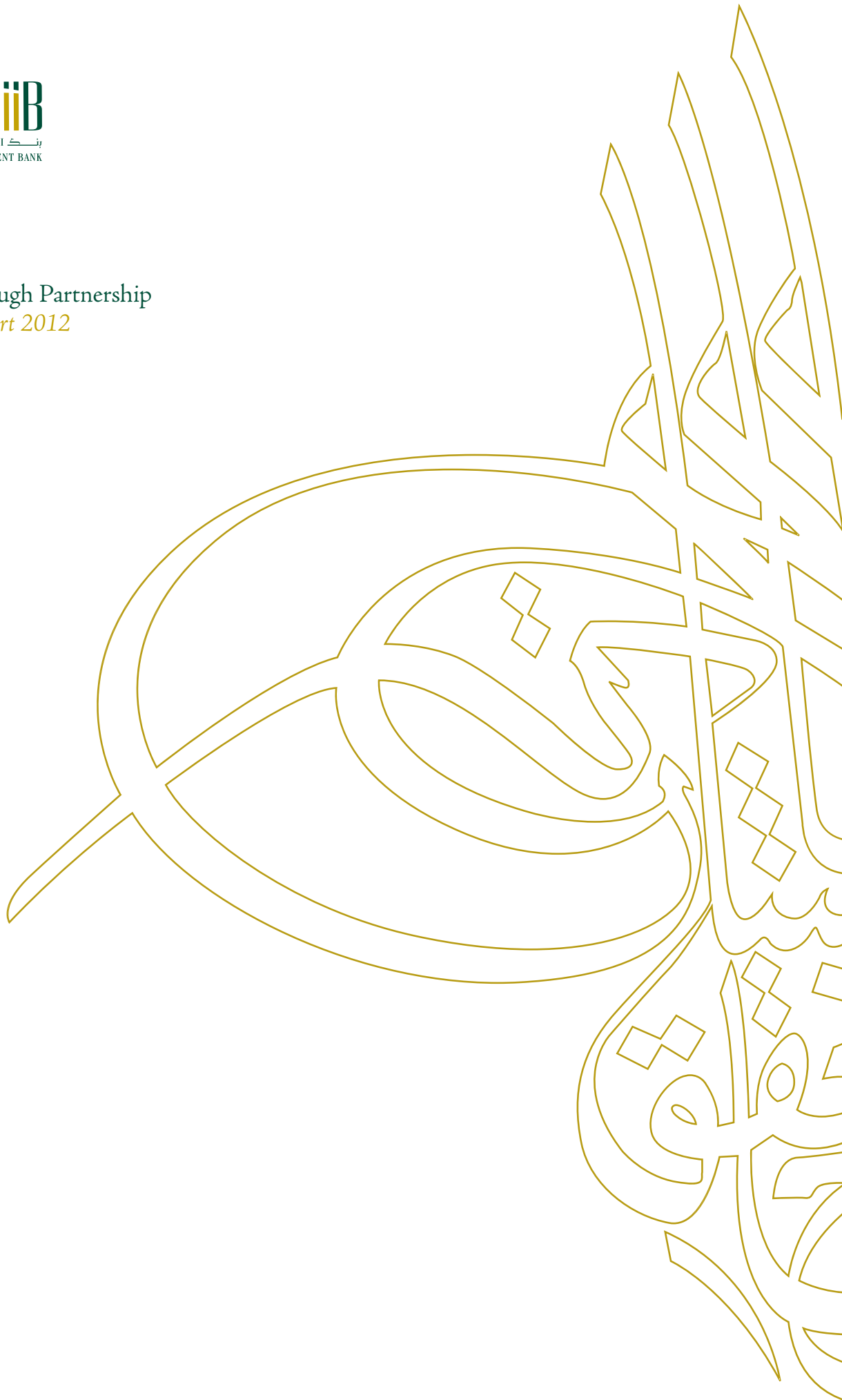




Success through Partnership
Annual Report 2012



2012 Highlights

- For years to come, we will look back upon 2012 as the year we created a compelling new future for IIB. Now and in the future, we have fundamentally re-calibrated our business model. A higher equity capital ratio, along with maintaining our liquidity reserves and leaner risk profile are elements that form a solid foundation for maintaining our stability and building shareholder trust. Trust that is essential for creating value in the long term.

Profile	Financial Summary	Corporate Governance	Annual Reviews	Financial Statements
2 Vision and Mission	4 Five Year Financial Summary 5 Summary of Principal Investment Structurings 2004-2012 6 Board of Directors' Report	10 Corporate Governance 10 Board of Directors	26 Chief Executive Officer's Review of Operations 32 Financial Review 34 Capital Structure 42 Risk Management 49 Organisation Structure 50 Shari'ah Supervisory Board Report	52 Independent Auditors' Report to The Shareholders 53 Consolidated Statement of Financial Position 54 Consolidated Statement of Income 55 Consolidated Statement of Cash Flows 56 Consolidated Statement of Changes In Equity 57 Notes to The Consolidated Financial Statements

14.2

Total Income (US\$ Millions)



8.2

Net Profit (US\$ Millions)



165.3

Total Assets (US\$ Millions)



7.6

Earnings per Share (US Cents)



Profile

International Investment Bank B.S.C. (c) (IIB) was incorporated as an Islamic investment bank on 6 October 2003, under commercial registration number 51867 as a Kingdom of Bahrain Joint Stock Company (closed). Operating under an Islamic wholesale banking license issued by the Central Bank of Bahrain, IIB commenced investment activities on 13 October 2003. IIB has an authorised capital of US\$ 200 million and its paid-up capital was increased during 2007 from US\$ 43 million to US\$ 110 million, through a combined rights issue and private placement issue. The Bank's shareholders are high net worth individuals, business houses and institutions from the GCC states. The core business activities of the Bank include investing on its own account and investment, underwriting and placement in real estate and private equity in conformity with Islamic Shari'ah. It aims to offer its clients an internationally diversified range of investments generated through its network of strategic partnerships.

Vision

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

Mission

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

- 4 Five Year Financial Summary
- 5 Summary of Principal Investment Structurings 2004-2012
- 6 Board of Directors' Report

Financial Summary

- Global confidence from investors in the financial markets were positive in the last quarter of 2012, although IIB will continue to adopt a policy of considered investment in 2013.



Five Year Financial Summary

14.2

Total income (US\$ Millions)

7.8

Operating profit (US\$ Millions)

8.2

Net profit (US\$ Millions)

	2012	2011	2010	2009	2008
Earnings (US\$ millions)					
Total income	14.2	3.1	3.5	6.3	34.9
Total expenses	6.4	5.7	6.7	8.9	16.6
Operating profit (loss)	7.8	(2.6)	(3.2)	(2.6)	18.3
Share of profit (loss) of associate	4.0	(3.4)	-	(0.1)	(4.1)
Impairment losses, provisions and FX	(3.6)	(3.4)	(17.5)	(25.2)	(0.7)
Net profit (loss)	8.2	(9.4)	(20.7)	(27.9)	13.5
Dividend (%) – cumulative 40%	-	-	-	-	7.0

Financial position (US\$ millions)

Total assets	165.3	148.5	160.2	179.5	218.7
Cash and due from financial institutions	35.5	61.5	33.4	57.7	120.5
Investments	106.9	75.9	83.9	68.3	62.9
Due to financial institutions	-	-	-	-	-
Equity	155.0	145.3	158.3	176.5	210.7

Ratios

Profitability

Return on average equity (%)	5.5	(6.2)	(12.4)	(14.4)	6.3
Return on average assets (%)	5.2	(6.1)	(12.2)	(14.0)	5.7
Earnings per share (cents)	7.6	(9)	(19)	(25)	13
Cost-to-income ratio (%)	45.1	183.6	190.3	141.3	47.6

Capital

Capital adequacy ratio (regulatory minimum 12%)	48	54	47	59	87
Equity/total assets (%)	98.0	97.8	98.8	98.3	96.3

Liquidity and other

Investments/total assets (%)	64.7	51.1	52.4	38.1	28.8
Liquid assets/total assets (%)	21.5	41.4	36.9	32.1	55.1
Assets under management (US\$ millions)	324.3	294.8	325.5	422.8	414.0
Number of employees (at year end)	32	33	40	47	50

Summary of Principal Investment Structurings 2004-2012

617.3 **2,386.0** **3,003.3**

Private equity (US\$ Millions)

Other funds (US\$ Millions)

Total transaction size (US\$ Millions)

Year	Investment Description	Location	Private Equity (US\$ millions)	Other Funds # (US\$ millions)	Total Transaction Size (US\$ millions)	
1	2004	Property fund **	Bahrain	18.6	18.5	37.1
2	2004	Independent power producer ***	China	23.0	267.0	290.0
3	2005	Housing development company @	Bahrain	22.6	0.6	23.2
4	2005	Income generating property *	UK	14.8	290.6	305.4
5	2005	Tower development *	Dubai	20.5	73.6	94.1
6	2005	Islamic investment bank	UK	19.8	448.0	467.8
7	2005	Paper manufacturing company	Abu Dhabi	12.0	35.1	47.1
8	2006	Income generating properties	France	50.8	68.7	119.5
9	2006	Real estate development company	Saudi Arabia	21.0	85.8	106.8
10	2006	Office tower development	Dubai	25.0	75.2	100.2
11	2007	Steel reinforcement bar manufacturing plant	Bahrain	13.0	28.4	41.4
12	2007	Income generating properties	Germany	99.3	133.7	233.0
13	2007	Real estate investment company	Saudi Arabia	2.7	10.7	13.4
14	2007/8	Mixed use tower development @	Abu Dhabi	65.0	132.4	197.4
15	2007/8	Commercial bank	Azerbaijan	26.0	20.8	46.8
16	2008	Automobile dealership company	Tunisia	36.0	30.0	66.0
17	2008	Sugar manufacturing company	Bahrain	20.5	136.1	156.6
18	2009/12	Shopping centre / mixed use development	Bosnia	94.0	82.9	176.9
19	2009/12	Affordable housing development	Saudi Arabia	32.7	447.9	480.6
Totals			617.3	2,386.0	3,003.3	

* Realised in 2006; ** Partial exits in 2006, 2007, 2009 with final exit in 2010; *** Realised in 2007; @ Partial exit in 2011 and 2012;

Comprises partners' contributions, borrowings and equity from IPO.

Sector Summary

Sector	Private Equity Raised (US\$ millions)	Other Funds (US\$ millions)	Total Transaction Size (US\$ millions)	
1	Real estate income generating	164.9	493.0	657.9
2	Real estate development	258.2	897.8	1,156.0
3	Private equity	175.6	976.7	1,152.3
4	Property fund	18.6	18.5	37.1
Totals		617.3	2,386.0	3,003.3

Principal Bankers and Professional Advisors

Principal Bankers	Ahli United Bank, Bahrain KFH, Bahrain Al Salam Bank, Bahrain Union National Bank, Abu Dhabi
External Auditors	Ernst & Young, Bahrain
External Legal Counsel	Qays H. Zu'bi, Bahrain

Board of Directors' Report



**Saeed Abdul
Jalil Al Fahim**
Chairman



Dear Shareholders, The Directors of International Investment Bank (IIB) are pleased to present the Annual Report of the Bank together with the Consolidated Financial Statements for the year ended 31 December 2012.

Operational background: an overview of 2012

World Economy

2012 saw the continued contraction of the Eurozone and Japanese economies, with BRIC countries such as Brazil, Russia, China and India also seeing weaker than expected growth.

The risks of a Eurozone collapse had abated slightly by the end of 2012, but the problems have still not been resolved and will continue to dominate Europe's economic and political agenda into 2013. The region's economy remains bleak, with the debt crisis depressing lending, investment and private consumption. Austerity programs in most of the Eurozone countries will also prevent improvement in 2013, and the upcoming Italian and German elections will be some of the largest trials for the region this year.

The growth of the US economy accelerated in the latter part of the year, following the second term win for President Obama, but this growth was complicated in the short term by the eleventh hour 'fiscal cliff' deal and the effect of Hurricane Sandy. Outlooks on the US economy expect it to continue to steadily grow in 2013, despite the headwinds of high household indebtedness, a weak housing market and tight credit conditions.

The Libor Scandal shook regulators around the world, who probed alleged manipulations by large US and European banks of the London Interbank offered rate (Libor) and other key benchmark lending rates. Libor is considered to be one of the most crucial interest rates in finance, underpinning approximately \$350 trillion in derivatives.

Middle East Economy

2012 provided a mixed economic scene for the Middle East and North Africa (MENA) regions. Countries affected by the 'Arab Spring' of 2011 are still facing disruption and low investor confidence, which in turn is holding back their growth. In response to rising unemployment and high inflation, governments in these countries have significantly expanded spending on social subsidies, which are forcing cuts elsewhere. Continued social demands and rising food and fuel prices will mean that economic prospects will likely be sluggish in 2013. As expected, economic outlooks differed for oil-importing and exporting countries. Owing to high oil prices and production, most of the MENA's oil-exporting countries – Kingdom of Bahrain amongst them - grew at healthy rates.

After a decade of debate, Saudi Arabia's mortgage laws were approved in mid 2012. This move has encouraged banks to expand lending and has seen an increase in the middle income housing market.

Kingdom of Bahrain Investment Banking

During 2012 Bahrain's private sector and national economy saw glimpses of recovery from the unrest in 2011. This revitalisation can be credited to government-funded projects and region-wide plans. Examples include the Mumtalakat - Bahrain's investment arm - strategy to increasingly invest at home, and the Gulf Cooperation Council's (GCC) 10-year, US\$ 10billion fund, which will utilise strategic partnerships with the private sector for infrastructure development and services across the Kingdom.

The GCC saw a wave of mergers and acquisitions in 2012, with companies streamlining their operations, and Kingdom of Bahrain was no exception, as the international financial backdrop contracted. Examples include Al Salaam Bank merging with Bahraini Saudi Bank, Ithmaar Bank and First Leasing Bank in the latter part of the year, as did Elaf Bank, Capital Management House and Capinvest.

(Sources: Economic Intelligence Unit, IMF, Financial Times, World Bank)

2013 Forecast

Looking ahead into next year, the overall outlook is one of a depressed global economy with continued regional uncertainty. Worldwide investor confidence in the financial markets will generally remain weak and be aggravated by the continued political instability and social unrest in the MENA region. As these uncertainties continue into a third year, investors will remain cautious, avoiding investments in real estate and private equity the main asset classes offered by the Bank. Investing in cash and liquid assets to avoid risk will remain investor priorities.

With these considerations in mind, it is expected that 2013 will continue to be another challenging year for the investment banking sector. Accordingly, the Board of Directors of IIB will focus on the possible acquisitions of recurring income-generating assets and investments in developing geographical regions.

Financial performance review 2012

2012 saw IIB achieve a net profit of US\$ 8.2 million, compared with 2011's net loss of US\$ 9.4 million. The Bank's total income increased notably by US\$ 11.1 million to US\$ 14.2 million as compared to the same period last year. This was largely due to a gain of US\$ 8.7 million from the sale of assets and investment banking fees of US\$ 3.2 million.

Profits due from financial institutions and receivables reduced from US\$ 1.6 million last year to US\$ 1.2 million in 2012, which was due to lower profit rates in the market and also a lower level of funds placed.

The management continued to streamline operations and retain strict controls over costs in 2012. Total expenses were US\$ 6.4 million in 2012, when compared to US\$ 5.6 million in 2011. This increase was mostly due to expenses associated with acquiring assets and placing investments with investors; such expenses were not incurred in 2011. Operating income was US\$ 7.8 million in 2012 compared to an operating loss of US\$ 2.6 million in the previous year.

The share of profits from associates increased from a loss of US\$ 3.4 million in 2011 to a profit of US\$ 4.0 million in 2012. Impairment losses and provisions increased slightly to US\$ 3.6 million in 2012. These losses are unrealised and may reverse looking ahead, should financial markets recover in the future.

IIB's Capital Adequacy Ratio continues to be strong at 48.2 per cent on 31 December 2012, which is over four times the minimum 12 per cent required by the Central Bank of Bahrain. The Bank follows a prudent approach in managing its capital, which provides the scope to acquire significant future risk assets from a regulatory capital standpoint. Details of the Bank's financial position and performance are provided in the Financial Review section and the Consolidated Financial Statements.

Investments; strategy and outcomes

IIB's investment strategy continues to remain cautious, with stringent criteria requirements having to be fulfilled when evaluating all new investment opportunities. Under these auspices, three new long-term investments were acquired in 2012, costing a total of US\$ 22.9 million. The Bank increased its shareholding in two existing investments for US\$ 3.4 million. Though some investments are currently yielding income, the Board considers that the new investment acquisitions provide an opportunity for capital appreciation over a holding period of 3 to 5 years.

The market slowdown, particularly in Europe and MENA countries, facing political uncertainty, have meant that there were no exits during the year. The Bank continued to actively market the mature investments under its management to potential investors, in order to achieve exits at attractive prices.

“IIB's investment strategy continues to remain cautious, with stringent criteria requirements having to be fulfilled when evaluating all new investment opportunities”.



Investments; offerings and proposals

During 2012, the Bank received and reviewed numerous proposals that constitute the deal "pipeline". However, in keeping with IIB's strategy of only investing in rigorously selected transactions that meet the Bank's strict criteria on risk and reward, no assets were acquired for immediate structuring and sale to investors.

