

# TAIB Bank B.S.C (c)

## Pillar 3 - Disclosures

31 December 2009

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## 1. Introduction

The Central Bank of Bahrain's (CBB) Basel 2 guidelines outlining the capital adequacy framework for banks incorporated in the Kingdom of Bahrain became effective from 1 January 2008. This report consists of the Basel Committee's Pillar 3 disclosure requirements in accordance with the Public Disclosures Module of the CBB's rule book. The objective of Pillar 3 is to improve market discipline through effective public disclosures.

Under the CBB's Basel II framework, all banks incorporated in Bahrain are currently required to maintain 12% minimum capital adequacy on a group wide consolidated basis. The CBB also requires banks incorporated in Bahrain to maintain a buffer of 0.5% above the minimum capital adequacy ratio. In the event that the capital adequacy ratio falls below 12.5% as applicable, additional prudential reporting requirements apply and a formal action plan setting out the measures to be taken to restore the ratio above the target level is to be formulated and submitted to the CBB. Consequently, the CBB requires the Group to maintain an effective minimum capital adequacy ratio of 12.5% on consolidated basis.

The Bank has adopted the standardized approach for Credit Risk, Market Risk and Operational Risk to determine the capital requirement.

As at 31 December 2009, the Group's total risk weighted assets amounted to US\$ 397.37 million and total regulatory capital amounted to US\$ 67.71 million. Accordingly, total Capital Adequacy Ratio on a consolidated basis for the group was 17.04%. This ratio exceeds the minimum capital requirements under the CBB's Basel II framework. The Bank intends to maintain a minimum total capital adequacy ratio of 15% on a consolidated basis.

The Bank views the Basel II Pillar 3 disclosures as an important means of increased transparency and accordingly has provided extensive disclosures in this report that is appropriate and relevant to the Bank's stakeholders and market participants.

This report should be read in conjunction with the Bank's consolidated Financial Statements including notes to the consolidated Financial Statements and Annual Report for the year ended 31 December 2009. There is a growing convergence of disclosures under International Financial Reporting Standards (IFRS) and the Basel II Pillar 3 disclosure requirements, which are in addition to or in some cases, serve to clarify the disclosure requirements of IFRS.

All figures presented in this report are in thousands of United States Dollars as at 31 December 2009 unless otherwise stated.

## 2. Pillar 3 Disclosures

### 2.1 Scope of Application

The Pillar 3 disclosures apply to TAIB Bank B.S.C (c) and its subsidiaries on a full consolidation basis in accordance with IFRS. The subsidiaries, their place of domicile and the Bank's ownership thereof are as under:

**Table 1 – Group Structure**

<b>Subsidiary</b>	<b>Domicile</b>	<b>Ownership</b>
TAIB Yatirim Bank A.S.	Turkey	100%
TAIB Yatirim A.S.*	Turkey	100%
PDF Kurusmal Finasman Danismanlik Hizmetleri A.S.*	Turkey	100%
TAIB Kazak Bank	Kazakhstan	100%
TAIB Securities W.L.L.	Kingdom of Bahrain	100%
TAIB Securities LLC **	United Arab Emirates	80%
TAIB Capital Corporation Limited	India	74%
TAIB Securities (India) Limited*	India	74%
TAIB Asset Management Company E.C.	Kingdom of Bahrain	100%
TAIB Securities Mauritius Limited	Mauritius	100%
TAIB Investments N.V.	Netherlands Antilles	100%
TAM Holdings Inc.	USA	100%
Delray Property Investments Inc.	USA	100%
SOSQ Property Investments Inc.	USA	100%
TAIB Securities Inc.	USA	100%
TAIB Securities Limited	United Kingdom	100%
TAIB (Suisse) S.A.	Switzerland	100%
TAIB Asia Limited	Hong Kong	100%
TAIB Invest Inc.	Cayman Islands	100%
TAIB GCC Blue Chip Fund	Kingdom of Bahrain	79%
TAIB Bank Qatar LLC	Qatar	100%

\* TAIB Yatirim A.S. is a 100% subsidiary of TAIB Yatirim Bank A.S and PDF Kurusmal Finasman a 100% subsidiary of TAIB Yatirim A.S

\* TAIB Securities (India) Limited is a 100% subsidiary of TAIB Capital Corporation Limited.

