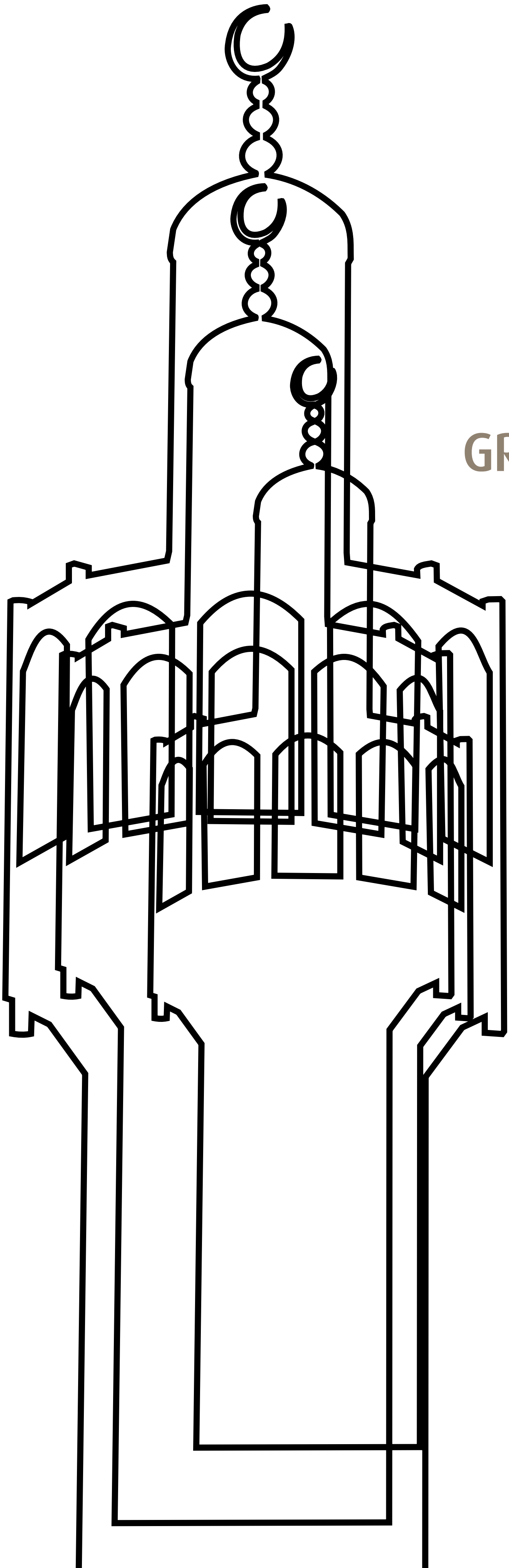

GROWTH IN EVERY LAYER

>ABC Islamic Bank Annual Report 2007

بنك المؤسسة العربية المصرفية الإسلامي (ش.م.ب.م)

ABC Islamic Bank (E.C.)

ABC Islamic Bank (E.C.) is a subsidiary of Arab Banking Corporation. The Group's international depth and strategic relationships within the region allows it to maintain its position as one of the leading banking groups in the Middle East and Europe. The group has sought to build its practice beyond the traditional roles of regional banks and move into advanced high value-added activities, establishing itself as a regional leader with immeasurable international experience.

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ABC Islamic Bank has experienced a record year with greater prosperity from every layer of the organisation. Inspired success is represented graphically throughout this year's annual report.

ABC Islamic Bank... Where Shari'a Compliance meets banking excellence.

VISION

To be the Islamic Bank of choice in the region and provide banking solutions for customer’s needs.

MISSION

Our mission is to uphold our carefully formulated Islamic principles in the quest for mutual prosperity for our clients and the Bank. In pursuit of our mission, we commit the Bank to the purist forms of Islamic banking products and services from a Shari’a perspective. We remain demonstrably independent from the conventional sector and recognise the importance of Islam’s social objectives in conducting our business. We are also committed to delivering a level of service that matches, or exceeds, the market practice internationally. To do so, we seek to employ the best available human resources and technology to apply the highest professional, moral and ethical standards.

CHAIRMAN'S STATEMENT

(All figures stated in US dollars)

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

At the time of writing my statement many of the world's financial markets were in a state of shock and turmoil as a result of the sub-prime saga and the resulting losses to international financial institutions. In contrast, the Islamic banking community in general has been immune to these developments and liquidity in the oil-rich countries of the Arab world in particular held up relatively well. It is against this backdrop that I am pleased to present to you, on behalf of the Board of Directors, the annual report and the consolidated financial statements of ABC Islamic Bank (E.C.) for the year ended December 31, 2007.

ABC Islamic Bank has now been a separately regulated entity within the ABC Group for 10 years, having taken the Islamic banking businesses initiated in the mid 1980s by the parent and expanded it in size and scope. It thus gives me special pleasure to be able to report, a decade on, that 2007 was a year of record profits for ABC Islamic Bank. The re-orientation and re-focussing of the Bank's mission which started in early 2004 has moved a further step forward and the aspiration to be one of the leading providers of international Islamic financial solutions is now a step closer. In several market segments, including Islamic syndicated financings, liquidity management and Shari'a structuring, the Bank is already recognised by industry practitioners as being a key player.

ABC Islamic Bank's core activity is the provision of a range of Shari'a-compliant financial solutions to institutional and corporate clients in the Arab and Islamic world and 2007 was another year of well-diversified growth. The Bank's balance sheet assets increased 66% year-on-year from $823 million to $1.4 billion. With costs showing moderate growth as additional resources in marketing, structuring and fund management were brought in and with revenues rising sharply from $10.9 million to $56.5 million, net profits were up over the previous year by more than 800%. More than half of the revenues were generated by well-timed and profitable disposals from the Bank's portfolio. There was also a strong performance in the Bank's underlying core business lines which, for the third year running, doubled revenues increasing profit margin income and fees significantly. On the liability side of the balance sheet, ABC Clearing Company, the industry's benchmark overnight liquidity management instrument programme continued to attract ever growing volumes of institutional funds and a healthy level of funding from other institutions to fund the Bank's balance sheet growth, reflecting a high degree of confidence both in ABC Islamic Bank and in the parent company.

During 2007 ABC Islamic Bank also distinguished itself as a Joint Lead Manager for the first and second private sector Sukuks issued by a corporate issuer from Saudi Arabia. The size of these two sukuks exceeded $1.6 billion.

BOARD OF DIRECTORS


Abdulmagid Breish
Chairman


Souheil Badro
Deputy Chairman


Naveed Khan
Managing Director


Amr Gadallah
Director


Duncan Smith
Director


Sh. Rashed Al Khalifa
Director


Ramnath Narayanan
Secretary to the Board

The Bank was also mandated lead arranger for the financing of the third GSM licence in Saudi Arabia, where it has a well-developed industry expertise in the telecommunications sector. The Bank was also the first in the industry to offer a Shari'a-compliant commodity hedging structure to several clients in the region.

Having noted in opening that the Islamic banking market held up relatively well as other markets faced a succession of challenges during the closing months of 2007, it has become clear that a key success factor looking forward will be to have prudently diversified sources and types of businesses. As ABC Islamic Bank sits firmly at the centre of the ABC Group's strategy it is in a position both to feed interesting opportunities to other ABC units and product areas and to benefit from referrals and opportunities in reciprocal cooperation. During the course of the year the Bank in conjunction with Group Treasury executed its first Profit Rate Swap in connection with an Islamic project financing transaction in the GCC, as well as originating corporate advisory mandates for ABC's Investment Banking Division in the region. In close collaboration with the Project & Structured Finance unit ABC Islamic Bank also completed several Shari'a Advisory mandates for oil and gas companies in the region. The bank also arranged several major complex financings including the first Islamic non-recourse securitisation to a leading automobile dealer in Saudi Arabia.

