GULF FINANCE HOUSE BSC

CONSOLIDATED FINANCIAL STATEMENTS

31 DECEMBER 2008

Commercial registration	:	44136 (registered with Central Bank of Bahrain as a wholesale Islamic bank)
Registered Office	:	Bahrain Financial Harbour PO Box 10006, Manama, Kingdom of Bahrain Telephone +973 17538538
Directors	:	Dr. Esam Yousif A. Janahi, *Chairman* Hamad A Aziz Al-Shaya, *Vice Chairman* Abdul Latif Abdullah Al-Meer Adel Dawood Al-Ohali Buti Bin Khalifa Al-Flasi Khalid Mohamed Najibi Samir Yacoub Al-Nefaisi Waleed A.Rahman Al-Ruwaih Yousif A.Latif Al-Sarkal Yousuf Mohammed Khayat
Company Secretary	:	Dr. Haider Majali
Auditors	:	KPMG

LDD 11-02-09 1021

CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2008

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CHAIRMAN'S REPORT
for the year ended 31 December 2008

Dear Shareholders,

In the name of Allah, the Beneficent, the Merciful, Prayers and Peace Be Upon the Last Apostle and Messenger, our Prophet Mohammed.

On behalf of the Board of Directors, it is my privilege to present the annual report of Gulf Finance House (GFH) for the year ended 31st December 2008. The year started with the deepening of the global financial crisis in the US and Europe and ended with the major advanced economies in recession. The commodity-exporting countries and emerging economies in general, were not immune as a result of the globalization of trade and capital flows. Commodity prices, especially oil reached unprecedented levels by the middle of the year and then crashed as the speculative bubble burst in the last quarter of the year. Nevertheless, the average price of oil for the year as a whole was close to US $100 per barrel. As a result, the GCC economies fared much better than most other countries in the world. It is therefore likely that the governments of the GCC ended 2008 with higher sovereign wealth despite losses on their holdings of international assets.

The financial and corporate sectors in the GCC also did better than their peers in the rest of the world thanks to the vigilance of the regulatory authorities. The liquidity shortage that affected the GCC financial markets in the second half of 2008 represented a severe test of financial institutions and, thankfully, demonstrated the resilience of the majority of them, especially the Sharia'a compliant among them. By the grace of Almighty and prudent management of risk and liquidity, GFH ended the year in a strong position despite the challenges and the tough operating environment.

GFH has built on its core economic infrastructure business while offering diversified investment opportunities as we expand the range of financial products available to our investor base. A continued focus on initiatives that address the urgent demands across industry and emerging world economies underlines the robust versatility of our business model despite the global economic downturn.

As we approach our 10th anniversary, GFH can look back proudly over a decade of innovation and consistent performance. From our base in the GCC, we have always taken a keen interest in the many emerging economies locally and throughout North Africa and Asia. GFH has never been moved by the pursuit of generic investment opportunities. Our work has been inspired by the design of intelligent economic and financial platforms that empower domestic and regional economies. We've reached out to Governments, listened closely to their aspirations and studied the minutiae of how best to harvest their domestic economic potential. Over the years these efforts have given rise to a variety of sector themed economic infrastructure projects including energy cities and financial harbours internationally.

GFH's tireless appetite for understanding the smallest details of each sector it explores has, perhaps inevitably led to the identification of more specialised industrial demand and the development of new and diversified investment opportunities. 2008, more than any year before has witnessed the diversification of GFH initiatives, leveraging the depth and breadth of its experience. With a record of creating Islamic financial institutions such as QInvest and Khaleeji Commercial Bank, GFH will continue to pursue the development of specialist Islamic financial entities offering intelligent, tailored solutions. First Energy Bank (FEB) was the latest in a planned stable of related initiatives and the first Islamic investment bank in the Middle East offering financial solutions tailored exclusively to the energy sector.

Alongside this development and after years of exposure to the challenges faced by the infrastructure sector, our Venture Capital division launched several initiatives designed to address the MENA-wide shortage of critical building materials and industrial services – conceiving local solutions to local problems.

CHAIRMAN'S REPORT
for the year ended 31 December 2008 *(continued)*

Financial Performance and Shareholder Returns

I am pleased to announce that GFH has enjoyed a profitable year despite the well documented global financial crisis, recording a net profit of US$ 291 million, a decrease of 14% on 2007 profits. While GFH recorded a strong performance in the first three quarters of 2008, the 4th quarter reflected a cautious trend amongst the global investment community. Despite this, GFH enjoys sufficient capitalization, a low and flexible cost base, and liquid assets that remain in excess of US$ 1 billion.

Profits in 2008 have been driven both by economic infrastructure initiatives at Tunis Financial Harbour, Caspian Energy Hub, Kazakhstan, and Energy City Libya and through the success of Cemena, which demonstrates the emerging contribution of our diversified business lines to overall revenue.

Our steady navigation of a challenging regional marketplace is attributable to a few key factors. Our strict adherence to Sharia'a principles precludes direct exposure to the toxic asset classes that have triggered the eradication of wealth across world markets. Secondly, the majority of GFH initiatives are focused on selected emerging economies and our thorough due diligence, Government partnerships and sector specialists are effective in mitigating risks typically associated with execution and delivery. Furthermore, in a competitive marketplace, we remain confident that available liquidity will look to the most intelligent, innovative and prescient investment opportunities, and GFH will continue to provide them in the year ahead.

Strategic Progress

2008 saw the launch of GFH initiatives in new territories with the announcement of Caspian Energy Hub in Kazakhstan and Energy City Libya. Both initiatives are an indication of the esteem GFH is now held in by Governments across MENA and Asia. Nations with inherent industrial and economic potential continue to place their faith in our ability to design tailored economic platforms. Accordingly we expect to expand further in other emerging markets as these nations look to enhance their economic infrastructure.

While the conception of economic infrastructure initiatives has historically been a core GFH business line, we have placed far greater emphasis on diversification throughout the past twelve months by building strong capability across our Venture Capital, Private Equity, Asset Management and Islamic Financial Institutions operations. We look forward to offering our loyal investors a full range of products and investment opportunities.

As part of our diversification, from a private equity and venture capital perspective we'll assume an opportunistic stance towards undervalued assets in the region. Equally, we'll continue to focus energy on opportunities within the defensive sectors like agriculture and food production.

We also anticipate a focus on new geographies starting with the world's other major Islamic financial hub in South East Asia. With the continued growth in sophistication and appeal of Islamic finance, we hope to bridge the two markets and deliver the whole range of GFH products to a new investment community.

Corporate Social Responsibility

The maintenance and thoughtful application of a Corporate Social Responsibility programme is a bedrock Islamic principal and an integral part of our operations. GFH has always looked to support important causes across the community it inhabits.

In 2008, GFH has made several donations that have benefitted over 700 Bahraini families, helping the poor in a responsible sustainable way through addressing their basic needs and ensuring an improved quality of life.

CHAIRMAN'S REPORT
for the year ended 31 December 2008 *(continued)*

We have also supported various funds and organisations responsible for supporting the needy in their respective locations and encouraging improved welfare.

Through donations to the Islamic Society, we are contributing to the construction of new modern housing for those who have been long deprived of homes and the provision of funds to educate young Bahrainis who would otherwise not enjoy the tremendous benefits of an education.

We also continue to sponsor the 'Crown Prince's International Scholarship Programme' which identifies and educates some of the most promising young Bahrainis.

GFH recognises the importance of reinvesting in the community and we will continue to support causes that empower Bahrainis, promote welfare and contribute to a brighter future throughout the Kingdom.

In recent weeks GFH also made a BD100,000 contribution to the Bahrain National Committee for the Support of Palestinians in Gaza, a Charity foundation Chaired by Shaikh Nasser bin Hamad Al Khalifa.

Looking Ahead

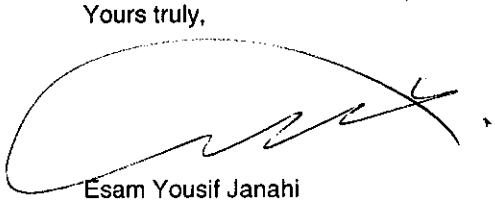
The global economy is facing enormous challenges but GFH is built on strong foundations and throughout a decade of success and innovation we have established ourselves as a leading regional Islamic investment bank.

As we embark on a new year, we expect the sophisticated and intuitive nature of our initiatives to be in even greater demand, creating value based on the specific long term needs of our investors. A different commercial landscape will require intelligent thinking to identify the specific economic, technological and industrial challenges that require urgent solutions, irrespective of the ebb and flow of the global economic tumult. With a track record for conceiving visionary solutions, GFH is well placed to adapt and flourish in a changing environment.

We will continue to focus initiatives on economies that offer attractive sector themed medium and long term growth prospects, capitalizing on the investment potential of countries, industries and ideas whose time have come.

We expect to be tested in the year ahead but with a strong pipeline of initiatives rapidly taking shape and a robust network of partners we look forward to further diversification and the continued success of our business in 2009. We are mindful of the role our Governmental partners continue to play in our achievements and we are forever grateful for the unique relationships we've established over the years. We thank the rulers and respective governments of The Kingdom of Bahrain, The People's Democratic Republic of Algeria, The People's Republic of China, The Republic of India, The Hashemite Kingdom of Jordan, The Republic of Kazakhstan, The State of Kuwait, The Great Socialist People's Libyan Arab Jamahiriya, The Kingdom of Morocco, The State of Qatar, The Kingdom of Saudi Arabia, The Tunisian Republic and the United Arab Emirates.

Yours truly,



Esam Yousif Janahi
Chairman

28 January 2009

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INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS
GULF FINANCE HOUSE BSC
Manama, Kingdom of Bahrain

28 January 2009

Report on the consolidated financial statements

We have audited the accompanying consolidated financial statements set out in pages 6 to 58 of Gulf Finance House B.S.C. ("the Bank") and its subsidiaries (together the "Group"), which comprise the consolidated balance sheet as at 31 December 2008, and the consolidated statements of income, changes in equity, cash flows, changes in restricted investment accounts and sources and uses of charity and zakah fund for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Responsibilities of the Board of Directors for the consolidated financial statements

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

Auditors' responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with both the Auditing Standards for Islamic Financial Institutions and International Standards on Auditing. Those standards require that we comply with relevant ethical requirements and plan and perform the audit to obtain reasonable assurance whether the consolidated financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting principles used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

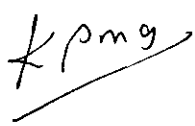
KPMG Fakhro, a registered partnership under Bahrain law,
is a member of KPMG International, a Swiss cooperative.

Independent auditors' report to the shareholders (continued)
28 January 2009

Opinion
In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as at 31 December 2008, and its financial performance, cash flows, changes in equity, changes in restricted investment accounts and sources and uses of charity and zakah 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.

In addition, in our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as at 31 December 2008 and its financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards.

Report on other legal and regulatory requirements
In addition, in our opinion, the Bank has maintained proper accounting records and the consolidated financial statements are in agreement therewith. We have reviewed the accompanying report of the chairman and confirm that the information contained therein is consistent with the consolidated financial statements. We are not aware of any violations of the Bahrain Commercial Companies Law 2001, the Central Bank of Bahrain and Financial Institutions Law 2006, the terms of the Bank's license or its memorandum and articles of association having occurred during the year ended 31 December 2008 that might have had a material effect on the business of the Bank or on its financial position. Satisfactory explanations and information have been provided to us by the management in response to all our requests.



CONSOLIDATED BALANCE SHEET
as at 31 December 2008 US$ 000's

	Note	2008	2007
ASSETS			
Cash and bank balances	4	13,863	15,383
Placements with financial institutions	5	1,275,675	711,978
Financing assets	6	69,189	96,179
Assets held-for-sale	7	611,996	446,882
Investment in associates	8	451,024	288,047
Available-for-sale investments	9	406,892	246,346
Receivable from investment banking services		222,343	171,183
Other assets	10	434,065	269,069
Total assets		**3,485,047**	2,245,067
LIABILITIES			
Investors' funds	14	538,784	139,876
Placements from financial and other institutions	15	937,538	355,548
Financing liabilities	16	634,895	586,620
Liabilities directly associated with assets held-for-sale	7	317,186	167,019
Other liabilities	17	87,826	115,674
Total liabilities		**2,516,229**	1,364,737
Unrestricted investment accounts	18	**1,945**	826
EQUITY			
Share capital	19	262,813	238,921
Treasury shares		(17,364)	(8,926)
Share premium		180,382	180,382
Statutory reserve		106,700	83,529
Share grants reserve	27	23,508	-
Investments fair value reserve		1,132	2,799
Retained earnings		409,702	382,799
Total equity (page 8)		**966,873**	879,504
Total liabilities, unrestricted investment accounts and equity		**3,485,047**	2,245,067
Off-balance sheet items			
Restricted investment accounts (page 11)		**74,222**	77,038

The consolidated financial statements, which consist of pages 6 to 58, were approved by the Board of Directors on 28 January 2009 and signed on its behalf by:

Esam Yousif A. Janahi
Chairman

Hamad A Aziz Al-Shaya
Vice-Chairman

Salah H. Rahimi
Deputy Chief Executive Officer

The accompanying notes 1 to 43 form an integral part of these consolidated financial statements.

