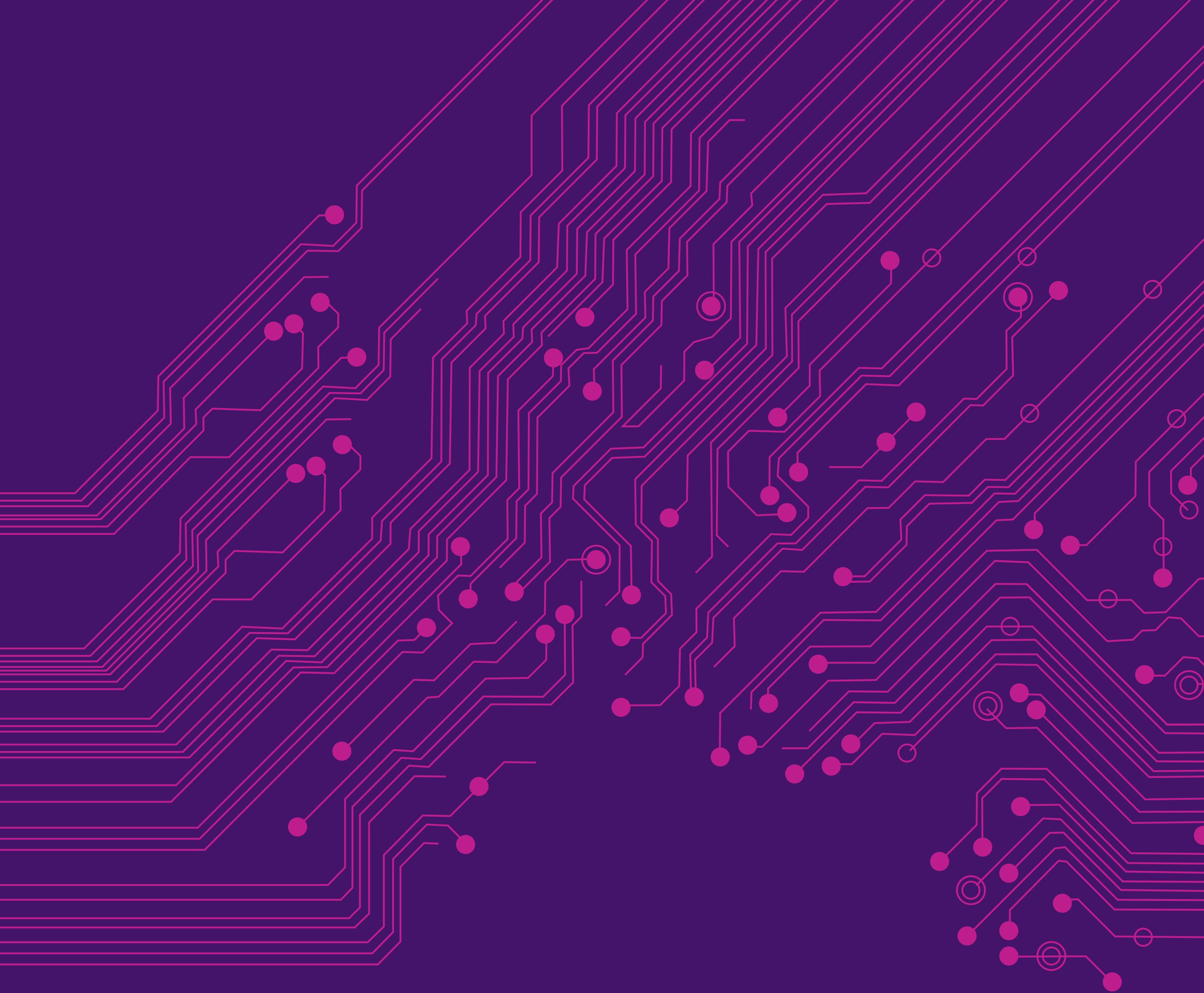


Innovating today **Defining tomorrow**

Annual Report 2011

بنك الخليج الدولي

GULF INTERNATIONAL BANK

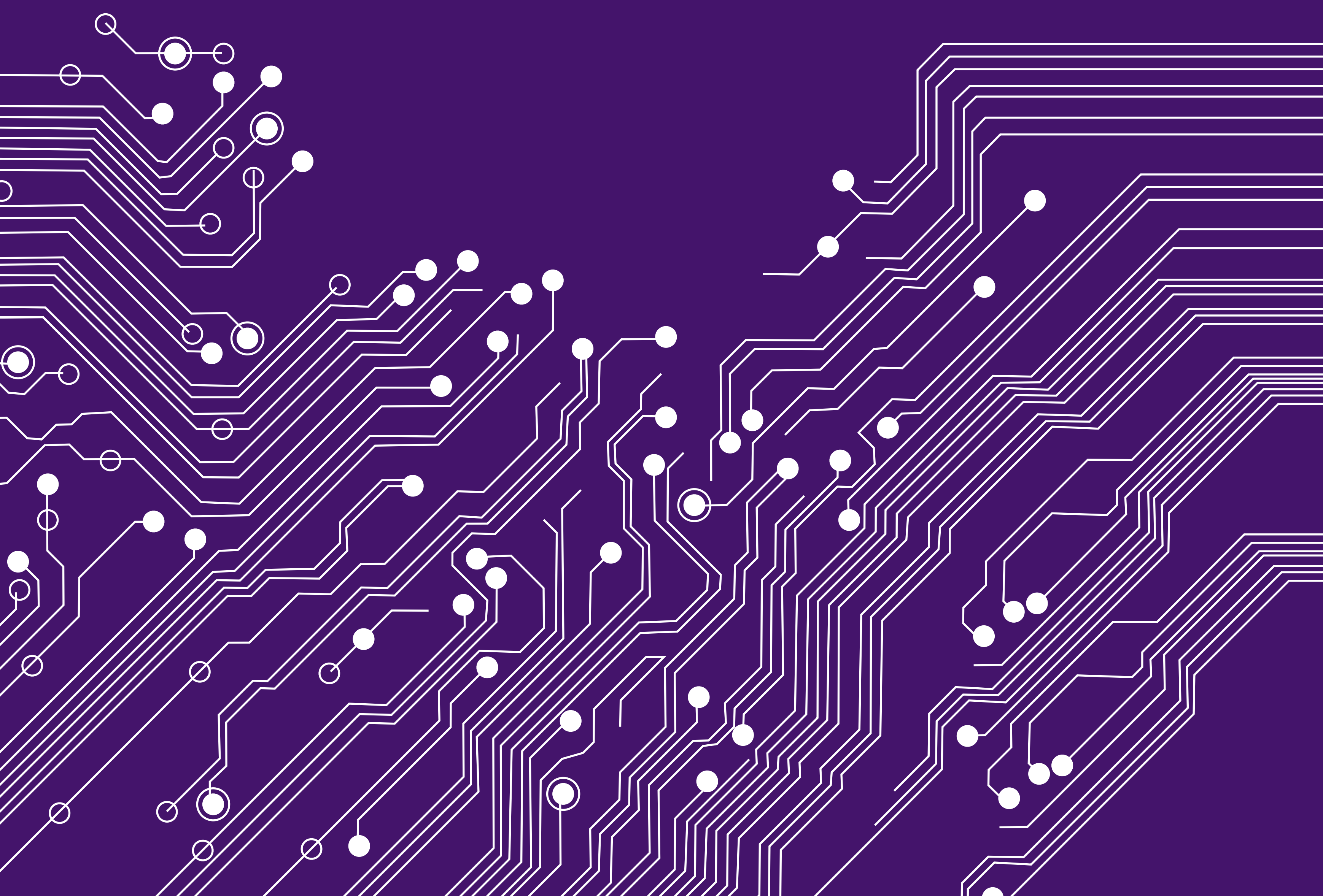
Contents

Gulf International Bank

Gulf International Bank (GIB) aims to be the international GCC bank with regional expertise, global outreach and innovative financial solutions; and to be a value-adding partner, leveraging cutting-edge technology and superior human capital.

GIB's mission is to provide innovative, convenient and customised financial products and services and, in parallel, to build and retain a reputation for trust, quality and reliability in order to establish GIB as the partner of choice and create long-term relationships. This will enable the Bank to add value for its customers, be an employer of choice and meet shareholders' objectives.

The Bank was established in the Kingdom of Bahrain in 1975, and it is licensed by the Central Bank of Bahrain as a conventional wholesale bank. It is owned by the six GCC governments, with the Public Investment Fund of Saudi Arabia holding a majority stake (97.2 per cent). GIB has branches in London, New York, Riyadh Based and Jeddah, and representative offices in Beirut and Abu Dhabi, in addition to its main subsidiaries, Gulf International Bank (UK) Limited, and GIB Capital.