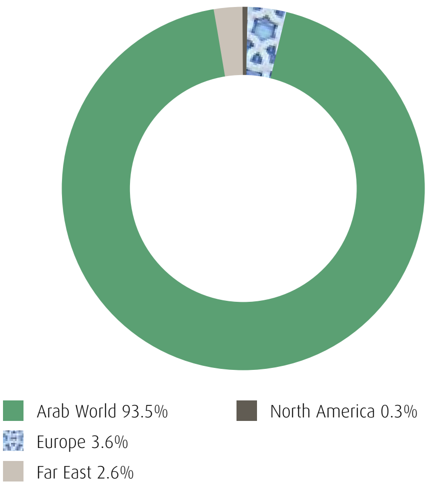
The oil exporting countries particularly those of the GCC in which the Bank has a large part of its portfolio have shown resilience during the on-going credit crunch, in fact using the conditions and the excess liquidity to look for corporate bargains in North America and Europe. On top of this, spending on infrastructure, petrochemical and commercial real estate projects at home continued largely unabated. With the above developments, opportunities for Islamic banks in the region remain great for 2008 and beyond.

One notable result of the broader market squeeze which did affect Islamic financial markets, was a widening of spreads in primary and secondary sukuk issues. However, due to the high issue volumes during the first part of the year, at a time when markets worldwide were witnessing a credit crunch, 2007 was a record year for international sukuk issuance.

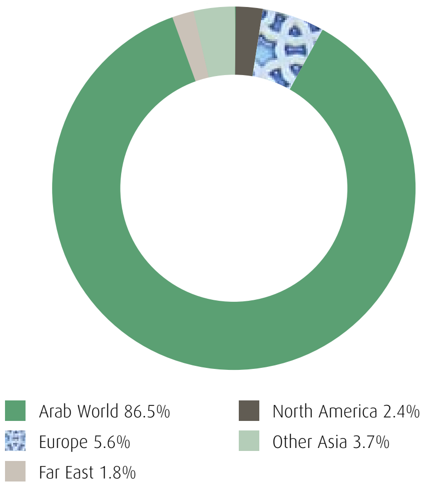
Taking the longer term view on the future shape of the Islamic banking industry it is evident that there has not been any slowdown in the amount of fresh capital being subscribed for new Islamic banks in Asia, Europe as well as the Arab World. As the future Islamic banking industry will be one of bigger, better capitalised banks rather than – as it has been in the past, smaller weaker ones – the Board of the parent bank decided to increase ABC Islamic Bank's paid in capital for the third time in recent years. As I have pointed out in previous reports, where necessary for particularly large underwritings or other types of transactions, Arab Banking Corporation, the parent bank, is able to extend the support of a $30 billion balance sheet but as ABC Islamic Bank's own capital grows, this support becomes required less and less.

CHAIRMAN'S STATEMENT

BREAKDOWN OF ASSETS BY REGION - 2007
PERCENTAGE



BREAKDOWN OF ASSETS BY REGION - 2006
PERCENTAGE



The financial success of 2007, though, was due as much to the commitment of employing, motivating, retaining and developing our own human resources and leading professionals as it was access to capital. A new group-wide program was introduced in the year to attract and train high performing graduates which will provide our future managers and leaders. In the near term there is also the need to bring in additional seasoned specialists to help push the business forward; in demonstration of this point, additional positions for Structuring, Securitisation, and Fund Management were created and filled during the year. As Islamic banking becomes more capital markets driven it is necessary to attract a broader range of professional skills.

In the regulatory sphere, assisted by the parent company, ABC Islamic took all the necessary steps to ensure readiness and full compliance with Basel 2 requirements as of January 1, 2008.

In connection with the above and in conclusion, I would like to thank the CBB for its continued diligence, regulatory oversight and promotion of Islamic banking within the region; the Bank's management has found its support and guidance invaluable.

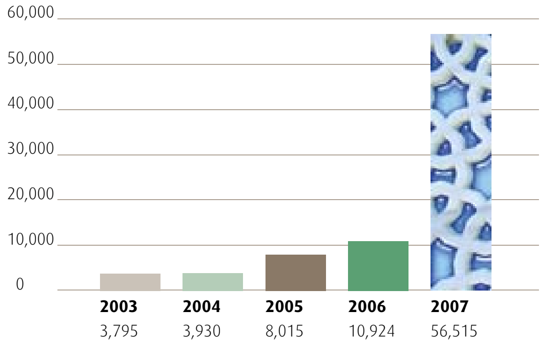
I also take this opportunity to thank all ABC Islamic Bank's clients for their custom and the close co-operation shown and to express the Board's appreciation to our Shari'a Board for their valuable direction and wisdom in all Shari'a matters. Finally, a special word in recognition of the efforts of our staff and senior management for this record performance. Their dedication, loyalty and hard work have been at the core of these results.

Abdulmagid Breish
Chairman

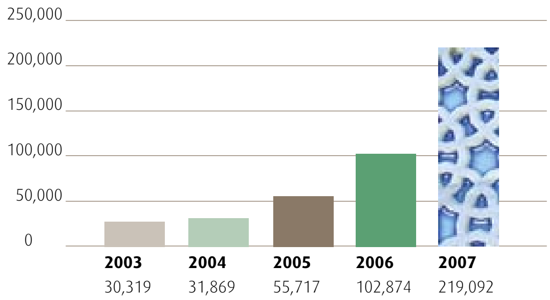
Import financing facility to finance the purchase of flat steel plant equipment for a Saudi customer.

FINANCIAL HIGHLIGHTS
(All figures stated in US dollars)

TOTAL OPERATING INCOME
US$ 000s



SHAREHOLDERS' FUNDS
US$ 000s



The bank made excellent progress during the year with total assets at year end of $1,365 million, a year-on-year increase of $542 million. There were substantial increases in available for sale investments (by 23%), Murabaha receivables (by 75%) and in Ijarah (by more than 100%). During 2007 the bank's net profit increased dramatically, from $5.3 million to $50.9 million. These results reflect both a further strengthening of the bank's core income producing business lines – for the third successive year – and proactive management of the bank's sukuk portfolio which produced some very large gains in the fourth quarter.

BALANCE SHEET

Asset categories posted across the board gains, with the largest increases taking place in Murabaha receivables and Ijarah.

Murabaha payables moved from $712.6 million to $1,131.5 million to support the increase in the asset base with the majority of this coming from banks and financial institutions, reflecting both a continuing confidence in the bank and an active programme of liability marketing.