CONSOLIDATED INCOME STATEMENT
for the year ended 31 December 2008

US$ 000's

	Note	2008	2007
Income from investment banking services	20	453,191	400,180
Placement, arrangement and management fees		33,233	13,421
Income from placements with financial institutions		29,555	38,821
Income from financing		1,533	10,118
Income from investment in associates	22	94,968	21,883
Income from available-for-sale investments	23	1,830	12,683
Income from partial sale of a subsidiary	24	-	83,826
Other income, net		3,276	7,051
Total income		**617,586**	587,983
Staff cost	25	134,542	103,798
Investment advisory expenses		48,524	48,351
Impairment allowances	26	39,712	15,362
Finance cost	21	63,507	56,482
Other expenses		39,416	20,732
Total expenses		**325,701**	244,725
Profit for the year		**291,885**	343,258
Attributable to:			
Shareholders of the parent Bank		291,885	340,063
Minority interest		-	3,195
		291,885	343,258
Earnings per share (US cents)			
Basic and diluted	31	**37.01**	42.79

The accompanying notes 1 to 43 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
for the year ended 31 December 2008

US$ 000's

2008	Share Capital	Treasury shares	Share premium	Statutory reserve	Share grants reserve	Invest-ments fair value reserve	Retained earnings	Total equity
Balance at 1 January 2008	238,921	(8,926)	180,382	83,529	-	2,799	382,799	879,504
Net fair value changes during the year	-	-	-	-	-	(1,667)	-	(1,667)
Net income recognised directly in equity	-	-	-	-	-	(1,667)	-	(1,667)
Profit for the year	-	-	-	-	-	-	291,885	291,885
Total recognised income and expense	**-**	**-**	**-**	**-**	**-**	**(1,667)**	**291,885**	**290,218**
Issue of bonus shares	23,892	-	-	-	-	-	(23,892)	-
Share grants vesting expense (note 27)	-	-	-	-	23,508	-	-	23,508
Dividend declared for 2007	-	-	-	-	-	-	(203,083)	(203,083)
Charity contribution declared for 2007	-	-	-		-	-	(3,000)	(3,000)
Board remuneration declared for 2007	-	-	-	-	-	-	(5,000)	(5,000)
Zakah contribution declared for 2007	-	-	-	-	-	-	(281)	(281)
Loss on sale of treasury shares	-	-	-	(6,555)	-	-	-	(6,555)
Purchase of treasury shares	-	(24,300)	-	-	-	-	-	(24,300)
Sale of treasury shares	-	15,862	-	-	-	-	-	15,862
Transfer to statutory reserve	-	-	-	29,726	-	-	(29,726)	-
Balance at 31 December 2008	**262,813**	**(17,364)**	**180,382**	**106,700**	**23,508**	**1,132**	**409,702**	**966,873**

The accompanying notes 1 to 43 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
for the year ended 31 December 2008 (continued)

US$ 000's

2007	Attributable to the shareholders of the parent									Minority interest	Total equity
	Share Capital	Advance towards share capital	Treasury Shares	Share premium	Subsidiary company share grants	Statutory reserve	Invest-ments fair value reserve	Retained earnings	Total		
Balance at 1 January 2007	212,674	2,708	(14,127)	178,321	1,804	46,337	364	239,663	667,744	-	667,744
Net fair value changes during the year	-	-	-	-	-	-	2,406	-	2,406	-	2,406
Transfer to income statement on disposal of available-for-sale investments	-	-	-	-	-	-	29	-	29	-	29
Net income recognised directly in equity	-	-	-	-	-	-	2,435	-	2,435	-	2,435
Net profit for the year	-	-	-	-	-	-	-	340,063	340,063	3,195	343,258
Total recognised income and expense	-	-	-	-	-	-	2,435	340,063	342,498	3,195	345,693
Issue of bonus shares	25,600	-	-	-	-	-	-	(25,600)	-	-	-
Increase in share capital	647	(2,708)	-	2,061	-	-	-	-	-	-	-
Share grants vesting charge for the period	-	-	-	-	90	-	-	-	90	-	90
Dividend declared for 2006	-	-	-	-	-	-	-	(134,391)	(134,391)	-	(134,391)
Charity contribution declared for 2006	-	-	-	-	-	-	-	(1,598)	(1,598)	-	(1,598)
Board remuneration declared for 2006	-	-	-	-	-	-	-	(1,375)	(1,375)	-	(1,375)
Zakah contribution declared for 2006	-	-	-	-	-	-	-	(1,402)	(1,402)	-	(1,402)
Profit on sale of treasury shares	-	-	-	-	-	2,737	-	-	2,737	-	2,737
Purchase of treasury shares	-	-	(50,193)	-	-	-	-	-	(50,193)	-	(50,193)
Sale of treasury shares	-	-	55,394	-	-	-	-		55,394	-	55,394
Allocation of minority interest on partial sale of shares in a subsidiary during the year	-	-	-	-	-	-	-	-	-	192,011	192,011
De-recognition on sale of controlling stake in a subsidiary (note 24)	-	-	-	-	(1,894)	(2,999)	-	4,893	-	(195,206)	(195,206)
Transfer to statutory reserve	-	-	-	-	-	37,454	-	(37,454)	-	-	-
Balance at 31 December 2007	238,921	-	(8,926)	180,382	-	83,529	2,799	382,799	879,504	-	879,504

The accompanying notes 1 to 43 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS
for the year ended 31 December 2008 US$ 000's

	2008	2007
OPERATING ACTIVITIES		
Proceeds from investment banking services	281,785	292,396
Placements from financial and other institutions, net	586,625	334,745
Cash receipts from 'water park' operations	5,980	-
Net increase in customers' current accounts	-	63,682
Financing assets, net	11,504	(116,256)
Short term financing of projects	(91,368)	(98,202)
Investors' funds received/ (paid), net	391,416	(324,562)
Placement, arrangement and management fees received	31,430	9,484
Income from financing assets	519	-
Income from short-term placements received	29,555	38,821
Finance expense	(63,700)	(56,483)
Payments for expenses	(255,188)	(160,217)
Cash flows from operating activities	**928,558**	(16,592)
INVESTING ACTIVITIES		
Net cash flows from partial sale of shares of a subsidiary	-	(30,204)
Net cash flow from available-for-sale investments	(62,307)	(41,063)
Purchase of investment in associates, net	(113,003)	(114,509)
Distributions received from associates	28,252	-
Cash flows in relation to a subsidiary held-for-sale, net	(38,627)	(239,171)
Proceeds from sale of trading and investment property	-	34,207
Income from sukuks received	-	4,523
Acquisition of a subsidiary	(8,351)	(50,000)
Payment for purchase of equipment and capital work-in-progress	(11,939)	(11,661)
Dividends received and other income	6,139	5,326
Cash flows from investing activities	**(199,836)**	(442,552)
FINANCING ACTIVITIES		
Financing liabilities, net	50,218	498,758
Net receipts from unrestricted investment accounts	1,119	82,946
Acquisition of treasury shares, net	(14,993)	14,106
Cash paid to charitable organisations	(1,313)	(1,857)
Board remuneration paid	(5,000)	(1,375)
Dividends paid	(196,576)	(130,075)
Cash flows from financing activities	**(166,545)**	462,503
Net increase in cash and cash equivalents	**562,177**	3,359
Cash and cash equivalents at 1 January	727,361	724,002
Cash and cash equivalents at 31 December	**1,289,538**	727,361
Cash and bank balances	13,863	15,383
Placements with financial institutions	1,275,675	711,978
	1,289,538	727,361

The accompanying notes 1 to 43 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN RESTRICTED INVESTMENT ACCOUNTS
for the year ended 31 December 2008

2008	Balance at 1 January 2008			Movements during the year						Balance at 31 December 2008		
Company	No of units (000)	Average value per share US$	Total US$ 000's	Investment US$ 000's	Revaluation US$ 000's	Gross income US$ 000's	Dividends paid US$ 000's	Bank's fees as an agent US$ 000's	Administration expenses US$ 000's	No of units (000)	Average value per share US$	Total US$ 000's
Mena Real Estate Company KSCC	150	0.37	58	-	(4)	-	-	-	-	150	0.36	54
Kuwait National Real Estate Investment & Services Co. KSCC	1,130	0.37	414	(712)	8	380	-	-	-	250	0.36	90
Gulf Holding Company	10,000	0.37	3,663	-	(39)	-	-	-	-	10,000	0.36	3,624
Gulf North Africa Holding Company KSCC	11,500	0.37	4,212	-	(44)	318	(318)	-	-	11,500	0.36	4,168
Gulf Real Estate Development Company	936	13.33	12,471	-	1	843	(843)	-	-	936	13.32	12,472
Al Basha'er Fund	245	13.72	3,365	(580)	(1,175)			-	-	203	7.93	1,610
Pan European Fund	35.85	1,474.40	52,855	-	(2,279)	2,834	(2,834)	-	-	35.85	1,410.76	50,576
Oman Development Company	-	-	-	1,628	-	-	-	-	-	522.50	3.12	1,628
			77,038	**336**	**(3,532)**	**4,375**	**(3,995)**	**-**	**-**			**74,222**

The accompanying notes 1 to 43 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN RESTRICTED INVESTMENT ACCOUNTS
for the year ended 31 December 2008 (continued)

2007	Balance at 1 January 2007			Movements during the year						Balance at 31 December 2007		
Company:	No of units (000)	Average value per share US$	Total US$ 000's	Investment US$ 000's	Revaluation US$ 000's	Gross income US$ 000's	Dividends paid US$ 000's	Bank's fees as an agent US$ 000's	Administration expenses US$ 000's	No of units (000)	Average value per share US$	Total US$ 000's
Mena Real Estate Company KSCC (formerly known as Gulf Development Real Estate Company KSCC)	10,910	0.35	3,775	(3,720)	3	(1,175)	1,175	-	-	150	0.37	58
Kuwait National Real Estate Investment & Services Co. KSCC	6,870	0.35	2,376	(1,985)	23	-	-	-	-	1,130	0.37	414
Bayan Holding Company KSCC	18,266	0.35	6,316	(6,316)	-	-	-	-	-	-	-	-
Gulf Holding Company	23,919	0.35	8,271	(4,813)	205	-	-	-	-	10,000	0.37	3,663
Gulf North Africa Holding Company KSCC	11,500	0.35	3,976	-	236	-	-	-	-	11,500	0.37	4,212
Gulf Real Estate Development Co (formerly known as Saudi Real Estate Company)	936	13.33	12,472	-	(1)	-	-	-	-	936	13.33	12,471
Al Basha'er Fund	753	8.97	6,751	(5,072)	-	1,792	-	(106)	-	245	13.72	3,365
Pan European Fund	35.85	1,315.40	47,155	-	5,700	4,943	(4,943)	-	-	35.85	1,474.40	52,855
Energy City Qatar Holding Company	-	-	-	18,000	-	6,300	(24,300)	-	-	-	-	-
Al Hareth French Property Fund	24.65	1,210.40	32,301	(34,129)	1,077	2,378	(1,585)	(42)	-	-	-	-
			123,393	(38,035)	7,243	14,238	(29,653)	(148)	-			77,038

The accompanying notes 1 to 43 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF SOURCES AND USES OF CHARITY AND ZAKAH FUND

for the year ended 31 December 2008

US$ 000's

	2008	2007
Sources of charity and zakah fund		
Contributions by the Bank	3,281	3,000
Non-Islamic income (note 33)	94	192
Total sources	**3,375**	3,192
Uses of charity fund and zakah fund		
Contributions to charitable organisations	(1,313)	(1,857)
Deconsolidation due to sale of subsidiary	-	(313)
Total uses	**(1,313)**	(2,170)
Excess of sources over uses	2,062	1,022
Undistributed charity and zakah fund at 1 January	3,656	2,634
Undistributed charity and zakah fund at 31 December (note 17)	**5,718**	3,656

The accompanying notes 1 to 43 form an integral part of these consolidated financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2008 US$ 000's

1 INCORPORATION AND PRINCIPAL ACTIVITY

Gulf Finance House BSC ("the Bank") was incorporated in 1999 in the Kingdom of Bahrain under Commercial Registration No. 44136. The Bank's shares are listed on the Bahrain, Kuwait and Dubai Financial Market Stock Exchanges. The Bank's Global Depository Receipts ('GDR') are listed in the London Stock Exchange (refer note 19). The Bank operates as an Islamic Wholesale Investment Bank under a license granted by the Central Bank of Bahrain ("CBB").

The Bank's activities are regulated by the CBB and supervised by a Religious Supervisory Board whose role is defined in the Bank's Memorandum and Articles of Association.

The principal activities of the Bank include investment advisory services and investment transactions which comply with Islamic rules and principles according to the opinion of the Bank's Shari'a Board.

Consolidated financial statements
The consolidated financial statements for the year comprise the financial statements of the Bank and its subsidiaries (together referred to as "the Group").

The significant wholly owned subsidiaries of the Bank include Al Areen Leisure and Tourism Company – 'The Lost Paradise of Dilmun SPC' ("water park") (refer note 11), Legends Development Company LLC (refer note 7) and Injazat Capital Limited (refer note 13).

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.

(a) Statement of compliance

The consolidated financial statements have been prepared in accordance with both the Financial Accounting Standards ('FAS') issued by the Accounting and Auditing Organisation for Islamic Financial Institutions and International Financial Reporting Standards ('IFRS').

(b) Basis of preparation

The financial statements are presented in US Dollars, being the principal currency of the Group's operations. They are prepared on the historical cost basis except for the measurement at fair value of certain risk management instruments, available-for-sale investments and investments in associates designated at fair value through profit or loss.