Board of Directors

H.E. Jammaz bin Abdullah Al-Suhaimi
Chairman
Kingdom of Saudi Arabia

Mr. Mansour bin Saleh Al Maiman
Vice Chairman, Secretary General of the Public Investment Fund
Kingdom of Saudi Arabia

H.E. Dr. Hamad bin Sulaiman Al-Bazai
Vice Minister of Finance, Ministry of Finance
Kingdom of Saudi Arabia

Dr. Abdullah bin Hassan Al-Abdul-Gader
Professor, King Fahd University of Petroleum & Minerals
Kingdom of Saudi Arabia

Mr. Sulaiman bin Abdullah Al-Hamdan
Chief Executive Officer, National Air Services
Kingdom of Saudi Arabia

Mr. Abdulla bin Mohammed Al Zamil
Chief Executive Officer, Zamil Industrial Investment Company
Kingdom of Saudi Arabia

Mr. Khaled bin Saleh Al-Mudaifer
President and CEO, Saudi Arabian Mining Company
Kingdom of Saudi Arabia

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Financial Highlights

	2011	2010	2009	2008	2007
EARNINGS (US$ millions)					
Net income/(loss) after tax	**104.5**	100.4	(152.6)	(396.2)	(757.3)
Net interest income	**143.8**	156.2	206.5	288.3	305.6
Fee and commission income	**48.5**	42.2	40.7	73.3	88.1
Operating expenses	**119.8**	113.3	122.8	142.9	141.2
FINANCIAL POSITION (US$ millions)					
Total assets	**16,788.9**	15,527.7	16,207.7	25,033.5	29,954.0
Loans	**6,751.8**	7,510.1	9,298.1	12,972.1	12,601.8
Investment securities	**3,151.7**	3,067.8	2,018.1	2,220.5	8,070.7
Senior term financing	**3,690.3**	3,176.6	3,007.9	2,431.5	2,657.8
Equity	**1,962.8**	1,918.0	1,779.4	1,925.5	2,215.3
RATIOS (Per cent)					
Profitability					
Return on average equity	**5.4**	5.4	(8.2)	(19.1)	(37.2)
Return on average assets	**0.6**	0.6	(0.7)	(1.4)	(2.8)
Capital					
Risk Asset Ratio [1]					
- Total	**23.3**	24.3	22.3	17.3	12.0
- Tier 1	**19.2**	18.7	16.4	12.5	9.5
Equity as % of total assets	**11.7**	12.4	11.0	7.7	7.4
Asset Quality					
Securities as % of total assets	**19.3**	20.3	12.8	9.7	31.4
Loans as % of total assets	**40.2**	48.4	57.4	51.8	42.1
Liquidity					
Liquid assets ratio	**58.2**	50.0	41.2	46.3	52.8
Deposits to loans cover (times) [2]	**2.0**	1.6	1.4	1.6	1.8

[1] From 2008, the risk asset ratio is calculated in accordance with CBB's Basel 2 guidelines, comparative ratios are presented in accordance with the Basel 1 guidelines of the Basel Committee on Banking Supervision.

[2] Deposits include senior term financing.

CREDIT RATINGS

	Fitch	Moody's	Standard & Poor's	Capital Intelligence
Long-term	A	A3	BBB+	A
Short-term	F-1	P-2	A-2	A1
Viability	BBB-			
Financial Strength		D+		BBB+

Chairman's Statement

Jammaz bin Abdullah Al-Suhaimi
Chairman

It is with a sense of pride and privilege that I present Gulf International Bank's Annual Report for the year ended 31st December 2011 on behalf of the Board of Directors. The year was a successful year for GIB. It witnessed the start of the implementation of a new business strategy that aims to transform GIB into a pan-GCC universal bank incorporating a unique retail bank offering. The Bank also recorded a good profit in spite of the challenging business environment regionally and globally.

Thanks to the proactive measures of derisking and deleveraging the balance sheet that were undertaken in the past couple of years, GIB was able to maintain its profitability levels during 2011. The Bank reported year-on-year increases in most income categories and delivered a consolidated net income after tax of US$104.5 million for the year, up from US$100.4 million in 2010. Net interest income was US$143.8 million, down from the previous year by 8 per cent. The year-on-year decrease was attributable to a lower average loan volume associated with ongoing deleveraging initiatives, and an increase in the cost of term finance as a result of actions taken to minimise the mismatch in the maturity profile of the Bank's assets and liabilities.

I would like to point out that while the increase in term finance has resulted in an additional cost, it has significantly reduced the Bank's previous reliance on short-term wholesale funding, thereby protecting the Bank in the stressed market environment that prevailed during most of 2011. During the year, GIB built a strong liquidity buffer that helped it withstand the pressures of the eurozone crisis.

Fee and commission income at US$48.5 million was US$6.3 million or 15 per cent higher than in 2010. As a result, fee-based income comprised 21 per cent of total income, reflecting continued success in the implementation of GIB's new strategic focus on non-asset-based, relationship-orientated services.

Trading income at US$17.6 million was 39 per cent up on the prior year, reflecting strong customer-related foreign exchange revenues. Other income, largely comprising dividends on equity investments and profits realised on the sale of investment securities and the repurchase of the Group's term financing, reached US$17.0 million, representing a 34 per cent increase on the prior year. Total expenses at US$119.8 million were 6 per cent up due to ongoing investment in the implementation of GIB's new strategy. A net provision release of US$1.9 million was recorded for 2011. The absence of a net provisioning requirement reflected the prudent and conservative provisioning actions taken by the Bank in previous years.

At the end of the year less than 10 per cent of the loan portfolio was funded by short-term wholesale deposits. As recognised by the international credit rating agencies, the managed reduction in the leverage of the loan portfolio to a lower, more prudent multiple of equity has strengthened the Bank's risk positioning.

GIB's robust funding position during 2011 reflected the confidence that the Bank's customers and counterparties have in its strong ownership and financial strength. The Basel 2 total and tier 1 capital adequacy ratios have been consistently strong throughout the year, reaching 23.3 per cent and 19.2 per cent respectively at 31st December 2011. I am pleased to announce that we have also succeeded in reducing the Bank's reliance on short-term wholesale funding, thereby ensuring early compliance with the new Basel 3 regulatory rules on liquidity risk management. During 2011, GIB successfully priced and closed a 3-year US$300 million Sukuk-al-Murabaha private placement as part of the US$900 million of new term finance raised during the year.

The Bank concluded a number of milestone transactions during the year. For example, it arranged SAR8.5 billion contracting facilities for the Saudi Binladin Group for the expansion and development of King Abdulaziz International Airport in Jeddah. In addition, the Bank successfully arranged a SAR489.5 million IPO for Hail Cement Company and a US$215 million 5-year Sukuk Al Istithmar for Almana Group.

I am also pleased with the progress made in the implementation of GIB's new strategy, which aims at a total transformation of the way the Bank conducts its business and will take it into new frontiers of sophisticated banking. The development phase of this strategy was completed in 2010, and the first steps towards implementation were executed in 2011. The strategy implementation involved the restructuring of the wholesale banking activity and preparations for launching a new retail banking business. Before this time next year, GIB plans to be able to have fully completed the execution of the strategy and launched its first retail banking stores. We have also selected the location for the Bank's office in Al Dhahran in the Eastern Province of Saudi Arabia. The office is expected to be fully operational during 2012.

Besides the business objectives, our new strategy involves a cultural transformation of the Bank. This included formulating a new vision, mission and set of corporate values, which will be more in keeping with our approach towards building relationships and getting closer to the customer. We will invest in new technology to give the retail business of our Bank a unique edge that will create a bank that the customer wants. In fact, our new IT systems will take GIB's entire offerings – retail and wholesale – into a whole new definition of customer satisfaction and interaction. We believe that these measures will, within a few years, achieve the expected levels of profitability and return on equity in line with the expectations of our shareholders.

With a return to profitability, we have an increased risk appetite and a new approach to managing it. In 2011, we enhanced the robust risk management framework that was already in place, and developed several structural initiatives to align with the new strategy. These included developing a retail risk department, articulating a new Risk Appetite Policy and Statement, a renewed focus on overall portfolio management, implementing the Moody's KMV internal risk rating model for corporates, and further strengthening wholesale banking risk management to encourage and support growth without sacrificing portfolio quality.

"Underscoring GIB's financial performance was the reaffirmation of the Bank's long-term issuer ratings by Fitch (A), Moody's (A3) and Standard & Poor's (BBB+) with a Stable Outlook. Such recognition constitutes a positive independent endorsement of the proactive and conclusive actions taken by GIB and its shareholders to address the challenges created by the global financial crisis."

On the corporate governance front, we continued to be vigilant in maintaining our regional leadership in this vital area by adopting a number of additional measures in accordance with the new requirements of the Central Bank of Bahrain, including, amongst other things, adopting a new Board Charter and setting up a new whistle-blowing programme that enhances the whistle-blowing provisions already existing in GIB's Code of Conduct.

Underscoring GIB's financial performance was the reaffirmation of the Bank's long-term issuer ratings by Fitch (A), Moody's (A3) and Standard & Poor's (BBB+) with a Stable Outlook. Such recognition constitutes a positive independent endorsement of the proactive and conclusive actions taken by GIB and its shareholders to address the challenges created by the global financial crisis. The affirmation of the Bank's credit ratings came at a time when many countries and financial institutions were downgraded. This reflects GIB's strong financial position and market confidence.

Although customer satisfaction is a reward in its own, it is always gratifying to receive recognition. GIB has been frequently recognised for its commitment to excellence and professionalism and the very best in customer service. In 2011, the Bank was presented with a number of awards, accolades well deserved by the teams that brought them home. We received three awards from *Global Banking and Finance Review:* Best Investment Bank in the GCC, Best Investment Bank in Bahrain and Best Investment Bank in KSA for our subsidiary GIB Capital. New York-based *Global Finance* magazine also selected GIB as the Best Investment Bank in Bahrain for 2011. UK-based *emeafinance* magazine named GIB as the Best Local Investment Bank in Bahrain, 2011. And finally, Dubai-based *Islamic Business & Finance* magazine named GIB as the Best Sukuk Arranger for the year 2011.