INCOME STATEMENT

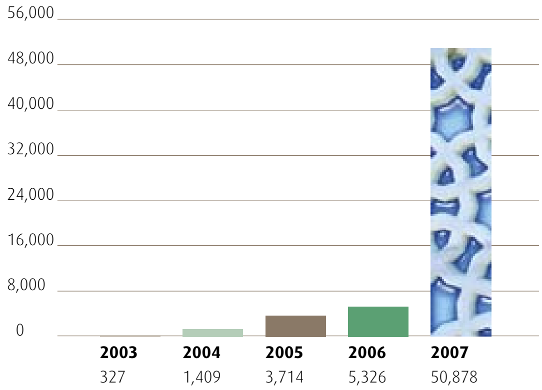
Margin Income before funding costs doubled from the 2006 figure, reflecting the overall asset growth. Profit on Murabaha payables was also higher reflecting similar growth in size, while the bank's share as a mudarib was again held constant to provide investors a higher share of operating profit. Other fees and commission income increased from $3.4 million to $4.6 million, continuing the healthy rise in this category. The largest single component in the income statement, however, was the substantial gain made on the sale of investments from the bank's portfolio. As a result of all of the above, total operating income increased five-fold from $10.9 million in 2006 to $56.5 million in 2007.

Costs were largely contained during the year with operating expenses increasing 13%. The major increase was again in staff costs which reflected additions to head count in marketing, structured finance and fund management, while other expenses were held in line. The provision of $303,000 made on a particular credit in 2006 was written back during the year as was predicted in this report last year. Before deduction of Zakah, net profit increased from $5.6 million to $51.1 million.

SOURCES AND APPLICATIONS OF FINANCIAL RESOURCES

Further recognising the growth in the Islamic banking market and ABC's aspirations within it, the bank's parent increased paid in capital from $82.5 million to $132.5 million during the year. This is the third increase made since the bank was fundamentally reorganized and re-launched in 2004.

NET PROFIT
US$ 000s



GEOGRAPHICAL & SECTORAL DIVERSIFICATION IN ASSETS & LIABILITIES

The bank adhered to its traditional strategy of focusing on serving Arab and Muslim economies and putting at its disposal the worldwide experience of ABC Group in international financial markets. Total assets invested in the Middle East and North Africa (MENA) region amounted to $1,276.5 million (94% of the total).

Banks and financial institutions again provided the bulk of the bank's funding with $1,086.8 million (96% of the total).

LIQUIDITY

The bank witnessed an improvement in liquidity caused by the increase in paid-up capital. This situation was improved by the increase in available for sale investments by $61.8 million and the increase in Murabaha payables by $418.8 million mainly from banks and financial institutions.

Total assets with maturities not exceeding one year amounted to $700.7 million (51% of the total) while those between one and three years amounted to $215.7 million (16% of the total).

SHAREHOLDERS EQUITY

Shareholders equity as at 31st December 2007 stood at $199.1 million as against $102.9 million at year end 2006. This was after the shareholders of ABC Islamic Bank approved a dividend payment of $20 million to the parent at the Annual General Meeting. The increase to equity over 2006 derived from the increase in paid up capital, increase in statutory and revaluation reserves and retained earnings, as well as an increase in fair market value reserves. The present level of equity is within the range of international banking guidelines and standards.

CAPITAL ADEQUACY

The bank abides by international regulatory authorities' requirements in all its financial ratios. The bank is also keen to comply with Central Bank of Bahrain (CBB) regulations and directives pertaining to Islamic banking transactions and practices. The bank's Capital Adequacy Ratio was calculated at 15.68 % in 2007 as compared with 16.56% the previous year. This ratio exceeds the minimum amount of 12% required by the CBB.

REPORT OF THE SHARI'A SUPERVISORY BOARD TO THE SHAREHOLDERS ON PERFORMANCE OF ABC ISLAMIC BANK (E.C.) FOR THE YEAR 2007

In the name of Allah, The Beneficent, The Merciful

Praise be to Allah, the Lord of the worlds, and blessing and peace be upon His Prophet Mohammad and the people of His house and His companions.

The Shareholders of ABC Islamic Bank (E.C.)

Assalam Alaikum Wa Rahmat Allah Wa Barakatuh

In compliance with the letter of appointment and the Bank's articles of association, we are required to submit the following report:

We have reviewed the principles and the contracts relating to the transactions and applications introduced by the ABC Islamic Bank (E.C.) (the Bank) during the year ended 31 December 2007. We have also conducted our review to form an opinion as to whether the Bank has complied with Shari'a Rules and Principles and also with the specific fatwas, rulings and guidelines issued by us.

The Bank's management is responsible for ensuring that the financial institution conducts its business in accordance with Islamic Shari'a Rules and Principles. It is our responsibility to form an independent opinion, based on our review of the operations of the Bank, and to report to you.

We conducted our review, with the cooperation of the Shari'a Compliance Officer, which included examining, on a test basis, each type of transaction, the relevant documentation and procedures adopted by the Bank.

We planned and performed our review so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the Bank has not violated Islamic Shari'a Rules and Principles.

In our opinion:

a) the contracts, transactions and dealings entered into by the Bank during the year ended 31 December 2007 that we have reviewed are in compliance with the Islamic Shari'a Rules and Principles;

b) the allocation of profit and charging of losses relating to investment accounts conform to the basis that had been approved by us in accordance with Islamic Shari'a Rules and Principles;


The Shari'a Board meeting with the Board of Directors.

c) all earnings that have been realised from sources or by means prohibited by Islamic Shari'a Rules and Principles have been disposed of to charitable causes; and

d) the calculation of Zakah is in compliance with Islamic Shari'a Rules and Principles.

The Board takes this opportunity to offer praise to Allah, exalted be He, His guidance, and to express its thanks to the Bank's management for their co-operation and their keenness in understanding and adherence to the rules of the noble Islamic Shari'a.

We beg Allah the Almighty to grant us all the success and straight-forwardness.

Wassalam Alaikum Wa Rahmat Allah Wa Barakatuh

Shari'a Supervisory Board

Dr. Abdul Latif Al Mahmood **Shaikh Nedham Yaqoubi** **Dr. Mohamed Ali Elgari**

5 Saffar 1429 H
12 February 2008 G

Manama, Kingdom of Bahrain

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AUDITORS' REPORT TO THE SHAREHOLDERS OF ABC ISLAMIC BANK (E.C.)

We have audited the accompanying consolidated balance sheet of ABC Islamic Bank (E.C.) ("the Bank") and its subsidiary ("the Group") as of 31 December 2007, and the related consolidated statements of income, cash flows, changes in equity, and sources and uses of zakah and charity funds for the year then ended. These consolidated financial statements and the Bank's undertaking to operate in accordance with Islamic Shari'a Rules and Principles are the responsibility of the Bank's Board of Directors. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

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

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as of 31 December 2007, the results of its operations, its cash flows, and sources and uses of zakah and charity funds for the year then ended in accordance with the Financial Accounting Standards issued by the Accounting and Auditing Organization for Islamic Financial Institutions and the Shari'a Rules and Principles as determined by the Shari'a Supervisory Board of the Bank.

We confirm that, in our opinion, proper accounting records have been kept by the Bank and the consolidated financial statements, and the contents of the Report of the Board of Directors relating to these consolidated financial statements, are in agreement therewith. We further report, to the best of our knowledge and belief, that no violations of the Bahrain Commercial Companies Law, nor of the Central Bank of Bahrain and Financial Institutions Law, nor of the memorandum and articles of association of the Bank, have occurred during the year ended 31 December 2007 that might have had a material adverse effect on the business of the Bank or on its consolidated financial position and that the Bank has complied with the terms of its banking licence.

