

**Liquidity Management Centre B.S.C. (c)**

**SHARI'A SUPERVISORY BOARD REPORT,  
REPORT OF THE BOARD OF DIRECTORS AND  
CONSOLIDATED FINANCIAL STATEMENTS**

**31 DECEMBER 2007**

## **INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF LIQUIDITY MANAGEMENT CENTRE B.S.C. (c)**

We have audited the accompanying consolidated balance sheet of Liquidity Management Centre B.S.C. (c) ["the Bank"] and its subsidiary [together "the Group"] as of 31 December 2007, and the related consolidated statements of income, cash flows and changes in equity 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 the 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 and its cash flows 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 Group.

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. We obtained all the information and explanations which we required for the purpose of our audit.

24 February 2008

Manama, Kingdom of Bahrain

Liquidity Management Centre B.S.C. (c)

CONSOLIDATED BALANCE SHEET

31 December 2007

	<i>Notes</i>	<i>2007</i> <i>US\$ 000's</i>	<i>2006</i> <i>US\$ 000's</i>
<b>ASSETS</b>			
Cash and balances with banks		<b>413</b>	403
Murabaha receivables	3	<b>13,197</b>	30,322
Investments	4	<b>271,044</b>	181,198
Investment properties		-	4,906
Other assets	5	<b>10,653</b>	3,141
Equipments		<b>261</b>	141
<b>TOTAL ASSETS</b>		<b>295,568</b>	220,111
<b>LIABILITIES AND EQUITY</b>			
<b>LIABILITIES</b>			
Due to sukukholders	6	<b>208,581</b>	158,352
Due to banks		<b>1,988</b>	-
Due to non banks		<b>17,000</b>	-
Other liabilities	7	<b>2,665</b>	3,749
		<b>230,234</b>	162,101
<b>EQUITY</b>			
Share capital	9	<b>51,000</b>	51,000
Reserves	9	<b>4,308</b>	2,055
Retained earnings		<b>10,026</b>	4,955
		<b>65,334</b>	58,010
<b>TOTAL LIABILITIES AND EQUITY</b>		<b>295,568</b>	220,111

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Aref Ahmed Al-Kooheji  
Chairman

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Emad Al Monayea  
Deputy Chairman

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Ahmed Abbas  
Chief Executive Officer

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

Liquidity Management Centre B.S.C. (c)

CONSOLIDATED STATEMENT OF INCOME

Year ended 31 December 2007

	<i>Notes</i>	<b>2007</b> <i>US\$ 000's</i>	<i>2006</i> <i>US\$ 000's</i>
Income from investments		<b>14,584</b>	7,731
Less: Return to Sukukholders		<b>(9,139)</b>	(6,397)
Less: Return to banks		<b>(129)</b>	-
Less: Return to non banks		<b>(714)</b>	-
		<b>4,602</b>	1,334
Income from Murabaha receivables		<b>996</b>	967
Investment Banking Fees	8	<b>9,696</b>	6,842
Gain on sale of investments carried at amortised cost		-	238
Loss on sale of investment available for sale		<b>(39)</b>	(479)
Gain on sale of investment properties		<b>243</b>	-
Other income		-	26
<b>OPERATING INCOME</b>		<b>15,498</b>	8,928
Staff costs		<b>2,529</b>	2,324
Depreciation		<b>70</b>	68
General and administrative expenses	10	<b>1,466</b>	443
<b>OPERATING EXPENSES</b>		<b>4,065</b>	2,835
<b>NET PROFIT FOR THE YEAR BEFORE 2006</b>		<b>11,433</b>	6,093
<b>DIRECTOR'S REMUNERATION</b>		<b>313</b>	-
Director's remuneration - 2006		<b>313</b>	-
<b>NET PROFIT FOR THE YEAR AFTER</b>		<b>11,120</b>	<b>6,093</b>
<b>DIRECTOR'S REMUNERATION</b>		<b>11,120</b>	<b>6,093</b>

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

Liquidity Management Centre B.S.C. (c)