GIB's positive outlook for 2012 and beyond must be seen against the backdrop of 2011, which was a turbulent year politically and economically. The GCC countries fared reasonably well despite these circumstances. This was largely due to vigorous state spending which supported the continued implementation of projects, spurred growth over several economic sectors and generated private spending. Oil production spiked during the course of the year, before easing by the second half; this further bolstered growth in the Gulf region. The relative strength of oil prices with the sharp gains in oil output augmented surplus balances in the fiscal and external accounts, and further allowed a build-up of already robust foreign exchange reserves. In addition, the GCC countries demonstrated better management of the deteriorating external environment during 2011 as banking sector liquidity improved and deleveraging progressed steadily.

As we enter 2012, there are expectations of a slowdown in global growth; factors affecting this include: the severity of the recession in Europe, the continued credit crunch, fiscal austerity and looming concerns about peripheral countries in the eurozone. There are also growing downside risks to the otherwise recent improvements in the economic condition of the United States; ongoing uncertainty towards China's ability to sustain its economic performance; and a tightened policy stance across key emerging countries resulting in slower growth prospects in major economies like Brazil and India.

In the Middle East and North Africa region, political uncertainty is expected to continue to influence overall developments, especially in the affected countries, while strong government spending and favourable oil prices will support growth levels across the GCC countries. However, while these economies remain bolstered by robust reserves accumulated from consecutive years of high oil prices, average growth levels during 2012 are expected to be lower amid a weaker global environment with a consequential impact on global oil demand. Still, GCC fiscal and current account surpluses are projected to remain at the same levels, although there will be increased vulnerability during 2012 to oil price movements.

With the difficult business environment that is predicted during the course of the coming months, it is comforting to know that GIB's strengths, including its solid shareholding and the implementation of the new business strategy, will keep us on track to provide shareholders with the expected enhanced return on equity that we expect will be competitive with the Bank's peers'. We are confident that the new strategy will enable

Chairman's Statement (continued)

GIB to take advantage of emerging business opportunities, continue its key role in Saudi Arabia and the region as a leading financial institution, and ensure greater prosperity for all our stakeholders.

On behalf of the Board of Directors, I would like to express my sincere appreciation for the financial support and guidance of our shareholders; the trust and loyalty of our clients; the positive collaboration of our business partners; and the constructive cooperation of the regulatory and supervisory authorities in the various jurisdictions where GIB operates.

Finally, I would like to pay tribute to the professionalism and dedication of the Bank's management and staff during 2011, which witnessed intensive mobilisation of resources to implement the new strategy. I thank you all for your positive attitude and dedication and wish you and the Bank continued success and prosperity in 2012 and the years ahead.

Jammaz bin Abdullah Al-Suhaimi
Chairman

The future at your fingertips

Management Review

Yahya A. Alyahya
Chief Executive Officer

Although 2011 was a challenging year, for GIB it was also a year of growth and anticipation. We achieved another year of profitability, building on the achievements of 2010, and developed a stronger funding position – all in spite of higher costs incurred in preparation for implementing the Bank's new strategy. We successfully navigated our way through the turbulent global financial markets and the events in the region. But, most importantly, we continued with implementing the new strategy – Enjaz 2015. With this new beginning and redefinition, an exciting organic change has already started to radically transform GIB and will continue to do so in the coming years.

With the implementation of the new strategy, GIB is set to become the pan-GCC universal bank with its core strengths reinterpreted, and a retail banking function will be added. This new business model sets us on an altogether different pedestal. There were many different moving parts that needed to meld and make this new model operational. Developing these and putting them in place was the dominant work of the year.

In preparation for the year ahead, the management worked tirelessly over the course of 2011 to complete the implementation of various work streams in order to prepare for the launch of the new retail business. The strategy implementation process included reorganising many different areas of operation, from wholesale banking and risk management to IT, communications and human resources, almost all with added responsibilities and broader functions.

Wholesale banking was restructured and expanded to make it more product-efficient and client responsive; this in itself has already created a new dynamism in this core pillar. With relationship management in focus, we are now better prepared to be able to cross-sell fee-based products and services and offer these to a broader client base, including large and mid-cap corporate customers.

When launched, our new retail banking business, which is the basis for our metamorphosis, will employ cutting-edge technology to deliver a new model in the region albeit with proven successes in other markets. As plans stand, it will be introduced first in Saudi Arabia, and then rolled out across the GCC within the coming years. We are confident that this will be the kind of bank that customers actively seek.

Our Treasury also continues to provide diversified and stable sources of funding, and additional revenue streams, while helping to reduce the Bank's vulnerability to external shocks.

In readiness, several change management initiatives were launched including workshops across all the different areas of the Bank. These were designed to encourage the acceptance of the inevitable cultural changes, which will result from the new strategy. Along with these, GIB's new vision, mission and values were articulated and communicated to sustain and boost the momentum of internal acceptance. We are delighted to report that they were enthusiastically taken on board by all participants and have been a source of renewed energy.

On the technology front, an intensive search and evaluation process was initiated to identify and finalise the required complex new technology platform – hardware, software and systems – to support the transformation of the Bank. With all these, we look forward to 2012 with renewed vigour and higher goals.

BUSINESS ACHIEVEMENTS

In spite of the global financial climate, GIB progressed steadily in its core areas of expertise, which continue to be our unmatched knowledge and experience added to our regional footprint and long-term connections with the world's leading financial institutions.

Also in 2011, GIB Financial Services (GIBFS), our investment banking arm in the Kingdom of Saudi Arabia, was rebranded as GIB Capital. The new name reinforces the company's continued focus on its core business activities of investment banking and capital market transactions. As hoped for, GIB Capital had an active year.

Building on last year's success, GIB continued to play a leading role in the region's corporate lending and finance. The Bank, for example, won a mandate from the Saudi Binladin Group to syndicate a SAR8.5 billion contracting facility to finance the expansion and development of the King Abdulaziz International Airport in Jeddah. GIB was initially mandated to arrange a SAR6 billion syndicated facility, which was subsequently raised to SAR8.5 billion.

The Bank also arranged an Initial Public Offering of SAR489.5 million for Hail Cement Company. With this IPO, GIB Capital confirmed its status as a market leader. It is the only investment bank in Saudi Arabia to have successfully executed at least one IPO transaction every year since 2008. The Bank also arranged on behalf of Almana Group a US$215 million 5-year floating rate Sukuk. GIB acted as sole bookrunner of this issuance.

Also during the year, two new fund concepts were developed. The Saudi Manufacturing Fund, which will focus on investing in manufacturing-related opportunities in Saudi Arabia, and the Housing Developers Fund, which will invest in low to medium income housing development projects in the Kingdom of Saudi Arabia. Both funds have received good interest from regional investors and are targeted for launch in early 2012.

GIB maintains a presence outside the GCC region through branches in London and New York and a representative office in Beirut. Based on significant trade flows and long-term relationships with the GCC, the Bank's international trade finance and institutional lending is mainly conducted in the MENA region. In 2011, the Bank continued to support international contractors and sponsors involved in projects across the region with their banking requirements. The North Africa region, which is managed by our London branch, saw repeat business in the area of trade finance and treasury out of Algeria and Morocco, which is all related to local financial institutions. Treasury continues to offer the Bank's client base a wide

"Although 2011 was a challenging year, for GIB it was also a year of growth and anticipation. We achieved another year of profitability, building on the achievements of 2010, and developed a stronger funding position – all in spite of higher costs and expenditure incurred in preparation for implementing the Bank's new strategy."

spectrum of financial solutions to meet their business needs ranging from the simple to the innovative, while generating trading revenues within prudent limits set by the Board of Directors.

Funding and liquidity remain of primary importance and Treasury has been successful in further diversifying the Bank's funding profile, while at the same time extending the average tenor of deposits. In addition, and in anticipation of Basle III requirements, the Bank raised US$900 million of term finance during the year, including a US$300 million 3-year Sukuk Private Placement, being the first of its kind in the Bank's history.

The Bank's investment securities portfolio represents a liquidity reserve. Credit quality is accordingly of vital importance to ensure the securities can be used to generate liquidity in the event of stressed markets or a financial crisis. Hence, US$500 million of high grade assets were purchased during 2011 to maintain an appropriately high stock of liquidity. In addition, the net free capital of the Bank is invested in the highest quality fixed rate bonds. The bonds are of a relatively short duration to provide an enhanced yield over short-term money market rates, while being prudently positioned in the event that interest rates rise in the medium term in anticipation of rising inflation.

Treasury continues to maintain its strategy of attracting skilled treasury professionals to provide its stakeholders with bespoke, tailored solutions and assist in the development of a long-term, sustainable franchise.

As an active participant in the international financial markets, GIB caters to a pan-continental client base. We have developed an understanding of our clients' investment objectives, and we deliver solutions that are predominantly tailored to client mandates and needs. At the end of 2011, our asset management team had funds under management of US$8.2 billion. The Bank's flagship fund, the GIB Emerging Markets Opportunities Fund, closed in December 2011 with a net asset value of US$147.4 million, up from US$106 million at launch in 2010. An active management strategy achieved a 10.1 per cent return net of fees for its investors, the Fund has been nominated for two awards by *Eurohedge* magazine: top emerging market fund of the year and top new fund of the year.

