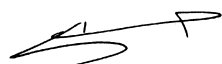


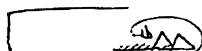
# Consolidated Balance Sheet

As of 31 December 2001

	Note	2001 BD '000	2000 BD '000
<b>Assets</b>			
Cash and balances with central banks		72,057	53,925
Treasury bills	4	37,330	17,542
Trading securities	5	-	5,383
Deposits and due from banks and other financial institutions		185,524	145,563
Loans, advances and overdrafts	6	480,790	499,448
Non-trading investment securities	7	253,568	250,142
Interest receivable and other assets	8	18,966	28,023
Kuwait Government bond	9	32,932	40,582
Investment in associated company	10	4,547	4,481
Premises and equipment		15,418	13,500
<b>Total assets</b>		<b>1,101,132</b>	<b>1,058,589</b>
<b>Liabilities, minority interest and equity</b>			
<i>Liabilities</i>			
Deposits and due to banks and other financial institutions		221,638	239,040
Borrowings under repurchase agreements		-	23,338
Medium term loans	11	84,825	75,400
Customers' current, savings and other deposits		651,687	584,491
Interest payable and other liabilities	12	15,670	19,733
<b>Total liabilities</b>		<b>973,820</b>	<b>942,002</b>
Minority interest		1,546	1,705
<i>Shareholder's equity</i>			
Share capital	13	56,906	56,906
Treasury stock	13	(1,053)	(1,026)
Statutory reserve	14	16,674	15,000
General reserve	14	20,000	20,000
Retained earnings	15	18,377	13,190
Proposed appropriations	16	14,812	10,812
Cumulative changes in fair value		50	-
<b>Total shareholder's equity</b>		<b>125,766</b>	<b>114,882</b>
<b>Total liabilities, minority interest and shareholder's equity</b>		<b>1,101,132</b>	<b>1,058,589</b>



Hassan Khalifa Al Jahalma  
Chairman



Jassem Hassan Ali Zainal  
Deputy Chairman



Murad Ali Murad  
Chief Executive

## Consolidated Statement of Income

For the year ended 31 December 2001

	Note	2001 BD '000	2000 BD '000
Interest income	17	65,832	75,397
Interest expense	18	42,093	54,600
Net interest income		23,739	20,797
Other operating income	19	13,063	10,634
<b>Net interest and other operating income</b>		<b>36,802</b>	<b>31,431</b>
Net provisions for losses on loans, advances and overdrafts	6	(1,465)	(2,563)
Net (provision) write backs for impairment in the value of non-trading investment securities and other assets and for contingencies	20	(190)	349
<b>Net operating income after provisions</b>		<b>35,147</b>	<b>29,217</b>
<b>Operating expenses</b>			
Staff costs		10,549	9,330
Other operating expenses		6,357	5,875
Depreciation		1,981	1,546
<b>Total operating expenses</b>		<b>18,887</b>	<b>16,751</b>
<b>Profit from operations</b>		<b>16,260</b>	<b>12,466</b>
Share of profit in associated company		471	540
<b>Profit before taxation and minority interest</b>		<b>16,731</b>	<b>13,006</b>
Taxation - foreign units		(153)	127
Minority interest		159	(13)
<b>Net profit for the year</b>		<b>16,737</b>	<b>13,120</b>
<b>Earnings per share (BD)</b>	34	<b>0,030</b>	<b>0,023</b>
<b>Dividend per share (BD)</b>	16	<b>0.025</b>	<b>0,018</b>

## Consolidated Statement of Changes in Shareholders' Equity

For the year ended 31 December 2001

	Share capital BD'000	Treasury stock BD'000	Statutory reserve BD'000	General reserve BD'000	Retained earnings BD'000	Proposed appropriations BD'000	Cumulative changes in fair values BD'000	Total BD'000
Balance at 31 December 1999	56,906	(822)	15,000	20,000	11,276	9,042	-	111,402
Net profit for the year - 2000	-	-	-	-	13,120	-	-	13,120
Net movement in treasury stock	-	(204)	-	-	-	-	-	(204)
Payment of dividend, directors' remuneration and donations	-	-	-	-	-	(9,042)	-	(9,042)
Proposed dividend	-	-	-	-	(10,167)	10,167	-	-
Proposed directors' remuneration	-	-	-	-	(195)	195	-	-
Proposed donations	-	-	-	-	(450)	450	-	-
Foreign exchange translation adjustment	-	-	-	-	(394)	-	-	(394)
<b>Balance at 31 December 2000</b>	<b>56,906</b>	<b>(1,026)</b>	<b>15,000</b>	<b>20,000</b>	<b>13,190</b>	<b>10,812</b>	<b>-</b>	<b>114,882</b>
Transition adjustment on adoption of IAS 39	-	-	-	-	3,860	-	-	3,860
Net profit for the year – 2001	-	-	-	-	16,737	-	-	16,737
Transfer to statutory reserve	-	-	1,674	-	(1,674)	-	-	-
Net movement in treasury stock	-	(27)	-	-	-	-	-	(27)
Portion of realised gain on sale of available for sale investments (previously included in retained earnings on adoption of IAS 39)	-	-	-	-	1,353	-	-	1,353
Payment of dividend, directors' remuneration and donation	-	-	-	-	-	(10,812)	-	(10,812)
Proposed dividend (Note 16)	-	-	-	-	(14,117)	14,117	-	-
Proposed directors' remuneration (Note 16)	-	-	-	-	(195)	195	-	-
Proposed donations (Note 16)	-	-	-	-	(500)	500	-	-
Net movement in cumulative changes in fair values of available-for-sale investment securities for the year	-	-	-	-	-	-	50	50
Foreign exchange translation adjustment	-	-	-	-	(277)	-	-	(277)
<b>Balance at 31 December 2001</b>	<b>56,906</b>	<b>(1,053)</b>	<b>16,674</b>	<b>20,000</b>	<b>18,377</b>	<b>14,812</b>	<b>50</b>	<b>125,766</b>
Month end average equity - 2001								116,136
Month end average equity - 2000								109,477

The foreign exchange translation adjustment represent the net foreign exchange translation loss arising from translating the financial statements of the Bank's foreign entities into Bahraini dinars. (Also see note 15)

## Consolidated Statement of Cash Flows

For the year ended 31 December 2001

	2001 BD '000	2000 BD '000
<b>Operating activities</b>		
Profit for the year before taxation and minority interest	16,731	13,006
Adjustment for:		
Net provisions (write backs) relating to:		
Loans, advances and overdrafts	1,465	2,563
Non trading investment securities and other assets and contingencies	190	(349)
Share of profit in associated company	(471)	(540)
Depreciation	1,981	1,546
Net translation adjustment on investments	2,781	4,402
Taxation of foreign branches	(153)	127
<b>(Increase) decrease in operating assets:</b>		
Treasury bills maturing after 91 days	12,654	42,370
Trading securities	-	1,800
Deposits and due from banks and other financial institutions	29,297	(27,166)
Loans, advances and overdrafts	10,395	3,626
Interest receivable and other assets	9,057	741
Kuwait Government bond	7,650	1,187
<b>Increase (decrease) in operating liabilities:</b>		
Deposits and due to banks and other financial institutions	(17,402)	15,401
Borrowings under repurchase agreements	(23,338)	(47,823)
Customers' current, savings and other deposits	67,196	20,701
Interest payable and other liabilities	(4,063)	1,397
<b>Net cash from operating activities</b>	<b>113,970</b>	<b>32,989</b>
<b>Investing activities</b>		
Purchase of investment securities	(204,621)	(140,815)
Maturities and redemptions of investment securities	215,668	106,474
Dividends received from associated company	405	304
Purchase of premises and equipment	(3,899)	(1,661)
<b>Net cash from (used in) investing activities</b>	<b>7,553</b>	<b>(35,698)</b>
<b>Financing activities</b>		
Medium term loans	9,425	37,700
Payment of dividend, donations and directors' remunerations	(10,812)	(9,042)
Net movement in treasury stock	(27)	(204)
<b>Net cash (used in) from financing activities</b>	<b>(1,414)</b>	<b>28,454</b>
Foreign exchange translation adjustment	(277)	(394)
<b>Increase in cash and cash equivalents</b>	<b>119,832</b>	<b>25,351</b>
Cash and cash equivalents at beginning of the year	160,355	135,004
<b>Cash and cash equivalents at end of the year</b> (Note 25)	<b>280,187</b>	<b>160,355</b>

## 1. Activities

The consolidated financial statements of Bank of Bahrain and Kuwait B.S.C. for the year ended 31 December 2001 were authorised for issue in accordance with a resolution of the directors on 27 January 2002.