\*\*TAIB Securities LLC. is a 80% subsidiary of TAIB Securities W.L.L.

## 2.2 Capital Management

The Bank's policy is to maintain sufficient capital to sustain investor, creditor and market confidence and to support future development of the business. The impact of the level of capital on return on shareholders' equity is also considered while maintaining a balance between the higher return that might be possible with leveraging and security afforded by sound capital position to absorb risks. The Bank's capital management framework is intended to ensure that there is sufficient capital to support the underlying risks of the Bank's business activities and to maintain a well-capitalised status under regulatory requirements. The Bank has Internal Capital Allocation Assessment Process (ICAAP) with the supporting Risk Management Framework and Risk Management Policies and Procedures to identify and measure the various risks that are not covered under Pillar 1 risks and to regularly assess the overall capital adequacy considering the risks and the Bank's planned business strategies. The non Pillar 1 risks covered under the ICAAP process include strategic risk, reputation and legal risk, concentration risk, liquidity risk, interest rate risk in the banking book etc. The ICAAP also keeps in perspective the Bank's strategic plans and credit growth expectations and the impact of all these on maintaining adequate capital levels. The Bank ensures that the capital adequacy requirements are met on a consolidated basis and also with local regulator's requirements, if any, in countries in which the Bank's subsidiaries operate. The Bank has complied with regulatory capital requirements throughout the period.

The Bank's paid up capital consists only of ordinary shares which have proportionate voting rights. The Bank does not have any other type of capital instruments. The Bank's Tier 1 capital comprises of share capital, share premium, eligible reserves and adjusted for retained profit or losses. The eligible reserves in Tier 1 exclude gains arising on asset revaluation reserve and re-measurement to fair value of available-for-sale financial assets. Further, the following items are adjusted from Tier 1 capital as per CBB guidelines:

- Unrealized losses on available-for-sale financial assets and goodwill are deducted.
- Losses for the year 2009 pursuant to external audit are also deducted.

The Bank's Tier 2 capital comprises 45% of asset revaluation reserve and unrealised gains arising on the re-measurement to fair value of available-for-sale financial assets.

Deductions relating to exposures in excess of 15% threshold of available capital have also been made from the Tier 1 and Tier 2 capital of the Bank as required by the CBB guidelines. The Bank does not have Tier 3 capital as at 31 December 2009.

The Bank has neither any subsidiary engaged in insurance business nor investments in insurance companies.

**Table 2 – Capital Structure and Capital Adequacy**

	<b>Tier 1</b>	<b>Tier 2</b>	<b>Total</b>
Share capital	107,833	-	107,833
Share premium	3,196	-	3,196
Statutory reserve	22,428	-	22,428
General reserve	7,453	-	7,453
Retained profit brought forward	(21,416)	-	(21,416)
Minority interest in consolidated subsidiaries	1,037	-	1,037
Goodwill on acquisition	(3,730)	-	(3,730)
Current cumulative net losses	(26,076)	-	(26,076)
Unrealised gross losses arising from fair valuing equity securities	(298)	-	(298)
Asset revaluation reserve - property, plant and equipment	-	4,094	4,094
Unrealised gains arising from fair valuing equities	-	360	360
<b>Total Available Capital</b>	<b>90,427</b>	<b>4,454</b>	<b>94,881</b>
Less: Deduction relating to exposures individually in excess of 15% of available capital	(22,718)	(4,454)	(27,172)
<b>Total Eligible Capital</b>	<b>67,709</b>	<b>-</b>	<b>67,709</b>
<b>Risk weighted exposures:</b>			
- Credit risk			275,933
- Operational risk			62,176
- Market risk			59,262
<b>Total Risk weighted exposure</b>			<b>397,371</b>
<b>Consolidated Capital Adequacy Ratio (%) :</b> <b>Tier 1 &amp; Total</b>			<b>17.04</b>

The Bank does not have Tier 3 capital as at 31 December 2009.