In 2011 we were able to enhance our robust risk management framework. GIB undertook several structural initiatives to align its risk management framework with the new business strategy. These included: implementation of Moody's KMV Risk Analyst Model for rating corporate customers, comprehensive risk management control, and enhanced market risk, operational risk and information security functions. The Bank also developed a clearly articulated Risk Appetite Policy and Risk Appetite Statement setting clearly defined boundaries for the types and level of risks the Bank is willing to accept in pursuit of it objectives. The resilience of GIB's Business Continuity Plan was proven when it was put to the test during the events in February and March in Bahrain, when the Bank was able to continue operations without any disruption from its disaster recovery site in Bahrain.

While GIB undergoes the transformation into a pan-GCC universal bank, our risk management is primed to continue to provide quality support to the Bank's business. The risk function will be further strengthened to support planned growth in the loan portfolio; the information security and operational risk frameworks are under enhancement to include the retail business; and retail risk functions are being established.

The outcome of these successes along with our well-recognised professionalism and strict adherence to risk management and best industry practices was the reaffirmation of the Bank's credit ratings by the major rating agencies: Fitch (A), Moody's (A3) and Standard & Poor's (BBB+). This recognises GIB's strong ownership structure and capitalisation, improved liquidity, and conservative provisioning.

In 2010, GIB received approval from the Saudi Arabian Monetary Agency to open a new branch in the Eastern Province of the Kingdom of Saudi Arabia. Over the course of 2011, we identified premises for the new branch in Al-Dhahran and started working on installations and design concepts. The new branch will help the Bank expand its operations in the Eastern Province, build stronger relationships with customers, and achieve greater market penetration in the region's largest economy.

Businesses successes are, at the end of the day, a result of the people behind any organisation. And, with our new stronger focus on relationships overall, we extend this approach to our own

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Management Review (continued)

personnel. We have therefore adopted various new human resource initiatives, to attract, retain and grow the human capital towards the achievement of our Enjaz 2015 objectives. The motivation and retention of our staff are enhanced by engaging them with transparent communication, developing leadership competencies, identifying key talents, job rotation, measuring and monitoring performance, benchmarking our compensation and benefits with the market and aligning all staff towards the organisation's values. We believe these initiatives reflect our commitment and will allow us to become an "Employer of Choice" in the region.

LOOKING FORWARD

During 2011, the GCC countries fared reasonably well despite the political and economic turmoil that characterised the year. This was due in large part to state spending, the relative strength of oil prices that, with the gains in oil output, strengthened surplus balances in fiscal and external accounts; augmenting a build-up of already robust foreign exchange reserves. In addition, the GCC countries demonstrated better management of the deteriorating external environment during 2011 as banking sector liquidity improved and deleveraging progressed steadily.

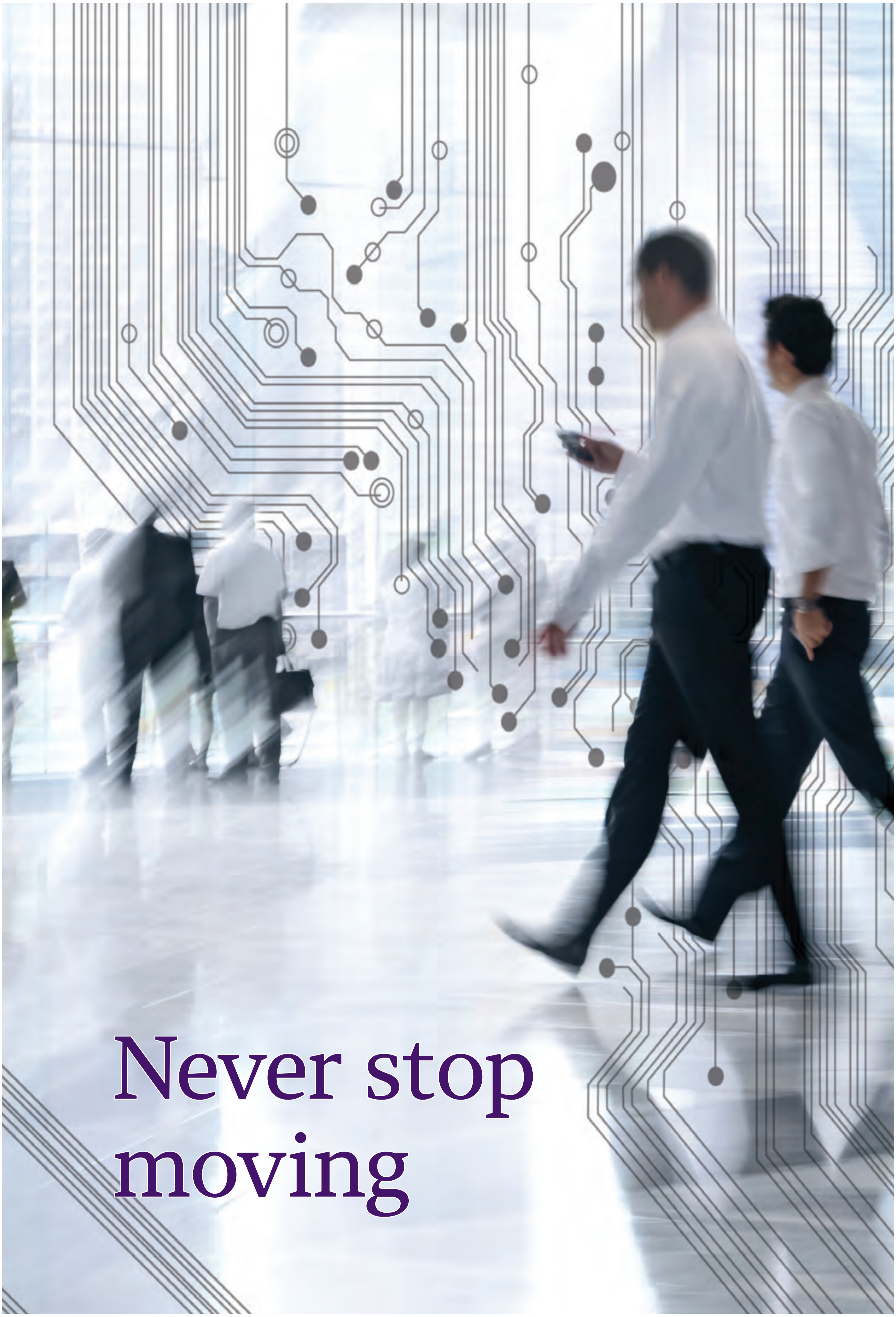
As we enter 2012, there is reason for us to be optimistic. Although the MENA region is expected to witness continuing political uncertainty, the GCC economies, where we have a large portion of our business, are expected, by most pundits to remain bolstered by robust oil reserves, strong government spending and favourable oil prices. Moreover, GCC fiscal and current account surpluses are projected to remain at similar levels while there will be increased vulnerability during 2012 to oil price movements.

All things considered, GIB's main financial indicators are positive: growth in profitability, the absence of any loan provision charge, a high level of liquidity and a significant increase in customer deposits coupled with an exceptionally strong capital adequacy ratio and no exposure to the debt of European governments impacted by the eurozone crisis. So, though in the short-term earnings may dilute as we commit to expenditures to build the new retail business, we expect that within five years our level of profitability will be commensurate with a return on equity that meets the expectations of our shareholders.

On all scores we came through 2011 stronger, confident of the direction we are heading to, and supported by our committed shareholders. So, we look forward to the year ahead with tremendous energy, prepared for the changes that are being made and the developments and advancements yet to come.

Finally, I want to thank you all – our staff and management for your positive attitude, commitment and loyalty and our shareholders and clients for trusting and supporting us. It is this faith in us that makes us determined to earn and deserve your continued confidence.

Yahya A. Alyahya
Chief Executive Officer



Never stop moving

Financial Review

GIB recorded consolidated net income after tax of US$104.5 million being US$4.1 million or 4 per cent up on the prior year.

Year-on-year increases were recorded in all income categories, with the exception of net interest income. Net interest income, which at US$143.8 million represented the Group's principal income source, was 8 per cent down on 2010. The year-on-year decrease was attributable to a lower average loan volume associated with ongoing derisking initiatives, and an increase in the cost of term finance as a result of proactive actions taken to minimise the mismatch in the maturity profile of the Group's assets and liabilities. While the additional term finance resulted in an increased cost to the Group, it significantly reduced the Group's previous reliance on less stable short-term wholesale funding, thereby protecting the Group in the prevailing stressed market environment. Fee-related income at US$48.5 million was US$6.3 million or 15 per cent higher than the previous year, reflecting positive progress in the implementation of GIB's new strategic focus on non-asset based, relationship-orientated services.

Trading income at US$17.6 million for the year was US$4.9 million or 39 per cent up on the prior year, reflecting strong customer-related foreign exchange income. Other income of US$17.0 million was US$4.3 million or 34 per cent up on the prior year, and consisted principally of dividends received from listed equity investments, and profits realised on the sale of investment securities for credit reasons and repurchases of the Group's own senior and subordinated debt. Total expenses of US$119.8 million were US$6.5 million or 6 per cent up on the prior year.

The year-on-year increase in expenses reflected ongoing investment in the implementation of GIB's new GCC-focused universal banking strategy. A net provision release of US$1.9 million was recorded for 2011. The provision release arose on the full repayment of a provisioned exposure. The absence of a net provisioning requirement reflected the prudent and conservative provisioning actions taken by the Group in previous years.

