

**Al Salam Bank-Bahrain B.S.C.**

**CONSOLIDATED FINANCIAL STATEMENTS**

**31 DECEMBER 2009**

## BOARD OF DIRECTORS' REPORT TO THE SHAREHOLDERS

The Directors of Al-Salam Bank-Bahrain BSC (“**the Bank**”) have the pleasure in submitting their report to the shareholders accompanied by the consolidated financial statements for the year ended 31 December 2009.

The consolidated financial statements comprise the financial statements of the Bank and its subsidiary, Bahraini Saudi Bank BSC (together known as “the Group”).

Fiscal year 2009 proved to be very challenging; yet the third full year of commercial operations had been successful representing your Bank’s fourth profitable period since its inception in April 2006. The Group’s total assets reached BD785.9 million, surpassing the US\$ 2 billion mark, with a net profit of BD 14 million (US\$ 37 million) for 2009.

The year under review saw the extension of credit and liquidity crunch experienced in the latter half of 2008 with fears of a double dip recession. In spite of extremely adverse market conditions, the Group managed to post a massive growth in total assets from BD554.5 million (US\$1.47 billion) at 31 December 2008 to BD785.9 million (US\$2.1 billion), an increase of BD231.4 million or 42% over 31 December 2008. This is largely due to the Bank’s successful acquisition of a 90.31% stake in Bahraini Saudi Bank BSC (BSB), a locally listed commercial bank in Bahrain. On the income side, the adverse business climate prevented planned exits of available for sale investments resulting in a 45% lower net profit. Whilst the gross operating income declined by 36% prudent cost management resulted in significant cost savings of 17% over corresponding figures for 2008.

The directors believe that to be a successful financial institution, the Group needs to build on its network within Bahrain, start on regional strategic expansion across the GCC and seriously consider venturing into family Takaful business to be able to offer a complete suite of Islamic financial services to its customer base. To this end, the Bank successfully acquired a 90.31% stake in BSB through a share exchange offer and expanded its branch and ATM network within Bahrain to 8 branches and 16 ATMs, respectively. This acquisition marked a major milestone in the history of your Bank which is actively seeking to identify similar opportunities to support inorganic growth and achieve its vision of becoming one of the largest Islamic financial institutions in the region. The Board and executive management are ambitious in positioning the Group as the largest Islamic bank in Bahrain in the coming years.

The directors have resolved to maintain BSB’s corporate legal status in the near future, so the Group could dedicate BSB to focus and complement the Group on Islamic retail and commercial banking operations in the Kingdom. Through this acquisition, the Group has created visibility in Bahrain and is enhancing its service delivery capabilities to small and medium sized clients through BSB, whilst the parent Bank is focussing on serving the large corporate, high net worth and ultra high net worth clients. Such an approach will not compromise on the Group’s service levels to its customers since the Bank had been successful in obtaining the Central Bank of Bahrain’s (“the CBB”) approval to offer services to the Group’s customers throughout its network. This means that regardless of where the customer established their accounts they will be able to operate their accounts throughout the entire Group’s branches.

During 2009, the Bank exercised extreme prudence in entering into new financing and investment transactions in order to preserve liquidity and bring only offerings that are backed by dependable cash flows. This is reflected in a modest 22% growth in the financing portfolio as the management has been watching the market conditions and the credit environment with a commitment to move away from real estate and create a diversified financing portfolio. On the investments side, the acquisition of a stake in Milton Gate, a trophy asset domiciled in Central London with a financially sound and established tenant

is a testimony of your Bank's commitment to bring only solid transactions to its client base. The Bank concluded the transaction in June 2009 and placed a majority stake with its investors at a running yield of 10% per annum paid quarterly. This deal also resulted in the Bank winning the International Real Estate Financing Summit (IREFME 2009) Award of Excellence for Outstanding Achievement in Islamic Real Estate Product Innovation. The marketing and sales of this transaction was concluded in a span of less than one month with demand from investors outweighing the offering size.

On the treasury front, the Group continued to expand its financial institutions relationship network. At 31 December 2009 your Group was a net lender to the banking system to the tune of BD173 million (US\$459 million) In addition, the Group invested in the CBB sukuk to the tune of BD33 million improving the financing portfolio diversification and strengthening the liquidity position as they are eligible for repurchase by the CBB in case of liquidity needs. Thus, the liquidity ratio of the Group remained extremely strong at 37.6%, net of due to banks and excluding the CBB sukuk, meaning 37.6% of customer liabilities were maintained in liquid funds. Throughout the fiscal year 2009, the executive management had been mindful of the need to be sufficiently liquid to ensure that customer needs are met timely. Since inception of the Bank in 2006, the Bank continues to be a net lender to the Banking system.

On the real estate sector front, anticipating strict regulations by the CBB, the Bank had tightened its investment in and financing to the real estate sector, and limited its exposure to 24% (31 December 2008: 30.0%) of its total assets. Given that there is a huge demand of dwelling units that are affordable, the Bank is committed to undertaking a role with the support of the Government of Bahrain in developing affordable housing solutions with a launch targeted in the later half of 2010. The Board and management are conscious of the need to check the Bank's concentration to the real estate sector and hence new businesses in this sector are being undertaken on a selective basis to take advantage of market opportunities and bearing in mind investor's cash yield expectations.

The Directors believe that recent challenges facing the banking sector will continue into 2010 and the Group is no exception to these challenges however, with a strong and growing deposit base and a robust risk management framework, we are confident that your Group is poised to outperform its peers in the medium to long term and to establish itself as a model for a universal Islamic bank.

In the Extraordinary General Assembly Meeting held on 4 May 2009, the shareholders approved the Bank's proposal to acquire up to 100% of the issued and fully paid up ordinary shares of BSB, consisting of 500,000,000 ordinary shares. The shareholders also approved an increase of the authorized share capital of your Bank from 1,200,000,000 shares of nominal value BD 0.100 each to 2,000,000,000 shares of nominal value BD 0.100 each. Following acquisition of a 90.31% stake in BSB, the Bank issued 225,775,075 ordinary shares to shareholders of BSB who accepted the Bank's offer thereby increasing the paid up shares to 1,425,775,075 shares.

Meanwhile, in the Extraordinary General Assembly Meeting held on 12 November 2009, the shareholders resolved to increase the number of the Bank's Board of directors to fourteen and have also endorsed the Board's recommendation to raise funding through the issuance of sukuk. Following this resolution, the Board of the Bank was expanded by two members and as resolved at the EGM held on 4 May 2009 invited two members from amongst the BSB shareholders who accepted the Bank's share exchange offer. Today, we are privileged to have Sheikh Abdulelah Mohammed Kaki and Mr Salman Saleh Al Mahmeed as part of the Board of Directors. Furthermore, the shareholders also resolved to amend the articles of association of the Bank to pass the Bank's obligation to pay Zakah from the earnings on to the shareholders effective 1 January 2009. These resolutions were implemented by the Bank.

Financially, fiscal year 2009 had seen a decline in net profit from BD25.5 million in 2008 to BD14 million in 2009, representing a return on equity of 7.6% (2008:16.1%). The gross operating income amounted to BD23.9 million (2008: BD37.6 million) and the operating expenses were BD9.4 million (2008: BD11.8 million). The reduction in the operating expenses is attributable to prudent cost management. The cost-to-income ratio for the year was 40.6% (2008:31.3%). The earnings per share (EPS) for the year amounted to 10.7 fils (2008: 21.3 fils). The directors have recommended cash dividend of 5 fils per share or 5% of the paid-up capital with a further 5% of the paid-up capital as bonus shares subject to shareholders' approval in the forthcoming Annual General Meeting.

**Retained earnings and appropriation of net income:**

	<b>BD'000</b>
<b>Balance at beginning of the year</b>	<b>12,575</b>
Net profit for the year – 2009	13,960
Transfer to statutory reserve	(1,396)
Transfer to investment reserve	(5,772)
Stock dividend	(7,129)
Proposed dividends	(7,129)
Charitable contributions	(100)
<b>Balance at end of the year</b>	<b><u>5,009</u></b>

Directors' and senior management interest:

As required by the Central Bank of Bahrain rule book set out below are the interests of Directors and Senior Managers in the shares of Al Salam Bank-Bahrain B.S.C. and the distribution of the shareholdings as of 31 December 2009.

	<b><u>31/12/2009</u></b>
Directors' shares	118,414,178
Senior Managers' shares	4,208,812
	<b><u>122,622,990</u></b>

Directors' remuneration, fees and expenses for attendance at Board meetings for 2009 amounted to BD250,000 (2008: BD 320,000).

<b>Percentage of shares held</b>	<b><u>No. of shares</u></b>	<b><u>2009 No. of Shareholders</u></b>	<b><u>% of total Outstanding shares</u></b>
Less than 0.5%	658,205,954	23,248	46.2
0.5% to less than 1%	264,097,908	25	18.5
1% up to less than 5%	362,504,950	15	25.4
Over 5%	140,966,263	1	9.9
<b>Total</b>	<b><u>1,425,775,075</u></b>	<b><u>23,289</u></b>	<b><u>100.00</u></b>

The Directors would like to express their appreciation to the leadership and ministries of the Kingdom of Bahrain, the Central Bank of Bahrain, correspondents, customers, shareholders and employees of the Bank for their support and collective contribution since the establishment of the Bank and we look forward to their continued support in the fiscal year 2010.

15 February 2010  
Manama, Kingdom of Bahrain

  
Mohammed Ali Rashid Alabbar  
Chairman

## **INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF AL SALAM BANK-BAHRAIN B.S.C.**

We have audited the accompanying consolidated statement of financial position of Al Salam Bank-Bahrain B.S.C. ("the Bank") and its subsidiary (together "the Group") as of 31 December 2009, and the related consolidated statements of income, comprehensive 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 Group's Board of Directors. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

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

The Board of Directors is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with the Financial Accounting Standards issued by the Accounting and Auditing Organisation for Islamic Financial Institutions and to operate in accordance with Islamic Shari'a. This responsibility includes: designing, implementing and maintaining internal controls relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

### **Auditors' Responsibility**

We conducted our audit in accordance with both International Standards on Auditing and Auditing Standards for Islamic Financial Institutions. 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 involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgement, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate for the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal controls. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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



INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF  
AL SALAM BANK-BAHRAIN B.S.C. (continued)

**Opinion**

In our opinion, the consolidated financial statements present fairly, in all material respects the consolidated financial position of the Group as of 31 December 2009, the results of its operations, its cash flows and changes in equity for the year then ended in accordance with the Financial Accounting Standards issued by the Accounting and Auditing Organization for Islamic Financial Institutions and the Islamic Shari'a Rules and Principles as determined by the Shari'a Supervisory Board of the Group.

**Other Regulatory Matters**

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

15 February 2010  
Manama, Kingdom of Bahrain

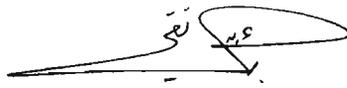
## CONSOLIDATED STATEMENT OF FINANCIAL POSITION

31 December 2009

		<i>31 December</i>	<i>31 December</i>
		<i>2009</i>	<i>2008</i>
	<i>Notes</i>	<i>BD</i>	<i>BD</i>
<b>ASSETS</b>			
Cash and balances with Central Bank of Bahrain	5	126,739,202	83,533,981
Central Bank of Bahrain Sukuk		32,907,875	31,095,000
Murabaha receivables from banks	6	149,303,782	87,167,449
Corporate Sukuk		16,949,546	-
Murabaha and Mudaraba receivables	7	87,273,825	72,483,745
Ijarah Muntahia Bittamleek	8	46,314,651	41,530,784
Musharaka financing		5,384,369	-
Assets under conversion	9	98,305,000	-
Non-trading investments	10	184,679,822	116,929,500
Investment in an associate	11	7,659,055	8,011,913
Investment property		1,177,528	1,177,528
Receivables and prepayments	12	26,902,192	21,032,829
Premises and equipment		2,337,436	2,583,796
Assets held-for-sale		-	88,934,033
<b>TOTAL ASSETS</b>		<b>785,934,283</b>	<b>554,480,558</b>
<b>LIABILITIES, UNRESTRICTED INVESTMENT ACCOUNTS AND EQUITY</b>			
<b>LIABILITIES</b>			
Murabaha and Wakala payables to banks		89,397,722	32,880,685
Wakala from non-banks		317,369,585	289,004,770
Customers' current accounts		32,699,944	42,985,844
Liabilities under conversion	9	120,402,000	-
Other liabilities	13	14,877,262	10,755,559
<b>TOTAL LIABILITIES</b>		<b>574,746,513</b>	<b>375,626,858</b>
<b>UNRESTRICTED INVESTMENT ACCOUNTS</b>	14	<b>9,409,467</b>	<b>6,370,219</b>
<b>EQUITY</b>			
Share capital	15	142,577,508	120,000,000
Reserves and retained earnings	15	41,356,388	39,660,956
Proposed appropriations	15	14,257,750	12,822,525
Total equity attributable to shareholders of the Bank		198,191,646	172,483,481
Non-controlling interest		3,586,657	-
<b>TOTAL EQUITY</b>		<b>201,778,303</b>	<b>172,483,481</b>
<b>TOTAL LIABILITIES, UNRESTRICTED INVESTMENT ACCOUNTS AND EQUITY</b>		<b>785,934,283</b>	<b>554,480,558</b>

These consolidated financial statements have been authorised for issue in accordance with a resolution of the Board of Directors dated 15 February 2010.