**Table 3 – Capital Adequacy of the Bank’s significant bank subsidiaries.**

	Subsidiaries	
<i>Under Basel II</i>	<b>TAIB Kazak Bank JSE, Kazakhstan</b>	<b>TAIB Yatirim Bank A.S, Turkey</b>
Tier 1 – Capital Adequacy Ratio (%)	48.02	89.16
Total – Capital Adequacy Ratio (%)	77.70	89.16

## 2.3 Credit Risk

As a private bank, the Bank is not engaged in commercial or retail banking activities in the normal course of business except for its commercial bank licensed subsidiary in Kazakhstan, and loans for margin trading activities and portfolio investments to selected high net worth clients. However, credit risk is the predominant risk type faced by the Group in its banking, investment and treasury activities both on and off balance sheet.

The Bank has a diversified on and off balance sheet credit portfolio, which are divided into counter party exposure classes in line with the CBB’s Basel II capital adequacy framework for the standardised approach for credit risk. A high-level description of the counter party exposure classes and the risk weights used to derive the Risk Weighted Assets (“RWA”) are as follows:

### **Sovereigns**

The sovereign portfolio comprises exposures to governments and their respective central banks. The risk weights are zero per cent for exposures in the relevant domestic currency of the sovereign, or for any exposures to GCC governments. Foreign currency claims on other sovereigns are risk weighted based on their external credit ratings. Certain multilateral development banks as determined by the CBB may be included in the sovereign portfolio and treated as exposures with a zero per cent risk weighting.

### **Banks**

Claims on banks are risk weighted based on their external credit ratings. A preferential risk weight treatment is available for qualifying short-term exposures to banks in their country of incorporation. Short-term exposures are defined as exposures with an original tenor of three months or less and denominated and funded in the respective domestic currency. The preferential risk weight for short-term claims is allowed on exposures in Bahraini Dinar/US Dollar in the case of Bahraini incorporated banks.

### **Corporates**

Claims on corporates are risk weighted based on their external credit ratings. A 100% risk weight is assigned to exposures to unrated corporates. A preferential risk weight treatment is available for certain corporates owned by the Government of Bahrain, as determined by the CBB, which are assigned a zero per cent risk weight.

### **Equities Investments**

The equities portfolio comprises equity investments in the banking book, i.e. the available-for-sale financial assets portfolio. The credit (specific) risk for equities in the trading book is included in market risk RWAs for regulatory capital adequacy calculation purposes.

A 100% risk weight is assigned to listed equities and funds. Unlisted equities and funds are risk weighted at 150%. Investments in rated funds are risk weighted according to the external credit rating.

## Real Estates Investments

Holdings of real estates, owned directly or indirectly by the Bank other than own premises, are risk weighted at 200% and premises occupied by the Bank are risk weighted at 100% as per CBB guidelines.

**In addition to the standard portfolios, other exposures are risk weighted as under:**

### Past due exposures

In accordance with the Bank's policy and CBB guidelines, loans on which payment of interest or repayment of principal are 90 days past due are defined as non-performing. All past due loan exposures, irrespective of the categorisation of the exposure, are classified separately under the past due exposures asset class. A risk weighting of either 100% or 150% is applied depending on the level of specific provision maintained against the exposure.

**Other assets** are risk weighted at 100%.

### External Credit Assessment Institutions (ECAI)

The Bank uses ratings issued by Fitch to derive the risk weightings under the CBB's Basel II capital adequacy framework.

The following are gross credit risk exposures considered for Capital Adequacy Ratio calculations comprising of banking book exposures.

