

# International Investment Bank

Annual Report 2007





International Investment Bank (IIB) was incorporated as an Islamic investment bank on 6 October 2003, under commercial registration number 51867 as a Bahrain Joint Stock Company (closed). It started investment activity on 13 October 2003 and operates under a Wholesale Banking Licence issued by the Central Bank of Bahrain.

IIB has an authorized capital of US\$ 200 million and 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; investment, underwriting and placement in real estate and private equity; and corporate finance, all 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.

CONTENTS	
Vision and Mission	02
Key Highlights of 2007	03
Principal Investment Offerings 2004-2007	04
Financial Summary	06
Board of Directors' Report	09
Corporate Governance	12
Board of Directors	12
Independent Shari'ah Supervisory Board	14
Executive Management	14
Other Senior Officers	15
Transaction Charts	17
Chief Executive Officer's Review of Operations	19
Principal Transactions in 2007	24
Financial Review	28
Risk Management	32
Organisation Structure	33
Shari'ah Supervisory Board Report	34
Independent Auditors' Report to the Shareholders	36
Statement of Income	38
Balance Sheet	39
Statement of Changes in Equity	40
Statement of Cash Flows	42
Notes to the Financial Statements	43

## VISION AND MISSION

To be a regional leader in private equity investment, real estate investment, asset management and corporate finance, 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.

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.

## KEY HIGHLIGHTS OF 2007

## FINANCIAL

+ **56.3%** **NET INCOME** for the year increased by 56.3% over 2006 to US\$ 21.1 million

+ **172.3%** **TOTAL ASSETS** increased by 172.3% over 2006 to US\$ 257.3 million

+ **252.4%** **TOTAL EQUITY** increased by 252.4% to US\$ 216.4 million

+ **12.9%** **RETURN ON AVERAGE EQUITY** increased to 27.1% from 24.0% in 2006

## NON FINANCIAL

- Five investments were arranged compared to three in 2006
- Total staff increased by 37.5% to 55 compared to 40 at 2006 year end
- Office space in Seef District was doubled

## PRINCIPAL INVESTMENT OFFERINGS 2004 – 2007

Year	Investment Description	Location	Private Equity Raised (US\$ millions)	Other Funds <sup>#</sup> (US\$ millions)	Total Transaction Size (US\$ millions)	
1	2004	Property fund **	Bahrain	18.6	18.5	37.1
2	2004/5	Independent power producer ***	Asia	23.0	267.0	290.0
3	2005	Housing development company	Bahrain	22.6	0.6	23.2
4	2005	Commercial property *	UK	14.8	290.6	305.4
5	2005	Commercial 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	Commercial property portfolio	France	50.8	68.7	119.5
9	2006	Real estate development company	Saudi Arabia	21.0	85.8	106.8
10	2006	Commercial tower development	Dubai	25.0	75.2	100.2
11	2007	Steel reinforcement bar manufacturing	Bahrain	13.0	28.4	41.4
12	2007	Commercial property	Germany	99.3	133.7	233.0
14	2007	Real estate investment company	Saudi Arabia	2.7	10.7	13.4
15	2007	Commercial tower development	Abu Dhabi	65.0	132.4	197.4
16	2007	Commercial bank	Azerbaijan	26.0	–	26.0
<b>Totals</b>			<b>434.1</b>	<b>1,668.3</b>	<b>2,102.4</b>	

\* Investment realized in 2006

\*\* Partial exit in 2006 and 2007

\*\*\* Investment realized in 2007

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

## SECTOR SUMMARY

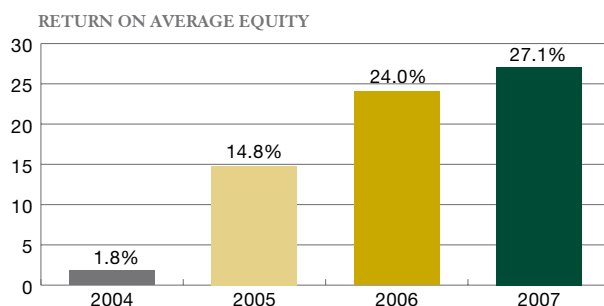
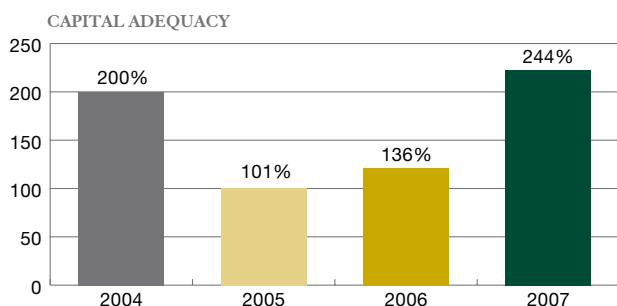
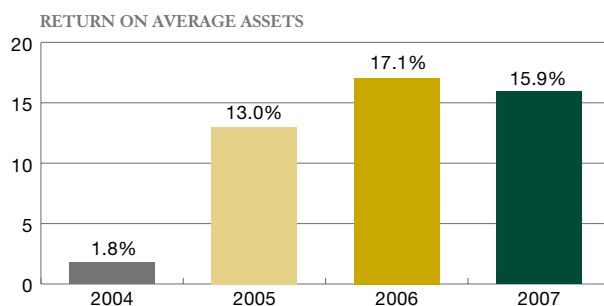
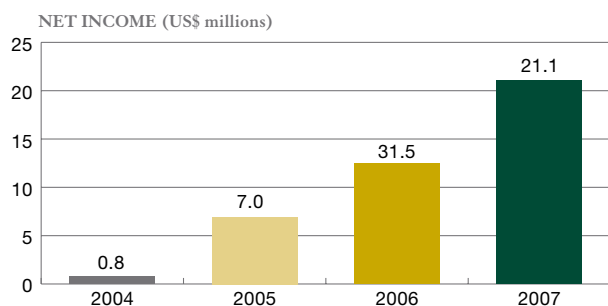
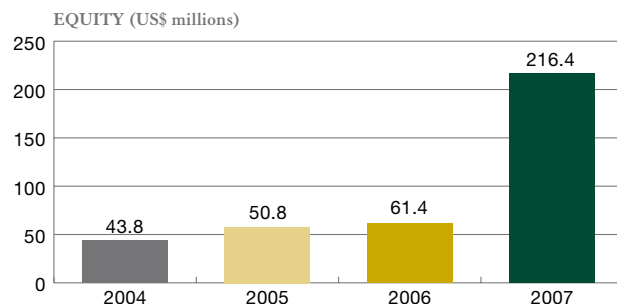
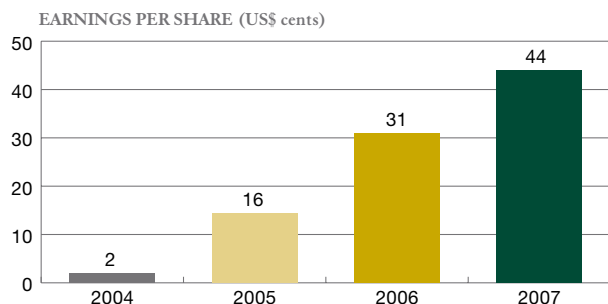
<b>Sector</b>	<b>Private Equity Raised</b> (US\$ millions)	<b>Other Funds</b> (US\$ millions)	<b>Total Transaction Size</b> (US\$ millions)
1 Real estate (income generating)	183.5	511.5	695.0
2 Real estate (development)	156.8	378.3	535.1
3 Private equity	93.8	778.5	872.3
<b>Totals</b>	<b>434.1</b>	<b>1,668.3</b>	<b>2,102.4</b>

## PRINCIPAL BANKERS AND PROFESSIONAL ADVISORS

Principal Bankers	Ahli United Bank, Bahrain
External Auditors	Ernst & Young, Bahrain
External Legal Counsel	Qays H. Zu'bi, Bahrain

## FOUR-YEAR FINANCIAL SUMMARY

	2007	2006	2005	2004
<b>Earnings</b> (US\$ millions)				
Total income	<b>34.3</b>	24.6	12.4	4.2
Total expenses	<b>13.2</b>	11.1	4.2	2.7
Net income	<b>21.1</b>	13.5	7.0	0.8
Dividend (%)	<b>15.0</b>	10.0	8.0	–
<b>Financial Position</b> (US\$ millions)				
Total assets	<b>257.3</b>	94.5	63.4	44.4
Due from financial institutions	<b>211.4</b>	53.5	26.2	28.0
Investments	<b>36.4</b>	16.4	13.7	14.1
Due to financial institutions	<b>-</b>	20.0	–	–
Equity	<b>216.4</b>	61.4	50.8	43.8
<b>Ratios</b>				
<b>Profitability</b>				
Return on average equity (%)	<b>27.1</b>	24.0	14.8	1.8
Return on average assets (%)	<b>15.9</b>	17.1	13.0	1.8
Earnings per share (cents)	<b>44</b>	31	16	2
Cost-to-income ratio (%)	<b>38.4</b>	45.2	43.5	81.5
<b>Capital</b>				
Capital adequacy (regulatory minimum 12%)	<b>244</b>	136	101	200
Equity/total assets (%)	<b>84.1</b>	65.0	80.2	98.5
<b>Liquidity and Other</b>				
Investments/total assets (%)	<b>14.1</b>	17.4	21.6	31.7
Liquid assets/total assets (%)	<b>83.6</b>	66.4	43.0	63.3
Assets under management (US\$ millions)	<b>343.1</b>	181.7	117.6	19.6
Number of employees	<b>55</b>	40	20	17





## BOARD OF DIRECTORS' REPORT



**Saeed Abdul Jalil Al Fahim**, CHAIRMAN

**Dear Shareholders,** I am pleased to report that International Investment Bank has demonstrated continued improvement during 2007 on each key performance indicator, despite a challenging and increasingly competitive business environment.

### **GCC ECONOMIC OVERVIEW**

2007 has witnessed a continued and strong growth in the GCC economies bolstered by the sustained increase in oil prices and the unremitting drive of the regional governments towards economic diversification, privatization and liberalization measures designed to further strengthen and increase the productivity of their economies. A large number of public and private investment projects have been launched which not only support the current and expected growth but also further accentuate the region's attractiveness to regional and international investors.

Several factors have helped develop a robust platform for the continued economic expansion of the region in the coming years. These include the aforementioned policies and initiatives of the regional governments, the large and increasing fiscal surpluses arising from high oil prices, a developing market for regional equities and the demand generating demographic profile of the region. The GCC stock markets now offer investors diverse investment options with a combined market capitalization of over US\$ 1 trillion. Over 600 listed companies are spread across various sectors such as banking and insurance, telecoms, real estate and industrials.

With increasing participation by the private sector, relative to that of the public sector, in the overall GDP growth, the current economic and policy landscape provides a sturdy bedrock for increasing investment opportunities for investors. This assessment forms the cornerstone of our expectations that investors will derive superior risk adjusted returns from investing in real estate and private equity transactions in the coming years.