  
 Mohamed Ali Rashid Alabbar  
 Chairman

  
 Youusif Taqi  
 Director & Chief Executive Officer

Al Salam Bank-Bahrain B.S.C.

CONSOLIDATED INCOME STATEMENT

Year ended 31 December 2009

	<i>31 December</i> <b>2009</b> <i>BD</i>	<i>31 December</i> <b>2008</b> <i>BD</i>
<b>OPERATING INCOME</b>		
Income from financing contracts	<b>16,710,523</b>	14,087,135
Gains on disposal of investments	<b>11,781,651</b>	30,266,556
Gains on investments designated as fair value through profit or loss	<b>5,772,270</b>	5,259,691
Other operating income (Note 16)	<b>911,486</b>	2,300,596
	<b>35,175,930</b>	51,913,978
Less: Profit paid and payable on Murabaha and Wakala from banks	<b>(1,118,975)</b>	(2,489,667)
Less: Profit on Wakala from non-banks	<b>(13,928,052)</b>	(9,279,138)
Less: Profit on unrestricted investment accounts	<b>(155,520)</b>	(219,939)
Less: Depreciation on Ijarah Muntahia Bittamleek (Note 8)	<b>(4,037,647)</b>	(2,323,976)
<b>TOTAL OPERATING INCOME</b>	<b>15,935,736</b>	37,601,258
<b>OPERATING EXPENSES</b>		
Staff costs	<b>5,130,940</b>	6,854,616
Premises and equipment cost	<b>723,322</b>	582,745
Depreciation	<b>1,009,690</b>	902,526
Other operating expenses	<b>2,853,219</b>	3,438,451
Total operating expenses	<b>9,717,171</b>	11,778,338
<b>PROFIT BEFORE RESULTS OF SUBSIDIARY AND ASSOCIATE</b>	<b>6,218,565</b>	25,822,920
Gain arising on acquisition of a subsidiary (Note 3)	<b>7,996,039</b>	-
Share of loss from an associate (Note 11)	<b>(254,224)</b>	(280,239)
Post acquisition profit from the subsidiary	<b>21,000</b>	-
Share of Shari'a prohibited income contributed to charity	<b>(18,965)</b>	-
<b>NET PROFIT FOR THE YEAR</b>	<b>13,962,415</b>	25,542,681
<i>Attributable to:</i>		
Equity holders of the Bank	<b>13,960,380</b>	25,542,681
Non-controlling interest	<b>2,035</b>	-
	<b>13,962,415</b>	25,542,681
<b>WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING</b>	<b>1,300,825,581</b>	1,200,000,000
<b>BASIC AND DILUTED EARNINGS PER SHARE (FILS)</b>	<b>10.7</b>	21.3

The attached notes 1 to 30 form part of these consolidated financial statements.

Al Salam Bank-Bahrain B.S.C.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

Year ended 31 December 2009

	<i>31 December</i> <b>2009</b> <i>BD</i>	<i>31 December</i> 2008 <i>BD</i>
<b>NET PROFIT FOR THE YEAR</b>	<b>13,962,415</b>	25,542,681
Other comprehensive income:		
Net change in fair value	<b>(367,968)</b>	-
Exchange differences on investment in an associate	<b>(98,634)</b>	99,010
<b>Other comprehensive income for the year</b>	<b>(466,602)</b>	99,010
<b>TOTAL COMPREHENSIVE INCOME FOR THE YEAR</b>	<b>13,495,813</b>	25,641,691
<i>Attributable to:</i>		
Equity holders of the Bank	<b>13,480,309</b>	25,641,691
Non-controlling interest	<b>15,504</b>	-
	<b>13,495,813</b>	25,641,691

Al Salam Bank-Bahrain B.S.C.

CONSOLIDATED STATEMENT OF CASH FLOWS

Year ended 31 December 2009

	<i>31 December 2009 BD</i>	<i>31 December 2008 BD</i>
<b>OPERATING ACTIVITIES</b>		
Net profit for the year	13,962,415	25,542,681
Adjustments:		
Depreciation	1,009,690	902,526
Unrealised (gains) / losses on investments designated as fair value through profit or loss	(5,772,270)	2,050,309
Share of loss from an associate	254,224	280,239
Operating income before changes in operating assets and liabilities	<u>9,454,059</u>	<u>28,775,755</u>
<b>Changes in operating assets and liabilities:</b>		
Mandatory reserve with Central Bank of Bahrain	(4,486,000)	(7,241,000)
Central Bank of Bahrain Sukuk	(1,812,875)	(10,715,000)
Murabaha receivables from banks with original maturities of 90 days or more	1,497,724	(1,240,065)
Corporate Sukuk	(17,456,513)	-
Murabaha and Mudaraba receivables	(14,790,080)	(39,842,146)
Ijarah Muntahia Bittamleek	(4,783,867)	(31,094,920)
Musharaka financing	(5,384,369)	-
Assets under conversion	9,030,000	-
Non-trading investments, net	(1,208,099)	(56,244,113)
Receivables and prepayments	(12,472,402)	(10,527,784)
Assets held-for-sale	28,164,080	(79,910,033)
Murabaha and Wakala payables to banks	56,517,037	(64,102,356)
Wakala from non-banks	28,364,815	182,096,061
Customers' current accounts	(10,285,900)	37,297,159
Liabilities under conversion	(6,262,000)	-
Other liabilities	(459,787)	1,250,688
Net cash from (used in) operating activities	<u>53,625,823</u>	<u>(51,497,754)</u>
<b>INVESTING ACTIVITIES</b>		
Cash flow arising on acquisition of a subsidiary	58,092,000	-
Purchase of premises and equipment	(265,331)	(507,070)
Net cash from (used in) investing activities	<u>57,826,669</u>	<u>(507,070)</u>
<b>FINANCING ACTIVITIES</b>		
Unrestricted investment accounts	3,039,248	(13,399,366)
Share issue expenses	(136,427)	-
Dividends	(12,000,000)	(12,000,000)
Net movement in non-controlling interests	(2,035)	-
Net cash used in financing activities	<u>(9,099,214)</u>	<u>(25,399,366)</u>
<b>NET CHANGE IN CASH AND CASH EQUIVALENTS</b>	<b>102,353,278</b>	<b>(77,404,190)</b>
Cash and cash equivalents at 1 January	<u>156,204,000</u>	<u>233,608,190</u>
<b>CASH AND CASH EQUIVALENTS AT 31 DECEMBER</b>	<b><u>258,557,278</u></b>	<b><u>156,204,000</u></b>
<b>Cash and cash equivalents comprise of:</b>		
Cash and other balances with Central Bank of Bahrain (Note 5)	104,616,277	67,263,285
Balances with other banks (Note 5)	4,755,925	3,389,696
Murabaha receivables from banks with original maturities of less than 90 days	149,185,076	85,551,019
	<u>258,557,278</u>	<u>156,204,000</u>

The attached notes 1 to 30 form part of these consolidated financial statements.

Al Salam Bank-Bahrain B.S.C.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

Year ended 31 December 2009

	Attributable to equity holders of the Bank										
	<i>Share capital</i>	<i>Statutory reserve</i>	<i>Retained earnings</i>	<i>Investment reserve</i>	<i>Changes in fair value</i>	<i>Foreign exchange translation reserve</i>	<i>Share premium reserve</i>	<i>Proposed appropriations</i>	<i>Total</i>	<i>Non-controlling interest</i>	<i>Total equity</i>
	<i>BD</i>	<i>BD</i>	<i>BD</i>	<i>BD</i>		<i>BD</i>	<i>BD</i>	<i>BD</i>	<i>BD</i>	<i>BD</i>	<i>BD</i>
Balance as of 1 January 2008	120,000,000	3,959,869	12,458,881	22,523,040	-	-	-	529,087	159,470,877	-	159,470,877
Total comprehensive income for the year	-	-	25,542,681	-	-	99,010	-	-	25,641,691	-	25,641,691
Zakah on 2008 earnings	-	-	(822,525)	-	-	-	-	822,525	-	-	-
Charitable donations	-	-	(100,000)	-	-	-	-	-	(100,000)	-	(100,000)
Transfer from investment reserve	-	-	2,050,309	(2,050,309)	-	-	-	-	-	-	-
Transfer to statutory reserve	-	2,554,268	(2,554,268)	-	-	-	-	-	-	-	-
Zakah paid	-	-	-	-	-	-	-	(529,087)	(529,087)	-	(529,087)
Zakah contribution	-	-	-	-	-	-	-	-	-	-	-
Dividends paid for 2007	-	-	(12,000,000)	-	-	-	-	-	(12,000,000)	-	(12,000,000)
Proposed dividends for 2008	-	-	(12,000,000)	-	-	-	-	12,000,000	-	-	-
	-	2,554,268	116,197	(2,050,309)	-	99,010	-	12,293,438	13,012,604	-	13,012,604
Balance at 31 December 2008	120,000,000	6,514,137	12,575,078	20,472,731	-	99,010	-	12,822,525	172,483,481	-	172,483,481
<b>Non-controlling interest arising on acquisition of a subsidiary (Note 3)</b>	-	-	-	-	-	-	-	-	-	<b>3,571,153</b>	<b>3,571,153</b>
<b>Total comprehensive income for the year</b>	-	-	13,960,380	-	-	-	-	-	13,960,380	2,035	13,962,415
<b>Other Comprehensive income:</b>											
Changes on investment in an associate	-	-	-	-	-	(98,634)	-	-	(98,634)	-	(98,634)
Net change in fair value	-	-	-	-	(381,437)	-	-	-	(381,437)	13,469	(367,968)
<b>Total comprehensive income - 2009</b>	-	-	<b>13,960,380</b>	-	<b>(381,437)</b>	<b>(98,634)</b>	-	-	<b>13,480,309</b>	<b>15,504</b>	<b>13,495,813</b>
	<b>120,000,000</b>	<b>6,514,137</b>	<b>26,535,458</b>	<b>20,472,731</b>	<b>(381,437)</b>	<b>376</b>	-	<b>12,822,525</b>	<b>185,963,790</b>	<b>15,504</b>	<b>185,979,294</b>
Transfer to investment reserve	-	-	(5,772,270)	5,772,270	-	-	-	-	-	-	-
Transfer to statutory reserve	-	1,396,038	(1,396,038)	-	-	-	-	-	-	-	-
Zakah paid	-	-	-	-	-	-	-	(822,525)	(822,525)	-	(822,525)
Charitable donations	-	-	(100,000)	-	-	-	-	-	(100,000)	-	(100,000)
Dividends paid for 2008	-	-	-	-	-	-	-	(12,000,000)	(12,000,000)	-	(12,000,000)
Proposed dividends for 2009 (Note 15.4)	-	-	(14,257,750)	-	-	-	-	14,257,750	-	-	-
Shares issued (Notes 3 and 15.1)	22,577,508	-	-	-	-	-	2,709,300	-	25,286,808	-	25,286,808
Share issue expenses	-	-	-	-	-	-	(136,427)	-	(136,427)	-	(136,427)
<b>Balance at 31 December 2009</b>	<b>142,577,508</b>	<b>7,910,175</b>	<b>5,009,400</b>	<b>26,245,001</b>	<b>(381,437)</b>	<b>376</b>	<b>2,572,873</b>	<b>14,257,750</b>	<b>198,191,646</b>	<b>3,586,657</b>	<b>201,778,303</b>

The attached notes 1 to 30 form part of these consolidated financial statements.