**Table 4 – Capital requirement for credit risk**

Basel II Asset Classification	Rated	Unrated	Total exposure (*)	Average risk weight	RWA	Capital charge
Cash Items	-	859	859	0%	-	-
Cash items in the process of collection	-	151	151	20%	30	4
Claims on sovereigns	30,145	-	30,145	0%	52	6
Claims on banks	99,333	21,647	120,980	42%	50,348	6,042
Claims on corporates	-	37,198	37,198	100%	37,198	4,464
Past due exposures	-	4,488	4,488	150%	6,732	808
Investment in equity portfolio	284	7,350	7,634	148%	11,264	1,351
Investment in funds	-	1,200	1,200	150%	1,801	216
Holding of Real Estate including premises occupied by the bank	-	82,729	82,729	188%	155,311	18,637
Others Assets	-	13,197	13,197	100%	13,197	1,584
<b>Total Credit Risk under the Standardised Approach</b>	<b>129,762</b>	<b>168,819</b>	<b>298,581</b>	<b>92%</b>	<b>275,933</b>	<b>33,112</b>

(\*) Exposure post credit risk mitigation and credit conversion.

**Table 5 – Gross credit exposure**

<b>Balance sheet Items:</b>	<b>Gross credit exposure</b>	<b>Average gross credit exposure</b>
Cash and balances with central banks	68,332	47,938
Placements with banks	92,629	112,812
Loans and advances	25,385	26,443
Available-for-sale financial assets	50,913	60,981
Investment in associate	19,451	17,166
Investment property	26,277	28,193
Property and equipment	17,870	18,242
Other assets	5,715	6,470
<b>Total on balance sheet credit exposure</b>	<b>306,572</b>	<b>318,245</b>
<b>Off balance sheet items:</b>		
Direct credit substitutes	19,400	15,855
Notes issuance and revolving underwriting facilities	240	340
Derivatives - foreign exchange contracts	479	688
<b>Total off balance sheet credit exposure</b>	<b>20,119</b>	<b>16,883</b>
<b>Total credit exposure (*)</b>	<b>326,691</b>	<b>335,128</b>

(\*) Exposure before credit risk mitigation and credit conversion.

The average gross credit exposure is calculated based on balances as at 31 December 2008, 30 June 2009 and 31 December 2009.

**Table 6 – Credit exposure by geographical segments**

Credit exposure	North America	Europe	Middle East	Rest of Asia	Total
Cash and balances with central banks	1,192	3,348	18,273	45,519	68,332
Placements with banks	10,774	16,991	62,719	2,145	92,629
Loans and advances	-	54	15,447	9,884	25,385
Available-for-sale financial assets	4,750	23,228	601	22,334	50,913
Investment in associate	-	14,232	5,219	-	19,451
Investment property	17,597	-	7,873	807	26,277
Property and equipment	255	2,380	13,591	1,644	17,870
Other assets	2,506	314	851	2,044	5,715
Off balance sheet items	-	364	13,853	5,902	20,119
<b>Total</b>	<b>37,074</b>	<b>60,911</b>	<b>138,427</b>	<b>90,279</b>	<b>326,691</b>

Exposure to Europe comprises of United Kingdom, France and Turkey

Exposure to North America comprises United States of America

Exposure to Middle East comprise of Bahrain, UAE, Saudi Arabia, Oman, Kuwait and Qatar.

Exposure to Rest of Asia comprises of China, India and the Far East.