Ernst & Young

12 February 2008
Manama, Kingdom of Bahrain

CONSOLIDATED BALANCE SHEET

31 December 2007

	Notes	2007 US$ 000's	2006 US$ 000's
ASSETS			
Cash and bank balances	3	**3,453**	1,882
Available for sale investments	4	**328,920**	267,168
Murabaha receivables	5	**730,373**	418,630
Musharaka financing		**2,084**	-
Ijarah	6	**265,061**	127,846
Equipment		**75**	128
Other assets	7	**34,916**	7,654
TOTAL ASSETS		**1,364,882**	823,308
LIABILITIES AND EQUITY			
Liabilities			
Other liabilities	8	**14,296**	7,785
Murabaha payables	9	**1,131,494**	712,649
		1,145,790	720,434
Equity			
Share capital	10	**132,500**	82,500
Statutory reserve	10	**9,441**	4,353
Available for sale reserve		**17,652**	2,312
Retained earnings		**59,499**	13,709
		219,092	102,874
TOTAL LIABILITIES AND EQUITY		**1,364,882**	823,308
MEMORANDUM ITEMS	11	**78,235**	14,831

Abdulmagid Breish
Chairman

Naveed Khan
Managing Director

The attached explanatory notes 1 to 20 form part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF INCOME
Year ended 31 December 2007

	Notes	2007 US$ 000's	2006 US$ 000's
Income from available for sale investments		**21,382**	11,350
Income from Murabaha receivables		**37,648**	18,830
Income from Musharaka financing		**88**	-
Ijarah income – net	6	**11,871**	4,579
		70,989	34,759
Profit on Murabaha payables		**(51,959)**	(27,189)
		19,030	7,570
Gain (Loss) on sale of available for sale investments - net		**32,866**	(88)
Fees and commission income	12	**4,619**	3,442
		56,515	10,924
Staff costs		**3,534**	3,182
Depreciation		**72**	56
Other expenses	13	**2,084**	1,817
		5,690	5,055
Recoveries/(Provisions) for credit losses	5	**303**	(303)
Net profit for the year before Zakah		**51,128**	5,566
Zakah		**(250)**	(240)
NET PROFIT FOR THE YEAR AFTER ZAKAH		**50,878**	5,326

The attached explanatory notes 1 to 20 form part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS
Year ended 31 December 2007

	2007 US$ 000's	2006 US$ 000's
OPERATING ACTIVITIES		
Net profit for the year after Zakah	**50,878**	5,326
Adjustment for:		
Depreciation	**72**	56
(Gain)/Loss on sale of available for sale investments	**(32,866)**	88
(Recoveries)/Provisions for credit losses	**(303)**	303
	17,781	5,773
Changes in:		
Murabaha receivables	**(311,440)**	(27,267)
Musharaka financing	**(2,084)**	-
Ijarah	**(137,215)**	(54,747)
Other assets	**(27,262)**	(5,194)
Other liabilities	**6,511**	902
Murabaha payables	**418,845**	163,878
Net cash (used in) from operating activities	**(34,864)**	83,345
INVESTING ACTIVITIES		
Purchase of available for sale investments	**(199,896)**	(156,234)
Proceeds from sale of available for sale investments	**186,350**	33,912
Purchase of equipment	**(19)**	(103)
Net cash used in investing activities	**(13,565)**	(122,425)
FINANCING ACTIVITY		
Increase in paid-up capital	**50,000**	40,000
Net cash from financing activity	**50,000**	40,000
NET INCREASE IN CASH AND CASH EQUIVALENTS	**1,571**	920
Cash and cash equivalents at 1 January	**1,882**	962
CASH AND CASH EQUIVALENTS AT 31 DECEMBER	**3,453**	1,882
OPERATIONAL CASH FLOWS FROM PROFITS		
Profit paid	**47,111**	21,162
Profit received	**67,530**	25,693

The attached explanatory notes 1 to 20 form part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

Year ended 31 December 2007

	Share capital	Statutory reserve	Available for sale reserve	Retained earnings	Total equity
	US$ 000's	US$ 000's	US$ 000's	US$ 000's	US$ 000's
Balance at 1 January 2007	82,500	4,353	2,312	13,709	102,874
Cumulative changes in fair values					
Transfer to profit and loss	-	-	(11,556)	-	(11,556)
Change in fair values	-	-	26,896	-	26,896
	-	-	15,340	-	15,340
Net profit for the year – 2007	-	-	-	50,878	50,878
Net income recognised during the year	-	-	15,340	50,878	66,218
Increase in share capital	50,000	-	-	-	50,000
Transfer to statutory reserve	-	5,088	-	(5,088)	-
Balance at 31 December 2007	**132,500**	**9,441**	**17,652**	**59,499**	**219,092**
Balance at 1 January 2006	42,500	3,820	481	8,916	55,717
Cumulative changes in fair values					
Transfer to profit and loss	-	-	88	-	88
Change in fair values	-	-	1,743	-	1,743
	-	-	1,831	-	1,831
Net profit for the year – 2006	-	-	-	5,326	5,326
Net income recognised during the year	-	-	1,831	5,326	7,157
Increase in share capital	40,000	-	-	-	40,000
Transfer to statutory reserve	-	533	-	(533)	-
Balance at 31 December 2006	82,500	4,353	2,312	13,709	102,874

The attached explanatory notes 1 to 20 form part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF SOURCES AND USES OF ZAKAH AND CHARITY FUNDS
Year ended 31 December 2007

	2007 US$ 000's	2006 US$ 000's
Sources of zakah and charity funds		
Balance at 1 January	**361**	312
Charity	**31**	75
Zakah due from the Bank (*)	**250**	240
Total sources	**642**	627
Uses of zakah and charity funds		
Zakah and charity paid to poor and needy	**(332)**	(266)
Undistributed zakah & charity funds at end of the year (Note 8)	**310**	361

* Zakah is calculated on the zakah base of the Group according to Financial Accounting Standard 9 issued by the Accounting and Auditing Organization for Islamic Financial Institutions using the net invested funds method and amounts to US$ 5,645,000 (2006: US$ 2,648,000) of which US$ 250,000 (2006: US$ 240,000) is payable by the Bank.

The attached explanatory notes 1 to 20 form part of these consolidated financial statements.

1. INCORPORATION AND ACTIVITIES

ABC Islamic Bank (E.C.) ['the Bank'] is an exempt joint stock company incorporated in the Kingdom of Bahrain on 10 December 1985 and registered with Ministry of Industry and Commerce under commercial registration (CR) number 16864. The Bank and its subsidiary ['the Group'] operate under a wholesale banking licence issued by the Central Bank of Bahrain (CBB) and are engaged in financial trading in accordance with the teachings of Islam (Shari'a). The postal address of the Bank's Registered Office is P O Box 2808, Manama, Kingdom of Bahrain. As of 31 December 2007, the total number of employees emplyed by the Bank was 17 (2006: 16).

Arab Banking Corporation B.S.C. (ABC B.S.C.), which operates under a wholesale banking licence issued by the CBB, holds 100% of the share capital of the Bank.

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

The ownership in the subsidiary of the Bank as at 31 December 2007 was as follows:

Name	Nature of Business	Date of incorporation	Country of incorporation	Amount and % of holding
ABC Clearing Company	Islamic Investment Company	30 November 1993	Cayman Islands	US$ 2,000 100% management shares

The Bank operates only in the Kingdom of Bahrain and does not have any branches.

The consolidated financial statements have been authorised for issue by the Board of Directors on 12 February 2008.

2. SIGNIFICANT ACCOUNTING POLICIES

Following is a summary of the significant accounting policies adopted in preparing the consolidated financial statements. These accounting policies are consistent with those used in the previous year.

