EMBARKING UPON A NEW STRATEGIC DIRECTION

ANNUAL REPORT **2014**

بنك البحرين الإسلامي

BisB

Embarking upon a new strategic direction

Following approval by the Board of Directors in April 2014, Bahrain Islamic Bank commenced the implementation of its new five-year strategy for growth, which was developed in collaboration with the Boston Consulting Group. Key objectives of the new strategy include focusing on core banking activities; disposing of non-performing investment assets; reducing the cost of capital and operating expenses; upgrading the information technology infrastructure; and exploiting opportunities for entering new markets outside Bahrain, with the aim of expanding the Bank's activities.

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His Royal Highness
Prince Khalifa bin Salman
Al Khalifa

The Prime Minister of
the Kingdom of Bahrain

His Majesty King
Hamad bin Isa
Al Khalifa

The King of
the Kingdom of Bahrain

His Royal Highness
Prince Salman bin Hamad
Al Khalifa

The Crown Prince,
Deputy Supreme Commander
and First Deputy Prime
Minister

CORPORATE OVERVIEW

Profile

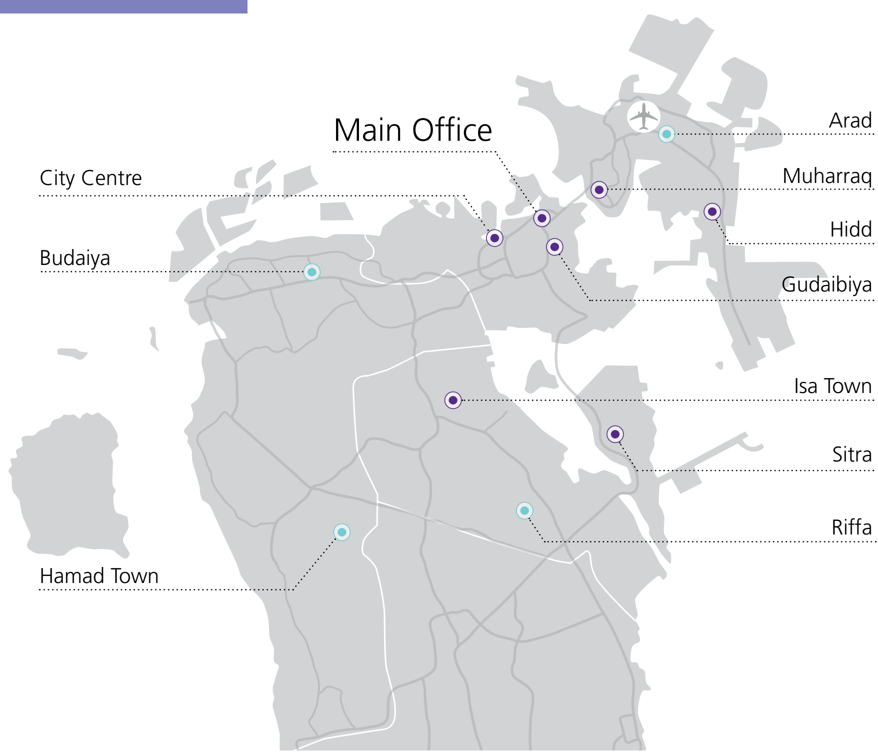
Bahrain Islamic Bank (BisB) is uniquely distinguished as being the first Islamic bank in the Kingdom of Bahrain, and the fourth in the GCC. Incorporated in 1979, BisB operates under an Islamic Retail banking licence from the Central Bank of Bahrain, and is listed on the Bahrain Bourse. At the end of 2014, the Bank's paid-up capital was BD 93 million, while total assets stood at BD 875 million.

By combining its unique heritage and tradition with the adoption of modern banking techniques, underscored by technology and innovation, BisB has maintained its status as the leading Sharia'a-compliant commercial bank in the Kingdom.



CUSTOMERS

Around the Kingdom



- Financial Malls
- Branches

VISION AND MISSION

Vision

Our vision is to be the preferred Islamic financial partner, going beyond boundaries to grow together.

Mission

Our mission is to deliver value to:

Customers: Exceeding their expectations and building loyalty.

Employees: Nurturing and retaining talent.

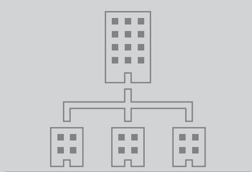
Shareholders: Maximising consistent returns.

Community: Honouring our social commitment to society.

EMPLOYEES

SHAREHOLDERS

COMMUNITY



7
Branches

4
Financial Malls

54
ATMs

FINANCIAL HIGHLIGHTS

Total assets
BD Million

875m

2014	2013	2012	2011	2010
875	910	833	839	936

Islamic financing
BD Million

510m

2014	2013	2012	2011	2010
510	437	415	392	414

Total operating income
BD Million

47m

2014	2013	2012	2011	2010
47	48	38	41	35

Investors' share in income
BD Million

7.5m

2014	2013	2012	2011	2010
7.5	11	14	15	18

Investments
BD Million

208m

2014	2013	2012	2011	2010
208	201	210	233	239

Unrestricted investment accounts
BD Million

635m

2014	2013	2012	2011	2010
635	713	661	638	741

Book value per share
Bahraini fils

85fils

2014	2013	2012	2011	2010
85	84	75	108	138

Share price
Bahraini fils

148fils

2014	2013	2012	2011	2010
148	136	82	90	129

OPERATIONAL HIGHLIGHTS

Retail Banking grows customer base

The launch of additional new initiatives, services and products during 2014, together with a continued focus on customer service, resulted in the Bank's retail customer base expanding by 14%, with Islamic financing growing by 19%, despite intensified competition in Bahrain's banking sector.

Corporate Banking extends help for SMEs

BisB extended its support for the small-and-medium enterprises (SMEs) sector in 2014 with an additional BD 20 million being made available to Tamkeen's Enterprise Financing Scheme. This raises the value of the Tamkeen-BisB agreement to BD 50 million, through which over 200 SMEs have benefited to date.

Enhancing customer service and convenience

Key customer service-related initiatives during 2014 include the opening of two additional financial malls, bringing the total to four; the launch of a Titanium MasterCard; and, for the first time in the Kingdom of Bahrain, the exclusive introduction of the Signature Debit Visa card for the Bank's Al Thuraya private and priority banking customers.

Strengthening the IT infrastructure

Key information technology achievements in 2014 include upgrading the core banking system; enhancing the disaster recovery site with the latest new technology; and finalising the information security framework in line with ISO 27001. The Bank also commissioned new systems in the areas of human resources, retail collections, purchasing and archiving.

Continued industry recognition

The considerable achievements by Bahrain Islamic Bank during 2014 – financial, business and operational – were recognised by receipt of the 'Best Islamic Bank in Bahrain' award from World Finance, a leading UK-based financial magazine. A distinguished judging panel reviewed nominations from the magazine's readers as part of the process of selecting winning institutions.

Financial results reflect success of new strategy

The excellent financial performance by Bahrain Islamic Bank in 2014, which saw net profit increase by 52% over the previous year, reflects the successful implementation of its new strategic focus on growing core activities and disposing of non-performing investment assets. The Bank relied fully on revenues and fees from financing and major activities, which were responsible for generating 82% of operating revenues. These were free from revaluations or unearned profits, with the exception of the successful exits from some investment portfolios and listed equities, which realised a net gain of BD 6.9 million.

CHAIRMAN'S STATEMENT

"Despite another year of intensified competition, I am pleased to report that the Bank's retail and corporate banking businesses performed well, and grew their respective market share of Bahrain's commercial banking sector during 2014"

In the name of Allah, the Most Beneficent, the Most Merciful. Prayers and Peace be upon the Last Apostle and Messenger, Our Prophet Mohammed, His Comrades and Relatives.

On behalf of the Board of Directors, it is my privilege to present the annual report and consolidated financial statements of Bahrain Islamic Bank (BisB) for the year ended 31 December 2014. This was a successful year for the Bank, during which we posted an increase in profitability, continued to improve our competitive edge, and commenced implementation of the Bank's new five year strategy for growth.

I am delighted to report that BisB achieved an improved financial performance in 2014. Net profit for the year increased by 52 percent to BD 9.3 million from BD 6.1 million in 2013; while total income grew by 19 percent to BD 43 million from BD 36 million the previous year. Earnings per share were 9.93 Bahraini fils compared with 6.52 fils in 2013.

BisB continued to maintain a strong balance sheet, with total assets standing at BD 875 million and owners' equity of BD 79 million at the end of 2014, while liquidity remained healthy at BD 121 million. Maintaining our prudent and conservative approach, we made impairment provisions totaling BD 12 million in 2014, in comparison with impairment provisions of BD 10 million in 2013, which reflects the success of measures taken during the year to address non performing investment and financing assets.

Despite another year of intensified competition, I am pleased to report that the Bank's retail and corporate banking businesses performed well, and grew their respective market share of Bahrain's commercial banking sector during 2014. This reflects our continued focus on delivering the highest levels of customer service, supported by the introduction of additional new innovative products and services.

At the same time, BisB continued to strengthen its corporate governance and risk management frameworks, and enhance its substantial investment in people and information technology. The Bank also maintained its enduring contribution to the economic and social well being of the Kingdom of Bahrain, and the development of the Islamic banking industry, through its enlightened corporate social responsibility programme.

In a significant development, Bahrain Islamic Bank commenced the implementation of its new five year strategy during the year.

Abdul Razak Abdulla Hassan Al Qassim
Chairman

Developed in collaboration with the Boston Consulting Group, it was approved by the Board of Directors in April 2014. Key objectives of the new strategy include focusing on core banking activities; orderly disposing of non performing investment assets; reducing the cost of capital and operating expenses; upgrading the information technology infrastructure; and exploiting opportunities for entering new markets outside Bahrain, with the aim of expanding the Bank's activities. As our financial and operational achievements during 2014 illustrate, we have made good progress in the initial implementation of our new strategy for growth.

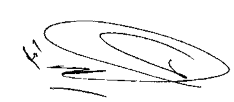
During the year, there were some changes to the composition of the Board of Directors. Dr. Sherif Elsayed Aly Ayoub, who represents the Islamic Development Bank (IDB), resigned from the Board following his appointment as Assistant Secretary General of the Islamic Financial Services Board. I thank Dr. Ayoub for his contribution and wish him every success in his new role. In turn, I would like to welcome Mr. Mohamed Hedi Mejai, who joins the Board of Directors as the new IDB representative, and whose expertise and experience will be of great benefit to the Board.

Also during the year, Mr. Mohammed Ebrahim Mohammed resigned as Chief Executive Officer of the Bank. On behalf of the Board, I thank him for his sterling contribution since 2007 and wish him well in his new endeavours. I take this opportunity to congratulate Mr. Mohammed Ahmed Janahi, who was promoted to Deputy Chief Executive Officer and appointed as Acting CEO. A veteran banker with over 40 years' experience, Mohammed joined BisB in 2007 as General Manager - Support Services, following various executive positions with NBB, Al Baraka Bank and Gulf Air. I wish him every success in his new position, and assure him of the Board's full support in carrying out his new responsibilities.

Looking ahead, the economic outlook for the Kingdom of Bahrain remains positive, driven by an improved performance from the non oil sector and increased state spending. The International Monetary Fund predicts that the Kingdom's economy will grow faster than regional and global averages this year, and that this trend will continue into 2015, albeit at a more moderate rate due to the impact of the recent decline in oil prices. Continued growth in the local economy will benefit business and trade, and have a positive effect on the banking and financial services industry. We therefore remain cautiously optimistic for the prospects of BisB in 2015, as we embark upon a new strategic direction and enter a new chapter in our long and pioneering history.

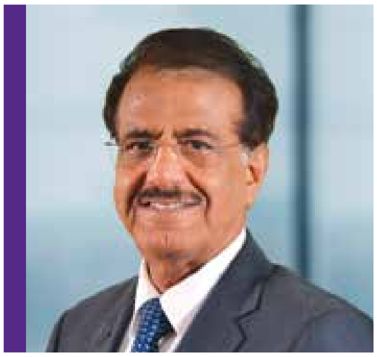
Finally, on behalf of the Board of Directors, I would like to extend my sincere appreciation to His Majesty the King of Bahrain, His Royal Highness the Prime Minister, and His Royal Highness the Crown Prince, for their wise leadership and visionary reforms; and also for their encouragement for the Islamic banking sector. Our thanks are also due to the Central Bank of Bahrain and various Government institutions for their continued guidance and cooperation.

I also take this opportunity to express our gratitude to the Bank's shareholders for their loyalty and support; to our Sharia'a Supervisory Board for its advice and supervision; and to the management and staff of BisB for their highly valued dedication and professionalism in yet another challenging year.



Abdul Razak Al Qassim
Chairman of the Board

BOARD OF DIRECTORS



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1. Mr. Abdul Razak Abdulla Al Qassim

Chairman
Executive & Non-Independent Director
Appointed on 5 June 2013

Mr. Abdul Razak Al Qassim is the Chief Executive Officer and Board member of National Bank of Bahrain (NBB). He joined NBB in 1977 after seven years with Chase Manhattan Bank. Abdul Razak Al Qassim is Chairman of the Board of Directors of Bahrain Islamic Bank (BisB); Chairman of Benefit Company; Chairman of Bahrain Association of Banks; Deputy Chairman, Chairman of Executive Committee and Member of Nomination and Remuneration Committee at Bahrain Telecommunication Company (Batelco); Deputy Chairman of Umniah Mobile Company (Jordan); Deputy Chairman of Dhivehi Raajeyge Gulhn plc. (Dhiraagu), Maldives; Deputy Chairman of Sure Guernsey Limited, Sure Jersey Limited and Sure Isle of Man Limited; Board Member of the Crown Prince International Scholarship Programme; Board Member of Deposit and URIA Protection Board at Central Bank of Bahrain. He holds a Master's degree in Management Sciences and a Sloan Fellowship from MIT (Massachusetts Institute of Technology), USA.

2. Brig. Khalid Mohammed Al Mannai

Vice Chairman
Non-Executive & Non-Independent Director
Appointed on 11 June 2013

Brigadier Khalid Mohammed Al Mannai is the General Manager of the Bahrain Military Pension Fund, and one of the co-founders of the GCC Expanded Military Pension Coverage Committee. He joined the Military Pension Fund after spending 30 years with the Bahrain Defence Force. Brigadier Al Mannai is a Board Member of Bahrain Telecommunications Company (Batelco), the Social Insurance Organisation (SIO) and Osool Asset Management Company. He holds a MBA from Sheffield Hallam University, UK; and has over 34 years' professional experience.

3. Mr. Talal Ali Al Zain

Board Member
Non-Executive & Independent Director
Elected on 7 July 2013

Mr. Talal Ali Al Zain is Chief Executive Officer of PineBridge Investments Middle East BSC (c), and Co-Head of Alternative Investments at PineBridge Investments. Prior to this, he was Board Member and CEO of Bahrain Mumtalakat Holding Company; having previously spent 18 years with Investcorp Bank as Managing Director and Co-Head of Placement & Relationship Management. Talal was Vice President of Private Banking International and Head of Investment Banking Middle East with Chase Manhattan Bank; as well as a Corporate Banker with Citibank Bahrain. Talal Al Zain is a Board Member of Bahrain Islamic Bank and the Bahrain Association of Banks. He previously chaired and served as a board member on many corporations including McLaren, the Bahrain Economic Development Board, Gulf Air, and Bahrain International Circuit. He holds an MBA in Finance from Mercer University, Atlanta, USA; and a BA in Business Administration (majoring in Accounting) from Oglethorpe University, Atlanta, USA.

4. Mr. Khalil Ebrahim Nooruddin

Board Member
Non-Executive & Independent Director
Elected on 7 July 2013

Mr. Khalil Ibrahim Nooruddin is an experienced banker, at both an executive and board level. Currently, he is the Managing Partner of Capital Knowledge, a consulting and training company. Over the past five years, he has concluded several consulting assignments for financial institutions, working on strategy formulation and implementation. Prior to this, Khalil Nooruddin worked for Investcorp Bank, Bahrain; UBS Asset Management in London and Zurich; and Chase Manhattan Bank in Bahrain. He is an active member of several civil and professional societies in Bahrain. A Chartered Financial Analyst, Mr. Nooruddin holds an MSc in Quantitative Analysis from the Stern Business School at New York University, USA; and a BSc in Systems Engineering from the King Fahd University of Petroleum & Minerals, Saudi Arabia. He has over 36 years' professional experience.

5. Mr. Ebrahim Hussain Ebrahim Aljassmi

Board Member
Non-Executive & Independent Director
Elected on 7 July 2013

Mr. Ebrahim Hussain Ebrahim Aljassmi was the Chief Executive Officer & Board Member of Khaleeji Commercial Bank until June 2012, and continued as Board Member until July 2013. Prior to this, he was Chief Executive Officer of the Liquidity Management Centre. Previously, at the Arab Banking Corporation, he held the positions of Vice President-Global Marketing Unit, Vice President-Treasury & Marketable Securities Department, and General Manager-ABC Securities. He has also worked for BBK Financial Services Company, and Shamil Bank. He holds an MBA from the University of Bahrain and a Bachelor's degree in Economics from the University of Kuwait; and has over 33 years' experience in both conventional and Islamic banking.

6. Mr. Othman Ebrahim Naser Al Askar

Board Member
Non-Executive & Independent Director
Elected on 7 July 2013

Mr. Othman Ebrahim Al Askar is the Director of the Investment department of Waqf Public Foundation of the State of Kuwait. He joined the Awqaf Foundation 1995, and held various positions before taking up his current post in 2010. Prior to this, he was Head of the Investment and Banks Department at Kuwait Public Transport Company. Othman Al Askar is a Board Member of the Educational Holding Group, Kuwait; and a former Board Member of Rasameel Structured Finance Company, Kuwait. He holds a BSc in Business Administration and Economics from the Washington Center University, USA; and has over 27 years' professional experience.

7. Mr. Mohammed Ahmed Abdulla

Board Member
Non-Executive & Non-Independent Director
Appointed on 11 June 2013

Mr. Mohammed Ahmed AlKhaja is the Head of Asset Management at Osool Asset Management Company. Prior to Osool, he held senior management positions at Credit Suisse AG-Bahrain Branch and Credit Suisse AG-Dubai. He started his career at HSBC Middle East, before moving to Merrill Lynch-Bahrain where he spent seven years. Mohammed Al Khaja is a Board Member, Chairman of the Nomination & Remuneration Committee and Audit Committee Member at both the Medgulf Group and Medgulf Allianz Takaful. Furthermore, he is a Board Member and Vice Chairman of the Audit Committee of Bahrain Commercial Facilities Company. He holds a Bachelor's degree in Accounting from the University of Bahrain, and is accredited to the National Association of Securities Dealers and the National Futures Association. Mr. AlKhaja has more than 16 years' professional experience.

8. Mrs. Fatima Abdulla Budhaish

Board Member
Executive & Non-Independent Director
Appointed on 5 June 2013

Mrs. Fatima Abdulla Budhaish is Assistant General Manager - Credit Risk at the National Bank of Bahrain (NBB). She joined NBB in 2004, and worked in various capacities before taking up her current position as Assistant General Manager in 2013. Prior to this, she spent five years with BBK. A Certified Public Accountant (USA), Mrs. Budhaish holds an Executive MBA from the University of Bahrain; and attended the Gulf Executive Development Programme at Darden School of Business, University of Virginia, USA. She has over 16 years' professional experience.

9. Dr. Sherif Ayoub

Board Member
Executive & Non-Independent Director
Appointed on 6 February 2014

Dr. Sherif Ayoub has over 16 years of experience in the finance, management consulting, and economic development domains. During his tenure as a Member of the Board of Directors of Bahrain Islamic Bank, he worked at the Islamic Development Bank (IDB) with an advisory responsibility over treasury, investments, and the development of the Islamic finance industry. Dr. Sherif Ayoub acquired his PhD in Finance from the University of Edinburgh in the United Kingdom having been previously educated at Columbia University (Master-level) and Baldwin Wallace University (Bachelor-level) in the United States of America. He has also served as a Visiting Fellow at Harvard University and a Visiting Scholar at INCEIF and IFSB in Malaysia. Dr. Sherif Ayoub is also a CFA Charterholder and a Certified Public Accountant (CPA). Dr. Sherif Ayoub submitted his resignation from the Board of Directors of Bahrain Islamic Bank in October 2014 after he left IDB to join the Islamic Financial Services Board (IFSB) in the position of Assistant Secretary General.

SHARIA'A SUPERVISORY BOARD

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1. Rev. Shaikh
Dr. Abdul Latif Mahmood Al Mahmood

Chairman

Shaikh Al Mahmood is a Member of the Sharia'a Supervisory Board of Takaful International and ABC Islamic Bank, Kingdom of Bahrain; ABC Islamic Bank, London; and the Joint Sharia'a Supervisory Board of AlBaraka Group. He has been a Preacher at a number of Bahrain's mosques since 1973; and a lecturer in Quran interpretation, jurisprudence and preaching. Shaikh Al Mahmood is a regular participant in jurisprudence, educational, economic, intellectual, social and cultural conferences and seminars.

2. Rev. Shaikh
Mohammed Jaffar Al Juffairi

Vice Chairman

Shaikh Aljuffairi is a former Judge of the High Sharia'a Court of Appeal, Kingdom of Bahrain; and seconded as President of the High Sharia'a Court, Ministry of Justice. He is a Friday Imam and speaker.

3. Rev. Shaikh
Adnan Abdullah Al Qattan

Member

Shaikh Al Qattan is a Preacher at the Ahmed Al Fateh Islamic Mosque. He is a Judge of the High Sharia'a, Ministry of Justice, Kingdom of Bahrain; a Puisne Justice of the High Sharia'a Court; and a lecturer at the Islamic Studies Department, University of Bahrain. Shaikh Al Qattan is Chairman of the Orphans and Widows Care Committee of the Royal Courts and the Pilgrimage Mission; and a Member of the Board of Directors of Sanabil for Orphan Care. He is a regular participant in Islamic committees, courses, seminars and conferences.

4. Rev. Shaikh
Dr. Nedham Mohammed Saleh Yacoubi

Member

Shaikh Yacoubi is a Member of several Sharia'a Supervisory Boards around the world, including Bahrain Islamic Bank, Ithmaar Bank, Gulf Finance House and ABC Islamic Bank, Kingdom of Bahrain; Abu Dhabi Islamic Bank and Sharjah Islamic Bank, UAE; ABC Islamic Bank, London; and the Islamic Accounting Standards Organization, Bahrain. He is the recipient of numerous awards in the field of Islamic Finance.

5. Rev. Shaikh
Dr. Essam Khalaf Al Enizi

Member

Shaikh Al Enizi is a Member of Sharia'a and Islamic Studies Faculty at the University of Kuwait. He is a Member of the Sharia'a Supervisory Committee at Boubayan Bank, Al Sham Bank, and Investment Dar, Kuwait; and the Bahrain-based Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI).

ACTING CHIEF EXECUTIVE OFFICER'S REPORT

"Throughout 2014, we intensified our focus on enhancing customer service, which is a key differentiator for the Bank. Important new initiatives in 2014 include the opening of a further two financial malls which offer a convenient 'one-stop-service' for customers; and the enhancement of retail and corporate eBanking services"

In the name of Allah, the Most Beneficent, the Most Merciful.

I am pleased to report that BisB posted another excellent performance in 2014. This was highlighted by a significant growth in profitability, strong performance by our core banking businesses, and further enhancements in customer service. At the same time, we continued to strengthen the Bank's institutional capability, and honour our commitment to corporate social responsibility. Such achievements underline our successful efforts in implementing the Bank's new five-year strategy.

Financial highlights
Illustrating the excellent financial performance by BisB in 2014, net profit increased by a significant 52 percent to BD 9.3 million from BD 6.1 million in 2013; and total income grew by 19 percent to BD 43 million from BD 36 million the previous year. Islamic financing witnessed an increase of 17 percent, investments in Sukuk grew by 113 percent, and current accounts rose by 30 percent. The Bank maintained a liquid assets ratio of 14 percent, while the cost of funding reduced by 32 percent.

Importantly, the Bank relied fully on revenues and fees from financing and major core activities, which were responsible for generating 82 percent of operating income. Moreover, the Bank successfully disposed of some investments assets including listed equities, managed funds and real estate, which realised a net gain of BD 7 million.

Business growth
The Bank's core business activities posted another strong performance in 2014.

The launch of additional new initiatives, services and products, together with a continued focus on customer service, resulted in the Retail customer base expanding by 14.5 percent and market share growing by 13.5 percent. Islamic financing increased by 17 percent, current accounts rose by 30 percent, and the cost of funding reduced by 32 percent. This was achieved against a backdrop of intensified competition in Bahrain's banking sector.

Corporate banking enjoyed another successful year in 2014. Achievements include improving market share by booking substantial new assets, and growing the number of borrowing relationships by 20 percent. BisB also extended its support for the small-to-medium enterprises (SMEs) sector with an additional BD 20 million being made available to Tamkeen's Enterprise Financing Scheme. This raises the value of the Tamkeen-BisB agreement to BD 50 million, through which over 200 SMEs have benefited to date.

Customer service
Throughout 2014, we intensified our focus on enhancing customer service, which is a key differentiator for the Bank. A major initiative in 2014 was the opening of a further two financial malls which offer a convenient 'one-stop-service' for customers. Other notable customer service-related initiatives include the enhancement of retail and corporate eBanking services; the launch of a new Titanium MasterCard; and, for the first time in the Kingdom of Bahrain, the exclusive introduction of the Signature Debit Visa card for the Bank's Al Thuraya private and priority banking clients.

Institutional capability
In line with the objectives of the Bank's new strategy, we continued to strengthen the Bank's operating infrastructure and streamline operations during 2014. In terms of human capital, we initiated an organisational right-sizing exercise, with some staff accepting an attractive voluntary early retirement option. At the same time, we maintained our focus on providing training and development opportunities for staff to realise their full potential and enhance their careers.

During the year, we continued to implement a major strategic revamp of the Bank's information and communication technology(ict) infrastructure. This included upgrading the core banking system; enhancing financial reporting and management information systems; and further streamlining back office operational processes and procedures. In addition, new state-of-the-art systems were installed in the areas of human resources, retail collections, purchasing and

Mohammed Ahmed Janahi
Acting Chief Executive Officer

archiving. We also maintained our focus on strengthening business continuity planning, with the successful upgrading and testing of the Bank's information security systems and disaster recovery site.

In 2014, we further enhanced the Bank's corporate governance and risk management framework in line with the latest regulatory requirements. Key developments in 2014 include taking the necessary steps to ensure compliance with the implementation of the Foreign Account Tax Compliance Act (FATCA), the launch of the Corporate Credit Reference Bureau, and the Sound Remunerations Policy issued by the Central Bank of Bahrain.

Corporate responsibility
BisB is committed to contributing to the economic development and social well-being of the Kingdom of Bahrain through a comprehensive corporate social responsibility programme. This includes supporting the development of the Islamic banking industry by sponsoring and participating in a number of key industry events. In 2014, the Bank was a Strategic Platinum sponsor of the 21^{st} World Islamic Banking Conference; and Gold sponsor of the annual Islamic Banking and Finance Conference organised by the Accounting & Auditing Organisation for Islamic Financial Institutions (AAOIFI). We also maintained our active support for numerous charitable, educational, medical, cultural, sporting and social organisations; while encouraging staff to participate in community activities.

Industry recognition
The considerable achievements by Bahrain Islamic Bank during 2014 – financial, business and operational – were recognised by receipt of the 'Best Islamic Bank in Bahrain' award from World Finance, a leading UK-based financial magazine. A prestigious judging panel, supported by a research team, reviewed nominations from the magazine's readers as part of the process of selecting winning institutions in the field of Islamic finance and banking.

Future outlook
Looking ahead, we remain confident about the future outlook for Bahrain, which is our core market; and are cautiously optimistic about the prospects for BisB in 2015. The Government has restated its commitment to ongoing social, political and economic reforms; and increased investment in major infrastructure projects. According to the Bahrain Economic Development Board, the allocation of up to US$ 4.4 billion for major capital works will supplement existing growth levels, and also strengthen the economy's base for longer-term development.

Latest forecasts by the IMF show that the Kingdom's GDP growth for 2014 is expected to be around 4 percent, well above the 2.7 percent predicted for the broader Middle East; and will continue to grow faster in 2015 than the global and regional economies, despite the effect of declining oil prices. With God's blessing,this should continue to have a positive impact on business and consumer confidence, which in turn will benefit the local banking sector in general, and BisB in particular.

Acknowledgements
In conclusion, I would like to express my gratitude to the Board of Directors for its confidence and encouragement, and the Sharia'a Supervisory Board for its guidance and supervision. Sincere appreciation is also due to our customers for their trust and loyalty, and our business partners for their positive and constructive cooperation. I would like to pay a special tribute to our management and staff for their continued dedication, innovation and professionalism, which contributed to another successful year for Bahrain Islamic Bank.

Allah the Almighty is the Purveyor of all Success.

Mohammed Ahmed Janahi
Acting Chief Executive Officer

EXECUTIVE MANAGEMENT

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1. Mohammed Ahmed Janahi
Acting Chief Executive Officer

Mr. Mohammed Ahmed Janahi is a veteran banker with a vast experience in banking and financial operations of over 45 years. He commenced his career with Bahrain Islamic Bank in 2007 in the position of General Manager Support Services. In September 2014, he assumed his current position. Prior to joining BisB, Mr. Janahi held a number senior executive positions in Citibank, National Bank of Bahrain, Al Baraka Islamic Bank and Gulf Air in Bahrain. Mr. Janahi attended numerous courses on administrative sciences, banking and leadership at renowned universities and institutes in Europe and USA. In addition, he also attended a number of intensive and diversified workshops at leading institutions and banks, including Citibank, Financial Times and the Executive Development Institute in London.

2. Abdulrahman Mohammed Turki
General Manager - Retail Banking

Abdulrahman Turki has 35 years' experience in banking. He took up his current position at BisB in 2008. Prior to this, he was Head of Islamic Retail Banking at Commercial Bank of Qatar. Abdulrahman held various positions with a number of other prominent regional banks, after starting his career with Aluminium Bahrain. He holds an MBA degree from the University of Strathclyde, Scotland, UK.

3. Yousif M. A. Karim
Acting General Manager - Corporate & Institutional Banking

Yousif A. Karim has 42 years' experience in banking operations and marketing. He took up his current position with BisB in 2011. Prior to this, he was General Manager - Riyadh branch of the National Bank of Bahrain. Yousif holds a Master's degree in Business Administration, Executive Management Diploma and Advance Banking Studies Diploma, in addition to attending various programmes both, locally and internationally.

4. Khalid Mohammed Al Doseri
Chief Financial Officer

Khalid Al Doseri has over 31 years' professional experience in banking and accountancy. He took up his current position with BisB in 2003. Prior to this, he worked for Ithmar Bank (Formerly Faysal Islamic Bank) for 13 years, and started his career with Kuwait Asia Bank. Khalid is a Board Member of the Liquidity Management Centre, Chairman of Risk Committee and Member of Executive Committee, and was previously a Board Member and Managing Director of Islamic Bank of Yemen from 2007 till 2009. He is a Certified Public Accountant from Oregon Board of Accountancy, USA; and holds an MBA degree from University of Glamorgan, Wales, UK. Khalid is a graduate of the Gulf Executive Development Programme at Darden School of Business, University of Virginia, USA.

5. Dr Mohammed S. Belgami
Head of Credit and Risk Management

Dr Mohammed Belgami has over 31 years' international experience in the fields of credit analysis, risk management, valuation, due diligence and financial management, and research and academia. He joined BisB in 2008 and took up his current position in 2013. Prior to this, Dr Mohammed held senior management positions with the Saad Trading, Contracting & Financial Services Company, and Kuwait Finance House-Bahrain; as well as academic positions with institutions in Bahrain and India. A Financial Risk Manager from the Global Association of Risk Professionals, he holds a Doctoral degree and Master's and Bachelor's degrees in Finance & Accounting and Commerce.