## 1 INCORPORATION AND PRINCIPAL ACTIVITIES

The parent company, Al Salam Bank-Bahrain B.S.C. ("the Bank") was incorporated in the Kingdom of Bahrain under the Bahrain Commercial Companies Law No. 21/2001 and was registered with Ministry of Industry and Commerce under Commercial Registration Number 59308 on 19 January 2006. The Bank is regulated and supervised by the Central Bank of Bahrain ("the CBB") and has an Islamic retail banking license and is operating under Islamic principles, and in accordance with all the relevant regulatory guidelines for Islamic banks issued by the CBB. The Bank's registered office is P.O. Box 18282, Building 22, Avenue 58, Block 436, Al Seef District, Kingdom of Bahrain.

During the year, the Bank acquired a 90.31% stake in Bahraini Saudi Bank B.S.C. (BSB), a publicly listed commercial bank in the Kingdom of Bahrain. BSB operates under a retail banking license issued by the Central Bank of Bahrain. BSB has applied for an Islamic retail banking license with the CBB and is awaiting approval. Subsequent to acquisition by the Bank, BSB has discontinued new conventional activities and the conversion into a fully compliant Islamic operations is in progress.

The Bank and its subsidiary BSB (together known as "the Group") operate through eight retail branches in the Kingdom of Bahrain. The Bank offers a full range of Shari'a-compliant banking services and products. The activities of the Bank include accepting money market placements, managing profit sharing investment accounts, offering Islamic financing contracts, dealing in Shari'a-compliant financial instruments as principal/agent, managing Shari'a-compliant financial instruments and other activities permitted for under the CBB's Regulated Banking Services as defined in the licensing framework.

## 2 ACCOUNTING POLICIES

### 2.1 BASIS OF PREPARATION

The consolidated financial statements are prepared on a historical cost basis, except for investments held at fair value through profit or loss, available-for-sale investments and investment properties. These consolidated financial statements incorporate all assets, liabilities and off balance sheet financial instruments held by the Group. Investment in Al Salam Bank-Algeria is equity accounted as per IAS 28, Investment in Associates (Note 11).

These consolidated financial statements are presented in Bahraini dinars, being the functional and presentation currency of the Group.

#### Statement of compliance

The consolidated financial statements of the Group are prepared in accordance with the Financial Accounting Standards (FAS) issued by the Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI) and in conformity with the Bahrain Commercial Companies Law and the Central Bank of Bahrain and Financial Institutions Law. In accordance with AAOIFI, for matters for which no AAOIFI standards exist, the Group uses the relevant International Financial Reporting Standard.

The Group presents its consolidated statement of financial position broadly in order of liquidity. An analysis regarding recovery or settlement within 12 months after the consolidated statement of financial position date (current) and more than 12 months after the consolidated statement of financial position date (non-current) is presented in Note 22.

#### Basis of consolidation

The consolidated financial statements comprise the financial statements of the Bank and its subsidiary for the year ended 31 December 2009. The financial statements of the Bank's subsidiary is prepared for the same reporting year as the Bank, using consistent accounting policies. Non Shari'a compliant assets and liabilities of the subsidiary are consolidated as set out in Note 9.

Subsidiaries are fully consolidated from the date on which control is transferred to the Bank. Control is achieved where the Bank has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The results of subsidiaries acquired during the year are included in the consolidated income statement from the date of gaining control over the subsidiary.

**2 ACCOUNTING POLICIES (continued)**

**2.1 BASIS OF PREPARATION (continued)**

Non-controlling interests represent the portion of profit or loss and net assets not owned, directly or indirectly, by the Group and are presented separately in the consolidated income statement and within equity in the consolidated statement of financial position, separately from parent shareholders' equity.

**2.2 SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES**

The preparation of the consolidated financial statements requires management to make judgements and estimates that affect the reported amount of financial assets and liabilities and disclosure of contingent liabilities. These judgements and estimates also affect the revenues and expenses and the resultant provisions as well as fair value changes reported in equity.

Judgements are made in the classification of fair value through profit or loss, assets held for sale or held-to-maturity investments based on management's intention at acquisition of the financial asset. As fully described below, judgements are also made in determination of the objective evidence that a financial asset is impaired.

*Classification of investments*

Management decides upon acquisition of an investment whether it should be classified as fair value through profit or loss, available for sale or held-to-maturity.

*Impairment of available-for-sale equity investments*

The Group treats available-for-sale equity investments as impaired when there has been a significant or prolonged decline in the fair value below its cost or where other objective evidence of impairment exists. In addition, the Group evaluates other factors, including normal volatility in share price for quoted equities and the future cash flows and the discount factors for unquoted equities.

**Estimation uncertainty**

The key assumptions concerning the future and other key sources of estimating uncertainty at the date of the statement of financial position, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below:

*Impairment losses on financial contracts*

The Group reviews its financial contracts on a regular basis to assess whether a provision for impairment should be recorded in the consolidated statement of income. In particular, considerable judgement 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.

*Collective impairment provisions on financial contracts*

In addition to specific provisions against individually significant financial contracts, the Group also considers the need for a collective impairment provision against financial contracts which although not specifically identified as requiring a specific provision, have a greater risk of default than when originally granted. This collective provision is based on any deterioration in the status, as determined by the Group, of the financial contracts since they were granted (acquired). The amount of the provision is based on the historical loss pattern for other contracts within each grade and is adjusted to reflect current economic changes.

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**2 ACCOUNTING POLICIES (continued)**

**2.2 SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES (continued)**

*Valuation of unquoted private equity and real estate investments*

Valuation of above investments is normally based on one of the following:

- valuation by independent external valuers;
- recent arm's length market transactions;
- current fair value of another instrument that is substantially the same;
- present value of expected cash flows at current rates applicable for items with similar terms and risk characteristics; or
- other valuation models.

The Group calibrates the valuation techniques periodically and tests these for validity using either prices from observable current market transactions in the same instrument or other available observable market data.

**2.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

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

**a) Financial contracts**

Financial contracts consist of cash and balances with banks and the Central Bank of Bahrain, Murabaha receivables (net of deferred profit), Mudaraba, Musharaka and Ijarah Muntahia Bittamleek. Balances relating to these contracts are stated net of provisions for impairment.

**b) Corporate sukuk**

These are quoted securities and classified as available-for-sale. These are recorded at the amortised cost and remeasured at fair value. Changes in fair value are recognized in the other comprehensive income until the investment is derecognised or the investment is determined to be impaired, upon which the cumulative fair value is transferred to consolidated income statement.

**c) Murabaha and Mudaraba receivables**

Murabaha and Mudaraba receivables are stated net of provision for impairment and deferred profits.

**d) Ijarah Muntahia Bittamleek**

Ijarah Muntahia Bittamleek assets comprises assets under lease, comprising aircraft, land and buildings, under terms that would transfer ownership of the assets to third parties at the end of the respective lease term.

Depreciation is provided on a straight-line basis on all Ijarah Muntahia Bittamleek assets other than land (which is deemed to have an indefinite life), at rates calculated to write off the cost of each asset over the short of either period of the lease or economic life of the asset.

**e) Musharaka**

These are initially stated at the fair value of the consideration given and subsequently remeasured at amortised cost less provision for impairment in value, if any.

**f) Assets and liabilities under conversion**

These represent assets and liabilities of BSB which are under conversion to Shari'a compliant products. These are initially measured at fair value at the date of acquisition and the subsequent measurement is as follows:

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**2 ACCOUNTING POLICIES (continued)**

**2.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

**f) Assets and liabilities under conversion (continued)**

*Assets under conversion:*

*Due from Banks and Loans and advances to customers:*

At amortised cost less any amounts written off and provision for impairment.

*Investments:*

These are classified as available-for-sale investments and are fair valued based on criteria set out in Note 2.3 g. Any changes in fair values subsequent to acquisition date are recognized in other comprehensive income.

*Liabilities under conversion:*

These are remeasured at amortised cost.

**g) Non-trading investments**

These are classified as held-to-maturity, available-for-sale or fair value through profit or loss.

All investments are initially recognised at cost, being the fair value of the consideration given including acquisition costs associated with the investment. Acquisition cost relating to investments designated as fair value through profit and loss is charged to consolidated income statement.

Following the initial recognition of investments, the subsequent period-end reporting values are determined as follows:

***Investments held-to-maturity***

Investments which have fixed or determinable payments and fixed maturity which are intended to be held-to-maturity, are carried at amortised cost, less provision for impairment in value.

***Investments available-for-sale***

After initial recognition, investments which are classified "available-for-sale" are normally remeasured at fair value, unless the fair value cannot be reliably determined, in which case they are measured at cost less impairment. Fair value changes are reported in the other comprehensive income until the investment is derecognised or the investment is determined to be impaired. On derecognition or impairment the cumulative gain or loss previously reported as "cumulative changes in fair value" within equity, is included in the consolidated income statement.

***Investments carried at fair value through profit or loss***

Investments in this category are designated as such on initial recognition if these investments are evaluated on a fair value basis in accordance with the Group's risk management policy and its investment strategy. These include all private equity investments including those in joint ventures and associates.

Investments at fair value through profit or loss are recorded in the balance sheet at fair value. Changes in fair value are recorded as "Gains on investments designated at fair value through profit or loss" in the consolidated income statement.

**h) Investment reserve**

Unrealised gains and losses resulting from revaluation of "investments carried at fair value through profit or loss" and "investment properties" recorded in the consolidated statement of income are appropriated to an investment reserve in equity and are not available for distribution to the shareholders. Upon disposal of such assets, the related cumulative gains or losses are transferred to retained earnings and become available for distribution.

**2 ACCOUNTING POLICIES (continued)**

**2.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

**i) Investment in an associate**

The Group's investments in its associates, that are acquired for strategic purposes, are accounted for under the equity method of accounting. Other equity investments in associates are accounted for as fair value through profit or loss by availing the scope exemption under IAS 28, Investments in associates. An associate is an entity over which the Group has significant influence and which is neither a subsidiary nor a joint venture. An entity is considered as an associate if the Group has more than 20% ownership of the entity or the Group has significant influence through any other mode.

Under the equity method, the investment in the associate is carried in the balance sheet at cost plus post-acquisition changes in the Group's share of net assets of the associate. Losses in excess of the cost of the investment in an associate are recognised when the Group has incurred obligations on its behalf. Goodwill relating to an associate is included in the carrying amount of the investment and is not amortised. The consolidated income statement reflects the Group's share of results of operations of the associate. Where there has been a change recognised directly in the equity of the associate, the Group recognises its share of any changes and discloses this, when applicable, in the consolidated statement of changes in equity.

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

After application of the equity method, the Group determines whether it is necessary to recognise an additional impairment loss on its investment in associates. The Group determines at each balance sheet date whether there is any objective evidence that the investment in associates are 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 income statement.

Profit and losses resulting from transactions between the Group and the associates are eliminated to the extent of the interest in associates.

Foreign exchange translation gains/losses arising out of the above investment in the associate are included in the other comprehensive income.

**j) Investment properties**

Investment properties are those held to earn rentals and/or for capital appreciation. These are initially recorded at cost, including acquisition charges associated with the property.

Subsequent to initial recognition, all investment properties are remeasured at fair value and changes in fair value are recognised in the consolidated statement of income as gain or loss in investment properties. The fair value of the investment properties is determined either based on valuations made by independent valuers or using internal models with consistent assumptions.

**k) Premises and equipment**

Premises and equipment are stated at cost less accumulated depreciation and any impairment in value. Depreciation is provided on a straight-line basis over the estimated useful lives of all premises and equipment, other than freehold land and capital work-in-progress.

- Computer hardware and software	3 to 5 years
- Furniture and office equipment	3 to 5 years
- Motor vehicle	5 years
- Leasehold Improvements	Over the lease period

**2 ACCOUNTING POLICIES (continued)**

**2.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

**l) Subsidiaries acquired with a view to sell**

A subsidiary acquired with a view to subsequent disposal within 12 months are classified as "held-for-sale" when the sale is highly probable. Related assets and liabilities of the subsidiary are shown separately on the balance sheet as "Assets held-for-sale" and "Liabilities relating to assets held-for-sale". Assets that are classified as held-for-sale are measured at the lower of carrying amount and fair value less costs to sell. Any resulting impairment loss reduces the carrying amount of the assets. Assets that are classified as held-for-sale are not depreciated.

Any impairment loss is recognised in the consolidated income statement for any initial and subsequent write down of these assets to fair value, less costs to sell. A gain for any subsequent increase in the fair value, less costs to sell, is recognised to the extent that it is not in excess of the cumulative impairment loss that was recognised.

**m) Business Combinations and goodwill**

Business combinations are accounted for using the purchase method of accounting. This involves recognising identifiable assets (including previously unrecognised intangible assets) and liabilities (including contingent liabilities and excluding future restructuring) of the acquired business at fair value. Any excess of the cost of acquisition over the fair values of the identifiable net assets acquired is recognised as goodwill. If the cost of acquisition is less than the fair values of the identifiable net assets acquired, the discount on acquisition is recognised directly in the consolidated income statement in the year of acquisition.