NET INTEREST INCOME

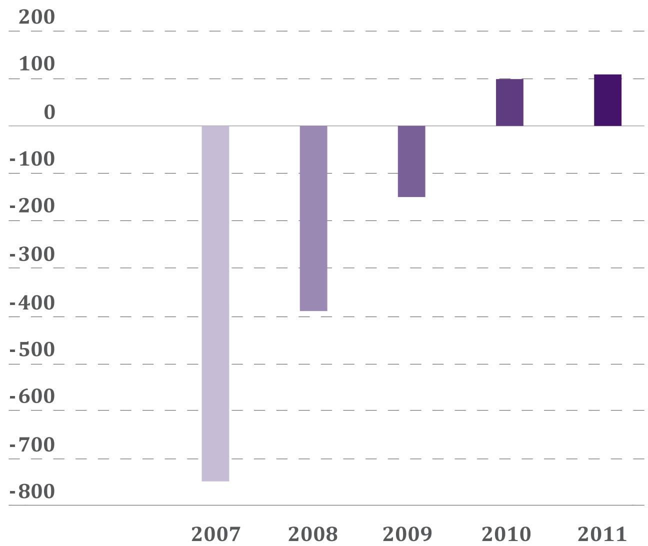
Net interest income at US$143.8 million was US$12.4 million or 8 per cent lower than in the prior year. Net interest income is principally derived from the following sources:-

- margin income on the wholesale lending portfolio,
- margin income on the investment securities portfolio,
- money book activities, and
- earnings on the investment of the Group's net free capital.

Net interest income also incorporates the cost of term finance.

The year-on-year decrease in net interest income was largely attributable to: (i) lower interest earnings derived from the wholesale lending portfolio as a result of a managed decrease in loan volumes, (ii) lower interest earnings on the investment of the net free capital attributable to a reduction in US interest rates to historically low levels, and (iii) a higher cost of term finance as a result of new term finance raised during 2010 and 2011.

Net income development (US$ millions)



	2007	2008	2009	2010	2011
Net income	(757.3)	(396.2)	(152.6)	100.4	104.5

Interest earnings on the wholesale lending portfolio accounted for 77 per cent of the Group's net interest income before the cost of term finance. Interest earnings derived from wholesale lending were 7 per cent lower than in the prior year due to the managed reduction in the loan portfolio during 2010 and 2011 as part of the initiative to delever and derisk the balance sheet. The deleveraging of the loan portfolio was completed in 2011 and a gradual increase in the loan volume is planned for the future with a strategic focus on relationship-based large and mid-cap corporate customers.

Margin income on the investment securities portfolio accounted for 11 per cent of net interest income before the cost of term finance. The interest earnings from the investment securities portfolio were 50 per cent up on the prior year. The significant year-on-year increase was attributable to a 12 per cent increase in the average volume of securities in 2011 and a more significant 35 per cent increase in the average spread on the portfolio resulting from higher spreads on new investment purchases in 2010 and 2011. The investment securities portfolio is primarily maintained as a liquidity reserve. The key factors underpinning the portfolio are therefore liquidity and quality rather than income-generating characteristics.

Money book earnings represent the differential between the funding cost of interest-bearing assets based on internal transfer pricing methodologies and the actual funding cost incurred by the Group. This includes benefits derived from the mismatch of the repricing profile of the Group's interest-bearing assets and liabilities. Money book earnings in 2011 accounted for 14 per cent of net interest income before term finance costs, and were 52 per cent higher than the prior year. This increase reflected a reduction in short-term funding costs attributable to a higher level of more cost-efficient customer deposits. As a result of a focus on

"GIB recorded consolidated net income after tax of US$104.5 million being US$4.1 million or 4 per cent up on the prior year."

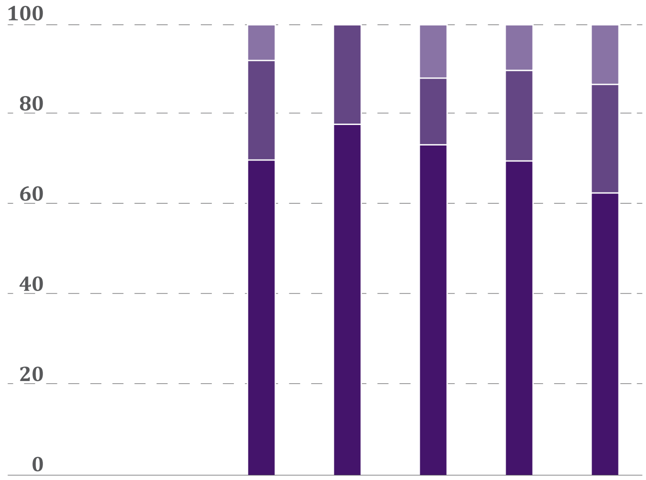
customer deposits from counterparties in the GCC, the increase in costs witnessed in the international interbank market, associated in particular with the eurozone crisis, had minimal impact on the Group's cost of funds or net interest earnings. The Group was a beneficiary of the general market uncertainties associated with the Arab Spring and eurozone events, with counterparties in the region becoming more risk sensitive and accordingly directing their funds to banks with strong financial profiles and ownership. As a result, GIB was able to be more selective in the sourcing of its deposits. During 2011, the Group was successful in increasing deposit average tenors, while reducing its cost of funds.

Earnings on the investment of the Group's net free capital were 8 per cent lower than in the prior year, and accounted for 10 per cent of net interest income before term finance costs. The net free capital was largely invested in shorter 2 and 3 year duration bonds reflecting the Group's view that economic conditions in the United States were not conducive to a rise in US interest rates in the short term, although the shorter tenor fixed rate instruments provide the opportunity to reinvest on maturity at higher yields in the event that interest rates rise in the short to medium term as a result of a more constructive outlook for the US economy.

At the end of 2011, circa. half of the Group's net free capital was invested in shorter duration fixed rate instruments, generating an enhanced return over short-term interest rates. Earnings on the net free capital in 2011 were negatively impacted by the historically low short-term US interest rates prevailing throughout the year.

The cost of term finance increased in 2011 as a result of new term finance raised during 2010 and 2011, being the principal contributor to the year-on-year decrease in net interest income. Net interest income in 2011 excluding term finance cost, was at the same level as in 2010. The new term finance was raised to reduce the mismatch between the maturities of the Group's assets and liabilities and accordingly reduce the Group's exposure to liquidity risk. The Group's historical reliance on funding longer tenor assets with short-term deposits and the associated liquidity and refinancing risk were recognised in 2009, and proactive actions were subsequently taken to raise new term finance to minimise this undue risk. As a result, almost US$3.0 billion of new term finance has been raised over the last three years. This effectively addresses one of the key focuses of the new Basel 3 regulatory guidelines, whereby banks will have less ability to fund longer tenor assets with shorter tenor wholesale deposits. The initiatives to reduce the Group's exposure to liquidity risk resulted in an US$11.8 million or 8 per cent year-on-year reduction in the Group's net interest income.

Gross income composition (%)



	2007	2008	2009	2010	2011
Net interest income	70.6	79.7	72.2	69.8	63.4
Fee and comission income	20.3	20.3	14.2	18.9	21.4
Trading and other income	9.1	-	13.6	11.3	15.2
Total	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

NON-INTEREST INCOME

Non-interest income comprises fee and commission income, trading income, and other income.

Fee and commission income at US$48.5 million was US$6.3 million or 15 per cent higher than in the prior year. An analysis of fee and commission income with prior year comparatives is set out in note 22 to the consolidated financial statements. Investment banking and management fees were US$24.6 million for the year, thereby representing half of fee and commission income. This income category comprises fees generated by the Group's asset management, fund management, corporate advisory and underwriting activities. Investment banking and management fees were at a similar level to the prior year and incorporated fees derived from a number of debt and equity capital market mandates during the year, as commented on in more detail in the Management Review section of the Annual Report. As referred to in note 35 to the consolidated financial statements, assets held in a fiduciary capacity amounted to US$8.1 billion at 31st December 2011. Commissions on letters of credit and

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Financial Review (continued)

guarantee at US$22.7 million were the second largest source of fee-based income and continued to make an important contribution to fee and commission income. A US$6.7 million or 42 per cent year-on-year increase in commissions on letters of credit and guarantee reflected an enhanced focus on supporting customers' commercial and trade finance requirements.

The Group's various trading activities recorded a US$17.6 million profit compared to a US$12.7 million profit in the previous year. Trading income is reported inclusive of all related income, including interest income, gains and losses arising on the purchase and sale, and from changes in the fair value of trading securities, dividend income, and interest expense, including all related funding costs. An analysis of trading income is set out in note 23 to the consolidated financial statements. Trading income in 2011 principally comprised a US$10.3 million profit arising on customer-related foreign exchange business. A US$3.2 million profit arose on managed funds, being only marginally lower than in the previous year. The investment in managed funds principally comprises a seed investment in an emerging market government-related debt fund managed by the Bank's London-based subsidiary, Gulf International Bank (UK) Limited (GIBUK). The fund, the Emerging Markets Opportunities Fund, generated a 10.1 per cent return in 2011. A US$3.7 million profit was also recorded on debt securities classified as trading. These represent emerging market debt securities that are being managed by GIBUK on behalf of the Parent Bank.

Other income of US$17.0 million principally comprised US$7.3 million of dividends received from equity investments classified as available-for-sale, US$5.0 million of profits realised on the sale of investment securities for credit reasons, and profits of US$4.7 million arising on the repurchase of the Group's own subordinated and senior debt. During 2011, the Group repurchased US$33.2 million of a subordinated floating rate note maturing in 2015 at a discount to the nominal value of the bonds. This profit was generated as a result of market events associated with the eurozone crisis and was exceptional in nature.