Bank of Bahrain and Kuwait B.S.C., (the Bank) a public shareholding company, was incorporated in the Kingdom of Bahrain by an Amiri Decree in March 1971 and registered with the Ministry of Commerce and Industry under Commercial Registration (CR) number 1234 dated 16 March 1971. The Bank operates in Bahrain under a banking licence issued by the Bahrain Monetary Agency. The overseas units operate under the laws of their respective countries. The Bank's registered office is at 43 Government Avenue, P O Box 597, Manama, Kingdom of Bahrain. The total number of employees of the Group as of 31 December 2001 is 694 (31 December 2000: 692).

## 2. Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Bank and its subsidiaries (the 'Group') after adjustment for minority interest. All inter company transactions and balances have been eliminated on consolidation.

## 3. Significant accounting policies

### Basis of preparation

The consolidated financial statements have been prepared in conformity with the Bahrain Commercial Companies Law, the Bahrain Monetary Agency Law and in accordance with International Accounting Standards issued by the International Accounting Standards Board (IASB), and interpretations issued by the Standing Interpretations Committee of the IASB.

The significant accounting policies adopted are as follows:

### Accounting convention

The consolidated financial statements are prepared under the historical cost convention as modified by the measurement at fair value of derivatives and trading and available for sale investment securities. In addition, as more fully discussed below, assets and liabilities that are hedged are carried at fair value to the extent of the risk being hedged.

### Change in accounting policies

The Group has adopted International Accounting Standard (IAS) 39 "Financial Instruments: Recognition and Measurement" for the year ended 31 December 2001. This has resulted in significant changes in the accounting policies of the Group in respect of recognition and measurement of financial instruments. In accordance with the transitional provisions of this standard, the Group has accounted for the changes in policies with effect from 1 January 2001 and has not restated comparatives. The major changes are as follows:

### Investment securities

Previously, the Group valued all non-trading investment securities at amortised cost, less provision for impairment. The Group has reclassified such investments as either "held to maturity", "available for sale" or "originated by the Bank". Those investments classified as available for sale have been remeasured at fair value, with the resulting gain or loss being taken directly to retained earnings on 1 January 2001. Subsequent gains and losses are reported as a separate component of equity. On sale these gains or losses are recycled through the statement of income. Investments classified as "held to maturity" or "originated by the Bank" continue to be carried at amortised cost, less provision for impairment.

### **3. Significant accounting policies** *continued*

#### **Derivatives**

As at the beginning of the financial year; the Group has recognised for the first time the fair value of all derivatives in its balance sheet as either assets or liabilities at their fair values. Any gains or losses (net of adjustments to related assets or liabilities) on fair value hedges at 31 December 2000 were adjusted against the balance of retained earnings at 1 January 2001.

#### **Provision for impairment of financial assets**

The calculation of impairment for loans, advances and overdrafts and other financial assets are now based on the net present value of anticipated future cash flows discounted at original interest rates. Previously, future recoveries were not discounted. The differences arising from recalculating impairment based on the net present value of future cash flows has been taken to retained earnings at 1 January 2001.

In accordance with IAS 39, an amount is recognised as interest income on impaired loans, through the process of amortisation, based on the rate of interest that was used to discount the anticipated future cash flows relating to the impaired loans.

#### **Effect of the changes in accounting policies**

The adoption of the standard has resulted in a credit adjustment to retained earnings at 1 January 2001 of BD 3,860 thousand.

#### **Trading securities**

Trading securities are held for a short-term period and are carried at fair value with any gain or loss arising from a change in fair value being included in the consolidated statement of income in the period in which it arises.

#### **Deposits with banks and other financial institutions and other money market placements**

Deposits with banks and other financial institutions and other money market placements are stated at cost less any amounts written off and provision for impairment. The carrying values of such assets, which are being effectively hedged for changes in fair value, are adjusted to the extent of the changes in fair value being hedged. Resultant gains or losses are recognised in the consolidated statement of income.

#### **Loans, advances and overdrafts**

Loans, advances and overdrafts are stated net of any amounts written off and provision for impairment.

Projections of future cash flows relating to loans, advances and overdrafts are made on the basis of a continuing appraisal of the lending portfolio having regard to the Group's previous experience and current economic conditions. The evaluations consider identified risks and potential impairment in the Group's individual and different portfolios of loans, advances and overdrafts based on historical patterns of losses.

#### **Non-trading investment securities**

These are classified as follows:

- Held-to-maturity
- Available-for-sale
- Originated by the bank

### **3. Significant accounting policies** *continued*

#### **Loans, advances and overdrafts** *continued*

All investments are initially recognised at cost, being the fair value of the consideration given, including acquisition charges associated with the investment. These include bonds, equities, managed funds and other investments. Investments in managed funds comprise investments in mutual funds, private equity and credit structured products.

Premiums and discounts on investments are amortised on a systematic basis to maturity, using the effective interest method, and taken to interest income.

#### **Held to maturity**

Investments which have fixed or determinable payments and which are intended to be held to maturity, are carried at amortised cost, less provision for impairment in value.

#### **Available for sale**

After initial recognition, investments which are classified "available for sale" are remeasured at fair value. Unless unrealized gains and losses on remeasurement to fair value are part of an effective hedging relationship, they are reported as a separate component of equity until the investment is sold, collected or otherwise disposed of, or the investment is determined to be impaired, at which time the cumulative gain or loss previously reported in equity is included in the statement of income for the period. Any gain or loss arising from a change in fair value of available for sale investments, which are part of an effective hedging relationship, is recognised directly in the consolidated statement of income to the extent of the changes in fair value being hedged.

#### **Originated by the bank**

Investments in debt securities, which are funded directly to the issuer, are stated at amortised cost less provision for impairment. An adjustment is made to such investments where effective fair value hedges have been made to adjust the value of the investment for the fair value being hedged, with the resultant gains or losses being recognised in the consolidated statement of income.

#### **Fair values**

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

For investment where there is no quoted market price a reasonable estimate of the fair value is determined by reference to the current market value of another instrument which is substantially the same, or is based on the net present value of future cash flows.

The fair value of options is based on internal pricing models.

#### **Kuwait Government Bond**

Kuwait Government Bond is stated at cost less impairment in value, if any.

#### **Investment in associated company**

Associates are companies in which the Group has a long term investment comprising an interest of not less than 20% in the voting capital or over which it exerts significant influence, and is accounted for using the equity method.

### **3. Significant accounting policies** *continued*

#### **Premises and equipment**

All items of premises and equipment are initially recorded at cost. Depreciation is provided on a straight-line basis over the estimated useful lives of all premises and equipment, other than freehold land which is deemed to have an indefinite life and leasehold premises which are depreciated by equal annual instalments over the remaining periods of respective leases. Expected future cash flows are not discounted to their present values in determining the recoverable amount of items of premises and equipment.

#### **Collateral pending sale**

The Group occasionally acquires real estate in settlement of certain loans, advances and overdrafts. Real estate is stated at the lower of the net realizable value of the related loans, advances and overdrafts and the current fair value of such assets assessed on an individual basis. Gains or losses on disposal, and unrealised losses on revaluation, are recognised in the consolidated statement of income.

#### **Deposits**

All money market and customer deposits are carried at amortised cost, less amounts repaid. An adjustment is made to these where effective fair value hedges have been made, to adjust the value of the deposit for the fair value being hedged, with the resultant gains or losses being recognised in the consolidated statement of income.

#### **Repurchase and resale agreements**

Assets sold with a simultaneous commitment to repurchase at a specified future date (repos) continue to be recognised in the balance sheet and are measured in accordance with accounting policies for non-trading investment securities. The counterparty liability for amounts received under these agreements is shown as borrowings under repurchase agreements. The difference between sale and repurchase price is treated as interest expense using the effective interest method. Assets purchased with a corresponding commitment to resell at a specified future date (reverse repos) are not recognised in the balance sheet, as the Group does not obtain control over the assets. Amounts paid under these agreements are included in deposits with banks and other financial institutions or loans and advances to customers, as appropriate. The difference between purchase and resale price is treated as interest income using the effective interest method.