6. Khalid Mahmood Abdulla
Head of Internal Audit

Khalid Mahmood Abdulla has 20 years of experience in accounting, auditing, banking and sharia. He took up his current position with BisB in 2006. Prior to this, he was Head of Internal Audit at Al Baraka Islamic Bank, having started his career with Arthur Anderson. Khalid is a Certified Public Accountant (CPA) California, USA, and attended the Leadership Development Program at Darden School of Business, University of Virginia, USA.

THE FINANCIAL MALLS OFFER A CONVENIENT 'ONE-STOP-SERVICE' FOR CUSTOMERS, PROVIDING THE HIGHEST LEVELS OF FUNCTIONALITY AND COMFORT TO ENSURE AN ENHANCED CUSTOMER EXPERIENCE.

REVIEW OF OPERATIONS

BUSINESS DIVISIONS

Retail Banking

BisB's retail banking business posted another strong performance in 2014, outperforming the CBB Consumer Finance Index for the sixth consecutive year, with the Bank's Islamic finance portfolio growing by 19% compared with 7% for the CBB Index. Key performance highlights include an increased customer base and market share; a reduction in the cost of funding; and growth across all main product lines and services. This performance was achieved despite intensified competition in the retail banking sector of the Kingdom of Bahrain.

The Bank successfully increased its retail customer base by 14%, grew its overall market share to 11%, and reduced its cost of funding by 32%. The excellent growth recorded by all main products during the year include Tas'heel Personal Finance growing by 19%; mortgage financing by 28% and auto financing by 7%; credit card accounts and receivables by 18% and 13% respectively; the Vevo Youth Account by 13% and the Iqra Investment Scheme by 7%; together with the Tejoori savings account by 5% and bancassurance by 7%.

Underpinning this strong performance was a continued focus on customer service, which acts as a key competitive differentiator for the Bank. Key customer service developments in 2014 include the opening of two new Financial Malls in Hamad Town and Riffa to complement the existing malls at Arad and Budaiya. These purpose-designed malls offer a convenient 'one-stop-service' for customers, providing the highest levels of functionality and comfort to ensure an enhanced customer experience. Feedback to date from customers and staff has been extremely positive, with customers benefiting from longer opening hours and convenient parking, and staff enjoying an enhanced working environment. As a result of four malls now being in operation, the branch network was reduced to seven outlets, with extended opening hours. In addition, nine new locations for BisB Automated Teller Machines were identified, including ATMs at selected UAE Exchange branches.

RETAIL BANKING GROWS CUSTOMER BASE

THE LAUNCH OF ADDITIONAL NEW INITIATIVES, SERVICES AND PRODUCTS DURING 2014, TOGETHER WITH A CONTINUED FOCUS ON CUSTOMER SERVICE, RESULTED IN THE BANK'S RETAIL CUSTOMER BASE EXPANDING BY 14 PERCENT, WITH ISLAMIC FINANCING GROWING BY 19 PERCENT, DESPITE INTENSIFIED COMPETITION IN BAHRAIN'S BANKING SECTOR.

During the year, the Bank continued to enhance its range of products and services. A key development was the launch of Al Thuraya Privileged Banking Services for high net worth clients. Al Thuraya provides a dedicated relationship manager who can advise clients on their specific banking and investment needs. Exclusive privileges include Visa Signature cards offering higher daily withdrawal and spending limits; global concierge services, special benefits at luxury hotels, and access to over 500 airport lounges worldwide; and comprehensive insurance cover. To support Al Thuraya clients, BisB became the first bank in Bahrain to offer the new Visa Signature debit card with exclusive benefits, as well as introducing the MasterCard Titanium card.

During the year, there was a further increase in the number of customers migrating to eBanking services, including a growth in credit card payments through the Benefit Payment Gateway.

These services will be further enhanced in 2015 with the planned introduction of a full-fledged Mobile Banking service, enabling customers to conduct transactions through their smart phones and tablets. The new eKiosks launched last year have proved to be popular with customers. As well as offering convenient access to online banking and credit card payment services, eKiosks provide information about ongoing product and services promotions; together with a practical guide on how to use and benefit from eBanking, including internet banking, mobile banking, phone banking and point-of-sale services.

In a significant development during 2014, BisB was appointed as a participating bank in the Government's new Social Housing Finance Scheme. This enables Bahraini citizens who are on the Ministry of Housing waiting list to purchase a housing unit from an accredited developer by obtaining financing from a participating bank, which will be supplemented by additional financial support from the Government.

To enable the Bank's staff to deliver the highest standards of customer service, priority continued to be placed on training and development, with a number of customised training programmes being conducted throughout 2014. These covered technical training courses for newly-appointed tellers; customer service-oriented sessions for sales staff in malls and branches, including sales and negotiation skills; and special leadership seminars for retail managers. In addition, regulatory-related training courses were held for anti-money laundering (AML), Know Your Customer (KYC), and the Foreign Account Tax Compliance Act (FATCA) for US entities and individuals.

The Bank's achievements during 2014 were recognised by receipt of the 'Best Islamic Bank in Bahrain' award from World Finance, a leading UK-based financial magazine. A prestigious judging panel supported by a research team, reviewed nominations from the magazine's readers as part of the process of selecting winning institutions in the field of Islamic finance and banking.

Corporate & Institutional Banking

In order to provide a more dedicated client service, BisB's Corporate & Institutional Banking division has been structured into separate teams responsible for corporate banking, structured finance, commercial banking and SME banking. The Bank focuses on three key segments – corporate financing, sovereign and quasi-sovereign institutions, and small-and-medium enterprises (SMEs).

The division benefited from improved market confidence in BisB following the changes to the Bank's shareholding structure during 2013, with NBB and the Social Insurance Organisation now jointly holding a majority stake. Together with its sharper segment focus and a more assertive business development approach, Corporate & Institutional Banking posted a strong performance in 2014.

During the year, the Bank continued to enhance its range of products and services. A key development was the launch of Al Thuraya Privileged Banking Services for high net worth clients.

The Bank managed to attract substantial new high-quality assets with existing and new clients; and a growth of 20% in the number of borrowing relationships. The increase in assets was achieved by reducing the cost of funding, which enabled the Bank to improve its lending rate and compete more effectively with both Sharia'a-compliant and conventional competitors. Another key achievement was a significant improvement in delinquent account recoveries, with a reduction in non-performing loans of over 30%.

Good progress was also made in the area of project financing, with a number of high-quality current transaction being finalised during the year; and the development of a strong pipeline of mandates that are expected to materialise in 2015. The Bank also expanded the provision of trade finance facilities for small-and-medium enterprises. Support for SME sector was enhanced with an additional BD 20 million being made available to Tamkeen's Enterprise Financing Scheme. This raises the value of the Tamkeen-BisB agreement to BD 50 million, from which over 200 SMEs have benefited to date.

During the year, the division maintained its focus on customer service, which serves as an important competitive differentiator. There has been an encouraging response to phase one of the new corporate internet banking service, with 90% of customers now using this new online facility. This will be further enhanced in 2015 with the addition of new transactional functionalities. An increased number of customers are also using the dedicated Contact Centre, which provides an enhanced personal service by telephone and e-mail.

Plans for 2015 include expanding trade finance activities and expanding the customer base in Bahrain; introducing new products such as Islamic overdrafts and cheque discounting; and continuing to reduce non-performing loans. In line with the Bank's new five-year strategy, the Corporate & Institutional Banking division will actively explore new business opportunities in markets outside Bahrain, including regional syndications, bilateral deals and Sukuk issues.

CORPORATE BANKING EXTENDS HELP FOR SMEs

BisB EXTENDED ITS SUPPORT FOR THE SMALL-TO-MEDIUM ENTERPRISES (SMEs) SECTOR IN 2014 WITH AN ADDITIONAL BD 20 MILLION BEING MADE AVAILABLE TO TAMKEEN'S ENTERPRISE FINANCING SCHEME. THIS RAISES THE VALUE OF THE TAMKEEN-BisB AGREEMENT TO BD 50 MILLION, THROUGH WHICH OVER 200 SMEs HAVE BENEFITED TO DATE.

113%

Sukuk portfolio growth in 2014

A NUMBER OF NON-CORE AND NON-PERFORMING INVESTMENT ASSETS WERE EXITED, GENERATING A NET GAIN OF BD 9 MILLION. THIS EXCESS LIQUIDITY WAS INVESTED IN SHORT- AND MEDIUM-TERM FIXED INCOME INSTRUMENTS.



ENHANCING CUSTOMER SERVICE AND CONVENIENCE

KEY CUSTOMER SERVICE-RELATED INITIATIVES DURING 2014 INCLUDE THE OPENING OF TWO ADDITIONAL FINANCIAL MALLS; THE LAUNCH OF A TITANIUM MASTERCARD; AND, FOR THE FIRST TIME IN THE KINGDOM OF BAHRAIN, THE EXCLUSIVE INTRODUCTION OF THE VISA SIGNATURE DEBIT CARD FOR AL THURAYA PRIVATE AND PRIORITY BANKING CUSTOMERS.

Treasury and Investments

The Bank's Treasury business had another successful year in 2014, continuing to manage the Bank's liquidity and attracting increased deposits, with the foreign exchange (FX) business being a major contributor to fee-based income. Following the change to the shareholding structure of BisB, previous relationships were re-established with regional banks, complementing the numerous relationships maintained over the years with Gulf-based and international banks. These interbank affiliations, which are managed by a dedicated Financial Institutions team, are essential in managing the Bank's liquidity and short-term funding requirements. BisB uses both Wakala and International Commodity Murabaha instruments in its interbank dealings.

Throughout the year, the Treasury team successfully enhanced profitability by executing various FX and money market strategies; increasing market making activities for GCC and major international currencies; and significantly reducing the Bank's overall cost of funding. Planned enhancements to the treasury infrastructure include an upgrade of the Reuters EIKON system, which will serve as a one-stop terminal for dealing and data capture.

A more conservative investment approach was adopted in 2014, with net income from investments totalling BD 5 million compared with BD 8.8 million the previous year. In line with implementing a key objective of the Bank's new five-year strategy, a number of non-core and non-performing investment assets were exited, generating a net gain of BD 9 million. This excess liquidity was invested in short- and medium-term fixed income instruments, resulting in the Sukuk portfolio growing by over 113%, and enhancing recurring income. The composition of the Bank's well-balanced investment portfolio consists of Sukuks, GCC equities and third-party funds; infrastructure projects such as Al Dur Power & Water Plant, in which BisB is a founding shareholder; and private equity transactions on a strictly case-by-case basis.

DURING THE YEAR, THE BANK CONTINUED ITS POLICY AIMED AT DEVELOPING ITS SERVICES AND PRODUCTS TO MEET CUSTOMERS' NEEDS AND DESIRES.

BisB CONTINUED TO INVEST IN THE TRAINING AND DEVELOPMENT OF ITS PEOPLE DURING 2014. FOCUS WAS PLACED ON LEADERSHIP AND STRATEGY; TECHNICAL SKILLS INCLUDING CREDIT RISK ANALYSIS AND RESTRUCTURING PROBLEM CREDITS; AND CUSTOMER SERVICE SKILLS SUCH AS SALES AND NEGOTIATION.

97%
Total Bahraini Workforce

THE NUMBER OF BAHRAINI NATIONALS EMPLOYED BY THE BANK REMAINED AT 97% OF THE TOTAL WORKFORCE – THE HIGHEST OF ANY BANK IN BAHRAIN.

SUPPORT SERVICES

Human Capital

In 2014, the Board approved a revised voluntary early retirement programme to facilitate the organisational right-sizing objective of the Bank's new five-year strategy to streamline operations and reduce costs. The number of Bahraini nationals employed by the Bank remained at 97% of the total workforce – the highest of any bank in Bahrain.

Another key HR project involved the development and Board approval of a variable remuneration policy in conformance with new rules from the Central Bank of Bahrain for sound remuneration practices by licensed banks. In line with new CBB rules, performance-based incentives were established for cascading down the organisation to link bonuses with the Bank's overall and divisional performance.

BisB successfully implemented its succession planning policy during the year. A number of senior management promotions took place, including a new Deputy Chief Executive Officer and Acting CEO, Assistant General Managers, and Senior Managers. BisB also commenced the phased implementation of a new SAP human resources management system. This includes applications for payroll, time and attendance, HR, training and an online staff self-service facility.

Training and Development

BisB continued to invest in the training and development of its people during 2014. Focus was placed on leadership and strategy; technical skills including credit risk analysis and restructuring problem credits and customer service skills such as sales and negotiation; In collaboration with the Compliance and Risk Management divisions, regulatory training was also conducted, covering Anti-Money Laundering (AML), Know Your Customer (KYC), Foreign Account Tax Compliance Act (FATCA) for US entities and individuals, Islamic Banking ethics and Financial Advise Programme (FAP)

STRENGTHENING THE IT INFRASTRUCTURE

KEY INFORMATION TECHNOLOGY ACHIEVEMENTS IN 2014 INCLUDE UPGRADING THE CORE BANKING SYSTEM; AND STRENGTHENING BUSINESS CONTINUITY PLANNING BY ENHANCING THE DISASTER RECOVERY SITE AND INFORMATION SECURITY FRAMEWORK. THE BANK ALSO COMMISSIONED NEW SYSTEMS IN THE AREAS OF HUMAN RESOURCES, RETAIL COLLECTIONS, PURCHASING AND ARCHIVING.

BisB also focused on strengthening business continuity planning, with the successful upgrading and testing of the disaster recovery site and information security systems.

The Bank also continued to support staff in gaining professional qualifications. During the year, five employees achieved certifications in financial services (CFA, CPA and CIPA) and human resources (HRME), while three employees achieved the Advanced Diploma in Islamic Finance (ADIF) certifications. The total number of training hours delivered in 2014 was over 4,000, with over 70 percent of staff attending training courses internally and externally.

Information & Communications Technology

In line with the Bank's new five-year strategy, a major upgrade of the information and communications technology (ICT) infrastructure commenced in 2014. New ICT developments during the year include finalising a new ICT policy; commencing the upgrade of the core banking system; enhancing financial reporting and MIS systems; revamping customer relationship management (CRM); finalising new frameworks for IT service management and information security; and further streamlining back office operational processes and procedures.

In addition, new state-of-the-art systems were installed in the areas of human resources, retail collections, purchasing and archiving. The Bank also focused on strengthening business continuity planning, with the successful upgrading and testing of the disaster recovery site and information security systems.

Good progress was made in the critical areas of IT service management (ITSM) and information security (IS). An ITSM framework and procedures, in line with ISO 2000 accreditation, were approved by the Board; and development of procedures commenced, along with certifying selected IT staff to the foundation level of IT infrastructure library (ITIL) standards. The information security framework, based on ISO 27001, was also finalised and reviewed by Internal Audit for subsequent approval by the Board. In addition, a network vulnerability assessment was conducted, and web penetration testing conducted; together with the development of a risk mitigation action plan.

ICT also continued to play a critical role in the development of new customer services. These include expanding the provision of eChannels such as retail and corporate online banking, and eKiosks; the opening of two new financial malls; and upgrading and expanding the ATM network. These developments were supported by uptime service levels of over 99%.

Central Operations

Central Operations supports the Bank's business lines through four dedicated units covering all transactions for payments, treasury back office, trade finance, and Islamic financing. During the year, the Bank continued to enhance its operational efficiency through increased automation, and identifying and implementing new ways of better utilising its resources. New developments include implementing a new electronic approval system (EAP) and electronic archiving for Islamic financing; and testing phase two of the straight-through-processing (STP) system to automate correspondent outward payments. In addition, full implementation of phase one of the new Sunguard Quantum treasury system was completed, and planning was finalised for implementation of phase two in early 2015. The overall level of automation within the Bank increased to 75 percent in 2014.

General Services

The role of General Services is to ensure the smooth day-to-day functioning of the Bank. The department's responsibilities cover archiving, mail, procurement, quality control, utilities, property management, branch renovations, maintenance, transport and security. Key activities in 2014 include the opening of new financial malls at Hamad Town and Riffa; ongoing refurbishment of head office departments and reception area; and finalising the head office external works. In addition, good progress was made with electronic archiving of documentation for all transactions and finalising a new barcode storage system; and completing an inventory of all fixed assets. The Bank has in place a 24-hour security room providing live viewing of CCTV footage from all financial malls, branches and ATMs across Bahrain.

Corporate Communications

During 2014, BisB continued to enhance its external and internal communications activities. External communications developments include the launch of a new responsive version of its website, which enables viewing from any smart devices; enhanced relationships with the media and other banks; and active participation in conferences and events, including sponsorship of Islamic Conferences. In terms of internal communications, a new staff suggestions and complaints system was introduced; and additional staff social events, including desert camping, were organised to improve inter-departmental communications.

‘BEST ISLAMIC BANK IN BAHRAIN 2014’ AWARD

THE CONSIDERABLE ACHIEVEMENTS BY BAHRAIN ISLAMIC BANK DURING 2014 – FINANCIAL, BUSINESS AND OPERATIONAL – WERE RECOGNISED BY RECEIPT OF THE ‘BEST ISLAMIC BANK IN BAHRAIN’ AWARD FROM WORLD FINANCE, A LEADING UK-BASED FINANCIAL MAGAZINE. A JUDGING PANEL WITH OVER 230 YEARS’ EXPERIENCE IN FINANCIAL AND BUSINESS JOURNALISM, SUPPORTED BY A DEDICATED RESEARCH TEAM, REVIEWED NOMINATIONS FROM THE MAGAZINE’S READERS AS PART OF THE PROCESS OF SELECTING WINNING INSTITUTIONS IN THE FIELD OF ISLAMIC FINANCE AND BANKING.

RISK MANAGEMENT REVIEW

As an inherent part of the Bank's activities, risk is managed through a process of ongoing identification, measurement, monitoring and reporting in line with the risk appetite of the Bank, which is set and guided by the Board of Directors. This process of risk management is critical to the continued profitability of BisB, and all individuals within the institution are personally accountable for the risk exposures relating to their responsibilities.

The Bank is exposed primarily to credit risk, liquidity risk, market risk (including profit rate, equity price and currency risks), operational risk, reputational risk and Sharia'a-compliant risk.

Risk management philosophy

The risk management philosophy of BisB is to identify, capture, monitor and manage the various dimensions of risk. The objective is to protect asset values and income streams so that the interests of the Bank's stakeholders are safeguarded; while optimising shareholders' returns, and maintaining risk exposure within the parameters set by the Board.

The Bank has defined its risk appetite within the broad framework of its Risk Strategy. BisB reviews and aligns its risk appetite in line with its evolving business plan, and changing economic and market scenarios. The Bank also assesses its tolerance for specific risk categories and its strategy to manage these risks.

Risk management framework

BisB has in place a comprehensive enterprise-wide integrated risk management framework (Risk Governance). This embraces all levels of authorities, organisational structure, people and systems required for the smooth functioning of risk management policies within the Bank.

The Board of Directors retains ultimate responsibility and authority for all risk matters, including establishing overall policies and procedures. The Board is assisted in fulfilling its responsibilities by the Acting Chief Executive, and various Board-level and Management committees.

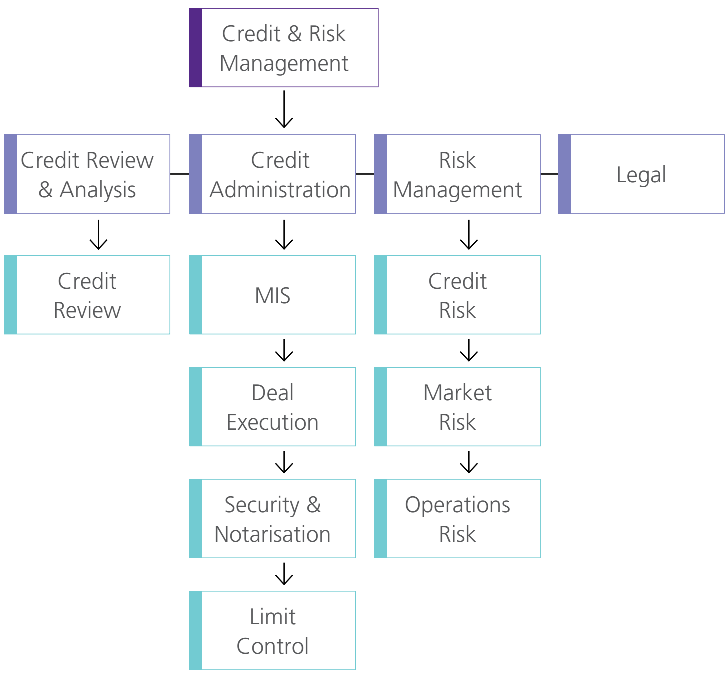
The Credit & Risk Management (C&RM) division – headed by an Assistant General Manager reporting to the Chief Executive on a day-to-day administrative basis, and to the Board Risk Committee – has day-to-day responsibility for managing the risks involved across all areas of the Bank. C&RM provides independent identification, measurement, monitoring and control of all risk parameters, while liaising with the business divisions that ultimately own the risks. C&RM comprises a number of specialist units, including Risk Management, Credit Review & Analysis, Credit Administration, Benefit Credit Reference Bureau Reporting, and Legal Affairs.

Developments in 2014

In light of the prevailing global and regional market conditions, the Bank placed the highest priority on further strengthening its risk management infrastructure during 2014. Key developments and initiatives achieved include:

- Implementing approved Business Continuity Planning framework.
- Introducing Corporate Credit Scoring Model (AVRA) and new pricing model.
- Preparing for Basel III implementation.
- Providing external training programme to business units and C&RM on Credit review, rating and restructuring.
- Participating in the Basel III working group set up by the Central Bank of Bahrain.
- Ensuring ongoing compliance with the policies of the Bank, and monitoring the enterprise-wide risk through various systems and processes.
- Ensuring ongoing compliance with the rules and regulations of the Central Bank of Bahrain and Basel II requirements.
- Monitoring Sharia'a-compliant risk as well as the other risks to which BisB is exposed.

Note: Additional information on the Bank's risk management framework, policies, processes and procedures is included in the Notes to the Consolidated Financial Statements and the Basel II Pillar 3 Public Disclosure sections of this annual report.



REMUNERATION DISCLOSURES

The Bank's total compensation approach, which includes the variable remuneration policy, sets out the Banks's policy on remuneration for Directors and senior management and the key factors that are taken into account in setting the policy.

During the year, the Bank adopted regulations concerning Sound Remuneration Practices issued by the Central Bank of Bahrain, and has proposed revisions to its variable remuneration framework. The revised policy framework and incentive components are subject to the approval of the shareholders in the upcoming Annual General Meeting. Once approved, the policy will be effective for the 2014 annual performance incentives and will be fully implemented for future periods.

The key features of the proposed remuneration framework are summarised below.

Remuneration strategy

It is the Bank's basic compensation philosophy to provide a competitive level of total compensation to attract and retain qualified and competent employees. The Bank's variable remuneration policy will be driven primarily by a performance based culture that aligns employee interests with those of the shareholders of the Bank. These elements support the achievement of the Bank's objectives through balancing rewards for both short-term results and long-term sustainable performance. This strategy is designed to share success, and to align employees' incentives with the risk framework and risk outcomes.

The quality and long-term commitment of all BisB's employees is fundamental to success. The Bank therefore aims to attract, retain and motivate the very best people who are committed to maintaining a career with the Bank, and who will perform their role in the long-term interests of shareholders. The Bank's reward package comprises the following key elements:

1. Fixed pay
2. Benefits
3. Annual performance bonus

A robust and effective governance framework ensures that the Bank operates within clear parameters of its compensation strategy and policy. All compensation matters, and overall compliance with regulatory requirements, are overseen by the Board Nomination & Remuneration Committee (NRC).

The Bank's remuneration policy in particular, considers the role of each employee and has set guidance on whether an employee is a Material Risk Taker and / or an Approved Person in a business line, control or support function. An Approved Person is an employee whose appointment requires prior regulatory approval because of the significance of the role within the Bank; and an employee is considered a Material Risk Taker if they are the Head of a significant business line or any individuals within their control who have a material impact on the Bank's risk profile.

In order to ensure alignment between what BisB pays its people and the business strategy, individual performance is assessed against annual and long-term financial and non-financial objectives summarized in the performance management system. This assessment also takes into account adherence to the Bank's values, risks and compliance measures and above all integrity. Altogether, performance is therefore judged not only on what is achieved over the short and long-term, but also importantly on how it is achieved, as the NRC believes the latter contributes to the long-term sustainability of the business.

NRC role and focus

The NRC has oversight of all reward policies for the Bank's employees. The NRC is the supervisory and governing body for compensation policy, practices and plans. It is responsible for determining, reviewing and proposing variable remuneration policy for approval by the Board. It is responsible for setting the principles and governance framework for all compensation decisions. The NRC ensures that all persons must be remunerated fairly and responsibly. The remuneration policy is reviewed on a periodic basis to reflect changes in market practices, the business plan and risk profile of the Bank.

The responsibilities of the NRC with regards to the Bank's variable remuneration policy, as stated in its mandate, include but are not limited to, the following:-

- Approve, monitor and review the remuneration system to ensure the system operates as intended.
- Approve the remuneration policy and amounts for each Approved Person and Material Risk-Taker, as well as total variable remuneration to be distributed, taking account of total remuneration including salaries, fees, expenses, bonuses and other employee benefits.
- Ensure remuneration is adjusted for all types of risks and that the remuneration system takes into consideration employees that earn the same short-run profit but take different amounts, of risk on behalf of the Bank.

REMUNERATION DISCLOSURES
CONTINUED

- Ensure that for Material Risk-Takers, variable remuneration forms a substantial part of their total remuneration.
- Review the stress testing and back testing results before approving the total variable remuneration to be distributed including salaries, fees, expenses, bonuses and other employee benefits.
- Carefully evaluate practices by which remuneration is paid for potential future revenues whose timing and likelihood remain uncertain. The NRC will question payouts for income that cannot be realised or whose likelihood of realisation remains uncertain at the time of payment.
- Ensure that for Approved Persons in risk management, internal audit, operations, financial control and compliance functions, the mix of fixed and variable remuneration is weighted in favour of fixed remuneration.
- Recommend Board member remuneration based on their attendance and performance and in compliance with Article 188 of the Bahrain Commercial Companies Law.
- Ensure appropriate compliance mechanisms are in place to ensure that employees commit themselves not to use personal hedging strategies or remuneration-and liability-related insurance to undermine the risk alignment effects embedded in their remuneration arrangements.

As outlined in the Corporate Governance section of the Annual Report, the Board is satisfied that all non-executive Directors are independent including the NRC members. The NRC comprises the following members:

NRC Member Name	Appointment date	Number of meetings attended
Abdul Razak Abdulla Hassan Al Qassim	5 June 2013	4
Khalid Mohammed Al Mannai	11 June 2013	4
Mohamed Ahmed Abdulla	11 June 2013	4

The aggregate remuneration paid to NRC members during the year in the form of sitting fees amounted to BHD 3,000 [2013: BHD 12,000].

External consultants

Consultants were appointed during the year to advise the Bank on amendments to its the variable remuneration policy to be in line with the CBB's Sound Remuneration Practices and Industry Norms. This included assistance in designing an appropriate Share-based Incentive Scheme for the Bank.

Scope of application of the remuneration policy

The variable remuneration policy has been adopted on a bank-wide basis.

Board remuneration

The Bank's Board remuneration is determined in line with the provisions of Article 188 of the Bahrain Commercial Companies Law, 2001. The Board of Directors' remuneration will be capped so that total remuneration (excluding sitting fees) does not exceed 10% of the Bank's net profit after all required deductions as outlined in Article 188 of the Companies law, in any financial year. Board remuneration is subject to approval of the shareholders in the Annual General Meeting. Remuneration of non-executive Directors does not include performance-related elements such as grants of shares, share options or other deferred stock-related incentive schemes, bonuses or pension benefits.

Variable remuneration for staff

Variable remuneration is performance related and consists primarily of the annual performance bonus award. As a part of staff's variable remuneration, the annual bonus rewards delivery of operational and financial targets set each year, the individual performance of the employees in achieving those targets, and their contribution to delivering the Bank's strategic objectives.

The Bank has adopted a Board approved framework to develop a transparent link between variable remuneration and performance. The framework is designed on the basis of meeting both satisfactory financial performance and the achievement of other non-financial factors, that will, all other things being equal, deliver a target bonus pool for employees, prior to consideration of any allocation to business lines and employees individually. In the framework adopted for determining the variable remuneration pool, the NRC aims to balance the distribution of the Bank's profits between shareholders and employees.

Key performance metrics at the Bank level include a combination of short term and long term measures and include profitability, solvency, liquidity and growth indicators. The performance management process ensures that all goals are appropriately cascaded down to respective business units and employees.

In determining the amount of variable remuneration, the Bank starts from setting specific targets and other qualitative performance measures that result in a target bonus pool. The bonus pool is then adjusted to take account of risk via the use of risk-adjusted measures (including forward-looking considerations).

The NRC carefully evaluates practices by which remuneration is paid for potential future revenues whose timing and likelihood remain uncertain. NRC demonstrates that its decisions are consistent with an assessment of the Bank's financial condition and future prospects.

The Bank uses a formalised and transparent process to adjust the bonus pool for quality of earnings. It is the Bank's objective to pay out bonuses out of realised and sustainable profits. If the quality of earnings is not strong, the profit base could be adjusted based on the discretion of the NRC.

For the overall Bank to have any funding for distribution of a bonus pool, threshold financial targets have to be achieved. The performance measures ensure that total variable remuneration is generally, considerably contracted where subdued or negative financial performance of the Bank occurs. Furthermore, the target bonus pool as determined above is subject to risk adjustments in line with the risk assessment and linkage framework.

Remuneration of control functions

The remuneration level of staff in the control and support functions allows the Bank to employ qualified and experienced personnel in these functions. The Bank ensures that the mix of fixed and variable remuneration for control and support function personnel should be weighted in favour of fixed remuneration. The variable remuneration of control functions is to be based on function-specific objectives and is not be determined by the financial performance of the business are as they monitor.

The Bank's performance management system plays a major role in deciding the performance of the support and control units on the basis of the objectives set for them. Such objectives are more focused on non-financial targets that include risk, control, compliance and ethical considerations, as well as the market and regulatory environment apart from value adding tasks which are specific to each unit.

Variable compensation for business units

The variable remuneration of the business units is primarily determined by key performance objectives set through the performance management system of the Bank. Such objectives contain financial and non-financial targets, including risk control, compliance and ethical considerations as well as market and regulatory requirements. The consideration of risk assessments in the performance evaluation of individuals ensures that any two employees who generate the same short-run profits but take different amounts of risk on behalf of the Bank are treated differently by the remuneration system.

Risk assessment framework

The purpose of risk linkages is to align variable remuneration to the risk profile of the Bank. In its endeavour to do so, the Bank considers both quantitative measures and qualitative measures in the risk assessment process. Both quantitative measures and human judgement play a role in determining any risk adjustments. The risk assessment process encompasses the need to ensure that the remuneration policy as designed reduces employees' incentives to take excessive and undue risks, is symmetrical with risk outcomes, and delivers an appropriate mix of remuneration that is risk aligned.

The NRC considers whether the variable remuneration policy is in line with the Bank's risk profile, and ensures that through the Bank's ex-ante and ex-post risk assessment framework and processes, remuneration practices where potential future revenues whose timing and likelihood remain uncertain are carefully evaluated.

Risk adjustments take into account all types of risk, including intangible and other risks such as reputation risk, liquidity risk and the cost of capital. The Bank undertakes risk assessments to review financial and operational performance against business strategy and risk performance prior to distribution of the annual bonus. The Bank ensures that total variable remuneration does not limit its ability to strengthen its capital base. The extent to which capital needs to be built up is a function of the bank's current capital position and its ICAAP.

The bonus pool takes into account the performance of the Bank which is considered within the context of the Bank's risk management framework. This ensures that the variable pay pool is shaped by risk considerations and Bank-wide notable events.

The size of the variable remuneration pool and its allocation within the bank takes into account the full range of current and potential risks, including:

(a) The cost and quantity of capital required to support the risks taken;
(b) The cost and quantity of the liquidity risk assumed in the conduct of business; and
(c) Consistency with the timing and likelihood of potential future revenues incorporated into current earnings.

The NRC keeps itself abreast of the Bank's performance against the risk management framework. The NRC will use this information when considering remuneration to ensure returns, risks and remuneration are aligned.