Portfolio; strategy and management

Liquidity enables the Bank to meet its payment obligations when they are due under normal and stress circumstances. IIB monitors future cash flows and the liquidity required for working capital and investment acquisitions on an ongoing basis and maintains significant cash and cash equivalent balances. At year end 2012, the Bank had ample liquid funds as evidenced by 21.5% of total assets represented by cash, bank balances and short-dated Murabaha placements plus a further 4.1% invested in regional listed equities, thereby maintaining 25.6% of the total assets in liquid and semi-liquid form. The majority of IIB's liquidity is held in low-risk murabaha placements with financially sound regional banks and an average tenor of 48 days in 2012.

Since 2007, IIB has relied solely on internal funding through its Shareholders' Equity and consequently has not resorted to any bank borrowings. This conservative policy of funding all assets only from equity has resulted in protecting and strengthening the Bank from any liquidity pressures from lending banks.

Portfolio; value and outcome

The Bank has performed a comprehensive valuation as at 31 December 2012 of all investments made in previous years with the assistance of expert independent valuers and consultants. In line with the International Financial Reporting Standards (IFRS), unrealised gains and losses are reflected in equity except when the investment is determined to be impaired, at which time the cumulative change is included in the Consolidated Statement of Income for the period. Impairment is defined as an unrealised significant or prolonged decline in the fair value below its cost that is unlikely to reverse in the near future. The aggregate net unrealised losses in investments and receivables recognised in equity and the Consolidated Statement of Income moved up to US\$ 1.9 million in 2012 (2011: US\$ 7.0 million), computed and booked in compliance with the relevant valuation rules and accounting standards.

Final remarks

IIB Recommendations; Appropriations and Zakah

The Board has recommended that no dividend will be paid for the year in order to retain its earnings and further strengthen the shareholders' equity to support future growth. As in the previous years, shareholders will directly pay their respective Zakah on their equity investments in the Bank. Using the Net Asset method of computation, the Zakah payable per share for 2012 is US\$ 0.011 (2011: US\$ 0.016).

Board Membership

There were no changes in the membership of the Board of Directors during 2012.

Acknowledgments

The Board of Directors, on behalf of the shareholders, extend their thanks to our executive management team and staff for their dedicated and committed service throughout the year. We also thank the Central Bank of Bahrain and the Ministry of Industry and Commerce for their invaluable support and strategic guidance.

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.
- 

Corporate Governance

Board of Directors

The Board meets regularly throughout the year in order to control strategic, financial, operational, internal control and compliance issues. It currently comprises one Executive Director, three Non-Executive Directors and five Independent Non-Executive Directors. Independent Non-Executive Directors are: Mr. Ahmed Salem Al Bugshan, Mr. Abdulwahab Al Wazzan, Mr. Ali Hashem Sadeq Hashem, Dr. Bader Ibrahim Mohammad Bin Saedan and Mr. Fared Bader.

1.	2.	3.
4.	5.	6.
7.	8.	9.

The Board of Directors comprised the following members as at 31 December 2012



1. H. E. Mr. Saeed Abdul Jalil Al Fahim**Chairman**

Non-Executive Director
 Chairman - Al Fahim Group, UAE; Chairman - Mubarak & Brothers Property & Financial Investment, Abu Dhabi, UAE; Former Board Member - National Bank of Abu Dhabi, Abu Dhabi, UAE; Former Board Member - United Arab Bank, Sharjah, UAE.

2. Mr. Ahmed Salem Bugshan**Vice Chairman and Chairman Nomination & Remuneration Committee**

Independent Non-Executive Director
 Chairman, President and Chief Executive Officer - Saudi Industrial Projects Co. (SIPCO), KSA; Chairman - Saudi Steel Profile Mfg. Co. Ltd., KSA; Director - Savoy Hotel, Sharm El Sheikh, Egypt; Board Member - Tirana Tourism Investment Co., Cairo, Egypt; Chairman - Westville Group, UK; Chairman - BMC Al-Mahdar Co, Yemen.

3. Mr. Abdulwahab Al Wazzan**Chairman Audit & Corporate Governance Committee**

Independent Non-Executive Director
 Vice Chairman and Board Member - National International Holding Company, Kuwait; Second Vice Chairman - Kuwait Chamber of Commerce & Industry, Kuwait; Board Member - Kuwait Petroleum Corporation, Kuwait; Former Chairman - Kuwait Real Estate Bank (Kuwait International Bank), Kuwait.

4. Mr. Rashed Abdul Jalil Al Fahim**Chairman Executive Committee and Member Nomination & Remuneration Committee**

Non-Executive Director
 Managing Director - Al Fahim Group, UAE; Director and Audit Committee Member - Arkan Building Materials, UAE; Director - Big Bus Company, London, UK; Director - Emirates Float Glass, UAE; Director - Ras Al Khaimah Cement Company, UAE; Director - Marjan Lighting Systems, UAE; Director - Dubai Pearl, UAE.

5. Mr. Ali Hashem Sadeq Hashem**Member Nomination & Remuneration Committee and Member Executive Committee**

Independent Non-Executive Director
 Chairman - Gulf Manufacturers, Egypt; Chairman - Rawasi Al Khaleej, Sharjah, UAE; Chairman - Tahweel Industries Co., UAE; Vice Chairman & CEO - Gulf Packaging Systems Co. Ltd., KSA; Vice Chairman & CEO - Prime Plastic Products, KSA; Vice Chairman & CEO - 3P Stretch Co., KSA; Vice Chairman & CEO - 3P Pipe Co., KSA; Director - Arabian Gulf Manufacturers, KSA; Director - Safra Co. Ltd., KSA; Shareholder - Jeddah Graphic, KSA; Shareholder - Tahweel Integrated Co. Ltd. KSA.

6. Dr. Bader Ibrahim Mohammad Bin Saedan**Member Executive Committee**

Independent Non-Executive Director
 CEO & Board Member - Al Saedan Real Estate Company, KSA; Chairman of the Board of Directors - Saudi Maintenance Made Simple, KSA; Chairman - Curzon Asset Management, UK; Director - Tunisian Saudi Real Estate Co., Tunisia; Director - Mawten R.E., KSA; Director - Real Estate Committee in the Chamber of Commerce and Industry, Riyadh, KSA; Member - Saudi Council of Engineers, KSA; Member - Young Arab Leaders, KSA; Member - Prince Salman Center for Social Affairs, KSA; Member - General Assembly of the Charitable Society for Orphans, KSA.

7. Mr. Ali Haider Suliman Al Haider**Member Audit & Corporate Governance Committee**

Non-Executive Director
 Vice Chairman - Suliman & Brothers Co W.L.L., Qatar; Vice Chairman - Salam Bounian, Qatar; Board Member - Salam International, Qatar; Board Member - Al Safa Trading Company, Qatar

8. Mr. Fareed Bader**Member Audit & Corporate Governance Committee and Member Executive Committee**

Independent Non-Executive Director
 Chairman & Managing Director - Bader Group of Companies, Bahrain; Chairman - Wafa IEI Middle East Property Investment, Bahrain; Chairman - Gulf Membrane and Coating Industries, Bahrain; Chairman - Star Gate Telecommunications, Bahrain; Chairman - Group 7 Security, Bahrain; Vice Chairman - Universe Environment Bahrain B.S.C., Bahrain; Board Member - Rotary Club Manama, Bahrain; Board Member - Bahrain Italian Association, Bahrain; Member - Bahrain British Forum, Bahrain; Member - Bahrain French Forum, Bahrain; Member - Bahrain Engineering Society, Bahrain; Member - Bahrain Chamber of Commerce and Industry, Bahrain.

9. Mr. Aabed Al-Zeera**Chief Executive Officer**

Executive Director
 Deputy Chairman - European Islamic Investment Bank Plc, UK; Vice Chairman - AmrahBank, Azerbaijan; Vice Chairman - Queenex Hygiene Paper Manufacturing Co., UAE; Director & Member Audit Committee - Artes S.A., Tunisia; Vice Chairman - Arabian Sugar Company B.S.C., Bahrain; Director - Universal Rolling W.L.L., Bahrain; Director - Ewaan Global Residential Company, KSA; Director - Connection Real Estate LLC, UAE.

Board Terms and Start Date of Current Term

All the current members of the Board of Directors were appointed on 30 March 2011. They hold their office for a term of three years.

Induction, Orientation and Training of New Directors

The Chairman of the Board ensures that each newly inducted director receives a formal and tailored induction to ensure his contribution to the Board from the beginning of his term. The induction process includes:

- a. Meetings with senior management;
- b. Visits to the Bank facilities;
- c. Presentations regarding strategic plans;
- d. Significant financial, accounting and risk management issues;
- e. Compliance programs;
- f. Meeting with internal, external auditors and legal counsel (as required); and
- g. Familiarisation of the Corporate Governance Guidelines

Written Code of Ethics and Business Conduct

The Bank has documented Code of Ethics and Business Conduct applicable to the Directors.

Election System of Director

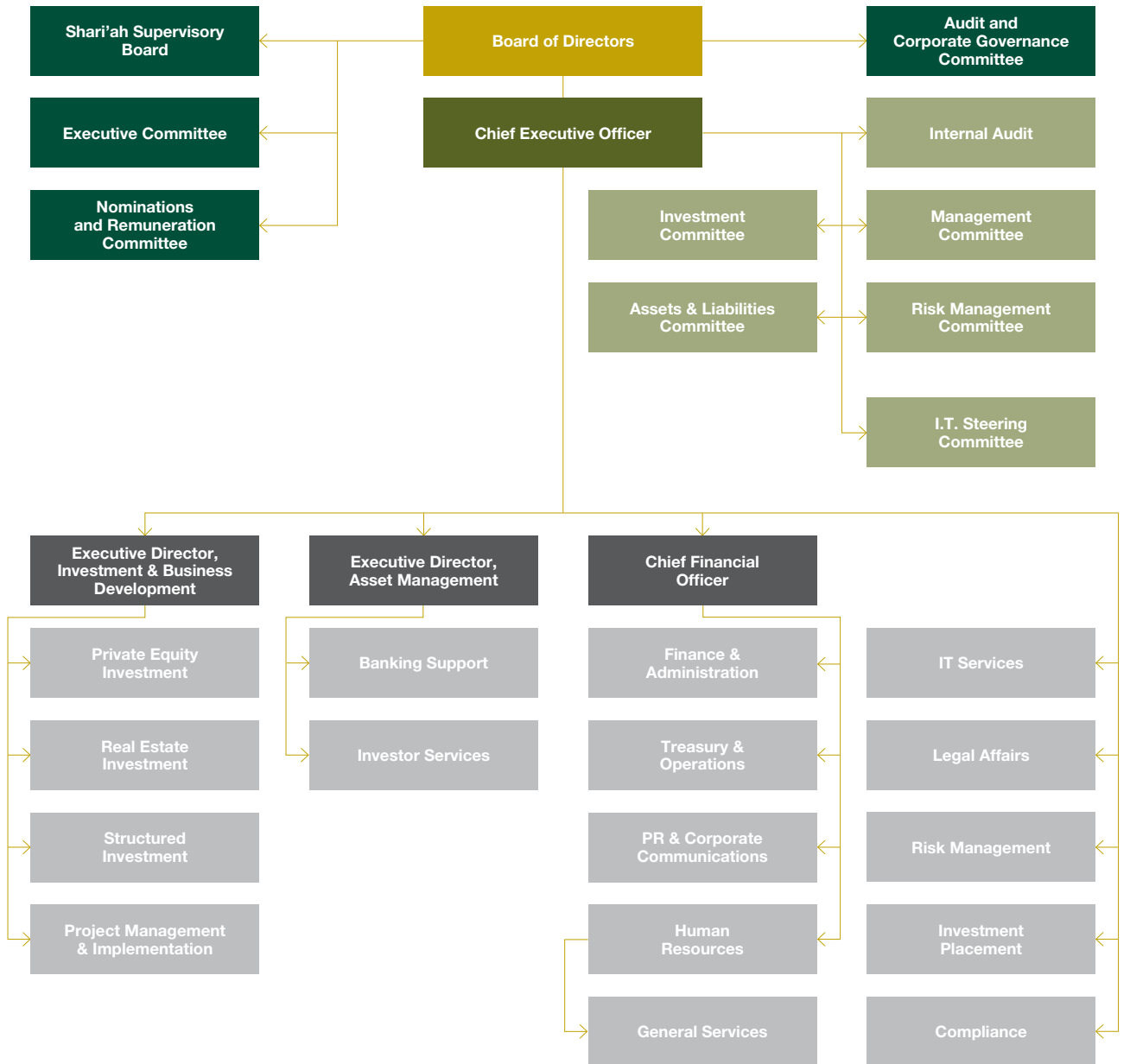
The new members are inducted to the Board of Directors through a nomination process. The new members are nominated by the Board who are later ratified/approved by the General Meeting of the Bank.

Material Transactions that Require Board Approval

Every investment and every funds transfer of US\$ 50 million or above require the approval of the Board of Directors.

The Bank makes effective use of Internal and External Auditors and the Senior Management have put in place appropriate systems and controls. The Audit and Corporate Governance Committee exercises oversight over the audit functions and disclosures.

Organisational Structure



Board of Directors' Meetings

The Board of Directors of the Bank meet at least four times in a year either in person or via teleconference or video conference.

Compliance with HC Module

The Bank monitors the compliance with the provisions of the High-Level Controls (H.C.) Module of the Rule book issued by the Central Bank of Bahrain on an ongoing basis on the roles and responsibilities of the Board of Directors, Board Committees and of the principles relating to Disclosure Requirements and Management Strategy. The Bank has complied with the HC module and amendments.

Directors' responsibility for AFS

The Board is responsible for causing the audited consolidated financial statements (AFS) to be prepared which accurately disclose the Bank's financial position. Although the Board has delegated the Audit and Corporate Governance Committee to ensure this objective is met, it has not delegated its ultimate responsibility for the consolidated financial statements. The Bank makes effective use of Internal and External Auditors and the Senior Management have put in place appropriate systems and controls. The Audit and Corporate Governance Committee exercises oversight over the audit functions and disclosures. The Audit and Corporate Governance Committee reviews the quarterly and the annual consolidated financial statements and the Board approves them.

Board of Directors' meetings and attendances during 2012

DATE	NAMES OF DIRECTORS ATTENDED IN PERSON OR VIA TELE/VIDEO CONFERENCE	NAMES OF DIRECTORS NOT ATTENDED
5-Mar-12	H. E. Mr. Saeed Abdul Jalil Al Fahim - Chairman Mr. Ahmed Salem Bugshan - Vice Chairman Mr. Rashed A. Jalil Al Fahim Mr. Ali Hashem Sadeq Hashem Dr. Bader Ibrahim Mohammad Bin Saedan Mr. Ali Haider Al Haider Mr. Abdulwahab Al Wazzan Mr. Fareed Bader Mr. Aabed Al-Zeera - CEO	
12-April-12	H. E. Mr. Saeed Abdul Jalil Al Fahim - Chairman Mr. Ahmed Salem Bugshan - Vice Chairman Mr. Rashed A. Jalil Al Fahim Mr. Ali Hashem Sadeq Hashem Mr. Ali Haider Al Haider Mr. Abdulwahab Al Wazzan Mr. Aabed Al-Zeera - CEO	Mr. Fareed Bader Dr. Bader Ibrahim Mohammad Bin Saedan
10-Oct-12	H. E. Mr. Saeed Abdul Jalil Al Fahim - Chairman Mr. Ahmed Salem Bugshan, Vice Chairman Mr. Ali Hashem Sadeq Hashem Dr. Bader Ibrahim Mohammad Bin Saedan Mr. Ali Haider Al Haider Mr. Abdulwahab Al Wazzan Mr. Fareed Bader Mr. Aabed Al-Zeera - CEO	Mr. Rashed Abdul Jalil Al Fahim
26-Dec-12	Mr. Ahmed Salem Bugshan - Vice Chairman Mr. Rashed A. Jalil Al Fahim Mr. Ali Hashem Sadeq Hashem Dr. Bader Ibrahim Mohammad Bin Saedan Mr. Ali Haider Al Haider Mr. Abdulwahab Al Wazzan Mr. Fareed Bader Mr. Aabed Al-Zeera - CEO	H. E. Mr. Saeed Abdul Jalil Al Fahim - Chairman

Board Committees

The Board has established four sub-committees and a Shari'ah Supervisory Board comprising expert, independent scholars, to assist the Board in expeditiously and effectively discharging its responsibilities. This committee structure ensures appropriate oversight by the Board of Directors while permitting efficient day-to-day management of the Bank. The members as at 31 December 2012 and summary terms of reference are as follows:

Executive Committee

Mr. Rashed Abdul Jalil Al Fahim (Chairman)
Mr. Ali Hashem Sadeq Hashem, Member
Dr. Bader Ibrahim Mohammad Bin Saedan, Member
Mr. Fareed Bader, Member

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

Executive Committees' meetings and attendances during 2012

DATE	NAMES OF DIRECTORS PRESENT	NAMES OF DIRECTORS NOT PRESENT
11-April-12	Mr. Rashed Abdul Jalil Al Fahim, Chairman Mr. Fareed Bader Mr. Ali Hashem Sadeq Hashem	Dr. Bader Ibrahim Mohammad Bin Saedan
20-Jun-12	Mr. Rashed Abdul Jalil Al Fahim, Chairman Mr. Fareed Bader Mr. Ali Hashem Sadeq Hashem	Dr. Bader Ibrahim Mohammad Bin Saedan
26-Jun-12	Dr. Bader Ibrahim Mohammad Bin Saedan Mr. Fareed Bader Mr. Ali Hashem Sadeq Hashem	Mr. Rashed Abdul Jalil Al Fahim, Chairman
20-Nov-12	Mr. Rashed Abdul Jalil Al Fahim, Chairman Dr. Bader Ibrahim Mohammad Bin Saedan Mr. Fareed Bader Mr. Ali Hashem Sadeq Hashem	
13-Dec-12	Mr. Rashed Abdul Jalil Al Fahim, Chairman Dr. Bader Ibrahim Mohammad Bin Saedan Mr. Fareed Bader Mr. Ali Hashem Sadeq Hashem	
25-Dec-12	Mr. Rashed Abdul Jalil Al Fahim, Chairman Dr. Bader Ibrahim Mohammad Bin Saedan Mr. Fareed Bader Mr. Ali Hashem Sadeq Hashem	

Audit and Corporate Governance Committee

Mr. Abdulwahab Al Wazzan (Chairman)
 Mr. Ali Haider Al Haider, Member
 Mr. Fareed Bader, Member

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

Audit and Corporate Governance Committee meetings during 2012

DATE	NAMES OF DIRECTORS ATTENDED IN PERSON OR VIA TELE/VIDEO CONFERENCE	NAMES OF DIRECTORS NOT ATTENDED
1-Mar-12	Mr. Abdulwahab Al Wazzan, Chairman Mr. Fareed Bader, Member Mr. Ali Haider Al Haider, Member	
10-May-12	Mr. Abdulwahab Al Wazzan, Chairman Mr. Fareed Bader, Member Mr. Ali Haider Al Haider, Member	
25-July-12	Mr. Abdulwahab Al Wazzan, Chairman Mr. Fareed Bader, Member, Mr. Ali Haider Al Haider, Member	
15-Oct-12	Mr. Abdulwahab Al Wazzan, Chairman Mr. Fareed Bader, Member Mr. Ali Haider Al Haider, Member	



Nominations and Remunerations Committee

Mr. Ahmed Salem Bugshan (Chairman)
Mr. Rashed Abdul Jalil Al Fahim, Member
Mr. Ali Hashem Sadeq Hashem, Member

Assists the Board in assessing candidates and recommending Board and management appointments, as well as to establish and update the remuneration policies and procedures including the level of remuneration paid to executive management.