Goodwill acquired in a business combination is initially measured at cost, being the excess of the cost of the business combination over the Bank's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities acquired. Gain on business combination, being the excess of the Bank's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities acquired over the cost of business acquisition is recognised as gain in the consolidated statement of income.

Following initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill is reviewed for impairment annually, or more frequently, if events or changes in circumstances indicate that the carrying value may be impaired.

**n) Impairment and uncollectability of financial assets**

An assessment is made at each statement of financial position date to determine whether there is objective evidence that a specific financial asset may be impaired. If such evidence exists, any impairment loss, is recognised in the consolidated income statement.

Impairment is determined as follows:

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

For available-for-sale equity investments reversal of impairment losses are recorded as increases in cumulative changes in fair value through equity.

In addition, a collective provision is made to cover impairment for specific assets where there is a measurable decrease in estimated future cash flows.

**o) Offsetting**

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

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**2 ACCOUNTING POLICIES (continued)**

**2.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

**p) Provisions**

Provisions are recognised when the Group 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.

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

The Group provides end of service benefits to its expatriate employees. Entitlement to these benefits is based upon the employees' final salary and length of service, subject to completion of a minimum service period. The expected costs of these benefits are accrued over the period of employment.

For Bahraini employees, the Group makes contributions to Social Insurance Organisation calculated as a percentage of the employees' salaries. The Group's obligations are limited to these contributions, which are expensed when due.

**r) Revenue recognition**

*Murabaha*

As the income is quantifiable and contractually determined at the commencement of the contract, income is amortized on a straight-line basis. Amortization of income is suspended when the Group believes that the recovery of these amounts may be doubtful or normally when the payments of Murabaha installments are overdue by 90 days, whichever is earlier.

*Corporate sukuk*

Income on Corporate sukuk is recognized on a time-proportionate basis based on underlying profit rate of the sukuk. Accrual of income is suspended when the Group believes that the recovery of these amounts may be doubtful or normally when the payments are overdue by 90 days, whichever is earlier.

*Mudaraba*

Income on Mudaraba transactions are recognised when the right to receive is established or these are declared by the Mudarib, whichever is earlier.

*Dividends*

Dividend income is recognised when the Group's right to receive the payment is established.

*Ijarah Muntahia Bittamleek*

Ijarah Muntahia Bittamleek income is recognised on a time-proportionate basis over the lease term. Income related to non-performing Ijarah Muntahia Bittamleek is suspended. Accrual of income is suspended when the Group believes that the recovery of these amounts may be doubtful or normally when the rental payments are overdue by 90 days, whichever is earlier.

*Musharaka*

Income on Musharaka is recognized when the right to receive payment is established or on distributions.

*Fees and commission income*

The Group earns fee and commission income from a diverse range of services it provides to its customers. Fee income can be divided into the following main categories:

Fee income on financing transactions: Fee earned on financing transactions including up-front fees and early settlement fees are recognised when earned. To the extent the fees are deemed yield enhancement they are recognised over the period of the financing contracts.

Fee income from transaction services: Fee arising from corporate finance, corporate advisory, arranging the sale of assets and wealth management are recognised when earned or on a time proportionate basis when the fee is linked to time.

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**2 ACCOUNTING POLICIES (continued)**

**2.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

**r) Revenue recognition (continued)**

*Fair value of financial assets*

For investments that are traded in organised financial markets, fair value is determined by reference to the prevailing market bid price on the balance sheet date.

For investments where there is no quoted market price, a reasonable estimate of fair value is determined by reference to valuation by independent external valuers or based on recent arm's length market transactions. Alternatively, the estimate would also be based on current market value of another instrument, which is substantially the same, or is based on the assessment of future cash flows. The cash equivalent values are determined by the Group at current profit rates for contracts with similar terms and risk characteristics.

For investments having fixed or determinable payments, fair value is based on the net present value of estimated future cash flows determined by the Group using current profit rates for investments with similar terms and risk characteristics.

**s) Foreign currencies**

Foreign currency transactions are recorded at rates of exchange prevailing at the dates of the transactions. Monetary assets and liabilities in foreign currencies at the statement of financial position date are retranslated at market rates of exchange prevailing at that date. Gains and losses arising on translation are recognised in the consolidated income statement. Non-monetary assets that are measured in terms of historical cost in foreign currencies are recorded at rates of exchange prevailing at the value dates of the transactions. Translation gains or losses on non-monetary items classified as "available-for-sale" and investment in associates are included in consolidated statement of changes in equity until the related assets are sold or derecognised at which time they are recognised in the consolidated income statement. Translation gains on non-monetary assets classified as "fair value through profit or loss" are directly recognised in the consolidated income statement.

**t) Trade and settlement date accounting**

Purchases and sales of financial assets are recognised on the trade date, i.e. the date that the Group purchases or sells the asset.

**u) Derecognition of 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:

- (i) the rights to receive cash flows from the asset have expired; or
- (ii) the Group has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass-through' arrangement; and
- (iii) either (a) the Group has transferred substantially all the risks and rewards of the asset, or (b) the Group has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred the control of the asset.

When the Group has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, 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. In that case, the Group also recognises an associated liability. The transferred asset and the associated liability are measured on a basis that reflects the rights and obligations that the Group has retained.

Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to pay.

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**2 ACCOUNTING POLICIES (continued)**

**2.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

**v) Derecognition of financial liabilities**

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires. Where an existing financial liability is replaced by another from the same source on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognised in the consolidated statement of income.

**w) Fiduciary assets**

Assets held in a fiduciary capacity are not treated as assets of the Group and are accordingly not shown in the consolidated statement of financial position.

**x) Dividends on ordinary shares**

Dividends on ordinary shares are recognised as a liability and deducted from equity when they are approved by the Bank's shareholders. Dividends for the year that are approved after the balance sheet date are included in the equity and are disclosed as an event after the balance sheet date.

**y) Unrestricted investment account holders (URIA)**

All unrestricted investment accounts are carried at capital received plus profit earned less amounts paid. Income to unrestricted investment account holders is allocated, net of Mudarib fees, on the basis of their average daily balances in proportion to shareholders' daily average balances.

**z) Zakah**

In accordance with the revised Articles of Association of the Bank, the responsibility to pay Zakah is on the shareholders of the Bank.

**aa) Cash and cash equivalents**

Cash and cash equivalents comprise cash and balances with Central Bank of Bahrain and Murabaha receivables from banks with maturities of less than 90 days from the date of acquisition.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

31 December 2009

**3 BUSINESS COMBINATION**

During the year, the Bank made an offer to acquire up to 100% of the issued and paid up shares of Bahraini Saudi Bank B.S.C. (BSB), a publicly listed commercial bank incorporated in the Kingdom of Bahrain, at an exchange ratio of one new share of the Bank for every two shares of BSB. The proposed acquisition through share exchange was approved by the shareholders of the Bank in their Extraordinary General Assembly Meeting held on 4 May 2009. The Bank acquired 90.31% stake in BSB and issued 225,775,075 ASBB new shares (Note 15.1). On 28 October 2009, the Board of BSB was reconstituted with three out of the five Board members of BSB representing ASBB gaining effective control over BSB.

The fair value of the identifiable assets and liabilities of BSB as of 28 October 2009 and the gain arising out of the acquisition are as follows:

	<i>Fair value</i> <i>BD</i>	<i>Carrying value</i> <i>BD</i>
<b>ASSETS ACQUIRED</b>		
Cash and balances at the Central Bank of Bahrain	58,092,000	58,092,000
Due from banks and financial institutions	5,680,000	5,680,000
Loans and advances to customers	72,281,000	79,857,000
Non-trading investments	28,870,000	30,310,000
Other assets	1,737,000	1,737,000
Premises and equipment	498,000	1,170,000
	<u>167,158,000</u>	<u>176,846,000</u>
<b>LESS: LIABILITIES ASSUMED</b>		
Due to banks and financial institutions	(22,452,000)	(22,452,000)
Customers' deposits	(103,811,000)	(103,811,000)
Other liabilities	(4,041,000)	(4,041,000)
	<u>(130,304,000)</u>	<u>(130,304,000)</u>
<b>FAIR VALUE OF NET ASSETS</b>	<u>36,854,000</u>	<u>46,542,000</u>
<b>GAIN ARISING ON ACQUISITION</b>		
Fair value of identifiable net assets acquired		36,854,000
Fair value of the consideration given (Note 15.1)		(25,286,808)
Fair value of non-controlling interest in BSB		(3,571,153)
<b>NEGATIVE GOODWILL</b>		<u>7,996,039</u>

The net cash inflow arising on acquisition amounted to BD 58,092,000. Other items including the issue of shares have been treated as non-cash item for the purpose of consolidated statement of cash flows.

From the date of acquisition, BSB has contributed BD 18,965 to the net profit of the Bank. If the combination had taken place at the beginning of the year, the Bank's share of net loss for the year would have been BD 3,661,167.



## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

31 December 2009

**4 CLASSIFICATION OF FINANCIAL INSTRUMENTS BY MEASUREMENT BASIS (continued)**

As at 31 December 2008, financial instruments were classified as follows:

	<i>Financial assets at fair value through profit or loss</i>	<i>Available for sale</i>	<i>Financial assets at cost / amortised cost</i>	<i>Total</i>
	<i>BD</i>	<i>BD</i>	<i>BD</i>	<i>BD</i>
<b>ASSETS</b>				
Cash and balances with				
Central Bank of Bahrain	-	-	83,533,981	83,533,981
Central Bank of Bahrain Sukuk	-	-	31,095,000	31,095,000
Murabaha receivables from banks	-	-	87,167,449	87,167,449
Murabaha and Mudaraba receivables	-	-	72,483,745	72,483,745
Ijarah Muntahia Bittamleek	-	-	41,530,784	41,530,784
Non-trading investments	116,929,500	-	-	116,929,500
Receivables	-	-	20,439,688	20,439,688
Assets held-for-sale	-	-	88,934,033	88,934,033
	<u>116,929,500</u>	<u>-</u>	<u>425,184,680</u>	<u>542,114,180</u>
<b>LIABILITIES AND UNRESTRICTED INVESTMENT ACCOUNTS</b>				
Murabaha and Wakala payables to banks	-	-	32,880,685	32,880,685
Wakala from non-banks	-	-	289,004,770	289,004,770
Customers' current accounts	-	-	42,985,844	42,985,844
Other liabilities	-	-	2,614,170	2,614,170
<b>UNRESTRICTED INVESTMENT ACCOUNTS</b>				
	-	-	6,370,219	6,370,219
	<u>-</u>	<u>-</u>	<u>373,855,688</u>	<u>373,855,688</u>

**5 CASH AND BALANCES WITH CENTRAL BANK OF BAHRAIN**

	<i>2009</i>	<i>2008</i>
	<i>BD</i>	<i>BD</i>
Mandatory reserve with Central Bank of Bahrain	<b>17,367,000</b>	12,881,000
Cash and other balances with Central Bank of Bahrain	<b>104,616,277</b>	67,263,285
Balances with other banks	<b>4,755,925</b>	3,389,696
	<u><b>126,739,202</b></u>	<u>83,533,981</u>

**6 MURABAHA RECEIVABLES FROM BANKS**

	<i>Up to 3 months 2009</i>	<i>Up to 3 months 2008</i>
	<i>BD</i>	<i>BD</i>
GCC	<b>149,303,782</b>	82,376,388
Europe	-	4,791,061
	<u><b>149,303,782</b></u>	<u>87,167,449</u>

Deferred profits on Murabaha receivables from banks amounted to BD 57,697 (2008: BD 31,685).

**7 MURABAHA AND MUDARABA RECEIVABLES**

Murabaha and Mudaraba receivables are shown net of deferred profits of BD9,664,651 (2008: BD8,026,806).

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**8 IJARAH MUNTAHIA BITTAMLEEK**

This represents net investments in assets leased for periods which either approximate or cover major parts of the estimated useful lives of such assets. The lease agreements stipulate that the lessor undertakes to transfer the leased assets to the lessee at the end of the lease term upon the lessee fulfilling all obligations under the lease agreement.