**Table 7 – Credit exposure by sectoral segments**

	Cash, balances with central Banks and placements	Loans and advances	Investment	Others	Off-balance sheet items	Total
Financial services	160,908	6,060	230	1,614	14,224	183,036
Government	53	-	13,395	141	-	13,589
Structured finance	-	-	2,565	-	-	2,565
Trade and transport	-	8,602	-	-	5,895	14,497
Real estate	-	207	72,582	-	-	72,789
Equity funds	-	-	7,844	53	-	7,897
Others	-	10,516	25	21,777	-	32,318
<b>Total</b>	<b>160,961</b>	<b>25,385</b>	<b>96,641</b>	<b>23,585</b>	<b>20,119</b>	<b>326,691</b>

**Table 8 – Related party transaction**

	Associates	Directors and senior management	Total
<b>Income Statement :</b>			
Interest income	1,423	27	1,450
Interest expense	3,401	149	3,550
Fee & commission income	1,000	-	1,000
Reimbursement of Directors expenses	-	105	105
Key management compensation	-	948	948
<b>Balance Sheet :</b>			
Deposits from customers	80,483	23,205	103,688
Loans & Advances extended	-	626	626

The Bank carries out transactions with related parties, defined as shareholders and directors of the Bank and its subsidiaries, and businesses in which shareholders and directors, individually or combined, have control or significant influence, in the normal course of business.

**Table 9 - Discussion on lending to highly leveraged and other high risk counterparties:**

The Group does not have any exposure to highly leveraged counterparties.

**Table 10 – Credit concentration greater than 15% of individual obligor limit.**

	Amount
Bank	-
Non bank	55,636

**Table 11 – Counterparty credit risk in derivative transaction**

	<b>Notional amount</b>	<b>Credit exposure</b>	<b>Capital requirement</b>
Direct credit substitutes	19,400	19,400	2,328
Notes issuance and revolving underwriting facilities	480	240	29
Foreign exchange contracts	28,899	479	57
<b>Total</b>	<b>48,779</b>	<b>20,119</b>	<b>2,414</b>

**Table 12 – Credit exposure by maturity**

	<b>Below 1 month</b>	<b>1 to 3 months</b>	<b>3 to 12 months</b>	<b>1 to 5 years</b>	<b>Over 5 to 10 years</b>	<b>Total</b>
<b>Exposures</b>						
Cash and balances with central banks	68,332	-	-	-	-	68,332
Placements with banks	90,484	-	2,145	-	-	92,629
Loans and advances	14,125	686	3,494	7,080	-	25,385
Available-for-sale financial assets	11,653	11,500	16,444	9,347	1,969	50,913
Investment in associate	-	-	-	-	19,451	19,451
Investment property	-	-	-	18,404	7,873	26,277
Property and equipment	-	-	144	4,656	13,070	17,870
Other assets	1,772	568	2,003	805	567	5,715
Total on balance sheet	186,366	12,754	24,230	40,292	42,930	306,572
Off balance sheet	156	360	19,516	87	-	20,119
<b>Total</b>	<b>186,522</b>	<b>13,114</b>	<b>43,746</b>	<b>40,379</b>	<b>42,930</b>	<b>326,691</b>

**Table 13 – Provision for investments - sectoral segments**

	<b>Property interest held for sale - equity</b>	<b>Private equity</b>	<b>Funds</b>	<b>Total</b>
At 1 January 2009	22,014	8,892	2,500	<b>33,406</b>
Charge for the year	6,610	31	6	<b>6,647</b>
Amounts utilized		(696)		<b>(696)</b>
Exchange rate movement		19		<b>19</b>
<b>At 31 December 2009</b>	<b>28,624</b>	<b>8,246</b>	<b>2,506</b>	<b>39,376</b>

**Table 14 – Provision for investments and related exposures**

	<b>Gross exposure</b>	<b>Provisions</b>	<b>Net exposure</b>
Property interests held for sale - equity	34,686	28,622	6,064
Private equity investments	8,248	8,248	-
Funds	2,506	2,506	-
<b>Total</b>	<b>45,440</b>	<b>39,376</b>	<b>6,064</b>

During 2009, fair value loss relating to available-for-sale financial assets amounting to US\$ 1.1 million was charged directly to the income statement.