The following table shows date and attendance details of the Nominations and Remuneration Committee meeting during the year.

Meeting Date: 9 October 2012

Mr. Ahmed Salem Bugshan, Chairman
Mr. Rashed Abdul Jalil Al Fahim
Mr. Ali Hashem Sadeq Hashem

Independent Shari'ah Supervisory Board

Being an Islamic Bank, IIB's Shari'ah Supervisory Board regularly reviews all investment products and business activities to ensure compliance with Islamic Shari'ah principles, it approves the Bank's financial statements and participates with management in the development of suitable investment products and services. IIB's Shari'ah Supervisory Board comprises three prominent GCC Islamic scholars who provide the Bank with pragmatic Islamic opinions. Brief biographies are as follows:

Sheikh Nizam Yaquby

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

Sheikh Osama Mohammed Saad Bahar

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

Sh. Abdul Nasser Omar Al Mahmood

Sh. Abdul Nasser is a member of the Islamic supervisory board of International Investment Bank and Bahrain Development Bank and is a senior manager in Shari'ah audit department at Khaleeji Commercial Bank. He holds a Masters in Business Administration from the Gulf University working on a thesis in Shari'ah control and review in Islamic banks. He also holds a Bachelors degree in Shari'ah and Islamic Studies from Qatar University.

Direct Investment and Business Development

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

Asset Management

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

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

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

Investment Placement

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

Support, Administration and Internal Controls

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

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

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

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

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

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

Compensation and Incentive Structures

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

At least two individuals are involved in each transaction, including two signatories on every funds transfer. Each transfer is approved and executed in accordance with "Levels of Authority" approved by the Board of Directors.

Executive Management

Management Committees

The Board has established five management committees, namely the Management Committee, Investment Committee, Risk Management Committee, Assets and 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 utilisation, IT, investment purchase/sale and management of all types of risk, including market, credit, liquidity and operational risks. The members as at 31 December 2012 and the summary terms of reference are as follows:

Management Committee

Mr. Aabed Al-Zeera (Chairman)
Mr. Michael Ross-McCall, Member
Mr. Narayanan Ganapathy, Member
Mr. Fadi Al Qassim, Member
Mr. Alyas Al Meftah, Member

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

Investment Committee

Mr. Aabed Al-Zeera (Chairman)
Mr. Fadi Al Qassim, Member
Mr. Alyas Al Meftah, Member
Mr. Narayanan Ganapathy, Member

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

Assets and Liabilities Committee

Mr. Narayanan Ganapathy (Chairman)
Mr. Michael Ross-McCall, Member
Mr. Ninan Varkey, Member
Ms. Haleema Ebrahim, Member
Mr. Fadi Al-Qassim, Member

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



Risk Management Committee

Mr. Michael Ross-McCall (Chairman)
Mr. Murtaza Ghulam, Member
Mr. Ninan Varkey, Member
Mr. Narayanan Ganapathy, Member

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

I.T. Steering Committee

Mr. Michael Ross-McCall (Chairman)
Mr. Murtaza Ghulam, Member
Mr. Said Itani, Member
Mr. Narayanan Ganapathy, Member

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

Chairman and Executive Managers**H.E. Saeed Abdul Jalil Al Fahim, Chairman**

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

Aabed Al-Zeera, Chief Executive Officer

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

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

Michael Ross-McCall, Chief Financial Officer

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

Narayanan Ganapathy, Director

Mr. Ganapathy is acting head of the Direct Investment and Business Development Department. He is a CFA charter holder, a member of the Institute of Chartered Accountants of India and holds a Master's degree in Finance from London Business School. He has over twelve years of international banking and corporate finance experience that he gained at KPMG, Deutsche Bank, London and Investate Realty in Bahrain.

Other Senior Officers**Alyas Al-Meftah, Director, Asset Placement**

Mr. Al-Meftah heads IIB's Asset Placement activity with particular emphasis on the western province of Saudi Arabia. Holding a degree in Business Administration and International Studies, he has held progressively more senior positions with international organisations over the last ten years. In particular, he was Sales Territory Manager with a leading logistics company as well as Marketing Manager with one of the region's leading real estate development projects. He joined IIB in 2005.

Ali Redha, Director, Internal Audit

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

Fadi Al-Qassim, Director, Direct Investment

Mr Al Qassim is a Director in Direct Investment and Business Development Department. He holds a B.Sc. in Civil Engineering from the University of Bahrain. He has 17 years' experience in civil design, engineering and monitoring projects up to the hand-over to owners. He is a certified ISO 9000:2000 internal auditor and an active member of both the Bahrain Society of Engineers and the Project Management Institute. He joined IIB in 2006.

Ninan Varkey, Head – Risk Management

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

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.

**Charitable Contributions**

The Bank made contributions and donations to Bahraini charities in 2012 aggregating to US\$ nil (2011: US\$ 50,000).

Non-Sharia Income

Any income derived from any investment or business that does not conform to the Sharia principles is considered as Non-Sharia Income. Such Non-Sharia Income is not recognised as the income of the Bank. If any such income arises in the course of the business, it is contributed to charity through Charitable Institutions.

For the year 2012, there was no Non-Sharia income for the Bank.

Review of Internal Control Process and Procedures

The Board is fully aware that the system of internal control cannot totally eliminate the risk of failure to achieve business objectives, and can only provide reasonable and not absolute assurance against material misstatement or loss.

The Board confirms that there is an on-going process of managing significant risks faced by the Bank and reviewing the system of internal control for the year under review. The key elements are described below:

- Formal organisation structure that clearly defines the framework for the line of reporting and hierarchy of authority.
- Policies and Procedures Manual on key activities that lay down the objective, scope, policies and operating procedures for the Bank which are subject to regular review and improvement.
- Regular internal audit visits to departments within the Bank to ensure compliance with Bank's Policies and Procedures and to review effectiveness of internal control systems.
- Clearly defined authorisation limits at appropriate levels are set out for controlling and approving capital expenditure and expenses.
- Regular Senior Management meetings are held to discuss and resolve major issues arising from business operations.
- Quarterly meetings for Audit and Corporate Governance Committee and the Board are held to discuss internal audit reports, periodic financial statements and issues that warrant Audit and Corporate Governance Committee and Board attention.

In respect of risk management framework, a Risk Management Committee was established, to evaluate, monitor and manage the risks that may impede the achievements of the Bank's business objectives.

A number of minor internal control weaknesses were identified during the year of review. None of the weaknesses have resulted in any material losses, contingencies or uncertainties.

Nature and approval process of related party transactions

The balance with related parties mainly comprises investments in associates. These associates are the companies where the Bank holds 20% or more of the share capital by way of direct investment or investment through Special Purpose Vehicles in its ordinary course of business. Such investments also go through the same approval processes as required for all investments of the Bank. Transactions with related parties in 2012 mainly comprise of share of loss from associates and remuneration paid to the Sharia'a Supervisory board.

Changes in Organisation Structure

There were no changes to the Organisation Structure of the Bank during the year.

Ownership Details of the Bank

Distribution of ownership by country

COUNTRY	NUMBER OF SHAREHOLDERS	NUMBER OF SHARES	PERCENTAGE
Kingdom of Bahrain	7	2,406,158	2.19%
State of Kuwait	39	16,452,201	14.96%
State of Qatar	11	6,931,862	6.30%
Kingdom of Saudi Arabia	34	28,882,213	26.26%
United Arab Emirates	19	52,323,363	47.57%
Total	110	106,995,797	97.28%
Treasury shares		3,000,000	2.72%
Overall Total	110	109,995,797	100.00%

Distribution of ownership by directors and senior managers

NAME	POSITION	NUMBER OF SHARES	PERCENTAGE
Saeed A. Jalil Al Fahim	Chairman	26,374,704	23.98%
Rashid A. Jalil Al Fahim	Board Member	-	0.00%
Ahmed Salem Bugshan	Board Member	3,908,404	3.55%
Ali Hashem Sadeq Hashem	Board Member	3,908,404	3.55%
Bader Ibrahim Mohammad Bin Saedan	Board Member	1,650,000	1.50%
Ali Haider Al Haider	Board Member	1,627,907	1.48%
Abdulwahab Al Wazzan	Board Member	813,953	0.74%
Fareeda G. Bader	Board Member	350,000	0.32%
Aabed Al Zeera	Board Member	162,791	0.15%
Overall Total		38,796,163	35.27%

Distribution of ownership by size of shareholding

SHAREHOLDING SIZE	NUMBER OF SHAREHOLDERS	NUMBER OF SHARES	PERCENTAGE
Above 5% ownership	1	26,374,704	23.98%
Less than 5% ownership	109	83,621,093	76.02%
Overall Total	110	109,995,797	100.00%

There was no trading in the Bank's shares by Directors and senior managers of the Bank during the year.
There are no shareholdings in the Bank by the Bahrain Government or other Governments.





Inquiries are made to the relevant departments as follows:

- **Investments and partnerships:**
invest@iib-bahrain.com
- **Existing Investors inquiries:**
portfolio@iib-bahrain.com
- **New investors:** placement@iib-bahrain.com
- **Financials and annual performance:**
enquiries@iib-bahrain.com

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

Remuneration to Board Members

The remuneration paid to Board members for the year 2012 was US\$ 63,000 (2011: nil).

Fees paid to External Auditors

Audit fee paid to the external auditors for the year 2012, including quarterly reviews of interim financial statements, was US\$ 86,207. Other fees paid to the external auditors for non-audit services including asset valuation reviews, quarterly review of prudential returns, PD disclosure reviews etc. for the year 2012 amounted to US\$ 86,074.

Communications Strategy

A summary of the Bank's quarterly and annual financial statements is published in local and regional newspapers. The Bank maintains a website www.iib-bahrain.com, which contains the last five years of annual financial data as at 31 December, together with summary financial data covering the interim quarterly financial statements. It also contains a profile of the Bank, details of the principal products and services, profiles of the senior managers and regular press releases concerning investment transactions and other developments.

Additional Governance Controls

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

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

Annual Reviews

- During 2012, the Bank recorded a net profit of US\$ 8.2 million, compared to a net loss of US\$ 9.4 million during 2011. Total assets at year-end 2012 aggregated to US\$ 165.3 million and included cash and cash equivalents of US\$ 35.5 million. Total equity at 31 December 2012 was US\$ 161.9 million. Assets under management at the end of 2012 amounted to US\$ 324.3 million.
- 

Chief Executive Officer's Review of Operations



Aabed Al-Zeera
Chief Executive
Officer



The financial services industry has witnessed an unprecedented series of setbacks in the recent past causing certain economies to experience recession, and in some cases a double or even a triple dip recession.

As compared to 2011, the global and regional economies generally experienced lower or negative growth in 2012. Against this rather uncertain, volatile and cautious economic environment, I am very pleased to report that IIB, after three challenging years of wading through losses, has demonstrated a strong perseverance of its strategy by returning to profitability in 2012. In addition, with a view to laying a strong foundation for the coming years, the Bank made five investments during the year costing US\$ 26.3 million, three of which were on new assets, with the remaining two being purchases of additional shares in the Bank's previous investments. The Bank has continued to focus on judicious use of risk capital, while striving to generate an acceptable return to its shareholders; as well as intensive management of existing assets to ensure that future risks and potential losses are minimised leading to optimum returns at the time of exit.

Business Development

With a generally low to medium level of risk tolerance, the Bank continues to focus on its 'tried and tested' investment philosophy of being highly selective and conservative. Accordingly, the Bank seeks to deploy its capital on profitable income producing private equity and real estate opportunities with strong operational history and a potential for capital growth. In 2012, the Business Development team has reviewed several investment proposals across asset classes and regions, and has concluded three investments during this period totaling US\$ 22.9 million.

The Bank participated in a joint venture with another financial institution in Bahrain, which acquired a 49% equity stake in Hungry Bunny, a fast food chain based in Saudi Arabia. The management believes that the overall growth in the fast food sector in Saudi Arabia, coupled with the Bank's strategic contribution to the company, creates enormous potential to generate a high return on investment, through regular dividends as well as potential value appreciation. The Bank also participated in an income generating deal within the aircraft leasing space in order to create a steady stream of revenue over the coming two to three years. With a high quality lessee and a long duration lease, the investment generates a 9% per annum cash yield, thereby contributing positively to the financial performance of the Bank. With a view to diversifying the investment portfolio, the Bank also acquired an indirect 10% equity stake in Leeds United Football Club (LUFC), an English Football club playing in the Championship, a second tier of the English Football league system. This investment is a "value play" with a high return potential should LUFC get promoted to Premier League.

The Bank's strategy, of maintaining enough liquidity to be able to undertake compelling investment opportunities, has already shown positive signs as the Bank has been able to "pick and choose" the right mix of investments for the year 2012.

Investment Placement

Investment Placement, by definition, is an adjunct to Business Development initiatives of the Bank. Accordingly, with no new investments having been undertaken in 2011 and 2012 with the objective of structuring and offering for sale to investors, there were no investment placements during the year, except for a partial placement of the Bank's investment in the Jeddah Project as described in the paragraph below.

Jeddah Project

This project comprises affordable housing units, commercial space and service amenities, over an area of approximately 1 million square meters strategically located north of Jeddah in the Dhahban district in the Kingdom of Saudi Arabia. The investment dynamics of the Jeddah project continue to be strong and with the project progressing well, the investment was partially sold to investors in the fourth quarter of 2012 with the remainder expected to be sold during the first half of 2013.

Sarajevo Project

The Bank also has the Sarajevo Project in the pipeline which will be due for placement shortly. This project comprises the construction of a real estate complex involving a hotel tower, a commercial office tower, a shopping mall and an entertainment center in Sarajevo, the capital of Bosnia & Herzegovina (Eastern Europe). The construction of the project has gained significant

momentum with part of the construction expected to be completed by the fourth quarter of 2013. Subject to market conditions, we believe that the investment will be ready for placement with select investors during the fourth quarter of 2013, when significant value enhancing initiatives currently underway come to fruition and investors' sentiments are expected to improve.

Asset Management

The Asset Management Department of the Bank has continued its detailed monitoring and management of the investment portfolio on behalf of its investors and the Bank. The Bank has a fiduciary duty to carefully monitor and manage the portfolio of investments for the benefit of the investors with the objective of improving performance and positioning the assets for eventual exit.

The current focus of the Asset Management Department is on improving the operational metrics for each investment in order to achieve value enhancement and maximise exit proceeds. This strategy is a byproduct of our thesis, that equity value growth in the private equity and real estate asset class is now substantially a function of operational growth. With the change in the investment landscape resulting from the adverse impact of the financial crisis, the previous sources of value growth, such as asset leverage and growth of exit multiples, are unlikely to contribute significantly to value accretion in the near term. The Bank believes that there are some investments which may be ripe for exits, and the Asset Management Department is in constant discussions with market players in order to achieve appropriate valuations for those investments.