Basis of preparation
The consolidated financial statements have been prepared in accordance with the Financial Accounting Standards issued by the Accounting and Auditing Organisation for Islamic Financial Institutions ['AAOIFI'] and in conformity with the Bahrain Commercial Companies Law, CBB and Financial Institutions Law. For matters which are not covered by AAOIFI standards, the Group uses the International Financial Reporting Standards ['IFRS'].

Accounting convention
The consolidated financial statements are prepared under the historical cost convention as modified for the re-measurement at fair value of certain available for sale investments.

The consolidated financial statements are prepared in US Dollars, being the functional currency of the Group's operations.

Basis of consolidation
The consolidated financial statements incorporate the financial statements of the Bank and its subsidiary. A subsidiary is an entity over which the Bank has control to govern its financial and operating policies in order to obtain benefits from its activities.

The results of subsidiary are included in the consolidated financial statements from the date on which control is transferred to the Bank and cease to be consolidated from the date on which control is transferred out of the Bank. All intercompany balances, transactions, income and expenses have been eliminated on consolidation.

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Murabaha receivables
Murabaha receivables consist mainly of deferred sales transaction agreements (murabaha) and are stated net of deferred profits and provision for impairment.

Available for sale investments
All investments are initially recognised at cost, being the fair value of the consideration given including acquisition costs associated with the investment.

After initial recognition, investments are remeasured at fair value. Fair value changes are reported as a separate component of equity until the investment is derecognised or the investment is determined to be impaired. On derecognition or impairment the cumulative gain or loss previously reported as "available for sale reserve" within equity, is included in the statement of income for the year.

The reversal of previously recognised impairment losses are recorded as increases in fair value reserve through equity.

Investments for which fair value cannot be determined or cannot be remeasured to fair value are carried at cost or at a previously revalued amount, less provision for any impairment.

Musharaka financing
Musharaka investments are partnership in which the Bank contributes capital. These are stated at the fair value of consideration given less impairment.

Equipment and Ijarah
These are initially recorded at cost. Ijarah comprise of plant and equipment.

Depreciation is provided on a straight-line basis on all equipment over its expected useful life.

Depreciation is provided on assets under Ijarah, at rates calculated to write off the cost of the asset over lease term.

The estimated useful lives of the assets for the calculation of depreciation are as follows:

Ijarah assets	1-10 years
Equipment	3-5 years

Murabaha payables
All Murabaha payables are carried at cost plus accrued profit less amounts repaid.

Provisions
Provisions are recognised when the Group has a present obligation (legal or constructive) arising from a past event and the cost to settle the obligation are both probable and able to be reliably measured.

Fair values
For investments traded in organised financial markets, fair value is determined by reference to stock exchange quoted market bid prices at the close of business on the balance sheet date.

For investments where there is no quoted market price, a reasonable estimate of the fair value is determined by reference to the current market value of another instrument with similar terms and characteristics, or is based on an assessment of the value of future cash flows or based on net asset value.

For Murabaha receivables, future cash flows are determined by the Group at current profit rates for financing contracts with similar terms and risk characteristics.

Revenue recognition

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

Musharaka financing
Income on musharaka financing is recognised when the right to receive payment is established or on distribution. Income related to accounts that are 90 days overdue is excluded from the statement of income.

Ijarah income
Income net of depreciation is recognised on a time-apportioned basis over the lease term.

Income that is 90 days or more overdue is excluded from income until it is received in cash.

Fees and commission income
Fees and commission income is recognised when earned.

Profit on Murabaha payables
Profit on Murabaha payables is accrued on the basis of terms and conditions of the individual contracts.

Taxation
There is no tax on corporate income in the Kingdom of Bahrain or in Cayman Islands. Therefore, no tax is payable.

Foreign currencies
Foreign currency transactions are recorded in US dollars at rates of exchange ruling at the value dates of the transactions. Monetary assets and liabilities in foreign currency are retranslated into US dollars at the rates of exchange ruling at the date of balance sheet. Any gains or losses are taken to consolidated statement of income.

Translation gains or losses on non-monetary items carried at fair value are included in equity as part of the fair value adjustment on available for sale investments.

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

Derecognition of financial assets and financial liabilities

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

- the right to receive cash flows from the asset have expired; or

- the Group has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to third party under a ‘pass-through’ arrangement; and

- either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the assets, but has transferred control of the asset.

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

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Derecognition of financial assets and financial liabilities (continued)

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

Zakah
Zakah is calculated on the zakah base of the Group according to Financial Accounting Standard 9 issued by the Accounting and Auditing Organization for Islamic Financial Institutions using the net invested funds method.

Cash and cash equivalents
Cash and cash equivalents comprise cash and bank balances with original maturities of less than 90 days.

Judgements
In the process of applying the Group's accounting policies, management has made the following judgements, apart from those involving estimations, which have the most significant effect in the amounts recognised in the consolidated financial statements:

Classification of investments
Management decides on acquisition of an investment whether it should be classified as held to maturity, held for trading, or available for sale.

For those deemed to be held to maturity management ensures that the requirements of FAS 17 and IAS 39 are met and in particular the Group has the intention and ability to hold these to maturity.

The Group classifies investments as trading if they are acquired primarily for the purpose of making a short term profit by the dealers.

All other investments are classified as available for sale.

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

Impairment
An assessment is made at each balance sheet date to determine whether there is objective evidence that a specific financial asset may be impaired. If such evidence exists, the estimated recoverable amount of that asset is determined and any impairment loss, based on the assessment by the Group of the value to it of anticipated future cash flows, is recognised in the consolidated statement of income. Specific provisions are created to reduce all impaired financial contracts to their expected realisable value.

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

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

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

Employees' end of service benefits
Provision is made for amounts payable under the Bahrain Labour law applicable to non-Bahraini employees' accumulated periods of service at the date of the balance sheet. Bahraini employees are covered under the General Organisation for Social Insurance scheme.

3. CASH AND BANK BALANCES

	2007	2006
	US$ 000's	US$ 000's
Balance with ABC B.S.C.	**2,918**	1,696
Cash and balance with other bank	**535**	186
	3,453	1,882

4. AVAILABLE FOR SALE INVESTMENTS

	2007			2006
	Cost	**Cumulative changes in fair values**	**Total carrying value**	Total
	US$ '000	**US$ '000**	**US$ '000**	US$ '000
Quoted Sukouks at fair value	**309,829**	**15,340**	**325,169**	240,293
Unqouted Sukouks at cost	**-**	**-**	**-**	26,875
Others	**3,751**	**-**	**3,751**	-
Carrying value	**313,580**	**15,340**	**328,920**	267,168

There are no impaired "available for sale investments" as of 31 December 2007 (2006: nil).

5. MURABAHA RECEIVABLES

	2007	2006
	US$ 000's	US$ 000's
International Commodity Murabaha	**25,500**	60,955
Murabaha receivables	**716,893**	363,695
Deferred profits	**(12,020)**	(5,717)
	730,373	418,933
Provisions for credit losses	**-**	(303)
	730,373	418,630

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

Murabaha receivables, which are non-performing as of 31 December 2007, amounted to US$ 4,069,000 (2006: US$ 5,281,000).