#### **Taxation**

There is no tax on corporate income in the Kingdom of Bahrain. Taxation on foreign operations is provided in accordance with the fiscal regulations of the respective countries in which the Group operates.

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

Costs relating to employees' end of service benefits are accrued in accordance with actuarial and other valuations as required by regulations applicable in each location.

#### **Provisions**

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

#### **Treasury stock**

Treasury stock is stated at cost adjusted for any gains or losses on sales. Treasury stock does not carry any voting rights or the right to dividends.

### **3. Significant accounting policies** *continued*

#### **Derivatives**

The Group enters into derivative instruments including futures, forwards, swaps, and options in the foreign exchange and capital markets. Derivatives are stated at fair value. The fair value of a derivative is the equivalent of the unrealised gain or loss from marking to market the derivative using prevailing market rates or internal pricing models. Derivatives with positive market values (unrealised gains) are included in other assets and derivatives with negative market values (unrealised losses) are included in other liabilities in the consolidated balance sheet.

For the purposes of hedge accounting, hedges are classified into two categories: (a) fair value hedges which hedge the exposure to changes in the fair value of a recognised asset or liability; and (b) cash flow hedges which hedge exposure to variability in cash flows that is either attributable to a particular risk associated with a recognised asset or liability or a forecasted transaction.

In relation to fair value hedges, which meet the conditions for hedge accounting, any gain or loss from remeasuring the hedging instrument to fair value is recognised immediately in the consolidated statement of income. The hedged item is adjusted for fair value changes relating to the risk being hedged and the difference is recognised in the consolidated statement of income.

In relation to cash flow hedges, which meet the conditions for hedge accounting, the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised initially in equity and the ineffective portion is recognised in the consolidated statement of income. The gains or losses on effective cash flow hedges recognised initially in equity are either transferred to the consolidated statement of income in the period in which the hedged transaction impacts the consolidated statement of income or included in the initial measurement of the cost of the related asset or liability.

For hedges which do not qualify for hedge accounting, any gains or losses arising from changes in the fair value of the hedging instrument are taken directly to the consolidated statement of income for the period.

Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated or exercised, or no longer qualifies for hedge accounting. At that point in time, any cumulative gain or loss on the hedging instrument recognised in equity remains in equity until the forecasted transaction occurs. Where the hedged transaction is no longer expected to occur, the net cumulative gain or loss recognised in equity is transferred to the net profit or loss for the period. In the case of fair value hedges of interest-bearing financial instruments any adjustment relating to the hedge is amortised over the remaining term to maturity.

#### **Fiduciary assets**

Assets held in trust or in a fiduciary capacity are not treated as assets of the Group and are, accordingly, not included in the consolidated financial statements.

#### **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 realize the asset and settle the liability simultaneously.

### 3. Significant accounting policies *continued*

#### Revenue recognition

Interest income and loan commitment fees are recognised on a time proportion basis, taking account of the principal outstanding and the rate applicable. An amount is recognised as interest income on impaired loans and advances and other financial assets, through the process of amortisation, based on the rate of interest that was used to discount the anticipated future cash flows relating to these impaired assets.

Other fees receivable are recognised when earned. Dividend income is recognised when the right to receive payment is established.

#### Foreign currencies

##### Translation of foreign currency transactions

Monetary assets and liabilities in foreign currencies are translated into Bahraini Dinars at rates of exchange prevailing at the balance sheet date. Any gains or losses are taken to the consolidated statement of income.

##### Translation of financial statements of foreign entities

The operations of overseas units are not deemed an integral part of the head office's operations as each is financially and operationally independent of the head office. The assets and liabilities of foreign entities are translated at rates of exchange ruling at the balance sheet date. Income and expense items are translated at average exchange rates for the period. Any exchange differences (including those on transactions which hedge such investments) are taken directly to retained earnings.

#### Cash and cash equivalents

Cash and cash equivalents comprise those balances of the following maturing within ninety-one days of the date of acquisition: cash and balances with central banks; treasury bills; deposits and due from banks and other financial institutions.

#### 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 net present value of future anticipated cash flows, recognised in the consolidated statement of income.

The provision for impairment of loans and advances also covers losses where there is objective evidence that losses may be present in components of the loans and advances portfolio at the balance sheet date. These have been estimated based on historical patterns of losses in each component, the credit ratings allotted to the borrowers and reflecting the current economic climate in which the borrowers operate.

#### Trade and settlement date accounting

All "regular way" purchases and sales of financial assets are recognised on the trade date, i.e. the date that the Bank commits to purchase the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame generally established by regulation or convention in the market place.

### 4. Treasury bills

These are short term treasury bills issued by the Governments of the Kingdom of Bahrain, the State of Kuwait and the Republic of India and are carried at amortised cost.

### 5. Trading securities

	2001 BD'000	2000 BD'000
Quoted equities	-	5,383

**6. Loans, advances and overdrafts**

a) The composition of the loans, advances and overdrafts portfolio is as follows:

**(i) Industry sector**

	<b>2001</b>	2000
	BD'000	BD'000
Trading and manufacturing	190,236	220,111
Banks and other financial institutions	73,828	93,380
Construction and real estate	91,863	82,429
Government and public sector	23,269	18,691
Consumer	136,014	125,079
Others	52,609	50,828
	<b>567,819</b>	<b>590,518</b>
Less: Provision for impairment	<b>(87,029)</b>	<b>(91,070)</b>
	<b>480,790</b>	<b>499,448</b>

**(ii) Geographical region**

	<b>2001</b>	2000
	BD'000	BD'000
Gulf Co-operation Council countries	493,997	510,669
European Community countries	14,270	10,717
Asia	57,896	62,704
Others	1,656	6,428
	<b>567,819</b>	<b>590,518</b>
Less: Provision for impairment	<b>(87,029)</b>	<b>(91,070)</b>
	<b>480,790</b>	<b>499,448</b>

b) Movements in provisions for loan losses including interest in suspense are as follows:

	<b>2001</b>	2000
	BD'000	BD'000
At 1 January	91,070	86,097
Adjustment arising from application of IAS 39	6,798	-
Charge for the year	4,750	5,537
Recoveries/write-backs	(3,285)	(2,974)
Interest suspended during the year; net	5,931	5,204
Amounts written off during the year; net	(16,740)	(2,761)
Interest recognised/amortised on impaired loans	(872)	-
Other movements	(623)	(33)
<b>Balance at 31 December</b>	<b>87,029</b>	<b>91,070</b>

Other movements include foreign exchange adjustments relating to loans, advances and overdrafts denominated in foreign currencies.

## 6. Loans, advances and overdrafts *continued*

c) As of 31 December 2001, gross loans, advances and overdrafts which were classified as impaired amounted to BD 94,983 thousand (2000: BD 99,648 thousand). The total of provisions carried and the value of securities held for these loans amounted to BD 94,658 thousand (2000: BD 99,028 thousand).

## 7. Non-Trading investment securities

	Available for sale BD '000	Held to maturity BD '000	2001 Total BD '000	2000 BD '000
Quoted equities	29,886	-	29,886	6,445
Quoted bonds	5,949	80,636	86,585	162,243
Treasury bonds	-	70,090	70,090	48,729
Managed funds	39,850	-	39,850	30,079
Other investments	3,264	23,893	27,157	2,646
	<b>78,949</b>	<b>174,619</b>	<b>253,568</b>	<b>250,142</b>

Included under available for sale investments are unquoted equity investments with a value of BD 4,169 thousand, which are carried at cost. This is due to the unpredictable nature of future cash flows and the lack of suitable alternate methods for arriving at a reliable fair value.

## 8. Interest receivable and other assets

	2001 BD'000	2000 BD'000
Interest receivable	8,344	11,874
Collateral pending sale	2,197	3,088
Accounts receivable	1,521	3,406
Murabaha receivables	-	4,696
Positive fair value of derivatives (Note 29)	1,670	490
Other	5,234	4,469
	<b>18,966</b>	<b>28,023</b>

## 9. Kuwait Government bond

The Central Bank of Kuwait purchased resident Kuwaiti customers' debts and resident debts of other Gulf Co-operation Council nationals held by the Kuwait branch of the Bank as of 1 August 1990 and related interest up to 31 December 1991 on behalf of the Government of Kuwait. The purchase value of these debts was settled by the issue of a bond with a value date of 31 December 1991. The bond matures over a maximum period of twenty years from the value date. Interest is payable semi annually in arrears at a rate specified for each six months by the Central Bank of Kuwait. During 2001, there were redemptions of bond, net of foreign exchange adjustments, amounting to BD 7,445,000 (2000: BD 1,187,000).