Financial Performance

A detailed analysis is provided in the Financial Review section. Total income in 2012 increased by US\$ 11.1 million to US\$ 14.2 million as compared with 2011. In addition, the Bank earned net profit from associates of US\$ 4.0 million versus a US\$ 3.4 million loss in 2011. The two main contributors to this significant improvement in 2012 were: structuring and placement fees of US\$ 2.6 million earned from the rights issue completed by a Bahrain-based investee company; and secondly gains of US\$ 8.7 million from the sale by an associate located in the Kingdom of Saudi Arabia of its assets and liabilities to a property fund. The operating profit improved from a loss of US\$ 2.6 million last year to a profit of US\$ 7.8 million in 2012. Impairment losses and provisions of US\$ 3.5 million were similar to the US\$ 3.4 million expense booked in 2011, derived from the rigorous year-end valuation process applied to all investments and other assets in accordance with the regulatory and accounting rules. The provisions are unrealised and may reverse should market values improve. The net profit for 2012 was US\$ 8.2 million.

Additionally, the Bank's core liquidity position continued to be strong throughout the year with liquid assets at year end 2012 representing 25.6% of total assets, of which 21.5% is in cash and cash equivalents. The ample liquidity and the absence of any borrowings make the balance sheet of IIB very strong and well positioned to capture opportunities that are expected to arise from the future recovery in the markets.

Information Technology

The Bank's Information Technology (IT) Department is responsible for providing IT infrastructure and communications systems in the most efficient and cost-effective manner in order to satisfy the requirements of its users. During 2012, a detailed review was performed by independent expert consultants and a number of low and medium risk recommendations were addressed. These included the download and installation of the latest operating system for network equipment, the installation of Windows updates and the updating of certain network components.

Disaster Recovery Centre (DRC)

The annual testing of DRC readiness was successfully completed by the Bank's key staff to ensure that all required basic systems will be available to use in case the Head Office is not available or the IT systems located there become non-operative. The DRC is governed by the business continuity plan and disaster recovery plan, which are regularly updated and approved by IIB's Board of Directors.

Legal Department

The existing controls were further strengthened during 2012 by the adoption of a Governance Framework covering all the Bank's special purpose vehicles, associates and subsidiaries. Following approval of IIB's Board of Directors, the new policy introduces formal enhanced corporate governance and accountability, including high standards for internal control, ethical practices, transparency and external reporting.

Compliance Department

The compliance function was enhanced in 2012 by the appointment of a full-time Compliance Officer who reports functionally to the Chairman of the Audit and Corporate Governance Committee. The Department identifies, assesses, advises, monitors, reports and educates on the Bank's compliance risk in order to ensure complete conformity to all applicable regulatory / legal rules and regulations at all times, in accordance with the Board-approved Compliance Manual and related checklists. In addition, commencing from 2013, the Department intends to introduce ongoing testing using a risk-based approach, to ensure that all departments are in compliance with the Compliance Manual.



Dhahban, Saudi Arabia.

Al Fareeda Residential Fund

Project Summary

IIB has a stake in the Al Fareeda Residential Fund, a unique opportunity in Saudi Arabia. The Al Fareeda Fund is a Shari'ah compliant closed-ended collective investment scheme established in accordance with the Investment Funds Regulations and other related regulations issued by the Capital Market Authority (CMA).

A one million square metre project, the Al Fareeda Residential Community Project is located 20 km north of Jeddah in Dhahban. Al Fareeda aims to create an advanced residential environment with integrated services that meet requirements and affordability for middle-income Saudi nationals.

The investment dynamics of the Jeddah project continue to be strong and with the project progressing well, the investment was partially sold to investors in the fourth quarter of 2012 with the remainder expected to be sold during the first half of 2013.

Spotlight on the Project

The Al Fareeda Residential Community Project is a fully integrated residential community comprising of 2088 villas and accommodating more than 10,000 people.

The Project will provide all necessary facilities including retail outlets, as well as a wide range of community facilities, comprising of mosques, schools, community centers, health centers and recreational spaces. The project is only a 15 minute drive from King Abdul Aziz International Airport, and 20 minutes from landmark Hera Street.

The Project, being developed by Ewaan Global Residential Company (EGRC), is well positioned to meet the expectations of middle-income Saudis for an advanced residential environment with integrated services.

Significant progress has taken place relating to construction of the Project. Construction of Zone 1 villas will be completed by end of Q2 2013 and Zone 2 villas will be completed by end of Q4 2013. Furthermore, Zone 3 villa construction has also started.

Spotlight on the Project Company

Ewaan Al Fareeda LLC, a Saudi Arabian real estate project development company, was established for the purpose of developing the Al Fareeda Residential Community Project. Board members comprise of the representatives of the shareholders who are the Islamic Corporation for the Development of the Private Sector (ICD) with 49.51%; Ewaan Global Residential Company (EGRC) with 23.53% and (IAF) with 26.96%.

The Fund has acquired a 100% of the Project from Ewaan Al Fareeda LLC, with expected returns being realised through the sale of residential units over the duration of the project.



Al Fareeda aims to create an advanced residential environment with integrated services that meet requirements and affordability for middle-income Saudi nationals.



Dubai, United Arab Emirates.

Emirates Airline Leasing

Project Summary

IIB recognises that the aerospace industry, particularly in the Middle East, is expected to produce positive results in upcoming years. Statistics show that global airline traffic is expected to grow at 5.1% per year, and Middle East airline traffic growth is projected to be at 6.6% a year. Furthermore, the Middle East is expected to account for 22% of the large airplane market over the next 20 years. And 33,500 planes valued at \$40 trillion are expected to be globally delivered in the next two decades, reflecting 3.6% annual growth in the global airplane fleet size.

The aircraft leasing industry is on the growth trend with the percentage of global fleet owned by operating lessors increasing from 18% to 30% over 1990-2005 period and potentially rising to 40% over the next decade. This expansion of the aircraft leasing market is largely due to the entry of several financial institutions in this industry. GECAS & ILFC are the two largest lessors in the market with a fleet of 1,755 and 1,031 respectively.

Spotlight on the Offering

In 2012 IIB opened up the opportunity to invest in the aerospace industry. IIB's participation is in an income generating deal within the aircraft leasing space, in order to create a steady stream of revenue over the coming two to three years. With a high quality lessee, Emirates Airline, and a long duration lease, the investment generates a 9% per annum cash yield, thereby contributing positively to the financial performance of the Bank.

Spotlight on the Project

The most popular 777 model, the Boeing 777-300ER, will be leased in this project, given its excellent performance. The aircraft, mostly used for long haul air transportation seats 360 passengers, and has a large twin engine aircraft with engines manufactured by General Electric (GE).

The aircraft was delivered to Emirates Airlines (EA) on a non-cancellable lease of 12 years which is renewable (at EA's option) for additional 3 years. Emirates revenue generation is geographically diversified with revenue from 6 continents, with no region contributing more than 30% of overall revenue.



Saudi Arabia, Kingdom of Bahrain, State of Kuwait and Sultanate of Oman.

Hungry Bunny

Project Summary

IIB, together with Tharawat Investment House (Tharawat) - a Bahrain-based Islamic investment house specialised in providing and management of alternative investment business – acquired a 49% stake in one of Saudi Arabia's top fast food chains.

The Hungry Bunny brand, which is owned by the Saudi businessman Mr. Mohamed bin Husain Al Dosary, is registered in the US, European Union, Middle East and the GCC states. The chain owns 38 branches which operate throughout Saudi Arabia, Kingdom of Bahrain, State of Kuwait and Sultanate of Oman under worldwide franchise agreements.

Hungry Bunny employs around 500 people of various nationalities and utilises advanced technologies, with 2012 sales totaling more than SR 52 million giving an 18% net profit margin in that year.

Investment Strategy

The management believes that the overall growth in the fast food sector in Saudi Arabia, coupled with the bank's strategic contribution to the company, creates enormous potential to generate a high return on investment, through regular dividends as well as potential value appreciation.

Hungry Bunny is currently building a high-tech facility using the latest European technological standards for processing different kinds of meat to be fully dedicated for its own brand and to serve other shopping centers.

Mr. Mohamed bin Husain Al Dosary, the owner of the remaining 51% of the Hungry Bunny restaurant chain, has previously expressed his optimism following the success of the acquisition with the involvement of IIB and Tharawat. It is anticipated that the experience and knowledge behind these two financial institutions will ensure that great expertise is used to take Hungry Bunny to a larger investor base through a public offering (IPO) on the Saudi stock market during the next four years.



Hungry Bunny employs around 500 people of various nationalities and utilises advanced technologies, with 2012 sales totaling more than SR 52 million giving an 18% net profit margin in that year.

Leeds United Football Club Partial Acquisition

Project Summary

The English Championship Football League has been a lucrative investment opportunity for business tycoons, oil barons and royal family members the world over, including the US, Russia, Kuwait, India and Brazil. IIB is aiming to capitalise on the favorable returns being seen by the league's success stories such as Vincent Tan (Cardiff City) and Nottingham Forrest (Al Hasawi Family), and has acquired a 10% stake in Leeds United Football Club (LUFC).

LUFC is a club which has held high positions and three winning spots in the Championship League – and as of April 2013 sits 11th in the table. LUFC has recovered from the financial difficulties which plagued its owner Ken Bates and his consortium of investors, until a restructuring saw it be successful in a plan to pay off its debt at a discounted rate. The club is based at Elland Road in Beeston Leeds, UK, and has seen a committed local following since its establishment in 1919.

Investment Strategy

The investment opportunity was introduced to IIB by Gulf Finance House (GFH) after its purchase of the club in December 2012. GFH exclusively own 90% of LUFC through its Dubai-based investment arm GFH-Capital, and are currently in talks with other regional players to participate in the investment. IIB has made a capital injection of £ 2.5 million against this acquisition.

IIB believes that GFH's plan to restructure the financial operations of the club and take on other strategic investors will make the club more sustainable and an attractive investment opportunity for IIB's shareholders in the future. Indeed since GFH's ownership, fans have already seen a reduction in match ticket prices, the introduction of half season tickets and a reduction in cost of season tickets for 2013-14. IIB anticipates capital appreciation over the medium-term, therefore we are currently taking the approach to hold the 10% investment in its portfolio, with a consideration to offer it once the club's financial position is solidified.



Leeds, England.



Sarajevo City Centre

Project Summary

A partnership between IIB and Saudi-based business group specialising in construction, Al Shiddi Group, the Sarajevo City Centre Project is shortly due for placement.

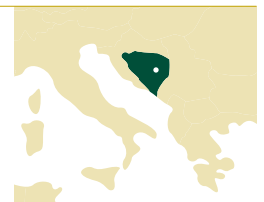
The project comprises the construction of a real estate complex involving a hotel tower, a commercial office tower, a shopping mall and an entertainment center in Sarajevo, the capital of Bosnia & Herzegovina (Eastern Europe).

The construction of the project has gained significant momentum with part of the construction expected to be completed by the fourth quarter of 2013. Subject to market conditions, IIB believe that the investment will be ready for placement with select investors during the fourth quarter of 2013, when significant value enhancing initiatives currently underway come to fruition and investor sentiment is expected to improve.

Spotlight on Sarajevo City Centre

The Sarajevo City Centre real estate project recently reached 60% total completion. The project is a unique hybrid complex comprising several main interconnecting features. The main building is a shopping mall and an entertainment complex with 5 levels that cover an area of 49,500 square meters. There is considerable interest from potential lessees with Letters of Interest received for 100% of the mall space.

The project also contains two towers, the first of which is a commercial complex that covers 6,500 square meters. The second tower will house a 5-star hotel with 224 rooms covering an area of 13,900 square meters. The hotel will be managed by Shaza Hotels, a sharia-based hotel operator located in Dubai.



Sarajevo, Bosnia and Herzegovina.

Financial Review

During 2012, the Bank recorded a net profit of US\$ 8.2 million, compared to a net loss of US\$ 9.4 million during 2011. Total assets at year-end 2012 aggregated to US\$ 165.3 million and included cash and cash equivalents of US\$ 35.5 million. Total equity at 31 December 2012 was US\$ 161.9 million. Assets under management at the end of 2012 amounted to US\$ 324.3 million.

The Capital Adequacy Ratio at 31 December 2012 was 48% versus the minimum permitted by the Central Bank of Bahrain of 12%. The significantly higher level of capital adequacy is consistent with the strategy of prudence and provides ample scope for future investments from a regulatory standpoint.

Income

The Bank's total income for 2012 was US\$ 14.2 million compared with US\$ 3.1 million in 2011 and mainly comprised investment banking fees together with a gain on conversion of an associate.

Investment banking fees in 2012 of US\$ 3.2 million (2011: US\$ 0.6 million) were generated from the structuring, underwriting and placement of two investments (US\$ 2.7 million), plus management fees earned on several prior year transactions (US\$ 0.5 million).

Income on due from financial and other institutions, being the profit on commodity murabaha deposits, was US\$ 1.2 million versus US\$ 1.6 million in 2011, reflecting a lower average profit rate and lower average funds available for placement.

Gain on sale of investments of US\$ 0.5 million arose from the sale of two investments during 2012. Gain on conversion of associate to investment at fair value through equity of US\$ 8.7 million (2011: US\$ nil) arose from the sale by an associate of its net assets and liabilities to a real estate fund in the Kingdom of Saudi Arabia.

Income from investment in real estate (net) in 2012 of US\$ 0.2 million was derived from a residential tower purchased in April 2010 and located in Manama, Kingdom of Bahrain.

Dividend income in 2012 of US\$ 0.14 million (2011: US\$ 0.13 million) was received from both IIB's investee companies and a MENA-listed equity. Other income of US\$ 0.05 million arose from gains on the sale of surplus equipment, while the total in 2011 of US\$ 0.6 million mainly comprised the profit on a short-term financing provided to a non-related third party that was fully repaid in 2011.

Share of Profit (loss) from Associates

In 2011 the Bank consolidated two subsidiaries through which investments were made in real estate development projects in the Kingdom of Saudi Arabia as well as in Bosnia. Since then, share of profit/(loss) in the associate companies in which the subsidiaries have invested together with a third associate company has been booked in IIB's Consolidated Income Statements. Total share of gains in associates in 2012 was US\$ 4.0 million compared to a loss of US\$ 3.4 million in 2011.

Expenses

Total expenses in 2012 aggregated to US\$ 6.4 million, an increase of US\$ 0.8 million (14.3%) compared to 2011. This increase arose mainly from higher deal-related costs (including travel, legal and professional) relating to due diligence and other acquisition costs for the new investments acquired during 2012 and due diligence costs associated with "pipeline" potential purchases in 2013, plus costs relating to the structuring and sale of investments. However, reductions in basic staff, depreciation, IT and occupancy expenses were achieved in 2012 as compared with the previous year.

Impairment Losses and Provisions

IIB booked unrealised impairment losses and provisions in 2012 in the Consolidated Statement of Income of US\$ 3.6 million (2011: US\$ 3.3 million) in respect of three quoted investments and three unquoted investments. As a measure of prudence against possible future losses, the Bank has made specific provisions of US\$ 0.7 million (2011: US\$ 0.9 million) against the Murabaha facility to, and management fees receivable from, an investee company located in the Kingdom of Bahrain.

Assets

Cash and cash equivalents at year-end 2012 were US\$ 35.5 million and represented 21.5% of total assets. These comprised cash, balances with banks and due from financial institutions (including placements by a subsidiary of US\$ 18.0 million) comprising commodity murabaha placements with financially sound banks rated BBB+ or higher and located in the GCC region. With the addition of investments in quoted equities, liquid assets aggregated to US\$ 42.3 million or 25.6% of total assets.

Receivables at 31 December 2012 of US\$ 22.1 million mainly comprised a US\$ 12.2 million receivable by a subsidiary from a fund manager in the Kingdom of Saudi Arabia against sale of units in the fund belonging to the subsidiary; short-term Shari'ah-compliant financing facilities of US\$ 7.2 million (net of provisions) granted to two investee companies to assist with working capital requirements; management fees receivable from investee companies; and other receivables from investee companies.

Total investments at 2012 year end increased by US\$ 31.0 million (40.8%) since 31 December 2011 to US\$ 106.9 million. The Bank made five investments in 2012 valued at US\$ 31.6 million at year end 2012, located in the GCC region and in Europe. In addition, there were net unrealised fair value losses in 2012 on listed equities of US\$ 1.8 million (2011: US\$ 4.5 million) and net unrealised gains on unquoted investments of US\$ 0.1 million (2011: net fair value loss of US\$ 1.6 million).

Investment in associates at the end of 2012 of US\$ 43.9 million (2011: US\$ 54.0 million) comprised four investments - three were located in the GCC region and one was located in Europe. The reduction of US\$ 10.1 million was mainly due to the partial sale during 2012 of investment in an associate in the Kingdom of Saudi Arabia.

Reflecting the purchases in 2012, total assets under management increased to US\$ 324.3 million from US\$ 294.8 million last year.

Liabilities and Equity

There were no borrowings at the year end and no reverse murabaha liabilities classified as due to financial institutions since January 2007. Other liabilities of US\$ 3.4 million (2011: US\$ 1.7 million) mainly comprised accrued expenses, payables to investors and payables to suppliers.

Owners' equity increased by US\$ 9.7 million to US\$ 155.0 million at the 2012 year end. The increase comprised of the net profit for the year of US\$ 8.2 million (2011: net loss US\$ 9.4 million) plus the net gain from movements in fair values and foreign currency translation in 2012 on investments of US\$ 1.5 million taken directly into equity.

The Bank's total income for 2012 was US\$ 14.2 million compared with US\$ 3.1 million in 2011 and mainly comprised investment banking fees together with a gain on conversion of an associate.

Capital Structure

1. Capital Base

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

The issued and paid up share capital of the Bank was US\$ 109,996 thousand at 31 December 2011 and 2012, comprising of 109,996 thousand shares of US\$ 1 each.