REMUNERATION DISCLOSURES
CONTINUED

Risk adjustments

The Bank has an ex-post risk assessment framework which is a qualitative assessment to back-test actual performance against prior risk assumptions.

In years where the Bank suffers material losses in its financial performance, the risk adjustment framework will work as follows:

- There will be considerable contraction of the Bank's total variable remuneration.
- At an individual level, poor performance by the Bank will mean individual KPIs are not met and hence employee performance ratings will be lower.
- Reduction in the value of deferred shares or awards.
- Possible changes in vesting periods and additional deferral applied to unvested rewards.
- Lastly, if the qualitative and quantitative impact of a loss incident is considered significant, a malus or clawback of previous variable awards may be considered.

The NRC, with the Board's approval, can rationalise and make the following discretionary decisions:

- Increase / reduce the ex-post adjustment
- Consider additional deferrals or increase in the quantum of non-cash awards
- Recovery through malus and clawback arrangements

Malus and Clawback framework

The Bank's malus and clawback provisions allow the Board of Directors to determine that, if appropriate, unvested elements under the deferred bonus plan can be forfeited / adjusted or the delivered variable remuneration recovered in certain situations. The intention is to allow the Bank to respond appropriately if the performance factors on which reward decisions were based turn out not to reflect the corresponding performance in the longer term. All deferred compensation awards contain provisions that enable the Bank to reduce or cancel the awards of employees whose individual behaviour has had a materially detrimental impact on the Bank during the concerned performance year.

Any decision to take back an individual's award can only be made by the Bank's Board of Directors.

The Bank's malus and clawback provisions allow the Board to determine that, if appropriate, vested / unvested elements under the deferred bonus plan can be adjusted / cancelled in certain situations. These events include the following:

- Reasonable evidence of willful misbehaviour, material error, negligence or incompetence of the employee causing the Bank/ the employee's business unit to suffer material loss in its financial performance, material misstatement of the Bank's financial statements, material risk management failure or reputational loss or risk due to such employee's actions, negligence, misbehavior or incompetence during the concerned performance year.
- The employee deliberately misleads the market and/or shareholders in relation to the financial performance of the Bank during the concerned performance year.

Clawback can be used if the malus adjustment on the unvested portion is insufficient given the nature and magnitude of the issue.

Components of Variable remuneration

Variable remuneration has the following main components:

Upfront cash	The portion of the variable compensation that is awarded and paid out in cash on conclusion of the performance evaluation process for each year.
Deferred Cash	The portion of variable compensation that is awarded and paid in cash on a pro-rata basis over a period of 3 years.
Upfront share awards	The portion of variable compensation that is awarded and issued in the form of shares on conclusion of the performance evaluation process for each year.
Deferred shares	The portion of variable compensation that is awarded and paid in the form of shares on a pro-rata basis over a period of 3 years.

All deferred awards are subject to malus provisions. All share awards are released to the benefit of the employee after a six month retention period from the date of vesting. The number of equity share awards is linked to the Bank's share price as per the rules of the Bank's Share Incentive Scheme. Any dividend on these shares is released to the employee along with the shares (i.e. after the retention period).

Deferred compensation

The CEO, his deputies and 5 most highly paid business line employees are subject to the following deferral rules:

Element of variable remuneration	Payout percentages	Vesting period	Retention	Malus	Clawback
Up-front cash	40%	immediate	-	-	Yes
Deferred cash	10%	3 years	-	Yes	Yes
Deferred share awards	50%	3 years	6 months	Yes	Yes

All other covered staff, i.e. Assistant General Manager level and above are subject to the following deferral rules:

Element of variable remuneration	Payout percentages	Vesting period	Retention	Malus	Clawback
Up-front cash	50%	immediate	-	-	Yes
Up-front share awards	10%	immediate	6 months	Yes	Yes
Deferred share awards	40%	3 years	6 months	Yes	Yes

The NRC, based on its assessment of the role profile and risk taken by an employee could increase the coverage of employees that will be subject to deferral arrangements.

Details of remuneration paid

(a) Board of Directors

BD 000's	2014	2013
• Sitting Fees	**248,000**	186,463
• Remuneration	**368,688**	-

REMUNERATION DISCLOSURES
CONTINUED

(a) Employee remuneration

2014

BD 000's	Number of staff	Fixed remuneration		Sign on bonuses	Guaranteed bonuses	Variable remuneration					Total
						Upfront		Deferred			
		Cash	Others	(Cash / shares)	(Cash / shares)	Cash	Shares	Cash	Shares	Others	
Approved persons											
- Business lines	5	861*	-	-	-	50	-	13	63	-	987
- Control & support	7	569	-	-	-	41	5	-	22	-	637
Other material risk takers	-	-	-	-	-	-	-	-	-	-	-
Other staff	358	8,685	-	-	-	637	-	-	-	-	9,322
TOTAL	**370**	**10,115**	-	-	-	**728**	**5**	**13**	**85**	-	**10,946**

* Includes end of service compensations.

2013

BD 000's	Number of staff	Fixed remuneration		Sign on bonuses	Guaranteed bonuses	Variable remuneration					Total
						Upfront		Deferred			
		Cash	Others	(Cash / shares)	(Cash / shares)	Cash	Shares	Cash	Shares	Others	
Approved persons											
- Business lines	4	641	-	-	-	121	-	-	-	-	762
- Control & support	8	661	-	-	-	105	-	-	-	-	766
Other material risk takers	-	-	-	-	-	-	-	-	-	-	-
Other staff	380	7,866	-	-	-	529	-	-	-	-	8,395
TOTAL	392	9,168	-	-	-	755	-	-	-	-	9,923

CORPORATE SOCIAL RESPONSIBILITY REVIEW

Since inception, BisB has been committed to contributing to the economic development and social well-being of the Kingdom of Bahrain. Our comprehensive corporate social responsibility (CSR) programme underlines the importance that the Bank places on its role as a responsible and caring corporate citizen. Some of the key activities of the Bank's CSR programme during 2014 are listed below.

Industry Sponsorships

By sponsoring and participating in major financial industry conferences and events, and supporting other initiatives, BisB actively contributes to the development of the global Islamic banking industry and the banking sector in the Kingdom of Bahrain:

- 2014 AAOIFI-World Bank Annual Conference on Islamic Banking & Finance.
- 2014 World Islamic Banking Conference.
- 2014 Global Islamic Finance Directory.
- Various activities of the Bahrain Association of Banks.

Developing Bahraini nationals

BisB not only provides employment and career opportunities for Bahraini nationals, who comprise 97% of the Bank's total staff; but also encourages entrepreneurship and nurtures tomorrow's business leaders, by supporting the following initiatives:

- BIBF Waqf Fund for Islamic Banking Training and Development.
- Enterprise Finance Scheme For SMEs in collaboration with Tamkeen.
- Ministry of Education training initiatives.
- Summer Internship programme for Bahraini university students.
- Students' trips to underdeveloped countries.
- Youth conferences, workshops and camping activities.

Increasing the awareness of Islam

As a leading Sharia'a-compliant financial institution, BisB is committed to raising awareness of Islam through support for national institutions such as the following:

- Rekaaz Bahrain 2014.
- Hijab campaign 2014.
- Ministry of Justice & Islamic Affairs Zakat Fund.
- Quran Education Centres.
- Muslim Education Society.
- Discover Islam.
- The International Quran Reading Competition.

Improving the well-being of the local community

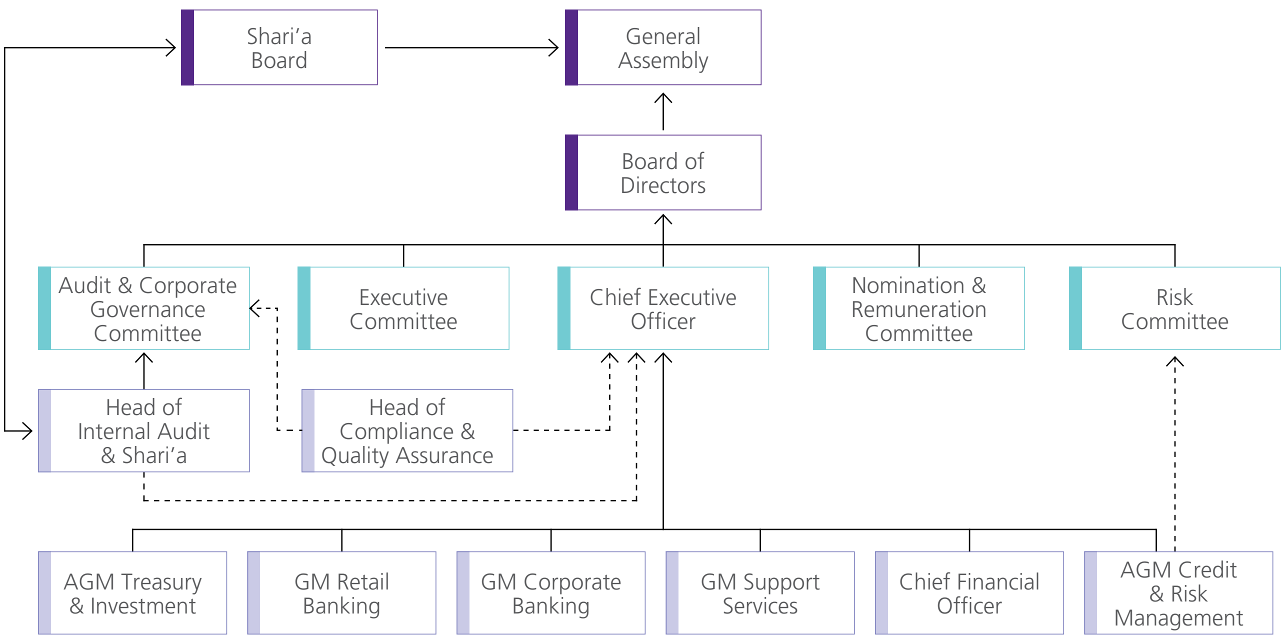
Through donations and other philanthropic activities, BisB contributes to improving the well-being and quality of life of the local community through:

- Support for a wide range of charitable, medical, educational, cultural, sporting and community organisations and events, including the Royal Charity Organisation.
- Financial assistance to needy families, individuals and deserving causes.

CORPORATE GOVERNANCE REVIEW

BisB is committed to upholding the highest standards of corporate governance, and the Central Bank of Bahrain's High-Levels Control Module (and its amendments). The Bank seeks to balance entrepreneurship, compliance and industry best practice, while creating value for all stakeholders. This includes, but is not limited to, conducting the policy and affairs of BisB in compliance with regulatory requirements. It also involves having the right checks and balances in place throughout the organisation to ensure that the right things are always done in the right way.

Governance and Organisation Structure



Developments in 2014

- Member of the Board of Directors, Dr. Sherif Elsayed Aly Ayoub, who represents the Islamic Development Bank (IDB), resigned from the Board following his appointment as Assistant Secretary General of the Islamic Financial Services Board.
- Mr. Mohammed Ebrahim Mohammed resigned as Chief Executive Officer.
- Mr. Mohammed Ahmed Janahi was appointed as Acting Chief Executive Officer.
- Mr. Mohammed Ahmed Janahi was promoted from General Manager - Support to Deputy CEO.
- Commenced implementation of the Bank's new five-year strategy developed in collaboration with the Boston Consulting Group, which was approved by the Board of Directors in April 2014.
- Appointed consultants to oversee compliance with the Foreign Account Tax Compliance Act (FATCA) according to the deadline set by the Central Bank of Bahrain (CBB).
- Complied with requirements of Sound Remuneration Policy issued by the CBB.
- Complied with requirements of the new Corporate Reference Bureau.
- Responded to the following CBB Consultation Papers:
  - Proposed Amendments on the Financial Crime (FC) Module for all Banks
  - New Client Assets Module (CL) for Volumes 1 and 2
  - Revised format for Prudential Information Reporting

Shareholder Ownership (5% and above)

Shareholder	Nationality	Number of Shares	Percentage
National Bank of Bahrain	Bahrain	241,838,206	25.74%
Islamic Development Bank	Saudi Arabia	165,804,485	17.64%
Social Insurance Organisation (Military Pension Fund)	Bahrain	121,113,559	12.89%
Social Insurance Organisation (GOSI)	Bahrain	121,019,103	12.88%
General Council of Kuwaiti Awqaf	Kuwait	67,946,033	7.23%

Shareholder Ownership (5% and above)

Country	Percentage	Number of Shares
Kingdom of Bahrain	68.38%	642,513,024
Kingdom of Saudi Arabia	18.53%	174,099,282
Kuwait	9.08%	85,278,340
United Arab Emirates	3.60%	33,793,459
Qatar	0.16%	1,527,003
Others	0.25%	2,462,391
Total	**100.000%**	**939,673,499**

Shareholder Ownership (5% and above)

Directors	Shares as of 31st Dec 2014
Abdul Razak Abdulla Al Qassim	100,000
Khalid Mohamed Al Mannai	No Shares transferred as of December 2014
Mohammed Ahmed Abdulla	No Shares transferred as of December 2014
Fatima Abdulla Budhaish	100,000
Talal Ali Al Zain	No Shares transferred as of December 2014
Khalil Ebrahim Nooruddin	No Shares transferred as of December 2014
Ebrahim Hussain AlJasmi	100,000
Othman Ebrahim Al Askar	100,000
Shari'a Members	
Shaikh Dr. Abdul Latif Mahmood Al Mahmood	185,492
Shaikh Nedham Mohamed Saleh Yacoubi	14,320
Senior Management	
Mohammed Ebrahim Mohammed*	100,000

* CEO, Mohammed Ebrahim Mohammed resigned on 31st August 2014.

Board of Directors

Role and Responsibilities of the Board

The primary responsibility of the Board of Directors is to provide effective governance over the Bank's affairs for the benefit of the shareholders; and to balance the interests of BisB's diverse constituencies, including associated concerns, employees and other stakeholders. In all actions taken by the Board, the Directors are expected to exercise their business judgement in what they reasonably believe to be in the best interests of the Bank.

The Board approves and oversees the implementation of the Bank's strategies; and reviews and approves the Bank's strategic plan. As part of its strategic review process, the Board reviews major plans of action and business plans; sets performance objectives; and oversees major investments, divestitures and acquisitions. Every year, at an annual Board strategy session, the Board formally reassesses the Bank's objectives, strategies and plans. The Board's responsibilities are described in more detail in the Corporate Governance Report published on the Bank's website, and in the Charter of the Board of Directors.

Board Composition

The Board of Directors of BisB comprises nine Executive and Non-Executive Directors, of which four are Independent Directors. Each term of the Board of Directors consists of three years. The last re-election of the Bank's Board of Directors was held at the Bank's Annual General Meeting (AGM) on 7 July 2013. Profiles of Board Members are listed on page 9 of this annual report.

1. Mr. Abdul Razaq Abdulla Al-Qassim - Chairman
2. Brig. Khalid Mohamed Al-Mannai - Vice Chairman
3. Mr. Talal Ali Al Zain - Member
4. Mr. Khalil Ebrahim Nooruddin - Member
5. Mr. Ebrahim Husain Ebrahim Al Jassmi - Member
6. Mr. Othman Ibrahim Al-Askar - Member
7. Mr. Mohammed Ahmed Abdulla - Member
8. Mrs. Fatima Abdulla Budhaish - Member
9. Dr. Sherif Ayoub (Resigned: 8 October 2014)

CORPORATE GOVERNANCE REVIEW
CONTINUED

Induction of new directors

The Board-approved Corporate Governance Policy requires each new Director to receive a formal and tailored induction from the Chairman and Senior Management, with respect to BisB's vision and strategic direction; core values including ethics; corporate governance practices; and financial matters and business operations.

Board Committees

The Board has constituted four Committees - Executive Committee, Audit Committee, Remuneration & Nomination Committee, and Risk Management Committee. Each of these committees has its own Charter that describes the responsibilities of its members.

Board Committees - Membership and Objectives

Board Committee	Members	Objectives
Executive Committee	Khalid Mohammed Al-Mannai (Chairman) Fatima Abdulla Budhaish Khalil Ebrahim Nooruddin (Previously, BisB's CEO - Mohammed Ebrahim Mohammed, was a non-voting member until 1 September 2014)	Review of strategy and performance. Review of new investment proposals, credit proposals and exit strategies. The committee meets six times per year.
Audit Committee (including Corporate Governance Committee responsibilities)	Ebrahim Hussain Al Jassmi (Chairman) Othman Ebrahim Al-Askar Dr. Sherif Ayoub	Oversight of integrity and reporting of the Bank's quarterly and annual financial statements. Review of risk, provision and impairment. Compliance with legal and regulatory requirements. The committee meets four times per year.
Nomination and Remuneration Committee	Abdul Razaq Abdulla Al-Qassim (Chairman) Khalid Mohammed Al-Mannai Mohammed Ahmed Abdulla	Oversight of the compensation and remuneration policy. Oversight of recruitment and promotion of key personnel and Board members The committee meets two times per year.
Risk Management Committee	Talal Ali Al Zain (Chairman) Fatima Abdulla Budhaish Mohammed Ahmed Abdulla	Monitoring the enterprise-wide risk profile independently. Risk guidance to the Board and Management periodically. The committee meets four times per year.

Evaluation of the Board and its Committees

The Nomination and Remuneration Committee carried out an evaluation of the Board and its Committees through the distribution of questionnaires to each Board Member, followed by an assessment of the Committees and Members. The Committee expressed its satisfaction with the positive results.

Directors' Remuneration

The aggregate Board sitting fees, including travel expenses, totalled BD 248,000 in 2014.

Directors' Attendance

The Board of Directors met eight times during 2014, details of which are given in the following table. This exceeds the minimum requirement of having at least four meetings in any given year, as stipulated by the Central Bank of Bahrain. The regulatory requirement that individual Board Members must attend at least 75% of all Board meetings in a given financial year to enable the Board to discharge its responsibilities effectively, was met by all Directors during 2014. The table also shows attendance of Directors at Board Committee meetings.

Directors' Attendance of Board Meetings - January to December 2014

Members	12 Jan	3 Feb	24 Mar	11 May	17 Jun	9 Jul	11 Aug	28 Oct
Abdul Razaq Al-Qassim (Joined 05 June 2013)	✓	✓	✓	✓	✓	X	✓	✓
Khalid Al-Mannai (Joined 11 June 2013)	✓	X	✓	✓	✓	✓	✓	✓
Fatima Budhaish (Joined 05 June 2013)	✓	✓	✓	✓	✓	✓	✓	✓
Mohammed Abdulla (Joined 11 June 2013)	✓	✓	✓	✓	✓	✓	✓	✓
Talal Al Zain (Joined 07 July 2013)	✓	✓	✓	✓	X	✓	✓	X
Khalil Nooruddin (Joined 07 July 2013)	✓	✓	✓	✓	✓	✓	✓	✓
Ebrahim Hussain Al Jassmi (Joined 07 July 2013)	X	✓	✓	✓	✓	✓	✓	✓
Othman Al-Askar (Joined 07 July 2013)	✓	✓	✓	✓	X	✓	X	✓
Dr. Sherif Ayoub (Resigned 08 Oct 2014)	X	X	✓	✓	✓	✓	✓	X

Sharia'a Supervisory Board

The Sharia'a Supervisory Board of BisB comprises five eminent and highly-experienced Sharia'a scholars. The Board's main responsibility is to advise the Bank's business units on any Sharia'a-related matters, and to ensure compliance with the tenets and requirements of Islamic Sharia'a in their operations. The Sharia'a Supervisory Board is also entrusted with the duty of directing, reviewing and supervising the activities of the Bank in order to ensure full compliance by BisB with Sharia'a rules and AAOIFI standards. Profiles of Sharia'a Supervisory Board Members are listed on page 11 of this annual report.

Rev. Shaikh Dr. Abdul Latif Mahmood Al Mahmood - Chairman

Rev. Shaikh Mohammed Jaffar Al Juffairi - Vice Chairman

Rev. Shaikh Adnan Abdullah Al Qattan - Member

Rev. Shaikh Dr. Nedham Mohammed Saleh Yacoubi - Member

Rev. Shaikh Dr. Essam Khalaf Al Enizi - Member

Sharia'a Supervisory Board - Membership and Attendance 2014

Members	23 Feb	11 May	7 Sep	30 Nov
Sh. Dr. Abdulatif Al-Mahmood (Chairman)	✓	✓	✓	✓
Sh. Moh'd Al-Jufairi	✓	✓	X	X
Sh. Adnan Al-Qattan	X	✓	✓	✓
Sh. Dr. Nidham Yacoubi	✓	✓	✓	✓
Sh. Dr. Esam Al-Enizi	✓	✓	✓	✓

CORPORATE GOVERNANCE REVIEW
CONTINUED

Executive Management

The Executive Management of BisB is headed by the Acting Chief Executive Officer, who is responsible for the day-to-day conduct of the Bank's business in line with policies and procedures approved by the Board of Directors. The Acting CEO is assisted by a highly-qualified and experienced Management Team, whose profiles are listed on page 15 of this annual report.

1. Mr. Mohammed Ahmed Janahi: Deputy Chief Executive Officer & Acting CEO
2. Mr. Abdulrahman Mohammed Turki: General Manager - Retail Banking
3. Mr. Yousuf M A Karim: General Manager - Corporate Banking
4. Mr. Khalid Mohammed Al Dossari: Chief Financial Officer
5. Mr. Khalid Mahmoud Abdulla: Head of Internal Audit
6. Dr. Mohammed S. Belgami: Head of Credit and Risk Management

Performance-Linked Management Incentive Structure

BisB implements a Performance Management Scheme, which is linked to incentives and competencies on an annual basis, for management and staff. The Bank pays monthly salaries, allowances and bonuses for the Chief Executive, General Managers, Senior Managers and Managers.

Senior Management Remuneration

The aggregate Senior Management remuneration, including basic salaries and fixed allowances was BD 825,000 for 2014.

Management Committees

A number of Management Committees have been established to assist the CEO and Management Team in carrying out their duties, and to ensure that there is adequate supervision of the Bank's activities.

Management Committees - Membership & Objectives

Committee	Members	Objectives
Asset & Liability Committee (ALCO)	Mohammed Ahmed Hasan Janahi (Chairman*) A. Rahman Turki Yusuf Abdul Kareem Dr. Mohammed Belgami Khalid Al Dossari Nader Al Bastaki Sameer Qaedi (*Previous Chairman was Mohammed Ebrahim Mohammed until 1 September 2014)	To manage and monitor the liquidity risk of the Bank on a coordinated and consistent basis.
Credit & Investment Committee (C&IC)	Mohammed Ahmed Hasan Janahi (Chairman*) A. Rahman Turki Yusuf Abdul Kareem Nader Al Bastaki Dr. Mohammed Belgami (*Previous Chairman was Mohammed Ebrahim Mohammed until 1 September 2014)	To exercise due care, diligence and skill to oversee, direct and review the management of credit risk within the financing portfolio of the Bank, and review policies and strategies for achieving investment objectives.
Information Technology Steering Committee	Mohammed Ahmed Hasan Janahi (Chairman*) Khalid Al Dossari A. Rahman Turki Dr. Mohammed Belgami Khalid Mahmood (*Previous Chairman was Mohammed Ebrahim Mohammed until 1 September 2014)	To plan, prepare, coordinate, implement, support and follow up on all issues related to IT and new projects implementation issues.
Human Resource Committee (HR)	Mohammed Ahmed Hasan Janahi (Chairman*) Khalid Al Dossari A. Rahman Turki Yusuf Abdul Kareem Dr. Mohammed Belgami Khalid Mahmood Nader Al Bastaki (*Previous Chairman was Mohammed Ebrahim Mohammed until 1 September 2014)	To monitor and assess the workforce regarding human resources issues, and monitor, review and analyse legislative and/or administrative changes related to human resources.

Committee	Members	Objectives
Qard Al Hassan, Donation & Zakah Committee	Mohammed Ahmed Janahi (Chairman*) Hamad Farooq Al Shaikh Khalid Waheeb Al Nasser Ali Hassan Duaij (*Previous Chairman was Mohammed Ebrahim Mohammed until 1 September 2014)	To discharge the Bank's social responsibilities toward society through distributing Zakah, charity funds, donations and good faith Qard for marriage, medical treatments, etc.
Provisioning Committee	Mohammed Ahmed Janahi (Chairman*) Dr. Mohammed Belgami Khalid Al Dossari Srinivas Nallamothu Khalid Mahmood (Observer) (*Previous Chairman was Mohammed Ebrahim Mohammed until 1 September 2014)	To assist the CEO in reviewing the Bank's provisions. Also responsible for formulating provision policies with a view to maintain the strategic risk levels objectives of the Bank.

Succession Planning

In compliance with CBB requirements, the Nomination & Remuneration Committee reviews and endorses the Bank's succession plan on an annual basis. The objective of the plan is to identify, develop and promote personnel to ensure that there are no disruptions to the functioning of the Bank, in an event that key personnel choose to leave BisB.

Compliance

In accordance with CBB guidelines, the Bank has a designated Head of Compliance, who is independent and reports directly to the Board of Directors; and has direct access to Senior Management and all confidential information of the Bank. The Compliance function acts as the central coordinator for all regulatory matters relating to the CBB, Bahrain Bourse, and other regulatory bodies. BisB has in place comprehensive policies and procedures to ensure full compliance with the relevant rules and regulations of the Central Bank of Bahrain, including appropriate anti-money laundering policies.

Anti-Money Laundering

BisB has a designated Money Laundering Reporting Officer (MLRO). The Bank has implemented an anti-money laundering and terrorism financing policy, and periodically trains its staff on the identification and reporting of suspicious transactions. BisB follows prudent practices related to 'Customer Due Diligence', 'Beneficial Ownership' and 'Know Your Customer' principles. In accordance with CBB requirements, the MLRO regularly reviews the effectiveness of the Bank's AML/CFT procedures, systems and controls.

Customer Complaints

The Complaints Resolution Unit of the Quality Assurance Department is responsible for managing customer complaints. After receiving a complaint, the Unit routes it to the concerned department for their response. After analysing the response, the customer is contacted accordingly. BisB customers may use the Bank's website or the call centre for lodging a complaint. All complaints are logged and monitored, and reported to the CBB.

Code of Conduct

BisB conducts itself in accordance with the highest standards of ethical behaviour. A Code of Business Conduct has been developed to govern the personal and professional conduct of all stakeholders The Code applies to directors, management, staff and temporary workers; and independent contractors and consultants, whether engaged by or otherwise representing the Bank and its interests.

Disclosure and Communications

BisB conducts all communications with its stakeholders in a professional, honest, transparent, understandable, accurate and timely manner. Main communications channels include an annual report, corporate brochure and website, and regular announcements in the appropriate local media. As part of its disclosure and communication strategy, the Bank's website (www.bisb.com) is the repository of financial information, together with Board of Directors' reports and financial commentary, financial statements, relevant information on BisB such as its key products and services, and press releases.

Note: Additional information is included in the BisB Corporate Governance report 2014, which is posted on the Bank's website: www.bisb.com.

FINANCIAL RESULTS REFLECT SUCCESS OF NEW STRATEGY

THE EXCELLENT FINANCIAL PERFORMANCE BY BAHRAIN ISLAMIC BANK IN 2014, WHICH SAW NET PROFIT INCREASE BY 52% OVER THE PREVIOUS YEAR, REFLECTS THE SUCCESSFUL IMPLEMENTATION OF ITS NEW STRATEGIC FOCUS ON GROWING CORE ACTIVITIES AND DISPOSING OF NON-PERFORMING INVESTMENT ASSETS. THE BANK RELIED FULLY ON REVENUES AND FEES FROM FINANCING AND MAJOR ACTIVITIES, WHICH WERE RESPONSIBLE FOR GENERATING 82% OF OPERATING REVENUES. THESE WERE FREE FROM REVALUATIONS OR UNEARNED PROFITS, WITH THE EXCEPTION OF THE SUCCESSFUL EXITS FROM SOME INVESTMENT PORTFOLIOS AND LISTED EQUITIES, WHICH REALISED A NET GAIN OF BD 7 MILLION.

SHARIA'A SUPERVISORY BOARD REPORT

For the year ended 31st December 2014

In The Name of Allah, most Gracious, most Merciful, Peace and Blessings Be Upon His Messenger.

To the shareholders of Bahrain Islamic Bank B.S.C.

Assalam Alaykum Wa Rahmatu Allah Wa Barakatoh.

In accordance to Articles of Association and the entrustment of the Sharia'a Board with supervising the Bank's activities from a Sharia perspective, we hereby submit the following report:

The Sharia'a Supervisory Board monitored the operations, related to the Bank throughout the year ended on 31st December 2014 to express opinion on the Bank's adherence to the provisions and principles of Islamic Sharia'a in its activities by following the guidelines and decisions issued by the Sharia'a Supervisory Board. The Sharia'a Supervisory Board believes that ensuring the conformity of its activities and investments with the provisions of Islamic Sharia'a is the sole responsibility of the Bank's Management while the Sharia'a Supervisory Board is only responsible for expressing an independent opinion and preparing a report thereabout.

The Sharia'a Supervisory Board's monitoring function included the checking and documentation of the procedures to scrutinize each operation carried out by the Bank, whether directly or through the Sharia'a Internal Audit department. We planned with the Sharia'a Internal Audit department to carry out monitoring functions by obtaining all the information and clarifications that were deemed necessary to confirm that the Bank did not violate the principles and provisions of Islamic Sharia'a. The Sharia'a Internal Audit department executed its mission of auditing the transactions and submitted its periodic reports to the Sharia'a Supervisory Board, which confirmed the Bank's commitment and conformity to the Sharia'a Supervisory Board's opinions.

The Sharia'a Supervisory Board obtained data and clarifications it deemed necessary to confirm that the Bank did not violate the Sharia'a principles and provisions of Islamic Sharia'a. The Sharia'a Board held a number of meetings during the year and replied to inquiries, in addition to approving a number of new products presented by the Management. The Sharia'a Supervisory Board discussed with the Bank's officials all transactions carried out by the Management throughout the year and reviewed the Bank's conformity with the provisions and principles of Islamic Sharia'a as well as the resolutions and guidelines of the Sharia'a Supervisory Board.

The Sharia'a Board reviewed the financial Statements for the year ended on 31st December 2014 with the notes and income statement and the Zakat calculation methods.

The Sharia'a Supervisory Board believes that:

1. Contracts, and transactions conducted by the Bank throughout the year ended on 31st December 2014 were in accordance with the standard contracts pre-approved by the Sharia'a Supervisory Board.
2. The distribution of profit on investment accounts was in line with the basis and principles approved by the Sharia'a Supervisory Board.
3. Any gains resulted from sources or means prohibited by the provisions and principles of Islamic Sharia'a, have been directed to the Charity and Donations Account according to SSB's resolution.
4. Zakah was calculated according to the provisions and principles of Islamic Sharia'a. The shareholders should pay their portion of Zakah on their shares as stated in the financial report.
5. The Bank was committed to the Sharia'a standards issued by the Accounting & Auditing Organization for Islamic Financial Institutions (AAOIFI).

We pray that Allah may grant all of us further success and prosperity.

Shaikh Dr. Abdul Latif Mahmood Al Mahmood
Chairman

Shaikh Mohammed Jaffer Al Juffairi
Vice Chairman

Shaikh Adnan Abdulla Al Qattan
Board Member

Shaikh Nedham Mohamed Saleh Yacoubi
Board Member

Rev. Shaikh Dr. Essam Khalaf Al Onazi
Board Member

FINANCIAL STATEMENTS 2014

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INDEPENDENT AUDITORS' REPORT

to the Shareholders of Bahrain Islamic Bank B.S.C.

Report on the consolidated financial statements

We have audited the accompanying consolidated financial statements of Bahrain Islamic Bank B.S.C. (the "Bank") and its subsidiaries (together the "Group") which comprise the consolidated statement of financial position as at 31 December 2014, the consolidated statements of income, cash flows, changes in owners' equity, sources and uses of good faith qard fund and sources and uses of zakah and charity fund for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Respective responsibilities of board of directors and auditors

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 board of directors of the Bank. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

Basis of opinion

We conducted our audit in accordance with Auditing Standards for Islamic Financial Institutions issued by Accounting and Auditing Organisation 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 includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

Opinion

In our opinion, the consolidated financial statements give a true and fair view of the consolidated financial position of the Group as at 31 December 2014, and of its consolidated results of operations, its consolidated cash flows, its consolidated changes in owners' equity, its consolidated sources and uses of good faith qard fund, and its consolidated sources and uses of zakah and charity fund for the year then ended in accordance with Financial Accounting Standards issued by the Accounting and Auditing Organisation for Islamic Financial Institutions and the Shari'a rules and principles as determined by the Shari'a Supervisory Board of the Bank.