5. MURABAHA RECEIVABLES (CONTINUED)

The movement in provisions for credit losses is as follows:

	2007	2006
	US$ 000's	US$ 000's
At 1 January	**303**	-
Recoveries	**(303)**	-
	-	-
Impairment	**-**	303
At 31 December	**-**	303

6. IJARAH

Ijarah comprise:

	2007	2006
	US$ 000's	US$ 000's
Ijarah Muntahia Bittamleek *	**152,881**	95,112
Others	**112,180**	32,734
	265,061	127,846

There are no impaired Ijarahs as of 31 December 2007 (2006: nil).

* In Ijarah Muntahia Bittamleek, the lessees are entitled to buy these assets at the end of Ijarah term.

	2007	2006
	US$ 000's	US$ 000's
Cost:		
At 1 January	**125,985**	83,719
Additions	**100,505**	44,933
Disposals	**(41,862)**	(2,667)
At 31 December	**184,628**	125,985
Depreciation:		
At 1 January	**30,873**	16,834
Provided during the year	**14,164**	14,039
Relating to disposals	**(13,290)**	-
At 31 December	**31,747**	30,873
Net book amount:		
At 31 December	**152,881**	95,112

6. IJARAH (CONTINUED)

The details of Ijarah income are as follows:

	2007	2006
	US$ 000's	US$ 000's
Ijarah income – gross	**26,035**	18,618
Depreciation provided during the year	**(14,164)**	(14,039)
Ijarah income – net	**11,871**	4,579

7. OTHER ASSETS

	2007	2006
	US$ 000's	US$ 000's
Receivable on sale of available for sale investments	**27,222**	-
Accrued income receivable	**7,043**	6,984
Mandatory reserve with Central Bank of Bahrain	**53**	53
Others	**598**	617
	34,916	7,654

8. OTHER LIABILITIES

	2007	2006
	US$ 000's	US$ 000's
Zakah and charity funds payable	**310**	361
Staff related accruals	**1,739**	1,503
Unearned income	**9,964**	2,355
Accrued charges	**2,283**	3,566
	14,296	7,785

9. MURABAHA PAYABLES

	2007	2006
	US$ 000's	US$ 000's
Customers' accounts	**44,662**	15,510
Banks and other financial institutions	**132,746**	122,947
ABC B.S.C.	**954,086**	574,192
	1,131,494	712,649

10. EQUITY

(i) Share capital

	Ordinary shares of US $ 100 each	
	2007	2006
	US$ 000's	US$ 000's
Authorised	**200,000**	200,000
Issued, subscribed and fully paid	**132,500**	82,500

An increase in the issued and paid up capital from US$ 82,500,000 to US$ 132,500,000 was approved in the extraordinary general meeting of the shareholders on 20 August 2007. In 2006, an increase in authorised share capital from US$ 52,500,000 to US$ 200,000,000 and an increase in issued and paid up capital from US$ 42,500,000 to US$ 82,500,000 were approved.

(ii) Statutory reserve
In accordance with the requirements of the Bahrain Commercial Companies Law, 10% of the net profit for the year has been transferred to statutory reserve. The Group may resolve to discontinue such annual transfers when the reserve total 50% of the paid up share capital. The reserve is not distributable but can be utilised as security for the purpose of a distribution in such circumstances as stipulated in the Bahrain Commercial Companies Law and with the prior approval of the CBB.

Proposed dividend
The group proposed a cash dividend of US$ 20,000,000 which will be submitted for formal approval in the Annual General Meeting on 28 February subject to regulatory approval.

11. MEMORANDUM ITEMS

Credit-related financial instruments
These include commitments to enter into financing contracts, which are designed to meet the requirements of the Group's customers.

Commitments to extend financing represents contractual commitments under Murabaha receivables. Commitments generally have fixed expiration dates, or other termination clauses. Since commitments may expire without being drawn upon, the total contract amounts do not necessarily represent future cash requirements.

Letters of credit, guarantees and acceptances commit the Group to make payments on behalf of customers contingent upon the failure of the customer to perform under the terms of the contract.

11. MEMORANDUM ITEMS (CONTINUED)

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

	2007	2006
	US$ 000's	US$ 000's
Letters of credit	**23,234**	8,036
Guarantees	**54,869**	3,898
Acceptances	**132**	2,897
	78,235	14,831

Irrevocable commitments to provide trading facilities at the balance sheet date amounted to US$ 268,674,000 (2006: US$ 85,716,000) of which US$ 21,381,000 (2006: US$ 72,718,000) expire in less than one year.

12. FEES AND COMMISSION INCOME

	2007	2006
	US$ 000's	US$ 000's
Income from fiduciary services	**1,501**	218
Other fees and comission income	**3,118**	3,224
	4,619	3,442

13. OTHER EXPENSES

	2007	2006
	US$ 000's	US$ 000's
Charges by ABC B.S.C.	**700**	700
Business related expenses	**421**	348
Professional fees and licenses	**427**	165
Other operating expenses	**536**	604
	2,084	1,817

14. SEGMENTAL INFORMATION

The activities of the Group are performed on an integrated basis. Therefore, any segmentation of operating income, expenses, assets and liabilities is not relevant. As such, operating income, expenses, assets and liabilities are not segmented.

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

15. RELATED PARTY TRANSACTIONS

The Group enters into transactions with ABC B.S.C. in the ordinary course of business at commercial rates. All the financing contracts with the related party are performing and are free of any provision for possible impairment.

The balances with the related party as of the balance sheet date are as follows:

	2007	2006
	US$ 000's	US$ 000's
Balance with ABC B.S.C.	**2,918**	1,696
Murabaha receivables	**25,500**	60,955
Murabaha payables	**954,086**	574,192

The income and expenses arising from dealing with the related party included in the statement of income are as follows:

	2007	2006
	US$ 000's	US$ 000's
Income from Murabaha receivables	**1,317**	1,340
Profit on Murabaha payables	**41,710**	17,941
Charges by ABC B.S.C.	**700**	700

In addition to transactions with ABC B.S.C., the Group incurred the following expenses relating to related parties:

	2007	2006
	US$ 000's	US$ 000's
Shari'a Supervisory Board	67	75
Short term employee benefits to key management personnel	644	539

Key management personnel are those that possess significant decision making and direction setting responsibilities, at different grades within the Group.

16. RISK MANAGEMENT

Introduction
Risk is inherent in the Bank's activities but it is managed through a process of ongoing identification, measurement and monitoring, subject to risk limits and other controls. This process of risk management is critical to the Bank's continuing profitability and each individual within the Bank is accountable for the risk exposures relating to his or her responsibilities. The Bank is exposed to credit risk, liquidity risk and market risk. It is also subject to operating risks.

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

The major risks to which the Group is exposed in conducting its business and operations, and the means and organisational structure it employs in seeking to manage them strategically in building shareholder value, are outlined below.

Risk management structure
Executive Management is responsible for implementing the Group's Risk Strategy/Appetite and Policy guidelines set by the Board Risk Committee (BRC), including the identification and evaluation on a continuous basis of all significant risks to the business and the design and implementation of appropriate internal controls to minimise them. This is done with the involvement of a Risk Manager and through the following senior management committees:

The Audit and Governance Committee is responsible to the Board for ensuring that the Group maintains an effective system of financial, accounting and risk management controls and for monitoring compliance with the requirements of the regulatory authorities.