Profitability Drivers

Driver	2011	2012 and Beyond
Loan volume	Loan volume stabilised at target loan to equity ratio	Planned increase in loan volume in 2012 and beyond
Loan margins	Higher loan margins through increased focus on GCC large and mid-cap corporates	Continued increase in loan margins by replacement of lower margin project finance lending with higher margin GCC large and mid-cap corporates
Income on net free capital	Historically low interest rate environment	Rising interest rate environment in context of rising inflation
Term finance cost	Increased term finance to eliminate liquidity risk (fully Basel 3 compliant)	Reduced term finance requirement as a result of short tenor lending
Fee and commission income	Reorganisation of wholesale banking to focus on relationship-based cross selling of fee-based products and services	Focus on cross selling of non-asset based products and services, e.g. investment banking services, asset management and private equity funds
Trading income: customer-related treasury revenue	Establishment of client services desk to focus on cross sell of treasury products	Continued focus on cross selling of treasury products
Expenses	Increase resulting from investment to support business growth	Investment associated with new business strategy, e.g. IT systems
Provisions	No net provisioning requirement	Significant non-specific provision buffer based on historical stressed probability of defaults

Higher Profitability Lower Profitability Unchanged Profitability

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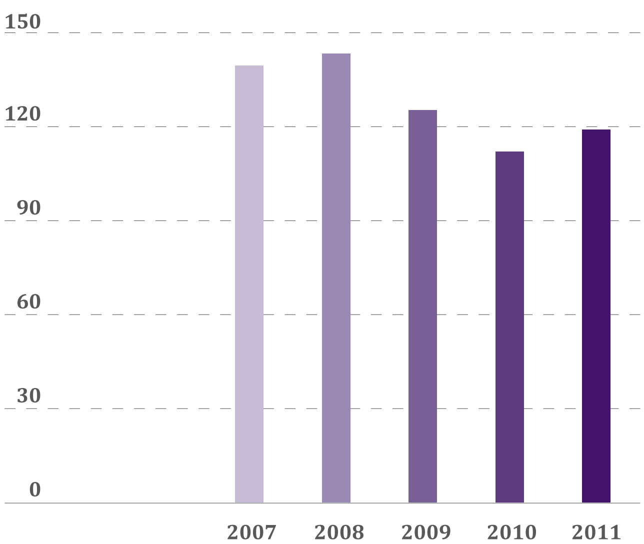
Expenses development (US$ millions)



	2007	2008	2009	2010	2011
Operating expenses	141.2	142.9	122.8	113.3	119.8

OPERATING EXPENSES

Operating expenses at US$119.8 million were US$6.5 million or 6 per cent up on the prior year although were nevertheless US$3.0 million below the level in 2009. 2009 expenses were also US$20.1 million or 14 per cent down on 2008. Thus, the Group's operating expenses have reduced by US$23.1 million or 16 per cent between 2008 and 2011. This reflects the significant beneficial impact on operating expenses derived from a cost realignment programme implemented in 2009. The programme included a reduction in staffing levels in line with the Group's operating model, a migration to uniform IT platforms, and associated operational efficiencies. The Group's expenses will, however, increase in the short term as a result of costs associated with the implementation of the new universal banking strategy.

Staff expenses, which accounted for almost two thirds of total operating expenses, were US$16.3 million or 27 per cent up on the prior year. The significant year-on-year increase was attributable to an exceptional reversal in 2010 of a prior year performance-related expense, and an increase in headcount during 2011. The Group's total headcount at 31st December 2011 of 484 staff was 44 higher than at the end of 2010. The increase in headcount reflected an enhancement of resources in business areas and certain support functions, including risk management, as well as the business build teams for the planned new retail bank.

Premises expenses at US$9.9 million were in line with the prior year.

Other operating expenses were US$9.7 million or 23 per cent lower than in the prior year. However, 2010 expenses included an exceptional strategy-related cost of US$15.0 million. Excluding this exceptional expense, other operating expenses were US$5.3 million or 20 per cent up on the prior year. The year-on-year increase was attributable to the ongoing investment associated with the implementation of the new business strategy and, in particular, costs relating to new information technology initiatives.

PROVISIONS

Following prudent provisioning actions in previous years in anticipation of a higher level of corporate defaults in the weakening economic environment at that time, provisioning requirements in 2011 were limited.

In 2011, there was a US$4.8 million provision charge for investment securities and a US$6.7 million release of loan provisions.

The investment security provision charge was entirely attributable to a provision for an impaired private equity investment. The investment was fully provisioned. All investment security specific provisions, amounting in total to US$58.2 million, related to impaired equity investments. The specific provisions represented 78 per cent of the gross value of the impaired investments.

The loan provision release arose on the full repayment of a specifically provisioned loan facility. In addition, US$35.0 million was reallocated from the non-specific provision to specific provisions in relation to five impaired loan facilities.

CAPITAL STRENGTH

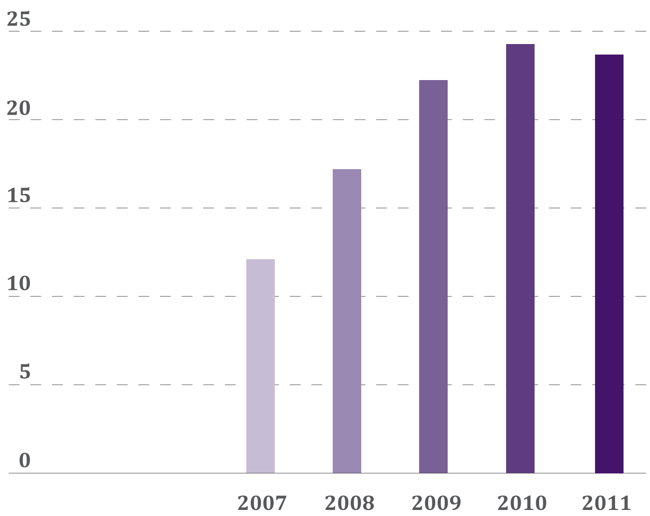
Total equity amounted to US$1,962.8 million at 31st December 2011. At the 2011 year end, the ratio of equity and tier 1 capital to total assets were both 11.7 per cent, ratios that are high by international comparison. The average tier 1 capital to total assets ratio of the top 1,000 world banks was 5.2 per cent according to a survey published in *The Banker* magazine in July 2011.

A US$44.8 million increase in total equity during 2011 comprised the net of the US$104.5 million profit for the year, and a US$59.7 million net decrease in the fair value of available-for-sale securities and derivative cash flow hedges. In accordance with IAS 39, changes in the fair values of securities classified as available-for-sale, and derivative cash flow hedges are accounted for in equity through the comprehensive statement of income. The net decrease in the fair value of available-for-sale securities reflected a general widening in credit spreads during 2011 resulting in a small decrease in the fair value of the investment securities portfolio.

The unrealised revaluation loss on investment securities at the 2011 year end was US$78.4 million compared to US$21.5 million at the end of 2010. This represented only 2.5 per cent of the total fair value of the investment securities portfolio. The relatively small unrealised revaluation loss reflected the high quality of the securities. Investment securities principally comprise investment grade-rated debt securities issued by major international and regional financial institutions and government-related entities.

Financial Review (continued)

Risk asset ratio (%)



	2007	2008	2009	2010	2011
Risk asset ratio	**12.0**	**17.3**	**22.3**	**24.3**	**23.3**

With a total regulatory capital base of US$2,389.3 million and total risk-weighted exposure of US$10,272.7 million, the risk asset ratio calculated in accordance with the Central Bank of Bahrain's Basel 2 guidelines was 23.3 per cent while the tier 1 ratio was a particularly strong 19.2 per cent. In accordance with international regulatory guidelines, the fair value adjustments to equity arising under IAS 39 in relation to available-for-sale securities and derivative cash flow hedges are excluded from the regulatory capital base, with the exception of unrealised gains and losses on equity investments. As a result, at the 2011 year end, net fair value losses of US$6.5 million were added back to equity to derive the regulatory capital base for capital adequacy purposes. The Group's regulatory capital base is enhanced by subordinated term financing facilities. The amount included in tier 2 capital at 31st December 2011 in respect of subordinated term finance was US$316.7 million. This was net of a discount of US$161.1 million for subordinated term finance that is within five years of its final contractual maturity date. The subordinated term financing facilities are approved for inclusion in tier 2 capital for capital adequacy purposes by the Group's regulator, the Central Bank of Bahrain.

At 31st December 2011, the regulatory capital base, excluding subordinated term financing, amounted to US$2,072.6 million. This level of regulatory capital would support an additional US$3.5 billion of 100 per cent risk-weighted assets while still maintaining the Group's target minimum risk asset ratio of 15 per cent. The Group therefore has more than sufficient regulatory capital to support future growth plans.