**Table 15 – Provision for investments and related exposure - geographical segments**

	<b>North America</b>	<b>Europe</b>	<b>Middle East</b>	<b>Rest of Asia</b>	<b>Total</b>
Exposure	22,587	20,998	355	1,500	<b>45,440</b>
Specific impairment provision	(22,587)	(14,934)	(355)	(1500)	<b>(39,376)</b>

The Bank does not have any significant collective impairment provision at 31 December 2009.

**Table 16 – Provision for loans and advances - sectoral segments**

	<b>Gross Exposure</b>	<b>Specific Provision</b>
Financial Services	1,536	(1,536)
Trade	7,405	(3,013)
Technology	40	(40)
Other Sectors	8,383	(8,383)
<b>Total</b>	<b>17,364</b>	<b>(12,972)</b>

No provision has been made on an impaired loans amounting to US\$ 4.3 million as the Bank holds collateral in the form of shares and cash. Impaired loans are past due over 3 years.

**Table 17 – Provisions for loans and advances - geographical segments**

	<b>North America</b>	<b>Europe</b>	<b>Middle East</b>	<b>Rest of Asia</b>	<b>Total</b>
Exposure	1,536	4,076	7,570	4,181	<b>17,364</b>
Specific impairment provision	(1,536)	(4,076)	(3,179)	(4,181)	<b>(12,972)</b>

**Table 18 – Provision movement for loans and advances - sectoral segments**

	<b>Financial Institutions</b>	<b>Corporate</b>	<b>Retail</b>	<b>Total</b>
At 1 January 2009	4,886	5,221	2,910	<b>13,017</b>
Charge for the year	-	334	3	<b>337</b>
Reversals & Other Movements	-	(379)	(3)	<b>(382)</b>
At 31 December 2009	4,886	5,176	2,910	<b>12,972</b>

## 2.4 Credit Risk Mitigation

The reduction of the capital requirement attributable to credit risk mitigation is calculated in different ways, depending on the type of credit risk mitigation, as under:

Adjusted exposure amount: The Bank uses the comprehensive method for eligible financial collateral such as cash and equities listed on a recognized stock exchange. The exposure amount and financial collateral, where applicable, are adjusted for market volatility through the use of supervisory haircuts (for currency mis-matches, price volatility and maturity-mismatches) that are specified by the CBB.

### Collateral and valuations principles

The main collaterals taken for risk mitigation on credit exposures are deposits held by customers, pledge of quoted shares, residential/commercial property mortgage, investment securities, counter-guarantees from other banks, etc. Other risk mitigants considered in one of the subsidiaries (Kazakhstan) include salary and end of service benefits assignment for personal loans, personal guarantees of promoters etc. However, for purposes of capital adequacy computation, only eligible collaterals recognized under Basel II are taken into consideration and there are no significant concentrations in such eligible collaterals taken for credit risk mitigation.

The Bank's credit policy defines the types of acceptable collateral and the applicable haircuts or loan-to-value ratio. The Bank has a system of independent valuation of collateral. In the case of real estate, valuation is done by independent valuers as stipulated in the Bank's credit policy. In respect of quoted shares and other securities, the valuation is done based on the closing price on the stock exchange. The market value of the collateral is actively monitored on a regular basis and requests are made for additional collateral in accordance with the terms of the underlying agreements. In general, lending is based on the credit worthiness and financial standing and not the collateral value. However, collateral is considered as a secondary alternative to fall back on in the event of default.

Eligible financial collateral, guarantees and credit derivatives, presented by standard portfolio are as under:

**Table 19 – Eligible financial collateral**

<b>Basel II Asset Classification</b>	<b>Gross credit exposure</b>	<b>Eligible Credit Risk Mitigant (CRM)</b>	<b>Net exposure</b>
Cash items	1,010	-	1,010
Claims on sovereigns	30,145	-	30,145
Claims on banks	142,549	(21,569)	120,980
Claims on corporates	43,739	(6,541)	37,198
Past due exposures	4,488	-	4,488
Investment in equity portfolio	7,634	-	7,634
Investment in funds	1,200	-	1,200
Holding of Real Estate including premises occupied by the Bank	82,729	-	82,729
Others Assets	13,196	-	13,196
<b>Total Credit Risk under the Standardised Approach</b>	<b>326,691</b>	<b>(28,110)</b>	<b>298,581</b>

**On and off-balance sheet netting:**

The legal documents that the Bank obtains from customers include clauses that permit the Bank to offset the customer's dues to the Bank against the Bank's dues. In case of certain counter party banks, the Bank has entered into specific netting agreements that provide for netting on and off-balance sheet exposures.