The following committees of ABC B.S.C. assist the Bank with its risk management:

The BRC is responsible for the continual review and approval of the ABC B.S.C.'s Risk Policies and Medium Term and Annual Risk Strategy/Appetite, within which business strategy, objectives and targets are formulated. The Committee reviews the Group's Risk Profile to ensure that it is within the ABC B.S.C. Risk Policies and Appetite parameters. It delegates authority to senior management to conduct day-to-day business within the prescribed policy and strategy parameters, whilst ensuring that processes and controls are adequate to manage the Risk Policies and Strategy.

The Head Office Credit Committee (HOCC) is responsible for credit decisions, setting country and other high level limits, dealing with impaired assets and general credit policy matters.

The Asset and Liability Committee (ALCO) is chiefly responsible for defining long-term strategic plans and short-term tactical initiatives for directing asset and liability allocation prudently for the achievement of the Group's strategic goals. ALCO monitors the Group's liquidity and market risks and the Group's risk profile in the context of economic developments and market fluctuations, to ensure that the Group's ongoing activities are compatible with the risk/reward guidelines approved by the BRC.

The Operational Risk Management Committee oversees the independent Operational Risk Management function and is responsible for defining long-term strategic plans and short-term tactical initiatives to prudently manage, control and measure exposure to operational risks.

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

16. RISK MANAGEMENT (CONTINUED)

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

For all levels throughout the Bank, specifically tailored risk reports are prepared and distributed in order to ensure that all business divisions have access to extensive, necessary and up-to-date information.

Credit risk
Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. The Group attempts to control credit risk by monitoring credit exposures, limiting transactions with specific counterparties, and continually assessing the creditworthiness of counterparties. In addition to monitoring credit limits, the Group manages the credit exposure by entering into collateral arrangements with counterparties in appropriate circumstances, and limiting the duration of exposure. In certain cases the Group may also close out transactions or assign them to other counterparties to mitigate credit risk.

The first level of protection against undue credit risk is through ABC B.S.C.'s country, industry and other risk threshold limits, together with customer and customer group credit limits, set by the BRC and the HOCC, and allocated between subsidiaries of ABC B.S.C. Credit exposure to individual customers or customer groups is then controlled through a tiered hierarchy of delegated approval authorities based on the risk rating of the customer under the Bank's internal credit rating system. Where unsecured facilities sought are considered to be beyond prudential limits, Group policies require collateral to mitigate the credit risk in the form of cash, securities, legal charges over the customer's assets or third-party guarantees. The Group also employs threshold 'risk adjusted return on capital' as a measure to evaluate the risk/reward relationship at the transaction approval stage.

Type of credit risk
Various contracts entered into by the Group comprise Murabaha receivables and Ijarah.

Murabaha receivables
The Group finances Murabaha transactions through buying a commodity which represent the object of the Murabaha and then resells this commodity to the Murabeh (beneficiary) after computing a margin of profit over cost. The sale price (cost plus the profit margin) is repaid in installments by the Murabeh over the agreed period. The Murabeh pays a down payment of the sale price upon signing the Murabaha contract.

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

16. RISK MANAGEMENT (CONTINUED)

Maximum exposure to credit risk without taking account of any collateral and other credit enhancements

The table below shows the maximum exposure to credit risk for the components of the balance sheet, including credit related commitments. The maximum exposure is shown gross, before the effect of migration through the use of master netting and collateral agreements.

	Gross maximum exposure	Gross maximum exposure
	2007	2006
	US$ '000	US$ '000
Available for sale investments	**328,920**	267,168
Murabaha receivables	**730,373**	418,630
Musharaka financing	**2,084**	-
Ijarah	**265,061**	127,846
Total	**1,326,438**	813,644
Letters of credit, guarantees and acceptances	**78,235**	14,831
Irrevocable commitments to provide trading facilities	**268,674**	85,716
Total	**346,909**	100,547

Concentrations of credit risk arise when a number of counterparties are engaged in similar business activities, or activities in the same geographic region, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations of credit risk indicate the relative sensitivity of the Group's performance to developments affecting a particular industry or geographic location. The Group seeks to manage its credit risk exposure through diversification of financing and investment activities to avoid undue concentrations of risks with individuals or groups of customers in specific locations or businesses.

16. RISK MANAGEMENT (CONTINUED)

The Bank's assets, liabilities, equity and memorandum items can be analysed by the following geographical regions:

	2007			2006		
	Assets	**Liabilities and Equity**	**Memorandum items**	Assets	Liabilities and Equity	Memorandum items
	US$ 000's	**US$ 000's**	**US$ 000's**	US$ 000's	US$ 000's	US$ 000's
Geographic region:						
North America	**3,868**	**-**	**-**	19,377	-	-
Western Europe	**-**	**-**	**-**	6,875	-	-
Other Europe (including Turkey)	**49,813**	**-**	**-**	38,932	-	-
Arab World:						
- Middle East	**1,276,506**	**1,364,791**	**78,235**	712,798	814,025	14,831
- Africa	**-**	**7**	**-**	-	9,126	-
Asia:						
- Far East	**34,695**	**84**	**-**	15,176	57	-
- Other	**-**	**-**	**-**	30,150	100	-
	1,364,882	**1,364,882**	**78,235**	823,308	823,308	14,831

16. RISK MANAGEMENT (CONTINUED)

An industry sector analysis of the Bank's assets, liabilities, equity and memorandum items is as follows:

	2007			2006		
	Assets	**Liabilities and Equity**	**Memorandum items**	Assets	Liabilities and Equity	Memorandum items
	US$ 000's	**US$ 000's**	**US$ 000's**	US$ 000's	US$ 000's	US$ 000's
Industry sector:						
Manufacturing	**263,365**	**15,238**	**22,252**	100,193	16	9,639
Construction	**263,307**	**22**	**-**	15,073	-	-
Trading	**61,278**	**811**	**-**	10,158	50	-
Banks and financial institutions	**359,825**	**1,102,687**	**1,104**	264,153	697,138	5,192
Government	**85,122**	**-**	**-**	149,117	-	-
Communication	**-**	**-**	**54,879**	125,113	-	-
Personal	**-**	**7**	**-**	-	256	-
Oil and Gas	**38,285**	**-**	**-**	29,402	-	-
Commercial real estate	**234,686**	**-**	**-**	21,853	-	-
Transportation	**12,357**	**-**	**-**	37,408	-	-
Other	**46,657**	**246,117**	**-**	70,838	125,848	-
	1,364,882	**1,364,882**	**78,235**	823,308	823,308	14,831

The credit quality of financial assets is managed by the Bank using internal credit ratings. These internal credit ratings range from 1 to 11 for each individual borrower. They are defined as follows:

High grade: These borrowers are rated between 1 and 3 and are of high credit quality, most with strong external credit ratings and considered as low risk.

Standard grade: These borrowers are rated between 4 and 8 and are of good to marginal credit quality, often with lower external credit ratings than high grade and considered as higher risk.

Substandard grade: These borrowers are rated between 9 and 10 and full repayment is questionable.

Past due or individually impaired: These borrowers are rated 11 and are expected to be total loss.

16. RISK MANAGEMENT (CONTINUED)

The table below shows the credit quality by class of financial asset, based on the Bank's credit rating system.