Report on other regulatory requirements

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

a) the Bank has maintained proper accounting records and the consolidated financial statements are in agreement therewith;
b) the financial information contained in the chairman's statement is consistent with the consolidated financial statements;
c) we are not aware of any violations during the year of the Bahrain Commercial Companies Law, the Central Bank of Bahrain and Financial Institutions Law, the CBB Rule Book (Volume 2 and applicable provisions of Volume 6 and CBB directives), the CBB Capital Markets Regulations and associated resolutions, the Bahrain Bourse rules and procedures or the terms of the Bank's memorandum and articles of association that would have had a material adverse effect on the business of the Bank or on its financial position; and
d) satisfactory explanations and information have been provided to us by management in response to all our requests.

Other matter

The financial statements of the Group as at and for the year ended 31 December 2013 were audited by another auditor whose audit report dated 3 February 2014 expressed an unqualified opinion on those financial statements and a modified conclusion on regulatory matters.

KPMG Fakhro
Partner Registration No. 100
11 February 2015

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

For the year ended 31 December 2014

	Note	2014 BD'000	2013 BD'000
ASSETS			
Cash and balances with banks and Central Bank	3	**52,118**	50,831
Placements with financial institutions	4	**68,567**	184,600
Financing assets	5	**408,021**	346,805
Investments securities	6	**123,561**	107,026
Ijarah Muntahia Bittamleek	8	**102,277**	90,356
Ijarah rental receivables	8	**14,065**	14,924
Investment in associates	7	**30,835**	36,236
Investment in real estate	10	**53,934**	58,219
Property and equipment	9	**17,101**	17,067
Other assets	11	**4,728**	4,230
TOTAL ASSETS		**875,207**	910,294
LIABILITIES, EQUITY OF INVESTMENT ACCOUNTHOLDERS AND OWNERS' EQUITY			
Liabilities			
Placements from financial institutions		**75,570**	95,144
Customers' current accounts		**137,423**	105,932
Other liabilities	12	**16,518**	13,608
Total Liabilities		**229,511**	214,684
EQUITY OF INVESTMENT ACCOUNTHOLDERS	13	**566,601**	617,494
Owners' Equity			
Share capital	14	**93,967**	93,967
Treasury shares	14	**(563)**	(563)
Reserves		**(14,320)**	(16,530)
Attributable to equity holders of the parent		**79,084**	76,874
Non-controlling interest		**11**	1,242
Total Owners' Equity		**79,095**	78,116
TOTAL LIABILITIES, EQUITY OF INVESTMENT ACCOUNTHOLDERS AND OWNERS' EQUITY		**875,207**	910,294
COMMITMENTS AND CONTINGENT LIABILITIES	15	**22,277**	15,991

The consolidated financial statements, which consist of pages 44 to 79, were approved by the Board of Directors on 11 February 2015 and signed on its behalf by:

Abdulrazaq Al Qassim	**Khalid Al Mannai**	**Mohammed Janahi**
Chairman	Vice Chairman	Acting Chief Executive Officer

The attached notes 1 to 32 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF INCOME

For the year ended 31 December 2014

	Note	2014 BD'000	2013 BD'000
INCOME			
Income from financing	17	**28,702**	32,504
Income from investment in Sukuk		**2,535**	4,921
		31,237	37,425
Less: Return on equity of investment accountholders	13.4	**(7,287)**	(10,860)
		23,950	26,565
Expense on placements from financial institutions		**(252)**	(264)
Fee and commission income		**6,452**	5,307
Income from investments	18	**4,410**	2,918
Income from investment in real estate	19	**8,568**	(807)
Share of results of associates	7	**(1,550)**	1,197
Net gain from foreign currencies		**1,273**	694
Total net income		**42,851**	35,610
EXPENSES			
Staff costs		**11,482**	10,013
Depreciation	9	**1,641**	1,644
Other expenses	20	**8,502**	8,080
Total expenses		**21,625**	19,737
Profit before impairment allowances		**21,226**	15,873
Impairment provisions on financing assets	21.1	**(7,593)**	(5,275)
Impairment provisions on investments	21.2	**(4,336)**	(5,411)
Impairment provisions on other assets	21.3	**-**	920
PROFIT FOR THE YEAR		**9,297**	6,107
BASIC AND DILUTED EARNINGS PER SHARE (fils)	23	**9.93**	6.52

Abdulrazaq Al Qassim
Chairman

Khalid Al Mannai
Vice Chairman

Mohammed Janahi
Acting Chief Executive Officer

The attached notes 1 to 32 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended 31 December 2014

	Note	2014 BD'000	2013 BD'000
OPERATING ACTIVITIES			
Profit for the year		**9,297**	6,107
Adjustments for non-cash items:			
Depreciation		**1,641**	1,644
Impairment provisions on financing assets	21.1	**7,593**	5,275
Impairment provisions on investments	21.2	**4,336**	5,411
Impairment provisions on other assets	21.3	**-**	(920)
Reversal of impairment / (Charge) on investment in real estates	19	**(3,617)**	1,321
Gain on sale of equity type instruments carried at fair value through equity	18	**(1,946)**	(995)
Gain on sale of investment in real estates	19	**(4,951)**	(514)
Share of results of associates	7	**1,550**	(1,197)
Unrealised gain on equity type instruments carried at fair value through statement of income	18	**-**	(55)
Dividends from investment in associates		**(70)**	-
Operating profit before changes in operating assets and liabilities		**13,833**	16,077
Working capital adjustments:			
Mandatory reserve with Central Bank of Bahrain		**1,685**	(4,485)
Financing assets		**(64,808)**	(27,389)
Ijarah Muntahia Bittamleek		**(15,021)**	1,393
Other assets		**(498)**	1,273
Customers' current accounts		**31,491**	18,800
Other liabilities		**2,911**	(1,031)
Placements from financial institutions		**(19,574)**	7,454
Customers' investment accounts		**(50,893)**	43,924
Net cash (used in) / from operating activities		**(100,874)**	56,016
INVESTING ACTIVITIES			
Disposal of investment in real estate	10	**7,799**	5,348
Dividends from investment in associates		**70**	-
Purchase of investments		**(50,229)**	(37,084)
Purchase of property and equipment		**(1,715)**	(3,181)
Disposal of property and equipment		**40**	-
Proceeds from disposal of investments		**31,849**	37,254
Net cash (used in) / from investing activities		**(12,186)**	2,337
FINANCING ACTIVITIES			
Dividends paid		**(1)**	(10)
Net cash used in financing activities		**(1)**	(10)
NET CHANGE IN CASH AND CASH EQUIVALENTS		**(113,061)**	58,343
Cash and cash equivalents at 1 January		**202,691**	144,348
CASH AND CASH EQUIVALENTS AT 31 DECEMBER		**89,630**	202,691
Cash and cash equivalents at year end comprise of:			
Cash on hand	3	**9,048**	7,750
Balances with CBB, excluding mandatory reserve deposits	3	**4,295**	2,926
Balances with banks and other financial institutions	3	**7,720**	7,415
Placements with financial institutions with original maturities less than 90 days	4	**68,567**	184,600
		89,630	202,691

The attached notes 1 to 32 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN OWNERS' EQUITY

For the year ended 31 December 2014

			Reserves								
	Share capital BD'000	**Treasury shares BD'000**	**Statutory reserve BD'000**	**General reserve BD'000**	**Real estate fair value reserve BD'000**	**Investments fair value reserve BD'000**	**Accumulated losses BD'000**	**Total reserves BD'000**	**Equity attributable to equity holders of the parent BD'000**	**Non-controlling interest BD'000**	**Total owners equity BD'000**
Balance at 1 January 2014	93,967	(563)	10,879	1,000	11,301	4,248	(43,958)	(16,530)	76,874	1,242	78,116
Profit for the year	-	-	-	-	-	-	9,297	9,297	9,297	-	9,297
Net movement in investments fair value reserve	-	-	-	-	-	(3,147)	-	(3,147)	(3,147)	-	(3,147)
Net movement in real estate fair value reserve	-	-	-	-	(3,940)	-	-	(3,940)	(3,940)	-	(3,940)
Transfer of profit to statutory reserve	-	-	930	-	-	-	(930)	-	-	-	-
Net movement in non-controlling interest	-	-	-	-	-	-	-	-	-	(1,231)	(1,231)
Balance at 31 December 2014	**93,967**	**(563)**	**11,809**	**1,000**	**7,361**	**1,101**	**(35,591)**	**(14,320)**	**79,084**	**11**	**79,095**
Balance at 1 January 2013	93,967	(563)	10,268	1,000	-	1,286	(36,195)	(23,641)	69,763	-	69,763
Changes due to adoption of FAS 26	-	-	-	-	13,259	-	(13,259)	-	-	-	-
As at 1 January 2013 (restated)	93,967	(563)	10,268	1,000	13,259	1,286	(49,454)	(23,641)	69,763	-	69,763
Profit for the year	-	-	-	-	-	-	6,107	6,107	6,107	-	6,107
Net movement in investments fair value reserve	-	-	-	-	-	2,962	-	2,962	2,962	-	2,962
Net movement in real estate fair value reserve	-	-	-	-	(1,958)	-	-	(1,958)	(1,958)	-	(1,958)
Transfer of profit to statutory reserve	-	-	611	-	-	-	(611)	-	-	-	-
Net movement in non-controlling interest	-	-	-	-	-	-	-	-	-	1,242	1,242
Balance at 31 December 2013	93,967	(563)	10,879	1,000	11,301	4,248	(43,958)	(16,530)	76,874	1,242	78,116

The attached notes 1 to 32 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF SOURCES AND USES OF GOOD FAITH QARD FUND

For the year ended 31 December 2014

	Qard Hasan receivables BD'000	Funds available for Qard Hasan BD'000	Total BD'000
Balance at 1 January 2014	**79**	**49**	**128**
Uses of Qard fund			
Marriage	**22**	**(22)**	**-**
Others (Waqf)	**3**	**(3)**	**-**
Total uses during the year	**25**	**(25)**	**-**
Repayments	**(24)**	**24**	**-**
Balance at 31 December 2014	**80**	**48**	**128**
Balance at 1 January 2013	15	113	128
Uses of Qard fund			
Marriage	26	(26)	-
Others (Waqf)	63	(63)	-
Total uses during the year	89	(89)	-
Repayments	(25)	25	-
Balance at 31 December 2013	79	49	128

	2014	2013
	BD'000	BD'000
Sources of Qard fund		
Contribution by the Bank	**125**	125
Donation	**3**	3
	128	128

The attached notes 1 to 32 form part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF SOURCES AND USES OF ZAKAH AND CHARITY FUND

For the year ended 31 December 2014

	2014 BD'000	2013 BD'000
SOURCES OF ZAKAH AND CHARITY FUNDS		
Undistributed zakah and charity funds at the beginning of the year	**225**	58
Non-Islamic income / late fee	**659**	687
Donations	**150**	150
Total sources of zakah and charity funds during the year	**1,034**	895
USES OF ZAKAH AND CHARITY FUNDS		
Philanthropic societies	**441**	300
Aid to needy families	**311**	370
Total uses of funds during the year	**752**	670
Undistributed zakah and charity funds at the end of the year	**282**	225

The attached notes 1 to 32 form part of these consolidated financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL INFORMATION

31 December 2014

1 INCORPORATION AND ACTIVITIES

Bahrain Islamic Bank B.S.C. (the "Bank") was incorporated in the Kingdom of Bahrain in 1979 by Amiri Decree No.2 of 1979 and registered with the Ministry of Industry and Commerce ("MOIC") under Commercial Registration (CR) number 9900, to carry out banking and other financial trading activities in accordance with the teachings of Islam (Shari'a). The Bank is licensed and regulated by the Central Bank of Bahrain ("CBB") and has a retail banking license. The Bank's Shari'a Supervisory Board is entrusted to ensure the Bank's adherence to Shari'a rules and principles in its transactions and activities. The Bank is listed on the Bahrain Bourse.

The Bank's registered office is at Building 722, Road 1708, Block 317, Manama, Kingdom of Bahrain.

The Bank has eleven branches (2013: fifteen), all operating in the Kingdom of Bahrain.

The consolidated financial statements include the financial statements of the Bank and its subsidiaries (together the "Group"). The Bank holds 100% of the share capital of both Abaad Real Estate Company B.S.C. (c) and BisB MMF Company B.S.C. (c), and 99.7% subscription of BisB Money Market Fund.

Abaad Real Estate Company B.S.C. (c) ("Abaad")

Abaad was incorporated in the Kingdom of Bahrain on 8 April 2003 with an authorised and fully paid-up share capital of BD 25 million. Abaad has started operations during the year 2007. The main activities of Abaad are the management and development of real estate (in accordance with the Islamic Shari'a rules and principles).

BisB MMF Company B.S.C. (c) ("MMF")

MMF was incorporated in the Kingdom of Bahrain as a closed joint stock company and registered with the Ministry of Industry and Commerce under Commercial Registration (CR) number 81322-1. The postal address of the Company is registered at, Building 722, Road 1708, Block 317, Diplomatic Area, Kingdom of Bahrain. The purpose of the MMF is limited to establishing funds (in accordance with the Islamic Shari'a rules and principles).

BisB Money Market Fund ("Fund")

Fund is an open ended investment fund constituted by an instrument dated 12 June 2012 and commenced its activities on 9 July 2012. The fund is a Bahrain domiciled Shari'a compliant retail collective investment scheme established by Bahrain Islamic Bank B.S.C. pursuant to the Central Bank of Bahrain regulations and directives as contained in the rulebook volume 7. The fund has been established by BisB MMF Company B.S.C. (c).

The consolidated financial statements were authorised for issue in accordance with a resolution of the Board of Directors issued on 11 February 2015.

2 SIGNIFICANT ACCOUNTING POLICIES

The significant accounting polices applied in the preparation of these consolidated financial statements are set out below. These accounting policies have been consistently applied by the Group and are consistent with those used in the previous year, except for those changes arising from revised/new AAOIFI financial accounting standards.

a. New standards, amendments, and interpretations effective from 1 January 2014:

There are no new AAOIFI accounting standards, amendments to standards and interpretations that are effective for the first time for the financial year beginning on or after 1 January 2014 that would be expected to have a material impact on the Group.

New standards, amendments and interpretations issued but not effective

The following new standards, amendments to standards and interpretations are effective for annual periods beginning on or after 1 January 2015 and are expected to be relevant to the Group.

FAS 27 – Investments Accounts

FAS 27 Investments accounts was issued in December 2014 replacing FAS 5 – 'Disclosures of Bases for Profit Allocation between Owner's Equity and Investment Account Holders' and FAS 6 – 'Equity of Investment Account Holders and their Equivalent'. This standard is effective for financial periods beginning 1 January 2016. The adoption of this standard would not have any significant impact on the financial statements of the Group.

The Bank has not early adopted any new standards during 2014.

NOTES TO THE CONSOLIDATED FINANCIAL INFORMATION

31 December 2014

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

b. Statement of Compliance

The consolidated financial statements are prepared in accordance with the Financial Accounting Standards issued by the Accounting and Auditing Organisation for Islamic Financial Institutions ("AAOIFI"), the Shari'a Rules and Principles as determined by the Shari'a Supervisory Board of the Group, the Bahrain Commercial Companies Law, the Central Bank of Bahrain and Financial Institutions Law and the CBB Rule Book (Volume 2, applicable provisions of Volume 6, and CBB directives), regulations and associated resolutions, rules and procedures of the Bahrain Bourse or the terms of the Bank's memorandum and articles of association in accordance with the requirements of AAOIFI, for matters for which no AAOIFI standard exists, the Group uses the relevant International Financial Reporting Standards ("IFRS") issued by International Accounting Standards Board.

c. Basis of preparation

The consolidated financial statements have been prepared on a historical cost basis, except for "investment in real estate", "equity type instruments carried at fair value through equity" and "equity type instruments carried at fair value through statement of income" that have been measured at fair value.

The preparation of consolidated financial statements requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. Estimates and underlying assumptions are reviewed on an on-going basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected. Management believes that the underlying assumptions are appropriate and the Group's consolidated financial statements therefore present the financial position and results fairly. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements, are disclosed in note 2 dd.

The consolidated financial statements have been presented in Bahraini Dinars ("BD"), being the functional currency of the Group's operations. All the values are rounded to the nearest BD thousand except when otherwise indicated.

d. Basis of consolidation

The consolidated financial statements comprise the financial statements of the Bank and its subsidiaries as at 31 December each year. A subsidiary is an entity over which the Bank has power to control, which is other than fiduciary in nature. The financial statements of the subsidiaries are prepared for the same reporting year as the Bank, using consistent accounting policies.

The subsidiaries are fully consolidated from the date of acquisition, being the date on which the Group obtained control, and continue to be consolidated until the date that such control ceases. Control is achieved where the Group has direct ownership of more than 50% of the voting rights over the subsidiaries or where the Group has the power, directly or indirectly, to govern the financial and operating policies of the entity so as to obtain benefits from its activities.

Losses within the subsidiaries are attributed to the non-controlling interest even if that results in a deficit balance.

The results of the subsidiaries acquired or disposed off during the year are included in the consolidated statement of income from the date of acquisition or up to the date of disposal, as appropriate.

All intra-group balances, income and expenses and unrealised gains and losses resulting from intra-group transactions are eliminated in full.

e. Cash and cash equivalents

For the purpose of the consolidated cash flows statement, "cash and cash equivalents" consist of cash on hand, balances with the Central Bank of Bahrain exluding mandatory reserve deposits, and balances with banks and other financial institutions, with original maturities of 90 days or less.

f. Placements with financial institutions

Placements with financial institutions comprise commodity Murabaha receivables and Wakala receivables. Commodity Murabaha receivables are stated net of deferred profits and provision for impairment, if any. Wakala receivables are stated at cost less provision for impairment, if any.

g. Financing assets

Financing assets comprise Shari'a compliant financing contracts with fixed or determinable payments. These include financing provided through Murabaha and Musharaka.

h. Murabaha financing

Murabaha financing consist mainly of deferred sales transactions (Murabaha) which are stated net of deferred profits and provisions for impairment, if any.

NOTES TO THE CONSOLIDATED FINANCIAL INFORMATION

31 December 2014

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

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

i. Musharaka financing

Musharaka financing are stated at the fair value of consideration given less impairment, if any.

Musharaka financing are a form of capital partnership. These are stated at fair value of consideration given less any impairment. Musharaka financing capital provided by the Group at inception in kind (if other than cash) is measured at the fair value of the assets. If the valuation of the assets results in a difference between fair value and book value, such difference is recognised as profit or loss to the Group.

j. Investments securities

Investments securities comprise of debt type instruments carried at amortised cost, equity type instruments carried at fair value through equity and equity type instruments carried at fair value through statement of income.

All investments securities, are initially recognised at cost, being the fair value of the consideration given including acquisition charges associated with the investment, except in the case of investments carried at fair value through statement of income, where the acquisition charges are expensed in the income statement.

Debt type instruments carried at amortised cost

Investments which have fixed or determinable payments and where the Group has both the intent and ability to hold to maturity are classified as debt type instruments carried at amortised cost. Such investments are carried at amortised cost, less provision for impairment in value. Amortised cost is calculated by taking into account any premium or discount on acquisition. Any gain or loss on such instruments is recognised in the consolidated statement of income when the instruments are de-recognised or impaired.

Equity type instruments carried at fair value through equity

Subsequent to acquisition, equity type instruments are remeasured at fair value, with unrealised gains and losses recognised in a separate component of equity until the investment is derecognised or the investment is determined to be impaired. On derecognition or impairment, the cumulative gain or loss previously recorded in equity is recognised in the consolidated statement of income for the year.

Impairment losses on equity type instruments carried at fair value through equity are not reversed through the consolidated statement of income and increases in their fair value after impairment are recognised directly in owners' equity.

Equity type instruments carried at fair value through statement of income

These are subsequently re-measured at fair value. All related realised and unrealised gains or losses are included in the consolidated statement of income.

k. Determination of fair value

For investments traded in organised financial markets, fair value is determined by reference to quoted market bid prices at the close of business on the consolidated statement of financial position date.

For investments where there is no quoted market price, a reasonable estimate of the fair value is determined by reference to the 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.

Investments at fair value through equity where the Bank is unable to determine a reliable measure of fair value on a continuing basis, such as investments that do not have a quoted market price or other appropriate methods from which to derive reliable fair values, are stated at cost less impairment allowances.

For Murabaha receivables the fair value is determined by the Bank at the end of the financial period at their cash equivalent value.

l. Investment in associates

The Group's investments in associates are accounted for under the equity method of accounting. Associates are entities over which the Group exercises significant influence but not control and which are neither subsidiaries nor joint ventures. Under the equity method, the investments in associates are carried in the consolidated statement of financial position at cost, plus post-acquisition changes in the

NOTES TO THE CONSOLIDATED FINANCIAL INFORMATION

31 December 2014

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

Group's share of net assets of the associate, less any impairment. The consolidated statement of income reflects the Group's share of the results of its associates. Where there has been a change recognised directly in the equity of the associates, the Group recognises its share of any changes and discloses this, when applicable, in the consolidated statement of changes in owners' equity. Unrealised profits and losses resulting from transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates.

The Group determines at each consolidated statement of financial position date whether there is any objective evidence that the investments in associates are impaired. If this is the case the Group calculates the amount of impairment as being the difference between the fair value of the associates and the carrying value and recognises this amount in the consolidated statement of income.

The reporting dates of the associates and the Group are identical and the associates accounting policies conform to those used by the Group for like transactions and events in similar circumstances. Latest available financial information is used to account for these under the equity method of accounting.

m. Ijarah Muntahia Bittamleek

These are initially recorded at cost. Ijarah assets and Ijarah Muntahia Bittamleek mainly comprise of land and buildings and certain other assets. Ijarah Muntahia Bittamleek is a lease whereby the legal title of the leased asset passes to the lessee at the end of the Ijarah (lease term), provided that all Ijarah instalments are settled.

Depreciation is calculated on all Ijarah Muntahia Bittamleek other than land (which is deemed to have an indefinite life), at rates calculated to write off the cost of each asset over its useful life.

n. Investment in real estate

Properties held for rental, or for capital appreciation purposes, or both, are classified as investment in real estate. Investments in real estate are initially recorded at cost, being the fair value of the consideration given and acquisition charges associated with the property. Subsequent to initial recognition, investments in real estate held for capital appreciation are re-measured at fair value and changes in fair value (only gains) are recognised as property fair value reserve in the consolidated statement of changes in owners' equity.

Losses arising from changes in the fair values of investment in real estate are firstly adjusted against the property fair value reserve to the extent of the available balance and then the remaining losses are recognised in the consolidated statement of income. If there are unrealised losses that have been recognised in the consoliated statement of income in previous financial periods, the current period unrealised gain shall be recognised in the consolidated statement of income to the extent of crediting back such previous losses in the consolidated statement of income. When the property is disposed of, the cumulative gain previously transferred to the property fair value reserve, is transferred to the consolidated statement of income.

o. Equipment

Equipment is recognised at cost. The cost of additions and major improvements are capitalised; maintenance and repairs are charged to the consolidated statement of income as incurred. Gains or losses on disposal are reflected in other income. Depreciation is provided on the straight-line basis over the estimated useful lives of the assets.

The calculation of depreciation is on the following basis:

Buildings	25 to 35 years
Fixtures and fittings	5 years
Equipment	5 years
Furniture	5 years

p. Equity of investment accountholders

All equity of investment accountholders is carried at cost plus profit and related reserves less amounts settled.

Equity of investment accountholders share of income is calculated based on the income generated from investment accounts after deducting Mudarib share. Operating expenses are charged to shareholders' funds and not included in the calculation.

The basis applied by the Group in arriving at the equity of investment accountholders' share of income is total income from jointly financed assets less Bank's portion of this income based on its proportion of the jointly financed assets. The portion of the income generated from equity of investment accountholders will be deducted as Mudarib share and the remaining will be distributed to the equity of investment accountholders.

NOTES TO THE CONSOLIDATED FINANCIAL INFORMATION
31 December 2014

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

q. Investment risk reserve

Investment risk reserves are amounts appropriated out of the income of equity of investment accountholders, after allocating the Mudarib share, in order to cater for future losses for equity of investment accountholders.

r. Profit equalisation reserve

The Group appropriates a certain amount in excess of the profit to be distributed to equity of investment accountholders after taking into consideration the Mudarib share of income. This is used to maintain a certain level of return on investment for equity of investment accountholders.

s. Zakah

Zakah is calculated on the Zakah base of the Group in accordance with FAS 9 issued by AAOIFI using the net invested funds method. Zakah is paid by the Group based on the consolidated figures of statutory reserve, general reserve and retained earning balances at the beginning of the year. The remaining Zakah is payable by individual shareholders. Payment of Zakah on equity of investment accountholders and other accounts is the responsibility of investment accountholders.

t. Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) arising from a past event and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of obligation.

u. Dividends

Dividends to shareholders are recognised as liabilities in the year in which they are declared.

v. Derecognition of financial assets and liabilities

Financial assets

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

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

  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.

Financial liabilities

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

w. Treasury shares

These are own equity instruments of the Group which are reacquired through its own broker. Treasury shares are deducted from equity and accounted for at weighted average cost. Consideration paid or received on the purchase, sale, issue or cancellation of the Group's own equity instruments is recognised directly in equity. No gain or loss is recognised in consolidated statement of income on the purchase, sale, issue or cancellation of own equity instruments.

x. Earnings prohibited by Shari'a

The Group is committed to avoid recognising any income generated from non-Islamic sources. Accordingly, all non-Islamic income is credited to a charity fund where the Group uses these funds for social welfare activities.

y. Joint and self financed

Investments, financing and receivables that are jointly funded by the Group and the equity of investment accountsholders are classified under the caption "jointly financed" in the consolidated financial statements. Investments, financing and receivables that are funded solely by the Bank are classified under "self financed".

NOTES TO THE CONSOLIDATED FINANCIAL INFORMATION

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2 SIGNIFICANT ACCOUNTING POLICIES (continued)

z. Offsetting

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

aa. Revenue recognition

Murabaha receivables

Income is recognised by proportionately allocating the attributable profits over the deferred period whereby each financial period carries its portion of profits irrespective of when cash is received. Income related to accounts that are 90 days overdue is excluded from the consolidated statement of income.

Musharaka investments

Income on Musharaka is recognised when the right to receive payment is established or on distribution. In the case of losses on musharaka, the Group's share of losses is recognised to the extent that such losses are being deducted from its share of the Musharaka capital.

Placements with financial institutions

Income on placements from financial institutions is recognised on a time apportioned basis over the period of the contract based on the principal amounts outstanding and the profit agreed with clients.

Ijarah Muntahia Bittamleek

Income from Ijarah Muntahia Bittamleek is recognised on a time-apportioned basis over the lease term. The Ijarah Muntahia Bittamleek income is net of depreciation. Income related to non-performing (90 days overdue) Ijarah Muntahia Bittamleek is excluded from the consolidated statement of income.

Dividends income

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

Income from Ijarah assets

Rental income is accounted for on a straight-line basis over the Ijarah term.

Fee and commission income

Fee and commission income is recognised when earned.

Group's share as a Mudarib

The Group's share as a Mudarib for managing equity of investment accountholders is accrued based on the terms and conditions of the related mudaraba agreements.

Income allocation

Income is allocated proportionately between equity of investment accountholders and shareholders on the basis of the average balances outstanding during the year.

bb. Foreign currencies

Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated into Bahraini Dinars at the rate of exchange ruling at the consolidated statement of financial position date. All differences are taken to the consolidated statement of income.

Translation gains or losses on non-monetary items carried at fair value are included in owners' equity as part of the fair value adjustment.

cc. Impairment of financial assets

An assessment is made at each consolidated financial position date to determine whether there is objective evidence that a specific financial asset or a group of financial assets may be impaired. If such evidence exists, the estimated recoverable amount of that asset is determined and any impairment loss, based on the assessment by the Group of the estimated cash equivalent value, is recognised in the consolidated statement of income. Specific provisions are created to reduce all impaired financial contracts to their realisable cash equivalent value. Financial assets are written off only in circumstances where effectively all possible means of recovery have been exhausted. Impairment is determined as follows:

(a) For assets carried at fair value, a significant or prolonged decline in fair value below its cost is an objective evidence of impairment. If such evidence exists impairment is the difference between cost and fair value, less any impairment loss previously recognised in the consolidated statement of income; and

NOTES TO THE CONSOLIDATED FINANCIAL INFORMATION

31 December 2014

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

cc. Impairment of financial assets (continued)

(b) For assets carried at amortised cost, impairment is the difference between carrying amount and the present value of future cash flows discounted at the original effective profit rate.

For equity type instruments carried at fair value through equity, impairment losses recognised in the consolidated statement of income cannot be reversed through the consolidated statement of income and are recorded as increases in cumulative changes in fair value through equity.

dd. Use of estimates and judgements in preparation of the consolidated financial statements

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

Going concern

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

Impairment

The Group assesses at each consolidated statement of financial position date whether there is objective evidence that a specific asset or a group of assets may be impaired. An asset or a group of assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that have occurred after the initial recognition of the asset (an incurred "loss event") and that loss event(s) has an impact on the estimated future cash flows of the asset or the group of the assets that can be reliably estimated.

Collective impairment provision

Impairment is assessed collectively for losses on Islamic financing facilities that are not individually significant and for individually significant facilities where the loss is incurred but not reported. Collective impairment is evaluated on each reporting date with each portfolio receiving a separate review.

Fair valuation of investments

The determination of fair values of unquoted investments requires management to make estimates and assumptions that may affect the reported amount of assets at the date of the consolidated financial statements. The valuation of such investments is based on the fair value criteria explained in note 2.i above.

Nonetheless, the actual amount that is realised in a future transaction may differ from the current estimate of fair value and may still be outside management estimates, given the inherent uncertainty surrounding valuation of unquoted investments.

Classification of investments

Management decides on acquisition of a financial asset whether it should be classified as equity type instrument carried at fair value through equity or through statement of income.

Fair value of investment in real estate

The fair value of investment in real estate is determined by independent real estate valuation experts based on recent real estate transactions with similar characteristics and locations.

ee. Trade date accounting

All "regular way" purchases and sales of financial assets are recognised on the trade date, i.e. the date that the Group commits to purchase or sell the asset.

ff. Employees' end of service benefits

Provision is made for amounts payable under the Bahrain Labour law applicable to non-Bahraini employees' accumulated periods of service at the date of the consolidated statement of financial position, subject to completion of a minimum period of employment. Provision for this is made by calculating the notional liability had all employees left at the reporting date.

Bahraini employees of the Group are covered by contributions made to the Social Insurance Organization scheme as a percentage of the employees' salaries. The Group's obligations are limited to these contributions, which are expensed when due.

NOTES TO THE CONSOLIDATED FINANCIAL INFORMATION

31 December 2014

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

gg. Shari'a supervisory board

The Group's business activities are subject to the supervision of a Shari'a Supervisory Board consisting of five members appointed by the general assembly.

hh. Financial guarantees

Financial guarantees are contracts that require the Group to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument. A financial guarantee contract is recognised from the date of its issue. The liability arising from a financial guarantee contract is recognised at the present value of any expected payment, when a payment under the guarantee has become probable.

ii. Statutory reserve

The Bahrain Commercial Companies Law 2001 requires that 10 per cent of the annual net profit be appropriated to a statutory reserve which is normally distributable only on dissolution. Appropriations may cease when the reserve reaches 50 per cent of the paid up share capital.

3 CASH AND BALANCES WITH BANKS AND CENTRAL BANK

	2014 **BD'000**	2013 BD'000
Cash on hand	**9,048**	7,750
Balances with CBB, excluding mandatory reserve deposits	**4,295**	2,926
Balances with banks and other financial institutions	**7,720**	7,415
	21,063	18,091
Mandatory reserve with CBB	**31,055**	32,740
	52,118	50,831

The mandatory reserve with CBB is not available for use in the day-to-day operations.