CONSOLIDATED STATEMENT OF CASH FLOWS

Year ended 31 December 2007

	2007 US\$ 000's	2006 US\$ 000's
<b>OPERATING ACTIVITIES</b>		
Net profit for the year before directors' remuneration	11,433	6,093
Adjustment for:		
Depreciation	70	68
Amortisation of premium on investments	(326)	(16)
Gain on sale of investment properties	(243)	-
Loss on sale of investment available for sale	39	479
Gain on sale of investments carried at amortised cost	-	(238)
	<u>10,973</u>	<u>6,386</u>
Operating profit before changes in operating assets and liabilities:	10,973	6,386
Changes in:		
Murabaha receivables	7,313	(7,313)
Other assets	(7,512)	(356)
Due to sukukholders	50,229	75,884
Due to banks	1,988	-
Due to non banks	17,000	-
Other liabilities	(1,084)	2,940
	<u>78,907</u>	<u>77,541</u>
Net cash from operating activities	78,907	77,541
<b>INVESTING ACTIVITIES</b>		
Purchase of investment carried at fair value through statement of income	-	(47)
Purchase of investments carried at amortised cost	(115,225)	(102,123)
Sale proceeds of investments carried at amortised cost/ held to maturity	31,807	8,894
Proceeds (Purchase) from/to investment properties	5,149	(4,906)
Sale proceeds of investment available for sale	8,064	-
Purchase of investments available for sale	(14,176)	-
Purchase of equipments	(190)	(77)
	<u>(84,571)</u>	<u>(98,259)</u>
Net cash used in investing activities	(84,571)	(98,259)
<b>FINANCING ACTIVITIES</b>		
Dividend paid	(3,825)	-
Directors' remuneration paid	(313)	(160)
Increase in share capital	-	30,000
	<u>(4,138)</u>	<u>29,840</u>
Net cash (used in) from financing activities	(4,138)	29,840
<b>(DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS</b>	<b>(9,802)</b>	<b>9,122</b>
Cash and cash equivalents at 1 January	<u>23,412</u>	<u>14,290</u>
<b>CASH AND CASH EQUIVALENTS AT 31 DECEMBER</b>	<b><u>13,610</u></b>	<b><u>23,412</u></b>
Cash and cash equivalents at year end comprise of:		
Cash and balances with banks	413	403
Murabaha receivables maturing within ninety days	13,197	23,009
	<u>13,610</u>	<u>23,412</u>

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

Liquidity Management Centre B.S.C. (c)

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

Year ended 31 December 2007

	<i>Reserves</i>						<i>Total equity</i> US\$ 000's
	<i>Share capital</i> US\$ 000's	<i>Statutory reserve</i> US\$ 000's	<i>General reserves</i> US\$ 000's	<i>Investment fair value reserve</i> US\$ 000's	<i>Total Reserves</i> US\$ 000's	<i>Retained earnings</i> US\$ 000's	
Balance at 1 January 2007	51,000	818	818	419	2,055	4,955	58,010
Cumulative changes in fair value	-	-	-	29	29	-	29
Transfer of fair value gain to reserve, net	-	-	-	-	-	-	-
<b><i>Income recognised directly in equity</i></b>	-	-	-	<b>29</b>	<b>29</b>	-	<b>29</b>
Net profit for the year	-	-	-	-	-	11,120	11,120
<b><i>Total income and expenses recognised during the year</i></b>	-	-	-	<b>29</b>	<b>29</b>	<b>11,120</b>	<b>11,149</b>
Transfer to statutory reserve	-	1,112	-	-	1,112	(1,112)	-
Transfer to general reserve	-	-	1,112	-	1,112	(1,112)	-
Dividend paid	-	-	-	-	-	(3,825)	(3,825)
<b>Balance at 31 December 2007</b>	<b>51,000</b>	<b>1,930</b>	<b>1,930</b>	<b>448</b>	<b>4,308</b>	<b>10,026</b>	<b>65,334</b>
Balance at 1 January 2006	20,000	209	209	154	572	1,504	22,076
Cumulative changes in fair value	-	-	-	1	1	-	1
Transfer of fair value gain to reserve, net	-	-	-	264	264	(264)	-
<b><i>Income recognised directly in equity</i></b>	-	-	-	<b>265</b>	<b>265</b>	<b>(264)</b>	<b>1</b>
Net profit for the year	-	-	-	-	-	6,093	6,093
<b><i>Total income and expenses recognised during the year</i></b>	-	-	-	<b>265</b>	<b>265</b>	<b>5,829</b>	<b>6,094</b>
Increase in share capital	30,000	-	-	-	-	-	30,000
Bonus shares issued	1,000	-	-	-	-	(1,000)	-
Directors' remuneration paid	-	-	-	-	-	(160)	(160)
Transfer to statutory reserve	-	609	-	-	609	(609)	-
Transfer to general reserve	-	-	609	-	609	(609)	-
<b>Balance at 31 December 2006</b>	<b>51,000</b>	<b>818</b>	<b>818</b>	<b>419</b>	<b>2,055</b>	<b>4,955</b>	<b>58,010</b>