**9. Kuwait Government bond** *continued*

Under the terms of the purchase agreement with the Central Bank of Kuwait, the amount of the bond will be adjusted, in respect of any differences arising, once the balances of the related debts have been agreed with the customers concerned. The Bank therefore has a contingent liability in this regard. During 1999, the Central Bank of Kuwait reduced the value of the bond by BD 66,000 and accumulated interest income of BD 32,000, and the adjustment relating to this was charged to income. During 2000 and 2001, there were no such reductions in value of the bond.

The Bank is required to manage the debts purchased by the Government of Kuwait without remuneration, in conformity with the regulations and instructions of the Central Bank of Kuwait.

The Bank also has a contingent asset in the form of a claim submitted for losses suffered as a result of the Iraqi invasion and occupation of Kuwait.

**10. Investment in associated company**

	2001		2000	
	% of Interest held	BD '000	% of Interest held	BD'000
Bahrain Commercial Facilities Company B.S.C. (incorporated in the Kingdom of Bahrain)	20.25	4,547	20.25	4,481
		4,547		4,481

**11. Medium Term loans**

The medium term loans are unsecured facilities obtained for general financing purposes and comprise:

	Amount US\$'000	Rate of interest	Maturity (Year)	Carrying amount	
				2001 BD'000	2000 BD'000
	75,000	Libor + 0.50%	2001	-	28,275
	50,000	Libor + 0.55%	2003	18,850	18,850
	75,000	Libor + 0.55%	2003	28,275	28,275
	100,000	Libor + 0.50%	2004	37,700	-
	300,000			84,825	75,400

**12. Interest payable and other liabilities**

	2001 BD'000	2000 BD'000
Interest payable	4,145	9,509
Accounts payable	3,494	1,746
Accrued expenses	1,867	1,562
Taxation	2,623	2,546
Negative fair value of derivatives (Note 29)	1,017	252
Provision for contingencies (Note 20)	1,696	2,262
Other	828	1,856
	15,670	19,733

### 13. Share capital

	<b>2001</b>	2000
	BD'000	BD'000
Authorised: 1,000,000,000 shares of BD 0.100 each	100,000	100,000
Issued and fully paid: 569,062,500 shares of BD 0.100 each	56,906	56,906

#### Treasury stock

Treasury stock represents the purchase by the Bank, either directly or indirectly, of its own shares. At the end of the year, the Bank held 4,369,666 (2000: 4,251,666) of its own shares. The shares are carried at cost adjusted for any gain or loss on sale. Treasury stock does not carry the right to dividends.

### 14. Reserves

#### Statutory reserve

The statutory reserve exceeds the minimum 25% of the issued share capital required by the Bahrain Commercial Companies Law. The reserve is not distributable except in such circumstances as stipulated in the Bahrain Commercial Companies Law, and following the approval of the Bahrain Monetary Agency. Effective 1 January 2002 annual transfers at the rate of 10% of the net profit for the year of the Bank will be made until such time as the reserve equals 50% of the issued share capital of the Bank.

#### General reserve

The transfer to general reserve has been made in accordance with the provisions of the Bank's articles of association and underlines the shareholders' commitment to enhance the strong equity base of the Bank. The general reserve is a distributable reserve, subject to the approval of the Bahrain Monetary Agency.

### 15. Retained earnings

Retained earnings are stated net of accumulated foreign exchange translation adjustments of BD 2,459 thousand (2000: BD 2,182 thousand) which relate to the investment in foreign entities. The retained earnings includes a sum of BD 70 thousand (2000: BD 70 thousand) relating to statutory reserves of subsidiary companies which are non-distributable.

### 16. Proposed appropriations

	<b>2001</b>	2000
	BD'000	BD'000
Dividend	14,117	10,167
Directors' remuneration	195	195
Donations	500	450
	<b>14,812</b>	<b>10,812</b>

The directors have proposed a cash dividend of 25% being BD 0.025 per share (2000: BD 0.018 per share) to be applied to the shares in issue, net of treasury stock, as of the balance sheet date.

The above appropriations will be submitted for formal approval at the Annual General Meeting to be held on 3 March 2002. The appropriations relating to the year 2000 were approved and paid during 2001.

**17. Interest income**

	<b>2001</b>	2000
	BD'000	BD'000
Loans and advances	38,371	47,410
Treasury bills and non-trading investment securities	17,682	19,362
Placement with banks and other money market placements	8,907	8,625
Interest on impaired loans	872	-
	<b>65,832</b>	<b>75,397</b>

**18. Interest expense**

	<b>2001</b>	2000
	BD'000	BD'000
Bank borrowings	12,759	16,924
Time deposits	27,976	37,053
Savings accounts	509	521
Other	849	102
	<b>42,093</b>	<b>54,600</b>

**19. Other operating income**

	<b>2001</b>	2000
	BD'000	BD'000
Dividend income	1,922	1,667
Fees and commissions, net	8,297	7,094
(Losses) gains on managed funds	(198)	632
Net gains (losses) on trading securities	868	(498)
Gains on foreign exchange	1,704	1,442
Other income	470	297
	<b>13,063</b>	<b>10,634</b>

**20. Provision for impairment**

	<b>Available for sale</b>	<b>Held to maturity</b>	<b>Total 2001</b>	2000
	BD '000	BD '000	BD '000	BD '000
<b>Non-trading investment securities</b>				
Balance at 1 January	1,678	1,510	3,188	3,188
Charge for the year	-	190	190	-
<b>Balance at 31 December</b>	<b>1,678</b>	<b>1,700</b>	<b>3,378</b>	<b>3,188</b>

**Other assets and contingencies**

Balance at 1 January	2,262	2,611
Write back	-	(349)
Amount settled	(566)	-
<b>Balance at 31 December</b>	<b>1,696</b>	<b>2,262</b>

## 21. Related party transactions

Certain related parties (principally the associated company, directors and senior management of the Group, their families and companies of which they are principal owners) were customers of the Group in the ordinary course of business. Facilities in the personal names of the directors are fully collateralised. The transactions with these parties were made on substantially the same terms, including interest rates, as those prevailing at the same time for comparable transactions with unrelated parties and did not involve more than a normal amount of risk.

Amounts outstanding as of the balance sheet date in respect of transactions entered into with related parties were as follows:

	2001		2000	
	Related companies BD '000	Others BD '000	Related companies BD '000	Others BD '000
Loans, advances and overdrafts	5,914	760	3,948	833
Direct credit substitutes	4,800	-	4,800	-
Non-trading investments	4,401	-	4,139	-
Deposits	4,944	785	6,916	412
Contingent liabilities	4,507	-	4,507	-

The income and expenses in respect of related parties included in the consolidated financial statements are as follows:

	2001 BD'000	2000 BD'000
Interest income on loans, advances and overdrafts	62	205
Investment income	734	376
Fees and commissions	2	171
Interest expense on deposits	388	488

## 22. Liquidity Risk

Liquidity risk is the risk that an institution will be unable to meet its funding requirements. Liquidity risk can be caused by market disruptions or a credit downgrade which may cause certain sources of funding to dry up immediately. To guard against this risk, management have diversified funding sources and assets are managed with liquidity in mind, maintaining a healthy balance of cash, cash equivalents, and readily marketable securities.