4 PLACEMENTS WITH FINANCIAL INSTITUTIONS

	Jointly financed **2014** **BD'000**	Jointly financed 2013 BD'000
Commodity Murabaha	**30,502**	121,566
Deferred profits	**(15)**	(33)
	30,487	121,533
Wakala	**38,080**	63,067
	68,567	184,600

5 FINANCING ASSETS

	Jointly financed **2014** **BD'000**	Jointly financed 2013 BD'000
Murabaha (note 5.1)	**308,710**	256,038
Musharaka (note 5.2)	**99,311**	90,767
	408,021	346,805

NOTES TO THE CONSOLIDATED FINANCIAL INFORMATION
31 December 2014

5 FINANCING ASSETS (continued)

5.1 Murabaha

	Jointly financed 2014 BD'000	Jointly financed 2013 BD'000
Tasheel	**201,487**	175,016
Tawarooq	**125,701**	93,835
Letters of credit refinance	**17,208**	16,713
Motor vehicles Murabaha	**17,139**	15,978
Credit cards	**12,357**	9,887
Others	**4,008**	414
	377,900	311,843
Qard fund	**80**	79
Gross receivables	**377,980**	311,922
Deferred profits	**(44,219)**	(36,814)
Provision for impairment (note 21)	**(25,051)**	(19,070)
	308,710	256,038

Non-performing Murabaha financing outstanding as of 31 December 2014 amounted to BD 21,593 thousand (2013: BD 25,568 thousand).

The Group considers the promise made in the Murabaha to the purchase orderer as obligatory.

The composition of the Murabaha financing portfolio before provision for impairment geographically and by sector is as follows:

	2014			2013		
	Europe	**Middle East**	**Total**	Europe	Middle East	Total
	BD'000	**BD'000**	**BD'000**	BD'000	BD'000	BD'000
Commercial	**-**	**85,971**	**85,971**	-	81,316	81,316
Financial institutions	**-**	**18,430**	**18,430**	7,270	11,302	18,572
Others including retail	**-**	**229,360**	**229,360**	-	175,220	175,220
	-	**333,761**	**333,761**	7,270	267,838	275,108

5.2 Musharaka

	Jointly financed 2014 BD'000	Jointly financed 2013 BD'000
Musharaka investment in real estate	**104,943**	98,788
Provision for impairment (note 21)	**(5,632)**	(8,021)
	99,311	90,767

Non-performing Musharaka financing outstanding as of 31 December 2014 amounted to BD 19,003 thousand (2013: BD 33,369 thousand).

NOTES TO THE CONSOLIDATED FINANCIAL INFORMATION
31 December 2014

6 INVESTMENTS

	2014			2013		
	Self financed BD'000	**Jointly financed BD'000**	**Total BD'000**	Self financed BD'000	Jointly financed BD'000	Total BD'000
i) Debt type instruments carried at amortised cost						
Sukuk						
At 1 January	**-**	**41,705**	**41,705**	-	44,406	44,406
Acquisitions	**-**	**50,229**	**50,229**	-	18,947	18,947
Disposals and redemptions	**-**	**(6,126)**	**(6,126)**	-	(21,648)	(21,648)
At 31 December	**-**	**85,808**	**85,808**	-	41,705	41,705
Provision for impairment	**-**	**(3,974)**	**(3,974)**	-	(3,340)	(3,340)
Total net Sukuk	**-**	**81,834**	**81,834**	-	38,365	38,365
ii) Equity type instruments carried at fair value through equity						
Quoted shares - at fair value						
At 1 January	**26,494**	**-**	**26,494**	24,920	-	24,920
Acquisitions	**-**	**-**	**-**	4,586	-	4,586
Fair value change	**(2,235)**	**-**	**(2,235)**	2,186	-	2,186
Disposals	**(16,941)**	**-**	**(16,941)**	(5,198)	-	(5,198)
Write off	**(4,849)**	**-**	**(4,849)**	-	-	-
At 31 December	**2,469**	**-**	**2,469**	26,494	-	26,494
Provision for impairment	**(1,076)**	**-**	**(1,076)**	(6,499)	-	(6,499)
Total net	**1,393**	**-**	**1,393**	19,995	-	19,995
Unquoted shares - at cost less impairment						
At 1 January	**29,249**	**-**	**29,249**	34,022	-	34,022
Acquisitions	**-**	**-**	**-**	920	-	920
Disposals	**(48)**	**-**	**(48)**	-	-	-
Write off	**-**	**-**	**-**	(5,693)	-	(5,693)
At 31 December	**29,201**	**-**	**29,201**	29,249	-	29,249
Provision for impairment	**(7,721)**	**-**	**(7,721)**	(7,119)	-	(7,119)
Total net	**21,480**	**-**	**21,480**	22,130	-	22,130
Unquoted managed funds - at cost less impairment						
At 1 January	**43,808**	**-**	**43,808**	41,970	-	41,970
Acquisitions	**-**	**-**	**-**	9,384	-	9,384
Foreign currency translation changes	**(1,242)**	**-**	**(1,242)**	-	-	-
Disposals	**(6,025)**	**-**	**(6,025)**	(7,546)	-	(7,546)
At 31 December	**36,541**	**-**	**36,541**	43,808	-	43,808
Provision for impairment	**(17,687)**	**-**	**(17,687)**	(18,138)	-	(18,138)
Total net	**18,854**	**-**	**18,854**	25,670	-	25,670
iii) Equity type instruments carried at fair value through statement of income						
Quoted investments						
At 1 January	**866**	**-**	**866**	426	-	426
Acquisitions	**-**	**-**	**-**	3,247	-	3,247
Fair value change	**-**	**-**	**-**	55	-	55
Disposals	**(866)**	**-**	**(866)**	(2,862)	-	(2,862)
At 31 December	**-**	**-**	**-**	866	-	866
Total net investments securities	**41,727**	**81,834**	**123,561**	68,661	38,365	107,026

NOTES TO THE CONSOLIDATED FINANCIAL INFORMATION

31 December 2014

7 INVESTMENT IN ASSOCIATES

	Self financed 2014 BD'000	Self financed 2013 BD'000
At 1 January	**36,236**	35,215
Share of (loss) / profit	**(1,550)**	1,197
Share of changes in investee's equity	**(821)**	(176)
Dividends received	**(70)**	-
Provision for impairment	**(2,960)**	-
At 31 December	**30,835**	36,236

Investments in associates comprise:

Name of associate	Ownership %	Country of incorporation	Nature of business
Takaful International Company B.S.C.*	22.75%	Bahrain	Takaful International Company B.S.C. was incorporated in 1989, and carries out Takaful and Retakaful activities in accordance with the teachings of Islamic Shari'a.
Liquidity Management Centre B.S.C. (c)	25.00%	Bahrain	Liquidity Management Centre B.S.C. (c) was incorporated in 2002 as a bank, licensed and regulated by the Central Bank of Bahrain to facilitate the creation of an Islamic inter-bank market that will allow Islamic financial services institutions to effectively manage their assets and liabilities.
Arabian C Real Estate Company	19.00%	Kuwait	Arabian C Real Estate Company is a Kuwaiti Shareholding Company incorporated in accordance with the Kuwaiti Commercial Companies law, Decree No.15 of 1960, as amended and regulated by the Ministry of Commerce & Industry of Kuwait. The company's activity focuses on real estate development and the overall management of a variety of strategic investments in the real estate and infrastructure sectors in GCC/MENA region.
Enjaz Property Development Company B.S.C. (c)	32.76%	Bahrain	Enjaz Property Development Company B.S.C.(c) is a closed joint stock company incorporated in the Kingdom of Bahrain and is registered with the Ministry of Industry and Commerce since 6 February 2008 under commercial registration number 67713-1. The company is engaged in the purchase and sale of land and property development.
Al Dur Energy Investment Company	29.41%	Bahrain	Al Dur Energy Investment Company is an exempt company with limited liability incorporated in the Cayman Islands on 10 June 2009 and operates under registration number 227032. The company operates in the Kingdom of Bahrain with the sole purpose of holding a 15% indirect interest in a power and water plant project company, Al Dur Power and Water Company B.S.C.(c), in the Kingdom of Bahrain.

* Takaful International Company B.S.C. is a listed company on the Bahrain Bourse. The latest available quoted price of BD 0.145 per share was as of 8 May 2014, no further trades have taken place on the company's shares since that date. The estimate fair value of the investment based on this price is BD 2,062 thousand (2013: BD 4,124 thousand).

NOTES TO THE CONSOLIDATED FINANCIAL INFORMATION

31 December 2014

8 IJARAH MUNTAHIA BITTAMLEEK

	2014					2013				
	Jointly financed					Jointly financed				
	Lands	Buildings	Aviation related assets	Others	Total	Land	Buildings	Aviation related assets	Others	Total
	BD'000	BD'000	BD'000	BD'000	BD'000	BD'000	BD'000	BD'000	BD'000	BD'000
Cost:										
At 1 January	40,588	56,058	7,287	9,101	113,034	38,913	56,772	11,157	7,585	114,427
Additions	6,824	37,766	589	2,548	47,727	4,167	10,222	-	1,516	15,905
Settlements	(3,107)	(28,712)	-	(887)	(32,706)	(2,492)	(10,936)	(3,870)	-	(17,298)
At 31 December	44,305	65,112	7,876	10,762	128,055	40,588	56,058	7,287	9,101	113,034
Depreciation:										
At 1 January	-	12,406	1,245	1,273	14,924	-	10,698	2,145	923	13,766
Provided during the year	-	3,431	547	959	4,937	-	3,580	507	350	4,437
Relating to settled assets	-	(5,793)	-	(3)	(5,796)	-	(1,872)	(1,407)	-	(3,279)
At 31 December	-	10,044	1,792	2,229	14,065	-	12,406	1,245	1,273	14,924
Provision for impairment (note 21)	(9,175)	(2,538)	-	-	(11,713)	(6,133)	(1,621)	-	-	(7,754)
Net book value:										
As at 31 December	35,130	52,530	6,084	8,533	102,277	34,455	42,031	6,042	7,828	90,356

Non-performing Ijarah Muntahia Bittamleek as of 31 December 2014 is BD 24,702 thousand (2013: BD 32,516 thousand).

Ijarah rental receivable comprises of both rental on Ijarah assets and depreciation charge on Ijarah Muntahia Bittamleek assets which is fully receivable from the customers.

9 PROPERTY AND EQUIPMENT

	2014						
	Lands BD'000	Buildings BD'000	Fixture and fitting BD'000	Equipment BD'000	Furniture BD'000	Work in progress BD'000	Total BD'000
Cost:							
At 1 January	7,183	4,535	2,906	8,008	677	3,269	26,578
Additions / Transfer	-	2,884	487	1,057	146	-	4,574
Disposals / Transfer	(40)	(32)	-	-	-	(2,859)	(2,931)
At 31 December	7,143	7,387	3,393	9,065	823	410	28,221
Depreciation:							
At 1 January	-	1,255	2,162	5,566	528	-	9,511
Provided during the year	-	216	355	984	86	-	1,641
Relating to disposed assets	-	(32)	-	-	-	-	(32)
At 31 December	-	1,439	2,517	6,550	614	-	11,120
Net Book Value	7,143	5,948	876	2,515	209	410	17,101

NOTES TO THE CONSOLIDATED FINANCIAL INFORMATION
31 December 2014

9 PROPERTY AND EQUIPMENT (continued)

	2013						
	Lands BD'000	Buildings BD'000	Fixture and fitting BD'000	Equipment BD'000	Furniture BD'000	Work in progress BD'000	Total BD'000
Cost:							
At 1 January	40	1,108	2,688	6,980	605	2,069	13,490
Additions	7,143	3,427	218	1,028	72	1,200	13,088
At 31 December	7,183	4,535	2,906	8,008	677	3,269	26,578
Depreciation:							
At 1 January	-	1,107	1,947	4,352	461	-	7,867
Provided during the year	-	148	215	1,214	67	-	1,644
At 31 December	-	1,255	2,162	5,566	528	-	9,511
Net Book Value	7,183	3,280	744	2,442	149	3,269	17,067

10 INVESTMENT IN REAL ESTATE

	Self financed	
	2014 BD'000	2013 BD'000
Lands	**51,339**	55,264
Buildings	**2,595**	2,955
	53,934	58,219

	2014 BD'000	2013 BD'000
At 1 January	**58,219**	64,888
Capitalized expediture	**257**	-
Disposal	**(7,799)**	(5,348)
Fair value changes	**3,257**	(1,321)
	53,934	58,219

Investment in real estate comprises properties located in the Kingdom of Bahrain and the United Arab Emirates.

Investment in real estate held for capital appreciation is stated at fair value as at 31 December each year, which has been determined based on valuations performed by independent third part property valuers who have the qualification and experience of valuing similar properties in the same location.

NOTES TO THE CONSOLIDATED FINANCIAL INFORMATION
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11 OTHER ASSETS

	2014 BD'000	2013 BD'000
Receivables	**1,907**	1,907
Staff advances	**1,177**	1,323
Prepaid expenses	**658**	608
Income receivables	**-**	167
Other	**986**	225
	4,728	4,230

12 OTHER LIABILITIES

	2014 BD'000	2013 BD'000
Managers' cheques	**4,150**	2,924
Payable to vendors	**3,039**	3,097
Accrued expenses	**3,334**	2,645
Life insurance (Takaful) fees payable	**1,928**	1,819
Dividends payable	**806**	807
Zakah and charity fund	**282**	225
Other	**2,979**	2,091
	16,518	13,608

13 EQUITY OF INVESTMENT ACCOUNTHOLDERS

As equity of investment accountholders' funds are commingled with the Group's funds for investment, no priority is granted to any party for the purpose of investments and distribution of profits.

The Group maintains an investment risk reserve amounting to BD 103 thousand (2013: BD 63 thousand) and maintains a profit equalisation reserve amounting to BD 395 thousand (2013: BD 295 thousand).

The Group's share, as Mudarib, in the profits of equity of investment accountholders is up to a maximum of 85% (2013: 65%).

13.1 Profit Distribution by Type of Account

The following table represents the distribution of profit by type of equity of investment accountholders:

	2014		2013	
	Percentage of funds invested	Distributed profit rate	Percentage of funds invested	Distributed profit rate
Account Type				
Defined deposits	**85%**	**1.29%**	85%	1.81%
Specific investment deposits	**85%**	**1.89%**	85%	2.86%
Investment certificates	**85%**	**3.50%**	85%	3.50%
Savings accounts	**45%**	**0.23%**	45%	0.25%
Iqra	**90%**	**2.16%**	90%	2.72%
Tejoori	**45%**	**0.23%**	45%	0.25%
Vevo	**45%**	**0.22%**	45%	0.25%

NOTES TO THE CONSOLIDATED FINANCIAL INFORMATION

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13 EQUITY OF INVESTMENT ACCOUNTHOLDERS (continued)

13.2 Equity of investment accountholders balances

	2014 BD'000	2013 BD'000
Type of Equity of Investment Accountholders		
Customer investment accounts		
Balances on demand	**246,880**	218,658
Contractual basis	**316,879**	395,256
Others	**2,842**	3,580
	566,601	617,494

13.3 Equity of Investment Accountholders Reserves

	2014 BD'000	Movement BD'000	2013 BD'000
Profit equalisation reserve	**395**	**100**	295
Investment risk reserve	**103**	**40**	63

13.4 Return on equity of investment accountholders

	2014 BD'000	2013 BD'000
Gross return to equity of investment accountholders	**23,519**	33,176
Profit equalization reserve	**(100)**	(295)
Group's share as a Mudarib	**(16,092)**	(22,021)
Investment risk reserve	**(40)**	-
Return on equity of investment accountholders	**7,287**	10,860

14 OWNERS' EQUITY

	2014 BD'000	2013 BD'000
(i) Share capital		
a) Authorised		
2,000,000,000 shares (2013: 2,000,000,000 shares) of BD 0.100 each	**200,000**	200,000
b) Issued and fully paid up		
939,673,499 shares (2013: 939,673,499 shares) of BD 0.100 each	**93,967**	93,967

(ii) Treasury Shares	2014		2013
	Number of Shares	**BD'000**	BD'000
At 31 December	**3,620,609**	**563**	563

	2014 BD'000
Cost of treasury shares	**563**
Market value of treasury shares	**536**

The treasury shares as a percentage of total shares in issue is 0.39%.

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14 OWNERS' EQUITY (continued)

Owners' equity instruments which are reacquired are deducted from equity. No gain or loss is recognised in the consolidated statement of income on the purchase, sale, issue or cancellation of the Group's own equity instruments.

(iii) Reserves

Statutory reserve
As required by Bahrain Commercial Companies Law and the Bank's articles of association, 10% of the net income for the year should be transferred to the statutory reserve. The Bank may resolve to discontinue such annual transfers when the reserve totals 50% of paid up share capital. A transfer has been made of BD 930 thousand (2013: BD 611 thousand) representing 10% of the profit for the year BD 9,297 thousand (2013: BD 6,107 thousand). The reserve is not distributable except in such circumstances as stipulated in the Bahrain Commercial Companies Law and following the approval of CBB.

General reserve
The general reserve is established in accordance with the articles of association of the Bank and is distributable following a resolution of shareholders at a general meeting and the approval of CBB. The Group may transfer any amount to the general reserve, as approved by the shareholders at a general meeting, out of the net income for the year after appropriating statutory reserve.

Fair value reserve on investment in real estate
This represents cumulative unrealised revaluation gains on investment in real estate. This reserve is transferred to the retained earnings upon sale of the investment in real estate.

Cumulative changes in fair value of investments
This represents the net unrealised gains or losses on equity investments relating to self financed investments.

(iv) Additional information on shareholding pattern

1) Names and nationalities of the major shareholders and the number of shares in which they have an interest of 5% or more of outstanding shares:

	2014			2013	
Names	**Nationality**	**Number of shares**	**% holding**	Number of shares	% holding
National Bank of Bahrain	Bahraini	**242,038,206**	**25.76%**	242,038,206	25.76%
Social Insurance Organisation	Bahraini	**121,113,560**	**12.89%**	121,147,267	12.89%
Social Insurance Organisation - Military Pension Fund	Bahraini	**121,113,559**	**12.89%**	121,113,559	12.89%
Islamic Development Bank	Saudi	**165,956,945**	**17.66%**	165,956,945	17.66%
General Council of Kuwaiti Awqaf	Kuwaiti	**68,013,739**	**7.24%**	68,013,739	7.24%

2) The Group has only one class of shares and the holders of these shares have equal voting rights.
3) Distribution schedule of shares, setting out the number and percentage of holders in the following categories:

	2014			2013		
	Number of shares	**Number of shareholders**	**% of total outstanding shares**	Number of shares	Number of shareholders	% of total outstanding shares
Less than 1%	**153,552,651**	**3,383**	**16.40%**	153,518,944	3,411	16.44%
1% up to less than 5%	**67,884,839**	**3**	**7.22%**	67,884,839	3	7.22%
5% up to less than 10%	**68,013,739**	**1**	**7.23%**	68,013,739	1	7.23%
10% up to less than 50%	**650,222,270**	**4**	**69.15%**	650,255,977	4	69.11%
	939,673,499	**3,391**	**100.00%**	939,673,499	3,419	100.00%

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14 OWNERS' EQUITY (continued)

Details of Directors' interests in the Group's shares as at the end of the year were:

Categories:

	2014		2013	
	No. of shares	**No. of Directors**	No. of shares	No. of Directors
	400,000	**4**	200,000	2

The following is the number of shares, and percentage of shareholding of Directors, Shari'a supervisory members and senior management (Assistant General Managers and above):

	2014		2013	
	No. of shares	**Percentage of Shareholding**	No. of shares	Percentage of Shareholding
Directors	**400,000**	**0.043%**	200,000	0.021%
Shari'a supervisory members	**199,812**	**0.021%**	205,725	0.022%
Senior management	**-**	**0.000%**	22,990	0.002%
	599,812	**0.064%**	428,715	0.045%

The Bank has adopted sound remuneration practices as required under volume 2 of the CBB rulebook. Accordingly the Bank has set up an employee share incentive scheme which is subject to approval by the shareholders the fourth coming annual general meeting for the year ended 31 December 2014.

15 COMMITMENTS AND CONTINGENT LIABILITIES

Credit related commitments

These include commitments to enter into financing contracts which are designed to meet the requirements of the Group's customers. Letters of credit and guarantees commit the Group to make payments on behalf of customers.

The Group has the following credit related commitments and contingent liabilities on behalf of customers:

	2014 BD'000	2013 BD'000
Letters of credit and acceptances	**2,775**	3,910
Guarantees	**18,760**	11,618
Operating lease commitments *	**742**	463
	22,277	15,991

* The Group has entered into commercial leases for certain branches. The remaining average period of these leases ranges between 1 month and 3 years with renewal terms included in the contracts. Renewals are at the option of the Bank. There are no restrictions placed upon the lessee by entering into these leases.

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15 COMMITMENTS AND CONTINGENT LIABILITIES (continued)

Future minimum rentals payable under non-cancellable operating leases as at 31 December are as follows:

	2014 BD'000	2013 BD'000
Within one year	**225**	379
After one year but not more than five years	**517**	84
	742	463

16 CAPITAL ADEQUACY

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

The Group's capital structure primarily consists of its paid-up capital, including share premium and reserves. From a regulatory perspective, a significant amount of the Group's capital is classified as Tier 1 as defined by the CBB, i.e. most of the capital is of a permanent nature.

The Group's capital adequacy policy is to maintain a strong capital base to support the development and growth of the business. Current and future capital requirements are determined on the basis of financing facilities growth expectations for each business group, expected growth in off-balance sheet facilities and future sources and uses of funds.

In August 2014, the Central Bank of Bahrain issued the final regulation to give effect to the Basel III framework which comes into effect on 1 January 2015. The Basel III framework significantly revises the definition of regulatory capital. The framework emphasis common equity as the predominant component of tier 1 capital by adding a minimum common equity tier 1 (CET 1) capital ratio. The Basel III rules also require institutions to hold capital buffers. For the purpose of calculating CET 1 capital, the regulatory adjustments (deductions) including amounts above the aggregate limit for significant investments in financial institutions, mortgage servicing rights, and deferred tax assets from temporary differences, will be deducted from CET1 over a phased manner to be fully deducted by 1 January 2019. The Bank's current capital position is sufficient to meet the new regulatory capital requirements.

The classification of the Group's capital in accordance with the regulatory requirements is as follows:

	2014 BD'000	2013 BD'000
Tier 1 Capital	**74,727**	51,125
Tier 2 Capital	**19,722**	13,073
Total Capital Base	**94,449**	64,198

To assess its capital adequacy requirements in accordance with the CBB requirements, the Group adopts the Standardised Approach for its Credit Risk, Basic Indicator Approach for its Operational Risk and Standardised Measurement Approach for its Market Risk. The capital requirements for these risks are as follows:

	2014 BD'000	2013 BD'000
Risk weighted exposure:		
Total Credit Risk Weighted Assets	**532,703**	492,627
Total Market Risk Weighted Assets	**15,769**	18,416
Total Operational Risk Weighted Assets	**56,583**	42,133
Total Regulatory Risk Weighted Assets	**605,055**	553,176
Capital Adequacy Ratio	**15.61%**	11.61%
Tier 1 Capital Adequacy Ratio	**12.35%**	9.24%
Minimum requirement	**12%**	12%

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17 INCOME FROM FINANCING

	2014 BD'000	2013 BD'000
Income from jointly financed Islamic financing assets:		
Income from Murabaha financing	**17,870**	18,987
Income from placements with financial institutions	**515**	895
Income from Musharaka financing	**5,474**	5,372
Income from Ijarah Muntahia Bittamleek - net *	**4,843**	7,250
	28,702	32,504

* The details of Income from Ijarah Muntahia Bittamleek is as follows:

	2014 BD'000	2013 BD'000
Income from Ijarah Muntahia Bittamleek – gross	**9,780**	11,687
Depreciation during the year (note 8)	**(4,937)**	(4,437)
	4,843	7,250

18 INCOME FROM INVESTMENTS

	2014 BD'000	2013 BD'000
Dividend income	**2,044**	1,494
Gain on sale of equity type instruments	**1,946**	995
Income from investment in Ijarah assets	**420**	374
Unrealised gain on equity type instruments carried at fair value through statement of income	**-**	55
	4,410	2,918

19 INCOME FROM INVESTMENT IN REAL ESTATE

	2014 BD'000	2013 BD'000
Gain on sale	**4,951**	514
Reversal of impairment / (Change)	**3,617**	(1,321)
	8,568	(807)

20 OTHER EXPENSES

	2014 BD'000	2013 BD'000
Card Centre expenses	**1,445**	1,435
Marketing and advertisement expenses	**1,124**	1,692
Premises and equipement expenses	**1,116**	1,053
Professional services	**1,018**	559
Information technology related expenses	**830**	1,019
Communication expenses	**772**	816
Board of directors sitting fees	**248**	48
Donations	**150**	150
Shari'a committee fees & remuneration	**80**	11
Board Remunerations*	**-**	300
Others	**1,719**	997
	8,502	8,080

* No provision for Board Remuneration made in 2014 as 2013 provision was not utilised.

NOTES TO THE CONSOLIDATED FINANCIAL INFORMATION
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21 PROVISION FOR IMPAIRMENT

21.1 Impairment provisions on financing assets

	Specific impairment		Collective impairment		Total	
	2014 BD'000	2013 BD'000	**2014 BD'000**	2013 BD'000	**2014 BD'000**	2013 BD'000
At 1 January	**30,672**	29,657	**4,173**	2,688	**34,845**	32,345
Charge for the year	**8,659**	8,087	**6,645**	1,485	**15,304**	9,572
Recoveries & write backs	**(7,711)**	(4,297)	**-**	-	**(7,711)**	(4,297)
	948	3,790	**6,645**	1,485	**7,593**	5,275
Amounts written off against provision	**(42)**	(2,775)	**-**	-	**(42)**	(2,775)
At 31 December	**31,578**	30,672	**10,818**	4,173	**42,396**	34,845

The above impairment provision relates to the following:

	2014 BD'000	2013 BD'000
Murabaha receivables	**25,051**	19,070
Musharaka investments	**5,632**	8,021
Ijarah Muntahia Bittamleek	**11,713**	7,754
	42,396	34,845

21.2 Impairment provisions on investments

	2014 BD'000	2013 BD'000
At 1 January	**35,096**	35,378
Charge for the year *	**6,657**	5,436
Recoveries & write backs	**(2,321)**	(25)
	4,336	5,411
Amounts written off against provision	**(4,849)**	(5,693)
Foreign currency translation changes	**(1,165)**	-
At 31 December	**33,418**	35,096

* Impairment charge includes BD 2,960 thousand impairment provision on investment in associates (2013: nil).

21.3 Impairment provisions on other assets

	2014 BD'000	2013 BD'000
At 1 January	**-**	3,609
Recoveries & write backs	**-**	(920)
Amounts written off against provision	**-**	(2,689)
	-	-

The fair value of collateral that the Group holds relating to non performing facilities at 31 December 2014 amounts to BD 65,298 thousand (31 December 2013: BD 105,892 thousand). The collateral consists of cash, securities and properties. The utilisation of the above collaterals will be on a customer by customer basis and will be limited to the customer's total exposure.

The Group has taken all the provision allocated to the non performing assets to their own capital. Hence the equity of investment accountholders was not charged for any provision for impairment.

NOTES TO THE CONSOLIDATED FINANCIAL INFORMATION
31 December 2014

22 ZAKAH

The total Zakah payable as of 31 December 2014 amounted to BD 444 thousand (2013: BD 207 thousand) of which the Bank has no Zakah payable (2013: BD nil) based on the statutory reserve, general reserve and retained earning as at 1 January 2014. The Zakah balance amounting to BD 444 thousand or 0.5 fils per share (2013: BD 207 thousand or 0.2 fils per share) is due and payable by the shareholders.

23 EARNINGS PER SHARE

Basic and diluted earnings per share is calculated by dividing the net profit or loss for the year by the weighted average number of shares during the year as follows:

	2014	2013
Profite for the year in BD'000	**9,297**	6,107
Weighted average number of shares	**936,053**	936,053
Basic and diluted earnings per share (fils)	**9.93**	6.52

Basic and diluted earnings per share are the same since the Group has not issued any instruments that would have a dilutive effect.

24 RELATED PARTY TRANSACTIONS

Related parties comprise of major shareholders, directors of the Bank, senior management, 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 Bank. The transactions with these parties were made on commercial terms.

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

	2014				
	Shareholders BD'000	**Associates and joint ventures BD'000**	**Directors and related entities BD'000**	**Senior management BD'000**	**Total BD'000**
ASSETS					
Placements with financial institutions	**-**	**4,734**	**-**	**-**	**4,734**
Financing assets	**-**	**-**	**2,339**	**-**	**2,339**
Investment in associates	**-**	**30,835**	**-**	**-**	**30,8 35**
Other assets	**-**	**-**	**64**	**194**	**258**
LIABILITIES AND EQUITY OF INVESTMENT ACCOUNTHOLDERS					
Customers' current accounts	**-**	**1,277**	**594**	**49**	**1,920**
Other liabilities	**-**	**1,928**	**-**	**-**	**1,928**
Equity of investment accountholders	**45,639**	**425**	**457**	**591**	**47,112**
INCOME					
Income from financing	**-**	**112**	**243**	**-**	**355**
Share of results of associates	**-**	**(1,550)**	**-**	**-**	**(1,550)**
Less: Return on equity of investment accountholders	**(990)**	**(7)**	**(6)**	**(21)**	**(1,024)**
EXPENSES					
Other expenses	-	-	**(328)**	**(825)**	**(1,153)**

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24 RELATED PARTY TRANSACTIONS (continued)

	2013				
	Shareholders BD'000	Associates and joint ventures BD'000	Directors and related entities BD'000	Senior management BD'000	Total BD'000
ASSETS					
Due from banks and financial institutions	-	9,481	-	-	9,481
Financing assets	-	-	2,111	44	2,155
Investment in associates	-	36,236	-	-	36,236
Other assets	-	-	-	244	244
Liabilities and Equity of investment accountholders					
Customers' current accounts	-	581	459	-	1,040
Other liabilities	-	1,644	-	-	1,644
Customers' investment accounts	-	2,373	443	-	2,816
INCOME					
Income from financing	-	173	123	-	296
Share of results of associates	-	1,197	-	-	1,197
Return on equity of investment accountholders	(281)	(10)	(9)	(26)	(326)
Expenses					
Other expenses	-	-	(358)	(895)	(1,253)

Compensation of the key management personnel is as follows:

Key management personnel includes staff at the grade of assistant general manager or above.

	2014 BD'000	2013 BD'000
Short term employee benefits	**688**	756
Other long term benefits	**137**	139
	825	895

25 RISK MANAGEMENT

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. These risks and the processes to mitigate these risks have not significantly changed from the previous year.

The Group is exposed mainly to credit, liquidity, market and operational risks.

Risk management objectives

The risk management philosophy of the Group is to identify, monitor and manage the various dimensions of risk with the objective of protecting asset values and income streams such that the interest of the Group's shareholders (and others to whom the Group owes a liability) are safeguarded, while maximising the returns intended to optimise the Group's shareholder return while maintaining it's risk exposure within self-imposed parameters.

The Group has defined its risk appetite within the parameters of its risk strategy. The Group reviews and realigns its risk appetite as per the evolving business plan of the Group with changing economic and market scenarios. The Group also assesses its tolerance for specific risk categories and its strategy to manage these risks.

NOTES TO THE CONSOLIDATED FINANCIAL INFORMATION
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25 RISK MANAGEMENT (continued)

Risk appetite of the Group is articulated in terms of the following dimensions:

1. Adequate capital level;
2. Stable profitability and growth;
3. Sufficient liquidity; and
4. Sound reputation.

Structure and Organization of the Risk Management Function

Risk Management Structure includes all levels of authorities, organizational structure, people and systems required for the effective functioning of risk management processes in the Group. The responsibilities associated with each level of the risk management structure and authorities include the following:

The Board retains ultimate responsibility and authority for all risk matters, including:

a. Establishing overall policies and procedures; and
b. Delegating authority to the Executive Committee, Credit and Investment Committee, Chief Executive Officer and further delegation to the management to approve and review.