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

31 December 2007

## 1 INCORPORATION AND ACTIVITIES

Liquidity Management Centre B.S.C. (c) (the "Bank") is a closed joint stock company incorporated in the Kingdom of Bahrain on 31 July 2002 and registered with Ministry of Industry and Commerce under commercial registration (CR) number 49092. The Bank operates in Kingdom of Bahrain under wholesale banking license issued by the Central Bank of Bahrain (CBB). The Bank is engaged in the following activities:

- Facilitate creation of an Islamic inter-bank money market that will allow Islamic Financial Services Institutions ("IFSI") to effectively manage their assets and liabilities.
- Provide short-term liquid, tradable asset backed treasury instruments (Sukuk) based on Islamic Shari'a principles where IFSI can invest their surplus liquidity.
- Provide short-term investment opportunities based on Islamic Shari'a principles.

The activities of the Bank and its wholly owned subsidiary (the "Group") are to carry out operations in accordance with the teachings of Islam (Shari'a). The Group's Shari'a Supervisory Board is entrusted to ensure the Group's adherence to Shari'a rules and principles in its transactions and activities.

For the purpose of attainment of its investment objectives, the Group also sets up establishments or finance divisions or carries on such activities which include but not restricted to the following:

- i) Act as an agent for Special Purpose Vehicles ("SPV") established to securitise assets.
- ii) Establish SPVs of various kinds to carry on all the activities connected therewith.
- iii) Facilitate the sourcing and securitisation of assets, acquired from various sources.
- iv) Establish lines of liquidity to support the issuance of securitised instruments (Sukuk).
- v) Actively trade Sukuk by offering buy/sell quotes and service all investors in Sukuk.

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

The Bank operates only in the Kingdom of Bahrain. The number of Group employees as of 31 December 2007 was 25 (2006: 17).

## 2.1 BASIS OF PREPARATION

The consolidated financial statements are prepared in accordance with Financial Accounting Standards issued by the Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI), in conformity with the Bahrain Commercial Companies Law, Central Bank of Bahrain and Financial Institution Law. For matters which are not covered by AAOIFI standards, the Group uses the International Financial Reporting Standards (the "IFRSs"). These consolidated financial statements are presented in US dollars, being the functional currency of the Group.

## 2.2 BASIS OF ACCOUNTING CONVENTION

The consolidated financial statements have been prepared on historical cost basis, except for investment properties, available for sale investments and investments carried at fair value through statement of income, that have been remeasured at fair value.

### 2.3 SIGNIFICANT ACCOUNTING POLICIES

The accounting policies used in the preparation of the consolidated financial statements are consistent with those used in the preparation of the annual consolidated financial statements for the year ended 31 December 2006, which were prepared in accordance with Financial Accounting Standards ["FAS"] issued by the Accounting and Auditing Organisation for Islamic Financial Institutions ["AAOIFI"].

#### **Basis of consolidation**

These consolidated financial statements incorporate the financial statements of the Bank and its wholly owned subsidiary "The Short Term Sukuk Centre B.S.C. (closed)" (STSC). A subsidiary is an entity over which the Bank has power to control, which is other than fiduciary in nature. The results of the subsidiary are included in the consolidated financial statements from the effective date of formation or acquisition. All intercompany balances and transactions, including unrealised profits arising from intra-group transactions, have been eliminated in full.

The financial statements of STSC are prepared for the same reporting year as the Bank using consistent accounting policies and adjustments have been made to bring into line any dissimilar accounting policies that may exist.