**22. Liquidity risk** *continued*

The maturity profile of the assets and liabilities at 31 December 2001 is as follows:

**As of 31 December 2001:**

	Less than one month BD'000	One month to one year BD'000	Over one year BD'000	Total BD'000
<b>Assets</b>				
Cash and balances with central banks	70,332	1,725	-	72,057
Treasury bills	30,695	6,635	-	37,330
Deposits and due from banks and other financial institutions	56,593	120,328	8,603	185,524
Loans, advances and overdrafts	114,211	77,687	288,892	480,790
Non-trading investment securities	7,071	84,366	162,131	253,568
Interest receivable and other assets	14,870	381	3,715	18,966
Kuwait Government bond	-	-	32,932	32,932
Investment in associated company	-	-	4,547	4,547
Premises and equipment	-	-	15,418	15,418
<b>Total assets</b>	<b>293,772</b>	<b>291,122</b>	<b>516,238</b>	<b>1,101,132</b>
<b>Liabilities</b>				
Deposits and due to banks and other financial institutions	107,133	106,749	7,756	221,638
Medium term loans	-	-	84,825	84,825
Customers' current, savings and other deposits	280,155	356,301	15,231	651,687
Interest payable and other liabilities	11,158	739	3,773	15,670
<b>Total liabilities</b>	<b>398,446</b>	<b>463,789</b>	<b>111,585</b>	<b>973,820</b>

## 22. Liquidity risk *continued*

As of 31 December 2000:

	Less than one month BD'000	One month to one year BD'000	Over one year BD'000	Total BD'000
<b>Assets</b>				
Cash and balances with central banks	53,674	251	-	53,925
Treasury bills	4,888	12,654	-	17,542
Trading securities	5,383	-	-	5,383
Deposits and due from banks and other financial institutions	102,875	42,675	13	145,563
Loans, advances and overdrafts	61,878	134,148	303,422	499,448
Non-trading investment securities	835	92,221	157,086	250,142
Interest receivable and other assets	24,201	389	3,433	28,023
Kuwait Government bond	-	-	40,582	40,582
Investment in associated company	-	-	4,481	4,481
Premises and equipment	-	-	13,500	13,500
<b>Total assets</b>	<b>253,734</b>	<b>282,338</b>	<b>522,517</b>	<b>1,058,589</b>
<b>Liabilities</b>				
Deposits and due to banks and other financial institutions	145,723	86,660	6,657	239,040
Borrowings under repurchase agreements	23,338	-	-	23,338
Medium term loans	-	28,275	47,125	75,400
Customers' current, savings and other deposits	367,596	199,907	16,988	584,491
Interest payable and other liabilities	15,697	807	3,229	19,733
<b>Total liabilities</b>	<b>552,354</b>	<b>315,649</b>	<b>73,999</b>	<b>942,002</b>

The above reflects the contractual maturities of assets and liabilities that have been determined on the basis of the remaining period at the balance sheet date to the contractual maturity date and does not take account of the effective maturities as indicated by the Bank's deposit retention history and the availability of liquid funds.

**23. Concentration of assets, liabilities and off balance sheet items**

The distribution of assets, liabilities and off-balance sheet items by geographic region and industry sector was as follows:

	2001			2000		
	Assets BD '000	Liabilities BD '000	Off balance sheet items BD '000	Assets BD '000	Liabilities BD '000	Off balance sheet items BD '000
<b>Geographical region:</b>						
Gulf Co-operation Council countries	838,670	900,707	198,087	782,529	857,554	191,505
North America	47,535	2,831	37,590	67,518	21,175	26,771
European Community countries	95,860	33,347	44,934	77,611	30,203	82,939
Asia	92,070	32,863	44,944	97,395	28,923	49,519
Others	26,997	4,072	1,679	33,536	4,147	3,189
	<b>1,101,132</b>	<b>973,820</b>	<b>327,234</b>	<b>1,058,589</b>	<b>942,002</b>	<b>353,923</b>
<b>Industry sector:</b>						
Trading and manufacturing	193,855	50,332	40,143	199,510	51,810	51,010
Banks and other financial institutions	336,576	227,021	228,899	336,856	339,283	235,662
Construction and real estate	77,509	8,706	32,445	79,379	3,682	27,785
Government and public sector	241,187	173,600	2,419	225,141	144,000	-
Consumer	87,968	116,575	-	90,263	89,852	-
Others	164,037	397,586	23,328	127,440	313,375	39,466
	<b>1,101,132</b>	<b>973,820</b>	<b>327,234</b>	<b>1,058,589</b>	<b>942,002</b>	<b>353,923</b>
<b>Month end average</b>	<b>1,117,913</b>	<b>1,001,777</b>	<b>340,618</b>	<b>1,078,017</b>	<b>968,540</b>	<b>414,673</b>

**24. Segmental information****Primary segment information**

For management purposes the Group is organised into four major business segments:

- Retail banking - Principally handling individual customer deposits and providing consumer finance type loans, overdrafts, credit facilities and funds transfer facilities, card businesses, foreign exchange and cash collateralised lending.
- Corporate banking - Principally handling loans and other credit facilities, deposit and current accounts for corporate and institutional customers in Bahrain.
- International banking - Principally handling loans and other credit facilities, deposit and current accounts for international corporate and institutional customers. This also covers the operations of the overseas units.
- Investment and - Principally providing money market, trading and treasury services as well as the management of the Group's funding operations. Investment activities involve handling investments in local and international markets, investment advisory services and funds management.

These segments are the basis on which the Group reports its primary segment information.

#### 24. Segmental information *continued*

Segment information for the year ended 31 December 2001 was as follows:

	Retail banking BD'000	Corporate banking BD'000	International banking BD'000	Investment & other activities BD'000	Total BD'000
Operating income before provisions	9,232	6,377	10,508	10,685	36,802
Segment result	2,683	4,350	6,113	5,558	18,704
Common costs					(942)
Income from associate					471
Minority interest					159
Net provisions					(1,655)
<b>Net profit</b>					<b>16,737</b>
Segment assets	82,317	203,121	432,157	365,652	1,083,247
Common assets					17,885
<b>Total assets</b>					<b>1,101,132</b>
Segment liabilities	218,763	254,952	351,129	145,246	970,090
Common liabilities					3,730
<b>Total liabilities</b>					<b>973,820</b>

Segment information for the year ended 31 December 2000 was as follows:

	Retail banking BD'000	Corporate banking BD'000	International banking BD'000	Investment & other activities BD'000	Total BD'000
Operating income before provisions	8,530	6,235	8,029	8,637	31,431
Segment result	3,092	4,408	3,924	4,320	15,744
Common costs					(937)
Income from associate					540
Minority interest					(13)
Net provisions					(2,214)
<b>Net profit</b>					<b>13,120</b>
Segment assets	76,242	207,926	449,881	306,816	1,040,865
Common assets					17,724
<b>Total assets</b>					<b>1,058,589</b>
Segment liabilities	197,520	221,771	321,293	199,606	940,190
Common liabilities					1,812
<b>Total liabilities</b>					<b>942,002</b>

**24. Segmental information** *continued***Secondary segment information**

Although the management of the Group is based primarily on business segments, the Group operates in two geographic markets; Middle East, which is designated as Regional, and North America, European Community countries, Asia and others, which are designated as International. The geographical analysis of operating income, segment results, total assets and total liabilities, is based primarily upon the domicile of the customer or the investment.

Geographical areas:	Regional		International		Total	
	2001 BD '000	2000 BD '000	2001 BD '000	2000 BD '000	2001 BD '000	2000 BD '000
Operating income before provisions	25,081	18,703	11,721	12,728	36,802	31,431
Segment results	12,016	7,214	6,688	8,530	18,704	15,744
Common costs					(942)	(937)
Income from associate					471	540
Minority interest					159	(13)
Net provisions					(1,655)	(2,214)
<b>Net profit</b>					<b>16,737</b>	<b>13,120</b>
Total assets	838,670	782,529	262,462	276,060	1,101,132	1,058,589
<b>Total liabilities</b>	<b>900,707</b>	<b>857,554</b>	<b>73,113</b>	<b>84,448</b>	<b>973,820</b>	<b>942,002</b>
Capital expenditure	3,813	1,563	86	98	3,899	1,661

**25. Cash and cash equivalents**

Cash and cash equivalents included in the statement of cash flows include the following balance sheet amounts:

	2001 BD'000	2000 BD'000	Change in the year BD'000
Cash and balances with central banks	72,057	53,925	18,132
Treasury bills maturing within ninety-one days	37,330	4,888	32,442
Deposits and due from banks and other financial institutions maturing within ninety-one days	170,800	101,542	69,258
<b>Cash and cash equivalents</b>	<b>280,187</b>	<b>160,355</b>	<b>119,832</b>

**26. Contingent liabilities and commitments****Credit-related commitments**

Credit-related commitments instruments include commitments to extend credit, standby letters of credit, guarantees and acceptances which are designed to meet the requirements of the Group's customers.