### **INVESTMENT OFFERINGS**

During 2007, the fourth year of full operations, IIB has structured several investment transactions. These include a steel re-bar manufacturing project in Bahrain, the first re-bar green-field project established in the Kingdom of Bahrain to support the growing construction, infrastructure and real estate sectors of the region; a portfolio of fully-tenanted prime commercial properties in Germany; real estate development projects in the Kingdom of Saudi Arabia and the United Arab Emirates; and the acquisition of a 49% stake in a commercial bank operating in The Republic of Azerbaijan.

Supported by its network of strategic and financial partners, the Bank has developed a pipeline of diversified investment opportunities, currently at various stages of due diligence, in GCC, North Africa, Europe and Asia. IIB will provide its investors a steady flow of attractive investment opportunities during 2008 and in the years to come.

### **FINANCIAL PERFORMANCE**

Net Income for the year has reached US\$ 21.1 million, representing an increase of 56.3% compared to US\$ 13.5 million earned in 2006. The result reflects the continued growth of IIB's business and its ability to effectively develop and offer a diverse range of attractive investment opportunities. Total Income increased by 40.2% to US\$ 34.3 million in 2007 from US\$ 24.6 million in 2006. This increase was mainly from investment banking fees which increased by 33.3% to US\$ 22.8 million from US\$ 17.1 million in 2006, generated from the structuring, underwriting and placement of new investments.

Total Expenses increased by US\$ 2.1 million, as IIB continued to build its staffing and operating infrastructure to support its growing business activities. Total Assets increased by 172.2% from the 2006 year end figure to US\$ 257.3 million. The increase represents mainly net receipts from investors in respect of the share issue of US\$ 138.9 million.

Profitability Ratios for 2007 are impressive, evidenced by annualized returns of 43.5% on Average Paid up Capital (ROC) and 27.1% on Average Equity (ROE). The capital adequacy ratio at 31 December 2007 of 244% is over 20 times greater than the minimum requirement of 12% by the Central Bank of Bahrain. This demonstrates a strong and prudent approach by the Bank in respect of risk management.

Since its inception, our Bank has continually improved its financial performance as indicated by investment banking revenues, asset base, profitability ratios and capital adequacy. This has been achieved while pursuing an ongoing strategy of investing across diverse asset classes and geographical regions in order to provide our investors with superior risk adjusted returns.

#### SHAREHOLDERS' DIVIDENDS

Given these excellent results, the Board is proposing to distribute a cash dividend of 15% for 2007. Investors who purchased shares in the rights and private placement offerings will receive dividends commencing from their share purchase dates. As in the previous years, the Board is also proposing that shareholders pay their respective Zakat on their equity investment in the Bank.

#### CAPITAL INCREASE

IIB increased its paid up capital from US\$ 43 million to US\$ 110 million reflecting the issuance of 67 million new ordinary shares. Following the receipt of the necessary regulatory approvals, the registration was completed on 30 December 2007.

#### OUTLOOK FOR 2008

Supported by the favorable economic landscape, the ample and increasing liquidity in the regional economies and strong investor demand for Shari'ah compliant investment products in real estate, infrastructure, manufacturing projects and services, the regional economies continue to offer a vibrant environment conducive to investments. In particular, the regional

investment banks anticipate a continued and strong growth in the demand for Shari'ah compliant investments.

The investment climate has become more competitive and challenging, due mainly to the intense competition from both regional and international investment banks for new business. This is creating downward pressures on yields in an environment of decreasing profit rates resulting in an upward pressure on regional and international asset valuations to levels which may not prove sustainable.

The continued shortage of qualified investment banking professionals has pushed up remuneration levels which can affect IIB's ambitious growth plans. The Bank is therefore introducing, beginning in 2008, a share incentive scheme designed to retain and attract key staff.

#### BOARD MEMBERSHIP

In November 2007, Mr. Khalid Othman Abu Hemed, Mr. Abdulla Ahmed Balamsh and Mr. Sulaiman Haider Sulaiman retired by rotation and did not seek re-election. I would like to warmly thank them for guiding the Bank in its initial years of operations.

I have pleasure in welcoming Mr. Bader Ibrahim Mohammad Bin Saedan and Mr. Ali Haider Sulaiman Al Haider to the Board and look forward to working with them as IIB continues to develop.

#### APPRECIATIONS

I would like to extend my thanks to my colleagues on the Board of Directors for their unrelenting support and guidance, to our management team and staff for their valuable efforts and finally the Central Bank of Bahrain and the Ministry of Industry and Commerce.

We look forward to continuing our mutually beneficial relationship in the years ahead.



**Saeed Abdul Jalil Al Fahim**  
CHAIRMAN



IIB acquired an equity stake of 49% in Amrahbank



IIB achieved a profitable exit following the sale of its 50% stake in One @ Business Bay

## 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.

### 1. BOARD OF DIRECTORS

The Board meets regularly throughout the year in order to control strategic, financial, operational, internal control and compliance issues. Subsequent to the Annual General Meeting on 12 March 2008, the Board comprises nine non-executive directors and one executive director.

#### Board Members

The Board of Directors comprised the following members as at 12 March 2008:



**MR. 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); 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.



**MR. AHMED SALEM BUGSHAN**  
VICE CHAIRMAN

President, Saudi Industrial Projects Company (SIPCO), Saudi Arabia; Member of the Board, Pepsi Cola, Egypt; Chairman, Savoy Hotels, Sharm Al-Sheikh.



**MR. AAMER ABDUL JALIL AL FAHIM**  
DIRECTOR

Managing Director of Al Fahim Group, UAE; Board Member of Abu Dhabi Commercial Bank; Board Member of Al Wathba Insurance Company; Member of Federal National Council, UAE; Board Member of Abu Dhabi Chamber of Commerce and Industry; Board Member of Al Qudra Holdings; Board Member of Al Safwa Islamic Financial Services; Chairman of Aradi Properties P.J.S.C.



**MR. EBRAHIM ESHAQ ABDULRAHMAN**  
DIRECTOR

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

**MR. ABDUL WAHAB MOHAMMED AL WAZZAN****DIRECTOR**

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

**MR. FAHAD FOUAD BUBSHAIT****DIRECTOR**

Chairman & CEO of Audeo Maxima International Ltd., UAE; Chairman of BubbleDeck Middle East LLC, UAE; Foreign Investments Advisor of Abdulla Fouad Holding Co. Ltd.; Former General Manager of Mantech Real Estate & Fouad Travel Agency (Abdulla Fouad Holding Company Ltd.), Saudi Arabia.

**MR. ALI HAIDER SULAIMAN AL HAIDER****DIRECTOR**

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

**MR. ALI HASHIM SADIQ HASHIM****DIRECTOR**

President & CEO, Gulf United Investment, Saudi Arabia; Chairman, Gulf Packaging Systems, Saudi Arabia; Member of the Board, Middle East Telecom (METCO), Saudi Arabia.

**MR. BADER IBRAHIM MOHAMMAD BIN SAEDAN****DIRECTOR**

General Manager, Al Saedan Real Estate Co, Saudi Arabia; Board Member, Commodore International, U.K; Board Member, Saudi Tunisian Real Estate Co., Tunisia; Board Member, Mautin R.E. Co., Saudi Arabia; Member of the R. E. Committee, Riyadh Chamber of Commerce & Industry.

**MR. AABED AL-ZEERA****DIRECTOR & CEO**

Chief Executive Officer, IIB; Director and Chairman of Executive Committee, European Islamic Investment Bank Plc, United Kingdom; Director of several companies of IIB.

During 2007, the following served as directors and retired by rotation on 4 November 2007 but did not seek re-election:

- Mr. Khalid Othman Abu Hemed
- Mr. Abdulla Ahmed Balamsh
- Mr. Sulaiman Haider Sulaiman

The following directors served on the Board from 4 November 2007 to date:

- Mr. Bader Ibrahim Mohammad Bin Saedan
- Mr. Ali Haider Sulaiman Al Haider

#### **Board Committees**

The Board's four sub-committees namely the Executive Committee; the Audit Committee; the Nominations Committee and the Remuneration Committee; as well as the Shari'ah Supervisory Board comprising expert, independent scholars continued to assist the Board in carrying out its responsibilities. The Remuneration Committee was constituted in 2007. This Committee assists the Board to determine the annual remuneration (including bonus and share purchase scheme) of Board members and executive management. The membership of these sub-committees comprises only members of the Board.

## **2. INDEPENDENT SHARI'AH SUPERVISORY BOARD**

IIB's Shari'ah Supervisory Board regularly reviews all investment products and business activities to ensure compliance with the Islamic Shari'ah, approves the Bank's financial statements and also 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, AAIQFI, 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. Bahar holds a Bachelor 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, he has been Shari'ah Compliance Officer at ABC Islamic Bank, Bahrain and is currently Head of Shari'ah Compliance at Al-Salam Bank, Bahrain.

## **3. 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.

#### **Executive Managers**

##### **AABED AL-ZEERA, CHIEF EXECUTIVE OFFICER**

Mr. Al-Zeera oversees the Executive Management team and chairs the Management Committee. He has over twenty five years of international banking experience with major financial institutions in the Kingdom of Bahrain and the United Arab Emirates. These 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.

**MOHAMED HADI MEJAI, EXECUTIVE DIRECTOR**

Mr. Mejai heads Direct 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 France and the 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. 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 in Kuwait.

**4. OTHER SENIOR OFFICERS****EIHAB AHMED, DIRECTOR,  
LEGAL & COMPLIANCE**

Mr. Ahmed graduated in 1994 with a Law Degree from the University of Khartoum, following which he spent 6 years as Legal Consultant at the Ministry of Justice of Sudan. He was a Public Prosecutor and for four years a Legal Advisor at the Bank of Khartoum. He then worked as Legal Consultant at BDO Jawad Habib, Bahrain and most recently as Head of Legal Department at Khaleej Finance & Investment Bank (Capinvest),

Bahrain. Mr. Ahmed is also a Certified Compliance Officer from the American Academy of Financial Management.

**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 20 years of experience in the financial services industry. He has held positions as President of Cochin Stock Exchange 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 11 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 15 years of experience in the appraisal, development and financing of mainly industrial and infrastructure projects in Europe, the Middle East, Africa and Central Asia.

**NADER ASAD, DIRECTOR, FINANCE AND  
ADMINISTRATION**

Mr. Asad holds a B.Sc. in Accounting from University of Bahrain and an M.B.A. from Heriot-Watt University in Edinburgh, UK. His professional qualifications include CFA, CPA, CMA, CIA and five other professional qualifications. He spent eight years providing audit and advisory services at PricewaterhouseCoopers and Arthur Andersen and before joining the Bank in 2005, he was Deputy Financial Controller at Bahrain Islamic Bank.