#### **Murabaha receivables**

Murabaha receivables are sales or credit terms, based on the delivery of a commodity, which is the subject of the Murabaha, by the seller to the buyer and enabling it to possess and benefit from the commodity, with the understanding that the buyer will pay the agreed price at a certain future date inclusive of a profit margin.

Receivable under murabaha contracts are stated net of provision for impairment if any, and deferred profits.

#### **Investments**

All investments other than 'investment carried at fair value through statement of income' are initially recognised at cost, being the fair value of the consideration given plus any directly attributable incremental costs of acquisition. 'Investment carried at fair value through statement of income' are recognised at cost.

Investments are classified as follows:

i) *Held to maturity*

Investments in Sukuk having fixed or determinable payments and fixed maturity where the Group has both the intent and the ability to hold such investments to maturity are classified as held to maturity. After initial recognition such investments are carried at amortised cost less provision for impairment in value.

ii) *Available for sale*

After initial recognition these investments are remeasured at fair value. All changes in fair value of such assets subsequent to initial recognition are reported in the consolidated statement of equity and held in a reserve until realisation.

iii) *Investments carried at amortised cost*

Sukuk (debt instruments) which do not meet the definition of held to maturity and which have fixed or determinable payments but are not quoted in an active market are treated as investments carried at amortised cost less provision for impairment in value. Amortised cost is calculated using the effective profit rate that takes into account the effect of any premium or discount on acquisition.

iv) *Carried at fair value through statement of income*

After initial recognition these investments are remeasured at fair value and the resultant gains or losses are included in the statement of income as "gain or loss on items fair valued through statement of income". Unrealised gains or losses are appropriated to a investment fair value reserve in accordance with AAOIFI. Upon realisation of these gains and losses, these are transferred to retained earnings.

31 December 2007

### 2.3 SIGNIFICANT ACCOUNTING POLICIES (continued)

#### **Investments Properties**

The Bank holds certain properties as investments to earn rental income, for capital appreciation, or both. Investment properties are measured initially at cost, including transaction costs. Subsequent to initial recognition, investment properties are stated at fair value, which reflects market conditions at the balance sheet date. Gains or losses arising from the changes in the fair values of investment properties are included in the consolidated statement of income in the year in which they arise.

In accordance with AAOIFI unrealised gains are appropriated to an investment fair value reserve and are transferred to retained earnings only when realised.

#### **Financial instruments**

Financial assets and financial liabilities carried on the balance sheet include cash and bank balances, murabaha receivables, investments, other assets, due to sukukholders, due to banks, due to non banks and other liabilities.

Financial instruments are classified as liabilities or equity in accordance with contractual arrangement. Profit, dividends, gains and losses relating to a financial instrument classified as a liability, are reported as expense. Distributions to holders of financial instruments classified as equity are charged directly to equity.

#### **Derecognition**

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

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

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

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

#### **Impairment and uncollectability of financial assets**

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 Bank 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.

#### **Sukuk assets under management**

Sukuk assets managed in a fiduciary capacity are not treated as assets of the Bank and accordingly are not included in the consolidated balance sheet.

31 December 2007

## 2.3 SIGNIFICANT ACCOUNTING POLICIES (continued)

### Revenue recognition

#### *Income from investments*

Income from investments is recognised on a time-apportioned basis over the period of investment. Income that is 90 days or more overdue is excluded from income until it is received in cash.

#### *Income from Murabaha receivables*

As the income is quantifiable and contractually determined at the commencement of the contract, the income is recognised on a time apportioned basis over the period of the contract based on the principal amounts outstanding and the profit rate agreed with customers. Income that is 90 days or more overdue is excluded from income until received in cash.

#### *Investment Banking Fees*

These comprise fee for structuring, arranging and underwriting deals. Structuring and arranging fee income is recognised by reference to percentage of completion method, measured by reference to the percentage of cost incurred to date to estimated total cost. Underwriting and other fees are recognised when earned.

#### *Return to Sukukholders*

Return to Sukukholders is recognised in accordance with the underlying contracts.

### Offsetting

Financial assets and financial liabilities are only offset and the net amount reported in the consolidated balance sheet when there is a religious or legal right to offset the recognised amounts and there is actual expectation of the Group to settle on a net basis.

### 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 resultant gains or losses are taken to income.

Non monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Translation gains or losses on non-monetary items carried at fair value are included in equity as part of the fair value adjustment on investments available for sale.