The preparation of financial statements in conformity with the IFRS 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. 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 3.

(c) Basis of consolidation

(i) *Subsidiaries*

Subsidiaries are those enterprises (including special purpose vehicles) controlled by the Bank. Control exists when the Group has the power, directly or indirectly, to govern the financial and operating policies of an enterprise so as to obtain benefits from its activities. Subsidiaries are consolidated from the date on which control is transferred to the Group and de-consolidated from the date that control ceases. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill.

2 *Significant accounting policies (continued)*

(ii) ***Associates***

Associates are those enterprises in which the Group hold, directly or indirectly, more than 20% of the voting power or exercises significant influence, but not control, over the financial and operating policies. On initial recognition of investment in each associate, the Bank makes an accounting policy choice as to whether the associate shall be equity accounted or designated as an investment at fair value through profit or loss.

The Group, being a venture capital organisation, designates certain of its investments in associates, as allowed by IAS 28 'Investments in Associates', as 'investments carried at fair value through profit or loss in accordance with IAS 39 [refer note 2 (e)].

If the equity accounting method is chosen for an associate, the consolidated financial statements include the Group's share of the associate's total recognised gains and losses. When the Group's share of losses exceeds its interest in an associate, the Group's carrying amount is reduced to nil and recognition of further losses is discontinued except to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of an associate.

(iii) ***Transactions eliminated on consolidation***

Intra-group balances and transactions, and any unrealised gains arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Unrealised losses are also eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment. Accounting policies of the subsidiary and associates have been changed where necessary to ensure consistency with the policies adopted by the Group.

(d) Foreign currency transactions

(i) ***Functional and presentation currency***

Items included in the consolidated financial statements are measured using the currency of the primary economic environment in which the entity operates (the functional currency). The consolidated financial statements are presented in US dollars, which is the Bank's functional and presentation currency.

(ii) ***Transactions and balances***

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement. Translation differences on non-monetary items carried at their fair value, such as certain available-for-sale equity securities, are included in investments fair value reserve.

(iii) ***Group companies***

The other Group companies functional currencies are either denominated in US dollars or currencies which are effectively pegged to the US Dollar, and hence, the translation of financial statements of the group entities that have a functional currency different from the presentation currency do not result in exchange differences.

2 *Significant accounting policies (continued)*

(e) Financial assets and liabilities

(i) Recognition and de-recognition

The Group initially recognises placements, financing assets, receivables, investors' funds and financing liabilities on the date at which they are originated. All other financial assets and liabilities are recognised at the trade date i.e. the date that the Group contracts to purchase or sell the asset, at which the Group becomes party to the contractual provisions of the instrument.

A financial asset or liability is initially measured at fair value which is the value of the consideration given (in the case of an asset) or received (in the case of a liability), including transaction costs that are directly attributable to its acquisition or issue.

The Group derecognises a financial asset when the rights to receive cash flows from the financial assets have expired or where the Group has transferred substantially all risk and rewards of ownership. The Group writes off certain financial assets when they are determined uncollectible. The Group derecognises a financial liability when its contractual obligations are discharged, cancelled or expire.

(ii) Measurement principles

Financial assets are measured either at fair value, amortised cost or in certain cases carried at cost.

Fair value measurement

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

When available, the Group measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm's length basis. If a market for a financial instrument is not active, the Group establishes fair value using a valuation technique. Valuation techniques include using recent arm's length transactions between knowledgeable, willing parties (if available), discounted cash flow analyses and other valuation models with accepted economic methodologies for pricing financial instruments.

Amortised cost measurement

The amortised cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the effective profit method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment. The calculation of the effective profit rate includes all fees and points paid or received that are an integral part of the effective profit rate.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2008 US$ 000's

2 Significant accounting policies (continued)

(f) Investments

(i) Classification

Investments, excluding investments in subsidiaries and equity accounted associates, are classified as carried at fair value through profit or loss, held-to-maturity or available-for-sale.

Investments carried at fair value through profit or loss are financial assets that are held for trading or which upon initial recognition are designated by the Group as at fair value through income statement. These include investment in certain associates [refer note 2 (c) (ii)].

Held-to-maturity investments are financial assets with fixed or determinable payments and fixed maturity that the Group has the positive intention and ability to hold to maturity, and which are not designated as carried at fair value through profit or loss or as available-for-sale.

Available-for-sale investments are financial assets that are not investments carried at fair value through profit or loss or held-to-maturity or loans and receivables. These include investments in quoted and unquoted equity securities.

(ii) Recognition

Investment securities are initially recognised at fair value, plus transaction costs for all financial assets not carried at fair value through profit or loss. Investments carried at fair value through profit or loss are initially recognised at fair value, and transaction cost are expensed in the profit or loss. Investment securities are subsequently accounted for depending on their classification as either held-to-maturity, fair value through profit or loss, or available-for-sale.

(iii) Subsequent measurement

Subsequent to initial recognition, investments at fair value through profit or loss and available-for-sale investments are re-measured to fair value. Held-to-maturity investments are measured at amortised cost less any impairment allowances. Available-for-sale investments which 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.

(iv) Gains and losses on subsequent measurement

Gains and losses arising from a change in the fair value of investments carried at fair value through profit or loss are recognised in the income statement in the period in which they arise. Gains and losses arising from a change in the fair value of available-for-sale investments are recognised in a separate fair value reserve in equity and when the investments are sold, impaired, collected or otherwise disposed of, the cumulative gain or loss previously recognised in the fair value reserve is transferred to the income statement.

(v) Fair value measurement principles

Fair value for quoted investments is their market bid price. For other unquoted investments, fair value is determined either by reference to the price of the most recent transactions in the shares, or based on recognised internal valuation models, or based on valuations undertaken by independent external valuers. For certain investments, the Group uses proprietary models, which usually are developed from recognised valuation models for fair valuation of certain available-for-sale investments and investments in associates designated at fair value through the profit or loss.

Some or all of the inputs into these models may not be market observable, but are estimated based on assumptions. Valuation adjustments are recorded to allow for model risks, bid-ask spreads, liquidity risks, as well as other factors. Management believes that these valuation adjustments are necessary and appropriate to fairly state the values of these investments.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2008 US$ 000's

2 *Significant accounting policies (continued)*

(g) Assets held-for-sale

(i) Classification

The Group classifies non-current assets or disposal groups as held for sale if its carrying amount is expected to be recovered principally through a sale transaction rather than through continuing use within twelve months. A disposal group is a group of assets to be disposed of, by sale or otherwise, together as a group in a single transaction, and liabilities directly associated with those assets that will be transferred in the transaction. A subsidiary acquired exclusively with a view to resale is classified as disposal group held for sale and income and expense from its operations are presented as part of discontinued operation in accordance with IFRS 5 "Non-current Assets Held for Sale and Discontinued Operations".

If the criteria for classification as held for sale are no longer met, the entity shall cease to classify the asset (or disposal group) as held for sale and shall measure the asset at the lower of its carrying amount before the asset (or disposal group) was classified as held for sale, adjusted for any depreciation, amortisation or revaluations that would have been recognised had the asset (or disposal group) not been classified as held for sale and its recoverable amount at the date of the subsequent decision not to sell. The Bank continues to classify non-current assets or disposal groups as held for sale where events or circumstances beyond the control of the Bank extend the period to complete the sale beyond twelve months and the Bank remains committed to its plan to sell.

(ii) Measurement

Non-current assets or disposal groups classified as held for sale, other than financial instruments measured under International Accounting Standard ('IAS') 39 'Financial Instruments: Recognition and Measurement', are measured at the lower of its carrying amount and fair value less costs to sell. Financial instruments that are non-current assets and 'held for sale' are carried at fair value in accordance with IAS 39.

(h) Placements with and from financial institutions

These comprise placements made or received in the form of international commodity murabaha contracts. Placements are usually short term in nature and are stated at their amortised cost.

(i) Financing assets

Financing assets comprise shari'a compliant commercial financing provided by the Group which are stated at amortised cost less impairment allowances.

(j) Cash and cash equivalents

For the purpose of statement of cash flows, cash and cash equivalents comprise cash, balances with banks and short-term highly liquid assets, (commodity Murabahas and certain short-term sukuks) with maturities of three months or less when acquired which are subject to insignificant risk of changes in fair value and are used by the Group in the management of its short-term commitments.

(k) Operating property and equipment

Operating property and equipment comprise assets used in the operations of the water park. Other equipment include assets used by the Bank. All property and equipment are stated at cost, net of accumulated depreciation. Depreciation is computed using the straight-line method to write-off the cost of the assets over their estimated useful lives ranging from 1 to 5 years for furniture, fixtures and equipments, motor vehicles and computers. Building is depreciated over a period 20 years. The assets residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2008 US$ 000's

2 *Significant accounting policies (continued)*

(l) **Impairment of assets**

The Bank assesses at each balance sheet date whether there is objective evidence that a asset is impaired. Objective evidence that financial assets (including equity securities) are impaired can include default or delinquency by a borrower, restructuring of a loan or advance by the Group on terms that the Group would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlate with defaults in the group. In addition, for an investment in an equity security, a significant or prolonged decline in its fair value below its cost is objective evidence of impairment.

Financial assets carried at amortised cost

For financial assets carried at amortised cost impairment is measured as the difference between the carrying amount of the financial assets and the present value of estimated cash flows discounted at the assets' original effective profit rate. Losses are recognised in income statement and reflected in an allowance account. When a subsequent event causes the amount of impairment loss to decrease, the impairment loss is reversed through the income statement.

Available-for-sale investments

In the case of investments in equity securities classified as available-for-sale and measured at fair value, a significant or prolonged decline in the fair value of the security below its cost is considered in determining whether the assets are impaired. If any such evidence exists for available-for-sale investments, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognised in income statement – is removed from equity and recognised in the income statement. Impairment losses recognised in the income statement on equity instruments are not subsequently reversed through the income statement. For available-for-sale investments carried at cost, the Group makes an assessment of whether there is an objective evidence of impairment for each investment by assessment of financial and other operating and economic indicators. Impairment is recognised if the estimated recoverable amount is assessed to be below the cost of the investment.

Other non-financial assets

The carrying amount of the Group's assets or its cash generating unit, other than financial assets, are reviewed at each balance sheet date to determine whether there is any indication of impairment. A cash generating unit is the smallest identifiable asset group that generates cash flows that largely are independent from other asset and groups. If any such indication exists, the asset's recoverable amount is estimated. The recoverable amount of an asset or a cash generating unit is the greater of its value in use or fair value less costs to sell. An impairment loss is recognised whenever the carrying amount of an asset or its cash generating unit exceeds its estimated recoverable amount. Impairment losses are recognised in the income statement. Impairment losses are reversed only if there is an indication that the impairment loss may no longer exist and there has been a change in the estimates used to determine the recoverable amount. Separately recognised goodwill is tested annually for impairment and carried at cost less accumulated impairment losses. Impairment losses on goodwill are not reversed.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2008 US$ 000's

2 *Significant accounting policies (continued)*

(m) Risk management instruments

The Group enters into shari'a compliant foreign exchange risk management instruments on behalf of its customers/ projects on a back-to-back basis and does not retain significant open positions. These derivative-type risk management instruments are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at their fair value. The fair value of a instrument is the equivalent of the unrealised gain or loss from marking to market the instrument using prevailing market rates. Instruments with positive market values (unrealised gains) are disclosed under other assets and instruments with negative market values (unrealised losses) are disclosed under other liabilities in the balance sheet. For risk management instruments that are not designated in a qualifying hedge relationship, all changes in its fair value are recognised immediately in the income statement.

(n) Financing liabilities

Financing liabilities comprise shari'a compliant financing facilities from financial institutions and financing raised through issue of Sukuk. Financing liabilities are initially measured at fair value plus transaction costs, and subsequently measured at their amortised cost using the effective profit rate method.

(o) Dividends and board remuneration

Dividends to shareholders and board remuneration are recognised as liabilities in the period in which they are declared.

(p) Treasury shares

The amount of consideration paid including all directly attributable costs incurred in connection with the acquisition of the treasury shares are recognised in equity. Consideration received on sale of treasury shares is presented in the financial statements as a change in equity. No gain or loss is recognised on the Group's income statement on the sale of treasury shares.

(q) Statutory reserve

The Bahrain Commercial Companies Law 2001 requires that 10 percent 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 percent of the paid up share capital.

(r) Revenue recognition

Income from investment banking services is recognised when the service is provided and income is earned. This is usually when the Bank has performed all significant acts in relation to a transaction and it is highly probable that the economic benefits from the transaction will flow to the Bank. Significant acts in relation to a transaction are determined based on the terms agreed in the private placement memorandum/ contracts for each transaction. The assessment of whether economic benefits from a transaction will flow to the Bank is determined when legally binding commitments have been obtained from underwriters and external investors for a substantial investment in the transaction. Income is then recognised on a pro-rata basis to the extent of such firm commitments received at the reporting date.

Income from investment banking services is received either in cash or in kind (i.e. equity shares in the investment being promoted by the Bank). Income received in kind is measured at the fair value of the consideration received. Generally the shares received are in privately held entities and there is no immediate market for trading. Fair value of consideration received in the form of shares is measured by reference to the transaction price paid by investors and as per the agreed pricing terms specified in the private placement memorandums.