The Bank's regulatory capital base of US\$ 127.5 million as at 31 December 2012 (31 December 2011: US\$ 129.5 million) comprised Tier 1 capital of US\$ 143.6 million (31 December 2011: US\$ 137.3 million) and Tier 2 capital of negative US\$ 16.1 million (31 December 2011: negative US\$ 7.8 million) as disclosed in Note 20 of the attached Consolidated Financial Statements.

There have been no changes to the capital structures during the year.

There are no restrictions in distributing profits by the subsidiaries of the Bank. However, such distribution should go through the legal and regulatory channels applicable in each jurisdiction. Mobilisation of capital, reserves and equivalent funds out of the subsidiaries to the parent is subject to the local rules and regulations. The parent is not subject to any restriction to support its subsidiary in the form of deposits or capital.

2. Capital Adequacy

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

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

As compared to the minimum capital adequacy ratio (CAR) of 12% prescribed by the Central Bank of Bahrain (CBB), the Bank's ratio at year-end 2012 was 48.18% (2011: 53.54%), being over four times the minimum ratio of 12%.

The ratio is derived from guidelines issued by CBB which are compatible with the "Basel II" Accord issued by the Basel Committee on Banking Supervision. The CAR measures total qualifying capital held by an institution in relation to its risk-weighted assets. In common with other banks incorporated in the Kingdom of Bahrain, the Bank commenced the ongoing measurement of its capital adequacy under the "Basel II" rules from 1 January 2008. Please refer to Note 20 Capital Management in the attached Consolidated Financial Statements.

Given the Capital Adequacy Ratio of the Bank as at 31 December 2012, it has ample capacity to record additional investments and still meet the minimum capital adequacy requirement of 12%. However, it plans to continue its conservative approach to liquidity and only modest investment purchases are planned for 2013.

3. Profile of Risk-weighted Assets and Capital Charge

The Bank has adopted the "Standardised" approach for credit risk and market risk and "Basic Indicator" approach for operational risk for regulatory reporting purposes. IIB's risk-weighted capital requirement for credit, market and operational risks as at 31 December 2012 are shown below.

4. Credit Risk

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

Cash and balances with banks and due from financial institutions

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

Receivables

Receivables have a risk weighting of 100%. These include funding provided to an unrated entity on a corporate murabaha basis that is repayable within 12 months.

Investments including assets held for sale and investment in associate

Investments listed on a recognised stock exchange attract a risk weighting of 100%. Unlisted investments have a 150% risk weighting and holdings of real estate are assigned a risk weighting of 200%.

Credit exposure and risk weighted assets considered for Capital Adequacy Ratio calculations comprising of banking book exposures are as follows:

As at 31 December 2012	Gross credit exposure US\$'000	Credit risk weighted assets US\$'000	Capital requirement US\$'000
Claims on banks - murabaha placements	17,565	7,393	924
Due from investee companies - murabaha	18,908	18,908	2,364
Equity investments - publicly held	8,184	8,184	1,023
Equity investments - privately held	29,941	44,912	5,614
Holding of real estate	40,607	81,212	10,152
Other assets	15,643	15,643	1,955
Total	130,848	176,252	22,032
As at 31 December 2011			
Claims on banks - murabaha placements	50,878	10,955	1,369
Due from investee companies - murabaha	7,292	7,292	912
Equity investments - publicly held	8,463	8,463	1,058
Equity investments - privately held	877	1,315	164
Holding of real estate	59,925	119,849	14,981
Other assets	3,822	3,822	478
Total	131,257	151,696	18,962

4. Credit Risk (continued)

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

The realised gains net of losses arising from investment sales or liquidations or buy back of shares by investee companies during the year ended 31 December 2012 were US\$ 0.54 million (2011: US\$ 0.02 million). The total net unrealised gains recognised in equity in 2012 aggregated to US\$ 1.47 million (2011: net losses US\$ 3.67 million).

Risk concentrations of the maximum exposure to credit risk

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

	Gross credit exposure 2012 US\$'000	Gross credit exposure 2011 US\$'000
CREDIT RISK ITEMS		
Murabaha with financial institutions	28,089	60,764
Murabaha with corporates	7,192	7,273
Investments	106,907	75,945
Other assets	23,086	4,521
Total Credit Risk Exposure	165,274	148,503

The above disclosure is considered to be reasonably representative of the level of credit risk of the Bank during the year, as there has been no significant fluctuation in the credit risk assets during the year ended 31 December 2012.



4.1 Distribution of the Gross Funded Exposures

(a) Geographical distribution of the gross funded exposures

The following table summarises the geographical distribution of exposure broken down into significant areas by major types of credit exposure:

	Murabaha with financial institutions US\$'000	Murabaha with corporates US\$'000	Murabaha with individual US\$'000	Investments US\$'000	Other assets US\$'000	Total US\$'000
As at 31 December 2012						
GEOGRAPHICAL REGION						
Kingdom of Bahrain	17,965	1,492	-	16,733	9,367	45,557
Europe	-	5,700	-	32,903	861	39,464
Other GCC countries	10,124	-	-	55,318	12,568	78,010
Africa	-	-	-	1,437	65	1,502
Asia	-	-	-	516	225	741
Total	28,089	7,192	-	106,907	23,086	165,274

As at 31 December 2011

GEOGRAPHICAL REGION

Kingdom of Bahrain	60,764	1,590	-	5,609	3,335	71,298
Europe	-	5,683	-	29,790	725	36,198
Other GCC countries	-	-	-	38,676	236	38,912
Africa	-	-	-	1,355	77	1,432
Asia	-	-	-	515	148	663
Total	60,764	7,273	-	75,945	4,521	148,503

(b) Industrial distribution of the gross funded exposures

The following table summarises the industrial distribution of funded exposure broken down by major types of credit exposures:

	Murabaha with financial institutions US\$'000	Murabaha with corporates US\$'000	Murabaha with individual US\$'000	Investments US\$'000	Other assets US\$'000	Total US\$'000
As at 31 December 2012						
INDUSTRY SECTOR						
Real estate-development	-	-	-	56,543	12,540	69,083
Real estate-income generating	-	5,700	-	8,878	683	15,261
Banking and financial institutions	28,089	-	-	3,248	7,683	39,020
Insurance	-	-	-	-	131	131
Manufacturing	-	1,492	-	8,608	1,216	11,316
Automotive	-	-	-	1,437	65	1,502
Others	-	-	-	28,193	768	28,961
Total	28,089	7,192	-	106,907	23,086	165,274

4.1 Distribution of the Gross Funded Exposures (continued)**(b) Industrial distribution of the gross funded exposures** (continued)

	Murabaha with financial institutions US\$'000	Murabaha with corporates US\$'000	Murabaha with individual US\$'000	Investments US\$'000	Other assets US\$'000	Total US\$'000
As at 31 December 2011						
INDUSTRY SECTOR						
Real estate-development		-	-	57,629	214	57,843
Real estate-income generating	-	5,683	-	8,709	703	15,095
Banking and financial institutions	60,764	-	-	1,233	845	62,842
Insurance	-	-	-	-	-	-
Manufacturing	-	1,590	-	7,019	1,399	10,008
Automotive	-	-	-	1,355	77	1,432
Others	-	-	-	-	1,283	1,283
Total	60,764	7,273	-	75,945	4,521	148,503

4.2 Single Counterparty Exposures

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

The Bank's exposure in excess of 15% of the obligor limit to individual counterparties based on regulatory "total available capital" at 31 December 2012 is shown below:

	2012			2011		
	C.A.R Limit (15%) US\$'000	On balance sheet exposure US\$'000	Capital deduction US\$'000	C.A.R Limit (15%) US\$'000	On balance sheet exposure US\$'000	Capital deduction US\$'000
Counterparty A	24,166	57,029	(32,863)	21,929	35,838	(13,909)
Counterparty B	24,166	24,956	(790)	21,929	24,737	(2,808)
Total			(33,653)			(16,717)

Capital deduction is equally deducted from Tier 1 and Tier 2.
There were no off-balance sheet exposures (2011:nil)

Protection against excessive credit risk is through country, industry and counterparty threshold limits. Single name concentrations are monitored on an individual basis.

4.3 Aging of Financial Assets

	Neither past due nor impaired US\$'000	Past due but not impaired US\$'000	Past due and individually impaired US\$'000	Total US\$'000
As at 31 December 2012				
Balances with banks	7,442	-	-	7,442
Due from financial institutions	28,089	-	-	28,089
Receivables	13,815	-	8,254	22,069
Other assets	110	-	-	110
Total	49,456	-	8,254	57,710
As at 31 December 2011				
Balances with banks	695	-	-	695
Due from financial institutions	60,764	-	-	60,764
Receivables	1,072	-	8,754	9,826
Other assets	222	-	-	222
Total	62,753	-	8,754	71,507

Past due and individually impaired are overdues of more than 1 year but less than 3 years. Past due and individually impaired are exposures to manufacturing, real estate, banking and financial institutions located in the Kingdom of Bahrain, Europe and Asia amounting to US\$ 2,383 thousand, US\$ 5,700 thousand and US\$ 171 thousand respectively.



5. Market Risk

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

	2012		2011	
	Risk weighted assets	Period end capital requirement	Risk weighted assets	Period end capital requirement
	US\$'000	US\$'000	US\$'000	US\$'000
Foreign exchange risk	38,925	4,866	34,538	4,317

The Bank has no exposure to profit rate risk, equity position risk or options risk, as the Bank does not maintain any trading book.

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.

	2012 Assets/ liabilities net US\$'000	2011 Assets/ liabilities net US\$'000
Euro	32,434	31,863
Pound Sterling	4,527	731
Others	1,964	1,944
Market risk weighted exposure	38,925	34,538

The Bank has no exposure to profit rate risk, equity position risk or options risk, as the Bank does not maintain any trading book.

6. Operational Risk

In accordance with the Basic Indicator approach methodology, operational risk and related capital requirements are as follows:

	2012 US\$'000	2008 US\$'000	2007 US\$'000
Total gross income	14,569	30,122	34,275

	2012 US\$'000	2011 US\$'000
INDICATOR OF OPERATIONAL RISK		
Average gross income multiply by number of years	26,322	29,651
Eligible portion for the purpose of calculation	15%	15%
Multiplier	12.5	12.5
Operational risk weighted exposure	49,354	55,596
Capital requirement (12.5%)	6,169	6,950

The operational risk has been calculated by the Bank by considering the total gross income of the years in which it has earned gross profits. Since the Bank suffered gross losses during the years 2009 to 2011, therefore those have been excluded from the calculation of operational risk.



Risk Management

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

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

The various risks to which the Bank is exposed and the principal risk management techniques are summarised below. Further information on risk management is contained in Note 19 to the Consolidated Financial Statements.

1. Credit Risk

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. The principle business of the Bank is Investment Banking. The process of managing the credit risk starts at the origination of the investment activity and compliance with investment criteria, guidelines and policies. The Bank manages credit risk by setting limits for individual counterparties, countries, regions and industry sectors. Limits are authorised by the Board of Directors based on management's recommendations, monitored by the Risk Management Department and reviewed regularly by the Risk Management Committee. Details of maximum exposure to credit risk by balance sheet components, geographical region, industry sector and credit rating are contained in Note 19.2 to the Consolidated Financial Statements in accordance with the requirements of IFRS 7.

Information disclosed in the annual report in respect of geographical region, industry sector and credit rating is prepared in accordance with the requirement of Prudential Information Report for Islamic Banks as at 31 December 2012. The disclosures are considered to be reasonably representative of the position during 2012 as there has been no significant fluctuation in the level of credit risk assets.

1.1 Credit Risk Concentrations and Thresholds

Protection against excessive credit risk is through country, industry and counterparty threshold limits. Single name concentrations are monitored on an individual basis. Under the CBB's single obligor regulations, banks incorporated in the Kingdom of Bahrain are required to obtain the CBB's approval for any planned exposure to a single counterparty exceeding 15% of the capital base. Individual exposures are described at Capital Structure section 4.

1.2 Excessive Risk Concentration

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

1.3 Geographical Distribution of Exposures

The geographical distribution of exposures, impaired assets and the related impairment provisions as at 31 December 2012 are analysed as follows:

	Gross funded credit exposure US\$'000	Impaired assets US\$'000	Provision against impaired assets US\$'000
Kingdom of Bahrain	45,557	3,973	1,590
Europe	39,464	10,210	4,510
Other Gulf Cooperation Council (GCC) countries	78,010	-	-
Africa	1,502	-	-
Asia	741	242	71
Total	165,274	14,425	6,171

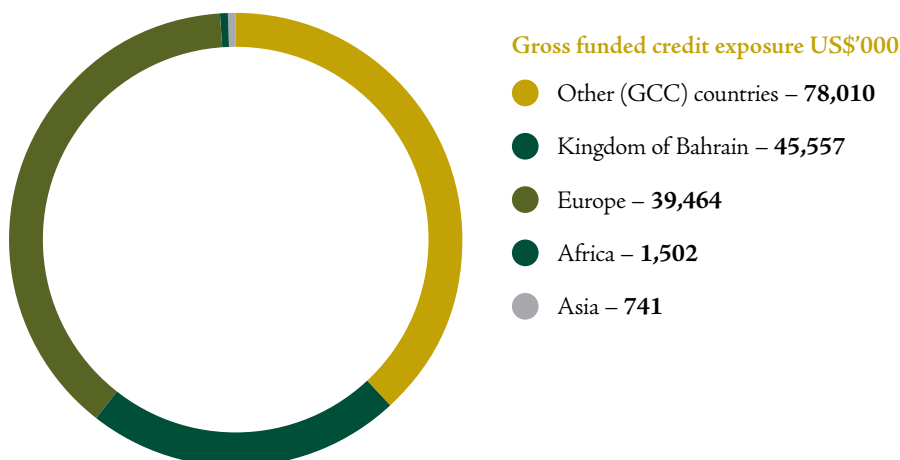
The impaired security is reflected at fair value based on the relevant closing stock market price as at 31 December 2012. The criteria used to allocate exposures to particular geographical areas is the country to which the funds were transferred.

1.4. Industrial sector analysis of the exposures

The industrial sector analysis of exposures, impaired assets and the related impairment provisions as at 31 December 2012 is as follows:

	Gross funded credit exposure US\$'000	Impaired securities US\$'000	Provision against securities US\$'000
Real estate – development	69,083	-	-
Real estate – income generating	15,261	10,210	4,510
Banking and financial institutions	39,020	242	71
Insurance	131	-	-
Manufacturing	11,316	3,973	1,590
Automotive	1,502	-	-
Others	28,961	-	-
Total	165,274	14,425	6,171

The Bank has no unfunded exposures as at 31 December 2012.



1.5. Large exposures

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

The following are the large exposures of US\$ 1,000,000 and over as of 31 December 2012:

	Large exposure (banks) US\$'000	% of exposure to equity		Large exposure (non banks) US\$'000	% of exposure to equity
BANKS			NON BANKS		
Bank A	10,123	6.25%	Counterparty A	38,344	23.69%
Bank B	3,943	2.44%	Counterparty B	24,956	15.42%
Bank C	3,431	2.12%	Counterparty C	17,966	11.10%
			Counterparty D	14,313	8.84%
			Counterparty E	10,000	6.18%
			Counterparty F	4,377	2.70%
			Counterparty G	4,102	2.53%
			Counterparty H	3,986	2.46%
			Counterparty I	3,880	2.40%
			Counterparty J	3,754	2.32%
			Counterparty K	3,238	2.00%
			Counterparty L	2,808	1.73%
			Counterparty M	2,509	1.55%
			Counterparty N	2,460	1.52%
			Counterparty O	2,155	1.33%
			Counterparty P	1,473	0.91%
			Counterparty Q	1,123	0.69%
			Counterparty R	1,105	0.68%
			Counterparty S	1,007	0.62%

1.6. Exposure by external credit rating

The Bank uses ratings issued by Standard & Poor's, Moody's, Capital Intelligence and Fitch to derive the risk weightings under the CBB's Basel 2 capital adequacy framework. Where ratings vary between rating agencies, the highest rating from the lowest two ratings is used to represent the rating for regulatory capital adequacy purposes. The following are gross credit risk exposures considered for Capital Adequacy Ratio calculations comprising of banking book exposures as at 31 December 2012:

	Gross credit exposure US\$'000	Rated exposure US\$'000	Unrated exposure US\$'000
Cash and claims on banks	35,532	13,537	21,995
Equity portfolio	106,907	-	106,907
Other exposures	22,835	-	22,835
Total	165,274	13,537	151,737

1.7. Intra-group transactions including exposures to related parties

Related parties represent associated companies, major shareholders, directors and key management personnel of the Bank and entities controlled, jointly controlled or significantly influenced by such parties. Pricing policies and terms of these transactions are on an arm's length basis and are identical to those applicable to transactions with all other parties. Exposures as at 31 December 2012 are as follows:

	Gross credit exposure US\$'000
EXPOSURES TO RELATED PARTIES	
Claims on associates	43,934
Claims on investee companies	22,066
Total	66,000
LIABILITIES TO RELATED PARTIES	
Deposit payable to shareholders	1,448

1.8. Impairment of assets

An assessment is made at each balance sheet date to determine whether there is objective evidence that a specific financial asset or group of financial assets may be impaired. If such evidence exists, an impairment loss is recognised in the Consolidated Statement of Income.