### Significant accounting judgments and estimates

In the process of applying the Group's accounting policies, management has made the following judgements and estimates, 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, investments carried at amortised cost, investment carried at fair value through statement of income or available for sale.

For those deemed to be held to maturity management ensures that the Group has the intention and ability to hold these to maturity.

The Group classifies debt instruments as carried at amortised cost if the debt instruments are not quoted in an active market.

Investments are classified as carried at fair value through statement of income if these investments are evaluated on a fair value basis in accordance with the Bank's risk management policy and its investment strategy. These include all private equity investments.

All other investments are classified as available for sale.

31 December 2007

## 2.3 SIGNIFICANT ACCOUNTING POLICIES (continued)

### Significant accounting judgments and estimates (continued)

#### *Impairment of investments*

The Group treats available for sale investments as impaired when there has been a significant or prolonged decline in the fair value below its cost or where other objective evidence of impairment exists. The determination of what is "significant" or "prolonged" requires considerable judgment.

#### *Fair value*

The determination of fair value is done for each investment individually in accordance with the valuation policies set out below:

- (i) For investments quoted in an active market, fair value is determined by reference to quoted market prices.
- (ii) For acquisition made within one year of the reporting date, cost is assumed to be the fair value. For other 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 investment which is substantially the same, or is based on an assessment of the value of future cash flows.
- (iii) The fair value of investment property is based on external valuations.

#### **Cash and cash equivalents**

Cash and cash equivalents comprise cash and balances with a banks and Murabaha balances maturing within ninety days from the acquisition date.

#### **Zakah**

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

#### **Employees' end of service benefits**

Provision is made for employees in accordance with the amounts payable under Bahrain Labour law applicable and the employment contracts based on accumulated periods of service at the date of balance sheet. Bahraini employees are also covered under the General Organisation for Social Insurance scheme.

#### **Shari'a Supervisory Board**

The Group's business activities are subject to the supervision of a Shari'a supervisory board consisting of four members appointed by the general assembly.

#### **Earnings prohibited by Shari'a**

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

#### **Dividends**

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

Liquidity Management Centre B.S.C. (c)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

31 December 2007

**3 MURABAHA RECEIVABLES**

	<i>2007</i> <i>US\$ 000's</i>	<i>2006</i> <i>US\$ 000's</i>
International commodities Murabaha		
Banks	13,197	25,136
Non banks	-	5,186
	<u>13,197</u>	<u>30,322</u>

The Bank considers the promise made by the purchase orderer in the Murabaha contract as obligatory. The effective profit return as of 31 December 2007 ranged between 4.35% to 6% per annum (2006: 4.2% to 7.35% per annum).

**4 INVESTMENTS**

	<i>Quoted</i> <i>2007</i> <i>US\$ 000's</i>	<i>Unquoted</i> <i>2007</i> <i>US\$ 000's</i>	<i>Total</i> <i>2007</i> <i>US\$ 000's</i>
Investments carried at amortised cost	-	256,299	256,299
Investments carried at fair value through statement of income	-	5,200	5,200
Available for sale	569	8,976	9,545
Total	<u>569</u>	<u>270,475</u>	<u>271,044</u>
	<i>Quoted</i> <i>2006</i> <i>US\$ 000's</i>	<i>Unquoted</i> <i>2006</i> <i>US\$ 000's</i>	<i>Total</i> <i>2006</i> <i>US\$ 000's</i>
Investments carried at amortised cost	-	157,897	157,897
Held to maturity	14,666	-	14,666
Available for sale	532	8,103	8,635
Total	<u>15,198</u>	<u>166,000</u>	<u>181,198</u>

Investments include an amount of US\$ 208.5 million (2006: US\$ 158.35 million) representing the underlying assets of the secured Short Term Sukuk Program (STS Program) of The Short Term Sukuk Centre B.S.C. (c) managed by the Bank. The maturities of these investments range from 1 to 5 years and the effective profit rate on these investments ranged between 3.75 % to 9.5 % per annum (2006: 3.63% to 7.99% per annum).