	<i>2009</i>	<i>2008</i>
	<i>BD</i>	<i>BD</i>
Movements in Ijarah Muntahia Bittamleek assets are as follows:		
At 1 January	<b>41,530,784</b>	10,435,863
Additions during the year	<b>8,821,514</b>	33,418,897
Ijarah assets depreciation - net	<b>(4,037,647)</b>	(2,323,976)
At 31 December	<b>46,314,651</b>	41,530,784

	<i>2009</i>	<i>2008</i>
	<i>BD</i>	<i>BD</i>
The future minimum lease receivable in aggregate are as follows:		
Due within one year	<b>17,183,480</b>	9,915,774
Due in one to five years	<b>22,179,292</b>	26,505,879
Due after five years	<b>6,951,879</b>	5,109,131
	<b>46,314,651</b>	41,530,784

	<i>2009</i>	<i>2008</i>
	<i>BD</i>	<i>BD</i>
Ijarah Muntahia Bittamleek are divided into the following asset classes:		
Aviation	<b>3,595,657</b>	3,836,702
Buildings	<b>42,718,994</b>	37,694,082
	<b>46,314,651</b>	41,530,784

The accumulated depreciation on assets subject to Ijarah amounted to BD 4,862,954 (31 December 2008: BD 3,464,322).

**9 ASSETS AND LIABILITIES UNDER CONVERSION**

These represent interest bearing non-Shari'a compliant assets and liabilities of BSB, a majority owned subsidiary of the Bank. At the balance sheet date, the conversion of the subsidiary into a fully compliant Islamic operations has just begun, accordingly these assets and liabilities have been reported as separate line items on the face of the consolidated statement of financial position. The details of these assets and liabilities under conversion are as follows:

	<i>BD</i>
<b>Assets</b>	
Due from banks and financial institutions	<b>6,839,000</b>
Loans and advances to customers	<b>63,770,000</b>
Non trading investments	<b>27,696,000</b>
	<b>98,305,000</b>
<b>Liabilities</b>	
Due to banks and financial institutions	<b>20,912,000</b>
Customers' deposits	<b>99,490,000</b>
	<b>120,402,000</b>

# Al Salam Bank-Bahrain B.S.C.

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### 9 ASSETS AND LIABILITIES UNDER CONVERSION (continued)

BSB has pledged certain investments with a financial institution having a carrying value of BD 22.5 million (2008: BD 25.8 million) as at 31 December 2009 against which there is no borrowing as at 31 December 2009 (2008: BD 9.4 million)

### 10 NON-TRADING INVESTMENTS

	<i>2009</i>	<i>2008</i>
	<i>BD</i>	<i>BD</i>
Quoted	<b>4,341,940</b>	4,045,637
Unquoted based on valuation techniques:		
- Market observable input	<b>137,201,435</b>	97,509,445
- Non-market observable input	<b>43,136,447</b>	15,374,418
	<b>184,679,822</b>	116,929,500

These represent investments designated as fair value through profit or loss and are carried at fair value.

Certain of these investments are recorded at fair value using valuation techniques as current market transactions or observable market data are not available. Their fair value is determined using a valuation model that has been tested against the prices of actual market transactions and using the Group's best estimate of the most appropriate model inputs.

### 11 INVESTMENT IN AN ASSOCIATE

The Group has investment in an associate, Al Salam Bank Algeria (ASBA), a bank incorporated in Algeria. Al Salam Bank Algeria is not listed on any stock exchange. The following table illustrates the summarised financial information of the Group's investment in ASBA:

	<i>2009</i>	<i>2008</i>
	<i>BD</i>	<i>BD</i>
Associate's balance sheet:		
Total assets	<b>69,691,689</b>	39,514,495
Total liabilities	<b>20,318,137</b>	3,224,932
Net assets	<b>49,373,552</b>	36,289,563
Total revenue	<b>1,076,952</b>	9,090
Total expenses	<b>2,842,396</b>	1,410,287
Net loss for the year	<b>(1,765,444)</b>	(1,401,197)
Group's share of associate's loss:	<b>(254,224)</b>	(280,239)

### 12 RECEIVABLES AND PREPAYMENTS

	<i>2009</i>	<i>2008</i>
	<i>BD</i>	<i>BD</i>
Profit receivable on Murabaha and Mudaraba	<b>1,250,769</b>	611,123
Rental receivable on Ijarah assets	<b>1,313,819</b>	278,838
Profit receivable on Sukuk	<b>263,221</b>	323,905
Prepayments	<b>688,395</b>	593,141
Other receivables	<b>23,385,988</b>	19,225,822
	<b>26,902,192</b>	21,032,829

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**12 RECEIVABLES AND PREPAYMENTS (continued)**

Other receivables include BD 17,892,079 relating to sale of investments. At 31 December 2008, the other receivables included BD 8,515,761 relating to sale of investments and majority of which was received during 2009.

**13 OTHER LIABILITIES**

	<i>2009</i>	<i>2008</i>
	<i>BD</i>	<i>BD</i>
Profit payable	<b>3,198,408</b>	2,614,170
Accounts payable and accruals	<b>7,274,517</b>	6,520,286
Dividends payable	<b>3,805,362</b>	1,504,598
End of service benefits	<b>598,975</b>	116,505
	<b><u>14,877,262</u></b>	<u>10,755,559</u>

**14 UNRESTRICTED INVESTMENT ACCOUNTS**

Unrestricted investment account holders' funds are commingled with the Bank's funds and used to fund / invest in Islamic financing contracts. According to the terms of acceptance of the unrestricted investment accounts, 100% of the funds are invested after deducting a mandatory reserve taking into consideration the relevant weightage, if any. Unrestricted investment accounts have no restriction on cash withdrawal. The Mudarib's share of profit ranges between 40% and 50%.

The Mudarib's share of profit during the year amounted to BD 152,010 (2008: BD 214,970). The average profit rate for the URIA holders is about 1.25% (2008: 2.5%)

During the current year, an amount of BD 39,754,541 which was included in unrestricted investment reserve as of 31 December 2008, has been reclassified to customers' current account to conform with current year presentation. This has not impacted the previously reported net income and total equity.

**15 EQUITY**

	<i>2009</i>	<i>2008</i>
	<i>BD</i>	<i>BD</i>
<b>15.1 SHARE CAPITAL</b>		
Authorised:		
2,000,000,000 (2008: 1,200,000,000) ordinary shares of BD 0.100 each	<b><u>200,000,000</u></b>	<u>120,000,000</u>
Issued and fully paid:		
Balance at the beginning of the year - 1,200,000,000 shares of BD 0.100 each	<b>120,000,000</b>	120,000,000
Issued during the year - 225,775,075 shares of BD 0.100 each (Note 3)	<b>22,577,508</b>	-
	<b><u>142,577,508</u></b>	<u>120,000,000</u>

Pursuant to a shareholders' resolution (Note 3), the Bank raised its authorised capital from BD 120 million to BD 200 million and issued 225,775,075 ordinary shares of ASBB to those shareholders of BSB who accepted the offer. At the offer closing date, the market price of the Bank's shares was BD 0.112 each. This resulted in proceeds of BD 25,286,808 from the new issue, including a share premium of BD 0.012 per share aggregating to BD 2,709,300.

**15.2 STATUTORY RESERVE**

As required by Bahrain Commercial Companies Law and the Bank's articles of association, 10% of the net profit for the year has been transferred to the statutory reserve. The Bank may resolve to discontinue such annual transfers when the reserve totals 50% of the paid up share capital of the Bank. The reserve is not distributable except in such circumstances as stipulated in the Bahrain Commercial Companies Law and following the approval of the Central Bank of Bahrain.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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**15 EQUITY (continued)**

## 15.3 INVESTMENT RESERVE

During the year the net unrealized gain of BD 5,772,270 (2008: net unrealized loss of BD 2,050,309) was transferred from retained earnings to investment reserve. The reserve represents unrealised gains and losses from revaluation of investments and investment properties carried at fair value though profit or loss, and is not available for distribution under the Bank's Shari'a policies until transferred back to retained earnings upon disposal of the assets and realisation of the gains.

## 15.4 PROPOSED APPROPRIATIONS

The Board of Directors in its meeting on 15 February 2010 has resolved to recommend a cash dividend of 5 fils per share or 5% of the increased paid-up capital (2008: 10 fils per share) and a further 5 fils or 5% of the paid-up capital as bonus shares, representing one bonus share for every twenty shares held subject to approval at the forthcoming annual general meeting.

**16 OTHER OPERATING INCOME**

	<i>2009</i>	<i>2008</i>
	<i>BD</i>	<i>BD</i>
Financing related fees and commissions	<b>233,536</b>	843,708
Transaction related fees	<b>50,901</b>	367,334
Fiduciary and other fees	<b>289,966</b>	840,504
Foreign exchange gains	<b>337,083</b>	249,050
	<b>911,486</b>	2,300,596

**17 RELATED PARTY TRANSACTIONS**

Related parties comprise major shareholders, directors of the Group, close members of their families, entities owned or controlled by them and companies affiliated by virtue of common ownership or directors with that of the Group. The transactions with these parties were made on commercial terms.

The significant balances with related parties at 31 December 2009 were as follows:

	<i>2009</i>			
	<i>Associates and joint ventures</i>	<i>Directors and related entities</i>	<i>Senior management</i>	<i>Total</i>
	<i>BD</i>	<i>BD</i>	<i>BD</i>	<i>BD</i>
<b>Assets:</b>				
Murabaha and Mudaraba receivables	<b>9,540,472</b>	<b>28,061</b>	<b>67,378</b>	<b>9,635,911</b>
Ijarah Muntahia Bittamleek	<b>14,097,973</b>	<b>3,595,657</b>	<b>178,189</b>	<b>17,871,819</b>
Musharaka financing	<b>5,234,068</b>	-	<b>99,165</b>	<b>5,333,233</b>
Assets under conversion	-	-	<b>27,000</b>	<b>27,000</b>
Receivables and prepayments	<b>2,733,999</b>	<b>8,795</b>	<b>14,672</b>	<b>2,757,466</b>
<b>Liabilities:</b>				
Wakala from non-banks	<b>15,593,252</b>	<b>511,091</b>	<b>311,761</b>	<b>16,416,104</b>
Customers' current accounts	<b>7,012,381</b>	<b>257,252</b>	<b>35,253</b>	<b>7,304,886</b>
Liabilities under conversion	-	-	<b>1,017,000</b>	<b>1,017,000</b>
Unrestricted investment accounts	<b>116,178</b>	<b>65,428</b>	<b>61,771</b>	<b>243,377</b>
Commitments	<b>4,623,584</b>	-	-	<b>4,623,584</b>
Contingent liabilities	<b>11,402,034</b>	<b>55,792</b>	-	<b>11,457,826</b>

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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**17 RELATED PARTY TRANSACTIONS (continued)**

The income and expenses in respect of related parties included in the consolidated financial statements are as follows:

	<i>2009</i>			
	<i>Associates and joint ventures BD</i>	<i>Directors and related entities BD</i>	<i>Senior management BD</i>	<i>Total BD</i>
<b>Income:</b>				
Income from other Islamic financing contracts	2,242,075	92,977	9,620	2,344,672
<b>Expenses:</b>				
Profit paid on Wakala from non-banks	281,460	33,515	14,197	329,172
Share of profits on unrestricted investment accounts	188	1,217	975	2,380
	<i>2008</i>			
	<i>Associates and joint ventures BD</i>	<i>Directors and related entities BD</i>	<i>Senior management BD</i>	<i>Total BD</i>
<b>Assets:</b>				
Murabaha and Mudaraba receivables	7,040,472	3,693,308	60,985	10,794,765
Ijarah Muntahia Bittamleek	12,556,290	6,301,531	179,595	19,037,416
Receivables and prepayments	8,669,913	91,225	14,583	8,775,721
<b>Liabilities:</b>				
Wakala from non-banks	26,966,966	141,577	1,031,541	28,140,084
Customer current accounts	-	180,255	49,004	229,259
Unrestricted investment accounts	3,242,180	100,680	44,142	3,387,002

The income and expenses in respect of related parties included in the consolidated financial statements are as

<b>Income:</b>				
Income from other Islamic financing contracts	605,768	419,558	15,731	1,041,057
Fees and commission income (Note 16)	40,905	-	-	40,905
<b>Expenses:</b>				
Profit paid on Wakala from non-banks	966,272	3,828	29,269	999,369
Share of profits on unrestricted investment accounts	-	192	4,879	5,071

As of 31 December 2009, Murabaha and Mudaraba receivables and Ijarah Muntahia Bittamleek included BD 3,595,657 (2008: BD3,693,308) of facilities provided to directors and their associates which are past due and on which profit is not being recognised.

Directors are compensated in the form of fees for attending board and committee meetings. Directors' remuneration, allowances and expenses for attending board and committee meetings for the year ended 31 December 2009 amounted to BD 250,000 (31 December 2008: BD 350,000).