Evidence of impairment may include indications that the investee company is experiencing significant financial difficulty, default or delinquency in profit or principal payments, the probability that they will enter bankruptcy or other financial re-organisation and that there is a measurable decrease in the estimated future cash flows such as changes in arrears or economic conditions that correlate with defaults.

Impairment is determined as follows:

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

1.9. Impairment losses on financial assets

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

2. Liquidity Risk and Funding Management

Liquidity risk is the risk that the Bank will be unable to meet its payment obligations when they fall due under both normal and stress circumstances. The Assets & Liabilities Committee (ALCO) monitors future cash flows and liquidity required for working capital and investment acquisition. The Bank's investments generally have a long-term maturity and hence, as a matter of policy, the long-term investments are funded from IIB's own capital. The Bank maintains significant cash and cash equivalent balances and also has access to geographically diversified funding sources, although no deposit liabilities or long-term funding by external counterparties were booked during 2012. The ratio of liquid assets (defined as cash, balances with banks, due from financial institutions and quoted investments) to total assets at 31 December 2012 is 25.6% (31 December 2011: 46.1%). Details of liquidity risk and funding management are contained in Note 19.3 to the Consolidated Financial Statements.

The table below shows an analysis of financial assets and liabilities as at 31 December 2012 analysed according to when they are expected to be recovered or settled.

	Within 1 month US\$ '000	1-3 months US\$ '000	3-6 months US\$ '000	6-12 months US\$ '000	Total within 12 months US\$ '000	1-5 years US\$ '000	Total US\$ '000
ASSETS							
Cash and claims on banks	35,532	-	-	-	35,532	-	35,532
Receivables	12,287	82	5,862	1,523	19,754	2,315	22,069
Investment in quoted equities	-	-	-	-	-	8,336	8,336
Investment in unquoted equities	-	-	-	-	-	50,263	50,263
Investment property	-	-	-	-	-	4,374	4,374
Investment in associates	-	-	-	-	-	43,934	43,934
Other assets	45	52	5	2	104	662	766
Total assets	47,864	134	5,867	1,525	55,390	109,884	165,274
LIABILITIES							
Other liabilities	247	1,517	1,219	-	2,983	412	3,395
Total liabilities	247	1,517	1,219	-	2,983	412	3,395
Net gap	47,617	(1,383)	4,648	1,525	52,407	109,472	161,879

The Bank maintains significant cash and cash equivalent balances and also has access to geographically diversified funding sources, although no deposit liabilities or long-term funding by external counterparties were booked during 2012.

2. Liquidity Risk and Funding Management (continued)

The maturity profile of assets and liabilities as at 31 December 2011 based on contractual maturity is as follows:

	Within 1 month US\$'000	1-3 months US\$'000	3-6 months US\$'000	6-12 months US\$'000	Total within 12 months US\$'000	1-5 years US\$'000	Total US\$'000
ASSETS							
Claims on banks	39,615	21,846	-	-	61,461	-	61,461
Receivables	27	4,454	1,703	1,257	7,441	2,385	9,826
Investment in quoted equities	-	-	-	-	-	8,659	8,659
Investment in unquoted equities	-	-	-	-	-	8,951	8,951
Investment property	-	-	-	-	-	4,374	4,374
Investment in associates	-	-	-	-	-	53,961	53,961
Other assets	46	142	30	-	218	1,053	1,271
Total assets	39,688	26,442	1,733	1,257	69,120	79,383	148,503
LIABILITIES							
Other liabilities	198	1,098	66	21	1,383	316	1,699
Total liabilities	198	1,098	66	21	1,383	316	1,699
Net gap	39,490	25,344	1,667	1,236	67,737	79,067	146,804



3. Market Risk

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

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

Note 19.4 to the Consolidated Financial Statements details the Bank's exposure to equity price risk, foreign currency risk and profit rate risk.

4. Operational Risk

Operational Risk is the risk of direct or indirect loss resulting from breaches in internal controls, processing errors, inadequate information systems, fraud, or external events. Its impact can be in the form of a financial loss, loss of reputation or loss of competitive position. Operational risk is inherent in all business activities and can never be eliminated entirely but can only be mitigated or minimised. The Bank minimises its exposure to such risk by ensuring that appropriate management control mechanisms, infrastructure, systems, internal controls and human resources are in place.

IIB has developed an operational risk framework, reviewed by experienced external consultants, that provides for identification, measurement, monitoring and control of potential risk events. A number of processes are used throughout the Bank including risk and control self assessments, key risk indicators (KRIs), event management, new product review / approval procedures and business continuity plans. In addition, Internal Audit Department issues regular reports including an annual organisation-wide risk assessment and the external auditors make recommendations on internal controls and processes. Business units are responsible for managing the operational risks relevant to their activities, supported by a disaster recovery program covering computer backup, data recovery and business continuity.

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

5. Legal Risk

Legal Risk is the risk arising from the potential that unenforceable contracts, lawsuits, or adverse judgements can disrupt or otherwise adversely affect the operations of the Bank. It has professional service arrangements with well-established local and international law firms. The policies and procedures of the Bank ensure that investments are made, funds are transferred, contracts are entered into, legal agreements are signed and any other binding arrangement is executed only after a rigorous legal due diligence has been performed either by the Legal and Compliance Departments or external legal counsel.

The Bank fully complied with all applicable laws and regulations during the year ended 31 December 2012, except for the non publishing of annual report for the year ended 31 December 2011 on time and accordingly paid a penalty of US\$ 6,100.

Organisation Structure

Chief Executive Officer

Aabed Al-Zeera,
Chief Executive Officer (CEO)

Anne Uson
Executive Secretary

Direct Investment & Business Development

Narayanan Ganapathy
Director

Fadi Al-Qassim
Director

Atif Naveed
Associate

Marieta Cano
Executive Secretary

Investment Placement

Alyas Al-Meftah
Director

Bashar Al-Shaikh
Principal

Omar Shaheen
Principal

Mona Mahmood Ghuloom
Coordinator

Bushra A.Hassan Al-Madhi
Coordinator

Asset Management

Murtaza Ghulam
Principal

Salah Hasan Habib
Associate, Investor Relations

Sadaf Gill
Analyst

Ruby Castro
Executive Secretary

Finance and Administration

Michael Ross-McCall
Chief Financial Officer (CFO)

Augustine Peter
Principal – Finance

Haleema Ebrahim
Associate – Treasury

Hassan Abbas
Officer

Hussain Ali Jassim
General Services Supervisor

Khulood Farhan
Receptionist & General Secretary

Information Technology

Said Itani
Head

Sayed Hussein Mahdi
Associate

Risk Management

Ninan Varkey
Head

Internal Audit

Ali Redha
Director

Human Resources

Sawsan Al-Ansari
Consultant

Corporate Communications & PR

Omar Shaheen
Principal

Compliance

Mohammed Juma Habib
Associate

Shari'ah Review

Mahmood Al-Qassab
Coordinator

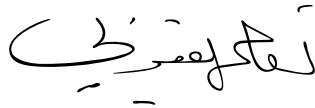
Shari'ah Supervisory Board Report

On the audited Financial Statements for the year ending December 31, 2012. International Investment Bank

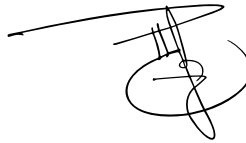
In compliance with the terms of our letter of appointment, we are required to report as follows:

The Shari'ah Supervisory Board ("SSB") was presented with all the investment deals and transactions that were conducted by the International Investment Bank ("Bank") during the course of the year ending December 31, 2012. The SSB reviewed the principles and contracts relating to all these investments and transactions in order to issue an independent opinion on whether the Bank followed the principles of the Islamic Shari'ah, specific fatwas, and guidelines issued by the SSB, where the Bank's management is responsible for ensuring that its operations are carried out in compliance with SSB rulings. Furthermore, the SSB has reviewed the internal review and update reports issued by the Internal Shari'ah Reviewer. The SSB responsibility is to present an independent view of the Bank's operations and to communicate it to the shareholders.

We beseech the Almighty to grant us excellence and success.
Wassalam Alaikum Wa Rahmat Allah Wa Barakatuh.



Sh. Nizam Yaqouby
Chairman



Sh. Abdul Nasser Al-Mahmoud
Member



Dr. Osama Bahar
Member

In our opinion:

1. The Bank's contracts, transactions and deals for the year ending December 31, 2012 are in compliance with the rules and principles of the Islamic Shari'ah.
2. 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.
3. No earnings have been realised from non-Shari'ah compliant sources during the fiscal year.
4. The Bank's calculation of Zakat is in compliance with the rules and principles of the Islamic Shari'ah and has been calculated as US\$ 0.011 per share in accordance with the Net Asset Method described in the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) standards and it is the responsibility of the shareholders to pay their Zakat allocation.

52	Independent Auditors' Report to The Shareholders
53	Consolidated Statement of Financial Position
54	Consolidated Statement of Income
55	Consolidated Statement of Cash Flows
56	Consolidated Statement of Changes In Equity
57	Notes to The Consolidated Financial Statements

Financial Statements

- Consolidated financial statements present fairly, in all material respects, the financial position of the Group as of 31 December 2012, and the results of its operations, its cash flows and changes in equity for the year then ended in accordance with Financial Accounting Standards issued by AAOIFI.

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

We have audited the accompanying consolidated statement of financial position of International Investment Bank B.S.C. (c) ["the Bank"] and its subsidiaries ["the Group"] as of 31 December 2012, and the related consolidated statements of income, cash flows and changes in equity for the year then ended. These consolidated financial statements and the Group's undertaking to operate in accordance with Islamic Shari'a Rules and Principles are the responsibility of the Bank's Board of Directors. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with Auditing Standards for Islamic Financial Institutions issued by the Accounting and Auditing Organisation for Islamic Financial Institutions ["AAOIFI"]. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statements presentation. We believe that our audit provides a reasonable basis for our opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as of 31 December 2012, and the results of its operations, its cash flows and changes in equity for the year then ended in accordance with Financial Accounting Standards issued by AAOIFI.

Other matters

As required by the Bahrain Commercial Companies Law and the Central Bank of Bahrain (CBB) Rule Book (Volume 2), we report that:

- a) the Bank has maintained proper accounting records and the consolidated financial statements are in agreement therewith; and
- b) the financial information contained in the Report of the Board of Directors is consistent with the consolidated financial statements.

We are not aware of any violations of the Bahrain Commercial Companies Law, the Central Bank of Bahrain and Financial Institutions Law, the CBB Rule Book (Volume 2 and applicable provisions of Volume 6) and CBB directives, or the terms of the Bank's memorandum and articles of association during the year ended 31 December 2012 that might have had a material adverse effect on the business of the Bank or on its consolidated financial position. Satisfactory explanations and information have been provided to us by management in response to all our requests. The Bank has also complied with the Islamic Shari'a Rules and Principles as determined by the Shari'a Supervisory Board of the Bank.



6 March 2013
Manama, Kingdom of Bahrain

Consolidated Statement of Financial Position

At 31 December 2012

	Notes	2012 US\$'000	2011 US\$'000
ASSETS			
Cash and balances with banks		7,443	697
Due from financial institutions	6	28,089	60,764
Receivables	7	22,069	9,826
Investments	8	58,599	17,610
Investment in real estate	9	4,374	4,374
Investment in associates	11	43,934	53,961
Equipment		656	1,049
Other assets		110	222
TOTAL ASSETS		165,274	148,503
LIABILITIES AND EQUITY			
Other liabilities	12	3,395	1,699
TOTAL LIABILITIES		3,395	1,699
OWNERS' EQUITY			
Share capital	13	109,996	109,996
Treasury shares	13	(6,798)	(6,798)
Share premium		72,050	72,050
Reserves	13	5,733	3,353
Accumulated deficit		(25,955)	(33,337)
		155,026	145,264
Non-controlling interest		6,853	1,540
TOTAL EQUITY		161,879	146,804
TOTAL LIABILITIES AND EQUITY		165,274	148,503



Saeed Abdul Jalil Al Fahim
Chairman of the Board of Directors



Abed Al Zeera
Chief Executive Officer

The attached explanatory notes 1 to 23 form part of these consolidated financial statements.

Consolidated Statement of Income

For the year ended 31 December 2012

	Notes	2012 US\$'000	2011 US\$'000
Income			
Investment banking fees	3	3,218	642
Income on due from financial institutions and receivables		1,233	1,644
Gain on sale of investments		542	20
Gain on conversion of associate to investment at fair value through equity	11	8,731	-
Unrealised fair value loss on investment in real estate	9	-	(159)
Income from investment in real estate, net		243	213
Dividend income		136	129
Other income		47	578
TOTAL INCOME		14,150	3,067
Expenses			
Corporate expenses		2,302	1,803
General and administration expenses	5	1,753	2,125
Selling expenses		992	743
Deal acquisition expenses		782	650
Asset management expenses		557	311
TOTAL EXPENSES		6,386	5,632
OPERATING INCOME / (LOSS)		7,764	(2,565)
Share of profit / (loss) from associates	11	3,962	(3,439)
NET PROFIT / (LOSS) BEFORE IMPAIRMENT LOSSES, PROVISIONS AND FOREIGN EXCHANGE GAINS / (LOSSES)		11,726	(6,004)
Impairment losses and provisions	7, 8	(3,588)	(3,303)
Gain / (loss) on foreign exchange		45	(102)
NET PROFIT / (LOSS) FOR THE YEAR		8,183	(9,409)
Attributable to:			
Equity holders of the parent		8,202	(9,330)
Non-controlling interest		(19)	(79)
		8,183	(9,409)



Saeed Abdul Jalil Al Fahim
Chairman of the Board of Directors



Aabed Al Zeera
Chief Executive Officer

The attached explanatory notes 1 to 23 form part of these consolidated financial statements.

Consolidated Statement of Cash Flows

For the year ended 31 December 2012

	Notes	2012 US\$'000	2011 US\$'000
OPERATING ACTIVITIES			
Net profit / (loss) for the year		8,183	(9,409)
Adjustments for:			
Depreciation		421	598
Gain on conversion of associate to investment at fair value through equity		(8,731)	-
Unrealised fair value loss on investment in real estate		-	159
Gain on sale of investments		(542)	(20)
Share of (profit) / loss from associates		(3,962)	3,439
Impairment losses and provisions		3,588	3,303
		(1,043)	(1,930)
Changes in operating assets and liabilities:			
Receivables		(2,291)	4,153
Other assets		112	1
Other liabilities		1,696	(205)
Purchase of investments		(15,363)	-
Proceeds from disposal of investments		-	422
Net cash (used in) / from operating activities		(16,889)	2,441
INVESTING ACTIVITIES			
Cash outflow on acquisition of subsidiary	10	(9,012)	-
Purchase of equipment		(28)	(190)
Net cash used in investing activities		(9,040)	(190)
(DECREASE) / INCREASE IN CASH AND CASH EQUIVALENTS			
		(25,929)	2,251
Cash and cash equivalents at beginning of the year		61,461	33,404
Cash and cash equivalents on conversion to subsidiary		-	25,806
CASH AND CASH EQUIVALENTS AT END OF THE YEAR		35,532	61,461
Cash and cash equivalents comprise:			
Cash and balances with banks		7,443	697
Due from financial institutions with original maturities of three months or less		28,089	60,764
		35,532	61,461

The attached explanatory notes 1 to 23 form part of these consolidated financial statements.

Consolidated Statement of Changes in Equity

For the year ended 31 December 2012

	Share capital US\$'000	Treasury shares US\$'000	Share premium US\$'000	Statutory reserve US\$'000	Reserves cumulative changes in fair value reserve US\$'000	Foreign currency translation reserve US\$'000	Total reserves US\$'000	Accu- mulated deficit US\$'000	Non- controlling interest US\$'000	Total US\$'000
Balance at 1 January 2012	109,996	(6,798)	72,050	5,588	(529)	(1,706)	3,353	(33,337)	1,540	146,804
Unrealised gains on re-measurement to fair value, net	-	-	-	-	151	399	550	-	-	550
Transferred to statement of income on impairment	-	-	-	-	923	-	923	-	-	923
Exchange differences on translation of foreign operations	-	-	-	-	-	87	87	-	31	118
Non controlling interest acquired	-	-	-	-	-	-	-	-	5,301	5,301
Net profit for the year	-	-	-	-	-	-	-	8,202	(19)	8,183
Transfer to statutory reserve	-	-	-	820	-	-	820	(820)	-	-
Balance at 31 December 2012	109,996	(6,798)	72,050	6,408	545	(1,220)	5,733	(25,955)	6,853	161,879
Balance at 1 January 2011	109,996	(6,798)	72,050	5,588	2,661	(1,222)	7,027	(24,007)	-	158,268
Unrealised losses on re-measurement to fair value, net	-	-	-	-	(6,075)	(484)	(6,559)	-	-	(6,559)
Transferred to statement of income on impairment	-	-	-	-	2,885	-	2,885	-	-	2,885
Non controlling interest acquired	-	-	-	-	-	-	-	-	1,619	1,619
Net loss for the year	-	-	-	-	-	-	-	(9,330)	(79)	(9,409)
Balance at 31 December 2011	109,996	(6,798)	72,050	5,588	(529)	(1,706)	3,353	(33,337)	1,540	146,804

The attached explanatory notes 1 to 23 form part of these consolidated financial statements.

Notes to the Consolidated Financial Statements

At 31 December 2012

1 Corporate Information and Activities

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

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

The Bank and its subsidiaries (together the "Group") operate in the Kingdom of Bahrain and the Cayman Islands.