## 2.5 Market Risk

The Bank uses the Standardized Approach for assessing the capital charge for market risk to cover interest rate risk, equity risk and foreign exchange risk. Total risk weighted assets are determined by multiplying the capital charge by 12.5.

The Bank has documented policies and procedures for the management of the trading portfolio. The Group seeks to manage the market risks it faces through diversification of exposures across dissimilar markets and the establishment of hedges in related securities, wherever necessary. To manage the Group's exposures, in addition to exercising business judgment and management experience, the Group utilises limit structures, including those relating to positions, portfolios, maturities and maximum allowable stop loss and book profit limits.

The back office in the Corporate Services Division, which is independent of the front office, is responsible for valuation which is done on an ongoing basis, based on quoted market prices from stock exchanges, independent third parties or amounts derived from cash flow models as appropriate.

The Bank does not have any exposures to commodity risk.

**Table 20 – Capital requirement for components of market risk**

	RWA	Capital requirement	Minimum value	Maximum value
Interest rate position risk	194	16	16	509
Equities position risk	10,482	839	629	927
Foreign exchange risk	48,536	3,882	3,486	3,883
Total general market risk	59,212	4,737	4,131	5,319
Total specific market risk	50	4	4	69
Total	59,262	4,741	4,135	5,388

## 2.6 Operational Risk

The Bank constantly strives to minimise operational risks (inherent in the Bank's activities, processes and systems) by ensuring that a strong control infrastructure is in place throughout the organisation and enhanced where necessary. A rigid internal check system is in place by the separation of front office and back office functions, internal audit and a higher degree of automation of mid-office and back office functions.

The Bank has in place an Operational Risk Management Framework (ORMF) supported by process for Risk and Control Self-Assessment (RCSA) and Operational Procedure guidelines. The various procedures and processes used to manage operational risks are regularly reviewed and updated and implemented through effective staff training, close monitoring of risk limits, segregation of duties, appropriate controls to safeguard assets and records, regular reconciliation of accounts and transactions, and financial management and reporting. In addition, regular internal audit reviews, business continuity planning and arrangements for insurance cover are in place to complement the processes and procedures.

The Bank uses the standardized approach for calculating operational risk capital charges. In this approach, the Bank's activities are divided into eight business lines according to Basel II guidelines. The capital charge for each business line is calculated by multiplying gross income by a factor (denoted by beta) assigned to that business line. Total risk weighted assets are determined by multiplying the capital charge by 12.5.

**Table 21 – Capital requirement for Operational Risk**

	2008	2007	2006
Gross income	5,214	39,884	35,409
Capital charge	3,750	5,978	5,193
Average of capital charges for 3 years			4,974
<b>Operational Risk Weighted Exposure</b>			<b>62,174</b>

## 2.7 Equity Position in Banking Book

The Bank holds certain investments in equity securities with the objective of gaining strategic advantage as well as capital appreciation on sale thereof. All equity positions in the Banking book are classified as “Available-for-Sale”. The accounting policies for “Available-for-Sale” instruments are described in detail in the Financial Statements under “Significant Accounting Policies”.