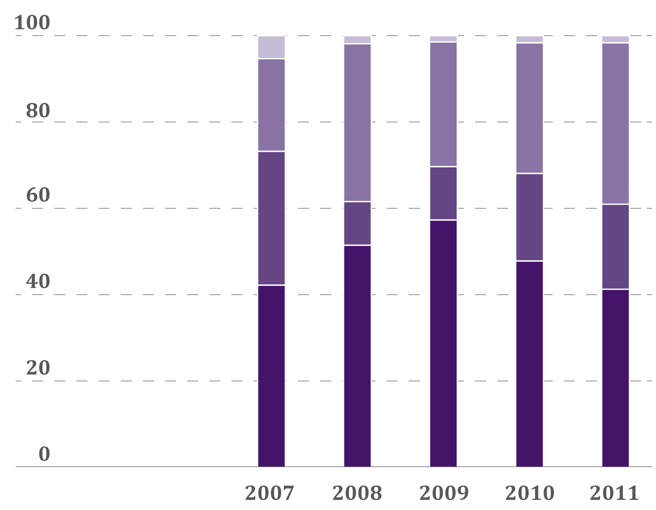
The risk asset ratio incorporates both market and operational risk-weighted exposures. With approval from the Central Bank of Bahrain, the Group applies the internal models approach for market risk, and the standardised approach for determining the capital requirement for operational risk. This demonstrates that the Group's regulator is satisfied that the Group's risk management framework fully meets the guidelines and requirements prescribed by both the Central Bank of Bahrain and the Basel Committee for Banking Supervision.

The Basel 2 Pillar 3 report set out in a later section of the Annual Report provides further detail on capital adequacy and the Group's capital management framework. The Group's policies in relation to capital management are set out in note 27 to the consolidated financial statements. As described in more detail in the note, the Group's policy is to maintain a strong capital base so as to maintain investor, counterparty and market confidence and to sustain the future development of the Group's business.

ASSET QUALITY

The geographical distribution of risk assets is set out in note 28 to the consolidated financial statements. The credit risk profile of financial assets, based on internal credit ratings, is set out in note 27(a) to the consolidated financial statements. This note demonstrates that 82 per cent of all financial assets, comprising liquid assets, placements, securities and loans, were rated 4- or above, i.e. the equivalent of investment grade-rated.

Asset mix by category (%)



	2007	2008	2009	2010	2011
Other	5.1	1.8	1.4	1.6	1.6
Placements and liquid assets	21.4	36.7	28.5	29.8	38.9
Securities	31.4	9.7	12.7	20.3	19.3
Loans and advances	42.1	51.8	57.4	48.3	40.2
Total	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

Further assessment of asset quality can be facilitated by reference to note 37 to the consolidated financial statements on the fair value of financial instruments. Based on the valuation methodologies set out in that note, the net fair values of all on- and off-balance sheet financial instruments at 31st December 2011 were not significantly different to their carrying amounts. All non-trading securities are classified as available-for-sale and measured at fair value. Investment securities are accordingly stated at fair value in the consolidated balance sheet.

At the 2011 year end, cash and other liquid assets, reverse repos and placements accounted for 39 per cent of total assets, investment securities accounted for 19 per cent, while loans and advances represented 40 per cent.

Investment Securities

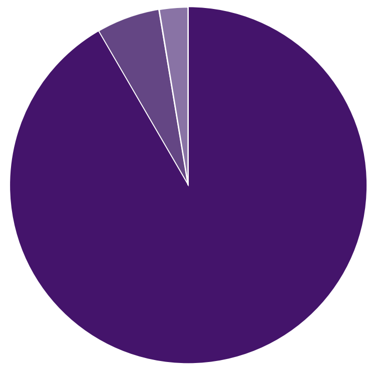
Investment securities totalled US$3,151.7 million at 31st December 2011. The investment securities portfolio, which is entirely classified as available-for-sale, primarily represents the Group's liquidity reserve and accordingly principally comprises investment grade-rated debt securities issued by major international and regional financial institutions and government-related entities.

An analysis of the basis used for determining the fair values of investment securities is set out in note 37 to the consolidated financial statements. At 31st December 2011, US$3,016.5 million or 99 per cent of investment securities that were valued at fair value, were valued based on quoted prices, while an additional US$107.0 million was valued based on cost less provisions for impairment. Only US$28.2 million was based on other valuation techniques. This represented private equity fund investments for which the fair values were based on the net asset values of the funds. No fair values of available-for-sale securities were derived from modelled-based valuation methodologies.

Investment securities comprise two types of debt security portfolios and a limited investment in equities and equity funds. The larger debt security portfolio comprises floating rate securities or fixed rate securities that have been swapped to yield constant spreads over LIBOR. These accounted for US$1,901.0 or two thirds of the total investment debt securities at the 2011 year end. The smaller debt security portfolio represents the investment of the Group's net free capital in fixed rate securities. This portfolio amounted to US$947.8 million at the end of 2011 and comprised investments in OECD and GCC government-related bonds. The Group had no exposure to troubled eurozone government debt, i.e. no exposure to Greek, Irish, Italian, Portuguese or Spanish government debt.

Equity investments at the end of 2011 amounted to US$302.9 million. Equity investments at 31st December 2011 included listed equities amounting to US$148.6 million received in settlement of a secured past due loan. The remaining equity investments largely comprised private equity-related investments.

Investment debt securities rating profile



	US$ millions	%
AAA to A-/Aaa to A3	2,610.1	91.6
BBB+ to BBB-/Baa1 to Baa3	163.6	5.8
Other debt securities	75.1	2.6
Total	**2,848.8**	**100.0**

An analysis of the investment securities portfolio by rating category is set out in note 9(a) to the consolidated financial statements. US$2,610.1 million or 92 per cent of the debt securities at the 2011 year end were rated A- or above. Based on the rating of the issuer, a further US$163.6 million or 6 per cent of the debt securities represented other investment grade-rated securities. Thus 98 per cent of the total debt securities comprised investment grade-rated securities.

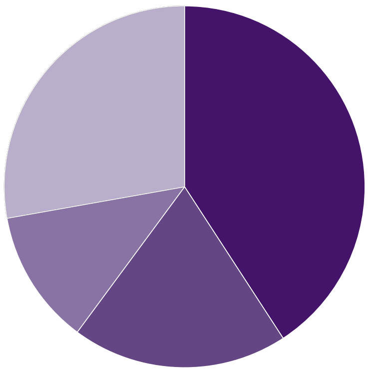
Other debt securities, the issuers of which are rated below BBB-/Baa3 or are unrated, amounted to US$75.1 million at the end of 2011, thus comprising only 2 per cent of the total investment debt securities portfolio. These largely comprised securities issued by unrated GCC entities.

There were no past due securities at 31st December 2011.

Impaired investment securities, representing securities against which a specific provision is maintained, amounted to only US$74.5 million at 31st December 2011. They comprised investments in managed funds that are closed to redemption for the foreseeable future, and private equity investments. The total specific provisions for impairment at 31st December 2011, amounting to US$58.2 million, represented 78 per cent of the gross impaired investment securities. The Group also held non-specific portfolio provisions of US$13.7 million at the 2011 year end.

Financial Review (continued)

Loan maturity profile



		US$ millions	%
	Year 1	2,754.8	40.8
	Years 2 & 3	1,306.1	19.3
	Years 4 & 5	814.6	12.1
	Over 5 years	1,876.3	27.8
	Total	**6,751.8**	**100.0**

Loans and Advances

Loans and advances amounted to US$6,751.8 million at the 2011 year end. This represented a US$758.3 million or 10 per cent decrease compared to the 2010 year end. 94 per cent of the loan portfolio at the 2011 year end represented lending within GIB's core market in the GCC states.

Based on contractual maturities at the balance sheet date, 41 per cent of the loan portfolio was due to mature within one year while 60 per cent was due to mature within three years. Only 28 per cent of loans were due to mature beyond five years. Details of the classification of loans and advances by industry are set out in note 10(a) to the consolidated financial statements, while the geographical distribution of loans and advances is contained in note 28. At 31st December 2011, 38 per cent of the gross loan portfolio comprised exposure to the energy, oil and petrochemical sector. This reflects the Group's previous strategic focus on project finance and syndicated lending in the GCC states.

The credit risk profile of loans and advances, based on internal credit ratings, is set out in note 27(a) to the consolidated financial statements. US$4,224.1 million or 63 per cent of total loans were rated 4- or above, i.e. the equivalent of investment grade-rated. Only US$276.8 million or 4 per cent of loans and advances were classified as individually impaired. Individually impaired loans represent loans for which there is objective evidence that the Group will not collect all amounts due in accordance with the contractual terms of the obligation. Therefore, 96 per cent of loans and advances were not individually impaired.

Total loan loss provisions at 31st December 2011 amounted to US$619.2 million. Counterparty specific provisions amounted to US$409.2 million while non-specific provisions were US$210.0 million. Total provisions of US$619.2 million represented 125 per cent of the gross book value of unsecured past due loans.

Specific provisions are determined based on the recoverable amount of the loan. The recoverable amount is measured as the present value of the expected future cash flows discounted based on the interest rate at the inception of the facility. Non-specific provisions are determined on a portfolio basis utilising an incurred loss model. The incurred loss model estimates the probable losses inherent within the portfolio at the balance sheet date but that have not been specifically identified. The model is based on applicable credit ratings and associated historical default probabilities, loss severity and rating migrations, and reflects the current macroeconomic, political and business environment and other pertinent indicators.

Non-specific loan provisions at 31st December 2011 amounted to US$210.0 million, representing a high 3.1 per cent of non-specifically provisioned loans. The probabilities of default applied in the calculation of the non-specific provisions at 31st December 2011 equated to a speculative-grade default rate of 13.9 per cent, exceeding the previous highest corporate default rates witnessed in July 1991. The default rates applied in the calculation of the non-specific loan provision and the resultant provisioning levels for senior, unsecured exposure by internal rating category were as follows:-

Internal rating grade	Probability of default (PDs)	Senior, unsecured provisioning level
1	0.03%	-
2+	0.03%	-
2	0.03%	-
2-	0.06%	-
3+	0.18%	0.1%
3	0.24%	0.1%
3-	0.36%	0.2%
4+	1.02%	0.6%
4	1.05%	0.6%
4-	1.29%	0.8%
5+	2.25%	1.4%
5	3.48%	2.1%
5-	6.21%	3.7%
6+	9.87%	5.9%
6	27.93%	16.8%
6-	39.45%	23.7%
7	83.61%	50.2%

The provisioning level is based on a Loss Given Default (LGD) of 60 per cent for senior, unsecured exposure.