The financial statements were authorised for issue in accordance with a resolution of the Board of Directors on 6 March 2013.

2 Accounting Policies

a) Basis of preparation

These consolidated financial statements have been prepared under the historical cost convention except for investments and investment in real estate which have been measured at fair value.

The consolidated financial statements are presented in United States Dollars ["US\$"] which is the Bank's functional currency. All values are rounded to nearest thousand dollars, except when otherwise indicated.

b) Statement of compliance

These consolidated financial statements have been prepared in accordance with Financial Accounting Standards ["FAS"] issued by the Accounting and Auditing Organisation for Islamic Financial Institutions ["AAOIFI"], the Islamic Shari'a Rules and Principles as determined by the Shari'a Supervisory Board of the Bank, the Bahrain Commercial Companies Law and the Central Bank of Bahrain and Financial Institutions Law, the CBB Rule Book (Volume 2 and applicable provisions of Volume 6) and CBB directives. In accordance with the requirements of AAOIFI, for matters for which no AAOIFI standards exist, the Group uses the relevant International Financial Reporting Standards ["IFRS"] issued by the International Accounting Standards Board ["IASB"].

c) Basis of consolidation

The consolidated financial statements comprise the financial statements of the Bank and its subsidiaries as at 31 December 2012. The financial information of the subsidiaries (including special purpose entities that the Bank consolidates) are prepared for the same reporting year as the Bank, using consistent accounting policies.

A subsidiary is an entity over which the Group has power to control, which is other than fiduciary in nature. Subsidiaries are fully consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date that such control ceases to exist. Control is achieved where the Group has the power, directly or indirectly, to govern the financial and operating policies of the entity so as to obtain benefits from its activities. The results of subsidiaries acquired or disposed of during the period are included in the consolidated statement of income from the date of acquisition or up to the date of disposal, as appropriate.

All intra-group balances, transactions, income and expenses are eliminated in full.

Non-controlling interest represents the portion of profit or loss and net assets of subsidiaries not owned, directly or indirectly, by the Group. Non-controlling interests are presented separately in the consolidated statement of income and within equity in the consolidated statement of financial position, separately from owners' equity. Any losses applicable to the non-controlling interest in excess of the non-controlling interests are allocated against the interests of the non-controlling interest even if this results in the non-controlling interest having a deficit balance.

At 31 December 2012

2 Accounting Policies (continued)**c) Basis of consolidation** (continued)

The following are the Group's subsidiaries as at 31 December 2012:

Name of subsidiary	Notes	Country of incorporation	Year of incorporation	Equity interest	Industry
Bahrain Bunny Shares and Securities W.L.L.	10	Kingdom of Bahrain	2012	63.10%	SPV for investment in fast food industry
Istethmary Sarajevo City Centre-I Limited		Cayman Islands	2009	93.77%	SPV for investment in real estate
Istethmary Petrochemical Holding Company B.S.C (c)		Kingdom of Bahrain	2008	100.00%	SPV for investment in real estate

d) Significant accounting judgments and estimates

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

Going concern

The Group's management has made an assessment of the Group's ability to continue as a going concern and is satisfied that the Group has the resources to continue in business for the foreseeable future. Furthermore, the Board of Directors is not aware of any material uncertainties that may cast significant doubt upon the Group's ability to continue as a going concern. Therefore, the consolidated financial statements continue to be prepared on a going concern basis.

Fair value*Fair value of unquoted investments at fair value through equity*

Where the fair value of the Group's investment portfolio cannot be derived from an organised market, they are determined using a variety of valuation techniques that include the use of mathematical models. The inputs to these models are derived from observable market data where possible, but where observable market data is not available, judgment by management is required to establish fair values. The judgments include consideration of comparable assets, discount rates and the assumptions used to forecast cash flows.

Fair value of investment in real estate

The fair value of investment in real estate is determined by independent real estate valuation experts. The determination of the fair value of such assets requires the use of judgment and estimates by independent valuation experts that are based on local market conditions existing at the date of the statement of financial position.

Impairment

The Group treats investments classified as fair value through equity as impaired when there has been a significant or prolonged decline in the fair value below its cost or where other objective evidence of impairment exists. The determination of what is "significant" or "prolonged" requires considerable judgment. In making this judgment, the Group evaluates, among other factors, normal volatility in share price and duration and the extent to which the fair value of quoted equities is less than its cost and the future cash flows and the discount factors for unquoted equities.

The Group reviews its doubtful financial contracts on each reporting date to assess whether a provision for impairment should be recorded in the statement of income. In particular, considerable judgment by management is required in the estimation of the amount and timing of future cash flows when determining the level of provisions required. Such estimates are necessarily based on assumptions about several factors involving varying degrees of judgment and uncertainty, and actual results may differ resulting in future changes to such provisions.

2 Accounting Policies (continued)

e) Summary of significant accounting policies

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

i) Foreign currency translation

Transactions and balances

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

Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency using rates of exchange prevailing at the statement of financial position date. All differences are taken to the consolidated 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 initial recognition. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates prevailing at the date when the fair value was determined. Translation gains or losses on non-monetary items carried at fair value are included in equity as part of the fair value adjustment on investments classified as fair value through equity.

Group companies

As at the reporting date, the assets and liabilities of subsidiaries are translated into the Group's presentation currency (US\$) at the rate of exchange prevailing at the statement of financial position date, and their statements of income are translated at the weighted average exchange rates for the year. Exchange differences arising on translation are recognised directly in equity. On disposal of a foreign subsidiary, the cumulative amount recognised in equity relating to that particular foreign subsidiary is recognised in the consolidated statement of income.

ii) Financial instruments

Financial instruments comprise financial assets and financial liabilities.

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

Incremental transaction costs associated with the acquisition of investments classified as fair value through equity are included in the cost of such investments.

Date of recognition

All financial assets and liabilities are initially recognised on the trade date, i.e. the date that the Group becomes a party to the contractual provisions of the instrument.

Initial measurement of financial instruments

The classification of financial instruments at initial recognition depends on the purpose for which the financial instruments were acquired and their characteristics. All financial instruments are initially recognised at their cost being the fair value of the consideration given plus any directly attributable incremental costs of acquisition or issue, except in the case of financial assets recorded at fair value through statement of income. In case of financial assets carried at fair value through statement of income, the incremental costs of acquisition or issue are immediately expensed in the consolidated statement of income.

Subsequent measurement of financial instruments

Cash and balances with banks

Cash and balances with banks are carried at amortised cost in the statement of financial position.

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.

At 31 December 2012

2 Accounting Policies (continued)**e) Summary of significant accounting policies** (continued)**ii) Financial instruments** (continued)*Investments*

Investments are initially designated as “fair value through equity” or “amortised cost”.

Fair value through equity

After initial recognition, investments designated as fair value through equity are remeasured at fair value. Unrealised gains and losses are recognised directly in equity in the ‘Investments fair value reserve’. When the investment is disposed of or determined to be impaired, the cumulative gain or loss, previously transferred to the investments fair value reserve, is recognised in the consolidated statement of income. Where the Group holds more than one investment in the same security they are deemed to be disposed of on a weighted average basis.

Amortised cost

These instruments are managed on a contractual yield basis and are not held for trading and have not been designated at fair value through statement of income. Such investments are carried at amortised cost, less provision for impairment in value. Amortised cost is calculated by taking into account any premium or discount on acquisition and using the effective profit rate method. Any gain or loss on such investments is recognised in the consolidated statement of income, when the investment is de-recognised or impaired.

iii) Investment in real estate

Real estate held for rental or capital appreciation purposes, or both, is classified as investment in real estate. Investment in real estate is initially recognised at cost including transaction costs and subsequently re-measured at fair value with the resulting unrealised gains being recognised in the statement of changes in equity under ‘cumulative changes in fair value reserve’. Losses after adjusting any unrealised gain in equity, are taken to the consolidated statement of income. In the case of unrealised losses that have been recognised in the statements of income in previous periods, the unrealised gains related to the current financial period are recognised to the extent of crediting back such previous losses in the statement of income. Any excess of such gains over such prior-period losses are added to the “cumulative changes in fair value reserve” in the statement of financial position.

iv) Derecognition of financial assets and financial liabilities*Financial assets*

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

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

When the Group has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Group’s continuing involvement in the asset.

Financial liabilities

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

2 Accounting Policies (continued)

e) Summary of significant accounting policies (continued)

v) Impairment of financial assets

The Group assesses at each reporting date whether there is any objective evidence that a financial asset or a group of financial assets is 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 has occurred after the initial recognition of the asset (an incurred 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated.

Evidence of impairment may include indications that the debtors or a group of debtors is experiencing significant financial difficulty, default or delinquency in profit or principal payments, the probability that they will enter bankruptcy or other financial reorganisation and where observable data indicates that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

Investments classified as fair value through equity

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

Investments carried at amortised cost

For financial assets carried at amortised cost, the Group first assesses individually whether objective evidence of impairment exists individually for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognised are not included in the collective assessment of impairment.

If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not yet been incurred). The carrying amount of the asset is reduced through the use of a provision account and the amount of the loss is recognised in the consolidated statement of income.

vi) Offsetting of financial instruments

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

vii) Investment in associates

The Group's investments in associates are accounted for under the equity method of accounting. These are entities over which the Group exercises significant influence. Significant influence is presumed to exist if the Bank holds, directly or indirectly through its subsidiaries, 20% or more of the voting rights in an entity, unless it can be clearly demonstrated otherwise. Conversely, the significant influence may also exist through agreements with the entity's other shareholders or the entity itself regardless of the level of shareholding that the Bank has in the said entity.

Under the equity method, an investment in an associate is initially recognised at cost and adjusted thereafter for the post-acquisition changes in the Group's share of net assets of the associate. Goodwill relating to an associate is included in the carrying amount of the investment and is not amortised or individually tested for impairment.

At 31 December 2012

2 Accounting Policies (continued)**e) Summary of significant accounting policies** (continued)**vii) Investment in associates** (continued)

After application of the equity method, the Group determines whether it is necessary to recognise any impairment loss with respect to the Group's net investment in the associate. The Group determines at each reporting date whether there is any objective evidence that the investment in the associate is impaired. If this is the case the Group calculates the amount of impairment as the difference between the recoverable amount of the associate and its carrying value and recognises the amount in the consolidated statement of income.

The consolidated statement of income reflects the share of the results of operations of the associate. Where there has been income or expense recognised in the other comprehensive income of the associate, the Group recognises its share of any such income or expense, when applicable, directly in equity. Gains and losses resulting from transactions between the Group and the associate are eliminated to the extent of stake in the associate.

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

Upon loss of significant influence over the associate, the Group measures and recognises any retaining investment at its fair value. Any difference between the carrying amount of the associate upon loss of significant influence and the fair value of the retaining investment and proceeds from disposal is recognised in the consolidated statement of income.

viii) Equipment

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

ix) Revenue recognition

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, placings with investors and arranging financing. These fees are recognised when earned, generally on receipt of cash and signed share purchase agreements by the Bank.

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

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

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

Rental income from investment in real estate is recognised on the basis of contractual amounts receivable on a time apportioned basis and recorded on a net basis in the statement of income as income from investment in real estate.

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

x) Employees' end of service benefits

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

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

xi) Zakat

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

2 Accounting Policies (continued)

e) Summary of significant accounting policies (continued)

xii) Cash and cash equivalents

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

xiii) Fiduciary assets

Assets held in a fiduciary capacity are not reported in the statement of financial position, as they are not the assets of the Bank.

xiv) Proposed dividend

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

xv) 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.

xvi) 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.

3 Investment Banking Fees

	Notes	2012 US\$'000	2011 US\$'000
Structuring fees	3.1	2,391	-
Management fees		509	642
Placement fees		318	-
		3,218	642

- 3.1 During the period, the Bank raised equity in the form of a rights issue for one of its investee companies. This fee represents the Bank's mark-up, which was partially received in the form of shares in the investee company.

4 Staff Costs

	2012 US\$'000	2011 US\$'000
Salaries and other staff related costs	4,060	3,153
End of service benefits	96	101
	4,156	3,254

The Bank classifies its expenses based on function and staff costs have been allocated to corporate, deal acquisition, selling and asset management expenses in the consolidated statement of income.

At 31 December 2012

5 General and Administration Expenses

	2012 US\$'000	2011 US\$'000
Depreciation	421	598
Rent and maintenance	303	407
Legal and professional	291	272
IT expenses	147	241
Printing and advertisement	100	136
Shari'a Supervisory Board remuneration	107	113
Directors' expenses	65	-
Communication	37	44
Donations	-	50
Others	282	264
	1,753	2,125

6 Due from Financial Institutions

	2012 US\$'000	2011 US\$'000
Commodity murabaha	28,116	60,830
Deferred income	(27)	(66)
	28,089	60,764

7 Receivables

	Notes	2012 US\$'000	2011 US\$'000
Receivables and prepayments	7.1	14,877	2,553
Due from investee companies	7.2	7,192	7,273
		22,069	9,826

7.1 Receivables and prepayments

	Notes	2012 US\$'000	2011 US\$'000
Management fee receivables		2,361	2,059
Receivable from investee companies		13,221	581
Other receivables		3	10
		15,585	2,650
Provisions	7.3	(708)	(97)
		14,877	2,553

Receivable from investee companies include an amount of USD 12,223 thousand receivable from the Al Fareeda Residential Fund in respect of units sold by it on behalf of the Bank's subsidiary.

7 Receivables (continued)**7.2 Due from investee companies**

	Notes	2012 US\$'000	2011 US\$'000
Commodity murabaha receivables		12,848	12,137
Deferred profit		(193)	(201)
		12,655	11,936
Provision / suspended profit	7.3	(5,463)	(4,663)
		7,192	7,273

7.3 Movement in provisions

	Receivables and prepayments 2012 US\$'000	Due from investee companies 2012 US\$'000	Total 2012 US\$'000	Total 2011 US\$'000
Opening	97	4,663	4,760	2,951
Charge during the year	611	120	731	1,133
Suspended profit during the year	-	680	680	676
	708	5,463	6,171	4,760

8 Investments

	2012 US\$'000	2011 US\$'000
<i>Fair value through equity</i>		
Equity instruments		
Quoted	8,336	8,659
Unquoted	14,141	8,951
Closed end mutual fund		
Unquoted	26,122	-
	48,599	17,610
<i>At amortised cost</i>		
Unquoted	10,000	-
	58,599	17,610

Impairment losses on investments charged during the year

	2012 US\$'000	2011 US\$'000
Impairment losses:		
Quoted	2,380	1,265
Unquoted	477	905
	2,857	2,170

8.1 Quoted and unquoted investments include US\$ 3,754 thousand (2011: US\$ 5,495 thousand) and US\$ 2,096 thousand (2011: US\$ 2,401 thousand) respectively, held on behalf of the Bank, in the name of related parties for which risk and rewards are borne by the Bank.

At 31 December 2012

9 Investment in Real Estate

	2012 US\$'000	2011 US\$'000
Opening balance	4,374	4,533
Fair value adjustment	-	(159)
	4,374	4,374

Investment in real estate comprises of an eleven-storey residential tower, managed by the Bank, with 23 apartments in the Kingdom of Bahrain. During the year the property has generated an average net monthly income of US\$ 20 thousand (2011: US\$ 18 thousand). The property is stated at fair value, determined based on valuations performed by two independent professional valuers as of 31 December 2012.

10 Business Combination

During 2012, the Bank established Bahrain Bunny Shares and Securities W.L.L. ["the Company"], a special purpose vehicle incorporated in the Kingdom of Bahrain, which holds a 49% equity stake in Hungry Bunny W.L.L. (a company incorporated in the Kingdom of Saudi Arabia).

Management estimates that the fair value of identifiable assets and liabilities of the consolidated subsidiary as at the date of acquisition were not materially different from their carrying value as disclosed below:

	Bahrain Bunny Shares and Securities W.L.L. US\$'000
Assets	
Cash and cash equivalents	53
Investment in associate	14,313
Total net assets	14,366
Liabilities	
Non controlling interest	5,301
Consideration settled in cash	(9,065)
Cash and cash equivalents in the subsidiary company acquired	53
Cash outflow on acquisition	(9,012)

11 Investment in Associates

	Notes	2012		2011	
		Ownership	US\$'000 Carrying value	Ownership	US\$'000 Carrying value
Al Shiddi International	11.1	32.98%	24,956	32.98%	24,738
Hungry Bunny W.L.L.	11.2	49.00%	14,313	-	-
IIB UAE Investments Limited	11.3	27.32%	5,718	27.32%	5,723
Ewaan Al Fareeda	11.4	26.96%	719	26.96%	25,272
			45,706		55,733
Provision			(1,772)		(1,772)
			43,934		53,961

11 Investment in Associates (continued)

The following is summarised financial information of the Group's investment in associates based on unaudited management accounts as at 31 December 2012:

	2012 US\$'000	2011 US\$'000
Total assets	99,545	229,210
Total liabilities	(5,243)	(15,921)
Net assets	94,302	213,289
Total income	53,580	511
Total expenses	6,294	6,971
Share of profit / (loss) from associates	3,962	(3,439)

11.1 Al Shiddi International has a controlling shareholding stake in a subsidiary which is being accounted for as unregistered capital by the subsidiary due to pending legal formalities and requirements of the Privatisation Commission in Bosnia. However, based on the substance of the transaction, the subsidiary has been consolidated in Al Shiddi International.