Placement, arrangement and management fees are recognised as income when earned and the related services are performed.

2 Significant accounting policies (continued)

(r) Revenue recognition (continued)

Income from placements with financial institutions are recognised on a time-apportioned basis over the period of the related contract.

Income from financing assets is recognised using the effective profit rates of the assets over the period of the contract.

Income from investments (**dividend income**) is recognised when the right to receive is established. This is usually the ex-dividend date for equity securities.

(s) Restricted investment accounts

Restricted investment accounts represents assets acquired by funds provided by holders of restricted investment accounts and their equivalent and managed by the Group as an investment manager based on either a Mudaraba contract or agency contract. The restricted investment accounts are exclusively restricted for investment in specified projects as directed by the investments account holders. Assets that are held in such capacity are not included as assets of the Bank in the consolidated financial statements.

(t) Unrestricted investment accounts

Unrestricted investment accounts are funds held by the Group, which it can invest at its own discretion. The unrestricted investment account holder authorises the Group to invest the account holders' funds 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. The Group charges management fee (Mudarib fees) to unrestricted investment account holders. Of the total income from unrestricted investment accounts, the income attributable to customers is allocated to investment accounts after setting aside provisions, reserves and deducting the Group's share of income. The allocation of income is determined by the management of the Group within the allowed profit sharing limits as per the terms and conditions of the unrestricted investment accounts. Administrative expenses incurred in connection with the management of the funds are borne directly by the Group and are not charged separately to investment accounts. Unrestricted investment accounts are carried at their book values and include amounts retained towards profit equalisation and investment risk reserves.

(u) 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 account where the Bank uses these funds for charitable means.

(v) Zakah

Pursuant to the decision of the shareholders', the Group is required to pay Zakah on its undistributed profits. The Group is also required to calculate and notify, under a separate report, individual shareholders of their pro-rata share of the Zakah payable by them on distributed profits. These calculations are approved by the Group's Shari'a Supervisory Board.

(w) Employees benefits

(i) Short-term benefits

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided. A provision is recognised for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

2 *Significant accounting policies (continued)*

(w) *Employees benefits (continued)*

(ii) Post employment benefits

Pensions and other social benefits for Bahraini employees are covered by the General Organisation for Social Insurance scheme, which is a "defined contribution scheme" in nature under IAS 19 'Employee Benefits', and to which employees and employers contribute monthly on a fixed-percentage-of-salaries basis. Contributions by the Bank are recognised as an expense in income statement when they are due.

Expatriate employees on fixed contracts are entitled to leaving indemnities payable under the Bahraini Labour Law for the Private Sector of 1976, based on length of service and final remuneration. Provision for this unfunded commitment, , which is a "defined benefit scheme" in nature under IAS 19, has been made by calculating the notional liability had all employees left at the balance sheet date. These benefits are in the nature of a "defined benefit scheme" and any increase or decrease in the benefit obligation is recognised in the income statement.

The Bank also operates a voluntary employees saving scheme under which the Bank and the employee contribute monthly on a fixed percentage of salaries basis. The scheme is managed and administered by a board of trustees who are employees of the Bank. The scheme is in the nature of a defined contribution scheme and contributions by the Bank are recognised as an expense in the income statement when they are due.

(iii) Share-based employee incentive scheme

The Bank operates a share-based incentive scheme for its employees (the "Scheme") whereby employee are granted the Bank's shares as compensation on achievement of certain market and non-market based performance conditions and service conditions (the 'vesting conditions').

The grant date fair value of equity instruments granted to employees is recognised as an employee expense, with a corresponding increase in equity over the period in which the employees become unconditionally entitled to the share awards.

Market conditions are taken into account when estimating the fair value of the equity instrument but are not considered for the purpose of estimating the number of equity instruments that will vest. Service and non-market performance conditions attached to the transactions are not taken into account in determining fair value but are considered for the purpose of estimating the number of equity instruments that will vest. The amount recognised as an expense is adjusted to reflect the number of share awards for which the related service and non-market performance vesting conditions are expected to be met, such that the amount ultimately recognised as an expense is based on the number of share awards that do meet the related service and non-market performance conditions at the vesting date. Amount recognised as expense are not trued-up for failure to satisfy a market condition.

(x) Provisions

A provision is recognised if, as a result of a past event, the Group has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation.

(y) Segment reporting

A segment is a distinguishable component of the Group that is engaged either in providing products or services (business segment) or in providing products or services within a particular environment (geographical segment), which is subject to risks and rewards that are different from those of other segment. The Group only operates in one primary segment of investment banking and other segments are not material.

3 CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES

The Group makes estimates and assumptions that effect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectation of future events that are believed to be reasonable under the circumstances.

Judgements

(i) Classification of investments

In the process of applying the Group's accounting policies, management decides on acquisition of an investment whether it should be classified as investments designated at fair value through profit or loss, held-to-maturity or available-for-sale investment securities. The classification of each investment reflects the management's intention in relation to each investment and is subject to different accounting treatments based on such classification [refer note 2 (f)].

(ii) Classification as assets held-for-sale

The Group classifies non-current assets or disposal groups as 'held for sale' if it's carrying amount is expected to be recovered principally through a sale transaction rather than through continuing use. In addition, the sale is expected to be completed within one year from the date of classification. The expected time of completion of sale and management's plan to sell is based on management assumptions in relation to the condition of the asset and its current performance and requires judgment. There is no certainty on the execution and completion of the sale transaction and any changes in the plan to sell may cause the classification of the disposal group to be changed and consequently the basis of measurement, presentation and disclosure in the consolidated financial statements.

(iii) Special purpose entities

The Group sponsors the formation of special purpose entities (SPE's) primarily for the purpose of allowing clients to hold investments. The Group provides corporate administration, investment management and advisory services to these SPE's, which involve the Group making decisions on behalf of such entities. The Group administers and manages these entities on behalf of its clients, who are by and large third parties and are the economic beneficiaries of the underlying investments. The Group does not consolidate SPE's that it does not have the power to control. In determining whether the Group has the power to control an SPE, judgements are made about the objectives of the SPE's activities, its exposure to the risks and rewards, as well as about the Group intention and ability to make operational decisions for the SPE and whether the Group derives benefits from such decisions.

Estimations

(i) Fair value of investments

The Group determines fair values of investment in associates designated at fair value through profit or loss that are not quoted in active markets by using valuation techniques such as discounted cash flows and recent transaction prices. Fair value estimates are made at a specific point in time, based on market conditions and information about the investee companies. These estimates are subjective in nature and involve uncertainties and matters of significant judgement and therefore, cannot be determined with precision. There is no certainty about future events (such as continued operating profits and financial strengths). It is reasonably possible, based on existing knowledge, that outcomes within the next financial year that are different from assumptions could require a material adjustment to the carrying amount of the investments. In case where discounted cash flow models have been used to estimate fair values, the future cash flows have been estimated by the management based on information from and discussions with representatives of the management of the investee companies, and based on the latest available audited and un-audited financial statements.

3 *CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES (continued)*

(ii) Impairment on available-for-sale investments

The Group determines that available-for-sale investments are impaired when there has been a significant or prolonged decline in the fair value below its cost. This determination of what is significant or prolonged requires judgment and is assessed for each investment separately. In case of quoted equity securities, the Group considers a decline of more than 30% in the fair value below cost to be significant and considers a decline below cost which persists for more than 6 months as prolonged.

Where fair values are not readily available and the investments are carried at cost, the recoverable amount of such investment is estimated to test for impairment. A significant portion of the Group's available-for-sale investments comprise of investments in long-term real estate development projects. In making a judgment of impairment, the Group evaluates among other factors, evidence of a deterioration in the financial health of the project, impacts of delays in execution, industry and sector performance, changes in technology, and operational and financing cash flows. It is reasonably possible, based on existing knowledge, that the current assessment of impairment could require a material adjustment to the carrying amount of the investments within the next financial year due to significant changes in the assumptions underlying such assessments.

(iii) Impairment on financing assets

Each counterparty exposure is evaluated individually for impairment and is based upon management's best estimate of the present value of the cash flows that are expected to be received. In estimating these cash flows, management makes judgements about a counterparty's financial situation, level of subordination available to the Bank and the net realisable value of any underlying assets. Each asset is assessed on its merits, and the workout strategy and estimate of cash flows considered recoverable are independently evaluated by the Risk Management Department and approved by the Board of Directors.

(iv) Impairment of cash generating units

Cash generating includes the Group's investments in certain subsidiaries that generate cash flows that are largely independent from other assets and activities of the Group. The basis of impairment assessment for such cash generating units is described in accounting policy 2 (l). It is the Group's intention to sell the subsidiary representing a separate cash generating unit through a private placement or sale to an owner-operator of the cash generating unit after sufficient level of operations are achieved. For the purposes of assessment of recoverable amount of a cash generating unit, the Group makes best estimates of the value in use from an owner-operator's perspective. It is reasonably possible, based on existing knowledge, that the current assessment of impairment could require a material adjustment to the carrying amount of these assets within the next financial year due to significant changes in assumptions underlying such assessments.

4 CASH AND BANK BALANCES

	2008	2007
Cash	8	112
Balances with banks	13,802	15,218
Deposit with central bank	53	53
	13,863	15,383

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2008

US$ 000's

5 PLACEMENTS WITH FINANCIAL INSTITUTIONS

	2008	2007
Gross commodity murabahas	1,276,188	713,923
Less: Deferred profits	(513)	(1,945)
	1,275,675	711,978

6 FINANCING ASSETS

	2008	2007
Murabahas	23,039	13,695
Wakala	62,650	82,484
	85,689	96,179
Less: Impairment allowances	(16,500)	-
	69,189	96,179

Murabaha financing receivables are net of deferred profits of US$ 375 (2007: US$ 992).

7 ASSETS AND LIABILITIES HELD-FOR-SALE

	2008	2007
Assets of a subsidiary held-for-sale	611,996	396,882
Investments in associates at fair value through profit or loss	-	50,000
	611,996	446,882
Liabilities directly associated with assets held-for-sale	**317,186**	167,019

Assets and liabilities of a subsidiary held-for-sale represent the Group's investment in a development infrastructure project. During 2008, the Group renegotiated the terms of the projects with the master developer and acquired additional rights to developable land area thus increasing its exposure and liability in the project. The assets of the subsidiary held-for-sale primarily include the freehold project land and the liability mainly represents payables to the owner / master developer towards the land cost.

At 30 June 2008, the Bank negotiated an agreement to assign its participating interest in the project company to a developer for a consideration exceeding the net investment in the subsidiary, subject to the master plan and other related approvals by the master developer. The Bank continues to retain performance obligation to the master developer for the project.

During the year, due to changes in the programme to sell, investments in associates of USD 50 million has been reclassified from assets held-for-sale to investment in associates (note 8).

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8 INVESTMENT IN ASSOCIATES

	2008	2007
- Designated at fair value through profit or loss	41,245	60,361
- Equity accounted	409,779	227,686
	451,024	288,047

(i) INVESTMENTS IN ASSOCIATES - DESIGNATED AT FAIR VALUE THROUGH PROFIT OR LOSS

	2008	2007
At 1 January	60,361	26,626
Acquisitions during the year	15,937	562
Disposals during the year, at carrying value	(17,890)	(2,975)
Reclassified on acquisition of controlling stake (note 13)	(17,163)	-
Fair value changes during the year	-	11,952
	41,245	36,165
Add: Reclassified from assets-held-for-sale	-	24,196
At 31 December	**41,245**	60,361

The Group accounts for certain investment in associates which are managed, evaluated and reported on internally, at fair value through profit or loss. Majority of the Bank's investments under this category are in the process of being liquidated/ exited and for certain investments the Group has received partial distributions during the year. At 31 December 2008, the valuation of such investments has been determined using offer prices and net asset value (for funds) and an appropriate adjustment for liquidity and marketability for current market conditions. The fair values determined were not materially different from the current carrying values of these investments.

The basis of valuation have been reviewed by the Management in terms of the appropriateness of the methodology, soundness of assumptions and correctness of calculations and have been approved by the Board of Directors for inclusion in the financial statements.

Summarised financial information of associates designated at fair value through income statement not adjusted for the percentage ownership held by the Group (based on unaudited management accounts):

	2008	2007
Total assets	97,795	153,384
Total liabilities	25,270	24,446
Total revenues	97,408	86,941
Total net profits / (losses)	8,361	(606)

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8 *INVESTMENT IN ASSOCIATES (continued)*

(ii) ***INVESTMENTS IN ASSOCIATES – EQUITY ACCOUNTED***

	2008	2007
At 1 January	227,686	10,300
Reclassification during the year (note 7)	50,000	132,455
Acquisitions during the year	125,000	75,000
Share of profits from associates	94,968	9,931
Distributions received during the year	(22,779)	-
Disposals during the year, at carrying value	(65,096)	-
At 31 December	**409,779**	227,686

Investment in associates – equity accounted includes the Group's investment of less than 20% in the equity of a financial institution. As the Group exercises significant influence over the financial institution through contractual terms and by way of its presence on the board of directors, the investment is accounted for as an investment in an associate.

During the year, the Group indirectly acquired 49.88% equity stake in Bahrain Financial Harbour Holding Company BSC (c) ('BFH') for US$ 125 million from its investors. The investment has been classified as investment in associates and accounted for under the equity accounting method.

During the year, investment in an associate of US$ 50 million has been reclassified from assets held-for-sale (refer note 7).

