial instruments which are recorded at the fair value using valuation techniques. These incorporate the Bank's estimate of assumptions that a market participant would make when valuing instruments.

### Financial Investments - available for sale

Available-for-sale financial assets valued using a valuation technique or pricing models primarily consist of unquoted equities.

These assets are valued using models which sometimes only incorporate data observable in the market and at other times use both observable and non-observable data. The non-observable inputs to the models include assumptions regarding the future financial performance of the investee, its risk profile and economic assumptions regarding the industry and geographical jurisdiction in which the investee operates.

### Movements in level 3 financial instruments measured at fair value

The following table shows a reconciliation of the opening and closing amount of level 3 financial assets and liabilities which are recorded at fair value:

	Unquoted 2009 US\$ '000
Balance at 1 January	6,912
Impairment loss recorded in statement of income	(671)
Fair value loss recorded in equity	(18)
Purchases, sales and settlements, net	(613)
Balance at 31 December	5,610

For the above financial instruments categorised as level 3, the Bank has used reasonably possible alternative assumption and adjusted the discount rate by 10% as a key unobservable model input. The effect of this will result in +/- 561 thousand adjustment in the carrying value of level 3 investments and related cumulative fair value change.

## 23. SEGMENTAL INFORMATION

The activities of the Bank are all related to investment banking activities. The Bank operates solely in the Kingdom of Bahrain and, as such, no geographical segment information is presented.

## 24. SOCIAL RESPONSIBILITY

The Bank discharges its social responsibilities through donations to charitable causes and organisations.

## 25. COMPARATIVE

Certain of the prior year figures have been reclassified to conform to the presentation adopted in the current year. Such reclassification did not affect the previously reported net income for the year or total equity.