Executive Committee (EC) comprises of three designated members of the Board of Directors. The Executive Committee is delegated authority by the Board to manage the ongoing activities of the Group. Decisions are taken by the Executive Committee either at periodic meetings or if the need arises, by circulation.

Credit and Investment Committee (CIC): As delegated by the Board of Directors and as per approved terms of reference, the Committee has been delegated with authorities and responsibilities including, approving extension or renewal of credit facilities, granting temporary excesses to customers with credit facilities approved by the Board, approving early repayments of facilities, monitoring the performance and quality of the Group's credit portfolio and overseeing the administration and effectiveness of and compliance with, the Group's credit policies through the review of such processes, reports and other information as it deems appropriate.

Risk Measurement and Reporting Systems

Based on the risk appetite, the Group has put in place various limits. These limits have been approved by the Board. Any limit breach is reported by the Risk Management Department (RMD) to the Credit Committee. The limits are reviewed and revised at least annually (or earlier if required).

a) 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.

Credit Risk Mitigation

Credit risk mitigation refers to the use of a number of techniques, such as obtaining collateral and guarantees to mitigate the credit risks that the Group is exposed to. Credit risk mitigants reduce the credit risk by allowing the Group to protect against counterparty non-performance of credit contracts through collaterals, netting agreements and guarantees.

Generally, the Group extends credit facilities only where supported by adequate tangible collateral security and/or audited financial statements. Facilities may be considered without adequate tangible collateral security when audited financial statements reveal satisfactory financial position/repayment ability and the facilities are properly structured and supported by assignments, guarantees, etc. as appropriate.

In general, personal guarantees of the partners/promoters/directors of the borrowing entity are obtained in support of credit facilities. In all cases, a statement of net worth of the guarantor is to be compiled by the Account Officer, so that adequate information is available at a future date in case the guarantees need to be enforced.

Notwithstanding the above, when facilities are extended to family owned limited liability entities, the following is normally obtained;

a. Collateral security, fully covering the exposure; or
b. Joint and several guarantees of shareholders directly involved in managing the entity as well as of shareholders owing at least 80% of the shares of the entity.

Third party guarantees in support of credit facilities are accepted only after review and approval of appropriate guarantor lines.

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25 RISK MANAGEMENT (continued)

a) Credit Risk (continued)

(i) Gross maximum exposure to credit risk

The market value of tangible collateral security is properly evaluated by the Group approved surveyors (for properties) or based on publicly available quotations. Only the amount of such security equivalent to the exposure is taken into account while considering credit facilities.

The CIC periodically reviews and approves the value of securities. It has also approved a list of acceptable securities.

The table below shows the gross maximum exposure to credit risk for the components of the consolidated statement of financial position, including credit related commitments. The figures represent gross exposure, without taking account of any collateral held or other credit enhancements.

	2014 BD'000	2013 BD'000
Cash and balances with banks and Central Bank	**43,070**	43,081
Placements with financial institutions	**68,567**	184,600
Financing assets	**438,704**	373,896
Ijarah Muntahia Bittamleek	**113,990**	98,110
Investments	**86,118**	41,705
Ijarah rental receivables	**14,065**	14,924
	764,514	756,316
Letters of credit, guarantees and acceptances	**21,535**	15,528

(ii) Risk concentrations of the maximum exposure to credit risk

Concentrations of credit risk 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 of credit risk indicate the relative sensitivity of the Group's performance to developments affecting a particular industry or geographic location. The Group seeks to manage its credit risk exposure through diversification of financing activities to avoid undue concentrations of risks with individuals or groups of customers in specific locations or businesses.

The distribution of the Group's assets, liabilities, equity of investment accountholders, commitments and contingent liabilities by geographic region and industry sector is as follows:

	Assets		Liabilities and equity of investment accountholders		Commitments and contingent liabilities	
	31 December 2014 BD'000	31 December 2013 BD'000	**31 December 2014 BD'000**	31 December 2013 BD'000	**31 December 2014 BD'000**	31 December 2013 BD'000
Geographical region						
Middle East	**867,636**	895,977	**788,901**	831,964	**22,277**	15,666
Rest of Asia	**-**	297	**913**	4	**-**	-
North America	**4,350**	1,280	**195**	183	**-**	-
Europe	**3,221**	12,740	**6,103**	27	**-**	325
	875,207	910,294	**796,112**	832,178	**22,277**	15,991
Industry sector						
Trading and manufacturing	**43,824**	77,461	**27,141**	17,045	**13,824**	7,665
Aviation	**8,241**	11,696	**17,114**	54,542	**466**	466
Real Estate	**246,215**	211,688	**15,916**	16,792	**632**	1,888
Banks and financial institutions	**119,083**	255,103	**109,928**	120,832	**2,543**	4,535
Personal / Consumer	**240,365**	237,957	**390,264**	477,706	**-**	-
Government Organization	**75,590**	47,424	**92,540**	63,232	**-**	-
Others	**141,889**	68,965	**143,209**	82,029	**4,812**	1,437
	875,207	910,294	**796,112**	832,178	**22,277**	15,991

NOTES TO THE CONSOLIDATED FINANCIAL INFORMATION
31 December 2014

25 RISK MANAGEMENT (continued)

(iii) Credit quality per class of financial assets

The credit quality of financial assets is managed by the Group using internal credit ratings. The table below shows the credit quality by class of asset, based on the Group's credit rating system. Amounts reported are gross of any provision for impairment.

	31 December 2014				
	Neither past due nor impaired				
	High grade BD'000	**Standard grade BD'000**	**Past due but not impaired BD'000**	**Individually impaired BD'000**	**Total BD'000**
Murabaha	**1,257**	**274,236**	**21,637**	**36,631**	**333,761**
Musharaka	**1,117**	**66,856**	**13,251**	**23,719**	**104,943**
Ijarah Muntahia Bittamleek	**-**	**72,234**	**6,742**	**35,014**	**113,990**
Ijarah rental receivables	**-**	**9,119**	**906**	**4,040**	**14,065**
	2,374	**422,445**	**42,536**	**99,404**	**566,759**

	31 December 2013				
	Neither past due nor impaired				
	High grade BD'000	Standard grade BD'000	Past due but not impaired BD'000	Individually impaired BD'000	Total BD'000
Murabaha	4,614	209,055	35,871	25,568	275,108
Musharaka	1,862	53,862	9,695	33,369	98,788
Ijarah Muntahia Bittamleek	-	53,542	12,275	32,293	98,110
Ijarah rental receivables	-	11,866	2,162	896	14,924
	6,476	328,325	60,003	92,126	486,930

Restructured facilities during the year amounted to BD 21,353 thousand (2013: BD 9,571 thousand), and they included amounts totalling BD nil (2013: BD 3,467 thousand) which were past due more than 90 days.

(iv) Aging analysis of past due but not impaired financing facilities per class of financial assets

2014	**Up to 30 days BD'000**	**31 to 60 days BD'000**	**61 to 90 days BD'000**	**Total BD'000**
Murabaha	**16,618**	**4,414**	**605**	**21,637**
Musharaka	**6,517**	**2,532**	**4,202**	**13,251**
Ijara Muntahia Bittamleek	**5,421**	**1,321**	**-**	**6,742**
	28,556	**8,267**	**4,807**	**41,630**
2013				
Murabaha	35,113	319	439	35,871
Musharaka	9,110	248	337	9,695
Ijara Muntahia Bittamleek	11,020	1,217	38	12,275
	55,243	1,784	814	57,841

NOTES TO THE CONSOLIDATED FINANCIAL INFORMATION

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25 RISK MANAGEMENT (continued)

b) Liquidity Risk

Liquidity risk is the risk that the Group will be unable to meet its liabilities when they fall due. Liquidity risk can be caused by market disruptions or credit downgrades which may cause certain sources of funding to cease immediately. To guard against this risk, the Group has a large customer base and assets are managed with liquidity in mind, maintaining a healthy balance of cash, cash equivalents, commodity Murabaha, Wakala receivables, credit lines and quoted investments.

The maturity profile of assets, liabilities and equity of investment accountholders at 31 December 2014 was as follows:

ASSETS	Up to 1 month BD '000	1 to 3 months BD '000	3 to 6 months BD '000	6 months to 1 year BD '000	1 to 3 years BD '000	Over 3 years BD '000	No fixed maturity BD '000	Total BD '000
Cash and balances with the banks and Central Bank	21,063	-	-	-	-	-	31,055	52,118
Placements with financial institutions	64,865	3,702	-	-	-	-	-	68,567
Financing assets	31,750	26,797	6,968	23,715	60,521	258,270	-	408,021
Ijarah Muntahia Bittamleek	14,573	13	2	7,569	11,451	68,669	-	102,277
Investments	24,760	6,933	9,129	-	8,266	53,096	21,377	123,561
Investment in associates	-	-	-	-	-	-	30,835	30,835
Investment in real estate	-	-	-	-	-	-	53,934	53,934
Ijarah rental receivables	-	-	-	14,065	-	-	-	14,065
Property and equipment	-	-	-	-	-	-	17,101	17,101
Other assets	-	-	4,728	-	-	-	-	4,728
Total assets	157,011	37,445	20,827	45,349	80,238	380,035	154,302	875,207
LIABILITIES AND EQUITY OF INVESTMENT ACCOUNTHOLDERS								
Placements from financial institutions	75,185	385	-	-	-	-	-	75,570
Customers' current accounts	137,423	-	-	-	-	-	-	137,423
Other liabilities	16,518	-	-	-	-	-	-	16,518
Equity of investment accountholders	127,278	78,299	80,252	271,858	5,931	-	2,983	566,601
Total liabilities and equity of investment accountholders	356,404	78,684	80,252	271,858	5,931	-	2,983	796,112
Liquidity gap	(199,393)	(41,239)	(59,425)	(226,509)	74,307	380,035	151,319	79,095
Cumulative liquidity gap	(199,393)	(240,632)	(300,057)	(526,566)	(452,259)	(72,224)	79,095	-

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25 RISK MANAGEMENT (continued)

b) Liquidity Risk (continued)

The maturity profile of assets, liabilities and equity of investment accountholders at 31 December 2013 was as follows:

ASSETS	Up to 1 month BD '000	1 to 3 months BD '000	3 to 6 months BD '000	6 months to 1 year BD '000	1 to 3 years BD '000	Over 3 years BD '000	No fixed maturity BD '000	Total BD '000
Cash and balances with the banks and Central Bank	18,091	-	-	-	-	-	32,740	50,831
Placements with financial institutions	157,659	17,996	8,945	-	-	-	-	184,600
Financing assets	22,985	20,087	11,049	31,781	67,804	193,099	-	346,805
Ijarah Muntahia Bittamleek	10,556	-	196	9	10,777	68,818	-	90,356
Investments	6,741	20,861	-	-	10,259	47,035	22,130	107,026
Investment in associates	-	-	-	-	-	-	36,236	36,236
Investment in real estate	-	-	-	-	-	-	58,219	58,219
Ijarah rental receivables	3,955	57	-	329	654	9,929	-	14,924
Property and equipment	-	-	-	-	-	-	17,067	17,067
Other assets	-	1,481	834	-	-	1,915	-	4,230
Total assets	219,987	60,482	21,024	32,119	89,494	320,796	166,392	910,294
LIABILITIES AND EQUITY OF INVESTMENT ACCOUNTHOLDERS								
Placements from financial institutions	79,371	7,484	8,289	-	-	-	-	95,144
Customers' current accounts	105,932	-	-	-	-	-	-	105,932
Other liabilities	13,608	-	-	-	-	-	-	13,608
Equity investment accountholders	100,094	106,212	128,470	273,981	5,850	-	2,887	617,494
Total liabilities and equity of investment accountholders	299,005	113,696	136,759	273,981	5,850	-	2,887	832,178
Liquidity gap	(79,018)	(53,214)	(115,735)	(241,862)	83,644	320,796	163,505	78,116
Cumulative liquidity gap	(79,018)	(132,232)	(247,967)	(489,829)	(406,185)	(85,389)	78,116	-

c) Market Risk

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to changes in market variables such as profit rates, equity prices, and foreign exchange rates.

(i) Profit rate risk

Profit rate risk arises from the possibility that changes in profit rates will affect future profitability or the fair values of financial instruments. The Group's management believe that the Group is not exposed to material profit rate risk as a result of mismatches of profit rate repricing of assets, liabilities and equity of investment accountholders as the repricing of assets, liabilities and equity of investment accountholders occur at similar intervals. The profit distribution to equity of investment accountholders is based on profit sharing agreements. Therefore, the Group is not subject to any significant profit rate risk.

However, the profit sharing agreements will result in displaced commercial risk when the Group's results do not allow the Group to distribute profits inline with the market rates.

NOTES TO THE CONSOLIDATED FINANCIAL INFORMATION
31 December 2014

25 RISK MANAGEMENT (continued)

(ii) Equity price risk

Equity price risk is the risk that the fair values of equities decrease as a result of changes in the levels of equity indices and the value of individual stocks. The equity price risk exposure arises from the investment portfolio. The Group manages this risk through diversification of investments in terms of geographical distribution and industry concentration.

In order to measure the risk of equity on its financial positions, the Group adopts a sensitivity analysis on its quoted equity portfolio for a 10% increase of the portfolio value with all other variables remaining constant. The effect of a similar decrease in equity prices is expected to be equal and opposite to the effect of the increase shown. Equity price risk variation as of 31 December is as follows:

	Increase in equity price %	**Sensitivity of profit or loss BD'000**	**Sensitivity of equity BD'000**
2014			
Kuwait Stock Exchange	**+10**	**-**	**139**
2013			
Bahrain Bourse	+10	10	806
Saudi Stock Exchange (TADAWUL)	+10	39	425
Oman Stock Exchange	+10	16	-
Kuwait Stock Exchange	+10	-	132
Qatar Stock Exchange	+10	-	320

As at the consolidated statement of financial position date, the Group has unquoted (equities and sukuk) of BD 104 million (31 December 2013: BD 33 million). The impact of changes in the value of these unquoted equities and sukuk and the related impact on equity will only be reflected when the financial instrument is sold or deemed to be impaired.

iii) Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Group views the Bahraini Dinar as its functional currency. The Board has set limits on positions by currency. Positions are monitored on a daily basis to ensure they are maintained within established limits.

The Group had the following significant net exposures denominated in foreign currencies as of 31 December:

	Equivalent Long (short) 2014 BD '000	Equivalent Long (short) 2013 BD '000
Currency		
Pound Sterling	**(1,149)**	(4,359)
Euro	**1,653**	(1,166)
Kuwaiti Dinars	**(11,490)**	(12,376)

As the Bahraini Dinar is pegged to the US Dollar, positions in US Dollars are not considered to represent significant currency risk.

Moreover, as the Group does not have significant exposure to other currencies, movement of the currency exchange rates against the Bahraini Dinar with other variables held constant will have an immaterial impact on the consolidated statement of income and owners' equity.d) Operational Risk

Operational risk is the risk of loss arising from system failure, human error, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to financial loss. The Group cannot expect to eliminate all operational risks, but through a control framework and by monitoring and responding to potential risks, the Group is able to manage the risks. Controls include effective segregation of duties, access, authorisation and reconciliation procedures, staff education and assessment processes, including the use of internal audit.

26 DEPOSIT PROTECTION SCHEME

"Deposits held with the Bank's Bahrain operations are covered by the regulation protecting Deposits issued by the Central Bank of Bahrain in accordance with Resolution No (34) of 2010. The scheme applies to all eligible accounts held with Bahrain offices of the Bank subject to specific exclusions, maximum total amount entitled and other regulations concerning the establishment of a Deposit Protection Scheme and a Deposit Protection Board.

NOTES TO THE CONSOLIDATED FINANCIAL INFORMATION
31 December 2014

27 SEGMENTAL INFORMATION

For management purposes, the Group is organised into three major business segments;

Corporate — Principally handling equity of corporate investment accountholders', corporate current accounts, and providing Islamic financing facilities to corporate customers.

Retail — Principally handling equity of individual retail customers' investment accountholders', retail current accounts, and providing Islamic financing facilities to individual customers.

Investment — Principally handling equity of banks' and financial institutions' investment accountholders, providing money market, trading and treasury services as well as the management of the Group's investment activities. Investment activities involve handling investments in local and international markets and investment in properties.

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 is disclosed as follows:

	31 December 2014			
	Corporate BD'000	Retail BD'000	Investment BD'000	Total BD'000
Total income	**7,955**	**21,716**	**13,180**	**42,851**
Total expenses	**(3,480)**	**(15,364)**	**(2,781)**	**(21,625)**
Provision for impairment	**(6,355)**	**(1,238)**	**(4,336)**	**(11,929)**
Profit / (loss) for the year	**(1,880)**	**5,114**	**6,063**	**9,297**
Other information				
Segment assets	**219,150**	**348,118**	**307,939**	**875,207**
Segment liabilities, and equity	**260,948**	**452,778**	**161,481**	**875,207**
	31 December 2013			
Total income	11,950	18,440	5,220	35,610
Total expenses	(3,021)	(13,878)	(2,838)	(19,737)
Provision for impairment	(3,619)	(1,656)	(4,491)	(9,766)
Profit / (loss) for the year	5,310	2,906	(2,109)	6,107
Other information				
Segment assets	205,594	287,777	416,923	910,294
Segment liabilities, and equity	298,522	433,083	178,689	910,294

The Group operates solely in the Kingdom of Bahrain and, as such, no geographical segment information is presented.

28 FINANCIAL INSTRUMENTS

Fair value hierarchy

Fair value is the amount for which an asset could be exchanged or a liability settled between knowledgeable and willing parties in an arm's length transaction.

Fair values of quoted securities / Sukuk are derived from quoted market prices in active markets, if available. For unquoted securities / Sukuk, fair value is estimated using appropriate valuation techniques. Such techniques may include using recent arm's length market transactions; reference to the current fair value of another instrument that is substantially the same; discounted cash flow analysis or other valuation models.

NOTES TO THE CONSOLIDATED FINANCIAL INFORMATION
31 December 2014

28 FINANCIAL INSTRUMENTS (continued)

The Group uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

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

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

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

The following table shows an analysis of financial instruments recorded at fair value by level of the fair value hierarchy at 31 December:

	Level 1 BD'000	Level 2 BD'000	Level 3 BD'000	Total BD'000
2014				
Investments carried at fair value through equity				
Quoted securities Equities	**1,393**	**-**	**-**	**1,393**
2013				
Investments carried at fair value through statement of income				
Quoted securities Equities	866	-	-	866
Investments carried at fair value through equity				
Quoted securities Equities	19,995	-	-	19,995
	20,861	-	-	20,861

Transfers between Level 1, Level 2 and Level 3

During the year ended 31 December 2013 there were no transfers between Level 1 and Level 2, and no transfers into or out of Level 3.

The carrying values of other financial assets and liabilities are not significantly different from their fair values at 31 December 2014, except for the Group's investments in Sukuk held at amortised cost amounting to BD 81,834 thousand (2013: BD 38,365 thousand) with fair values amounting to BD 81,181 thousand (2013: BD 40,033 thousand).

29 EARNINGS AND EXPENSES PROHIBITED BY SHARI'A

The Group is committed to avoid recognising any income generated from non-Islamic sources. Accordingly, all non-Islamic income is credited to a Qard fund account where the Group uses these funds for various social welfare activities. The movements in these funds is shown in statement of sources and uses of good faith Qard fund. The non-Islamic income includes the penalties charged on late repayments for Islamic facilities.

30 SHARI'A SUPERVISORY BOARD

The Group's Shari'a Supervisory Board consists of three Islamic scholars who review the Group's compliance with general Shari'a principles and specific Fatwas, rulings and guidelines issued. 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.

31 SOCIAL RESPONSIBILITY

The Group discharges its social responsibilities through Zakah and charity fund's expenditures and donations to good faith Qard fund for marriage, refurbishment, medical treatments, etc.

32 COMPARATIVE FIGURES

Certain of the prior year's figures have been reclassified to conform to the presentation adopted in the current year. Such reclassification did not affect previously reported profit or owners' equity.

BASEL II, PILLAR III DISCLOSURES

CONTENTS

BASEL II, PILLAR III DISCLOSURES

31 December 2014

1 Background

The Public Disclosures under this section have been prepared in accordance with the Central Bank of Bahrain ("CBB") requirements outlined in its Public Disclosure Module ("PD"), Section PD-1: Annual Disclosure requirements, CBB Rule Book, Volume II for Islamic Banks. Rules concerning the disclosures under this section are applicable to Bahrain Islamic Bank B.S.C. (the "Bank") being a locally incorporated Bank with a retail banking license, and its subsidiaries together known as (the "Group").

The Board of Directors seeks to optimise the Group's performance by enabling the various Group business units to realise the Group's business strategy and meet agreed business performance targets by operating within the agreed capital and risk parameters and the Group risk policy framework.

2 Capital Adequacy

The primary objectives of the Group's capital management are to ensure that the Group complies with externally imposed capital requirements and the Group maintains strong credit ratings and healthy capital ratios in order to support its business and to maximise shareholders' value.

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

The Group's capital structure is primarily made up of its paid-up capital, and including reserves. From a regulatory perspective, the significant amount of the Group's capital is in Tier 1 form as defined by the CBB, i.e., most of the capital is of a permanent nature.

The Group's capital adequacy policy is to maintain a strong capital base to support the development and growth of the business. Current and future capital requirements are determined on the basis of financing facilities growth expectations for each business group, expected growth in off-balance sheet facilities, and future sources and uses of funds. To assess its capital adequacy requirements in accordance with CBB requirements, the Group adopts the Standardised Approach for its Credit Risk, Basic Indicator Approach for its Operational Risk and Standardised Measurement Approach for its Market Risk. All assets funded by profit sharing investment accounts are subject to Board approval.

All transfer of funds or regulatory capital within the Group is carried out after proper approval process.

As part of the risk management practice, the Group has already implemented Sunguard system to be Basel II compliant as prescribed by CBB.

For the purposes of guidance every table was cross referenced with the relevant paragraph number of the Central Bank of Bahrain's Public Disclosures Module.

BASEL II, PILLAR III DISCLOSURES

31 December 2014

2 Capital Adequacy (continued)

Table – 1. Capital Structure (PD-1.3.12, 1.3.13, 1.3.14 and 1.3.15)

The following table summarises the eligible capital as of 31 December 2014 after deductions for Capital Adequacy Ratio (CAR) calculation:

	Tier 1 BD'000	Tier 2 BD'000
Components of capital		
Issued and fully paid ordinary shares	93,404	-
General reserves	1,000	-
Legal / statutory reserves	10,879	-
Accumulated losses brought forward	(43,958)	-
Less:		
Unrealised gross losses arising from fair valuing equity securities	(316)	-
Tier 1 Capital before PCD deductions	**61,009**	-
Net Profit for the year		9,297
Asset revaluation reserve - Property and equipment (45% only)		3,312
Unrealised gains arising from fair valuing equities (45% only)		484
Profit Equalization Reserve		395
Investment risk reserve		103
Collective impairment loss provision		6,067
Tier 2 Capital before PCD deductions		**19,658**
Total available capital		**80,667**
Deductions		
Significant minority investments in banking, securities and other financial entities unless pro-rata consolidated	-	-
Investment in insurance entity greater than or equal to 20%	(847)	(847)
Total Deductions	(847)	(847)
Tier 1 and Tier 2 eligible capital before additional deduction	60,162	18,811
Additional deduction from Tier 1 to absorb deficiency in Tier 2	**(327)**	**(327)**
Tier 1 and Tier 2 eligible capital	**59,835**	**18,484**
Aggregation	**14,892**	**1,238**
TOTAL ELIGIBLE CAPITAL	**74,727**	**19,722**

	Amount of exposures BD'000
Total Credit Risk Weighted Assets	532,703
Total Market Risk Weighted Assets	15,769
Total Operational Risk Weighted Assets	56,583
TOTAL REGULATORY RISK WEIGHTED ASSETS	**605,055**
CAPITAL ADEQUACY RATIO	**15.61**
Minimum requirement	12%

BASEL II, PILLAR III DISCLOSURES
31 December 2014

2 Capital Adequacy (continued)

Table – 2. Capital requirements by type of Islamic financing contracts (PD-1.3.17)

The following table summarises the amount of exposures as of 31 December 2014 (gross of deductions) subject to standardised approach of credit risk and related capital requirements by type of Islamic financing contracts:

	Risk Weighted Assets BD'000	Capital requirements BD'000
Type of Islamic Financing		
Placements with financial institutions	10,192	1,223
Financing assets	181,108	21,733
Investments	92,759	11,131
Ijarah muntahia bittamleek*	45,397	5,448
Ijarah rental receivables	6,698	804
	336,153	40,337
Other credit exposures	172,118	20,654
	508,271	60,992

*The risk weighted assets have been allocated on a pro-rata basis due to system limitation.

Table – 3. Capital requirements for market risk (PD-1.3.18)

The following table summarises the amount of exposures as of 31 December 2014 subject to standardised approach of market risk and related capital requirements:

Market Risk - Standardised Approach	Foreign exchange risk (BD'000)
	1,066
Total of Market Risk - Standardised Approach	**1,066**
Multiplier	12.5
RWE for CAR Calculation (BD'000)	13,325
Total Market Risk Exposures (BD'000)	**13,325**
Total Market Risk Exposures - Capital Requirement (BD'000)	**1,599**

Table – 4. Capital requirements for operational risk (PD-1.3.30 (a & b) and PD-1.3.19)

The following table summarises the amount of exposures as of 31 December 2014 subject to basic indicator approach of operational risk and related capital requirements:

Indicators of operational risk	
Average Gross income (BD'000)	28,004
Multiplier	12.5
	350,046
Eligible Portion for the purpose of the calculation	15%
Total Operational Risk Exposure (BD'000)	52,507
Total Operational Risk Exposures - Capital Requirement (BD'000)	6,301

Table – 5. Capital Adequacy Ratios (PD-1.3.20)

The following are Capital Adequacy Ratios as of 31 December 2014 for total capital and Tier 1 capital:

	Total capital ratio	**Tier 1 capital ratio**
Top consolidated level	**15.61**	12.34

BASEL II, PILLAR III DISCLOSURES
31 December 2014

3 Risk Management

3.1. Bank-wide Risk Management Objectives

The risk management philosophy of the Group is to identify, capture, monitor and manage the various dimensions of risk with the objective of protecting asset values and income streams such that the interest of the Group's shareholders (and others to whom the Group owes a liability) are safeguarded, while maximising the returns intended to optimise the Group's shareholder return while maintaining it's risk exposure within self-imposed parameters.

The Group has defined its risk appetite within the parameters of its Risk Strategy. The Group reviews and realigns its risk appetite as per the evolving business plan of the Group with changing economic and market scenarios. The Group also assesses its tolerance for specific risk categories and its strategy to manage these risks.

In addition to satisfying the minimum regulatory capital requirements of CBB, the Group seeks to constantly identify and quantify, to the extent possible, the various risks that are inherent in the normal course of its business and maintain appropriate internal capital levels as per the ICAAP framework. The main objective of the Group's ICAAP is to ensure that adequate capital is retained at all times to support the risks the Group undertakes in the course of its business.

The Group has an established internal capital adequacy assessment process (ICAAP) as per the requirements under Pillar III of Basel II. ICAAP prescribed measures are designed to ensure appropriate identification, measurement, aggregation and monitoring of the Group's risk. It also defines an appropriate level of internal capital in relation to the Group's overall risk profile and business plan.

3.2. Strategies, Processes, and Internal Controls

3.2.1 Group's risk strategy

Capital Management policies and Risk Charter define the Group's risk strategy. Comprehensive Risk Management Policy Framework is approved by the Board. These are also supported by appropriate limit structures. These policies provide an enterprise-wide integrated risk management framework in the Group.

The risk charter identifies risk objectives, policies, strategies, and risk governance both at the Board and management level. The capital management policy is aimed at ensuring financial stability by allocating enough capital to cover unexpected losses.

Limit structures serve as key components in articulating risk strategy in quantifiable risk appetite. They are further supported by a comprehensive framework for various risk silos with its own policies and methodology documents. In addition, the Group is in the process of implementing various risk systems to help quantify not just the regulatory capital but also the economic capital allocated to various portfolios.

The Group is exposed to various types of risk, such as market, credit, profit rate, liquidity and operational, all of which require comprehensive controls and ongoing oversight. The risk management framework summarises the spirit behind Basel II, which includes management oversight and control, risk culture and ownership, risk recognition and assessment, control activities and segregation of duties, adequate information and communication channels, monitoring risk management activities and correcting deficiencies.

3.2.2 Credit risk

The Group manages its credit risk exposure by evaluating each new product/activity with respect to the credit risk introduced by it. The Group has established a limit structure to avoid concentration of risks for counterparty, sector, and geography.

3.2.3 Market risk

The Group proactively measures and monitors the market risk in its portfolio using appropriate measurement techniques such as limits on its foreign exchange open positions although they are insignificant. The Group regularly carries out stress testing to assess the impact of adverse market conditions on its market risk sensitive portfolio.

The Group has established a limit structure to monitor and control the market risk in its equity type instruments portfolio. These limits include maximum Stop-loss limits, position limits, VaR limits and maturity limits.

3.2.4 Operational risk

The Group has implemented SunGuard's Operational Risk Management system ‹SWORD' for recording the potential risks, controls, and events on a continuous basis. As part of implementation, the Group has carried out Risk Control Self Assessment ("RCSA") exercise on a regular basis. The system also measures the Operational risk appetite based on the predefined limits/thresholds.

The Group has established a clear segregation of duties, through documentation and implementation of policies and procedures. This ensures objectivity, security, and avoids conflicts of interest. Maker checker concept and dual eye principles are applied across the Group, where possible.

3.2.5 Equity price risk

Equity price risk is the risk that the fair values of equities decrease as a result of changes in the levels of equity indices and the value of individual stocks. The equity price risk exposure arises from the investment portfolio. The Group manages this risk through diversification of investments in terms of geographical distribution and industry concentration.

BASEL II, PILLAR III DISCLOSURES

31 December 2014

3 Risk Management (continued)

3.2.6 Profit rate risk

Profit rate risk arises from the possibility that changes in profit rates will affect future profitability or the fair values of financial instruments. The Group's management believes that the Group is not exposed to material profit rate risk as a result of mismatches of profit rate repricing of assets, liabilities, and equity of investment accountholders. The profit distribution to investment accountholders is based on profit sharing agreements. Therefore, the Group is not subject to any significant profit rate risk.

However, the profit sharing agreements will result in displaced commercial risk when the Group's results do not allow the Group to distribute profits inline with market rates.

3.2.7 Displaced Commercial Risk

Displaced commercial risk ("DCR") refers to the market pressure to pay returns that exceeds the rate that has been earned on the assets financed by the liabilities, when the return on assets is under performing as compared with competitor's rates.

The Group manages its displaced commercial risk by placing gap limits between the returns paid to investors and market returns.

The Group manages its displaced commercial risk as outlined in the Risk Charter of the Group. The Group may forego its fee in case displaced commercial risk arises. The Group benchmarks its rates with other leading banks in the market.

All the above strategies used have been effective throughout the reporting year.