**5 OTHER ASSETS**

	<i>2007</i> <i>US\$ 000's</i>	<i>2006</i> <i>US\$ 000's</i>
Fee income receivable	4,610	311
Accrued revenue	5,336	2,426
Prepaid expenses	90	29
Others	617	375
	<u>10,653</u>	<u>3,141</u>

31 December 2007

**6 DUE TO SUKUKHOLDERS**

Due to Sukukholders represent STS program Sukuk owned by the investors in the secured Short Term Sukuk Program (STS Program) of The Short Term Sukuk Centre B.S.C. (c) managed by the Bank. The investors are the legal owners of the underlying investments of US\$ 208.5 million (2006: 158.35 million) of the STS program as disclosed in note 4. Returns paid to the Sukukholders during the year ranged between 4.7 % to 6.25 % per annum (2006: 4.39% to 5.85% per annum).

**7 OTHER LIABILITIES**

	<i>2007</i>	<i>2006</i>
	<i>US\$ 000's</i>	<i>US\$ 000's</i>
Staff related payables	<b>1,579</b>	1,138
Others	<b>1,086</b>	2,611
	<b>2,665</b>	3,749

**8 INVESTMENT BANKING FEES**

	<i>2007</i>	<i>2006</i>
	<i>US\$ 000's</i>	<i>US\$ 000's</i>
Sukuk and Islamic Financing fees and commissions income	<b>9,009</b>	5,026
Underwriting	<b>687</b>	1,816
	<b>9,696</b>	6,842

**9 EQUITY****(i) Share capital**

	<i>2007</i>	<i>2006</i>
	<i>US\$ 000's</i>	<i>US\$ 000's</i>
Authorised		
200,000,000 ordinary shares of US\$ 1 each	<b>200,000</b>	200,000
Issued, subscribed and fully paid		
51,000,000 ordinary shares of US\$ 1 each	51,000	20,000
Increase in share capital	-	31,000
	<b>51,000</b>	51,000

**(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 a statutory reserve. The Bank 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 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.

**(iii) General reserve**

The directors have approved a transfer of 10% of the net profit of the Group for the year to general reserve in accordance with the Bank's Articles of Association. The general reserve is distributable subject to the prior approval of the CBB.

31 December 2007

**9 EQUITY (continued)****(iv) Investment fair value reserve**

Investment fair value reserve represents unrealised gains resulting from re-measurement of available-for-sale and investment carried at fair value through statement of income. This reserve is distributable upon value realisation, which takes place at the time of actual exit or derecognition.

**10 GENERAL AND ADMINISTRATIVE EXPENSES**

	<i>2007</i>	<i>2006</i>
	<i>US\$ 000's</i>	<i>US\$ 000's</i>
Directors remuneration and related expenses(10.1)	452	-
Legal and professional fees	352	41
Advertising and marketing	57	48
Others	605	354
	<u>1,466</u>	<u>443</u>

**10.1 DIRECTORS REMUNERATION AND RELATED EXPENSES**

	<i>2007</i>	<i>2006</i>
	<i>US\$ 000's</i>	<i>US\$ 000's</i>
Board of Directors remuneration accruals -2007	400	-
Board of Directors meetings related expenses	52	-
	<u>452</u>	<u>-</u>

**11 RELATED PARTY TRANSACTIONS**

The Group enters into transactions with its shareholders, members of the Shari' a supervisory Board of the Group and their related concerns in the ordinary course of business. All the financing transactions with related parties are performing and are free of provisions for possible impairment.

The balances of major transactions with related parties which mainly comprises

	<i>2007</i>	<i>2006</i>
	<i>US\$ 000's</i>	<i>US\$ 000's</i>
Cash and balances with bank	405	403
Murabaha receivables	13,197	12,611
Due to Sukukholders	73,449	100,462
Due to banks	1,988	-

The income and expenses arising from dealing with related parties comprises shareholders included in the consolidated statement of income are as follows:

	<i>2007</i>	<i>2006</i>
	<i>US\$ 000's</i>	<i>US\$ 000's</i>
Income from Murabaha receivables	450	514
Return to Sukukholders	3,609	3,599
Gain on sale of investment properties	243	-
Return to banks	129	-
Shari' a Supervisory Board	52	48

Key management personnel are those that possess significant decision making and direction setting responsibilities and includes personnel above manager level. Compensation of these key management personnel is as follows:

Short term employee benefits	1,089	706
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## Liquidity Management Centre B.S.C. (c)

### NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

31 December 2007

#### 12 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. For STS Program the Bank manages liquidity risk by entering into liquidity support agreements with other financial institutions/shareholders.