Summarised financial information of associates that have been equity accounted not adjusted for the percentage ownership held by the Group:

	2008	2007
Total assets	2,631,054	1,581,912
Total liabilities	1,330,469	665,139
Total revenues	326,494	90,475
Total net profits	218,815	56,423

9 AVAILABLE-FOR-SALE INVESTMENTS

	2008	2007
At 1 January	246,346	320,137
Acquisitions during the year	205,732	81,376
Disposals during the year, at carrying value	(26,308)	(73,190)
De-consolidated on partial sale of subsidiary (note 24)	-	(37,821)
Impairment allowances	(17,211)	(10,526)
Fair value changes during the year	(1,667)	2,406
	406,892	282,382
Less: Reclassified to assets-held-for-sale	-	(36,036)
At 31 December	**406,892**	246,346

9 *AVAILABLE-FOR-SALE INVESTMENTS (continued)*

Investments amounting to US$ 401,665 (2007: US$ 239,448) in unquoted equity securities are carried at cost less impairment in the absence of a reliable measure of fair value. Such investments are either private equity investments managed by external investment managers or represent investments in projects promoted by the Group. The Group intends to exit these investments principally by means of strategic buy outs or through initial public offerings.

The movement in impairment allowances for available-for-sale investments were as follows:

	2008	2007
At 1 January	26,486	15,960
Impairment charge for the year	17,211	10,526
At 31 December	**43,697**	26,486

10 **OTHER ASSETS**

	2008	2007
Project costs recoverable	29,320	38,831
Project financing	216,635	151,587
Receivable from sale of investment securities	58,410	1,427
Operating property and equipment of a water park (note 11)	44,341	47,812
Other equipment (note 12)	19,449	12,042
Goodwill on acquisition of subsidiaries (note 13)	17,375	2,240
Others	48,535	15,130
	434,065	269,069

Impairment allowances recognised during the year amounts to US$ 6,000 (2007: 4,836).

11 **OPERATING PROPERTY AND EQUIPMENT OF A WATER PARK**

During the previous year, the Bank acquired the 'Lost Paradise of Dilmun Water Park', Bahrain (the 'water park') from Al Areen Desert Spa & Resort Holding Company BSC (c). The water park operations were subsequently transferred to Al Areen Leisure and Tourism Company, The Lost Paradise of Dilmun SPC a wholly owned subsidiary of the Bank. The water park commenced commercial operations on 1 August 2007.

Operating property and equipment comprise the assets of the water park. The carrying amount of the water park's operating property and equipment is as follows:

	2008	2007
Cost	49,218	48,405
Accumulated depreciation	(4,877)	(593)
Net carrying value	**44,341**	**47,812**

11 *OPERATING PROPERTY AND EQUIPMENT OF A WATER PARK (continued)*

The results of the water park operations that have been consolidated during the year is as follows:

	31 December 2008 (12 months)	31 December 2007 (9 months)
Gross revenues	6,379	1,651
Operating and other expenses	(7,925)	(3,251)
Depreciation	(4,284)	(593)
Net loss	**(5,830)**	(2,193)

12 **OTHER EQUIPMENT**

	Furniture	Fixtures and equipment	Motor vehicles	Computers	2008 Total	2007 Total
Cost						
At 1 January	1,184	1,278	184	5,181	7,827	7,956
Additions	1,729	12,590	282	5,169	19,770	2,726
Assets of subsidiary acquired during the year	79	438	50	183	750	-
Disposals	(136)	(245)	-	(27)	(408)	
De-consolidated on disposal of subsidiary	-	-	-	-	-	(2,855)
At 31 December	**2,856**	**14,061**	**516**	**10,506**	**27,939**	7,827
Depreciation						
At 1 January	899	1,016	14	2,774	4,703	3,522
Charge for year	418	1,658	83	2,180	4,339	1,880
Disposals	(126)	(234)	-	(27)	(387)	
De-consolidated on disposal of subsidiary	-	-	-	-	-	(699)
At 31 December	**1,191**	**2,440**	**97**	**4,927**	**8,655**	4,703
Net book value At 31 December	**1,665**	**11,621**	**419**	**5,579**	**19,284**	3,124
Capital work-in-progress	-	-	-	165	165	8,918
Total	**1,665**	**11,621**	**419**	**5,744**	**19,449**	12,042

13 ACQUISITION OF A SUBSIDIARY

In July 2008, through a series of purchases, the Bank acquired an additional 61% stake in Injazat Capital Limited (ICL), an existing associate – designated at fair value through profit or loss. ICL is now a wholly owned subsidiary of the Group and is being consolidated with the financial statements of the Bank. ICL is an asset management and investment banking institution registered in the Dubai International Financial Centre. The acquisition had the following effect on the Group's assets and liabilities on the acquisition date:

	Amount on date of acquisition US$ 000's
Net fair value of assets acquired	3,184
Net fair value of liabilities acquired	(1,156)
Net identifiable assets and liabilities	**2,028**
Goodwill on acquisition	15,135
Less: Carrying value of investment on the date of acquisition	(8,333)
Net consideration paid	**8,830**
Less: Cash acquired on date of acquisition	(479)
Net cash out flows on acquisition for the purposes of cash flow statement	**8,351**

The value of assets and liabilities recognised on acquisition are their estimated fair values which are not considered to be different from their carrying value on the date of acquisition. The pre-acquisition carrying value of the assets and liabilities was determined based on applicable IFRS's immediately before the acquisition. The fair values of identifiable assets and liabilities acquired have been determined provisionally for the purposes of the 31 December 2008 consolidated financial statements. The management is currently in the process of completing the transaction related due diligence and identification of potential intangible assets.

The goodwill recognised on the acquisition is attributable mainly to the skills and technical talent of the acquired business's work force, and the synergies expected to be achieved from integrating the license of ICL into the Group's existing business. In December 2008, the license of ICL was upgraded from a investment firm license to a investment banking license.

14 INVESTORS' FUNDS

These represent funds of projects set-up or promoted by the Bank which are placed with the Bank pending utilisation by the projects concerned.

15 PLACEMENTS FROM FINANCIAL AND OTHER INSTITUTIONS

These comprise short-term international commodity murabaha accepted from financial and other institutions as part of the Group's treasury activities.

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16 FINANCING LIABILITIES

	2008	2007
Murabaha financing facility	300,478	397,456
Wakala financing facility	145,788	-
Sukuk liability	188,629	189,164
	634,895	586,620

Financing liabilities comprise murabaha financing facility from financial institutions and financing raised through issue of Sukuk. During the year, the Bank raised additional short term wakala financing of US$ 150 million from a financial institution to support its investment activities.

The Bank announced a US$ 1 billion medium term Sharia'a compliant Sukuk issuance programme (the 'Programme') in 2007. The Programme provides a facility for the issuance of Sukuk Certificates in series (each, a "Series"). Under the terms of the Programme, the Bank has issued its first Series of Sukuk Certificates amounting to US$ 200 million in 2007. The Sukuk Certificates issued under the Programme have a tenure of 5 years and returns based on an agreed spread of 125 bps over the benchmark rate (LIBOR). The Sukuk Certificates issued are secured by a pool of assets of the Group and has a liquidity facility provided by the Bank to support timely payments of distributions under the Programme. The Sukuk Certificates issued have been admitted for trading on the London Stock Exchange's Gilt Edged and Fixed Interest Market. The applicable rate of return of sukuk shall be increased by 0.5% per annum if the investment grading falls below BBB- of the rating agencies.

At 31 December 2008, the Sukuk Certificates are secured by the Bank's investment in associates with carrying values of US$ 284,779 (2007: 215,968). The Wakala financing facility is secured by the Bank's investment in BFH (note 8).

17 OTHER LIABILITIES

	2008	2007
Employee accruals	42,446	87,937
Unclaimed dividends	13,483	5,945
Provision for employees' leaving indemnities	910	458
Charity and zakah fund (refer page 13)	5,718	3,656
Accounts payable	6,321	6,535
Accrued expenses and others	18,948	11,143
	87,826	115,674

18 UNRESTRICTED INVESTMENT ACCOUNTS

Unrestricted investment accounts primarily comprise Mudarabah deposits accepted by the Bank during the year. The average gross rate of return in respect of unrestricted investment accounts was 2.89% for 2008 (2007: 8.51%). Approximately 2.89% / US$ 95 (2007: 5.45% / US$ 5,574) was distributed to investors and the balance was either set aside for provisions and/or retained by the Bank as a Mudarib fee. Unrestricted investment accounts include profit equalisation reserve of US$ 3 (2007: US$ Nil) and investment risks reserve of US$ 2 (2007: US$ Nil). The funds received from unrestricted investment account holders have been commingled and jointly invested with the Group in placements with financial institutions.

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19 SHARE CAPITAL

	2008	2007
Authorised: 909,090,909 ordinary shares of US$ 0.33 each	**300,000**	300,000
Issued and fully paid up: 796,401,811 (2007: 724,001,646) shares of US$ 0.33 each	**262,813**	238,921

During the year, the paid up capital of the Bank increased from US$ 238,921 to US$ 262,813 as a result of issue of bonus shares (ten shares for every hundred shares held) for 2007 amounting to US$ 23,892.

During 2007, the Bank admitted its Global Depository Receipts ('GDR') for listing in the London Stock Exchange (LSE). The Bank and its shareholders offered 106.6 million shares in the form of GDRs in a secondary issue to investors in Europe and USA. Each GDR represents 10 ordinary shares of the Bank.

At 31 December 2008, the Bank held 8,448,808 (2007: 5,089,571) treasury shares.

In the shareholders extra-ordinary meeting held on 17 February 2008, the shareholders approved the increase of authorised capital from US$ 300 million to US$ 500 million. The Bank is currently in the process of obtaining the necessary regulatory approvals for updating its memorandum and articles of association.

Additional information on shareholding pattern

(i) The Bank has only one class of equity shares and the holders of these shares have equal voting rights.

(ii) Distribution schedule of equity shares, setting out the number of holders and percentage in the following categories:

Categories*	Number of Shares	Number of Shareholders	% of total outstanding shares
Less than 1%	689,919,302	3,547	86.63
1% up to less than 5%	55,104,569	4	6.92
5% up to less than 10% **	51,377,940	1	6.45
	796,401,811	3,552	100

** Expressed as a percentage of total outstanding shares of the Bank.*

***Represents the shares held by Deutsche Bank Trust Co. Americas, USA as custodians of the Bank's Global Depository Receipts, London.*

20 INCOME FROM INVESTMENT BANKING SERVICES

Income from investment banking services includes US$ 130,000 (2007: US$ 44,471) which has been received by the Group in kind in the form of shares in exchange for investment banking services rendered.

20 *INCOME FROM INVESTMENT BANKING SERVICES (continued)*

Income from investment banking services includes US$ 100 million in-kind in the form of shares in a cement investment company promoted by the Bank in lieu of cement rights and permits secured and transferred by the Bank to the investment company. This income is measured at the fair value of the shares received measured by reference to the transaction price paid by investors and as per the agreed pricing terms specified in the private placement memorandum. The value of the rights and permits transferred in its current form and condition is supported by valuation prepared by a firm of independent cement industry consultants.

21 TOTAL FINANCE INCOME AND EXPENSE

	2008	2007
TOTAL FINANCE INCOME		
Income from placements with financial institutions	29,555	38,821
Income from financing assets	1,533	10,118
Income from investments in Sukuk (note 23)	-	4,523
	31,088	53,462
TOTAL FINANCE COST		
Investors' funds	10,908	14,121
Placements from financial and other institutions	18,572	33,033
Financing liabilities	33,929	5,320
Unrestricted investment accounts	98	4,008
	63,507	56,482
NET FINANCE EXPENSE	**(32,419)**	(3,020)

22 INCOME FROM INVESTMENT IN ASSOCIATES

	2008	2007
Net changes in the fair value changes on investments designated at fair value through profit or loss	-	11,952
Share of profits from associates under equity method	94,968	9,931
	94,968	21,883

23 INCOME FROM AVAILABLE-FOR-SALE INVESTMENTS

	2008	2007
Dividend income	1,609	1,487
Gain on sale	221	6,673
Income from sukuks	-	4,523
	1,830	12,683

24 INCOME FROM PARTIAL SALE OF A SUBSIDIARY

During 2007, the Bank sold 59.995% stake in Khaleeji Commercial Bank BSC (c), which was a wholly owned subsidiary of the Bank, and recognised again of US$ 83,826. With effect from 30 September 2007, the subsidiary's financial statements have been de-consolidated from the consolidated financial statements of the Group.

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25 STAFF COST

	2008	2007
Salaries and benefits	131,151	102,128
Social insurance expenses	1,423	1,006
Other staff expenses	1,968	664
	134,542	103,798

26 IMPAIRMENT ALLOWANCES

	2008	2007
Available-for-sale investments (note 9)	17,212	10,526
Financing assets (note 6)	16,500	-
Project receivables (note 10)	6,000	4,836
	39,712	15,362

27 SHARE-BASED EMPLOYEE COMPENSATION SCHEME

In the annual general meeting on 18 February 2008, the shareholders approved a management incentive plan ('the plan') which involves the issue of the Bank's shares of up to 25% (181 million shares) of the Bank's paid-up capital to senior executive management on achievement of certain market and non-market based performance conditions and service conditions set by the Board of Directors. As per the terms of the plan, 181 million share awards were made to eligible employees on the grant date.