**ALAA BUHUSSAIN, DIRECTOR**

Mr. Buhussain is a graduate of the University of Manchester, UK with a Bachelor Degree in Economics with honors, specializing in Accounting and Finance. He is currently pursuing a Masters in Business Administration (MBA) with Manchester Business School, UK. Mr. Buhussain is a Chartered Financial Analyst (CFA) and prior to joining IIB, was a Senior Vice President at Forsyth Partners and head of the firm's operations in Bahrain. Previously, he was Vice President of Wealth Management at Addax Investment Bank and a member of the founding team with responsibility for structuring and evaluating investment products.

**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.

**5. COMMUNICATIONS**

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

The Bank maintains a website [www.iib-bahrain.com](http://www.iib-bahrain.com) which contains the Annual Report for the last two years, 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 can be made to the relevant departments as follows:

Investment and partnership opportunities:  
[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)

**6. ADDITIONAL GOVERNANCE CONTROLS**

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

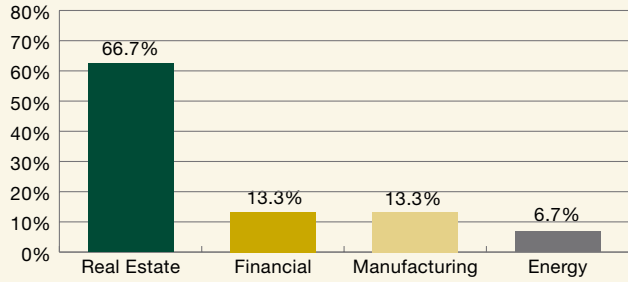
Corporate governance is also supported by the ongoing reviews performed by the Internal Audit Department and the External Auditors. The reviews confirm that the policies and internal control procedures conform to best practice and are being fully complied with by management and staff.

**7. NEW PAID-UP CAPITAL**

During 2007, the issued share capital was increased from 43,000,000 ordinary shares of nominal value US\$ 1 to 109,995,797 ordinary shares.

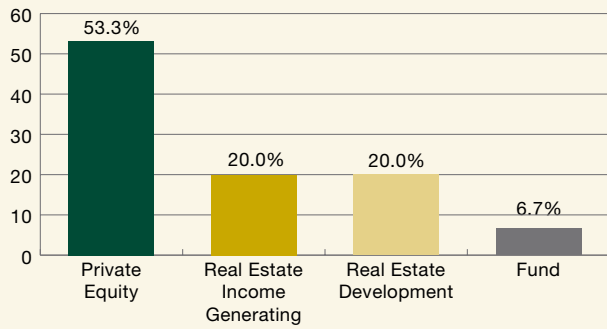
**TRANSACTIONS BY MARKET SECTOR**

(December 2007)



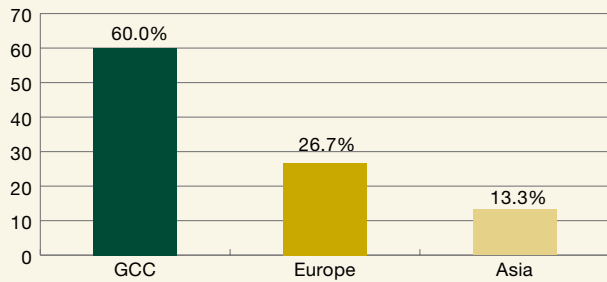
**TRANSACTIONS BY INVESTMENT TYPE**

(December 2007)



**TRANSACTIONS BY REGION**

(December 2007)





## CHIEF EXECUTIVE OFFICER'S REVIEW OF OPERATIONS



**Abed Al-Zeera**, CHIEF EXECUTIVE OFFICER

During 2007 International Investment Bank B.S.C. (c) (IIB) has continued to demonstrate strong earnings growth, coupled with improvement on each key performance metric.

We are pleased to state that IIB's strong capital base and close relationship with its shareholders and the network of high caliber financial institutions, consultants and other counterparties has helped the Bank to meet investors' access to a well diversified portfolio of investments with superior risk adjusted returns.

The Bank enters 2008 with a robust investment pipeline and will be announcing a number of compelling deals in the months ahead.

### INVESTMENT OFFERINGS

During 2007, the fourth year of full operations, IIB concluded the following investment transactions:

- A steel re-bar manufacturing project, the first re-bar green-field project established in the Kingdom of Bahrain to support the growing construction, infrastructure and real estate sectors of the Kingdom and the region.
- A portfolio of fully-tenanted prime commercial properties in Germany.
- Real estate development projects in The Kingdom of Saudi Arabia and the United Arab Emirates.
- The acquisition of a 49% stake in a commercial bank operating in the Republic of Azerbaijan, which is in the advanced stages of finalization.

A description of the principal transactions is provided in the next section.

### INVESTMENT EXITS

The Bank's majority partners in its 2005 investment offering in an Asia-based independent power producer sold the business in mid 2007. Investors have received two payments and IIB is pursuing a further payout for its investors.

In addition, the Bank made a profit of US\$ 1.4 million on the sale of land located in the Seef district of the Kingdom of Bahrain. The Bahrain Property Fund successfully exited from two properties in its portfolio and provided an attractive return to its investors.

### CAPITAL INCREASE

IIB increased its paid up capital from US\$ 43 million to approximately US\$ 110 million reflecting an increase of 67 million new shares. The rights issue was fully subscribed while the private placement offering of 30,000,000 shares was oversubscribed by 33.3%. Following the receipt of the necessary regulatory approvals, the registration was completed on 30 December 2007. The number of shareholders has increased from 44 to 106.

### OFFICE SPACE

During the year, a second floor in the iconic Almoayyed Tower in the Seef business district has been leased and fitted out. The flexible premises have the capacity to house approximately double the existing staff numbers, to cater for the expected expansion in services in the coming years.

**KEY APPOINTMENTS**

The Bank's employees have increased from 40 at the end of 2006 to 55 at year end 2007. Appointments included its Executive Director – Asset Management and Head of Risk Management, In addition, the Investment Placement team was considerably expanded. These key appointments equip IIB to achieve its planned investment objectives and operating performance.

**POLICIES AND PROCEDURES**

The Bank has strengthened its internal corporate governance by establishing a codified set of policies and procedures in respect of its key departments and activities. These were approved by the Board of Directors during 2007.

**CORE BANKING SYSTEM**

During the year, the Bank has intensively evaluated and short-listed several core banking systems out of which one will be implemented during 2008. The implementation will automate a number of key processes, including accounting, financial control, risk management and customer relationship management. It will represent a major investment and is essential to the Bank's long-term growth and development.

**CORPORATE GOVERNANCE**

As part of its continuing initiatives to strengthen internal processes and controls, the Bank in 2007 has established a number of management committees, namely the Investment Committee, Assets & Liabilities Committee, Risk Management Committee and IT Steering Committee. All committees function within charters that are approved by the Board of Directors.

**PERFORMANCE OUTLOOK**

IIB is well poised to deliver its planned profitability and transactions in 2008 and in the years to come from its larger capital base, robust transactions currently in its pipeline, continual support from shareholders and the efforts of IIB's strong management team.

Challenges continue to confront performance, in particular the current and expected uncertain outlook on the US Economy and the possibilities of further volatility in the stock markets from the sub prime crisis. Profit rates and asset yields continue to face downward pressures. Coupled with the general increase in liquidity and decreasing profit rates, asset prices and valuations are likely to increase resulting in higher entry valuations on new investments. On the operational side, banks continue to experience a shortage of qualified investment banking professionals which challenge our growth plans in the months to come. IIB has taken adequate steps to not only retain staff but also to attract sufficient new talent to meet its resource requirements.



**Aabed Al-Zeera**  
CHIEF EXECUTIVE OFFICER

**EXECUTIVE MANAGEMENT**

From left to right: Mr. Subhash Jalan, Executive Director, Asset Management; Mr. Eihab Ahmed, Director, Legal & Compliance; Mr. Michael Ross-McCall, Chief Financial Officer; Mr. Abed Al-Zeera, Chief Executive Officer; Mr. Mohamed Hadi Mejai, Executive Director, Direct Investment & Business Development.

**INVESTMENT PLACEMENT TEAM**

(From left to right): Bader Ali, Associate; Bashar Al-Shaikh, Associate; Nader Al-Khalili, Principal; Rayan Kazerooni, Director; Ebrahim Al-Shaibeh, Director; Alyas Al-Meftah, Director; Jassim Al-Shaikh, Principal; Fawzan Al-Naser, Principal; Sh. Daaj Al-Khalifa, Principal; Mohammed Khonji, Principal.

**DIRECT INVESTMENT & BUSINESS DEVELOPMENT TEAM**

(From left to right): Alaa Buhussain, Director; Ashwin Kumar, Associate; Suad Almoayed, Associate; Hakan Gunay, Director; Atif Naveed, Associate; Mohamed Hadi Mejai, Executive Director; Nasser Eldine Bayoun, Principal; Marieta Cano, Executive Secretary; Al-Imran Khan, Associate; Jamal Mayouf, Principal; Fadi Al-Qassim, Project Manager.

## PRINCIPAL TRANSACTIONS IN 2007

**IIB STEEL COMPANY I LIMITED**

TOTAL TRANSACTION SIZE US\$ 41 MILLION

In April 2007, IIB acquired the 35% equity stake in the US\$ 41 Million Bahrain based steel reinforcement bar manufacturer, Universal Rolling WLL ("UNIROL").

The rationale for the acquisition was primarily the strong outlook for the regional steel industry in general, and that of reinforcement bars in particular, supported by the growing steel demand in the GCC region. This demand results from ongoing and announced massive real estate, construction and infrastructure development projects in the region over the coming several years.

Steel reinforcement bars are one of the major components in the construction projects and generally represent around 15-20% of the total construction costs. The demand for such re-bars in the GCC region is phenomenal and most of the requirement is currently imported. The demand in the Kingdom of Bahrain alone is around 350,000 tons per annum and increasing.

UNIROL is constructing an industrial facility which will produce 170,000 tons per annum of such re-bars. It has the distinction of being the first plant of its kind in the Kingdom. Its operations are endorsed by international reputable consultants from the UK, Germany and the United States of America.

The manufacturing process employs the state-of-the-art German Thermo Mechanical Treatment Technology (TMT).

**"This will enable UNIROL to manufacture and market superior re-bar products than those currently available and imported into the country. The company will have a first mover advantage, creating the opportunity to capture a significant share of the local re-bar market."**

The Internal Rate of Return (IRR) for this investment is expected to be around 23% per annum over a five year horizon.

**IIB GERMAN PROPERTY COMPANY LIMITED**

TOTAL TRANSACTION SIZE €159 MILLION

In May 2007, IIB acquired a high quality portfolio of commercial real estate properties in Munich, Germany, valued at €159 Million. IIB acquired a 95% stake in this portfolio which comprises three commercial properties rented to a blue chip German company and strategically located 3 kilometers from the Munich City Centre.

IIB acquired the portfolio in partnership with a renowned asset manager, who owns the balance of 5% and has extensive experience in the structuring and management of Shari'ah compliant real estate investments in Europe.