The contractual maturities of assets and liabilities have been determined on the basis of the remaining period at the date of the balance sheet to the contractual maturity date. The maturity profile of the assets and liabilities at the year end are based on contractual repayment arrangements.

The maturity profile of assets, liabilities and equity is as follows:

<b>31 December 2007</b>	<i>Up to 1 month US\$ 000's</i>	<i>1 to 3 months US\$ 000's</i>	<i>3 to 6 months US\$ 000's</i>	<i>6 months to 1 year US\$ 000's</i>	<i>1 to 3 years US\$ 000's</i>	<i>Over 3 years US\$ 000's</i>	<i>No fixed maturity US\$ 000's</i>	<i>Total US\$ 000's</i>
<b>ASSETS</b>								
Cash and balances with banks	413	-	-	-	-	-	-	413
Murabaha receivables	13,197	-	-	-	-	-	-	13,197
Investments	12,004	2,222	6,180	2,287	86,170	162,181	-	271,044
Other assets	2,356	5,521	1,928	580	65	-	203	10,653
Equipments	-	-	-	-	-	-	261	261
<b>Total assets</b>	<b>27,970</b>	<b>7,743</b>	<b>8,108</b>	<b>2,867</b>	<b>86,235</b>	<b>162,181</b>	<b>464</b>	<b>295,568</b>
<b>LIABILITIES AND EQUITY</b>								
Due to Sukukholders	188,758	4,511	-	15,312	-	-	-	208,581
Due to banks	-	-	1,988	-	-	-	-	1,988
Due to non banks	-	-	-	17,000	-	-	-	17,000
Other liabilities	482	-	-	2,178	-	-	5	2,665
Equity	-	-	-	-	-	-	65,334	65,334
<b>Total liabilities and equity</b>	<b>189,240</b>	<b>4,511</b>	<b>1,988</b>	<b>34,490</b>	<b>-</b>	<b>-</b>	<b>65,339</b>	<b>295,568</b>
<b>Liquidity gap</b>	<b>(161,270)</b>	<b>3,232</b>	<b>6,120</b>	<b>(31,623)</b>	<b>86,235</b>	<b>162,181</b>	<b>(64,875)</b>	
<b>Cumulative liquidity gap</b>	<b>(161,270)</b>	<b>(158,038)</b>	<b>(151,918)</b>	<b>(183,541)</b>	<b>(97,306)</b>	<b>64,875</b>	<b>-</b>	

The net funding requirement with regards to cumulative liquidity gap are managed through liquidity lines amounting to US\$ 125 million as at 31 December 2007 provided by the shareholders and other financial institutions(utilised US\$ 73.45 million).

Liquidity Management Centre B.S.C. (c)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

31 December 2007

**12 LIQUIDITY RISK (continued)**

31 December 2006	<i>Up to 1 month US\$ 000's</i>	<i>1 to 3 months US\$ 000's</i>	<i>3 to 6 months US\$ 000's</i>	<i>6 months to 1 year US\$ 000's</i>	<i>1 to 3 years US\$ 000's</i>	<i>Over 3 years US\$ 000's</i>	<i>No fixed maturity US\$ 000's</i>	<i>Total US\$ 000's</i>
<b>ASSETS</b>								
Cash and balances with banks	403	-	-	-	-	-	-	403
Murabaha receivables	23,009	-	5,186	2,127	-	-	-	30,322
Investments	-	532	-	696	51,473	128,497	-	181,198
Investment properties	-	-	4,906	-	-	-	-	4,906
Other assets	359	320	2,446	-	-	-	16	3,141
Equipments	-	-	-	-	-	-	141	141
<b>Total assets</b>	<b>23,771</b>	<b>852</b>	<b>12,538</b>	<b>2,823</b>	<b>51,473</b>	<b>128,497</b>	<b>157</b>	<b>220,111</b>
<b>LIABILITIES AND EQUITY</b>								
Due to Sukukholders	158,352	-	-	-	-	-	-	158,352
Other liabilities	1,054	2,146	293	-	-	256	-	3,749
Equity	-	-	-	-	-	-	58,010	58,010
<b>Total liabilities and equity</b>	<b>159,406</b>	<b>2,146</b>	<b>293</b>	<b>-</b>	<b>-</b>	<b>256</b>	<b>58,010</b>	<b>220,111</b>
Liquidity gap	(135,635)	(1,294)	12,245	2,823	51,473	128,241	(57,853)	
Cumulative liquidity gap	(135,635)	(136,929)	(124,684)	(121,861)	(70,388)	57,853	-	