The share awards are in the nature of options and have been fair valued as such. The fair value of the share awards with market conditions is measured using a simulation based model (Monte Carlo simulation). The model inputs used include share price on the measurement date of US$ 3.15 per share, exercise price of US$ 0.65 per share, expected volatility of 38% and risk free rate of 2.1%. The dividend yield was set at zero as the share awards will be entitled to dividends during the vesting period. The fair value per share award at the grant date was US$ 0.90 per share. Service and non-market performance conditions attached to the awards are not taken into account in determining fair value. The share awards have an initial lock-in period of 3 years and vest rateably over varied vesting periods of up to 10 years as per the terms of the plan. The vesting charge during the year amounted to US$ 23,508 and a corresponding amount has been credited to equity under the 'share grant reserve'.

Due to the steep decline in the share price of the Bank in the second half of 2008, as at 31 December 2008, it is highly unlikely that the market based performance conditions shall be achieved on completion of the performance period and hence no share awards are expected to vest to the benefit of the employees under the current scheme. As the determination of fair value of the share awards at the grant date considered the effect of the market condition, the amount recognised as expense shall not be adjusted for failure to satisfy a market condition.

Considering the effect of current market conditions on the existing scheme, the Board of Directors in its meeting dated 22 December 2008 approved a replacement scheme for employees which is based on non-market based performance and service conditions. The revised scheme has lowered the number of share awards to be granted to 108.6 million shares. The revised scheme shall be effective from the performance year 2009.

28 ASSETS UNDER MANAGEMENT

The Group provides corporate administration, investment management and advisory services to its project companies, which involve the Group making decisions on behalf of such entities. Assets that are held in such capacity are not included in these consolidated financial statements. At the balance sheet date, the Group had assets under management of US$ 2,312,392 (2007:US$ 2,141,855). During the year, the Bank has charged management fees amounting to US$ 5,840 (2007: US$ 4,180) for the activities related to management of assets.

29 RELATED PARTY TRANSACTIONS

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial and operating decisions. Related parties include entities over which the Group exercises significant influence, major shareholders, directors and executive management of the Group.

A significant portions of the Group's income from investment banking services and management fees are from entities over which the Group exercises influence. Although these entities are considered related parties, the Group administers and manages these entities on behalf of its clients, who are by and large third parties and are the economic beneficiaries of the underlying investments.

The significant related party balances and transactions included in these consolidated financial statements are as follows:

	2008	2007
Assets		
Cash and bank balances	4,569	9,480
Placements with financial institutions	70,091	51,563
Financing assets	69,189	96,179
Investment in associates	451,024	288,047
Assets held-for-sale	-	50,000
Available-for-sale investments	374,285	116,876
Receivable from investment banking services	222,343	171,183
Other assets	251,630	139,831
Liabilities		
Investors' funds	538,784	132,735
Placements from financial and other institutions	675,015	165,497

	2008	2007
Income		
Income from investment banking services	453,191	400,180
Placement, arrangement and management fees	5,841	4,296
Income from investment in associates	94,968	21,883
Income from short-term placements	366	1,472
Income from financing assets	1,533	4,703
Expenses		
Impairment allowances	39,712	15,362
Finance cost on placements	11,954	17,948

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29 RELATED PARTY TRANSACTIONS (continued)

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

Categories*	Number of Shares	Number of Directors
Less than 1%	2,556,888	5
1% up to less than 5%	10,402,475	1

** Expressed as a percentage of total outstanding shares of the Bank.*

Details of material contracts involving directors' include:

	2008	2007
Directors' participation in investments promoted by the Group	131,685	22,235

Key management personnel of the Group comprise of the Board of Directors and key members of management having authority and responsibility for planning, directing and controlling the activities of the Group. The key management personnel compensation is as follows:-

	2008	2007
Board remuneration	5,000	1,200
Board member fees	2,279	840
Share based payments	21,550	-
Salaries and other short-term benefits	49,389	49,523
Post employment benefits	235	204

30 PROPOSED APPROPRIATIONS

The Board of Directors of the Bank propose a dividend of 40% (2007: 95%) of the paid-up capital and other appropriations, subject to the approval of the shareholders' at the annual general meeting, as follows:

	2008	2007
Proposed dividend *	105,125	226,975
Charity contribution	3,000	3,000
Directors' remuneration	5,000	5,000

* Proposed dividend include bonus shares recommended by the Board of Directors at the rate of twenty share for every hundred shares held at the date of the Shareholders Annual General Meeting (2007: ten share for every hundred shares held).

31 EARNINGS PER SHARE

Basic earnings per share is calculated by dividing the profit for the year by the weighted average number of equity shares outstanding during the year.

Basic EPS	2008	2007
Profit for the year (US$ 000's)	291,885	340,063
Weighted average number of equity shares (Nos. in 000's)	788,665	715,142
Basic earnings per share (in US cents)	**37.01**	42.79

The Bank has contingently issuable shares in the form of share grants awarded during the year. However, as it is highly unlikely that the awards will vest, the share grants are not considered to be dilutive (note 27).

32 ZAKAH

Based on the computation approved by the Shari'a Board, the Bank has appropriated US$ 1,312 (2007: US$ 1,402) from retained earnings towards payment of Zakah which is included in other liabilities.

Zakah is directly borne by the shareholders on distributed profits and investors in restricted investment accounts. The Bank does not collect or pay Zakah on behalf of its shareholders and investors in restricted investment accounts. Zakah payable by the shareholders is computed by the Bank on the basis of the method prescribed by the Bank's Shari'a Supervisory Board and notified to shareholders annually. Zakah payable by the shareholders in respect of the proposed distributable profits (refer note 30) for the year ended 31 December 2008 is US cents 0.17 (2007: US cents 0.73) for every share held.

33 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 account where the Group uses these funds for charitable means. Movements in non-Islamic funds are shown in the statement of sources and uses of charity funds.

The Group receives profits from deposits placed with the Central Bank of Bahrain and other incidental or required deposits. These earnings are utilised exclusively for charitable purposes and amounts to US$ 94 (2007: US$ 192).

34 SHARI'A SUPERVISORY BOARD

The Group's Shari'a Supervisory Board consists of four 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.

35 SOCIAL RESPONSIBILITY

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

36 MATURITY PROFILE

2008	Gross undiscounted cash flows						Carrying amount
	Up to 3 months	3 to 6 months	6 months-1 year	1 to 3 years	Over 3 years	Total	
Assets							
Bank balances	13,855	-	-	-	-	13,855	13,855
Placements with financial institutions	1,276,188	-	-	-	-	1,276,188	1,275,675
Financing assets	-	-	-	69,189	-	69,189	69,189
Assets held-for-sale	75,844	75,844	151,688	308,620	-	611,996	611,996
Investment in associates	50,977	-	43,318	121,950	234,779	451,024	451,024
Available-for-sale investments	3,193	1,234	66,255	196,112	140,098	406,892	406,892
Receivable from investment banking services	142,343	80,000	-	-	-	222,343	222,343
Other financial assets	94,179	16,374	158,434	83,514	-	352,501	352,501
Total assets	**1,656,579**	**173,452**	**419,695**	**779,385**	**374,877**	**3,403,988**	**3,403,475**

2008	Gross undiscounted cash flows						Carrying amount
	Up to 3 months	3 to 6 months	6 months-1 year	1 to 3 years	Over 3 years	Total	
Liabilities							
Investors' funds	511,559	-	-	27,225	-	538,784	538,784
Placements from financial and other institutions	941,252	2,250	-	-	-	943,502	937,538
Financing liabilities	8,462	8,461	16,923	497,279	189,422	720,547	634,895
Liabilities held-for-sale	37,922	37,922	75,844	165,498	-	317,186	317,186
Other liabilities	70,093	-	4,883	12,850	-	87,826	87,826
Total liabilities	**1,569,288**	**48,633**	**97,650**	**702,852**	**189,422**	**2,607,845**	**2,516,229**
Unrestricted investment accounts	1,945	-	-	-	-	**1,945**	**1,945**
Off-balance sheet items							
Restricted investment accounts	-	-	-	74,222	-	**74,222**	**74,222**
Capital commitments	66,924	35,571	-	-	-	**102,495**	**102,495**

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36 MATURITY PROFILE (continued)

2007	Gross undiscounted cash flows						Carrying amount
	Up to 3 months	3 to 6 months	6 months - 1 year	1 to 3 years	Over 3 years	Total	
Assets							
Bank balances	15,271	-	-	-	-	15,271	15,271
Placements with financial institutions	621,010	74,079	18,577	-	-	713,666	711,978
Financing assets	20,580	13,217	-	72,739	-	106,536	96,179
Assets held-for-sale	-	446,882	-	-	-	446,882	446,882
Investment in associates	-	-	70,902	-	217,145	288,047	288,047
Available-for-sale investments	8,516	-	120,959	56,408	60,463	246,346	246,346
Receivable from investment banking services	171,183	-	-	-	-	171,183	171,183
Other financial assets	35,050	152,967	13,654	7,380	-	209,051	209,051
Total assets	871,610	687,145	224,092	136,527	277,608	2,196,982	2,184,937

2007	Gross undiscounted cash flows						Carrying amount
	Up to 3 months	3 to 6 months	6 months- 1 year	1 to 3 years	Over 3 years	Total	
Liabilities							
Investors' funds	134,982	3,397	1,497	-	-	139,876	139,876
Placements from financial and other institutions	264,858	91,648	-	-	-	356,506	355,548
Financing liabilities	9,681	9,681	109,362	362,268	212,447	703,439	586,620
Liabilities held-for-sale	-	167,019	-	-	-	167,019	167,019
Other liabilities	111,633	-	1,638	2,403	-	115,674	115,674
Total liabilities	521,154	271,745	112,497	364,671	212,447	1,482,514	1,364,737
Unrestricted investment accounts	826	-	-	-	-	826	826
Off-balance sheet items							
Restricted investment accounts	-	-	-	77,038	-	77,038	77,038
Capital commitments	7,082	-	-	-	-	7,082	7,082

The previous table shows the cash flows on the Group's financial assets and liabilities and unrecognised commitments on the basis of their earliest possible contractual maturity. The Group's expected cash flows on these instruments vary significantly from this analysis. For example, investors' funds and unrecognised commitments are not all expected to be drawn down immediately.

37 CONCENTRATION OF ASSETS, LIABILITIES, UNRESTRCITED AND RESTRICTED INVESTMENT ACCOUNTS

(a) Industry sector

2008	Trading and manufacturing	Banks and financial institutions	Development Infrastructure	Technology	Others	Total
Assets						
Cash and bank balances	-	13,322	-	-	541	**13,863**
Placements with financial institutions	-	1,275,675	-	-	-	**1,275,675**
Financing assets	-	-	69,189	-	-	**69,189**
Assets held-for-sale	-	-	611,996	-	-	**611,996**
Investment in associates	24,452	241,802	175,000	9,770	-	**451,024**
Available-for-sale investments	100,000	43,027	174,295	-	89,570	**406,892**
Receivable from investment banking services	-	78	222,232	33	-	**222,343**
Other assets	1,294	10,600	129,897	-	292,274	**434,065**
Total assets	**125,746**	**1,584,504**	**1,382,609**	**9,803**	**382,385**	**3,485,047**
Liabilities						
Investors' funds	186,405	162,565	46,688	-	143,126	538,784
Placements from financial and other institutions	-	937,538	-	-	-	937,538
Financing liabilities	-	453,127	-	-	181,768	634,895
Liabilities held-for-sale	-	-	317,186	-	-	317,186
Other liabilities	-	517	8,434	-	78,875	87,826
Total liabilities	**186,405**	**1,553,747**	**372,308**	**-**	**403,769**	**2,516,229**
Unrestricted investment accounts	-	-	-	-	1,945	**1,945**
Off-Balance sheet items						
Restricted investment accounts	-	-	72,612	-	1,610	**74,222**

37 *Concentration of assets, liabilities, unrestricted and restricted investment accounts (continued)*

(a) *Industry sector (continued)*

2007	Trading and manufacturing	Banks and financial institutions	Development Infrastructure	Technology	Others	Total
Assets						
Cash and bank balances	-	15,218	-	-	165	15,383
Placements with financial institutions	-	711,978	-	-	-	711,978
Financing assets	-	-	96,179	-	-	96,179
Assets held-for-sale	-	-	446,882	-	-	446,882
Investment in associates	24,196	225,478	8,410	19,250	10,713	288,047
Available-for-sale investments	-	13,250	214,771	-	18,325	246,346
Receivable from investment banking services	-	-	171,183	-	-	171,183
Other assets	41	16,674	178,498	-	73,856	269,069
Total assets	24,237	982,598	1,115,923	19,250	103,059	2,245,067
Liabilities						
Investors' funds	1,582	2,092	102,476	-	33,726	139,876
Placements from financial and other institutions	-	355,548	-	-	-	355,548
Financing liabilities	-	586,620	-	-	-	586,620
Liabilities held-for-sale	-	-	167,019	-	-	167,019
Other liabilities	2	6	257	-	115,409	115,674
Total liabilities	1,584	944,266	269,752	-	149,135	1,364,737
Unrestricted investment accounts	-	826	-	-	-	826
Off-Balance sheet items	-	-	73,763	-	3,365	77,038
Restricted investment accounts						

37 *Concentration of assets, liabilities, unrestricted and restricted investment accounts (continued)*