The acquisition was predicated on the strength of the commercial real estate sector in Germany which IIB believes offers a robust and attractive growth potential. The market dynamics of the property sector in the major cities of Germany, particularly Munich, are strong as a result of the large and growing commercial and industrial economic base. The city has witnessed a record transaction volume in 2006 with growth of nearly 130% over that of 2005. The letting market in 2006 grew by a substantial 13% over the previous year.

**“This reflects strong demand from tenants and IIB believes that the acquired portfolio is well positioned to enable investors to realize maximum gains from the emerging trends in the local Munich property market.”**

The projected Internal Rate of Return (IRR) on this investment is in excess of 10.1% per annum over an investment horizon of five years with a cash yield of 7% per annum.



#### **IIB ABU DHABI PROPERTIES I LIMITED**

TOTAL TRANSACTION SIZE US\$ 197 MILLION

In June 2007, IIB launched a new \$65 Million property fund which will own and develop two plots of land in the Danet Abu Dhabi Master Development Project in Abu Dhabi, UAE.

IIB & its investors have 66.7% indirect stake in the project company and 33.3% is owned by United Friends Company (UFC), a UAE based company. It has acquired two plots of land at Danet Abu Dhabi and will develop the land into a mixed use 21 storey twin tower office building connected at the basement and podium levels. One of the two towers will comprise office units whilst the other will be a mix of office and residential units. The towers will also include retail and entertainment units and a car park for 632 cars. The objective of the company is to let the units initially and eventually sell the towers.

This project was launched in recognition of the growing demand for state-of-the-art office units and upmarket residential units in Abu Dhabi contrasted with the relative short supply of such buildings. The city is projected to witness population growth rates of nearly 7% over the period 2006-2010. The real estate market

in Abu Dhabi has seen large increases in property values and rentals which are expected to continue over the coming several years.

**“Coupled with the new policies of the Abu Dhabi government that will spur further growth, increasing demand for space by growing tourism, the relaxation of real estate ownership regulations and the launch of mega projects in the emirate, the property market of Abu Dhabi is likely to witness continued growth rates.”**

IIB projects that the investors of IIB Abu Dhabi Properties 1 will realize an Internal Rate of Return (IRR) in excess of 24% per annum over the coming 3-5 years.



#### **IIB AZERBAIJAN LIMITED**

**TOTAL TRANSACTION SIZE US\$ 26 MILLION**

In October 2007, IIB announced its acquisition of a 49% stake in “Amrahbank”, one of the fastest growing banks in the Republic of Azerbaijan. With a strong network of 20 branches and a staff strength of 250, the bank is the most profitable private sector bank in Azerbaijan in terms of Return on Equity.

Azerbaijan is the world's fastest growing economy with an average growth rate of more than 30% in the last two years. The country has achieved rapid growth for several consecutive years starting in 1996 mainly as a result of an increasingly transparent and supportive business environment. The growth in the overall economy is expected to maintain its current pace.

The main economic and demographic indicators point to a huge potential for growth in the financial services sector in Azerbaijan and, more specifically, in the untapped demand for Islamic banking products and services.

**“Amrahbank is well positioned to seize the benefits of being a pioneer in the provision of Shari’ah compliant financial products in Azerbaijan.”**

The Internal Rate of Return (IRR) for this investment is projected to be around 21.8% per annum over an anticipated five year investment horizon.

## FINANCIAL REVIEW

### OVERVIEW

During the year ended 31 December 2007, the Bank recorded net income of US\$ 21.1 million, compared to US\$ 13.5 million during 2006, an increase of 56.3%. Total assets at year-end 2007 aggregated to US\$ 257.3 million, up 172.3% or US\$ 162.8 million as compared to year-end 2006. Net cash from operating activities was US\$ 36.4 million (2006: US\$ 19.4 million) and cash and cash equivalents were a healthy US\$ 215.1 million at the end of 2007.

The key financial ratios were strong in 2007. The return on average equity rose from 24.0% in 2006 to 27.1%, while return on average assets decreased slightly from 17.1% to 15.9%. Earnings per share improved from 31 cents to 44 cents.

### INCOME

The Bank's total income increased by 39.6% during 2007 to US\$ 34.3 million. This was driven mainly by higher investment banking fees which increased from US\$ 17.1 million in 2006 to US\$ 22.8 million, earned from the structuring, underwriting and placement of new investments. This is a clear validation of the business model that IIB has put in place, which is founded principally on the generation of fee income from arranging and placing investments.

Income on due from financial institutions, being the profit on commodity murabaha and mudaraba deposits, was US\$ 4.3 million versus US\$ 1.8 million in 2006, reflecting the increase in total assets. The gain on investment property in 2007 was US\$ 1.4 million related to the sale of a plot of land in the Seef district of the Kingdom of Bahrain. IIB earned a net gain on foreign exchange of US\$ 2.2 million (2006: US\$ 0.1 million) arising from holding net assets unhedged in mainly Euro and Pounds Sterling. The Bank also earned profit in 2007 of US\$ 3.2 million from an associate relating to the unrealized gain in value of land held for investment in the UAE.

### EXPENSES

Total expenses in 2007 at US\$ 13.2 million were US\$ 2.1 million higher than those in the previous year. Underwriting fees in 2007 were US\$ 2.2 million (2006: nil) relating to one investment offering. All other transactions were successfully placed on a non-underwritten basis. Excluding underwriting fees, expenses reduced in 2007 by US\$ 0.1 million. Staff costs of US\$ 6.9 million dropped by US\$ 0.5 million as compared to 2006. General and administration expenses in particular travel, legal and professional fees, printing and advertising all increased in 2007 arising from the higher level of business activity. The Cost-to-Income Ratio reduced to 38.4% from 45.2% in 2006 and compares very favourably with regional and international investment banks.

### ASSETS

Cash and cash equivalents, comprising cash, balances with banks and due from financial institutions, at year-end 2007 of US\$ 215.1 million were US\$ 152.3 million higher than a year earlier. The extra liquidity was provided from retained profit and the net proceeds from the share issue during 2007 of US\$ 138.9 million.

Investments increased by US\$ 20.0 million (121.4%) to US\$ 36.4 million, represented by the Bank's retention in investment deals offered to investors in 2007, less one sale and one partial exit during the year. The investment property in Seef district was sold with a book value of US\$ 3.3 million. The 2007 total includes a balance of US\$ 12.6 million in respect of an investment offering partly sold at the year end. Investment in associates represented a 20% shareholding of US\$ 2.7 million in an asset management company being established in the Kingdom of Saudi Arabia and a 26% shareholding of US\$ 9.6 million in a company established in the UAE to purchase land for investment purposes.

Other assets of US\$ 4.8 million (2006: US\$ 14.6 million) mainly comprised balances receivable from various IIB

investment offering companies (SPVs). Reflecting the new investment offerings in 2007 less the one exit, assets under management increased by 88.8% from US\$ 181.7 million to US\$ 343.1 million.

#### LIABILITIES AND EQUITY

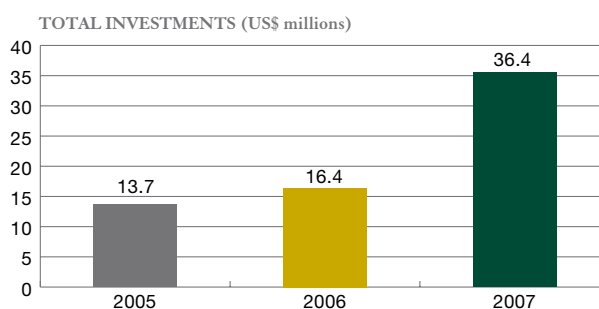
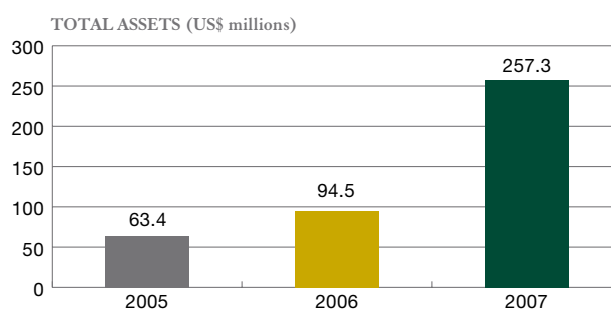
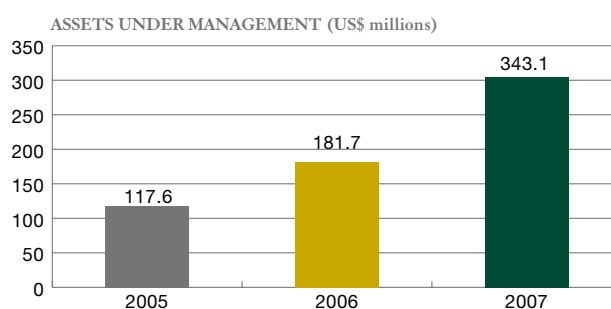
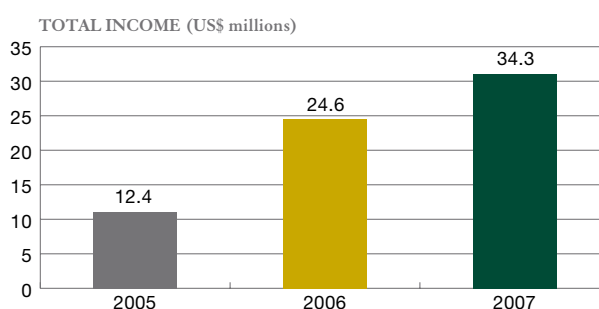
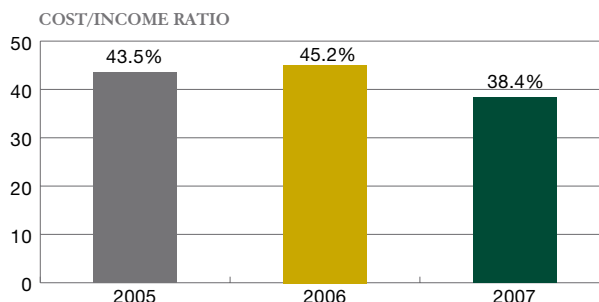
There were no borrowings on the balance sheet at the year end, compared with due to financial institutions at the end of 2006 of US\$ 20.0 million. Other liabilities of US\$ 40.9 million (2006: US\$ 13.1 million) mainly comprised US\$ 20.2 million payable for an investment offering and US\$ 15.3 million received from investors in advance of the offering closing date.

Equity increased by 252.3% to US\$ 216.4 million, mainly from the 2007 net income and the net proceeds from the share issue aggregating to US\$ 138.9 million. The share issue was very successful with the issue of 27.1 million rights shares and 39.896 million shares through private placement, being 17.5% oversubscribed in total and 33.0% oversubscribed for the private placement offering. Equity includes proposed appropriations of US\$ 10.2 million for the 2007 dividend which is subject to the shareholders' approval.

#### CAPITAL ADEQUACY

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 2007 was 244% (2006: 134%), being over 20 times above the minimum ratio. This ratio, reflecting credit and market risk, is based on guidelines issued by CBB which are compatible with the "Basel I" 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.