The net funding requirement with regards to cumulative liquidity gap are managed through liquidity lines amounting to US\$ 95 million provided by the shareholders (fully utilised).

**13 CREDIT RISK AND CONCENTRATION OF ASSETS AND LIABILITIES**

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 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. According to the term of STS program, the Sukukholders bear the credit risk arising from investments on account of default. However, the Bank bears the risk of a rating downgrade of its holding in sukuk assets.

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 concentration of assets and liabilities is as below:

	<u>2007</u>		<u>2006</u>	
	<i>Assets</i> <i>US\$ 000's</i>	<i>Liabilities</i> <i>and equity</i> <i>US\$ 000's</i>	<i>Assets</i> <i>US\$ 000's</i>	<i>Liabilities</i> <i>and equity</i> <i>US\$ 000's</i>
<b>Geographic region:</b>				
Bahrain	99,299	166,345	88,197	69,679
Other GCC countries	196,269	129,223	131,914	150,432
	<u>295,568</u>	<u>295,568</u>	<u>220,111</u>	<u>220,111</u>
<b>Industry sector:</b>				
Banks and financial institutions	50,812	272,530	30,934	206,843
Government	19,895	-	48,053	-
Real estate	168,039	3,357	128,293	3,385
Others	56,822	19,681	12,831	9,883
	<u>295,568</u>	<u>295,568</u>	<u>220,111</u>	<u>220,111</u>

Exposures to Banks and non Banks which exceeds 15% of the Bank's capital and reserves amount to US\$ 202 million as at 31 December 2007 (2006: US\$ 147 million). CBB approval has been obtained on these exposures.

**14 PROFIT SHARE RISK**

This arises from the possibility that changes in the market profit margin will affect the value of financial instruments. The Bank monitors and adjusts its maturity structure to minimise the related risk.

As part of managing the STS Program the Bank is exposed to profit rate risk, since returns to Sukuk holders are based on a floating rate compared to return from certain investments in Sukuk at fixed rate.

**15 CURRENCY RISK**

The Group had no significant foreign currency exposures at the balance sheet date.

31 December 2007

**16 SUKUK ASSETS UNDER MANAGEMENT**

	<i>2007</i>	<i>2006</i>
	<i>US\$ 000's</i>	<i>US\$ 000's</i>
Sukuk assets under management		
Sukuk at Face Value	<b>1,181,500</b>	951,500
Sukuk Outstanding	<b>1,136,500</b>	951,500
Sukuk partially redeemed	<b>45,000</b>	-
Proprietary		
Sukuk in STSC at Face Value	<b>88,500</b>	83,500
Sukuk in STSC Outstanding	<b>84,900</b>	83,500
Sukuk partially redeemed	<b>3,600</b>	-

The Bank acts as an agent for facilitating the sourcing and securitisation of assets. The proprietary assets are included in the balance sheet of "Short Term Sukuk Centre B.S.C. (c)" (consolidated subsidiary), while client assets, which are managed in fiduciary capacity without risk or recourse to the Bank, are not included in the consolidated balance sheet.

**17 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.

**18 FAIR VALUE OF FINANCIAL INSTRUMENTS**

Fair value is the amount for which an asset could be exchanged or a liability settled between knowledgeable and willing parties in an arm's length transaction. Consequently, differences can arise between carrying values and fair value estimates.

Available for sale investments amounting to US\$ 9.5 million (2006: US\$ 8.6 million) are carried at cost due to lack of suitable methods for arriving at a reliable fair value for these investments.

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

During the year there were no earnings realised by the Group from transactions which were not permitted by Shari'a.

**20 COMMITMENTS**

The Bank has investments related commitment of US\$ 15 million (2006: Nil) as at 31 December 2007.