(b) Geographic region

2008	GCC countries	Other MENA	Other Asia	UK	Europe (excluding UK)	USA	Total
Assets							
Cash and bank balances	8,235	1,078	-	870	3,680	-	13,863
Placements with financial institutions	961,355	-	-	76,345	237,975	-	1,275,675
Financing assets	14,344	-	-	-	54,845	-	69,189
Assets held-for-sale	611,996	-	-	-	-	-	611,996
Investment in associates	444,000	7,024	-	-	-	-	451,024
Available-for-sale investments	320,768	27,710	48,547	-	6,867	3,000	406,892
Receivable from investment banking services	112	141,788	80,000	-	443	-	222,343
Other assets	369,213	64,630	-	209	-	13	434,065
Total assets	**2,730,023**	**242,230**	**128,547**	**77,424**	**303,810**	**3,013**	**3,485,047**
Liabilities							
Investors' funds	327,650	59,783	147,101	2,687	1,563	-	538,784
Placements from financial and other institutions	923,958	5,250	-	8,330	-	-	937,538
Financing liabilities	334,417	-	-	300,478	-	-	634,895
Liabilities held-for-sale	317,186	-	-	-	-	-	317,186
Other liabilities	87,826	-	-	-	-	-	87,826
Total liabilities	**1,991,037**	**65,033**	**147,101**	**311,495**	**1,563**	**-**	**2,516,229**
Unrestricted investment accounts	1,398	543	4	-	-	-	**1,945**
Off-Balance sheet items							
Restricted investment accounts	23,646	-	-	-	50,576	-	**74,222**

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37 Concentration of assets, liabilities, unrestricted and restricted investment accounts (continued)

(b) Geographic region (continued

2007	GCC countries	Other MENA	Other Asia	UK	Europe (excluding UK)	USA	Total
Assets							
Cash and bank balances	12,404	-	389	331	-	2,259	15,383
Placements with financial institutions	705,961	-	-	-	6,017	-	711,978
Financing assets	29,360	-	-	-	66,819	-	96,179
Assets held-for-sale	446,882	-	-	-	-	-	446,882
Investment in associates	288,047	-	-	-	-	-	288,047
Available-for-sale investments	170,840	29,408	41,000	-	5,098	-	246,346
Receivable from investment banking services	-	-	171,183	-	-	-	171,183
Other assets	244,228	302	23,817	238	471	13	269,069
Total assets	1,897,722	29,710	236,389	569	78,405	2,272	2,245,067
Liabilities							
Investors' funds	66,505	46,856	24,196	886	1,433	-	139,876
Placements from financial and other institutions	350,545	5,003	-	-	-	-	355,548
Financing liabilities	-	-	-	586,620	-	-	586,620
Liabilities held-for-sale	167,019	-	-	-	-	-	167,019
Other liabilities	115,674	-	-	-	-	-	115,674
Total liabilities	699,743	51,859	24,196	587,506	1,433	-	1,364,737
Unrestricted investment accounts	826	-		-	-	-	826
Off-Balance sheet items							
Restricted investment accounts	24,181	-	-	-	52,857	-	77,038

38 FINANCIAL INSTRUMENTS

a) FAIR VALUES OF FINANCIAL INSTRUMENTS

Fair value is an amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. Other than certain available-for-sale investments of US$ 401,665 (2007: US$ 239,448) and Financing assets of US$ 69,189 (2007: US$ 96,179), the estimated fair values of the Group's other financial instruments are not significantly different from their book values.

b) CLASSIFICATION OF FINANCIAL INSTRUMENTS

The classification of the financial instruments of the Group is as given below:

	Designated at fair value through profit or loss	Available-for-sale	Loans and receivables	Other amortised cost	Total carrying value
2008					
Assets					
Cash and bank balances	-	-	13,863	-	13,863
Placements with financial institutions	-	-	1,275,675	-	1,275,675
Financing assets	-	-	69,189	-	69,189
Investments in Associates	41,245	-	-	-	41,245
Available-for-sale investments	-	406,892	-	-	406,892
Receivable from investment banking services	-	-	222,343	-	222,343
Other financial assets	-	-	352,501	-	352,501
Total financial assets	**41,245**	**406,892**	**1,933,571**	-	**2,381,708**
Liabilities					
Investors' funds	-	-	-	538,784	538,784
Placements from financial and other institutions	-	-	-	937,538	937,538
Financing liabilities	-	-	-	634,895	634,895
Other financial liabilities	-	-	-	87,826	87,826
Total financial liabilities	-	-	-	2,199,043	**2,199,043**
Unrestricted investment accounts	-	-	-	1,945	**1,945**

38 *FINANCIAL INSTRUMENTS (continued)*

b) CLASSIFICATION OF FINANCIAL INSTRUMENTS (continued)

2007	Designated at fair value through profit or loss	Available-for-sale	Loans and receivables	Other amortised cost	Total carrying value
Assets					
Cash and bank balances	-	-	15,383	-	15,383
Placements with financial institutions	-	-	711,978	-	711,978
Financing assets	-	-	96,179	-	96,179
Investments in Associates	60,361	-	-	-	60,361
Available-for-sale investments	-	246,346	-	-	246,346
Receivable from investment banking services	-	-	171,183	-	171,183
Other financial assets	-	-	209,051	-	209,051
Total financial assets	60,361	246,346	1,203,774	-	1,510,481
Liabilities					
Investors' funds	-	-	-	139,876	139,876
Placements from financial and other institutions	-	-	-	355,548	355,548
Financing liabilities	-	-	-	586,620	586,620
Other liabilities	-	-	-	114,566	114,566
Total financial liabilities	-	-	-	1,196,610	1,196,610
Unrestricted investment accounts	-	-	-	826	826

39 COMMITMENTS AND CONTINGENCIES

The commitments contracted in the normal course of business of the Group:

	2008	2007
Commitments to invest	31,562	-
Underwriting commitment	79,580	-
Un-drawn commitments to extend finance	20,000	-
Capital commitments	1,353	7,667

The Group potentially has a commitment under a constructive obligation to extend finance to one of its projects of up to US$ 170 million (2007: US$ 170 million). In the opinion of the management, based on their assessment of expected cash flows from the project, the financing is not expected to be drawn down. In the event of a drawdown, the Group would have a charge over the assets of the project.

The Group has also issued financial guarantees to financial institutions to secure credit facility arrangements of US$ 21,970 (2007: US$ 128,440) for projects managed by the Group.

Performance obligations

During the ordinary course of business, the Group may enter into performance obligations in respect of its infrastructure development projects. It is the usual practice of the Group to pass these performance obligations, wherever possible, on to the companies that own the projects. In the opinion of the management, no liabilities are expected to materialise on the Group at 31 December 2008 due to the performance of any of its projects.

40 FINANCIAL RISK MANAGEMENT

Overview

Financial instruments of the Group include bank balances, placement with and from financial institutions, financing assets and financing liabilities, investment securities, investments in associates, certain receivables, investors' funds and other liabilities. Accounting policies for financial instruments are set out in note 2.

The Group has exposure to the following risks from its use of financial instruments:

- credit risk;
- liquidity risk;
- market risks; and
- operational risk

This note presents information about the Group's exposure to each of the above risks, the Group's objectives, policies and processes for measuring and managing risk, and the Group's management of capital.

40 *FINANCIAL RISK MANAGEMENT (continued)*

Risk management framework

The key element of our risk management philosophy is for the Risk Management Department ('RMD') to provide independent monitoring and control while working closely with the business units which ultimately own the risks. The Head of Risk Management reports directly to the CEO and has access to the Chairman and the Board of Directors.

Our Board of Directors has overall responsibility for establishing our risk culture and ensuring that an effective risk management framework is in place. The Board has established an Executive Risk Management Committee, which is responsible for developing and monitoring the Bank's risk management policies in the specified areas. The committee also continuously monitors consistent implementation of the Board approved policies in the Bank and reports deviations if any to the Risk Management Committee of the Board. The committee consists of heads of business and other functional units in the Bank and reports regularly to the Risk Management Committee of the Board. The Board of Directors approves and periodically reviews our risk management policies and strategies. The Board Risk Management Committee is responsible for implementing risk management policies, guidelines and limits and ensuring that monitoring processes are in place. The RMD, together with the Internal Audit and Compliance Departments, provide independent assurance that all types of risk are being measured and managed in accordance with the policies and guidelines set by the Board of Directors.

The RMD submits a quarterly Risk Review and Investment Review report to the Board Risk Committee. The Risk Review report describes the potential issues for a wide range of risk factors and classifies the risk factors from low to high. The Risk Review report also provides comments as to how risk factors are being addressed by the Group and the change in risk rating from the previous quarter. For each investment, which includes development infrastructure projects, the Investment Review report gives updated valuations and impairment assessment of each investment, a description of significant developments on projects or issues as well as an update on the strategy and exit plan for each project.

a) Credit risk

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Group's, placements with financial institutions, financing assets and other receivables from project companies. For risk management reporting purposes, the Group considers and consolidates all elements of credit risk exposure (such as individual obligor default risk, country and sector risk).

Management of investment and credit risk

The Board of Directors has delegated responsibility for the management of credit risk to its Board Investment Committee (BIC). This committee establishes operating guidelines and reviews and endorses the CEOs and Investment Department recommendations for investment strategies, products and services. Its actions are in accordance with the investment policies adopted by the Board of Directors.

The RMD is responsible for oversight of the Group's credit risk, including:

- Formulating investment and credit policies in consultation with business units, covering credit assessment, risk reporting, documentary and legal procedures, and compliance with regulatory and statutory requirements.
- Establishing the authorisation structure for the approval and renewal of investment and credit facilities. Authorisation limits are also allocated to Executive Management. Larger facilities require approval by EIC and the Board of Directors based on the authority limits structure of the Bank.

40 *FINANCIAL RISK MANAGEMENT (continued)*

- Reviewing and assessing credit risk. Risk department assesses all investment and credit exposures in excess of designated limits, prior to investments / facilities being committed. Renewals and reviews of investments / facilities are subject to the same review process.
- Limiting concentrations of exposure to counterparties, geographies and industries.
- Developing and maintaining the Group's risk grading in order to categorise exposures according to the degree of risk of financial loss faced and to focus management on the attendant risks. The risk grading system is used in determining where impairment provisions may be required against specific investment / credit exposures. The current risk grading framework consists of two broad grades "Unimpaired" and "Impaired", reflecting risk of default and the availability of collateral or other credit risk mitigation. Risk is assessed on an individual basis for each investment / receivable and is reviewed at least once a year. The Group does not perform a collective assessment of impairment for its credit exposures as the credit characteristics of each exposure is considered to be different. The responsibility for setting risk grades lies with the final approving authority as appropriate. Risk grades are subject to regular reviews by Group RMD.
- Reviewing compliance of business units with agreed exposure limits, including those for selected industries, country risk and product types. Regular reports are provided to BIC on the exposure limits.
- Providing advice, guidance and specialist skills to business units to promote best practice throughout the Group in the management of investment / credit risk.

The Risk Management Department works alongside the Investment Department at all stages of the deal cycle, from pre-investment due diligence to exit, and provides an independent review of every transaction. A fair evaluation of investments takes place every quarter with inputs from the Investment department and RMD. Quarterly updates of investments are reviewed by the Board of Directors. Regular audits of business units and Group Credit processes are undertaken by Internal Audit.

40 *FINANCIAL RISK MANAGEMENT (continued)*

The Group's maximum exposure to risk at 31 December 2008 is as follows:

Exposure to credit risk

2008	Bank Balances	Placement with financial institutions	Financing assets	Receivable from investment banking services	Other financial assets
Neither past due nor impaired					
Carrying amount	**13,855**	**1,275,675**	**14,344**	**120,000**	**399,078**
Past due but not impaired					
Past due comprises					
30 – 60 days	-	-	-	-	-
60 – 90 days	-	-	-	54,000	-
90 – 180 days	-	-	-	15,000	-
Above 180 days	-	-	-	33,343	10,000
Carrying amount – Past due but not impaired	-	-	-	**102,343**	**10,000**
Individually impaired					
Gross amount	-	-	71,345	3,076	12,497
Allowance for impairment	-	-	(16,500)	(3,076)	(12,497)
Carrying amount – Individually impaired	-	-	**54,845**	-	-
Carrying amount	**13,855**	**1,275,675**	**69,189**	**222,343**	**409,078**

Other financial assets includes project financing of US$ 109,000 (2007: US$ Nil) renegotiated during the year.

40 FINANCIAL RISK MANAGEMENT (continued)

Exposure to credit risk (continued)

2007	Bank Balances	Placement with financial institutions	Financing assets	Receivable from investment banking services	Other financial assets
Neither past due nor impaired					
Carrying amount	15,271	711,978	46,992	171,183	185,313
Past due but not impaired					
Past due comprises					
30 – 60 days	-	-	10,301	-	-
60 – 90 days	-	-	545	-	-
90 – 180 days	-	-	509	-	607
Above 180 days	-	-	37,832	-	23,263
Carrying amount – Past due but not impaired	-	-	49,187	-	23,870
Individually impaired					
Gross amount	-	-	-	3,076	5,455
Allowance for impairment	-	-	-	(3,076)	(5,455)
Carrying amount – Individually impaired	-	-	-	-	-
Carrying amount	15,271	711,978	96,179	171,183	209,183

40 *FINANCIAL RISK MANAGEMENT (continued)*

Impaired receivables

Impaired receivables are those for which the Group determines that it is probable that it will be unable to collect all payments due according to the contractual terms of the receivables agreement(s). These exposures are graded "Impaired" in the Group's internal credit risk grading system.