CBB has stated that all banks incorporated in Bahrain should adopt the "Basel II" rules commencing from 1 January 2008. Under this Accord, IIB's CAR at 2007 year end was 126%.



**ADMINISTRATION TEAM**

(From left to right) Ali Redha, Director, Internal Audit; Hussain Ali, Supervisor, General Services; Nilda Johnston, Executive Secretary; Hussein Mahdi, Information Technology Officer; Ninan Varkey, Head of Risk Management; Michael Ross-McCall, Chief Financial Officer; Nader Asad, Director, Finance & Administration; Eihab Ahmed, Director, Legal & Compliance; Said Itani, Head of Information Technology; Hassan Abbas, Accountant; Augustine Peter, Principal, Finance & Administration.

**ASSET MANAGEMENT TEAM**

(From left to right) Mazar Jalal, Principal; Hasan Abu-Hasan, Head of Engineering Services; Sadaf Gill, Analyst; Ruby Castro, Executive Secretary; Subhash Jalan, Executive Director; Mahmood Al-Qassab, Coordinator; Murtaza Ghulam, Principal.

## RISK MANAGEMENT

The Board of Directors has 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, Investment Committee and Audit Committee, through the programs implemented by the Internal Audit Department.

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. 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 various risks to which the Bank is exposed and the principal risk management techniques are summarised below. Further information on risk management is contained in Note 21 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 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. Details of maximum exposure to Credit Risk by balance sheet components, geographical region, industry sector and credit rating are contained in Note 21.2 to the Financial Statements.

### 2. LIQUIDITY RISK

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. The Assets & Liabilities Committee (ALCO) monitors future cash flows and liquidity required for working capital and investment acquisition. IIB maintains significant cash and cash equivalent balances and also has access to geographically diversified funding sources. The ratio of liquid assets to total assets as at 31 December 2007 was 84%.

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 according to when they are expected to be recovered or settled is contained in Note 20 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 trade in investments or foreign currencies. 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. Note 21.4 to the Financial Statements gives details of 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. The Bank minimises its exposure by ensuring that appropriate infrastructure, controls, systems and trained, competent people are in place.

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 premises continuity.

### 5. LEGAL RISK

Legal Risk is the risk arising from the potential that unenforceable contracts, lawsuits, or adverse judgements can disrupt or otherwise negatively affect the operations of the Bank. IIB has sought to mitigate its exposure to Legal Risk by establishing a Legal and Compliance Department headed by a qualified and experienced lawyer. In addition, it has relationships with well-established local and international law firms. The policies and procedures of the Bank ensure that funds are only committed after full legal due diligence has been performed.

## ORGANISATION STRUCTURE

**EXECUTIVE MANAGEMENT**

Aabed Al-Zeera	Chief Executive Officer
Mohamed Hadi Mejai	Executive Director, Direct Investment & Business Development
Michael Ross-McCall	Chief Financial Officer
Subhash Jalan	Executive Director, Asset Management

**DIRECT INVESTMENT & BUSINESS DEVELOPMENT**

Hakan Gunay	Director
Alaa Buhussain	Director
Nasser Eldine Bayoun	Principal
Jamal Mayouf	Principal
Fadi Al-Qassim	Project Manager
Al-Imran Khan	Associate
Ashwin Kumar	Associate
Atif Naveed	Associate
Bishayer Al-Khaja	Associate
Suad Almoayed	Associate

**INVESTMENT PLACEMENT**

Ebrahim Al-Shaibeh	Director
Rayan Kazerooni	Director
Alyas Al-Meftah	Director
Nader Al-Khalili	Principal
Jassim Al-Shaikh	Principal
Fawzan Al-Naser	Principal
Daajj Al-Khalifa	Principal
Mohamed Khonji	Principal
Bader Ali	Associate
Bashar Al-Shaikh	Associate
Salah Habib	Associate
Mohammed Habib	Associate

**ASSET MANAGEMENT**

Murtaza Ghulam	Principal
Mazar Jalal	Principal
Hasan Abu Hassan	Head of Engineering Services
Fatima Al Aradi	Investors Relations Officer
Mahmoud Al-Qassab	Co-ordinator
Sadaf Gill	Analyst

**FINANCE & ADMINISTRATION**

Nader Asad	Director
Augustine Peter	Principal
Haleema Ebrahim	Associate
Hassan Abbas	Accountant
Reem Ayoub	Officer, Corporate Communications

**INFORMATION TECHNOLOGY**

Said Itani	Head of Information Technology
Hussein Mahdi	Officer

**LEGAL & COMPLIANCE**

Eihab Ahmed	Director
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**RISK MANAGEMENT**

Ninan Varkey	Head of Risk Management
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**INTERNAL AUDIT**

Ali Redha	Director
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## 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, 2007. 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, 2007 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 Osama Mohammed Saad Bahar**

MEMBER OF THE SHARI'AH SUPERVISORY BOARD

25 Safar 1429  
2 March 2008



## INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS



We have audited the accompanying financial statements of International Investment Bank B.S.C. (c) ("the Bank") which comprises of the balance sheet as at 31 December 2007 and the statement of income, statement of changes in equity and statement of cash flows 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 both the Financial Accounting Standards issued by the Accounting and Auditing Organisation for Islamic Financial Institutions, to operate in accordance with Islamic Shari'ah and International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal controls relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances. In addition, the Board of Directors is responsible for the Bank's undertaking to operate in accordance with Islamic Shari'ah 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 the Auditing Standards for Islamic Financial Institutions and International Standards on Auditing. Those standards require that we comply with the relevant ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal 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 control. 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 2007 and of its financial performance and its cash flows for the year then ended in accordance with Financial Accounting Standards issued by the Accounting and Auditing Organisation for Islamic Financial Institutions and the Islamic Shari'ah Rules and Principles as determined by Shari'ah Supervisory Board of the Bank.

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

**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 2007 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 licence.

The logo for Ernst & Young, featuring the company name in a stylized, cursive script.

2 March 2008  
Manama, Kingdom of Bahrain

## STATEMENT OF INCOME

FOR THE YEAR ENDED 31 DECEMBER 2007

	Notes	2007 US\$'000	2006 US\$'000
<b>INCOME</b>			
Investment banking fees	3	22,776	17,147
Exit income		–	4,300
Income on due from financial institutions	4	4,307	1,792
Unrealised loss on available for sale securities		(283)	–
(Loss)/gain on sale of investments, net		(14)	1,046
Gain on investment property	10	1,368	–
Gain on financial assets fair valued through statement of income		456	85
Gain on foreign exchange		2,162	148
Dividend income		326	39
Share of profit of associate	11	3,177	–
<b>TOTAL INCOME</b>		<b>34,275</b>	<b>24,557</b>
<b>EXPENSES</b>			
Corporate expenses		3,256	3,278
Underwriting fees		2,223	–
Deal acquisition expenses		2,031	2,702
Selling expenses		2,155	1,974
Expense on due to financial institutions		90	288
Asset management expenses		946	906
General and administration expenses	6	2,100	1,650
Depreciation		365	294
<b>TOTAL EXPENSES</b>		<b>13,166</b>	<b>11,092</b>
<b>NET INCOME FOR THE YEAR</b>		<b>21,109</b>	<b>13,465</b>

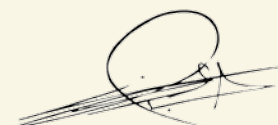
The attached explanatory notes 1 to 26 form part of these financial statements

## BALANCE SHEET

AT 31 DECEMBER 2007

	Notes	2007 US\$'000	2006 US\$'000
<b>ASSETS</b>			
Cash and balances with banks	7	3,668	9,250
Due from financial institutions	8	211,396	53,473
Investments	9	24,113	13,157
Investment property	10	–	3,284
Investment in associates	11	12,288	–
Other assets	12	4,789	14,596
Equipment		1,066	772
<b>TOTAL ASSETS</b>		<b>257,320</b>	<b>94,532</b>
<b>LIABILITIES AND EQUITY</b>			
Due to financial institutions		–	20,000
Other liabilities	13	40,926	13,117
<b>TOTAL LIABILITIES</b>		<b>40,926</b>	<b>33,117</b>
<b>EQUITY</b>			
Share capital	14	109,996	43,000
Treasury shares	14	(113)	(113)
Share premium	14	71,867	–
Reserves	14	24,418	14,238
Proposed appropriations	15	10,226	4,290
<b>TOTAL EQUITY</b>		<b>216,394</b>	<b>61,415</b>
<b>TOTAL LIABILITIES AND EQUITY</b>		<b>257,320</b>	<b>94,532</b>

The financial statements were authorized for issue in accordance with a resolution of the Board of Directors on 2 March 2008.



**Saeed Abdul Jalil Al Fahim**  
Chairman



**Aabed Al-Zeera**  
Chief Executive Officer

The attached explanatory notes 1 to 26 form part of these financial statements

## STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 31 DECEMBER 2007

	Share capital US\$'000	Treasury shares US\$'000	Share premium US\$'000	Reserves	
				Statutory reserve US\$'000	Cumulative changes in fair value reserve US\$'000
<b>Balance at 1 January 2007</b>	43,000	(113)	–	2,125	703
Cumulative changes in fair value	–	–	–	–	(703)
Transfer to retained earnings on realization	–	–	–	–	–
Transfer of fair value gain to reserve	–	–	–	–	–
<b>Income recognised directly in equity</b>	–	–	–	–	(703)
Net income for the year	–	–	–	–	–
<b>Total income and expenses for the year</b>	–	–	–	–	(703)
Transfer to liability	–	–	–	–	–
Transfer to statutory reserve	–	–	–	2,111	–
Proceeds from issue of share capital net of share issue expenses (note 14)	66,996	–	71,867	–	–
Proposed appropriation (note 15)	–	–	–	–	–
<b>Balance at 31 December 2007</b>	<b>109,996</b>	<b>(113)</b>	<b>71,867</b>	<b>4,236</b>	<b>–</b>
Balance at 1 January 2006	43,000	–	–	779	–
Cumulative changes in fair value	–	–	–	–	703
Transfer of fair value loss to reserve	–	–	–	–	–
Income recognised directly in equity	–	–	–	–	703
Net income for the year	–	–	–	–	–
Total income and expenses for the year	–	–	–	–	703
Transfer to liability	–	–	–	–	–
Dividend on treasury shares transferred to retained earnings	–	–	–	–	–
Transfer to statutory reserve	–	–	–	1,346	–
Purchase of treasury shares (note 14)	–	(113)	–	–	–
Proposed appropriation (note 15)	–	–	–	–	–
<b>Balance at 31 December 2006</b>	<b>43,000</b>	<b>(113)</b>	<b>–</b>	<b>2,125</b>	<b>703</b>