3.3 Structure and Organisation of Risk Management Function

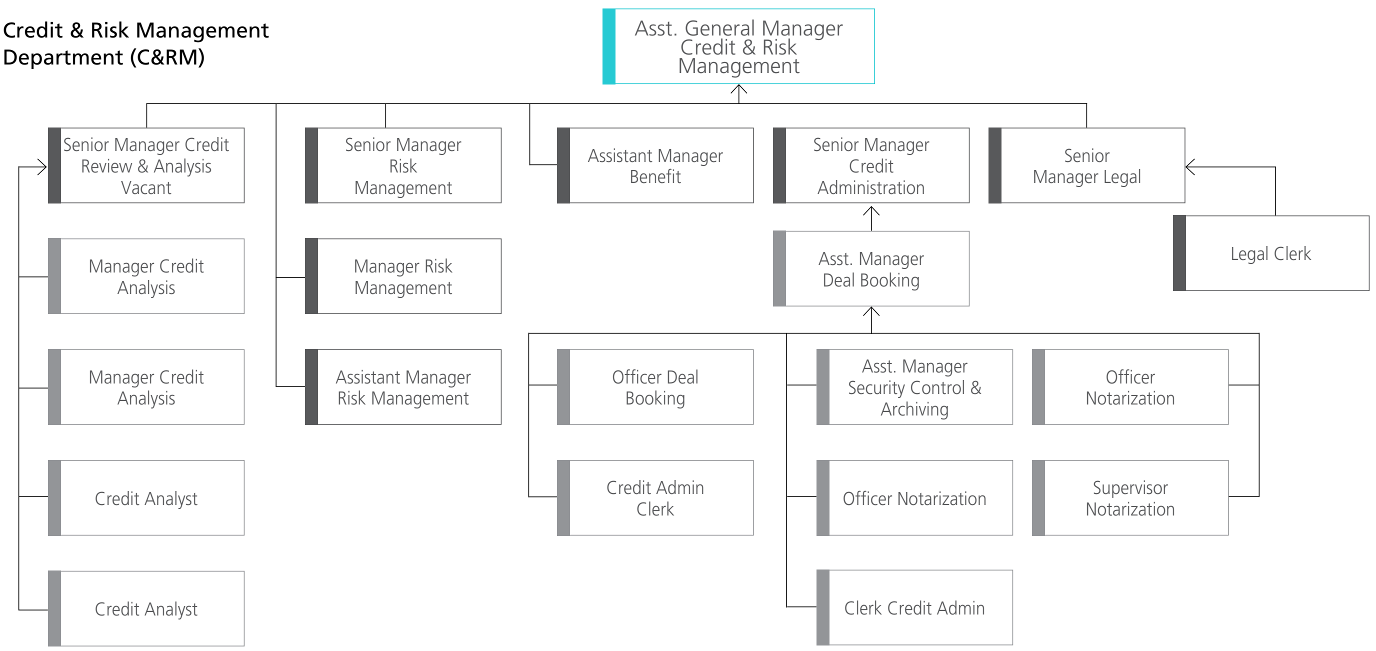
Risk Management Structure includes all levels of authorities (including Board level Risk committee), organisational structure, people, and systems required for the smooth functioning of risk management processes in the Group. The responsibilities associated with each level of risk management structure and authorities include the following:

The Board retains ultimate responsibility and authority for all risk matters, including:

a Establishing overall policies and procedures, and

b. Delegating authority to Executive Committee, Credit Committee, the Chief Executive Officer and further delegation to management to approve and review.

Credit & Risk Management Department (C&RM)



3.4 Risk Measurement and Reporting Systems

Based on risk appetite of the Group, the Group has put in place various limits. These limits have been approved by the Board of Directors. Any limit breaches are reported to the respective senior management committees and the Board by the Credit and Risk Management Department ("CRMD"). The limits are reviewed and revised at least on an annual basis or when is deemed required.

The Group has developed a risk measurement and reporting system that generates various types of reports which has enhanced the monitoring process of the Group.

BASEL II, PILLAR III DISCLOSURES
31 December 2014

3 Risk Management (continued)

3.5 Credit Risk

3.5.1 Introduction

Credit risk is the risk of financial loss if a customer or counterparty fails to meet an obligation under a contract. It arises principally from lending and investment activities. The Group controls credit risk by monitoring credit exposures, and continually assessing the creditworthiness of counterparties. Financing contracts are mostly secured by collateral in the form of mortgage financed or other tangible securities.

The Group manages and controls credit risk by setting limits on the amount of risk it is willing to accept in terms of counterparties, product types, geographical area, and industry sector. The Group has established a credit quality review process to provide early identification of possible changes in the creditworthiness of counterparties, including regular collateral revisions. Counterparty limits are established by the use of a credit risk classification system, which assigns each counterparty a risk rating. Risk ratings are subject to regular revision by the Credit Review and Analysis Department ("CR&AD"). Any changes to the Credit Risk Policy will be approved by the Board.

All credit proposals undergo a comprehensive risk assessment examining the customer's financial condition, trading performance, nature of the business, quality of management, and market position, etc. In addition, the Group's internal risk rating model scores these quantitative and qualitative factors. The credit approval decision is then made and terms and conditions are set.

Exposure limits are based on the aggregate exposure to counterparty and any connected entities across the Group. Corporate contracts/ facilities are reviewed on an annual basis by CR&AD.

3.5.2 Types of credit risk

Financing contracts mainly comprise due from banks and financial institutions, Murabaha receivables, Musharaka investments, and Ijarah muntahia bittamleek.

Due from banks and financial institutions

Due from banks and financial institutions comprise commodity murabaha receivables and wakala receivables.

Murabaha receivables

The Group finances these transactions through buying the commodity which represents the object of the Murabaha contract and then reselling this commodity to the Murabeh (beneficiary) at a profit. The sale price (cost plus profit margin) is repaid in installments by the Murabeh over the agreed period. The transactions are secured at times by the object of the Murabaha contract (in case of real estate finance) and other times by a total collateral package securing the facilities given to the Murabeh.

Musharaka investments

Musharaka is a form of partnership between the Group and its clients whereby each party contributes to the capital of partnership in equal or varying degrees to establish a new project or share in an existing one, whereby each of the parties becomes an owner of the capital on a permanent or declining basis. Profits are shared in an agreed ratio, but losses are shared in proportion to the amount of capital contributed.

Ijarah Muntahia Bittamleek

The legal title of the assets under Ijarah muntahia bittamleek only passes to the lessee at the end of the Ijarah term, through gift, consideration, or gradual sale, provided that all Ijarah instalments are settled.

3.5.3 Past Due and impaired Islamic financing

The Group defines non-performing facilities as the facilities that are overdue for a period of 90 days or more. These exposures are placed on a non-accrual status with income being recognised to the extent that it is actually received. It is the Group's policy that when an exposure is overdue for a period of 90 days or more, the whole financing facility extended is considered as non performing, not only the overdue instalments/payments.

As a policy the Group places on a non-accrual basis any facility where there is reasonable doubt about the collectability of the receivable, irrespective of whether the customer concerned is currently in arrears or not.

3.5.4 External credit assessment institutions

The Group relies on external ratings for rated corporate customers and counterparties. The Group uses Standard & Poor's, Fitch, Moody's and Capital Intelligence to provide ratings for such counterparties. In case of unrated counterparties, the Group will assess the credit risk on the basis of defined parameters. These ratings are used for risk assessment and calculation of risk weighted equivalents.

3.5.5 Definition of Geographical distribution

The geographic distribution of the credit exposures is monitored on an ongoing basis by Group's Risk Management Department and reported to the Board on a quarterly basis. The Group's classification of geographical area is according to its business needs and the distribution of its portfolios.

BASEL II, PILLAR III DISCLOSURES
31 December 2014

3 Risk Management (continued)

3.5.6 Concentration risk

Concentration risk is the credit risk stemming from not having a well diversified credit portfolio, i.e. being overexposed to a single customer, industry sector or geographic region. As per CBB's single obligor regulations, banks incorporated in Bahrain are required to obtain the CBB's prior approval for any planned exposure to a single counterparty, or group of connected counterparties, exceeding 15% of the regulatory capital base.

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.

3.5.7 Credit risk mitigation

Credit risk mitigation refers to the use of a number of techniques, like collaterals and guarantees to mitigate the credit risks that the Group is exposed to. Credit risk mitigants reduce the credit risk by allowing the Group to protect against counterparty non-performance of credit contracts through collaterals, netting agreements, and guarantees.

Generally, the Group extends credit facilities only where supported by adequate tangible collateral security and/or audited financial statements. Facilities may be considered without adequate tangible collateral security, when audited financial statements reveal satisfactory financial position/repayment ability and the facilities are properly structured and supported by assignments, guarantees, etc. as appropriate.

In general, personal guarantees of the partners/promoters/directors of the borrowing entity are obtained in support of credit facilities. In all cases, a statement of net worth of the guarantor is to be compiled by the Account Officer, so that adequate information is available at a future date in case the guarantees need to be enforced.

The market value of tangible collateral security are properly evaluated by the Group approved valuers (for properties) or based on publicly available quotations. Only the Loan-able value of such security is taken into account while considering credit facilities.

From time to time, the Credit and Investment Committee reviews and approves the loan-able value of securities. It has also approved a list of acceptable securities.

The majority of the Group's current credit portfolio is secured through mortgage of commercial real estate properties. The Group may dispose off the assets as a last resort after carrying out due legal process.

3.5.7.1 General policy guidelines of collateral management

Acceptable Collaterals: The Group has developed guidelines for acceptable collaterals. Assets offered by customers must meet the following criteria to qualify as acceptable collateral:

a. Assets must be maintaining their value, at the level prevalent at inception, until maturity date of the facility granted;

b. Such assets should be easily convertible into cash, if required (liquidity);

c. There should be a reasonable market for the assets (marketability); and

d. The Group should be able to enforce its rights over the asset if necessary (enforceability).

Ownership: Prior to valuation or further follow up on the offered collateral, Credit Administration ensures satisfactory evidence of the borrower's ownership of the assets.

Valuation: All assets offered as collateral are valued by an appropriate source either in-house (through another department in the Group) or by an external appraiser (real estate related collateral). The Group maintains a list of independent appraisers, approved by management.

a. **Valuation of shares and goods:** Where competent staff is available within the Group, the valuation is conducted in-house. The Group performs in-house valuation on the following types of securities:
   - Pledge of shares of local companies;
   - Pledge of international marketable shares and securities; and
   - Pledge and hypothecation of goods.

   International shares are valued at the quotes available from stock exchanges, periodicals, etc.

b. **Valuation of real estate and others:** Besides assets mentioned above the valuation of following securities are also conducted:
   - Real Estate;
   - Equipment and machinery; and
   - Precious metals and jewellers.

The Credit Administration requests the concerned department to arrange for the valuation from approved valuators.

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3 Risk Management (continued)

3.5 Credit Risk (continued)

The following additional guidelines are also followed by the Group:

a. No facility should be disbursed until credit documentation is properly signed and security/guarantees required have been signed and registered, where required. Exceptional cases can be considered by sanctioning authorities; and

b. All documents received as security or support for credit facilities will be lodged in the safe custody through the Credit Administration and should be kept under dual control. Group must ascertain that collateral providers are authorised and acting within their capacity.

3.5.7.2 Guarantees

In cases where a letter of guarantee from parent company or a third party is accepted as credit risk mitigants, the Group ensures that all guarantees are irrevocable, legal opinion has been obtained from a legal counsellor domiciled in the country of guarantor (overseas) regarding the enforceability of the guarantee, if the guarantor / prime obligor is domiciled outside Bahrain and all guarantees should be valid until full settlement of the facilities. Also no maturity (negative) mismatch is permissible between the guarantee and exposure.

3.5.7.3 Custody / collateral management

The assets, or title to the asset, will be maintained in the Group's custody or with custodian approved by the Group. The Credit Administration will obtain confirmation of the assets held with each custodian on an annual basis.

The release of collateral without full repayment of all related financial obligations requires authorisation of the same level that originally approved and sanctioned the facility. Substitution of collateral is permitted if the new collateral would further minimise the Group's risk exposure.

When collateral is released to the customer, the Head of Credit Administration obtains and maintains in his records acknowledgement of receipt from the customer or his/her authorised representative.

3.5.8 Counterparty credit risk

The Group has adopted the Standardised Approach to allocate capital for counterparty credit risk. The Group has put in place an internal counterparty limit structure which is based on internal / external ratings for different types of counterparties. The Group has also set concentration limits as a percentage of its capital based on internal and external grades. In case of a counterparty rating downgrade / deterioration, the Group may require further collateral or advise the counterparty to reduce its exposure on a case by case basis.

3.5.8.1 Exposure

The measure of exposure reflects the maximum loss that the Group may suffer in case counterparty fails to fulfil its commitments. Exposure shall always be calculated on the basis of approved limits or actual outstanding exposure (Financing facilities, Investments or others), whichever is higher.

3.5.8.2 Counterparty

A counterparty is defined as an obligor (individual/company/other legal entity), a guarantor of an obligor, or a person receiving funds from the Group, the issuer of a security in case of a security held by the Group, or a party with whom a contract is made by the Group for financial transactions.

3.5.8.3 Group exposure

Group exposure is defined as the total exposure to all counterparties closely related or connected to each other. For this purpose, a Group is two or more counterparties related in such a way that financial soundness of one may affect the financial soundness of the other(s) and one of them has a direct or indirect control over the other(s).

3.5.8.4 Connected counterparties

Connected counterparties are companies or individuals connected with the Group or its subsidiaries and associated companies (whether such association is due to control or shareholding or otherwise), Directors and their associates (whether such association is due to control, family links or otherwise), members of the Shari'a Supervisory Board, management and other staff, and shareholders holding more than 10% or more of the equity voting rights in the Group.

3.5.8.5 Large exposure

Large exposure is any exposure whether direct, indirect, or funded by equity of investment accountholders to a counterparty or a group of closely related counterparties which is greater than or equal to 10% of the Group's capital base.

Prior written approval from the CBB is required in the following cases:

a. If any counterparty (single/group) exposure exceeds 15% of Group's Capital Base; and

b. If any facility (new/extended) to an employee is equal or above BD100,000 (or equivalent).

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31 December 2014

3 Risk Management (continued)

3.5 Credit Risk (continued)

3.5.8.6 Maximum exposure
The Group has set an internal maximum exposure limit in the light of CBB guidelines.

3.5.8.7 Reporting
The Group reports large counterparty exposures (as defined above) to CBB on periodic basis. The Group reports the exposures on a gross basis without any set-off. However, debit balances on accounts may be offset against credit balances where both are related to the same counterparty, provided the Group has a legally enforceable right to do so.

3.5.8.8 Other matters
As a Group's strategy, exposure to connected counterparties may be undertaken only when negotiated and agreed on an arm's length basis.

The Group shall not assume any exposure to its external auditors.

3.5.9 Related party transactions
The disclosure relating to related party transactions has been made in the consolidated financial statements as of 31 December 2014. All related party transactions have been made on arm's length basis.

3.5 Credit Risk
Table – 6. Credit Risk Exposure (PD-1.3.23(a))
The following table summarises the amount of gross funded and unfunded credit exposure as of 31 December 2014 and average gross funded and unfunded exposures over the year ended 31 December 2014 allocated to own capital and current account and profit sharing investment account (PSIA):

	Own Capital and Current Account		Profit Sharing Investment Account	
	Total gross credit exposure	*Average gross credit exposure over the year BD'000	Total gross credit exposure BD'000	*Average gross credit exposure over the year BD'000
Funded				
Cash and balances with banks and central Bank	21,063	25,590	31,055	32,225
Placements with financial institutions	17,362	24,891	51,205	73,409
Financing assets	103,317	97,965	304,704	288,920
Investments securities	59,474	60,522	64,087	56,568
Ijarah muntahia bittamleek	25,898	24,136	76,379	71,184
Ijarah rental receivables	3,561	3,761	10,504	11,092
Investment in associates	30,835	36,040	-	-
Investment in real estate	53,934	54,016	-	-
Property and equipment	17,101	17,084	-	-
Other assets	4,728	4,016	-	-
Unfunded				
Commitments and contingent liabilities	22,277	18,653	-	-
Total	**359,550**	**366,674**	**537,934**	**533,398**

*Average balances are computed based on month end balances.

BASEL II, PILLAR III DISCLOSURES

31 December 2014

3 Risk Management (continued)

3.5 Credit Risk (continued)

Table – 7. Credit Risk – Geographic Breakdown (PD-1.3.23(b))

The following table summarises the geographic distribution of exposures as of 31 December 2014, broken down into significant areas by major types of credit exposure:

	Own Capital and Current Account* Geographic area					Profit Sharing Investment Account* Geographic area				
	North America BD'000	Europe BD'000	Middle East BD'000	Rest of Asia BD'000	Total BD'000	North America BD'000	Europe BD'000	Middle East BD'000	Rest of Asia BD'000	Total BD'000
Cash and balances with banks and central Bank	4,350	153	16,560	-	21,063	-	-	31,055	-	31,055
Placements with financial institutions	-	-	17,362	-	17,362	-	-	51,205	-	51,205
Financing assets	-	-	103,317	-	103,317	-	-	304,704	-	304,704
Investments securities	-	967	58,507	-	59,474	-	2,850	61,237	-	64,087
Ijarah muntahia bittamleek	-	-	25,898	-	25,898	-	-	76,379	-	76,379
Ijarah rental receivables	-	-	3,561	-	3,561	-	-	10,504	-	10,504
Investment in associates	-	-	30,835	-	30,835	-	-	-	-	-
Investment real estate	-	-	53,934	-	53,934	-	-	-	-	-
Property and equipment	-	-	17,101	-	17,101	-	-	-	-	
Other assets	-	-	4,728	-	4,728	-	-	-	-	-
Total	**4,350**	**1,120**	**331,803**	**-**	**337,273**	**-**	**2,850**	**535,084**	**-**	**537,934**

* Geographical distribution of exposure into significant areas by major type of credit exposure is based on counterparty's country of incorporation.

Table – 8. Credit Risk – Industry Sector Breakdown (own capital and current account) (PD-1.3.23(c))

The following table summarises the distribution of funded and unfunded exposures as of 31 December 2014 by industry, broken down into major types of credit exposure:

	Profit Sharing Investment Account Industry Sector							
	Trading and Manufacturing BD'000	Banks and Financial Institutions BD'000	Real Estate BD'000	Aviation BD'000	Personal & Consumer Finance BD'000	Governmental Organisation BD'000	Others BD'000	Total BD'000
Funded								
Cash and balances with banks and central Bank	-	16,768	-	-	-	4,295	-	21,063
Placements with Financial institutions	-	17,362	-	-	-	-	-	17,362
Financing assets	9,356	239	20,753	10	51,381	601	20,977	103,317
Investments securities	-	13,349	31,869	-	-	9,588	4,668	59,474
Ijarah muntahia bittamleek	1,227	74	11,962	1,623	11,012	-	-	25,898
Ijarah rental receivables	514	1	1,775	454	647	-	170	3,561
Investment in associates	-	7,989	10,331	-	-	-	12,515	30,835
Investment real estate	-	-	53,934	-	-	-	-	53,934
Property and equipment	-	-	-	-	-	-	17,101	17,101
Other assets	-	1,907	-	-	1,167	-	1,654	4,728
Unfunded								
Commitments and contingent liabilities	13,824	2,543	632	466	-	-	4,812	22,277
Total	**24,921**	**60,232**	**131,256**	**2,553**	**64,207**	**14,484**	**61,897**	**359,550**

BASEL II, PILLAR III DISCLOSURES

31 December 2014

3 Risk Management (continued)

3.5 Credit Risk (continued)

Table – 9. Credit Risk – Industry Sector Breakdown (profit sharing investment account) (PD-1.3.23(c))

The following table summarises the distribution of funded and unfunded exposures as of 31 December 2014 by industry, broken down into major types of credit exposure:

	Profit Sharing Investment Account Industry Sector							
	Trading and Manufacturing BD'000	**Banks and Financial Institutions BD'000**	**Real Estate BD'000**	**Aviation BD'000**	**Personal & Consumer Finance BD'000**	**Governmental Organisation BD'000**	**Others BD'000**	**Total BD'000**
Funded								
Cash and balances with banks and central Bank	-	-	-	-	-	31,055	-	**31,055**
Placement with financial institutions	-	51,205	-	-	-	-	-	**51,205**
Financing assets	27,594	705	61,206	31	151,535	1,773	61,860	**304,704**
Investment securities	-	9,261	13,871	-	-	28,277	12,678	**64,087**
Ijarah muntahiah bittanleek	3,618	218	35,277	4,786	32,480	-	-	**76,379**
Ijarah rental receivables	1,515	4	5,235	1,337	1,910	-	503	**10,504**
Investment in associates	-	-	-	-	-	-	-	-
Investment in real estates	-	-	-	-	-	-	-	-
Property and equipment	-	-	-	-	-	-	-	-
Other assets	-	-	-	-	-	-	-	-
Total	32,727	61,393	115,589	6,154	185,925	61,105	75,041	537,934

Table – 10. Credit Risk – Financing Facilities to Highly Leveraged or Other High Risk Counterparties (PD-1.3.23(e))

The following balances represent the financing facilities to highly leveraged or other high risk counterparties as of 31 December 2014:

	Own Capital and Current Account BD'000	**Profit Sharing Investment Account BD'000**	**Total BD'000**
Counterparties	123	364	487
Counterparty # 1	**123**	**364**	**487**

Table – 11. Credit Risk – Concentration of Risk (PD-1.3.23(f))

The following balances represent the concentration of risk to individual counterparties as of 31 December 2014:

	Own capital and current account BD'000	**Profit Sharing Investment Account BD'000**	**Total BD'000**
Counterparties	12,514	-	12,514
Counterparty #1	**12,514**	-	**12,514**

BASEL II, PILLAR III DISCLOSURES

31 December 2014

3 Risk Management (continued)

3.5 Credit Risk (continued)

Table – 12. Credit Risk – Residual Contractual Maturity Breakdown (Own Capital and Current Account) (PD-1.3.23(g) PD-1.3.38)

The following table summarises the residual contractual maturity of own capital and current account breakdown of the whole credit portfolio as of 31 December 2014, broken down by major types of credit exposure:

	Own Capital and Current Account										
	Up to One months BD'000	1-3 months BD'000	3-6 months BD'000	6-12 months BD'000	1-3 years BD'000	3-5 years BD'000	5-10 years BD'000	10-20 years BD'000	Over 20 years* BD'000	No fixed maturity BD'000	Total BD'000
Assets											
Cash and balances with banks and central Bank	21,063	-	-	-	-	-	-	-	-	-	21,063
Placements with financial institutions	16,425	937	-	-	-	-	-	-	-	-	17,362
Financing assets	4,758	3,386	1,629	8,301	17,478	22,452	36,460	5,831	3,022	-	103,317
Investments securities	5,235	2,411	2,312	-	2,093	4,565	41,403	-	1,455	-	59,474
Ijarah muntahia bittamleek	1,756	-	-	1,615	892	1,538	4,071	7,581	8,445	-	25,898
Ijarah rental receivables	94	-	2	158	464	414	883	1,000	546	-	3,561
Investment in associates	-	-	-	-	-	-	-	-	30,835	-	30,835
Investment real estate	-	-	-	-	-	-	-	-	-	53,934	53,934
Property and equipment	-	-	-	-	-	-	-	-	-	17,101	17,101
Other assets	893	1,177	-	-	2,658	-	-	-	-	-	4,728
Total Assets	**50,224**	**7,911**	**3,943**	**10,074**	**23,585**	**28,969**	**82,817**	**14,412**	**44,303**	**71,035**	**337,273**

* All non performing facilities have been classified as over 20 years.

Table – 13. Credit Risk – Residual Contractual Maturity Breakdown (Profit Sharing Investment Account) (PD-1.3.23(g) PD-1.3.38)

The following table summarises the residual contractual maturity of profit sharing investment account breakdown of the whole credit portfolio as of 31 December 2014, broken down by major types of credit exposure:

	Profit Sharing Investment Account										
	Up to One months BD'000	1-3 months BD'000	3-6 months BD'000	6-12 months BD'000	1-3 years BD'000	3-5 years BD'000	5-10 years BD'000	10-20 years BD'000	Over 20 years* BD'000	No fixed maturity BD'000	Total BD'000
Assets											
Cash and balances with bank-sand central Bank	-	-	-	-	-	-	-	-	-	31,055	31,055
Placements with financial institutions	48,441	2,764	-	-	-	-	-	-	-	-	51,205
Financing assets	14,032	9,982	4,806	24,482	51,546	66,217	107,529	17,197	8,913	-	304,704
Investments securities	15,439	7,112	6,818	-	6,173	13,463	10,795	-	4,287	-	64,087
Ijarah muntahia bittamleek	5,180	-	-	4,764	2,631	4,535	12,005	22,358	24,906	-	76,379
Ijarah rental receivables	277	-	6	466	1,368	1,220	2,605	2,951	1,611	-	10,504
Total Assets	**83,369**	**19,858**	**11,630**	**29,712**	**61,718**	**85,435**	**132,934**	**42,506**	**39,717**	**31,055**	**537,934**

* All non performing facilities have been classified as over 20 years.

BASEL II, PILLAR III DISCLOSURES
31 December 2014

3 Risk Management (continued)

3.5 Credit Risk (continued)

Table – 14. Credit Risk – Impaired Exposures, Past Due Exposures and Allowances (Own capital and current account by industry sector) (PD-1.3.23(h) PD-1.3.24(b) PD-1.3.24(d))

The following table summarises the impaired facilities, past due facilities, and allowances financed by own capital and current account disclosed by major industry sector as of 31 December 2014:

	Profit Sharing Investment Account											
		Aging of non-performing or past due or impaired Islamic financing contacts				Specific allowances				* General allowances		
	Non-performing or past due or impaired Islamic financing contracts BD'000	Less than 3 months** BD'000	3 months to 1 year BD'000	1 to 3 years BD'000	Over 3 years BD'000	Balance at the beginning of the year BD'000	Charges during the year BD'000	Charge-offs during the year BD'000	Balance at the end of year BD'000	General allowances beginning balance BD'000	General allowances movement BD'000	General allowances ending balance BD'000
Trading and Manufacturing	4,395	1,463	2,856	48	28	246	711	159	798	-	-	-
Real Estate	18,352	2,357	971	3,132	11,892	5,762	1,039	54	6,747	-	-	-
Banks and Financial Institutions	-	-	-	-	-	-	127	-	127	-	-	-
Personal / Consumer Finance	5,794	3,804	942	743	305	1,758	117	1,750	125	-	-	-
Others	4,269	1,732	769	1,716	52	-	199	-	199	-	-	-
No specific sector	-	-	-	-	-	-	-	-	-	1,057	1,683	2,739
Total	**32,810**	**9,356**	**5,537**	**5,639**	**12,277**	**7,766**	**2,193**	**1,963**	**7,996**	**1,057**	**1,683**	**2,739**

* General allowance represents collective impairment provision against exposures which, although not specifically identified, have a greater risk of default than when originally granted.

** This includes amounts not due and amounts past due less than 90 days relating to non-performing or past due or impaired Islamic financing contracts.

The Group's collective retail model uses the net flow rate method, where probability of default is calculated on an account level segregated by buckets of number of days past due. Loss given default is at annual average recovery rates, which is reviewed annually.

The Group's collective corporate model uses the expected loss method. Data is grouped in economic sectors and probability of default and loss given default is calculated for these sectors.

BASEL II, PILLAR III DISCLOSURES
31 December 2014

3 Risk Management (continued)

3.5 Credit Risk (continued)

Table – 15. Credit Risk – Impaired Exposures, Past Due Exposures and Allowances (profit sharing investment account by industry sector) (PD-1.3.23(h))

The following table summarises the impaired facilities, past due facilities, and allowances financed by profit sharing investment account disclosed by major industry sector as of 31 December 2014:

	Profit Sharing Investment Account											
	Non-performing or past due or impaired Islamic financing contracts	Aging of non-performing or past due or impaired Islamic financing contacts				Specific allowances				* General allowances		
		Less than 3 months** BD'000	3 months to 1 year BD'000	1 to 3 years BD'000	Over 3 years BD'000	Balance at the beginning of the year BD'000	Charges during the year BD'000	Charge-offs during the year BD'000	Balance at the end of year BD'000	General allowances beginning balance BD'000	General allowances movement BD'000	General allowances ending balance BD'000
	BD'000											
Trading and Manufacturing	12,963	4,315	8,423	143	82	727	2,095	467	2,355	-	-	-
Real Estate	54,123	6,950	2,864	9,238	35,071	16,994	3,064	160	19,898	-	-	-
Banks and Financial Institutions	-	-	-	-	-	-	373	-	373	-	-	-
Personal / Consumer Finance	17,088	11,217	2,779	2,192	900	5,185	346	5,163	368	-	-	-
Others	12,587	5,106	2,267	5,062	152	-	588	-	588	-	-	-
No specific sector	-	-	-	-	-	-	-	-	-	3,116	4,962	8,079
Total	**96,761**	**27,588**	**16,333**	**16,635**	**36,205**	**22,906**	**6,466**	**5,790**	**23,582**	**3,116**	**4,962**	**8,079**

* General allowance represents collective impairment provision against exposures which, although not specifically identified, have a greater risk of default than when originally granted.

** This includes amounts not due and amounts past due less than 90 days relating to non-performing or past due or impaired Islamic financing contracts.

Although the above table shows the portion of impairment provision related to PSIA, the Group has taken all the provision to their own capital. Hence the PSIA were not charged for any of the impairment provision.

The Group's collective retail model uses the net flow rate method, where probability of default is calculated on an account level segregated by buckets of number of days past due. Loss given default is at annual average recovery rates, which is reviewed annually.

The Group's collective corporate model uses the expected loss method. Data is grouped in economic sectors and probability of default and loss given default is calculated for these sectors.

Table – 16. Credit Risk – Impaired Exposures, Past Due Exposures and Allowances (own capital and current account and profit sharing investment account by geographic area) (PD-1.3.23(i) PD-1.3.24(c))

The following table summarises the past due facilities and allowances financed by own capital and current account and profit sharing investment account disclosed by geographical area as of 31 December 2014:

	Own Capital and Current Account			Profit Sharing Investment Account		
	Non- performing or past due or impaired Islamic financing contracts BD'000	Specific Impairment provision BD'000	Collective Impairment provision BD'000	Non- performing or past due or impaired Islamic financing contracts BD'000	Specific Impairment provision BD'000	Collective Impairment provision BD'000
Middle East	32,810	7,996	2,739	96,761	23,582	8,079
Total	**32,810**	**7,996**	**2,739**	**96,761**	**23,582**	**8,079**

BASEL II, PILLAR III DISCLOSURES
31 December 2014

3 Risk Management (continued)

3.5 Credit Risk (continued)

Table – 17. Credit Risk – Restructured Financing Facilities (PD-1.3.23(j))

The following table summarises the aggregate amount of restructured financing facilities during the year financed by own capital and current account and profit sharing investment account as of 31 December 2014:

	Own capital and current account Aggregate amount BD'000	Profit Sharing Investment Account Aggregate amount BD'000
Restructured financing facilities	4,015	11,842
Total	**4,015**	**11,842**

	Gross of Deferred Profit and provisions	Deferred Profit	Provision	Net Exposure
Total Islamic Financing	670,551	117,856	42,396	510,299
Restructured financing facilities	22,945	3,460	3,628	15,857
Percentage	**3.42%**	**2.94%**	**8.56%**	**3.11%**

The provision on restructured facilities is BD 3,628 Million and the impact on present and future earnings is not significant.

Table – 18. Credit Risk Mitigation (PD-1.3.25 (b) and (c))

The following table summarises the exposure as of 31 December 2014 by type of Islamic financing contract covered by eligible collateral:

	Total exposure covered by	
	Eligible collateral BD'000	Guarantees BD'000
Financing assets	9,892	14,799
Ijarah muntahia bittamleek	618	1,125
Total	**10,510**	**15,924**

	Guarantees BD'000	Risk Weighted BD'000
Type of Guarantees		
Tamkeen Guarantee	14,924	7,108
Bank Guarantee	1,000	476
Total	**15,924**	**7,584**

BASEL II, PILLAR III DISCLOSURES
31 December 2014

3 Risk Management (continued)

3.5 Credit Risk (continued)

Table – 19. Counterparty Credit (PD-1.3.26 (b))

The following table summarises the counterparty credit risk exposure covered by collateral after the application of haircuts as of 31 December 2014:

	BD'000
Gross positive fair value of contracts	
Netting Benefits	88,031
Netted current credit exposure	**88,031**
Collateral held:	
-Cash	10,510
-Shares	8
-Real Estate	357,295
Total	**367,813**

A haircut of 30% is applied on the Real Estate collateral.

3.6 Market Risk

3.6.1 Introduction

The Group has accepted the definition of market risk as defined by CBB as "the risk of losses in on- and off-balancesheet positions arising from movements in market prices."

3.6.2 Sources of market risk

For the Group, market risk may arise from movements in profit rates, foreign exchange markets, equity markets, or commodity markets. A single transaction or financial product may be subject to any number of these risks.