Past due but not impaired exposures

Financing assets and short-term project financing
Certain financing assets and short-term project financing facilities are past due but the Group believes that impairment is not appropriate on the basis of the level of future expected cash flows and / or the stage of collection of amounts owed to the Group. These are primarily short term funding to the project Special Purpose Entities (SPEs). The credit and investment exposure to these SPEs is reviewed together by reviewing project cash flows periodically.

Receivable from investment banking services
The Bank recognises investment banking income based on underwriting commitments and placements with external investors. These placements are made with sophisticated individual investors, corporates and financial institutions.

The Bank believes that the past due income receivable from investment banking services is not impaired based on specific credit assessment of the financial strengths of investors and underwriters and the stage of collection of the amounts.

Allowances for impairment

The Group establishes an allowance for impairment losses that represents its estimate of incurred losses in its receivables. This allowance is a specific loss component that relates to individually significant exposures based on individual assessment for impairment.

Write-off policy

The Group writes off a receivables (and any related allowances for impairment losses) when the Group RMD determines that the receivables are uncollectible and after obtaining approval from the CBB. This determination is reached after considering information such as the occurrence of significant changes in the payee / issuer's financial position such that the payee / issuer can no longer pay the obligation, or that proceeds from collateral will not be sufficient to pay back the entire exposure.

40 *FINANCIAL RISK MANAGEMENT (continued)*

Concentration risk

Concentration risk arises when a number of counterparties are engaged in similar economic 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. The Group seeks to manage its concentration risk by establishing and constantly monitoring geographic and industry wise concentration limits.

The geographical and industry wise distribution of assets and liabilities are set out in note 35.

Concentration by location for financial assets is measured based on the location of the underlying operating assets, and not based on the location of the investment (which is generally based in tax efficient jurisdictions).

b) Liquidity risk

Liquidity risk is defined as the risk that the Group will not have funds available to meet its financial liabilities as they fall due.

Management of liquidity risk

The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation.

Treasury receives information from other business units regarding the liquidity profile of their financial assets and liabilities and details of other projected cash flows arising from projected future business. Treasury then maintains a portfolio of short-term liquid assets, largely made up of short-term liquid murabaha placements with financial institutions and other inter-bank facilities, to ensure that sufficient liquidity is maintained within the Bank as a whole. The liquidity requirements of business units are met through Treasury to cover any short-term fluctuations and longer term funding to address any structural liquidity requirements. It is our policy to keep a large part of our assets in highly liquid short-term instruments.

The daily liquidity position is monitored and regular liquidity stress testing is conducted under a variety of scenarios covering both normal and more severe market conditions. All liquidity policies and procedures are subject to review and approval by ALCO. Daily reports cover the liquidity position of the Bank. A summary report, including any exceptions and remedial action taken, is submitted regularly to ALCO.

Exposure to liquidity risk

Our three primary measures of liquidity are stock of liquid assets, surplus cash capital and net funding requirements. For this purpose liquid assets include cash and cash equivalents and placements with financial institutions. Cash capital is defined as the aggregate of the Banks capital base and inter-bank liabilities maturing later than 12 months. Cash capital is used to fund long term funding requirements including investment in associates, available-for-sale investments and equipments.

40 *FINANCIAL RISK MANAGEMENT (continued)*

Details of the reported Group ratio of liquid assets and surplus cash capital at the reporting date and during the reporting period were as follows:

	Liquid asset / Total asset		Surplus cash capital	
	2008	2007	**2008**	2007
At 31 December	37.02%	31.58%	1.965	2.092
Average for the period	37.49%	35.04%	2.333	1.966
Maximum for the period	40.74%	40.37%	2.701	2.092
Minimum for the period	33.60%	31.11%	1.965	1.778

c) Market risk

Market risk is the risk that changes in market prices, such as profit rate, equity prices, foreign exchange rates and credit spreads (not relating to changes in the obligor's / issuer's credit standing) will affect the Group's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk.

Management of market risks

As a matter of general policy, the Group shall not assume trading positions on its assets and liabilities, and hence the entire balance sheet is a non-trading portfolio. All foreign exchange risk within the Bank is transferred to Treasury. The Group seeks to manage currency risk by continually monitoring exchange rates. Profit rate risk is managed principally through monitoring profit rate gaps and by having pre-approved limits for repricing bands. Overall authority for market risk is vested in the Asset Liability Committee (ALCO). RMD is responsible for the development of detailed risk management policies (subject to review and approval by ALCO) and for the day-to-day review of their implementation.

Exposure to profit rate risk

The principal risk to which non-trading portfolios are exposed is the risk of loss from fluctuations in the future cash flows or fair values of financial instrument because of a change in market profit rates. Majority of the Group's profit based asset and liabilities are short term in nature, except for certain long term liabilities which have been utilised to fund the Group's strategic investments in its associates.

40 *FINANCIAL RISK MANAGEMENT (continued)*

Exposure to profit rate risk (continued)

A summary of the Group's profit rate gap position on non-trading portfolios is as follows:

2008	Up to 3 months	3 to 6 months	6 months-1 year	1 to 3 years	Over 3 years	Total
Assets						
Placements with financial institutions	1,276,188	-	-	-	-	**1,276,188**
Financing assets	-	-	-	69,189	-	**69,189**
Total assets	**1,276,188**	**-**	**-**	69,189	**-**	**1,345,377**
Liabilities						
Investors' funds	511,559	-	-	27,225	-	**538,784**
Placements from financial and other institutions	941,252	2,250	-	-	-	**943,502**
Financing liabilities	8,462	8,462	16,923	497,280	189,423	**720,550**
Total liabilities	**1,461,273**	**10,712**	**16,923**	**524,505**	**189,423**	**2,202,836**
Unrestricted investment accounts	**1,945**	**-**	**-**	**-**	**-**	**1,945**
Profit rate sensitivity gap	**(187,030)**	**(10,712)**	**(16,923)**	**(455,316)**	**(189,423)**	**(859,404)**

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40 FINANCIAL RISK MANAGEMENT (continued)

Exposure to profit rate risk(continued)

2007	Up to 3 months	3 to 6 months	6 months-1 year	1 to 3 years	Over 3 years	Total
Assets						
Placements with financial institutions	693,702	18,276	-	-	-	711,978
Financing assets	20,335	12,961	-	62,883	-	96,179
Total assets	714,037	31,237	-	62,883	-	808,157
Liabilities						
Investors' funds	142,476	3,397	1,497	-	-	147,370
Placements from financial and other institutions	344,160	5,002	-	-	-	349,162
Financing liabilities	-	-	91,230	306,277	189,113	586,620
Total liabilities	486,636	8,399	92,727	306,277	189,113	1,083,152
Unrestricted investment accounts	826	-	-	-	-	826
Profit rate sensitivity gap	226,575	22,838	(92,727)	(243,394)	(189,113)	(275,821)

The management of profit rate risk against profit rate gap limits is supplemented by monitoring the sensitivity of the Group's financial assets and liabilities to various standard and non-standard profit rate scenarios. Standard scenarios that are considered on a monthly basis include a 100 basis point (bp) parallel fall or rise in all yield curves worldwide. An analysis of the Group's sensitivity to an increase or decrease in market profit rates (assuming no asymmetrical movement in yield curves and a constant balance sheet position) is as follows:

100 bps parallel increase / (decrease)	**2008**	2007
At 31 December	±8,455	±2,604
Average for the period	±7,142	±2,025
Maximum for the period	±8,455	±2,604
Minimum for the period	±5,812	±1,145

Overall, profit rate risk positions are managed by Treasury, which uses placements from/ to financial institutions to manage the overall position arising from the Group's activities.

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40 *FINANCIAL RISK MANAGEMENT (continued)*

Exposure to profit rate risk – non-trading portfolios (continued)

The effective profit rates on the financial assets, liabilities and unrestricted investment accounts are as follows:

	2008	2007
Placements with financial institutions	2.68%	5.11%
Financing assets	3.34%	6.20%
Investment securities – Sukuks	-	7.24%
Investors' funds	2.51%	3.92%
Placements from financial and other institutions	2.78%	5.99%
Financing liabilities	5.09%	6.34%
Unrestricted investments	2.89%	5.40%

Exposure to foreign exchange risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Groups major exposure is in GCC currencies, which are primarily pegged to the US Dollar. The Group had the following significant net exposures denominated in foreign currency as of 31December:

	2008 US$ Equivalent	2007 US$ Equivalent
Sterling Pounds	1,325	1,684
Euros	7,357	5,995
Jordanian Dinar	8,171	416
Kuwaiti Dinars	61,999	4,172
Other GCC Currencies (*)	519,809	64,900

(*) These currencies are pegged to the US Dollar.

The management of foreign exchange risk against net exposure limits is supplemented by monitoring the sensitivity of the Group's financial assets and liabilities to various foreign exchange scenarios. Standard scenarios that are considered on a monthly basis include a 5% plus / minus increase in exchange rates, other than GCC pegged currencies. An analysis of the Group's sensitivity to an increase or decrease in foreign exchange rates (assuming all other variables, primarily profit rates, remain constant) is as follows:

	2008 US$ Equivalent	2007 US$ Equivalent
Sterling Pounds	66	84
Euros	368	300
Jordanian Dinar	409	21
Kuwaiti Dinars	3,100	209

Exposure to other market risks

Equity price risk on quoted investments is subject to regular monitoring by Group Risk, but is not currently significant in relation to the overall results and financial position of the Group.

40 FINANCIAL RISK MANAGEMENT (continued)

d) Operational risk

Operational risk is the risk of loss arising from systems and control failures, fraud and human errors, which can result in financial and reputation loss, and legal and regulatory consequences. The Group manages operational risk through appropriate controls, instituting segregation of duties and internal checks and balances, including internal audit and compliance. In addition the Group is committed to recruitment in addition to training of staff. The Risk Management Department is in charge of identifying, monitoring and managing operational risk in the Bank. The Bank is currently in the process of conducting Risk Control Self Assessment of Operational risk in all departments of the Bank to identify the important Key Risk Areas and Key Risk Triggers. This process is expected to be completed by the end of 2009.

41 CAPITAL MANAGEMENT

The Group's regulator Central Bank of Bahrain (CBB) sets and monitors capital requirements for the Group as a whole. In implementing current capital requirements CBB requires the Group to maintain a prescribed ratio of total capital to total risk-weighted assets. Banking operations are categorised as either trading book or banking book, and risk-weighted assets are determined according to specified requirements that seek to reflect the varying levels of risk attached to assets and off-balance sheet exposures.

The Group's policy is to maintain strong capital base so as to maintain investor, creditor and market confidence and to sustain the future development of the business. Capital requirements of CBB have been complied through out the year.

With effect from 1 January 2008, the Bank is required to comply with the provisions of the revised Capital Adequacy Module of the CBB (revised based on the Basel II framework) in respect of regulatory capital. The Bank has adopted the standardised approach to credit and basic indicator approach for operational risk management under the revised framework. There has been no significant change in the amount of available regulatory capital under the two norms. Further, as the Bank has not migrated to advanced approach for computation of risk weighted assets, there is no significant change in the measurement of risk weighted assets for credit risk.

The Group's regulatory capital position at 31 December was as follows:

Capital adequacy	**2008 Basel II actual**	2007 Basel II pro forma	2007 Basel I actual
Total risk weighted assets	**3,829,993**	**2,666,730**	2,430,808
Tier 1 capital	481,098	401,669	876,705
Tier 2 capital	117,013	223,726	1,259
Total regulatory capital	**598,111**	**625,395**	877,964
Total regulatory capital expressed as a percentage of total risk weighted assets	**15.62%**	**23.45%**	36.12%

The Bank has complied with all externally imposed capital requirements through out the year.

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42 NEW INTERNATIONAL FINANCIAL REPORTING STANDARDS AND INTERPRETATIONS NOT YET ADOPTED

During the year, the following new/ amended IFRS's standards and interpretations relevant to the activities of the Group have been issued which are not yet mandatory for adoption by the Group:

- IAS 1 Presentation of Financial Statements (amended) (effective for annual period beginning on or after 1January 2009)
- IAS 23 - Borrowing Costs (effective for annual period beginning on or after 1January 2009)
- IFRS 2 Share-based Payment: Vesting Conditions and Cancellations (effective for annual period beginning on or after 1 January 2009); and
- IAS 32 Financial Instruments: Presentation and IAS 1Presentation of Financial Statements: Puttable Financial Instruments and Obligations Arising on Liquidation (effective for annual period beginning on or after 1 January 2009)

The adoption of these standards and interpretations and certain other amendments to existing standards with varied effective dates made by International Accounting Standards Board as part of its first annual improvements project are not expected to have any material impact on the financial statements.

43 COMPARATIVES

Certain prior year amounts have been reclassified to conform to the current year's presentation. Such reclassifications do not affect previously reported net profit or equity.

In 2007, the Bank sold 59.995% stake in Khaleeji Commercial Bank BSC (c), which was previously a wholly owned subsidiary of the Group. With effect from 30 September 2007, the subsidiary's financial statements were de-consolidated from the consolidated financial statements of the Group. Accordingly, the comparative income statement, statement of changes in equity and cash flows for the year ended 31 December 2007 are not directly comparable with the current period figures.