The attached explanatory notes 1 to 26 form part of these financial statements

## STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 31 DECEMBER 2007

Reserves	Investment	Retained	Total	Proposed	Total
	fair value reserve US\$'000	earnings US\$'000	reserves US\$'000	appropriations US\$'000	US\$'000
	304	11,106	14,238	4,290	61,415
	-	-	(703)	-	(703)
	(304)	304	-	-	-
	67	(67)	-	-	-
	(237)	237	(703)	-	(703)
	-	21,109	21,109	-	21,109
	(237)	21,346	20,406	-	20,406
	-	-	-	(4,290)	(4,290)
	-	(2,111)	-	-	-
	-	-	-	-	138,863
	-	(10,226)	(10,226)	10,226	-
	67	20,115	24,418	10,226	216,394
	343	3,230	4,352	3,440	50,792
	-	-	703	-	703
	(39)	39	-	-	-
	(39)	39	703	-	703
	-	13,465	13,465	-	13,465
	(39)	13,504	14,168	-	14,168
	-	-	-	(3,432)	(3,432)
	-	8	8	(8)	-
	-	(1,346)	-	-	-
	-	-	-	-	(113)
	-	(4,290)	(4,290)	4,290	-
	304	11,106	14,238	4,290	61,415

## STATEMENT OF CASH FLOWS

FOR THE YEAR ENDED 31 DECEMBER 2007

	Notes	2007 US\$'000	2006 US\$'000
<b>OPERATING ACTIVITIES</b>			
Net income for the year		21,109	13,465
Adjustments for:			
Depreciation		365	294
(Gain)/loss on financial assets fair valued through statement of income		(456)	94
Unrealized re-measurement loss on investment		283	–
Loss/(gain) on sale of investments, net		14	(1,046)
Gain on sale of investment property	10	(1,368)	–
Share of profit of associates	11	(3,177)	–
		16,770	12,807
Changes in operating assets and liabilities:			
Other assets		9,807	7,395
Other liabilities		27,797	301
Purchase of investments		(14,230)	(5,279)
Proceeds from disposal of investments		2,730	4,192
Purchase of investment in associate		(6,444)	–
Net cash from operating activities		36,430	19,416
<b>INVESTING ACTIVITIES</b>			
Purchase of investment in associate		(2,667)	–
Proceeds from sale of investment property	10	4,652	–
Purchase of equipment		(659)	(624)
Net cash from (used in) investing activities		1,326	(624)
<b>FINANCING ACTIVITIES</b>			
Purchase of treasury shares		–	(113)
Proceeds from issue of shares, net		138,863	–
Dividends paid		(4,278)	(3,192)
Due to financial institutions		(20,000)	20,000
Net cash from financing activities		114,585	16,695
<b>INCREASE IN CASH AND CASH EQUIVALENTS</b>		<b>152,341</b>	<b>35,487</b>
Cash and cash equivalents at beginning of the year		62,723	27,236
<b>CASH AND CASH EQUIVALENTS AT END OF THE YEAR (NOTE 16)</b>		<b>215,064</b>	<b>62,723</b>

The attached explanatory notes 1 to 26 form part of these financial statements

## NOTES TO THE FINANCIAL STATEMENTS

AT 31 DECEMBER 2007

### 1 CORPORATE INFORMATION

International Investment Bank B.S.C. (c) ("the Bank") operates under a Wholesale Islamic Banking Licence issued by the Central Bank of Bahrain. 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'ah.

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 37th floor Al Moayyed Tower, PO Box 11616, Manama, Kingdom of Bahrain.

### 2 ACCOUNTING POLICIES

#### a) Basis of preparation

The 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 and available for sale investment at fair value.

The financial statements are presented in United States Dollars which is the Bank's functional currency.

#### *Statement of compliance*

The financial statements of the Bank are prepared in accordance with both International Financial Reporting Standards ("IFRS") and Financial Accounting Standards issued by the Accounting and Auditing Organisation for Islamic Financial Institutions ("AAOIFI"), and are in conformity with the Bahrain Commercial Companies Law and the Central Bank of Bahrain and Financial Institutions Law.

#### b) Significant accounting judgments and estimates

In the process of applying the Bank's accounting policies, management has used its judgement and made estimates in determining the amounts recognised in the financial statements. The most significant use of judgements 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, fair value is determined on disposal of significant portion or on occurrence of an arm's length transaction involving a third party.

#### *Classification of investments*

Real estate investments acquired to earn rentals or for capital appreciation are classified as investment property.

Management decides on acquisition of an investment whether it should be classified as "carried at fair value through statement of income" or "available for sale". Investments are classified as carried at fair value through statement of income when they are designated as at fair value on initial recognition. All other investments are classified as 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 judgement.

## NOTES TO THE FINANCIAL STATEMENTS

AT 31 DECEMBER 2007

**c) Changes in accounting policies and disclosures*****IFRS adopted in the current year***

The accounting policies are consistent with those used in the prior years except that during the year, the Bank adopted IFRS 7 Financial Instruments: Disclosures and consequent amendments to IAS 1 – Capital Disclosures which have resulted in amended and additional disclosures regarding financial instruments and associated risks and the Bank's objectives, policies and processes for managing capital.

***Standards and Interpretations issued at 31 December 2007 but not adopted***

Revised IAS 1 – Presentation of Financial Statements (effective for the year ending 31 December 2009) has not been adopted by the Bank. The application of this standard will result in amendments to the presentation of the financial statements.

**d) 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 retranslated at the functional currency 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 at the date when the fair value was determined. Translation gains or losses on non-monetary items carried at fair value (other than those carried at fair value through statement of income) are included in equity as part of the fair value adjustment on investment available for sale.

## NOTES TO THE FINANCIAL STATEMENTS

AT 31 DECEMBER 2007

### 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 due to financial institutions and other liabilities.

Incremental transaction costs associated with the acquisition of investments available for sale are included in the cost of such investments.

#### **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 cost being the fair value of the consideration given at their fair value.

#### **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 "carried at fair value through statement of income" or "available for sale".

Incremental transaction costs associated with the acquisition of investments available for sale are included in the cost of such investments.

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

- **Carried at fair value through statement of income**

Realised gains and losses, dividends and unrealized gains and losses arising from the re-measurement to fair value, are included in the statement of income as 'gain on items fair valued through statement of income'.

As such investments would be classified as "available for sale" under AAOIFI, the unrealized gains arising from re-measurement to fair value are appropriated to an investment fair value reserve and are transferred to retained earnings only when realised.

## NOTES TO THE FINANCIAL STATEMENTS

AT 31 DECEMBER 2007

- **Available for sale**

Fair value changes are reported as a separate component of equity until the investment is derecognized, 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 can not be reliably measured are carried at cost less impairment losses, if any.

Investments for which fair value can not be determined, are carried at cost.

**Due to financial institutions**

This represents funds payable to financial institutions on the principles of murabaha contracts and are stated at principal plus accrued profit payable.

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 derecognized where:

- The right to receive cash flows from the asset has expired.
- 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.
- 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 (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 derecognized when the obligation specified in the contract is discharged, cancelled or expired.

iv) *Impairment of financial assets*

The Bank assesses at each balance sheet date 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 (an incurred "loss event") and that loss event(s) have an impact on the estimated future cash flows of the financial asset or the group of the financial assets that can be reliably estimated.

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 income statement – is removed from equity and recognised in the income statement. Impairment losses on equity investments are not reversed through the income statement; increases in their fair value after impairment are recognised directly in equity.

## NOTES TO THE FINANCIAL STATEMENTS

AT 31 DECEMBER 2007

*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 realize the asset and settle the liability simultaneously.

*vi) Investment properties*

Investment properties are investments to earn rental income, for capital appreciation or both. Investment properties are measured initially at cost, including transaction costs. Subsequent to initial recognition, investment properties are stated at fair value, which reflects market conditions at the balance sheet date. Gains or losses arising from changes in the fair values of investment properties are included in the statement of income.

In accordance with AAOIFI, unrealized gains or losses are appropriated to an investment fair value reserve and are transferred to retained earnings only when realised.

*vii) Investment in associate*

An associated company (or associate) is one in which the Bank exercises significant influence (but not control) over its operations, generally accompanying, directly or indirectly, a shareholding of between 20% and 50% of the equity share capital and is accounted for by the equity method.

Under the equity method, the investment in an associate is initially recognised at cost and adjusted thereafter for the post-acquisition change in the Bank's share of net assets of the investor. The Bank recognizes 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.

*viii) 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.

*ix) 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 clients and arranging financing. These fees are recognised when earned, generally on receipt of 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.

## NOTES TO THE FINANCIAL STATEMENTS

AT 31 DECEMBER 2007

**x) Exit income**

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

**xi) Income on due from financial institutions**

Income on due from financial institutions represents income from murabaha and mudaraba 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 90 days or more overdue is excluded from income.

Mudaraba 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.

**xii) Dividends**

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

**xiii) Employees' end of service benefits**

Provision is made for leaving indemnity payable under the Bahraini Labour Law applicable to non-Bahraini employees' 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.

**xiv) Amounts due to financial institutions**

Amounts due to financial institutions are recognised on a time apportioned basis over the period of the contracts based on the principal amounts outstanding and the profit agreed with clients.

**xv) Zakah**

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

**xvi) Taxation**

There is no tax on corporate income in the Kingdom of Bahrain.

**xvii) Cash and cash equivalents**

Cash and cash equivalents comprise cash and balances with banks with original maturities of less than three months.

**xviii) Fiduciary assets**

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

**xix) Proposed dividend**

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

**xx) 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.

**xxi) 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 2007

**3 INVESTMENT BANKING FEES**

	2007 US\$'000	2006 US\$'000
Acquisition, structuring and placement fees	22,776	15,869
Management fees	-	736
Brokerage fees	-	542
	<b>22,776</b>	<b>17,147</b>

**4 INCOME ON DUE FROM FINANCIAL INSTITUTIONS**

	2007 US\$'000	2006 US\$'000
Profit on commodity murabaha	4,293	1,665
Income on investment in mudaraba	14	127
	<b>4,307</b>	<b>1,792</b>

**5 STAFF COSTS**

	2007 US\$'000	2006 US\$'000
Salaries and other staff related costs	6,750	7,243
End of service benefits	167	124
	<b>6,917</b>	<b>7,367</b>

The Bank classifies its expenses based on function and hence the staff cost has been allocated to Business Development, Placement, Post Acquisition and Asset Management functions.