Commitments to extend credit represents contractual commitments to make loans and revolving credits. Commitments generally have fixed expiration dates or other termination clauses and normally require a payment of fees. Since commitments may expire without being drawn upon, the total contracted amounts do not necessarily represent future cash requirements.

## 26. Contingent liabilities and commitments *continued*

### Credit-related commitments *continued*

Standby letters of credit, guarantees and acceptances ("standbys") 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. Standby letters of credit, which are included under guarantees, would have market risk if issued or extended at a fixed rate of interest. However, these contracts are primarily made at a floating rate.

The Group has exposure, in the normal course of business, to the following contingent liabilities and commitments:

	2001 BD'000	2000 BD'000
<b>Commitments on behalf of customers:</b>		
Letters of credit	23,026	22,059
Guarantees	116,469	86,394
Acceptances	6,046	8,047
	<b>145,541</b>	<b>116,500</b>
<b>Irrevocable commitments</b>		
Undrawn loan commitments	11,701	19,106
Capital commitments	434	1,595
Commitments in respect of investments	7,893	8,040
	<b>20,028</b>	<b>28,741</b>
	<b>165,569</b>	<b>145,241</b>

In the normal course of its banking activities the Bank has irrevocably guaranteed to the holders of units in Global Futures Plus Fund, on final redemption date, the return of either the principal amount of US\$ 1,000 per unit, or the net asset value per unit, whichever is higher. As of 31 December 2001, the net asset value per unit amounted to US\$ 1,161.15 (31 December 2000: Net asset value per unit US\$ 1,095.82).

## 27. Credit risk and concentration of 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 master netting agreements and collateral arrangements with counterparties in appropriate circumstances, and limiting the duration of exposure. In certain cases, the Group may close out transactions or assign them to other counterparties to mitigate credit risk.

Concentrations of credit risk arise when a number of counterparties are engaged in similar business activities, or activities in the same geographical 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 geographical location.

**27. Credit risk and concentration of credit risk** *continued*

All policies relating to credit are reviewed and approved by the Board of Directors. An Executive Committee, consisting of six senior members of the Board of Directors, reviews and approves all larger credits. In addition, all larger credits in excess of approval authority of the Executive Committee are approved by the Board of Directors.

Credit limits are established for all customers after a careful assessment of their creditworthiness. The limits for domestic and international borrowers are approved by a three member committee. These limits, depending upon the level of authority required, are approved by the Executive Committee and the Board of Directors respectively and they are subject to the Bahrain Monetary Agency's large exposure limit criteria. Standard procedures, outlined in the Bank's Credit Procedures Manual, require that all credit proposals be subjected to a detailed screening by a designated credit officer.

The Group seeks to manage its credit risk exposure through diversification of lending activities to avoid undue concentrations of risks with individuals or groups of customers in specific locations or businesses. It also obtains security when appropriate.

Details of the composition of the loans, advances and overdrafts portfolio are set out in note 6 to the consolidated financial statements.

Details of the industry sector analysis and the geographical distribution of assets, liabilities and off balance sheet items are set out in note 23 to the consolidated financial statements.

## 28. Interest rate risk management

Interest rate risk arises from the possibility that changes in interest rates will affect the value of financial instruments. The Group is exposed to interest rate risk as a result of mismatches or gaps in the amounts of assets and liabilities and off balance sheet instruments that mature or reprice in a given period. The Group manages this risk by reviewing the repricing of assets and liabilities on a continuous basis.

The Group's interest rate sensitivity position, based on the earlier of contractual repricing or maturity dates, is as follows:

As of 31 December 2001:

	Less than one month BD'000	One month to one year BD'000	Over one year BD'000	Not exposed to interest rate risk BD'000	Total BD'000
Cash and balances with central Banks	48,113	-	-	23,944	72,057
Treasury bills	30,695	6,635	-	-	37,330
Deposits and due from banks and other financial institutions	45,849	128,920	-	10,755	185,524
Loans, advances and overdrafts	194,145	177,435	101,725	7,485	480,790
Non-trading investment securities	5,563	79,880	166,120	2,005	253,568
Interest receivable and other assets	-	-	-	18,966	18,966
Kuwait Government bond	-	32,932	-	-	32,932
Investment in associated company	-	-	-	4,547	4,547
Premises and equipment	-	-	-	15,418	15,418
<b>Total assets</b>	<b>324,365</b>	<b>425,802</b>	<b>267,845</b>	<b>83,120</b>	<b>1,101,132</b>
Deposits and due to banks and other financial institutions	79,833	106,749	7,756	27,300	221,638
Medium term loans	-	84,825	-	-	84,825
Customers' current, savings and other deposits	211,018	364,184	6,390	70,095	651,687
Interest payable and other liabilities	-	-	-	15,670	15,670
Minority interest	-	-	-	1,546	1,546
Equity	-	-	-	125,766	125,766
<b>Total liabilities, minority interest and equity</b>	<b>290,851</b>	<b>555,758</b>	<b>14,146</b>	<b>240,377</b>	<b>1,101,132</b>
On-balance sheet gap (a)	33,514	(129,956)	253,699		
Off-balance sheet gap (b)		622	(622)		
<b>Total interest rate sensitivity gap</b>	<b>33,514</b>	<b>(129,334)</b>	<b>253,077</b>		
<b>Cumulative interest rate sensitivity gap</b>	<b>33,514</b>	<b>(95,820)</b>	<b>157,257</b>		

**28. Interest rate risk management continued**

As of 31 December 2000:

	Less than one month BD'000	One month to one year BD'000	Over one year BD'000	Not exposed to interest rate risk BD'000	Total BD'000
Cash and balances with central banks	34,606	-	-	19,319	53,925
Treasury bills	4,888	12,654	-	-	17,542
Trading securities	25	-	-	5,358	5,383
Deposits and due from banks and other financial institutions	77,700	38,184	13	29,666	145,563
Loans, advances and overdrafts	234,128	172,313	81,333	11,674	499,448
Non-trading investment securities	7,721	117,427	124,194	800	250,142
Interest receivable and other assets	-	-	-	28,023	28,023
Kuwait Government bond	-	40,582	-	-	40,582
Investment in associated company	-	-	-	4,481	4,481
Premises and equipment	-	-	-	13,500	13,500
<b>Total assets</b>	<b>359,068</b>	<b>381,160</b>	<b>205,540</b>	<b>112,821</b>	<b>1,058,589</b>
Deposits and due to banks and other financial institutions	125,342	82,122	6,657	24,919	239,040
Borrowings under repurchase agreements	23,338	-	-	-	23,338
Medium term loans	28,275	47,125	-	-	75,400
Customers' current, savings and other deposits	328,980	199,908	16,988	38,615	584,491
Interest payable and other liabilities	-	-	-	19,733	19,733
Minority interest	-	-	-	1,705	1,705
Equity	-	-	-	114,882	114,882
<b>Total liabilities, minority interest and equity</b>	<b>505,935</b>	<b>329,155</b>	<b>23,645</b>	<b>199,854</b>	<b>1,058,589</b>
On-balance sheet gap (a)	(146,867)	52,005	181,895		
Off-balance sheet gap (b)	12,064	(16,672)	4,608		
<b>Total interest rate sensitivity gap</b>	<b>(134,803)</b>	<b>35,333</b>	<b>186,503</b>		
<b>Cumulative interest rate sensitivity gap</b>	<b>(134,803)</b>	<b>(99,470)</b>	<b>87,033</b>		

(a) The on-balance sheet gap represents the net amounts of on-balance sheet items.

(b) The off-balance sheet gap represents the net notional amounts of off balance sheet financial instruments such as interest rate swaps, which are used to managed interest rate risk.