Profit rate risk is the sensitivity of financial products to changes in the profit rates. Profit rate risk arises from the possibility that changes in profit rates will affect future profitability or the fair values of financial instruments. The Group's management believe that the Group is not exposed to material profit rate risk as a result of mismatches of profit rate repricing of assets, liabilities, and equity of investment accountholders as the repricing of assets, liabilities and equity of investment accountholders occur at similar intervals. The profit distribution to equity of investment accountholders is based on profit sharing agreements. Therefore, the Group is not subject to any significant profit rate risk.

Foreign exchange risk is the sensitivity of financial products to changes in spot foreign exchange rates. The value of the Group's portfolio which is denominated in a number of currencies may be exposed to these risks when converted back to the Group's base currency.

Equity price risk is the sensitivity of financial products to the changes in equity prices. Equity risk arises from holding open positions in equities or equity based instruments, thereby creating exposure to a change in the market price of the equity. In addition to Group performance expectations, equity prices are also susceptible to general economic data and sector performance expectations.

Commodity risk is defined as inhernt risk in financial product arisinf from their sensitivity to changes in commodity prices. Since prices in commodity markets are determined by fundamental factors (i.e. supply and demand of the underlying commodity) these markets may be strongly correlated within particular sector and less correlated across sectors.

3.6.3 Market risk strategy

The Group's Board is responsible for approving and reviewing (at least annually) the risk strategy and significant amendments to the risk policies. The Group's senior management is responsible for implementing the risk strategy approved by the Board, and continually enhancing the policies and procedures for identifying, measuring, monitoring and controlling risks.

In line with the Group's risk management objectives and risk tolerance levels, the specific strategies for market risk management include:

1 The Group will manage its market risk exposure by evaluating each new product / activity with respect to the market risk introduced by it;

2 The Group will proactively measure and continually monitor the market risk in its portfolio;

3 The Group will at all time hold sufficient capital in line with the CBB Pillar 1 regulatory capital requirements;

4 The Group will establish a market risk appetite which will be quantified in terms of a market risk limit structure;

5 The Group will establish a limit structure to monitor and control the market risk in its portfolio. These limits will include position limits, maximum/stop loss limits, factor sensitivity limits, VaR limits and maturity limits;

6 The Group will carry out stress testing periodically using the worst case scenarios to assess the effects of changes in the market value due to changing market conditions;

BASEL II, PILLAR III DISCLOSURES

31 December 2014

3 Risk Management (continued)

3.6 Market Risk (continued)

3.6.3 Market risk strategy (continued)

7 The Group will periodically carry out back testing of market risk assessment models in order to evaluate their accuracy and the inherent model risk;

8 The Group will match the amount of floating rate assets with floating rate liabilities; and

9 The Group will clearly identify the foreign currencies in which it wishes to deal in and actively manage its market risk in all foreign currencies in which it has significant exposure.

Market risk measurement techniques includes the use of a number of techniques for market risk measurement. The risk measurement techniques mentioned in this section are used for measuring market risk in both trading book as well as banking book.

The various techniques which are used by the Group for the measurement, monitoring and control of market risk are as follows:

a. Overnight open positions;

b. Stop loss limits;

c. Factor sensitivity limits;

d. VaR limits; and

e. Profit rate risk gap analysis.

3.6.5 Market risk monitoring and limits structure

The Asset and Liability Committee (ALCO) proposes through the Executive Committee and Board the tolerance for market risk. Based on these tolerances, Risk and Compliance Unit and Treasury have established appropriate risk limits that maintain the Group's exposure within the strategic risk tolerances over a range of possible changes in market prices and rates.

3.6.6 Limits monitoring

The Treasury Department and Risk and Compliance Unit monitor the risk limits for each transaction, ensure that the limits are well within set parameters and report periodically to top management.

3.6.7 Breach of limits

In case a limit is breached, an approval from the CEO is required to continue with the transaction. An immediate report is provided to the ALCO after every significant limit breach. This breach is also reported to and approved by the Executive Committee (EXCOM). The limits are revised at least bi-annually or when deemed required.

3.6.8 Portfolio review process

On a monthly basis, Risk and Compliance Unit reviews the Group's assets and liabilities portfolio to evaluate the overall corporate exposure to market risk. As part of the review, Risk and Compliance Unit also monitors the Group's overall market exposure against the risk tolerance limits set by the Board. Risk and Compliance Unit also reviews the adherence to approved limits to control the market risk. Changes, if any, in market risk limits are communicated to business units after review by the GM-C&RM/CEO and approval by the ALCO or EXCOM, as per the delegated authorities approved by the Board. Balance sheet exposure is being reviewed on a quarterly basis by the Board level Audit and Risk committees.

3.6.9 Reporting

Risk and Compliance Unit generates at regular periodic intervals market risk management reports. These reports aim to provide the Group's senior management with an up-to-date view of its market risk exposure.

3.6.10 Stress testing

Stress tests produce information summarising the Group's exposure to extreme, but possible, circumstances and offer a way of measuring and monitoring the portfolio against extreme price movements of this type. The Group's Risk and Compliance Unit employs four stress categories: profit rates, foreign exchange rates, equity prices and commodity prices. For each stress category, the worst possible stress shocks that might realistically occur in the market are defined.

3.6.11 Foreign subsidiary

The Group does not have any foreign subsidiary.

BASEL II, PILLAR III DISCLOSURES

31 December 2014

3 **Risk Management** (continued)

3.6 **Market Risk** (continued)

Table – 20. Market Risk Capital Requirements (PD-1.3.27 (b))

The following table summarises the capital requirement for foreign exchange risk as of 31 December 2014;

	Foreign exchange risk BD'000
Foreign exchange risk	**13,325**
Foreign exchange risk capital requirement	**1,599**
Maximum value capital requirement	**1,599**
Minimum value capital requirement	**1,066**

3.7 Operational Risk

3.7.1 Introduction

Operational risk is the risk of loss arising from system failure, human error, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to financial loss. The Group cannot expect to eliminate all operational risks, but through a control framework and by monitoring and responding to potential risks, the Group is able to manage the risks. Controls include effective segregation of duties, access, authorisation and reconciliation procedures, staff education and assessment processes, including the use of internal audit.

3.7.2 Sources of operational risk

The different sources of operational risks faced by the Group can be classified broadly into the following categories;

1. People risk which arises due to staffing inadequacy, unattractive remuneration structure, lack in staff development policies, lack in procedures for appointment, unhealthy professional working relationship and unethical environment;
2. Processes risk which arises due to inadequate general controls, inadequate application controls, improper business and market practices and procedures, inappropriate/inadequate monitoring and reporting; and
3. Systems (Technology) risk which arise due to integrity of information - lacking in timelines of information, omission and duplication of data; hardware failures due to power surge, obsolescence or low quality.

3.7.3 Operational risk management strategy

As a strategy, the Group will identify the sources of operational risks in coordination with each business unit. The Group carried out Risk Control Self-Assessments (“RCSA”), and plans to do a continuous and on-going exercise to identify the operational risks it is exposed to.

The Group on a continuous basis will:

a. assess the effectiveness of controls associated with identified risks;
b. regularly monitor operational risk profiles and material exposures to losses; and
c. identify stress events and scenarios to which it is vulnerable and assess their potential impact, and the probability of aggregated losses from a single event leading to other risks.

3.7.4 Operational risk monitoring and reporting

The internal monitoring and reporting process ensures a consistent approach for providing pertinent information to senior management for the quick detection and correction of deficiencies in the policies, processes, and procedures for managing operational risk through ongoing, periodic reviews.

The objective of the reporting process is to ensure relevant information is provided to senior management and the Board to enable the proactive management of operational risk. The process ensures a consistent approach for providing information that enables appropriate decision making and action taking.

3.7.5 Operational risk mitigation and control

The business units, in consultation with Risk and Compliance Unit will determine all material operational risks and decide the appropriate procedures to be used to control and/or mitigate the risks.

For those risks that cannot be controlled, the business units in conjunction with Risk and Compliance Unit will decide whether to accept the risks, reduce the level of business activity involved, transfer the risk outside the Group or withdraw from the associated activity completely. Risk and Compliance Unit facilitates the business units in co-developing the mitigation plans.

BASEL II, PILLAR III DISCLOSURES
31 December 2014

3 Risk Management (continued)

3.7 Operational Risk (continued)

3.7.6 Business Continuity Plan (BCP)

The Group has also developed a comprehensive business continuity plan detailing the steps to be taken in the event of extreme conditions to resume the Group's operations with minimum delay and disturbance. The plan is in implementation stage. Elements of contingency plans and disaster recovery processes include operating systems, physical space, telecommunications and resources.

3.7 Operational Risk

Table - 21. Operational Risk Exposure (PD-1.3.30 (a), (b) & (c))

The following table summarises the amount of exposure subject to basic indicator approach of operational risk and related capital requirements:

	Gross income		
	2013 BD'000	**2012 BD'000**	**2011 BD'000**
Total Gross Income	**35,375**	**23,780**	**24,856**
Indicators of operational risk			
Average Gross income (BD'000)			28,004
Multiplier			12.5
			350,046
Eligible Portion for the purpose of the calculation			15%
TOTAL OPERATIONAL RISK WEIGHTED EXPOSURE (BD'000)			**52,507**

Risk and Compliance Unit ensures that the BCP is kept up to date and tested once a year in a simulated environment to ensure that it can be implemented in emergency situations and that the management and staff understand how it is to be executed. Results of this testing conducted by Risk and Compliance Unit is evaluated by the GM-C&RM and presented to the EXCOM/Board for evaluation.

3.8 Equity Position in the Banking Book

Equity price risk is the risk that the fair values of equities decrease as a result of changes in the levels of equity indices and the value of individual stocks. The equity price risk exposure arises from the Group's investment portfolio.

The accounting policies, including valuation methodologies and their related key assumptions, are disclosed in the consolidated financial statements as of 31 December 2014. Equity type instruments carried at fair value through equity and investment properties are kept for capital gain purposes, all other investments including investments in associates are kept for strategic long term holdings.

Table – 22. Equity Position Risk in Banking Book (PD-1.3.31 (b) (c) & (f))

The following table summarises the amount of total and average gross exposure of equity based financing structures by types of financing contracts and investments as of 31 December 2014;

	Total gross exposure BD'000	* Average gross exposure BD'000	Publicly traded BD'000	Privately held BD'000	Risk weighted assets BD'000	Capital Requirements BD'000
Sukuk	81,834	71,223	-	81,834	15,728	1,887
Equity investments	22,873	23,988	1,393	21,480	41,532	4,984
Funds	14,870	17,354	-	14,870	29,363	3,524
Total	**119,577**	**112,565**	**1,393**	**118,184**	**86,623**	**10,395**

* Average balances are computed based on month end balances.

BASEL II, PILLAR III DISCLOSURES
31 December 2014

3 Risk Management (continued)

3.8 Equity Position in the Banking Book (continued)

Table – 23. Equity Gains or Losses in Banking Book (PD-1.3.31 (d) & (e))

The following table summarises the cumulative realised and unrealised gains or (losses) during the year ended 31 December 2014;

	BD'000
Cumulative realised gain arising from sales orliquidations in the reporting period	1,946
Total unrealised losses recognised in the consolidated statement of financial positionbut not through consolidated statement of income	-
Unrealised losses included in Tier 1 Capital	310
Unrealised gains included in Tier 2 Capital	484

* This unrealised gain is discounted by 55% before including it in Tier 2 Capital

3.9 Equity of Investment Accountholders ("IAH")

The Group may require to decrease or increase loses or profit on certain IAH accounts for the purpose of income smoothing. Thus the Group is exposed to some of the price risk on assets funded by equity of Investment Accountholders ("IAH"). The CBB requires the Group to maintain capital to cover the price risk arising from 30% of assets funded by IAH on a pro-rata basis.

The Group is authorised by the IAH to invest the account holder's funds on the basis of Mudaraba contract in a manner which the Group deems appropriate without laying down any restrictions as to where, how, and for what purpose the funds should be invested. Under this arrangement the Group can commingle the equity of investment accountholders investment funds with its own funds (owner's equity) or with other funds the Group has the right to use (e.g. current accounts or any other funds which the Group does not receive on the basis of Mudaraba contract). The IAH and the Group generally participate in the returns on the invested funds. In such type of contract, the Group is not liable for any losses incurred on the joint pool other than the loss resulting from gross negligence or wilful misconduct on the part of the Group or due to the Group's violation of the terms and conditions as agreed between the Group and the IAH.

The amount received from the customer on account of equity of investment accountholders is not invested completely in the portfolio of selected investments as the Group is required to maintain a cash reserve with CBB. In addition, the Group requires to set aside certain amount to meet operational requirements. The income allocated to the equity of investment accountholders deposits being received is in accordance with the utilisation of such deposits. The utilisation rate is determined by the ALCO with the approval of Shari'a Supervisory Board.

If at any point of time in a particular pool the funds of IAH exceed the assets, the excess amount shall be treated to be invested in commodity Murabaha and earn the average rate of profit on Commodity Murabaha earned during the excess period. There should be no inter-pool financing at any point of time. The Group should establish a control to avoid excess fund in any pool to be used in other pool.

Proposal for new products is initiated by the business lines within the Group and ALCO review such proposal to ensure that the new product is in line with the Group's business and risk strategy. All new products require the approval of the Shari'a Supervisory Board of the Bank. The business lines of the Group have expertise in creating high end value added products offering a wide range of products, expected return, tenors, and risk profile. Information on new products or any change in the existing products will be placed on the Group's website or published in the media.

The Group has designed special quality assurance units whom reports complaints directly to the CEO. The complaints are investigated by personnel not directly related to the subject matter of the complaints.

The Group offers equity of investment accountholders in different currencies for maturity periods ranging from 1 month, 3 month, 6 month, 9 month, 12 month and 36 month. The customer signs written contract covering all terms and conditions of the investment, including tenor, basis of profit allocation, and early withdrawal.

Because equity of investment accountholders is a significant funding source for the Group, the Group regularly monitors rate of return offered by competitors to evaluate the expectation of its IAH. The Group's policy provide whole or partial waiver of the Mudarab share of income from investment in order to provide a reasonable return to its investors.

The Group comingles its own funds and equity of investment accountholders funds which are invested together. The Group has identified two pools of assets where the equity of investment accountholders funds are invested and income from which is allocated to such is account.

The Group has already developed a written policies and procedures applicable to its portfolio of equity of investment accountholders. equity of investment accountholders funds are invested and managed in accordance with Shari'a requirements.

- Pool A: Low risk assets or generating low yield.
- Pool B: High risk assets or generating high yield.

BASEL II, PILLAR III DISCLOSURES

31 December 2014

3 Risk Management (continued)

3.9 Equity of Investment Accountholders ("IAH") (continued)

Profits of an investment jointly financed by the Group and the equity of investment accountholders holders shall be allocated between them according to the contribution of each of the Group and the IAH in the jointly financed investment separately for each Joint pool A and B. Operating expenses incurred by the Group are not charged to investment account. In case of the loss resulting from the transactions in a jointly financed investment, such loss shall first be deducted from undistributed profits, if any. Any excess of such loss shall be deducted from Investment Risk Reserve (IRR). Any remaining of such loss shall be deducted from the total balance of fund available in the Joint pool, as at that date, in the respective ratio of the Group's and IAH's respective contribution to the joint fund. Impairment provisions shall only be allocated to Pool B in the ratio of capital contribution by Bank and IAH of Pool B. The reversal of this provision in future year shall be allocated between Bank and IAH of Pool B in the ratio of capital contribution at the time the reversal is made. The loss can be entirely borne by the shareholders of the Group subject to the approval of the Board. Equity of investment accountholders deposits are measured at their book value.

In case of early withdrawal of IAH fund before completion of the term, the effective utilisation method will be applied.

Table – 24. Equity of Investment Accountholders by Type (PD-1.3.33 (a))

The following table summarises the breakdown of equity of investment accountholders accounts as of 31 December 2014:

	BD'000
Customers	566,601
Total	**566,601**

Table – 25. Equity of Investment Accountholders Ratios (PD-1.3.33 (d) & (f))

The following table summarises the return on average assets and mudarib share as a percentage of the total investment profit for the year ended 31 December 2014;

Profit Paid on Average IAH Assets *	1.12%
Mudarib Fee to Total IAH Profits	65.00%

* Average assets funded by IAH have been calculated using month end balances.

Table – 26. Equity of Investment Accountholders Ratios (PD-1.3.33 (e) & (g))

The following table summarises the profit distributed to IAH and financing ratios to the total of IAH by type of investment account holder for the year ended 31 December 2014:

Account Type	**Profit distributed to total IAH**	**Percentage to total IAH**
Saving accounts (including VEVO)	3.53%	19.57%
Defined accounts - 1 month	0.96%	0.99%
Defined accounts - 3 months	0.35%	0.35%
Defined accounts - 6 months	0.61%	0.56%
Defined accounts - 9 months	0.00%	0.00%
Defined accounts - 1 year	3.26%	2.56%
Investment certificates	0.92%	0.28%
IQRA Deposits	1.41%	0.69%
Tejoori Deposit	3.68%	19.32%
Customer's deposits	81.88%	44.88%
Bank's deposits	3.40%	10.80%
	100%	**100%**

The calculation and distribution of profits was based on average balances.

BASEL II, PILLAR III DISCLOSURES

31 December 2014

3 Risk Management (continued)

3.9 Equity of Investment Accountholders ("IAH") (continued)

Table – 27. Equity of Investment Accountholders to Total Financing (PD-1.3.33 (h) & (i))

The following table summarises the percentage of counterparty type to total financing for each type of Shari'a-compliant contract to total financing as of 31 December 2014:

	Percentage of Financing to Total Financing
Placements with financial institutions	10.16%
Financial institutions	60.47%
Investment in Sukuk	12.13%
Ijarah muntahia bittamleek	15.16%
Ijarah rental receivables	2.08%

	Percentage of Counterparty Type to Total Financing						
	Trading and Manufacturing	Banks and Financial Institutions	Real Estate	Aviation	Personal & Consumer Finance	Governmental Organisation	Others
Placements with financial institutions	0.00%	10.16%	0.00%	0.00%	0.00%	0.00%	0.00%
Financial institutions	5.48%	0.14%	12.15%	0.01%	30.07%	0.35%	12.28%
Investment in Sukuk	0.00%	1.25%	2.75%	0.00%	0.00%	5.61%	2.52%
Ijarah muntahia bittamleek	0.72%	0.04%	7.00%	0.95%	6.45%	0.00%	0.00%
Ijarah rental receivables	0.30%	0.00%	1.04%	0.27%	0.38%	0.00%	0.10%
	6.5%	**11.59%**	**22.94%**	**1.22%**	**36.90%**	**5.96%**	**14.89%**

Table – 28. Equity of Investment Accountholders Share of Profit (PD-1.3.33 (l) (m) & (n))

The following table summarises the share of profits earned by and paid out to profit sharing investment accounts and the Group as Mudarib for the year ended 31 December 2014:

Share of profit earned by IAH before transfer to/from reserves - BD '000	23,419
Percentage share of profit earned by IAH before transfer to/from reserves	31.12%
Share of profit paid to IAH after transfer to/from reserves - BD '000	7,287
Percentage share of profit paid to IAH after transfer to/from reserves	31.59%
Share of profit paid to Bank as mudarib - BD '000	16,092

Table – 29. Equity of Investment Accountholders Percentage Return to Profit Rate of Return (PD-1.3.33 (q))

The following table summarises the average distributed rate of return or profit rate on profit sharing investment accounts for the year ended 31 December 2014:

	3 month	6 month	12 month	36 month
Percentage of average distributed rate of return to profit rate of return	0.73%	0.84%	1.06%	3.50%

BASEL II, PILLAR III DISCLOSURES

31 December 2014

3 Risk Management (continued)

3.9 Equity of Investment Accountholders ("IAH") (continued)

Table – 30. Equity of Investment Accountholders Type of Assets (PD-1.3.33 (r) & (s))

The following table summarises the types of assets in which the funds are invested and the actual allocation among various types of assets for the year ended 31 December 2014:

	Opening Actual Allocation BD'000	Movement During the Period BD'000	Closing Actual Allocation BD'000
Cash and balances with banks and central Bank	32,740	(1,685)	31,055
Placements with financial institutions	164,758	(96,191)	68,567
Financing assets	309,527	98,494	408,021
Investment in sukuk	38,841	42,994	81,835
Ijarah muntahia bittamleek	80,643	21,634	102,277
Ijarah rental receivables	13,320	745	14,065
Total	**639,829**	**65,991**	**705,820**

Table – 31. Equity of Investment Accountholders Profit Earned and Paid (PD-1.3.33 (w))

The following table summarises the amount and rate of return of profits earned by the Group and paid out to equity of investment accountholders over the past five years:

	Profit Earned (jointly financed)		Profit Paid to (IAH)	
	BD'000	%age	BD'000	%age
2014	**23,491**	**3.55%**	**7,539**	**1.14%**
2013	32,849	4.98%	11,124	1.69%
2012	30,662	5.21%	13,993	2.38%
2011	33,029	5.53%	14,742	2.31%
2010	3,083	4.46%	17,721	2.61%
2009	35,694	5.27%	17,638	2.81%

Table – 32 Treatment of assets financed by IAH (PD-1.3.33 (v))

	Assets BD'000	RWA BD'000	RWA for Capital Adequacy Purposes BD'000	Capital Requirements BD'000
Cash and balances with banks and central Bank	31,055	-	-	-
Placements with financial institutions	51,205	16,012	4,804	576
Financing assets*	304,704	274,563	82,369	9,884
Investment in sukuk	64,087	24,708	7,412	889
Ijarah muntahia bittamleek*	76,379	68,824	20,647	2,478
Ijarah rental receivables	10,504	10,503	3,151	378
	537,934	**394,610**	**118,383**	**14,206**

* The amounts have been allocated on pro-rata basis due to system limitation.

BASEL II, PILLAR III DISCLOSURES

31 December 2014

3 Risk Management (continued)

3.10 Liquidity Risk

3.10.1 Introduction

Liquidity risk is defined as "the risk that the Group will be unable to meet its obligations as they come due because of an inability to obtain adequate funding or to liquidate assets".

3.10.2 Sources of liquidity risk

The sources of liquidity risk can broadly be categorised in the following:

a. Funding risk is the risk of not being able to fund net outflows due to unanticipated withdrawal of capital or deposits;

b. Call risk is the risk of crystallisation of a contingent liability; and

c. Event risk is the risk of rating downgrades or other negative public news leading to a loss of market confidence in the Group.

3.10.3 Bank's funding strategy

The Board reviews the funding strategy on an annual basis and amends the existing strategy, as deemed necessary. For this purpose, all business units advise the Treasurer of their projected liquidity requirements and contributions at the start of each year as part of annual budgeting process.

The funding strategy highlights any anticipated liquidity shortfalls, the funding requirements to finance these shortfalls and their impact on the statement of financial position. The Group's Risk Charter and Liquidity Policy address liquidity contingency plan to deal with stressed scenarios and outline an action plan that can be taken in the event of liquidity stress situation.

3.10.4 Liquidity risk strategy

The Group monitors the liquidity position by comparing maturing assets and liabilities over different time buckets of up to 1 month, 1-3 months, 3-6 months, 6 months to 1 year, 1-3 years, and over 3 years. The Group carries out stress testing periodically using the worst case scenarios to assess the effects of changes in market conditions on the liquidity of the Group. As a strategy the Group maintains a large customer base and good customer relationships.

The Treasury Department, in conjunction with Risk and Compliance Unit periodically reviews/updates (at least annually) the liquidity risk strategy which is evaluated by ALCO before presenting to the EXCOM and the Board for approval.

3.10.5 Liquidity risk measurement tools

The Group uses a combination of techniques for measurement of its liquidity risk. These include liquidity gap analysis, liquidity ratio limits and minimum liquidity guidelines.

3.10.6 Liquidity risk monitoring

The Group has set the tolerance for liquidity risk which are communicated to the Risk and Compliance Unit and Treasury Department. Based on these tolerances, Risk and Compliance Unit and Treasury have established appropriate risk limits that maintain the Group's exposure within the strategic risk tolerances over a range of possible changes in liquidity situations.

3.10.7 Liquidity limits structure

The Group uses a combination of different limits to ensure that liquidity is managed and controlled in an optimal manner. The Group has set the following limits for monitoring liquidity risks:

a. Liquidity Gap limits;

b. Liquidity Ratio limits; and

c. Minimum Liquidity Guideline ("MLG").

3.10.8 Liquidity risk stress testing

To evaluate whether the Group is sufficiently liquid, behavior of the Group's cash flows under different conditions are observed.

BASEL II, PILLAR III DISCLOSURES

31 December 2014

3 **Risk Management** (continued)

3.10 Liquidity Risk (continued)

3.10.9 Contingency funding plan

The Group does contingency funding exercises which details procedures to be followed by the Group, in the event of a liquidity crisis or a situation where the Group faces stressed liquidity conditions. The contingency funding plan will be an extension of day to day liquidity management and involves maintenance of an adequate amount of liquid assets and management of access to funding resources. The ALCO members discuss and monitor the situation over regular time-intervals to ensure sufficient liquidity in the Group.

Table – 33. Liquidity Ratios (PD-1.3.37)

The following table summarises the liquidity ratios for the past five years:

	2014	2013	2012	2011	2010	2009
Due from banks and financial institutions / Total Assets	**7.83%**	20.28%	15.90%	17.73%	22.27%	12.10%
Islamic Financing / Customer Deposits excluding banks	**72.48%**	70.80%	72.32%	114.41%	115.46%	123.01%
Customer Deposits / Total Assets	**64.74%**	67.83%	68.87%	63.08%	64.13%	57.28%
Liquid Assets / Total Assets	**13.79%**	25.86%	21.17%	22.70%	27.02%	16.06%
Growth in Customer Deposits	**(8.24%)**	7.66%	8.36%	(11.71%)	14.86%	21.98%

3.11 Profit Rate Risk

Profit rate risk is the potential impact of the mismatch between the rate of return on assets and the expected rate of funding due to the sources of finance.

Senior management identifies the sources of profit rate risk exposures based upon the current as well as forecasted balance sheet structure of the Group. The profit rate risk in the Group may arise due to the following transactions:

a. Murabaha transactions;

b. Wakala transactions;

c. Ijarah muntahia bittamleek;

d. Sukuk; and

e. Musharaka investments.

The Group's management believe that the Group is not exposed to material profit rate risk as a result of mismatches of profit rate repricing of assets, liabilities and equity of investment accountholders as the repricing of assets, liabilities and equity of investment accountholders occur at similar intervals. The profit distribution to equity of investment accountholders is based on profit sharing agreements. Therefore, the Group is not subject to any significant profit rate risk.

3.11.1 Sources of Profit Rate Risk

The different profit rate risks faced by the Group can be classified broadly into the following categories.

a. Re-pricing risk which arises from timing differences in the maturity (for fixed rate) and re-pricing (for floating rate) of assets, liabilities and off balance sheet positions. As profit rates vary, these re-pricing mismatches expose the Group's income and underlying economic value to unanticipated fluctuations;

b. Yield curve risk which arises when unanticipated shifts of the yield curve have adverse effects on the Group's income and/or underlying economic value;

c. Basis risk which arises from imperfect correlation in the adjustment in the rate earned on products priced and the rate paid on different instruments with otherwise similar re-pricing characteristics. When profit rates change, these differences can give rise to unexpected changes in the cash flows and earnings spread between assets, liabilities, and off balance sheet instruments of similar maturities or re-pricing frequencies; and

d. Displaced Commercial Risk refers to the market pressure to pay returns that exceeds the rate that has been earned on the assets financed by the liabilities, when the return on assets is under performing as compared with competitors rates.

BASEL II, PILLAR III DISCLOSURES

31 December 2014

3 Risk Management (continued)

3.11.2 Profit rate risk strategy

The Group is not exposed to interest rate risk on its financial assets as no interest is charged. However, the fair value of financial assets may be affected by current market forces including interest rates. The Group recognises income on certain of its financial assets on a time-apportioned basis. As a strategy the Group:

a. has identified the profit rate sensitive products and activities it wishes to engage in;
b. has established a limit structure to monitor and control the profit rate risk of the Group;
c. measures profit rate risk through establishing maturity/re-pricing schedule that distributes profit rate sensitive assets, liabilities and off-balance sheet items in pre-defined time bands according to their maturity; and
d. makes efforts to match the amount of floating rate assets with floating rate liabilities in the banking book.

3.11.3 Profit rate risk measurement tools

The Group uses the following tools for profit rate risk measurement in the banking book:

a. Re-pricing gap analysis which measures the arithmetic difference between the profit-sensitive assets and liabilities of the banking book in absolute terms; and
b. Basis Point Value ("BPV") analysis which is the sensitivity measure for all profit rate priced products and positions. The BPV is the change in net present value of a position arising from a 1 basis point shift in the yield curve. This quantifies the sensitivity of the position or portfolio to changes in profit rates.

3.11.4 Profit rate risk monitoring and reporting

The Group has implemented information systems for monitoring, controlling and reporting profit rate risk. Reports are provided on a timely basis to EXCOM and the Board of Directors. The Risk and Compliance Unit monitors these limits regularly. GM-C&RM reviews the results of gap limits and exceptions, if any, and recommends corrective action to be taken which is approved by ALCO or EXCOM, according to authority parameters approved by the Board.

Table – 34. Profit Rate Risk in Banking Book (PD-1.3.40 (b))

The following table summarises the effect on the value of assets, liabilities and economic capital for a benchmark change of 200 bp in profit rates as of 31 December 2014:

	Effect on value of Asset BD'000	Effect on value of Liability BD'000	Effect on value of Economic Capital BD'000
Upward rate shocks:	(3,372)	3,372	-
Downward rate shocks:	10,468	(10,468)	-

Table – 35. Quantitative Indicators of Financial Performance and Position (PD-1.3.9 (b) PD-1.3.33 (d))

The following table summarises the basic quantitative indicators of financial performance for the past 5 years:

	2014	2013	2012	2011	2010	2009
Return on average equity	**11.80%**	8.26%	(42.31%)	(17.23%)	(33.02%)	(12.64%)
Return on average assets	**1.00%**	0.70%	(4.33%)	(1.96%)	(4.30%)	(2.17%)
Cost to Income Ratio	**55.10%**	53.44%	80.14%	74.89%	107.73%	70.66%

	2014	2013	2012	2011	2010
Mudarabah profit / Mudarabah assets	**4.73%**	5.54%	5.14%	5.44%	4.74%
Mudarabah profit paid / Mudarabah assets	**1.14%**	1.61%	2.34%	2.43%	2.55%
PER & IRR Movment	**(155)**	233	63	-	-
Rate of Return on IAH	**1.12%**	1.52%	2.11%	2.31%	2.39%

CBB Penalties (PD 1.3.44)

During the period, penalties amounting to BD 24,400 (2013: BD 12,900); (2012: BD 400) were imposed by the CBB for delay in submission of various regulatory returns. In addition, a penalty of BD 50 was imposed by the CBB for failure to update certain information in a particular report.

BASEL II, PILLAR III DISCLOSURES
31 December 2014

4 Glossary of Terms

ALCO	Assets and Liabilities Committee
BCP	Business Continuity Plan
BisB	Bahrain Islamic Bank B.S.C.
BPV	Basis Point Value
CA Module	Capital Adequacy Module
CAR	Capital Adequacy Ratio
CBB	Central Bank of Bahrain
CRMD	Credit and Risk Management Department
CR & AD	Credit Review and Analysis Department
C&IC	Credit and Investment Committee
DCR	Displaced Commercial Risk
Excom	Executive Committee
FX	Foreign Exchange
GM-C&RM	General Manager-Credit and Risk Management
Group	Bahraini Islamic Bank B.S.C. and its subsidiaries
HR Committee	Human Resource Committee
IAH	Investment Account Holder
ICAAP	Internal Capital Adequacy Assessment Process
IFRS	International Financial Reporting Standards
IT Committee	Information Technology Committee
IRR	Investment Risk Reserve
MLG	Minimum Liquidity Guidelines
PCD	Prudential Consolidation and Deduction Requirements Module
PD	Public Disclosure
PER	Profit Equalisation Reserve
PSIA	Profit Sharing Investment Account
RCSA	Risk and Control Self-Assessment
RMC	Risk Management Committee
RWE	Risk Weighted Exposures
VaR	Value-at-Risk
L/C	Letter of Credit
L/G	Letter of Guarantee