**6 GENERAL AND ADMINISTRATION EXPENSES**

	2007 US\$'000	2006 US\$'000
Rent and maintenance	389	211
Legal and professional	111	384
Printing and advertisement	357	263
Communication	49	91
Shari'ah Supervisory Board	104	56
Directors' remuneration	330	150
Others	760	495
	<b>2,100</b>	<b>1,650</b>

## NOTES TO THE FINANCIAL STATEMENTS

AT 31 DECEMBER 2007

**7 CASH AND BALANCES WITH BANKS**

	2007 US\$'000	2006 US\$'000
Cash on hand	2	1
Balances with banks	3,666	9,249
	<b>3,668</b>	<b>9,250</b>

**8 DUE FROM FINANCIAL INSTITUTIONS**

	2007 US\$'000	2006 US\$'000
Commodity murabaha	211,534	52,328
Less: Deferred income	(138)	(157)
	<b>211,396</b>	<b>52,171</b>
Investments in mudaraba	–	1,302
	<b>211,396</b>	<b>53,473</b>

**9 INVESTMENTS**

	Notes	2007 US\$'000	2006 US\$'000
<b>Carried at fair value through statement of income</b>			
Bahrain Property Fund		560	1,887
<b>Available for sale at fair value</b>			
IIB European Investment Company Limited	9.1	1,654	2,640
<b>Available for sale at cost</b>			
IIB Power Company Limited and Asean Investment Company Limited		–	962
Sahab Al-Khaleej Real Estate Company B.S.C. (c)	9.2	1,565	1,565
IIB Paper Company Limited	9.3	906	906
British Islamic Insurance Holdings Limited	9.4	1,871	1,871
IIB KSA Investments B.S.C. (c)	9.5	1,349	1,466
IIB France Investments Holding B.S.C. (c)	9.6	1,144	1,144
Sabaak Leasing and Investment Company K.S.C.C.	9.7	372	372
IIB Abu Dhabi Properties 1 Limited	9.8	12,556	–
IIB German Property Company Limited	9.9	1,954	–
IIB Steel Company Limited 1	9.10	182	–
IIB UAE Investments Limited	9.11	–	344
		<b>24,113</b>	<b>13,157</b>

## NOTES TO THE FINANCIAL STATEMENTS

AT 31 DECEMBER 2007

- 9.1 The Bank holds an investment in European Islamic Investment Bank Plc ("EIIIB") through a special purpose vehicle incorporated in Cayman Islands (IIB European Investment Company Limited). EIIIB provides investment banking activities, is regulated by the UK Financial Services Authority and was listed in UK's Alternative Investment Market ("AIM") in May 2006.
- 9.2 The Bank holds an investment in Sahab Al- Khaleej Real Estate Company B.S.C. (c) (formerly Housing Development Company B.S.C. (c)) ("the Company") which has been established in Bahrain with the principal objective of developing residential properties. The Company has not yet started its operations.
- 9.3 The Bank holds an investment in Queenex Hygiene Paper Manufacturing Company LLC ("Queenex") through a special purpose vehicle incorporated in Cayman Islands (IIB Paper Company Limited), which was established to hold a 49% stake in Queenex, a tissue paper manufacturing company in the United Arab Emirates. Queenex has not yet started its operations.
- 9.4 British Islamic Insurance Holding Limited ("the Company") is the first independent group of UK companies to provide insurance ("Takaful") products that are wholly Shari'ah compliant under the laws of England and Wales. The Company is under formation.
- 9.5 IIB KSA Investments B.S.C. (c) is a company established in the Kingdom of Bahrain for the purpose of acquiring a 16.3% equity stake in Ewaan International Housing Limited ("EWAAN"). EWAAN is a real estate development company established during the current year in the Kingdom of Saudi Arabia with the primary purpose of focusing on the development and project management of medium to large scale residential projects in the Kingdom of Saudi Arabia.
- 9.6 The Bank holds an investment in INO-Real Estate SAS ("France Company") through a special purpose vehicle incorporated in the Kingdom of Bahrain (IIB France Investments Holding B.S.C. (c)). The France Company was created to acquire, through Shari'ah compliant lease agreements, a portfolio of six real estate commercial properties in France.
- 9.7 Sabaak Leasing and Investment Company K.S.C.C. is incorporated in the State of Kuwait, providing operating and financial leases, as well as new and innovative products under Islamic principles.
- 9.8 The Bank holds an investment in IIB Abu Dhabi Properties 1 Limited, a special purpose vehicle incorporated in Cayman Islands with limited liability.
- 9.9 The Bank holds an investment in a portfolio of three office buildings in Munich, Germany through a special purpose vehicle incorporated in Cayman Islands with limited liability (IIB German Property Company Limited) which was established to invest in the sukuk of German Portfolio Company, which owns the three office buildings in Germany. As the investment was acquired during the year, management do not believe that the cost is substantially different from the fair value.
- 9.10 The Bank holds an investment in Universal Rolling WLL ("UNIROL"), a Bahraini company, through a special purpose vehicle incorporated in Cayman Islands with limited liability (IIB Steel Company Limited 1) which was established to own 35% of UNIROL, which will manufacture steel re-bars.
- 9.11 The Bank holds an investment in IIB UAE Investments Limited, a special purpose vehicle incorporated in Cayman Islands with limited liability. IIB Bay Tower Investment Limited, a subsidiary of IIB UAE Investment Limited, was established to own 65% of Bay Development Properties Limited. During the year, the Bank's holding in IIB UAE Investments Limited has been increased to 26% and as a result this investment has been transferred to "investment in associate" (note 11).

## NOTES TO THE FINANCIAL STATEMENTS

AT 31 DECEMBER 2007

**10 INVESTMENT PROPERTY**

During the year, the Bank sold its investment property amounting to US\$ 4.652 million (2006: Nil) carried at US\$ 3.284 million (2006: US\$ 3.284 million) realising a profit of US\$ 1.368 million (2006: Nil).

**11 INVESTMENT IN ASSOCIATES**

	Notes	2007 US\$'000	2006 US\$'000
Ewaan Capital	11.1	2,667	–
IIB UAE Investments Limited	9.11	9,621	–
		<b>12,288</b>	–

11.1 The Bank has a 20% (2006: Nil) interest 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 2007.

The following table shows the summarized financial information of the Bank's investment in associates:

	2007 US\$'000	2006 US\$'000
<b>Share of associates' balance sheet</b>		
Assets	14,558	–
Liabilities	2,270	–
<b>NET ASSETS</b>	<b>12,288</b>	–
Share of profit of associate	3,177	–

During the year, Bay Development Properties Limited ("the Company") in which IIB UAE Investments Limited owns approximately 65% of the equity, has signed a sale/purchase agreement with a buyer to sell the investment property. Later on, the Company has terminated this sale/purchase agreement on the basis that the buyer has failed to fulfill his contractual obligation. The buyer has commenced a court action against the Company for i) the appointment of a receiver to reserve the property, ii) specific performance of the sale/purchase agreement and iii) the sum of AED 124 million (US\$ 33.8 million), being the amount paid for the plot of land pursuant to the sale/purchase agreement. The management has advised that it is possible, but not probable that the action will succeed and accordingly no provision for any claims has been made in these financial statements.

**12 OTHER ASSETS**

	2007 US\$'000	2006 US\$'000
Receivable from Bay Development Properties Limited	3,384	–
Receivable from IIB France Investments Holding B.S.C. (c)	222	8,569
Receivable from IIB KSA Investments B.S.C. (c)	174	–
Receivable from Ewaan International Housing Limited	134	–
Receivable from Bahrain Property Fund	54	2,060
Receivable from investors	–	3,492
Others	821	475
	<b>4,789</b>	14,596

## NOTES TO THE FINANCIAL STATEMENTS

AT 31 DECEMBER 2007

**13 OTHER LIABILITIES**

	2007 US\$'000	2006 US\$'000
Payable for deals	20,161	122
Payable to investors	15,349	6,629
Accrued expenses	3,174	6,126
Payable to IIB German Property Company Limited	1,989	–
Dividends payable	253	240
	<b>40,926</b>	<b>13,117</b>

**14 EQUITY**

	2007 Number of shares '000	2006 Number of shares '000
<b>AUTHORIZED SHARE CAPITAL</b>		
Ordinary Shares of US\$ 1 each	200,000	200,000

	Number of shares '000	Value US\$'000
<b>ISSUED AND FULLY PAID SHARE CAPITAL</b>		
At 1 January and 31 December 2006	43,000	43,000
Ordinary shares of US\$ 1 issued in cash	66,996	66,996
<b>At 31 December 2007</b>	<b>109,996</b>	<b>109,996</b>

On 30 December 2007, the Bank issued 66.996 million shares at an average price of US\$ 2.077 per share (including share premium and share issue expenses) amounting to US\$ 139.184 million. Share issue expenses of US\$ 0.321 million have been offset against the share issue proceeds.

**TREASURY SHARES**

	Number of shares '000	Value US\$'000
At 1 January 2006	–	–
Purchase of treasury shares during the year	100	113
<b>As at 1 January and 31 December 2007</b>	<b>100</b>	<b>113</b>

**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.

## NOTES TO THE FINANCIAL STATEMENTS

AT 31 DECEMBER 2007

**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.

**INVESTMENT FAIR VALUE RESERVE**

This represents unrealized revaluation gains on investment carried at fair value through statement of income and unrealized revaluation gain on investment property as required by AAOIFI. This reserve is distributable upon value realization, which takes place at the time of actual exit or derecognition.

**15 PROPOSED APPROPRIATIONS**

At 31 December 2007 a cash dividend of US\$ 0.15 per share (totalling US\$10.226 million) has been proposed and will be submitted for formal approval by the shareholders at the Annual General Meeting. For shares issued during the year, the dividend is apportioned based on the period from the date of funds received by the Bank to 31 December 2007.

A cash dividend of US\$0.10 per share (totalling US\$4.290 million) was approved at the 2006 Annual General Meeting and was paid in 2007 following that approval.

**16 CASH AND CASH EQUIVALENTS**

Cash and cash equivalents included in the statement of cash flows include the following balance sheet amounts:

	Notes	2007 US\$'000	2006 US\$'000
Cash and balances with banks	7	3,668	9,250
Due from financial institutions with an original maturity within ninety days	8	211,396	53,473
<b>CASH AND CASH EQUIVALENTS</b>		<b>215,064</b>	<b>62,723</b>

**17 ASSETS UNDER MANAGEMENT**

Total assets under management as at 31 December 2007 were:

	2007 US\$'000	2006 US\$'000
Proprietary	31,491	10,914
Client	311,592	170,756
	<b>343,083</b>	<b>181,670</b>

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.

## NOTES TO THE FINANCIAL STATEMENTS

AT 31 DECEMBER 2007

**18 TRANSACTIONS WITH RELATED PARTIES**

Related parties comprise major shareholders, directors, key management personnel and Shari'ah Supervisory Board of the Bank and entities controlled, jointly controlled or significantly influenced by them and companies where the Bank holds more than 10% of the voting power.