11.2 During the year, the Bank acquired an equity stake in Hungry Bunny W.L.L. through its subsidiary as disclosed in note 10. As at the date of the statement of financial position the shares had not been registered in the name of the subsidiary due to pending legal formalities in the Kingdom of Saudi Arabia. The Bank expects that these will be completed by March 2013.

11.3 During 2007, Bay Development Properties Limited ("the Company"), in which IIB UAE Investments Limited owns 64.80% of the equity, entered into a conditional sale/purchase agreement with a buyer to sell an investment property. Subsequently, the Company terminated this sale/purchase agreement on the basis that the buyer failed to fulfill his contractual obligation. The buyer then commenced a court action against the Company for specific performance of the sale/purchase agreement.

Since 2007, there have been a number of Court and Appeal Court hearings and decisions. On 4 July 2012, the Court of First Instance issued a verdict in favour of the Company, which the buyer has appealed in the Court of Appeals. The Appeal hearing was set for 27 November 2012 on which the buyer has submitted documents. The decision of the Appeal hearing is expected in February 2013, and the Company is confident that the Court of Appeals will decide in favour of the Company.

The legal title of the land is still held in the name of the buyer but the sale and transfer of investment property is restricted by the Dubai Land Department.

11.4 During 2012, Ewaan Al Fareeda sold all its assets and liabilities (net carrying value SAR 350 million) to a mutual fund incorporated in the Kingdom of Saudi Arabia (Al Fareeda Residential Fund ("Fund")) for a consideration of SAR 550 million payable in the form of 55 million units of the Fund with a par value SAR 10 each. Ewaan Al Fareeda has transferred these units to shareholders as a repayment of their investment. As a result of this transaction the Bank acquired 26.96% units of the Fund. However, the Fund is assisting in the placement of these units to investors and has received signed unit purchase agreements from various investors as at the date of the statement of financial position, which reduced the Bank's shareholding to 18.13%. Further, the Bank does not have significant influence over the Fund as it is managed by a fund manager independently. Therefore, the Bank has classified its investment in the Fund units as fair value through equity. Resultantly, the Bank has fair valued the investment on the date of classification and the difference between the carrying value and fair value amounting to USD 8,731 thousand has been recognised as gain in the statement of income.

12 Other Liabilities

	2012 US\$'000	2011 US\$'000
Payable to a shareholder	1,448	1,094
Accrued expenses	1,839	515
Other payables	108	90
	3,395	1,699

At 31 December 2012

13 Owners' Equity**13.1 Share capital**

	2012 US\$'000	2011 US\$'000
Authorised: 200,000,000 ordinary shares of US\$ 1 each	200,000	200,000
Issued and fully paid:		
109,996,000 ordinary shares of US\$ 1 each	109,996	109,996

13.2 Treasury Shares

	2012		2011	
	Number of shares '000	Value US\$'000	Number of shares '000	Value US\$'000
At 31 December	3,000	6,798	3,000	6,798

13.3 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 until 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.

13.4 Cumulative changes in fair value reserve

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

13.5 Foreign currency translation reserve

This represents unrealised losses on translation of assets classified as fair value through equity denominated in foreign currencies.

14 Proposed Appropriations

The Board of Directors of the Bank has not proposed any cash dividend for 2012 (2011: US\$ Nil).

15 Zakat

In the absence of appointment of the Bank to pay zakat on behalf of shareholders, the responsibility of payment of zakat is on individual shareholders of the Group. The amount of zakat payable by shareholders is US\$ 0.011 per share (2011: US\$ 0.016 per share) calculated under Net Assets method and approved by the Shari'a Supervisory Board of the Bank.

16 Balances and Transactions with Related Parties

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

The significant balances with related parties are as follows:

	Shareholders/ directors US\$'000	Others US\$'000	Total 2012 US\$'000	2011 US\$'000
Assets				
Investments	-	685	685	973
Investment in associate	-	43,934	43,934	53,961
Receivable from investee companies	-	15	15	11
Liabilities				
Other liabilities - payable to a shareholder	1,448	-	1,448	1,094

Transactions with related parties during the year are as follows:

	Notes	Shareholders/ directors US\$'000	Others US\$'000	Total 2012 US\$'000	2011 US\$'000
Income					
Share of loss from associates	11	-	3,962	3,962	(3,439)
Investment banking fees	3.1	-	2,629	2,629	-
Expenses					
Directors' remuneration		65	-	65	-
Shari'a Supervisory Board remuneration		-	107	107	113

Compensation of key management personnel was as follows:

	2012 US\$'000	2011 US\$'000
Short term employee benefits	2,666	1,961
End of service benefits	182	191
	2,848	2,152

17 Commitments

	2012 US\$'000	2011 US\$'000
Operating lease relating to rented premises		
Expiring within one year	244	244
Expiring in one to three years	51	294
	295	538

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18 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 19.3 "Liquidity risk and funding management" for the Bank's contractual undiscounted repayment obligations.

As at 31 December 2012

	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	3 to 5 years US\$'000	Undated US\$'000	Total US\$'000
ASSETS							
Cash and balances with banks	7,443	-	7,443	-	-	-	7,443
Due from financial institutions	28,089	-	28,089	-	-	-	28,089
Receivables	12,948	2,783	15,731	6,338	-	-	22,069
Investments	-	-	-	48,599	10,000	-	58,599
Investment in real estate	-	-	-	4,374	-	-	4,374
Investment in associate	-	-	-	43,934	-	-	43,934
Other assets (including equipment)	97	7	104	3	-	659	766
Total assets	48,577	2,790	51,367	103,248	10,000	659	165,274
LIABILITIES							
Other liabilities	2,893	91	2,984	411	-	-	3,395
Total liabilities	2,893	91	2,984	411	-	-	3,395
Net gap	45,684	2,699	48,383	102,837	10,000	659	161,879

As at 31 December 2011

	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	3 to 5 years US\$'000	Undated US\$'000	Total US\$'000
ASSETS							
Cash and balances with banks	697	-	697	-	-	-	697
Due from financial institutions	60,764	-	60,764	-	-	-	60,764
Receivables	4,481	2,960	7,441	2,385	-	-	9,826
Investments	-	-	-	17,610	-	-	17,610
Investment in real estate	-	-	-	4,374	-	-	4,374
Investment in associates	-	-	-	53,961	-	-	53,961
Other assets (including equipment)	187	31	218	4	-	1,049	1,271
Total assets	66,129	2,991	69,120	78,334	-	1,049	148,503
LIABILITIES							
Other liabilities	1,296	87	1,383	315	-	1	1,699
Total liabilities	1,296	87	1,383	315	-	1	1,699
Net gap	64,833	2,904	67,737	78,019	-	1,048	146,804

19 Risk Management

19.1 Introduction

Risk is inherent in the Bank's 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, operational risk and legal risk.

a) Risk management structure

Board of Directors

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

Shari'a Supervisory Board

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

Executive Committee

The Executive Committee comprising of the Board members 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 initiate detailed due diligence procedures.

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 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.

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19 Risk Management (continued)**19.1 Introduction** (continued)**b) Risk measurement and reporting systems**

Currently, the Bank's assets mainly comprise cash and balances with banks, due from financial institutions, receivables and investments (including investment in real estate and investment in associate). 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 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.

19.2 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

The table below shows the maximum exposure to credit risk for the components of the statement of financial position. There is no unfunded exposure and no significant use of master netting and collateral agreements.

	Notes	Gross credit exposure 2012 US\$'000	Gross credit exposure 2011 US\$'000
Credit risk items:			
Balances with banks		7,442	695
Due from financial institutions	6	28,089	60,764
Receivables	7	22,069	9,826
Other assets		110	222
Total Credit Risk Exposure		57,710	71,507

The above disclosure is considered to be reasonably representative of the level of credit risk of the Bank, as there has been no significant fluctuation in the credit risk assets during the year.

19 Risk Management (continued)**19.2 Credit risk** (continued)**b) Geographical distribution of the gross funded exposures**

The following table summarises the geographical distribution of exposures broken down into significant areas by major types of credit exposure as follows:

As at 31 December 2012

	Balances with banks US\$'000	Due from financial institutions US\$'000	Receivables US\$'000	Other assets US\$'000	Total US\$'000
Geographical region:					
Bahrain	7,442	17,965	2,650	110	28,167
Europe	-	-	6,561	-	6,561
Other GCC countries	-	10,124	12,568	-	22,692
Africa	-	-	65	-	65
Asia	-	-	225	-	225
	7,442	28,089	22,069	110	57,710

As at 31 December 2011

	Balances with banks US\$'000	Due from financial institutions US\$'000	Receivables US\$'000	Other assets US\$'000	Total US\$'000
Geographical region:					
Bahrain	695	60,764	2,957	222	64,638
Europe	-	-	6,408	-	6,408
Other GCC countries	-	-	236	-	236
Africa	-	-	77	-	77
Asia	-	-	148	-	148
	695	60,764	9,826	222	71,507

At 31 December 2012

19 Risk Management (continued)**19.2 Credit risk** (continued)**c) Industry distribution of the gross funded exposures**

The following table summarises the industry distribution of exposures broken down into significant areas by major types of credit exposures as follows:

As at 31 December 2012

	Balances with banks US\$'000	Due from financial institutions US\$'000	Receivables US\$'000	Other assets US\$'000	Total US\$'000
Industry sector:					
Real estate-development	-	-	12,540	-	12,540
Real estate-income generating	-	-	6,383	-	6,383
Banking and financial institutions	7,442	28,089	240	-	35,771
Manufacturing	-	-	2,708	-	2,708
Automotive	-	-	65	-	65
Others	-	-	133	110	243
	7,442	28,089	22,069	110	57,710

As at 31 December 2011

	Balances with banks US\$'000	Due from financial institutions US\$'000	Receivables US\$'000	Other Assets US\$'000	Total US\$'000
Industry sector:					
Real estate-development	-	-	206	-	206
Real estate-income generating	-	-	6,383	-	6,383
Banking and financial institutions	695	60,764	159	-	61,618
Manufacturing	-	-	2,992	-	2,992
Automotive	-	-	77	-	77
Others	-	-	9	222	231
	695	60,764	9,826	222	71,507

d) Credit quality per class of financial assets

The Group uses the ratings assigned by External Credit Assessment Institutions [ECAI] to ascertain credit quality of financial assets. ECAI considered by the Group are Standard and Poor's, Moody's and Fitch. The counterparties for which a rating is not available are classified under "unrated". The table below analyses the credit quality of the Bank's maximum credit exposure as per the credit ratings of the counterparties:

	2012 US\$'000	2011 US\$'000
Credit rating:		
A+ and better	10,040	28,838
A and A-	-	-
BB+ and better	3,497	2,855
Unrated	44,173	39,814
	57,710	71,507

19 Risk Management (continued)**19.2 Credit risk** (continued)**e) Aging of financial assets****As at 31 December 2012**

	Neither past due nor impaired US\$'000	Past due but not impaired US\$'000	Past due and individually impaired US\$'000	Total US\$'000
Balances with banks	7,442	-	-	7,442
Due from financial institutions	28,089	-	-	28,089
Receivables	12,115	1,590	8,364	22,069
Other assets	110	-	-	110
	47,756	1,590	8,364	57,710

As at 31 December 2011

	Neither past due nor impaired US\$'000	Past due but not impaired US\$'000	Past due and individually impaired US\$'000	Total US\$'000
Balances with banks	695	-	-	695
Due from financial institutions	60,764	-	-	60,764
Receivables	1,072	-	8,754	9,826
Other assets	222	-	-	222
	62,753	-	8,754	71,507

Past due represents amounts overdue for 90 days or more. These are real estate exposures located mainly in Europe.

f) Rescheduled receivables

Receivables amounting to US\$ Nil (2011: US\$ 6,972 thousand) have been rescheduled during the year.

g) 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 2012 was US\$ 17,966 thousand (2011: US\$ 29,766 thousand).

19.3 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.

All other liabilities of the Bank are payable on demand.

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19 Risk Management (continued)**19.4 Market risk**

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

a) Equity price risk

Equity price risk is the risk that the fair value of equity investments decreases as a result of fluctuations in the respective stock market indices. The Bank has fair value through equity investments quoted on overseas stock exchanges. Based on the values at 31 December 2012, a change in the quoted price of plus or minus 10% would change the value of these investments by plus or minus US\$ 834 thousand (2011: US\$ 866 thousand) with a corresponding increase or decrease in equity, except in cases where impairment losses are accrued which will result in a decrease being taken to the statement of income.

The Bank also has unquoted investments carried at fair value using either net asset values or valuations from independent valuers. Based on the values at 31 December 2012, a change in the valuation of 10% would change the value of these investments by plus or minus US\$ 1,414 thousand (2011: US\$ 895 thousand) with a corresponding increase or decrease in equity, except in cases where impairment losses are accrued which will result in a decrease being taken to the statement of income.

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.

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

	2012 US\$'000	2011 US\$'000
Euro	3,100	3,023
Others	15	64
	3,115	3,087

Sensitivity Analysis

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

	Change in exchange rate (+/-) %	2012 Effect on net income/ equity (+/-) US\$'000	2011 Effect on net income/ equity (+/-) US\$'000
Euro	10%	310	302
Others	10%	2	6

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 2012, a +/- 0.25% change in the profit rate, with all other variables constant, would have resulted in a +/- US\$ 135 thousand (2011: US\$ 164 thousand) impact on the consolidated statement of income.

19 Risk Management (continued)

19.4 Market risk (continued)

d) Legal risk

Legal risk is the risk arising from the potential that unenforceable contracts, lawsuits, or adverse judgements can disrupt or otherwise adversely affect the operations of the Bank. The Bank has mitigated its exposure to legal risk by entering into professional service arrangements with well-established local and international law firms. The policies and procedures of the Bank ensure that investments are made, funds are transferred, contracts are entered into, legal agreements are signed and any other binding arrangement is executed only after a rigorous legal due diligence has been performed either by the Legal and Compliance Department or external legal counsel.

20 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.

For the purposes of comparison, the proforma capital position as at 31 December, regulatory capital and risk weighted assets have been calculated in accordance with Basel II requirements as adopted by the CBB.

20.1 Capital adequacy ratio

	Notes	2012 US\$'000	2011 US\$'000
Regulatory capital			
Tier 1 capital	20.2	127,453	129,474
Total regulatory capital		127,453	129,474
Risk weighted assets	20.3	264,531	241,830
Total capital adequacy ratio		48.18%	53.54%
Minimum regulatory ratio		12%	12%

At 31 December 2012

20 Capital Management (continued)**20.2 Tier 1 Capital**

	2012 US\$'000	2011 US\$'000
Share capital	109,996	109,996
Treasury shares	(6,798)	(6,798)
Share premium	72,050	72,050
Statutory reserve	6,408	5,588
Cumulative changes in fair value reserve	(2,079)	(3,347)
Accumulated deficit	(25,955)	(33,337)
Non-controlling interest	6,853	1,540
Core Tier 1 Capital	160,475	145,692
Deductions	(16,827)	(8,359)
Tier 1 Capital before adjustments for negative balance of Tier 2	143,648	137,333
Negative balance of Tier 2	(16,195)	(7,859)
Tier 1 Capital net of negative Tier 2 Capital	127,453	129,474

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

20.3 Risk weighted assets

	Basel II 2012 US\$'000	Basel II 2011 US\$'000
Credit risk weight assets	176,252	151,696
Market risk weight assets	38,925	34,538
Operational risk weight assets	49,354	55,596
	264,531	241,830

Credit risk-weighted assets

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

Market risk-weighted assets

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

Operational risk-weighted assets

In calculating operational risk-weighted assets, the Bank uses the Basic Indicator Approach which calculates operational risk-weighted assets as a proportion of the average of three years' revenues.

21 Fair Value of Financial Instruments

Determination of fair value and fair value hierarchy

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

- Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities;
- Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly; and
- Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

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

	2012			Total US\$'000
	Level 1 US\$'000	Level 2 US\$'000	Level 3 US\$'000	
<i>Investments at fair value through equity</i>				
Quoted	8,336	-	-	8,336
Unquoted	-	31,209	9,054	40,263
	8,336	31,209	9,054	48,599
	2011			
	Level 1 US\$'000	Level 2 US\$'000	Level 3 US\$'000	Total US\$'000
<i>Investments at fair value through equity</i>				
Quoted	8,659	-	-	8,659
Unquoted	-	5,118	3,833	8,951
	8,659	5,118	3,833	17,610

There has been no transfers from level 1 and level 2 to level 3 during the years 2012 and 2011.

Financial instruments recorded at fair value

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

Financial Investments - fair value through equity

Fair value through equity financial assets valued using a valuation technique or pricing models primarily consist of unquoted equities.

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

At 31 December 2012

21 Fair Value of Financial Instruments (continued)**Movements in level 3 financial instruments measured at fair value**

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

	Unquoted 2012 US\$'000	Unquoted 2011 US\$'000
Balance at 1 January	3,833	4,114
Impairment losses recorded in consolidated statement of income	-	(344)
Fair value loss recorded in equity	(292)	(489)
Purchases, sales and settlements, net	5,513	552
Balance at 31 December	9,054	3,833

For the above financial instruments categorised as level 3, the Bank has used reasonably possible alternative assumptions and adjusted the discount rate by 10% as a key unobservable model input. The effect of this will result in +/- US\$ 1,932 thousand (31 December 2011: US\$ 383 thousand) adjustment in the carrying value of level 3 investments and related cumulative fair value change.

22 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.

23 Social Responsibility

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