**Table 22 – Equity position in banking book**

	<b>Gross risk-weighted exposures</b>	<b>Capital requirement</b>
Listed	373	45
Unlisted	7,261	1,306
<b>Total</b>	<b>7,634</b>	<b>1,351</b>

**Table 23 – Unrealised gains and losses**

	<b>Amount</b>	
Total unrealized gains and losses recognised on the balance sheet but not through the income statement		
Fair value reserve (net)		501
<b>Unrealised gains and losses included in Tier One and Tier Two capital</b>		
	<b>Tier 1</b>	<b>Tier 2</b>
Fair value reserve:		
Unrealized gross losses arising from fair valuing equity securities	298	
Unrealized gains arising from fair valuing equity securities		360
Asset revaluation reserve:		
Property, plant and equipment		4,094

## **2.8 Interest Rate Risk in Banking Book**

Interest Rate Risk is measured by the extent to which changes in the market interest rates impact margins, net interest income and the economic value of the Bank's equity. The Bank's asset and liability management process is utilised to manage interest rate risk through the structuring of on-balance sheet and off-balance sheet portfolios. Net interest income will be affected as a result of volatility in interest rates to the extent that the re-pricing structure of interest bearing assets differs from that of liabilities. The Bank's goal is to achieve stable earnings growth through active management of the assets and liabilities mix while, selectively positioning it to benefit from near-term changes in interest rate levels. Overall non-trading interest rate risk positions are managed by the Treasury division, which uses investment securities, placements with banks, deposits from banks and derivative instruments to manage the overall position arising from the Bank's non-trading activities. Reports on overall position and risks are submitted to senior management for review and positions are adjusted if deemed necessary. In addition, the Asset Liability Committee ("ALCO") regularly reviews the interest rate sensitivity profile and its impact on earnings. Strategic decisions are made with the objective of producing a strong and stable interest income stream over time.

Deposits without a fixed maturity are considered as repayable on demand and are accordingly included in the overnight maturity bucket.

**Table 24 – Interest rate risk in banking book**

<b>Assets</b>	<b>Less than 3 months</b>	<b>3 months to 1 year</b>	<b>Over 1 year</b>	<b>Non- Interest bearing</b>	<b>Total</b>
Cash and balances with central banks	42,169	-	-	26,056	68,225
Placements with banks	88,991	2,144	-	1,494	92,629
Financial Assets at fair value through profit or loss	-	194	-	5,241	5,435
Loans and advances	8,612	2,208	6,304	8,121	25,245
Available-for-sale financial assets	21,509	32,608	8,712	14,942	77,771
Investment in associate	-	-	-	20,205	20,205
Investment property	-	-	-	26,277	26,277
Property and equipment	-	-	-	21,360	21,360
Intangible assets	-	-	-	1,514	1,514
Goodwill	-	-	-	3,730	3,730
Other assets	-	-	-	5,715	5,715
<b>Total</b>	<b>161,281</b>	<b>37,154</b>	<b>15,016</b>	<b>134,655</b>	<b>348,106</b>
<b>Liabilities</b>					
Deposits from banks	24,000	-	-	525	24,525
Deposit from customers	111,370	21,575	1,565	59,397	193,907
Other liabilities	-	-	-	17,313	17,313
Long term debt	-	-	7,516	-	7,516
Non-controlling interests - Funds	-	-	-	791	791
<b>Total</b>	<b>135,370</b>	<b>21,575</b>	<b>9,081</b>	<b>78,026</b>	<b>244,052</b>
Interest rate sensitivity gap	25,911	15,579	5,935	-	-
Cumulative Interest rate sensitivity gap	25,911	41,490	47,425	-	-

There are no interest rate sensitive off-balance sheet exposures at 31 December 2009.

**Table 25 – Sensitivity analysis – Interest rate risk**

<b>Annualised</b>	<b>Up to 3 Months</b>	<b>3 Months to 1 Year</b>	<b>Over 1 Year</b>	<b>Total</b>
at 50 bps increase	130	78	30	238
at 100 bps increase	259	156	59	474
at 200 bps increase	518	312	119	949

**2.9 Discussion on impact of acquisition:**

No acquisition has taken place during the year 2009.

**2.10 Discussion on changes in the capital structure:**

There was no change in the capital structure of the Bank during 2009.