Compensation of key management personnel, consisting solely of short-term benefits, paid during the year was BD 2,182,000 (2008: BD 2,753,000).

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**18 CONTINGENT LIABILITIES AND COMMITMENTS**

The Group has the following commitments:

	<b>2009</b>	<i>2008</i>
	<i>BD</i>	<i>BD</i>
<b>Contingent liabilities on behalf of customers</b>		
Guarantees	<b>19,077,412</b>	13,261,042
Letters of credit	<b>1,674,596</b>	-
Acceptances	<b>409,000</b>	-
	<b>21,161,008</b>	13,261,042
<b>Irrevocable Unutilised commitments</b>		
Unutilised financing commitments	<b>13,473,354</b>	2,434,840
Unutilised non-funded commitments	<b>7,424,343</b>	-
Unutilised capital commitments	<b>5,681,007</b>	5,027,488
	<b>26,578,704</b>	7,462,328
	<b>47,739,712</b>	20,723,370

Letters of credit, guarantees (including standby letters of credit) commit the Group to make payments on behalf of customers contingent upon their failure to perform under the terms of the contract.

Commitments generally have fixed expiration dates, or other termination clauses. Since commitment may expire without being drawn upon, the total contract amounts do not necessarily represent future cash requirements.

**Operating lease commitment - Group as lessee**

The Group has entered into a five-year operating lease for its premises. Future minimal rentals payable under the non-cancellable lease are as follows:

	<b>2009</b>	<i>2008</i>
	<i>BD</i>	<i>BD</i>
Within 1 year	<b>664,515</b>	451,095
After one year but not more than five years	<b>85,435</b>	448,371
	<b>749,950</b>	899,466

**19 RISK MANAGEMENT****19.1 Introduction**

Risk is inherent in the Group's activities but it 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 Group's continuing profitability and each individual within the Group is accountable for the risk exposures relating to his or her responsibilities. The Group is exposed to credit risk, liquidity risk and market risk, the latter being subdivided into trading and non-trading risks. It is also subject to early repayment risk and operational risks.

The independent risk control process does not include business risks such as changes in the environment, technology and industry. They are monitored through the Group's strategic planning process.

**Risk management structure**

The Board of Directors is ultimately responsible for identifying and controlling risks; however, there are separate independent bodies responsible for managing and monitoring risks.

**19 RISK MANAGEMENT (continued)**

**19.1 Introduction (continued)**

***Board of Directors***

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

***Executive Committee***

The Executive Committee has the responsibility to monitor the overall risk process within the Group.

***Shari'a Supervisory Board***

The Group's Shari'a Supervisory Board is entrusted with the responsibility to ensure the Group's adherence to Shari'a rules and principles in its transactions and activities.

***Credit/ Risk Committee***

Credit/ Risk committee recommends the risk policy and framework to the Board. Its primary role is selection and implementation of risk management systems, portfolio monitoring, stress testing, risk reporting to the Board, Board Committees, Regulators and Executive management. In addition, individual credit transaction approval and monitoring is an integral part of the responsibilities of Credit/Risk Committee.

***Asset and Liability Committee***

The Asset and Liability Committee establishes policy and objectives for the asset and liability management of the Group's financial position in terms of structure, distribution, risk and return and its impact on profitability. It also monitors the cash flow, tenor and cost/yield profiles of assets and liabilities and evaluates the Group's financial position both from profit rate sensitivity and liquidity points of view, making corrective adjustments based upon perceived trends and market conditions, monitoring liquidity, monitoring foreign exchange exposures and positions.

***Board Audit Committee***

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

***Internal Audit***

Risk management processes throughout the Group are audited by the internal audit function, that examines both the adequacy of the procedures and the Group's compliance with the procedures. Internal Audit discusses the results of all assessments with management, and reports its findings and recommendations to the Audit Committee.

***Risk measurement and reporting systems***

The Group's risks are measured using a method which reflects both the expected loss likely to arise in normal circumstances and unexpected losses, which are an estimate of the ultimate actual loss based on statistical models. The models make use of probabilities derived from historical experience, adjusted to reflect the economic environment. The Group also runs worse case scenarios that would arise in the event that extreme events which are unlikely to occur do, in fact, occur.

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

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**19 RISK MANAGEMENT (continued)**

**19.1 Introduction (continued)**

***Risk measurement and reporting systems (continued)***

Information compiled from all the businesses is examined and processed in order to analyse, control and identify early risks. This information is presented and explained to the Board of Directors, the Credit / Risk Committee, and the head of each business division. The report includes aggregate credit exposure, credit metric forecasts, hold limit exceptions, liquidity ratios and risk profile changes. On a monthly basis detailed reporting of industry, customer and geographic risks takes place. Senior management assesses the appropriateness of the allowance for credit losses on a quarterly basis. The Board of Directors receives a comprehensive risk report once a quarter which is designed to provide all the necessary information to assess and conclude on the risks of the Group.

For all levels throughout the Group, specifically tailored risk reports are prepared and distributed in order to ensure that all business divisions have access to extensive, necessary and up-to-date information. A daily briefing is given to the Chief Financial Officer and all other relevant members of the Group on the utilisation of market limits, proprietary investments and liquidity, plus any other risk developments.

**Excessive risk concentration**

Concentrations arise when a number of counterparties are engaged in similar business activities, or activities in the same geographic 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 Group's performance to developments affecting a particular industry or geographical location.

In order to avoid excessive concentrations of risk, the Group's policies and procedures include specific guidelines to focus on maintaining 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 contract will fail to discharge an obligation and cause the other party to incur a financial loss. The Group attempts to control credit risk by monitoring credit exposures, setting limits for transactions with counterparties, and continually assessing the creditworthiness of counterparties.

In addition to monitoring credit limits, the Group manages the credit exposures by entering into collateral arrangements with counterparties in appropriate circumstances and by limiting the duration of the exposure.

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**19 RISK MANAGEMENT (continued)****19.2 CREDIT RISK (continued)****Maximum exposure to credit risk without taking account of any collateral and other credit enhancements**

The table below shows the maximum exposure to credit risk for the components of the consolidated statement of financial position. The maximum exposure is shown gross, before the effect of mitigation through the use of master netting and collateral agreements.

		<i>Gross maximum exposure 2009 BD</i>	<i>Gross maximum exposure 2008 BD</i>
<b>ASSETS</b>			
Balances with other banks		<b>4,755,925</b>	3,389,696
Murabaha receivables from banks	6	<b>149,303,782</b>	87,167,449
Corporate sukuk		<b>16,949,546</b>	-
Murabaha and Mudaraba receivables	7	<b>58,352,606</b>	52,058,745
Ijarah Muntahia Bittamleek	8	<b>42,341,351</b>	37,688,214
Musharaka financing		<b>5,384,369</b>	-
Assets under conversion	9	<b>77,972,000</b>	-
Receivables	12	<b>26,011,951</b>	20,115,783
Assets held-for-sale		-	88,934,033
Total		<b>381,071,530</b>	289,353,920
Contingent liabilities and commitments		<b>48,489,662</b>	7,462,328
<b>Total credit risk exposure</b>		<b>429,561,192</b>	296,816,248

Where financial instruments are recorded at fair value the amounts shown above represent the current credit risk exposure but not the maximum risk exposure that could arise in the future as a result of changes in values.

***Type of credit risk***

Various contracts entered into by the Bank comprise Murabaha receivables, Mudaraba investments, Musharaka receivables, and Ijarah Muntahia Bittamleek contracts. Murabaha receivables contracts cover land, buildings, commodities, motor vehicles and others. Mudaraba investments consist of financing transactions entered through other Islamic banks and financial institutions. The various financial instruments are:

***Murabaha receivables***

The Bank arranges Murabaha transactions by buying an asset (which represents the object of the Murabaha) and then selling this asset to customers (beneficiary) after adding a margin of profit over the cost. The sale price (cost plus profit margin) is repaid in installments over the agreed period.

***Ijarah Muntahia Bittamleek***

The legal title of the leased asset under Ijarah Muntahia Bittamleek passes to the lessee at the end of the Ijarah term, provided that all Ijarah installments are settled and the lessee purchases the asset.

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**19 RISK MANAGEMENT (continued)****19.2 CREDIT RISK (continued)**

a) The credit quality of Balances with Banks and Murabaha receivables from banks subject to credit risk is as follows:

	31 December 2009				
	Neither past due nor impaired			Past due or individually impaired	Total
	'A' Rated	'B' Rated	Unrated		
	BD	BD	BD	BD	BD
Balances with Banks	4,402,197	106,333	247,395	-	4,755,925
Murabaha receivables from banks	93,228,373	11,465,654	44,609,755	-	149,303,782
	<b>97,630,570</b>	<b>11,571,987</b>	<b>44,857,150</b>	<b>-</b>	<b>154,059,707</b>

	31 December 2008				
	Neither past due nor impaired			Past due or individually impaired	Total
	'A' Rated	'B' Rated	Unrated		
	BD	BD	BD	BD	BD
Balances with Banks	3,175,883	165,353	48,460	-	3,389,696
Murabaha receivables from banks	60,638,666	7,540,000	18,988,783	-	87,167,449
	<b>63,814,549</b>	<b>7,705,353</b>	<b>19,037,243</b>	<b>-</b>	<b>90,557,145</b>

The ratings referred to in the above tables are by one or more of the 4 international rating agencies (Standards & Poors, Moody's, Fitch and Capital Intelligence). The unrated exposures are with various high quality Middle East financial institutions, which are not rated by a credit rating agency. In the opinion of the management, these are equivalent to "A" rated banks.

b) The credit quality of Corporate sukuk, Murabaha and Mudaraba receivables, Ijarah Muntahia Bittamleek, Musharaka financing, Assets under conversion and Receivables that are subject to credit risk, based on internal credit ratings, is as follows:

	31 December 2009				
	Neither past due nor impaired			Past due but not impaired	Total
	Satisfactory	Watch List	Substandard		
			but not impaired		
BD	BD	BD	BD	BD	
Corporate sukuk	16,949,546	-	-	-	16,949,546
Murabaha and Mudaraba receivables	37,511,971	7,539,492	-	13,301,143	58,352,606
Ijarah Muntahia Bittamleek	31,646,790	-	3,960,000	6,734,561	42,341,351
Musharaka financing	5,384,369	-	-	-	5,384,369
Assets under conversion	77,972,000	-	-	-	77,972,000
Receivables	26,011,951	-	-	-	26,011,951
	<b>195,476,627</b>	<b>7,539,492</b>	<b>3,960,000</b>	<b>20,035,704</b>	<b>227,011,823</b>

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**19 RISK MANAGEMENT (continued)****19.2 CREDIT RISK (continued)**

	<i>31 December 2008</i>				
	<i>Neither past due nor impaired</i>				
	<i>Satisfactory</i>	<i>Watch List</i>	<i>Substandard</i>	<i>Past due but</i>	<i>Total</i>
	<i>BD</i>	<i>BD</i>	<i>but not</i>	<i>not impaired</i>	<i>BD</i>
		<i>impaired</i>	<i>BD</i>		
		<i>BD</i>	<i>BD</i>	<i>BD</i>	<i>BD</i>
Murabaha and Mudaraba receivables	66,756,279	-	-	5,727,466	72,483,745
Ijarah Muntahia Bittamleek	41,507,924	-	-	22,860	41,530,784
	<b>108,264,203</b>	<b>-</b>	<b>-</b>	<b>5,750,326</b>	<b>114,014,529</b>

All internal risk ratings are tailored to the various categories and are derived in accordance with the Group's rating policy. The attributable risk ratings are assessed and updated regularly.

c) Past due but not impaired Murabaha and Mudaraba receivables, and Ijarah Muntahia Bittamleek are analysed as follows:

	<i>31 December 2009</i>			
	<i>0-30 days</i>	<i>31-90 days</i>	<i>&gt; 90 days</i>	<i>Total</i>
	<i>BD</i>	<i>BD</i>	<i>BD</i>	<i>BD</i>
Murabaha and Mudaraba receivables	<b>1,740,965</b>	<b>4,609,596</b>	<b>6,950,582</b>	<b>13,301,143</b>
Ijarah Muntahia Bittamleek	<b>1,724,478</b>	<b>692,024</b>	<b>4,318,059</b>	<b>6,734,561</b>
	<b>3,465,443</b>	<b>5,301,620</b>	<b>11,268,641</b>	<b>20,035,704</b>

	<i>31 December 2008</i>			
	<i>0-30 days</i>	<i>31-90 days</i>	<i>&gt; 90 days</i>	<i>Total</i>
	<i>BD</i>	<i>BD</i>	<i>BD</i>	<i>BD</i>
Murabaha and Mudaraba receivables	-	2,034,158	3,693,308	5,727,466
Ijarah Muntahia Bittamleek	22,860	-	-	22,860
	<b>22,860</b>	<b>2,034,158</b>	<b>3,693,308</b>	<b>5,750,326</b>

All the past due but not impaired Murabaha and Mudaraba receivables and Ijarah financing are covered by collateral of BD 42,034,664 (2008: BD 8,901,056).