## 28. Interest rate risk management *continued*

The effective interest rate (effective yield) of a monetary financial instrument is the rate that, when used in a present value calculation, results in the carrying amount of the instrument. The rate is a historical rate for a fixed rate instrument carried at amortised cost and a current market rate for a floating rate instrument or an instrument carried at fair value. The effective interest rates by major currencies for each of the monetary financial instruments are as follows:

	2001 Effective interest rate %			2000 Effective interest rate %		
	BD	KD	US\$	BD	KD	US\$
<b>Assets</b>						
Treasury bills	4.7	4.7	-	6.3	6.4	-
Deposits and due from banks and financial institutions	4.5	5.8	3.8	6.6	6.8	6.5
Loans, advances and overdrafts (c)	8.8	6.7	5.7	10.6	8.1	7.5
Non-trading investment securities	-	-	6.4	-	-	6.9
Kuwait Government bond	-	3.8	-	-	5.5	-
<b>Liabilities</b>						
Deposits and due to banks and other financial institutions	4.1	4.8	4.6	6.4	6.5	6.4
Borrowings under repurchase agreements	-	-	-	-	-	6.4
Medium term loans	-	-	4.9	-	-	7.1
Customers' current, savings and other deposits (d)	3.5	4.4	4.5	5.1	6.5	6.5

(c) The effective interest rate for loans, advances and overdrafts has been computed by excluding non performing loans.

(d) The effective interest rates have been computed by excluding non-interest bearing accounts which form a small proportion of such deposits.

**29. Derivatives**

In the ordinary course of business the Group enters into various types of transactions that involve derivative financial instruments. A derivative financial instrument is a financial contract between two parties where payments are dependent upon movements in price in one or more underlying financial instrument, reference rate or index. Derivative financial instruments include forwards, futures, swaps and options.

The table below shows the positive and negative fair values of derivative financial instruments, which are equivalent to the market values, together with the notional amounts analysed by the term to maturity. The notional amount is the amount of a derivative's underlying asset, reference rate or index and is the basis upon which changes in the value of derivatives are measured. The notional amounts indicate the volume of transactions outstanding at year end and are neither indicative of the market risk nor credit risk.

31 December 2001:	Positive fair value BD '000	Negative fair value BD '000	Notional Amount Total BD '000	Notional amounts by term to maturity		
				Within 3 months BD '000	3 - 12 months BD '000	1 - 5 years BD '000
<b>Derivatives held for trading:</b>						
Interest rate swaps	-	4	15,080	7,540	-	7,540
Forward foreign exchange contracts	866	879	33,555	8,897	5,834	18,824
Options	144	-	9,757	1,762	7,995	-
<b>Derivatives held as fair value hedges:</b>						
Interest rate swaps	3	3	10,688	-	10,688	-
Forward foreign exchange contracts	657	131	92,585	88,156	4,429	-
	<b>1,670</b>	<b>1,017</b>	<b>161,665</b>	<b>106,355</b>	<b>28,946</b>	<b>26,364</b>
<b>31 December 2000:</b>						
	Positive fair value BD '000	Negative fair value BD '000	Notional Amount Total BD '000	Notional amounts by term to maturity		
				Within 3 months BD '000	3 - 12 months BD '000	1 - 5 years BD '000
<b>Derivatives held for trading:</b>						
Interest rate swaps	-	-	35,815	-	28,275	7,540
Forward foreign exchange contracts	490	252	28,247	26,699	1,548	-
Options	-	-	6,524	4,639	1,885	-
Forward interest rate agreements	-	-	33,930	7,540	26,930	-
<b>Derivatives held for hedging purposes:*</b>						
Interest rate swaps	-	-	21,082	-	16,049	5,033
Forward foreign exchange contracts	-	-	76,674	76,674	-	-
Forward interest rate agreements	-	-	6,409	-	6,409	-
	<b>490</b>	<b>252</b>	<b>208,681</b>	<b>115,552</b>	<b>80,556</b>	<b>12,573</b>

\* Fair values for derivatives held for hedging purposes at 31 December 2000 have not been given as they and the related financial asset or liability was not fair value accounted.

## **29. Derivatives** *continued*

### **Derivative product types**

Forwards and futures are contractual agreements to either buy or sell a specified currency, commodity or financial instrument at a specific price and date in the future. Forwards are customised contracts transacted in the over-the-counter market. Foreign currency and interest rate futures are transacted in standardised amounts on regulated exchanges and are subject to daily cash margin requirements. Forward rate agreements are effectively tailor-made interest rate futures which fix a forward rate of interest on a notional loan, for an agreed period of time starting on a specified future date.

Swaps are contractual agreements between two parties to exchange interest or foreign currency differentials based on a specific notional amount. For interest rate swaps, counterparties generally exchange fixed and floating rate interest payments based on a notional value in a single currency. For currency swaps, fixed or floating interest payments and notional amounts are exchanged in different currencies.

Options are contractual agreements that convey the right, but not the obligation, to either buy or sell a specific amount of a commodity or financial instrument at a fixed price, either at a fixed future date or at any time within a specified period. The Group does not engage in the writing of options.

### **Derivative related credit risk**

Credit risk in respect of derivative financial instruments arises from the potential for a counterparty to default on its contractual obligations and is limited to the positive fair value of instruments that are favourable to the Group. All of the Group's derivative contracts are entered into with other financial institutions.

### **Derivatives held or issued for trading purposes**

Most of the Group's derivative trading activities relate to positioning and arbitrage. Positioning involves managing positions with the expectation of profiting from favourable movements in prices, rates or indices. Arbitrage involves identifying and profiting from price differentials between markets or products.

### **Derivatives held or issued for hedging purposes**

The Group has adopted a comprehensive system for the measurement and management of risk. Part of the risk management process involves managing the Group's exposure to fluctuations in foreign exchange rates (currency risk) and interest rates through asset and liability management activities. It is the Group's policy to reduce its exposure to currency and interest rate risks to acceptable levels as determined by the Board of Directors. The Board has established levels of currency risk by setting limits on counterparty and currency position exposures. Positions are monitored on a daily basis and hedging strategies used to ensure positions are maintained within established limits. The Board has established levels of interest rate risk by setting limits on the interest rate gaps for stipulated periods. Assets and liabilities interest rate gaps are reviewed on a weekly basis and hedging strategies used to reduce the interest rate gaps to within the limits established by the Board.

As part of its asset and liability management the Group uses derivatives for hedging purposes in order to reduce its own exposure to currency and interest rate risks. This is achieved by hedging specific financial instruments, forecasted transactions as well as strategic hedging against overall balance sheet exposures.

The Group uses forward foreign exchange contracts and currency swaps to hedge against specifically identified currency risks. In addition, the Group uses interest rate swaps and interest rate futures to hedge against the interest rate risk arising from specifically identified fixed interest rate loans. The Group also uses interest rate swaps to hedge against the cash flow risks arising on certain floating rate loans. In all such cases the hedging relationship and objective, including details of the hedged item and hedging instrument, are formally documented and the transactions are accounted for as fair value hedges.

**29. Derivatives *continued***

Interest rate risk is managed by monitoring the repricing of assets and liabilities and entering into interest rate swaps and futures to hedge a proportion of the interest rate exposure. Since strategic hedging does not qualify for special hedge accounting related derivatives are accounted for as trading instruments.

**30. Currency risk**

The functional currency of the Group is the Bahraini dinar.

The Group had the following significant net exposures denominated in foreign currencies as of the balance sheet date:

	2001 BD '000	2000 BD '000
	equivalent long (short)	equivalent long (short)
US Dollar	39,140	2,738
Japanese Yen	(19)	123
Pound Sterling	(50)	(90)
Kuwaiti Dinar	49	45
Omani Riyal	79	32
Saudi Riyal	(531)	(114)
Others	342	133

**31. Funds under management**

At 31 December 2001, clients' funds managed in a fiduciary capacity, without risk or recourse to the Bank, amounted to BD 12,448 thousand (31 December 2000: BD 3,182 thousand).

**32. Subsidiaries**

The subsidiaries of the Bank, all of which have 31 December as their financial year end, are as follows:

	Ownership	Country of incorporation	Activity
BBK Financial Services W.L.L.	100%	Bahrain	Brokerage
Al Khaleej Islamic Investment Bank E.C.	65%	Bahrain	Islamic banking
CrediMax B.S.C. (c)	100%	Bahrain	Credit card operations

### 33. Fair value of financial instruments

The table below sets out the estimated carrying values and fair values of those on- and off balance sheet financial instruments where fair values are materially different from carrying amounts in the consolidated financial statements:

	31 December 2001			31 December 2000		
	Carrying value BD '000	Fair value BD '000	Difference BD '000	Carrying value BD '000	Fair value BD '000	Difference BD '000
<b>Financial assets</b>						
Non-trading investments securities	253,568	255,387	1,819	250,142	253,241	3,099

As explained in note 7, included under non-trading investments are unquoted equity investments with a value of BD 4,169 thousand for which fair value cannot be reliably determined.