	Neither past due nor impaired			
	High grade	Standard grade	Sub-standard grade	Total
	2007	2007	2007	2007
	(1-3)	(4-8)	(9-10)	
Available for sale investments	**46,221**	**282,699**	**-**	**328,920**
Murabaha receivables	**119,424**	**606,880**	**4,069**	**730,373**
Musharaka financing	**-**	**2,084**	**-**	**2,084**
Ijarah	**224,967**	**40,094**	**-**	**265,061**
	390,612	**931,757**	**4,069**	**1,326,438**

	Neither past due nor impaired			
	High grade	Standard grade	Sub-standard grade	Total
	(1-3)	(4-8)	(9-10)	
	2006	2006	2006	2006
Available for sale investments	127,173	139,995	-	267,168
Murabaha receivables	127,882	285,468	5,281	418,631
Ijarah	112,319	15,527	-	127,846
	367,374	440,990	5,281	813,645

Past due but not impaired financial assets
As of 31 December 2007, Murabaha receivables that were past due amounted to US$ 4,069,000 (2006: US$ 4,069,000), all of which were past due for more than 90 days.

Financial assets whose terms have been renegotiated
As of 31 December 2007, there were no financial assets whose terms were renegotiated during the year (2006: nil).

Collateral and other credit enhancements
The amount and type of collateral depends on an assessment of the credit risk of the counterparty. The types of collateral mainly includes cash, charges over real estate properties, inventory and trade receivables.

Management monitors the market value of collateral, requests additional collateral in accordance with the underlying agreement, and monitors the market value of collateral obtained during its review of the adequacy of the allowance for impairment losses. The Bank also makes use of master netting agreements with counterparties.

Market risk
The Group uses ABC B.S.C.'s established risk management policies and limits within which exposure to market risk is monitored. These are measured and controlled by the Risk Management Department (RMD) with strategic oversight exercised by Asset and Liability Committee (ALCO). The RMD's Market Risk Management (MRM) unit is responsible for developing and implementing market risk policy and risk measuring/monitoring methodology and for reviewing all new trading products and product limits prior to ALCO approval. MRM's core responsibility is to measure and report market risk against limits throughout the ABC B.S.C.'s subsidiaries.

16. RISK MANAGEMENT (CONTINUED)

Profit rate risk

Profit rate risk arises from the possibility that changes in profit rates will affect the future profitability or the fair values of the financial instruments. The Group is exposed to profit rate risk as a result of mismatches or gaps in the amounts of assets and liabilities that mature in a given period.

At the year end, the Group was exposed to profit rate risk on its financial assets and financial liabilities. The following table indicates the profit rates during the year expressed as a percentage of the principal outstanding.

	2007	2006
	%	%
Available for sale investments	**5.17 - 7.61**	5.74 - 7.65
Murabaha receivables	**4.83 - 9.19**	5.79 - 8.77
Musharaka financing	**6.33**	-
Ijarah	**4.24 - 6.90**	5.79 - 7.49
Murabaha payables	**4.50 - 5.70**	4.41 - 5.71

The sensitivity for every 25 basis points increase in profit rates of the Group's statement of income, with all other variables held constant, would be an increase of profit by US$ 2,315,000 (2006: US$ 1,396,000).

Currency risk

The Group's transactions are carried out substantially in US Dollars, and as such currency risk is minimal.

Liquidity risk

Liquidity risk is the risk that an institution will be unable to meet its net funding requirements. Liquidity risk can be caused by market disruptions or credit downgrades which may cause certain sources of funding to cease immediately. To guard against this risk, management has diversified funding sources and assets are managed with liquidity in mind.

The following table summarises the maturity profile of the Group's assets and liabilities. The contractual maturities of assets and liabilities have been determined on the basis of the remaining period at the balance sheet date to the contractual maturity date and do not take account of the effective maturities as indicated by the Group's deposit retention history.

16. RISK MANAGEMENT (CONTINUED)

Liquidity risk (continued)
The maturity profile of assets, liabilities, and equity is as follows:

31 December 2007	Up to 1 month	1 to 3 months	3 to 6 months	6 months to 1 year	1 to 3 years	Over 3 years	No fixed maturity	Total
	US$ 000's	US$ 000's	US$ 000's	US$ 000's	US$ 000's	US$ 000's	US$ 000's	US$ 000's
ASSETS								
Cash and bank balances	3,453	-	-	-	-	-	-	3,453
Available for sale investments	2,993	3,751	1,500	1,500	43,815	275,361	-	328,920
Murabaha receivables	142,077	166,677	227,838	102,128	79,790	11,863	-	730,373
Musharaka financing	-	-	-	-	2,084	-	-	2,084
Ijarah	908	8,693	6,712	5,265	89,982	153,501	-	265,061
Equipment	-	-	-	-	-	-	75	75
Other assets	27,222	-	-	-	-	-	7,694	34,916
Total assets	176,653	179,121	236,050	108,893	215,671	440,725	7,769	1,364,882
LIABILITIES AND EQUITY								
Other liabilities	-	-	-	-	-	-	14,296	14,296
Murabaha payables	377,813	376,934	281,472	77,847	17,428	-	-	1,131,494
Equity	-	-	-	-	-	-	219,092	219,092
Total liabilities and equity	377,813	376,934	281,472	77,847	17,428	-	233,388	1,364,882
Net liquidity gap	(201,160)	(197,813)	(45,422)	31,046	198,243	440,725	(225,619)	
Cumulative liquidity gap	(201,160)	(398,973)	(444,395)	(413,349)	(215,106)	225,619		

16. RISK MANAGEMENT (CONTINUED)

Liquidity risk (continued)

31 December 2006	Up to 1 month	1 to 3 months	3 to 6 months	6 months to 1 year	1 to 3 years	Over 3 years	No fixed maturity	Total
	US$ 000's	US$ 000's	US$ 000's	US$ 000's	US$ 000's	US$ 000's	US$ 000's	US$ 000's
ASSETS								
Cash and bank balances	1,882	-	-	-	-	-	-	1,882
Available for sale investments	-	-	1,500	15,598	95,875	154,195	-	267,168
Murabaha receivables	136,292	102,327	37,036	64,658	50,351	27,966	-	418,630
Ijarah	501	3,056	5,561	9,169	23,877	85,682	-	127,846
Equipment	-	-	-	-	-	-	128	128
Other assets	-	-	-	-	-	-	7,654	7,654
Total assets	138,675	105,383	44,097	89,425	170,103	267,843	7,782	823,308
LIABILITIES AND EQUITY								
Other liabilities	-	-	-	-	-	-	7,785	7,785
Murabaha payables	309,147	202,458	146,127	38,688	16,229	-	-	712,649
Equity	-	-	-	-	-	-	102,874	102,874
Total liabilities and equity	309,147	202,458	146,127	38,688	16,229	-	110,659	823,308
Net liquidity gap	(170,472)	(97,075)	(102,030)	50,737	153,874	267,843	(102,877)	
Cumulative liquidity gap	(170,472)	(267,547)	(369,577)	(318,840)	(164,966)	102,877		

17. FAIR VALUE OF FINANCIAL INSTRUMENTS

The estimated fair values of financial assets and financial liabilities are not materially different from their carrying values as stated in the consolidated balance sheet.

18. SHARI'A SUPERVISORY BOARD

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

19. EARNINGS AND EXPENSES PROHIBITED BY SHARI'A

Earnings realised during the year from transactions that were not permitted by Shari'a amounted to US$ 31,121 (2006: US$ 75,467) out of which US$ 3,661 (2006: US$ 26,688) is interest from money at call with banks. This amount has been taken to charity.

20. SOCIAL RESPONSIBILITY

The Group discharges its social responsibility by paying out zakah and charity to organisations approved by Shari'a Supervisory Board.

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