The maximum credit risk, without taking into account the fair value of any collateral and Shari'a-compliant netting agreements, is limited to the amounts on the statement of financial position plus commitments to customers disclosed in Note 18 except capital commitments.

During the year BD 9,520,469 (2008: BD 2,350,000) of financing facilities to individuals were renegotiated. All renegotiated facilities are performing and are fully secured.

At 31 December 2009, the amount of credit exposure in excess of 10% of the Group's equity to individual counterparties was nil (2008: nil).

At 31 December 2009, impaired financial assets of the Group amounted to BD 59,387,000 (2008: Nil) against which provision of BD 47,507,000 (2008: Nil) was held.

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**19 RISK MANAGEMENT (continued)****19.3 Legal risk and claims**

Legal risk is the risk arising from the potential that unenforceable contracts, lawsuits or adverse judgments can disrupt or otherwise negatively affect the operations of the Group. The Group has developed controls and procedures to identify legal risks and believes that losses will be minimized.

As at 31 December 2009, legal suits amounting to BD 1,681 thousand (2008: BD 1,661 thousand) were pending against the Group. Based on the opinion of the Group's legal counsel, the total estimated liability arising from these cases is not considered to be material to the Group's financial position as the Group also has filed counter cases against these parties.

**20 CONCENTRATIONS**

Concentrations arise when a number of counterparties are engaged in similar business activities, or activities in the same geographic 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 Group's performance to developments affecting a particular industry or geographic location. The Group manages its credit risk exposure through diversification of financing activities to avoid undue concentrations of risks with customers in specific locations or businesses.

The distribution of assets, liabilities and unrestricted investment accounts by geographic region and industry sector was as follows:

	<i>Assets</i>	<i>Liabilities, unrestricted investment accounts and equity</i>	<i>Contingent liabilities and Commitments</i>	<i>Assets</i>	<i>Liabilities, unrestricted investment accounts and equity</i>	<i>Commitments</i>
	<i>2009</i>	<i>2009</i>	<i>2009</i>	<i>2008</i>	<i>2008</i>	<i>2008</i>
	<i>BD</i>	<i>BD</i>	<i>BD</i>	<i>BD</i>	<i>BD</i>	<i>BD</i>
<b>Geographic region</b>						
GCC	718,880,971	560,808,591	32,549,873	502,539,276	357,555,010	2,465,607
Arab World	9,565,905	2,791,538	-	9,917,696	4,978,221	-
Europe	23,087,333	11,641,916	48,252	6,106,964	6,856,091	-
Asia	27,105,676	8,734,207	12,346,647	32,222,098	12,600,551	2,278,578
America	2,274,539	179,728	-	1,709,064	7,204	-
Others	5,019,859	-	3,544,890	1,985,460	-	2,718,143
	<b>785,934,283</b>	<b>584,155,980</b>	<b>48,489,662</b>	554,480,558	381,997,077	7,462,328
Equity	-	201,778,303	-	-	172,483,481	-
	<b>785,934,283</b>	<b>785,934,283</b>	<b>48,489,662</b>	554,480,558	554,480,558	7,462,328

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**20 CONCENTRATIONS (continued)**

	<i>Liabilities, unrestricted investment accounts and equity</i>			<i>Liabilities, unrestricted investment accounts and equity</i>		
	<i>Assets</i>	<i>Assets</i>	<i>Contingent liabilities and Commitments</i>	<i>Assets</i>	<i>Assets</i>	<i>Commitments</i>
	<i>2009</i>	<i>2009</i>	<i>2009</i>	<i>2008</i>	<i>2008</i>	<i>2008</i>
	<i>BD</i>	<i>BD</i>	<i>BD</i>	<i>BD</i>	<i>BD</i>	<i>BD</i>
<b>Industry sector</b>						
Trading and manufacturing	10,418,502	15,798,137	16,626,581	12,752,030	423,602	48,789
Banks and financial institutions	257,170,260	143,696,752	344,000	109,199,534	72,547,160	-
Real estate	188,081,853	60,406,242	23,331,597	167,869,248	68,098,462	4,242,721
Aviation	10,373,462	8,536	-	5,090,915	1,025,554	-
Individuals	45,768,760	206,897,595	1,726,150	23,199,665	106,905,733	1,167,200
Government and public sector	127,925,297	87,211,278	-	135,204,195	97,537,011	1,218,851
Others	146,196,149	70,137,440	6,461,334	101,164,971	35,459,555	784,767
	785,934,283	584,155,980	48,489,662	554,480,558	381,997,077	7,462,328
Equity	-	201,778,303	-	-	172,483,481	-
	785,934,283	785,934,283	48,489,662	554,480,558	554,480,558	7,462,328

**21 MARKET RISK**

Market risk arises from fluctuations in global yields on financial instruments and foreign exchange rates that could have an indirect effect on the Group's assets value and equity prices. The Board has set limits on the risk that may be accepted. This is monitored on a regular basis by the Asset and Liability Committee of the Group.

**21.1 EQUITY PRICE RISK**

Equity price risk arises from fluctuations in equity prices. The Board has set limits on the amount and type of investments that may be accepted. This is monitored on an ongoing basis by the Group's Investment Committee.

The effect on income (as a result of changes in the fair values of non-trading investments held at fair value through profit or loss and assets held for sale) solely due to reasonably possible changes in equity prices, is as follows:

	<i>2009</i>			
	<i>10% increase</i>		<i>10% decrease</i>	
	<i>Effect on</i>	<i>Effect on</i>	<i>Effect on</i>	<i>Effect on</i>
	<i>Effect on Comprehensive net profit</i>			
	<i>BD</i>	<i>BD</i>	<i>BD</i>	<i>BD</i>
Quoted:				
GCC	434,194	172,700	(434,194)	(172,700)
Unquoted	18,033,788	1,514,600	(18,033,788)	(1,514,600)

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

31 December 2009

**21 MARKET RISK (continued)**

## 21.1 EQUITY PRICE RISK (continued)

	2008			
	10% increase		10% decrease	
	<i>Effect on</i>	<i>Effect on</i>	<i>Effect on</i>	<i>Effect on</i>
	<i>net profit</i>	<i>Comprehensive</i>	<i>net profit</i>	<i>Comprehensive</i>
	<i>BD</i>	<i>income</i>	<i>BD</i>	<i>income</i>
	<i>BD</i>	<i>BD</i>	<i>BD</i>	<i>BD</i>
Quoted:				
GCC	404,564	-	(404,564)	-
Unquoted	11,288,386	-	(11,288,386)	-

Assets under conversion (Note 9) include quoted equities of BD 1,727,000 (2008: Nil) and unquoted equities of BD 15,146,000 (2008: Nil). In determining the effect of price volatility on above, equity positions included in assets under conversion have been considered.

## 21.2 PROFIT RETURN RISK

The Group has exposure to fluctuations in the profit rates on its assets and liabilities. The Group recognises income on certain financial assets on a time-apportioned basis. The Group has set limits for profit return risk and these are monitored on an ongoing basis by the Group's Asset Liability Committee (ALCO).

The Group manages exposures to the effects of various risks associated with fluctuations in the prevailing levels of market profit rates on its financial position and cash flows.

The effect on income solely due to reasonably possible immediate and sustained changes in profit return rates, affecting both floating rate assets and liabilities and fixed rate assets and liabilities with maturities less than one year are as follows:

	2009			
	<i>Change in</i>	<i>Effect on</i>	<i>Change in</i>	<i>Effect on</i>
	<i>rate</i>	<i>net profit</i>	<i>rate</i>	<i>net profit</i>
	<i>%</i>	<i>BD</i>	<i>%</i>	<i>BD</i>
US dollars	<b>0.25</b>	<b>179,609</b>	<b>(0.25)</b>	<b>(179,609)</b>
Bahraini dinars	<b>0.25</b>	<b>344,051</b>	<b>(0.25)</b>	<b>(344,051)</b>

	2008			
	<i>Change in</i>	<i>Effect on</i>	<i>Change in</i>	<i>Effect on</i>
	<i>rate</i>	<i>net profit</i>	<i>rate</i>	<i>net profit</i>
	<i>%</i>	<i>BD</i>	<i>%</i>	<i>BD</i>
US dollars	0.25	506,153	(0.25)	(506,153)
Bahraini dinars	0.25	1,656,026	(0.25)	(1,656,026)

In addition to profit rate bearing financing contracts considered in arriving at the effect on net profits, the assets under conversion includes BD 81,088,000 of financial assets and BD 120,001,000 of financial liabilities which are interest bearing. The Group is in the process of converting these into Shari'a compliant contracts. If all the interest bearing assets and liabilities were converted into Shari'a complaint contract on 1 January 2010, the change in profit rate by 0.25% would result in a profit or loss of BD 97,283.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

31 December 2009

**21 MARKET RISK (continued)**

## 21.3 CURRENCY RISK

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Board has set limits on positions by currency. Positions are monitored on a periodic basis by the Group's Asset Liability Committee to ensure positions are maintained within established limits.

Substantial portion of the Group's assets and liabilities are denominated in Bahrain dinars or US dollars. The Group had the following significant net long positions in foreign currencies as of 31 December :

	<i>2009</i>	<i>2008</i>
	<i>BD</i>	<i>BD</i>
US Dollars	<b>10,402,462</b>	17,090,387
Saudi Riyals	<b>55,801,876</b>	57,553,210

The effect on income solely due to reasonably possible immediate and sustained changes in exchange rates is as follows:

	<i>2009</i>			
	<i>Change in rate %</i>	<i>Effect on net profit BD</i>	<i>Change in rate %</i>	<i>Effect on net profit BD</i>
US dollars to Bahraini dinars	<b>1</b>	<b>104,025</b>	<b>(1)</b>	<b>(104,025)</b>
Saudi Riyals to Bahraini dinars	<b>1</b>	<b>558,019</b>	<b>(1)</b>	<b>(558,019)</b>

	<i>2008</i>			
	<i>Change in rate %</i>	<i>Effect on net profit BD</i>	<i>Change in rate %</i>	<i>Effect on net profit BD</i>
Saudi Riyals to Bahraini dinar				
US dollars to Bahraini dinars	1	170,904	(1)	(170,904)
Saudi Riyals to Bahraini dinars	1	575,532	(1)	(575,532)

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

31 December 2009

**22 LIQUIDITY RISK**

Liquidity risk is the risk that the Group will be unable to meet its liabilities as they fall due. Liquidity risk can be caused by market disruptions or credit downgrades which may impact certain sources of funding. To mitigate this risk, management has diversified funding sources and assets are managed with liquidity in mind, maintaining an adequate balance of cash, cash equivalents and readily marketable securities. Liquidity position is monitored on an ongoing basis by the Group's Asset Liability Committee.