- a) Loans, advances and overdrafts : Due to time and cost constraints and the lack of a secondary market, it is not practicable to determine the fair value of loans, advances and overdrafts to customers with sufficient reliability.
- b) Kuwait Government bond : It is not practicable to determine the fair value of Kuwait Government bond with sufficient accuracy, as the future cash flows are not determinable.

### 34. Earnings per share

Earnings per share at the year end is calculated by dividing the net profit for the year by the weighted average number of shares outstanding during the year as follows:

	<b>2001</b>	2000
Net profit for the year (BD '000)	<b>16,737</b>	13,120
Weighted average number of shares, net of treasury stock, outstanding during the year	<b>564,721,541</b>	564,993,233
Earnings per share (BD)	<b>0.030</b>	0.023

No figure for diluted earnings per share has been presented as the Bank has not issued any instruments which would have an impact on earnings per share when exercised.

**35. Capital adequacy**

The risk asset ratio calculated in accordance with the capital adequacy guidelines established for the global banking industry is as follows:

	<b>2001</b>	2000
	BD '000	BD '000
<b>Capital base:</b>		
Tier 1 - Equity	125,567	114,882
- Minority interest	1,546	1,705
Tier 2 - General provision (limited to 1.25% of risk weighted assets)	1,925	1,636
Tier 3	-	-
<b>Total capital base (a)</b>	<b>129,038</b>	<b>118,223</b>
<b>Credit risk weighted exposure:</b>		
On-balance sheet	597,618	594,222
Off-balance sheet	110,242	85,488
<b>Total</b>	<b>707,860</b>	<b>679,710</b>
<b>Market risk weighted exposure:</b>		
On-balance sheet	-	-
Off-balance sheet	6,750	4,405
<b>Total</b>	<b>6,750</b>	<b>4,405</b>
<b>Total risk weighted exposure (b)</b>	<b>714,610</b>	<b>684,115</b>
<b>Capital adequacy (a/b * 100)</b>	<b>18.05%</b>	<b>17.28%</b>
<b>Minimum requirement</b>	<b>12%</b>	<b>12%</b>

## Income Statement Summary

	2001	2000	Variance	Change
	BD millions	BD millions	BD millions	Per cent
Net interest income	23.7	20.8	2.9	13.9
Other income	13.6	11.2	2.4	21.4
Total operating income	37.3	32.0	5.3	16.6
Operating expenses	18.9	16.8	2.3	13.2
Taxation and minority interest	0.0	(0.1)	0.1	N/A
Net profit before provisions	18.3	15.3	3.0	19.5
Net provisions	1.7	2.2	(0.5)	(23.8)
<b>Net profit for the year</b>	<b>16.7</b>	<b>13.1</b>	<b>3.5</b>	<b>27.2</b>

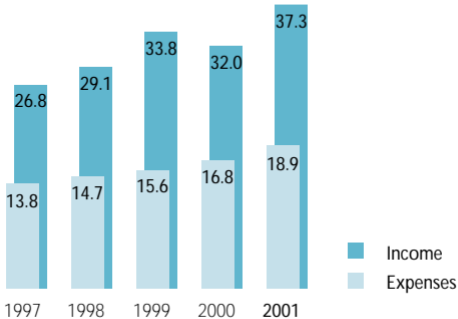
## Other Income

BD millions



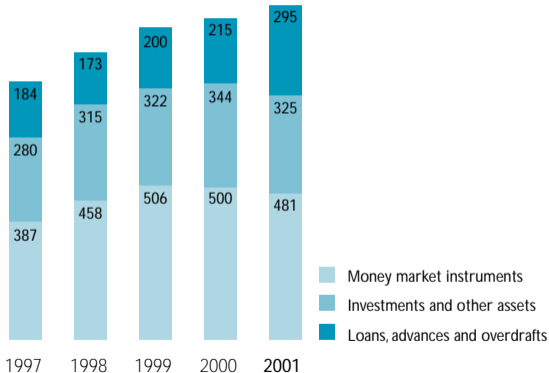
## Income and Expenses

BD millions



## Total Assets

BD millions



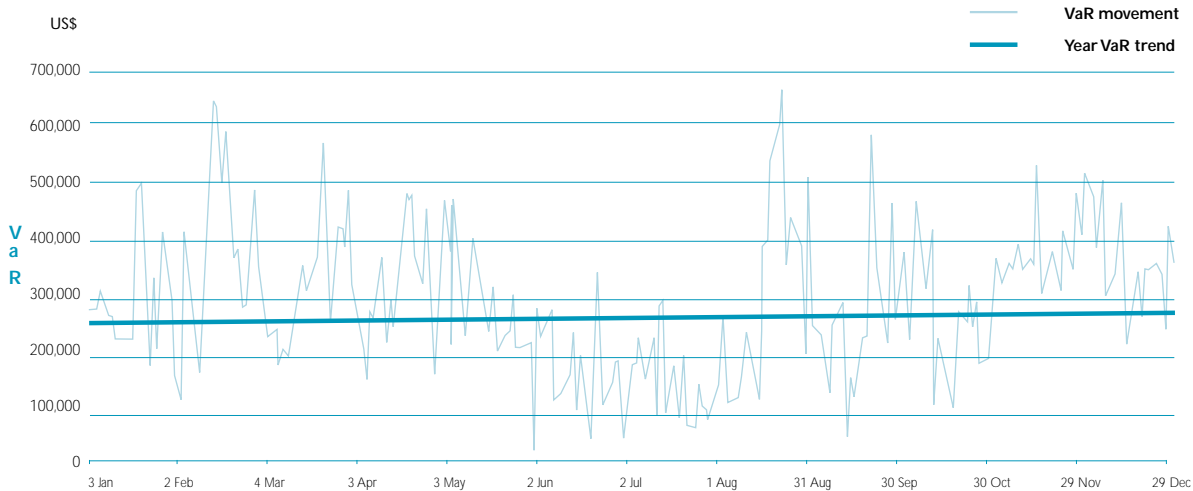
## Balance Sheet Summary

	2001	2000	Variance	Change
	BD millions	BD millions	BD millions	Per cent
Cash and balances at central banks	72.1	55.3	16.8	30.4
Treasury bills	37.3	17.5	19.8	112.6
Deposits and due from banks	185.5	144.2	41.3	28.6
Loans, advances and overdrafts	480.8	499.4	(18.6)	(3.7)
Investments	258.1	260.0	(1.9)	(0.7)
Kuwait Government debt bonds	32.9	40.6	(7.7)	(19.0)
Other assets	34.4	41.6	(7.2)	(17.3)
<b>Total assets</b>	<b>1,101.1</b>	<b>1,058.6</b>	<b>42.5</b>	<b>4.0</b>
Deposits and due to banks	221.6	239.0	(17.4)	(7.3)
Medium term loans	84.8	75.4	9.4	12.5
Borrowings under repurchase agreements	0.0	23.3	(23.3)	(100.0)
Customer deposits	651.7	584.5	67.2	11.5
Other liabilities	15.7	19.8	(4.1)	(20.7)
<b>Total liabilities</b>	<b>973.8</b>	<b>942.0</b>	<b>31.8</b>	<b>3.4</b>
Minority interest	1.5	1.7	(0.2)	(12.1)
Shareholders' equity	125.8	114.9	10.9	9.5
<b>Total liabilities, minority interest and shareholders' equity</b>	<b>1,101.1</b>	<b>1,058.6</b>	<b>42.5</b>	<b>4.0</b>

**Selected Key Ratios (per cent)**

	2001	2000
<b>Profitability</b>		
Return on average assets	1.50	1.22
Return on average equity	13.9	11.6
Operating expenses/total income	50.7	52.4
<b>Liquidity</b>		
Loans and advances/total assets	43.7	47.2
Investments/total assets	26.4	28.4
Liquid assets/total assets	31.6	29.9
<b>Capital Adequacy</b>		
Total qualifying capital/risk weighted assets	18.1	17.3
Non inter-bank deposits/loans and investments	95.4	85.4
Shareholders' equity/total assets	11.4	10.8

## Consolidated VaR for Bahrain (Head Office ) and Kuwait (Branch)



## Back testing for quarter ended 31 December, 2001