The significant balances with related parties were as follows:

	Shareholders/ directors US\$'000	Others US\$'000	Total 2007 US\$'000	2006 US\$'000
<b>ASSETS</b>				
Investment in Bahrain Property Fund	–	560	560	1,887
Receivable from Bahrain Property Fund	–	54	54	2,060
<b>LIABILITIES</b>				
Payable to Bahrain Property Fund	–	–	–	114
Payable to investors	3,994	–	3,994	1,956

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

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

	Shareholders/ directors US\$'000	Others US\$'000	Total 2007 US\$'000	2006 US\$'000
<b>INCOME</b>				
Investment banking fees	10,227	–	10,227	5,522
Gain on items fair valued through statement of income	–	456	456	36
Dividend income	–	101	101	–
<b>EXPENSES</b>				
Underwriting fees	2,223	–	2,223	–
Directors' remuneration	330	–	330	150
Shari'ah Supervisory Board remuneration	–	104	104	56

Compensation of key management personnel was as follows:

	2007 US\$'000	2006 US\$'000
Short term employee benefits	4,172	5,168
End of service benefits	122	131
	<b>4,294</b>	<b>5,299</b>

## NOTES TO THE FINANCIAL STATEMENTS

AT 31 DECEMBER 2007

**19 COMMITMENTS**

	Notes	2007 US\$'000	2006 US\$'000
Investment related	19.1	20,000	–
Operating lease	19.2	1,390	1,780
		<b>21,390</b>	1,780

19.1 The Bank has committed to pay US\$ 20 million (2006: nil) through its Special Purpose Vehicle to a Bank in Azerbaijan, subject to regulatory approval from the authorities in Azerbaijan.

19.2 At 31 December 2007, the Bank had commitments of non-cancelable operating leases relating to leasehold premises. Of the commitments, US\$ 0.39 million (2006: US\$ 0.39 million) expire within one year and the remaining expire within two to five years.

**20 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 21.3 "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	Total US\$'000
<b>ASSETS</b>					
Cash and balances with banks	3,668	–	3,668	–	3,668
Due from financial institutions	211,396	–	211,396	–	211,396
Investments	–	–	–	24,113	24,113
Investments in associates	–	9,621	9,621	2,667	12,288
Other assets	–	4,789	4,789	–	4,789
Total assets	215,064	14,410	229,474	26,780	256,254
<b>LIABILITIES</b>					
Other liabilities	–	40,926	40,926	–	40,926
Total liabilities	–	40,926	40,926	–	40,926
<b>NET GAP</b>	215,064	(26,516)	188,548	26,780	215,328

## NOTES TO THE FINANCIAL STATEMENTS

AT 31 DECEMBER 2007

The maturity profile of assets and liabilities as at 31 December 2006 based on contractual maturity 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	Total US\$'000
<b>ASSETS</b>					
Cash and balances with banks	9,250	–	9,250	–	9,250
Due from financial institutions	53,473	–	53,473	–	53,473
Investments	–	962	962	12,195	13,157
Investment property	–	3,284	3,284	–	3,284
Other assets	12,536	2,060	14,596	–	14,596
Total assets	75,259	6,306	81,565	12,195	93,760
<b>LIABILITIES</b>					
Due to financial institutions	20,000	–	20,000	–	20,000
Other liabilities	–	13,117	13,117	–	13,117
Total liabilities	20,000	13,117	33,117	–	33,117
<b>NET GAP</b>	55,259	(6,811)	48,448	12,195	60,643

**21 RISK MANAGEMENT****21.1 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'ah Supervisory Board**

The Shari'ah 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'ah, 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.

## NOTES TO THE FINANCIAL STATEMENTS

AT 31 DECEMBER 2007

### **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.

### **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.

## NOTES TO THE FINANCIAL STATEMENTS

AT 31 DECEMBER 2007

**21.2 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 2007 was US\$ 159.3 million (2006: US\$ 17.8 million). Subsequent to the year end, the Bank has received US\$ 156 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 2007 US\$'000	Gross maximum exposure 2006 US\$'000
<b>CREDIT RISK ITEMS</b>			
Balances with banks	7	3,666	9,249
Due from financial institutions	8	211,396	53,473
Other assets – receivables	12	4,789	14,596
<b>Total Credit Risk Exposure</b>		<b>219,851</b>	<b>77,318</b>

- ll) The analysis of the Bank's financial assets having credit risk exposure as at 31 December 2007 is as follows:

	Banking activities US\$'000	Others US\$'000	Total US\$'000
<b>GEOGRAPHICAL REGION</b>			
Bahrain	215,062	1,172	216,234
Other Gulf Cooperation Council (GCC) countries	–	3,597	3,597
Far East & Asia	–	20	20
	<b>215,062</b>	<b>4,789</b>	<b>219,851</b>

The analysis by geographical region of the Bank's financial assets having credit risk exposure as at 31 December 2006 is as follows:

	Banking activities US\$'000	Others US\$'000	Total US\$'000
<b>GEOGRAPHICAL REGION</b>			
Bahrain	62,722	12,857	75,579
Other Gulf Cooperation Council (GCC) countries	–	1,719	1,719
Far East & Asia	–	20	20
	<b>62,722</b>	<b>14,596</b>	<b>77,318</b>

## NOTES TO THE FINANCIAL STATEMENTS

AT 31 DECEMBER 2007

III) The industry sector analysis of the Bank's financial assets having credit risk exposure as at 31 December 2007 is as follows:

	Banking activities US\$'000	Others US\$'000	Total US\$'000
<b>INDUSTRY SECTOR</b>			
Real estate	–	3,968	3,968
Banking and financial institutions	215,062	–	215,062
Others	–	821	821
	<b>215,062</b>	<b>4,789</b>	<b>219,851</b>

The industry sector analysis of the Bank's financial assets having credit risk exposure as at 31 December 2006 is as follows:

	Banking activities US\$'000	Others US\$'000	Total US\$'000
<b>INDUSTRY SECTOR</b>			
Real estate	–	10,629	10,629
Banking and financial institutions	62,722	–	62,722
Others	–	3,967	3,967
	<b>62,722</b>	<b>14,596</b>	<b>77,318</b>

*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 2007 is as follows:

	Banking activities US\$'000	Others US\$'000	Total US\$'000
<b>CREDIT RATING</b>			
A– (by Standard & Poor's)	215,062	–	215,062
Unrated	–	4,789	4,789
	<b>215,062</b>	<b>4,789</b>	<b>219,851</b>

## NOTES TO THE FINANCIAL STATEMENTS

AT 31 DECEMBER 2007

The credit rating analysis of the Bank's financial assets having credit risk exposure as at 31 December 2006 is as follows:

	Banking activities US\$'000	Others US\$'000	Total US\$'000
<b>CREDIT RATING</b>			
A- (by Standard & Poor's)	41,358	-	41,358
Unrated	21,363	14,596	35,959
	62,721	14,596	77,317

**21.3 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.

The table below summarises the maturity profile of the Bank's financial liabilities at 31 December 2007 based on contractual undiscounted repayment obligations. Note 20 (Maturity analysis of assets and liabilities) shows the expected maturities of these liabilities.

Total US\$'000	On Demand	Less than 3 months US\$'000	3 months to 1 year US\$'000	1 to 5 years US\$'000	US\$'000
Other liabilities	-	-	20,061	-	20,061
<b>Total undiscounted financial liabilities</b>	-	-	20,061	-	20,061

The table below summarises the maturity profile of the Bank's financial liabilities at 31 December 2006 based on contractual undiscounted repayment obligations.

Total US\$'000	On Demand	Less than 3 months US\$'000	3 months to 1 year US\$'000	1 to 5 years US\$'000	US\$'000
Due to financial institutions	-	20,052	-	-	20,052
<b>Total undiscounted financial liabilities</b>	-	20,052	-	-	20,052

**21.4 Market risk**

Market risk is the risk to earnings resulting from adverse movements in foreign currency rates, profit rate yield curves and equity prices. The Bank has no significant concentration of market risk and does not trade in investments or foreign currencies. 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 2007, the Bank has an indirect quoted investment in European Islamic Investment Bank Plc listed in the United Kingdom's Alternative Investment Market ("AIM"). Based on the value at 31 December 2007, a change in the quoted price of plus or minus 10% would change the value of this investment by plus or minus US\$ 0.165 million with a corresponding increase or decrease in equity.

## NOTES TO THE FINANCIAL STATEMENTS

AT 31 DECEMBER 2007

Further, a change in the net asset value of plus or minus 10% in Bahrain Property Fund, the Bank's available for sale investment carried at fair value, would change the value of investment by US\$ 0.056 million with a corresponding increase or decrease in equity.

The Bank also has unquoted investments carried at cost where the impact of changes in equity prices will only be reflected in the income statement when the investment is sold or deemed to be impaired or when a third party transaction in the investment gives a reliable indication of fair value, which will be reflected in equity.

**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 resultant positions in these currencies are not considered to represent currency risk. The Bank had the following foreign currency exposures at 31 December 2007:

	Assets US\$'000	Liabilities US\$'000	Net US\$'000
Euro	–	131	131
Pound Sterling	–	5	5
	–	136	136

The Bank had the following foreign currency exposures at 31 December 2006:

	Assets US\$'000	Liabilities US\$'000	Net US\$'000
Euro	5,600	–	5,600
Pound Sterling	3,610	–	3,610
	9,210	–	9,210

## NOTES TO THE FINANCIAL STATEMENTS

AT 31 DECEMBER 2007

*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.

	<b>Change in exchange rate (+/-) %</b>	<b>2007 Effect on net income (+/-) US\$ '000</b>	<b>2006 Effect on net income (+/-) US\$ '000</b>
Euro	<b>10%</b>	<b>13</b>	560
Pound Sterling	<b>10%</b>	<b>1</b>	361

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 2007, a +/- 1% change in the profit rate, with all other variables constant, would have resulted in a +/- US\$ 0.53 million (2006: US\$ 0.37 million) impact on the statement of income.

**22 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.

## NOTES TO THE FINANCIAL STATEMENTS

AT 31 DECEMBER 2007

The Bank's capital adequacy ratio under Basel I, calculated in accordance with the capital adequacy guidelines issued by the Central Bank of Bahrain, is as follows:

	2007 US\$'000	2006 US\$'000
<b>REGULATORY CAPITAL BASE</b>		
Tier 1 capital	<b>206,168</b>	57,446
Tier 2 capital	<b>67</b>	664
Total regulatory capital	<b>206,235</b>	58,110
<b>RISK WEIGHTED ASSETS</b>	<b>84,604</b>	42,706
<b>Tier 1 capital adequacy ratio</b>	<b>244%</b>	135%
<b>Total capital adequacy ratio</b>	<b>244%</b>	136%

Tier 1 capital comprises: share capital; share premium; statutory reserve; foreign currency translation reserve; retained earnings, including current year profit; minority interests less accrued dividends and goodwill. Certain adjustments are made to IFRS based results and reserves, as prescribed by the Central Bank of Bahrain. Tier 2 capital comprises fair value reserves.

The above information is based on the Central Bank of Bahrain prudential returns regulations, applicable as at the balance sheet date.

**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 EVENTS AFTER THE BALANCE SHEET DATE**

The Bank has concluded the structuring of an investment which is awaiting regulatory approval from the country of origin. The Bank expects to realise acquisition, structuring and placement fees of US\$ 5.6 million in 2008 when the required approval is expected to be obtained.

**26 COMPARATIVES**

Certain of the prior year's figures have been reclassified to conform to the presentation adopted in the current year, due to change in the presentation of statement of income which is now based on functions after the nature of expenses.





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