The table below summarises the expected maturity profile of the Group's assets and liabilities as at 31 December 2009 and 2008:

	<i>31 December 2009</i>				<i>Total</i>
	<i>Up to 3 months BD</i>	<i>3 months to 1 year BD</i>	<i>1 to 5 years BD</i>	<i>Over 5 years BD</i>	
<b>ASSETS</b>					
Cash and balances with					
Central Bank of Bahrain	<b>109,372,202</b>	-	<b>17,367,000</b>	-	<b>126,739,202</b>
Central Bank of Bahrain					
Sukuk	-	<b>32,907,875</b>	-	-	<b>32,907,875</b>
Murabaha receivables from banks	<b>149,303,782</b>	-	-	-	<b>149,303,782</b>
Corporate Sukuk	-	-	<b>16,949,546</b>	-	<b>16,949,546</b>
Murabaha and Mudaraba receivables	<b>20,096,505</b>	<b>14,665,487</b>	<b>52,511,833</b>	-	<b>87,273,825</b>
Ijarah Muntahia Bittamleek	<b>7,062,692</b>	<b>10,120,788</b>	<b>22,179,292</b>	<b>6,951,879</b>	<b>46,314,651</b>
Musharaka financing	<b>5,323</b>	<b>15,894</b>	<b>5,363,152</b>	-	<b>5,384,369</b>
Assets under conversion	<b>30,901,000</b>	<b>17,156,000</b>	<b>50,248,000</b>	-	<b>98,305,000</b>
Non-trading investments	-	-	<b>184,679,822</b>	-	<b>184,679,822</b>
Investment in an associate	-	-	<b>7,659,055</b>	-	<b>7,659,055</b>
Investment properties	-	-	-	<b>1,177,528</b>	<b>1,177,528</b>
Receivables and prepayments	<b>25,233,471</b>	<b>1,129,996</b>	<b>538,725</b>	-	<b>26,902,192</b>
Premises and equipment	-	-	<b>2,337,436</b>	-	<b>2,337,436</b>
	<b>341,974,975</b>	<b>75,996,040</b>	<b>359,833,861</b>	<b>8,129,407</b>	<b>785,934,283</b>
<b>LIABILITIES AND UNRESTRICTED</b>					
<b>    INVESTMENT ACCOUNTS</b>					
Murabaha and Wakala payables					
to banks	-	-	<b>89,397,722</b>	-	<b>89,397,722</b>
Wakala from non-banks	-	<b>47,882,064</b>	<b>269,487,521</b>	-	<b>317,369,585</b>
Customers' current accounts	<b>32,699,944</b>	-	-	-	<b>32,699,944</b>
Liabilities under conversion	<b>87,810,000</b>	<b>14,120,000</b>	<b>18,472,000</b>	-	<b>120,402,000</b>
Other liabilities	<b>13,512,479</b>	<b>1,096,818</b>	<b>267,965</b>	-	<b>14,877,262</b>
Unrestricted investment accounts	-	-	<b>9,409,467</b>	-	<b>9,409,467</b>
	<b>134,022,423</b>	<b>63,098,882</b>	<b>387,034,675</b>	-	<b>584,155,980</b>

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

31 December 2009

**22 LIQUIDITY RISK (continued)**

	<i>31 December 2008</i>				<i>Total BD</i>
	<i>Up to 3 months BD</i>	<i>3 months to 1 year BD</i>	<i>1 to 5 years BD</i>	<i>Over 5 years BD</i>	
<b>ASSETS</b>					
Cash and balances with					
Central Bank of Bahrain	83,533,981	-	-	-	83,533,981
Central Bank of Bahrain					
Sukuk	-	6,620,000	24,475,000	-	31,095,000
Murabaha receivables from banks	87,167,449	-	-	-	87,167,449
Murabaha and Mudaraba receivables	29,807,777	16,005,000	26,555,359	115,609	72,483,745
Ijarah Muntahia Bittamleek	6,022,862	3,892,912	26,505,879	5,109,131	41,530,784
Non-trading investments	-	-	116,929,500	-	116,929,500
Investment in an associate	-	-	-	8,011,913	8,011,913
Investment properties	-	-	-	1,177,528	1,177,528
Receivables and prepayments	20,055,603	256,556	720,670	-	21,032,829
Premises and equipment	-	-	2,583,796	-	2,583,796
Assets held-for-sale	-	19,715,428	69,218,605	-	88,934,033
	<u>226,587,672</u>	<u>46,489,896</u>	<u>266,988,809</u>	<u>14,414,181</u>	<u>554,480,558</u>
<b>LIABILITIES AND UNRESTRICTED INVESTMENT ACCOUNTS</b>					
Murabaha and Wakala payables					
to banks	-	-	32,880,685	-	32,880,685
Wakala from non-banks	-	97,980,280	191,024,490	-	289,004,770
Customers' current accounts	-	-	42,985,844	-	42,985,844
Other liabilities	10,182,013	573,360	186	-	10,755,559
Unrestricted investment accounts	-	-	6,370,219	-	6,370,219
	<u>10,182,013</u>	<u>98,553,640</u>	<u>273,261,424</u>	<u>-</u>	<u>381,997,077</u>

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

31 December 2009

**22 LIQUIDITY RISK (continued)**

The table below summarizes the maturity profile of the Group's financial liabilities at 31 December, 2009 and 2008 based on contractual undiscounted repayment obligation:

	<i>31 December 2009</i>				
	<i>On</i>	<i>Up to</i>	<i>3 months</i>	<i>1 to 5</i>	<i>Total</i>
	<i>demand</i>	<i>3 months</i>	<i>to 1 year</i>	<i>years</i>	
	<i>BD</i>	<i>BD</i>	<i>BD</i>	<i>BD</i>	<i>BD</i>
<b>LIABILITIES, UNRESTRICTED INVESTMENT</b>					
<b>ACCOUNTS COMMITMENTS AND CONTINGENT LIABILITIES</b>					
Murabaha and Wakala payables					
to banks	-	89,397,722	-	-	89,397,722
Wakala from non-banks	-	250,849,368	47,882,064	18,638,153	317,369,585
Customers' current accounts	32,699,944	-	-	-	32,699,944
Liabilities under conversion	-	87,810,000	14,120,000	18,472,000	120,402,000
Unrestricted investment accounts	-	9,409,467	-	-	9,409,467
Unutilised financing commitments	13,749,000	-	3,052,062	4,096,635	20,897,697
Unutilised capital commitments	-	-	3,544,890	2,136,117	5,681,007
Contingent liabilities	19,119,412	538,000	1,503,596	-	21,161,008
Other Liabilities	-	9,592,243	435,818	598,975	10,627,036
Profit due on financing contracts	-	986,136	2,167,981	2,882,088	6,036,205
	<b>65,568,356</b>	<b>448,582,936</b>	<b>72,706,411</b>	<b>46,823,968</b>	<b>633,681,671</b>

	<i>31 December 2008</i>				
	<i>On</i>	<i>Up to</i>	<i>3 months</i>	<i>1 to 5</i>	<i>Total</i>
	<i>demand</i>	<i>3 months</i>	<i>to 1 year</i>	<i>years</i>	
	<i>BD</i>	<i>BD</i>	<i>BD</i>	<i>BD</i>	<i>BD</i>
<b>LIABILITIES, UNRESTRICTED INVESTMENT</b>					
<b>ACCOUNTS AND COMMITMENTS</b>					
Murabaha and Wakala payables					
to banks	-	32,880,685	-	-	32,880,685
Wakala from non-banks	-	218,957,897	68,928,893	1,117,980	289,004,770
Customers' current accounts	-	42,985,844	-	-	42,985,844
Unrestricted investment accounts	-	6,370,219	-	-	6,370,219
Unutilised financing commitments	-	-	2,434,840	-	2,434,840
Unutilised capital commitments	-	-	777,766	4,249,722	5,027,488
Profit due on financing contracts	-	-	1,213,866	-	1,213,866
	<b>-</b>	<b>301,194,645</b>	<b>73,355,365</b>	<b>5,367,702</b>	<b>379,917,712</b>

31 December 2009

**23 SEGMENT INFORMATION****Primary segment information**

For management purposes, the Group is organised into four major business segments:

- Banking** - principally managing Shari'a compliant profit sharing investment accounts, and offering Shari'a compliant financing contracts and other Shari'a-compliant products. This segment comprises corporate banking, retail banking and private banking and wealth management.
- Treasury** - principally handling Shari'a-compliant money market, trading and treasury services including short-term commodity Murabaha.
- Investments** - principally the Banks' proprietary portfolio and serving clients with a range of investment products, funds and alternative investments.
- Capital** - manages the undeployed capital of the bank by investing it in high quality financial instruments, incurs all expenses in managing such investments and accounts for the capital governance related expenses.

These segments are the basis on which the Group reports its primary segment information. Transactions between segments are conducted at estimated market rates on an arm's length basis. Transfer charges are based on a pool rate which approximates the cost of funds.

Segment information for the year ended 31 December 2009 was as follows:

	<i>31 December 2009</i>				
	<i>Banking BD</i>	<i>Treasury BD</i>	<i>Investments BD</i>	<i>Capital BD</i>	<i>Total BD</i>
Operating income	7,887,189	2,499,936	5,583,228	7,709,233	23,679,586
Segment result	<u>4,101,065</u>	<u>1,492,838</u>	<u>2,709,240</u>	<u>5,659,272</u>	<u>13,962,415</u>
<b>Other information</b>					
Segment assets	<u>208,248,481</u>	<u>336,170,782</u>	<u>171,962,098</u>	<u>69,552,922</u>	<u>785,934,283</u>
Segment liabilities, and equity	<u>471,408,521</u>	<u>103,403,261</u>	<u>984,408</u>	<u>210,138,093</u>	<u>785,934,283</u>
	<i>31 December 2008</i>				
	<i>Banking BD</i>	<i>Treasury BD</i>	<i>Investments BD</i>	<i>Capital BD</i>	<i>Total BD</i>
Operating income	12,358,078	1,363,925	11,360,600	12,518,655	37,601,258
Segment result	<u>8,053,899</u>	<u>131,570</u>	<u>8,111,172</u>	<u>9,246,040</u>	<u>25,542,681</u>
<b>Other information</b>					
Segment assets	<u>111,419,675</u>	<u>206,307,380</u>	<u>164,730,985</u>	<u>72,022,518</u>	<u>554,480,558</u>
Segment liabilities, and equity	<u>332,442,317</u>	<u>41,505,053</u>	<u>1,000,000</u>	<u>179,533,188</u>	<u>554,480,558</u>

**23 SEGMENT INFORMATION (continued)**

**Secondary segment information**

The Group primarily operates in the GCC and derives substantially all its operating income and incurs all operating expenses in the GCC.

**24 FIDUCIARY ASSETS**

Funds under management at the year-end amounted to BD 60,706,388 (2008: BD 25,000,000). These assets are held in a fiduciary capacity and are not included in the consolidated statement of financial position.

**25 SHARI'A SUPERVISORY BOARD**

The Bank's Shari'a Supervisory Board consists of four Islamic scholars who review the Group's compliance with general Shari'a principles and specific fatwa's, rulings and guidelines issued by the Bank's Shari'a supervisory Board. Their review includes examination of evidence relating to the documentation and procedures adopted by the Group to ensure that its activities are conducted in accordance with Islamic Shari'a principles.

**26 FAIR VALUE OF FINANCIAL INSTRUMENTS**

The estimated fair value of the Group's financial instruments are not significantly different from their carrying values as at 31 December 2009 and 2008.

**27 EARNINGS AND EXPENSES PROHIBITED BY SHARI'A**

As explained in Note 3, the Bank acquired a 90.31% stake in BSB. Effective 28 October 2009, the Bank established control over the subsidiary. Since the subsidiary is still in the process of being converted into an Islamic bank, the share of post acquisition net profit of BD 18,965 derived from non-Shari'a compliant transactions, has been set aside for charity.

In addition to the above, the Bank received income totaling BD 55,724 (2008: BD 2,767) from conventional financial institutions on current account balances during the year. These funds were held as payable to charity as they are in the nature of Shari'a prohibited income.

**28 SOCIAL RESPONSIBILITY**

The Group discharges its social responsibility through charity fund expenditures and donations to the good faith qard fund which is used for charitable purposes. During the year the Group paid an amount of BD 914,983 (2008: BD 536,084) on account of charitable donations.

**29 ZAKAH**

Pursuant to a resolution of the shareholders in an EGM held on 12 November 2009, it was resolved to amend the articles of association of the Bank to inform the shareholders of their obligation to pay Zakah on income and net worth. Consequently, Zakah is not recognized in the consolidated income statement as an expense. The total Zakah payable by the shareholders for 2009 has been determined by the Shari'a supervisory board as BD 571,532 or 0.40 fils per share. In 2008, a sum of BD 822,525 was contributed by the Bank with an obligation of BD 615,249 or 0.51 fils per share payable by the shareholders.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

31 December 2009

**30 CAPITAL ADEQUACY**

The adequacy of the Group's capital is monitored using, primarily, the rules and ratios established by the Basel Committee on Grouping Supervision and adopted by the Central Bank of Bahrain. The primary objective of the Group's capital management is to ensure that it complies with externally imposed capital requirements. The Group complied in full with all externally imposed capital requirements during the years ended 31 December 2009 and 31 December 2008.

The risk assets ratio calculations, in accordance with the 'Basel II' capital adequacy guidelines of the Central Bank of Bahrain are as follows:

	<i>2009</i>	<i>2008</i>
	<i>BD</i>	<i>BD</i>
Capital base (Tier 1)	<b>179,564,000</b>	107,989,000
Credit risk weighted exposures	<b>555,389,000</b>	393,251,000
Market risk weighted exposures	<b>2,950,000</b>	3,213,000
Operational risk weighted exposures	<b>68,803,000</b>	40,410,000
Total risk weighted exposure	<b>627,142,000</b>	436,874,000
Capital adequacy	<b>28.6%</b>	24.7%
Minimum requirement	<b>12.0%</b>	12.0%