For the purpose of the calculation of the non-specific provision, the Group only takes account of collateral held in the form of

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cash or exchange-traded equities. While collateral in the form of securities, unlisted equities and physical assets is used for risk mitigation and protection purposes, it is not taken into account in the calculation of the non-specific provision.

The gross and net book values of unsecured past due loans at 31st December 2011 amounted to US$496.1 million and US$238.0 million respectively. The specific provisioning coverage for unsecured past due loans was therefore 52 per cent. Net unsecured past due loans of US$238.0 million included US$99.2 million of loans that were subject to restructuring programmes and for which interest was current and being paid on due dates. The restructurings were all at an advanced stage and expected to be finalised within the first half of 2012, following which the loans will revert to performing status.

The restructuring programmes are not anticipated to result in an economic loss for the Group. Excluding the past due loans that were under restructuring and current, other net unsecured past due loans were only US$138.8 million, representing 2 per cent of total net loans. Past due loans are defined as those loans for which either principal or interest is over 90 days past due. Under IAS 39, interest on impaired loans should be recognised in income based on the net book value of the loan and the interest rate that was used to discount the future cash flows for the purpose of measuring the recoverable amount. However, in accordance with guidelines issued by the Group's regulator, the CBB, interest on past due loans is only to be recognised in income on a cash basis. In view of the Group's high provisioning coverage for impaired loans, the difference between the two bases of accounting is not material.

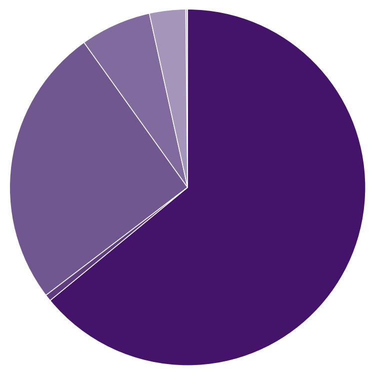
Other Asset Categories

Cash and other liquid assets, amounting to US$858.7 million at the 2011 year end, are analysed in note 5 to the consolidated financial statements. They principally comprised cash and balances with banks, government bills, and certificates of deposits held for liquidity management purposes.

Placements totalled US$5,394.0 million at the 2011 year end and were well diversified by geography as illustrated in note 28 to the consolidated financial statements. Placements were largely with GCC and European bank counterparties, representing the Group's two principal operating locations. Placements represented 32 per cent of total assets at the 2011 year end. A high level of placements was being maintained in the prevailing uncertain and volatile market environment. At the end of 2011, placements were supplemented by US$280.0 million of securities purchased under agreements to resell. These represented collateralised placements.

Trading securities at US$83.7 million comprised investments in managed funds, providing exposure to emerging market government-related debt and alternative investments. During 2011, the Group's investments in hedge funds continued to reduce and were only US$4.0 million at the end of 2011. The Group is continuing to reduce its investments in hedge funds with the intention of fully exiting the investments at the earliest possible opportunity.

Risk asset and commitment exposure



	US$ millions	%
GCC	12,867.4	64.1
Other MENA countries	120.4	0.6
Europe	5,114.6	25.5
North America	1,293.6	6.4
Asia	670.2	3.3
Latin America	22.7	0.1
Total	**20,088.9**	**100.0**

Risk Asset and Commitment Exposure

Risk asset and commitment exposure at 31st December 2011 amounted to US$20,088.9 million. Risk assets and commitments comprise all assets included in the balance sheet (with the exception of other assets) and credit-related contingent items. As referred to earlier, an analysis of risk asset and commitment exposure by category and geography is contained in note 28 to the consolidated financial statements. As is evident from this note, US$12,867.4 million or 64 per cent of total risk assets and commitments represented exposure to counterparties and entities located in the GCC states. The remaining risk asset exposure largely represented short-term placements with major European banks. An analysis of derivative and foreign exchange products is set out in note 31 while a further analysis of credit-related contingent items together with their risk-weighted equivalents is contained in note 32.

FUNDING

Bank and customer deposits at 31st December 2011 totalled US$10,069.6 million. Customer deposits amounted to US$8,520.3 million at the 2011 year end, representing 85 per cent of total deposits. A lower funding requirement resulting from deleveraging initiatives, including a managed reduction in the loan portfolio, as well as proactive actions to reduce undue depositor concentrations contributed to a reduction in the Group's funding requirements and a resultant decrease in less stable bank deposits. Bank deposits at 31st December 2011 amounted to US$1,549.3 million, representing only 15 per cent of total deposits.

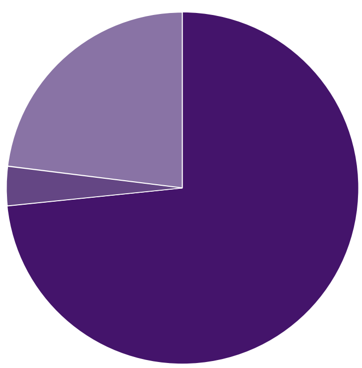
Financial Review (continued)

Total deposits are analysed by geography in note 13 to the consolidated financial statements. US$7,387.4 million or 73 per cent of total deposits were derived from counterparties in GCC countries. Deposits derived from non-MENA countries, principally Europe, amounted to US$2,317.9 million or 23 per cent of total deposits. The deposits from counterparties in non-MENA countries largely related to deposit activity by the Bank's London-based subsidiary, Gulf International Bank (UK) Limited. These deposits do not represent a core funding source for the Group. This compares to placements with non-MENA counterparties of US$4,537.7 million and are placed on a short-term basis in the money market. The Group is therefore a net placer of funds in the international interbank market, and accordingly has no net reliance on the international interbank market.

Securities sold under agreements to repurchase (repos) were US$283.3 million at 31st December 2011. The Group utilises its high quality and highly rated investment securities to raise funding on a collateralised basis where effective from a cost and tenor perspective, as well as constantly validating its ability to repo the securities as part of the Group's liquidity contingency plans.

There was a significant reduction in repos during 2011 due to the generally lower funding requirement associated with the decrease in the loan volume and a policy in the prevailing uncertain market environment to have ready access to the Group's high quality investment security portfolio as a liquidity reserve.

Deposits - geographical profile



	US$ millions	%
GCC countries	7,387.4	73.4
Other MENA countries	364.3	3.6
Other countries	2,317.9	23.0
Total	**10,069.6**	**100.0**

Senior term financing at 31st December 2011 totalled US$3,690.3 million. New senior term finance of US$900.3 million was raised during 2011. This included a US$500.0 million five year term deposit from the Group's majority shareholder, the Public Investment Fund, and a US$300.0 million three year Sukuk issued on a private placement basis to institutional investors. The new term finance was raised in advance of maturities in 2012, amounting in total to US$1,756.8 million. Further commentary on liquidity and funding is provided in the Basel 2 Pillar 3 report.

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Rising to the challenge

Corporate Governance Statement

SOUND GOVERNANCE PRACTICES

When GIB was established in 1975, its Agreement of Establishment and Articles of Association, subscribed at the time by the GCC Governments that created it, set the foundation of solid governance practices for the Bank. From the start, sound corporate governance has been essential at GIB, both in achieving organisational integrity and efficiency as well as in attaining fairness for all stakeholders.

Over the years, GIB has progressively adopted and implemented standards of corporate governance relevant to publicly-traded financial institutions although it is not a listed company, and since 2003 GIB has regularly published a statement on corporate governance in its Annual Reports.

In 2010, when the Central Bank of Bahrain (CBB) introduced new corporate governance requirements for banks in Bahrain, GIB had already put in place many measures that are hallmarks of good corporate governance practices, such as comprehensive mandates for the Board of Directors, for directors and for Board committees, a Code of Conduct (Code on Conduct, Ethics and Avoiding Conflicts of Interest) in both English and Arabic published on the Bank's website, a detailed Corporate Policy Manual and operating policies that anticipated the CBB's new requirements.

In 2011, GIB adopted additional measures that included, amongst other things, a new Board Charter, updated mandates for the Board committees, a new Whistle-blowing Programme that enhances the whistle-blowing provisions already existing in the GIB Code of Conduct, a review of the classification of directors and a realignment of Board committees.

In March 2011, the Board of Directors prepared for its shareholders' Annual General Meeting (AGM), and for the CBB, a report on GIB's compliance with the new CBB rules on corporate governance, which explained any non-compliance. A similar "Comply or Explain" report was also produced for this year's AGM, and it will be an item on the agenda of future shareholders annual general meetings. The explanations contained in this year's "Comply or Explain" report are also reproduced at the end of this section of the Annual Report. GIB is of course also disclosing in this Annual Report the additional information required to be disclosed in annual reports in accordance with Section PD-1.3.8 of the CBB Rulebook, and the Board is also disclosing to the Shareholders the information to be disclosed to them annually under Section PD-6.1.1 of the Rulebook.

2011 ACCOMPLISHMENTS

GIB implemented during 2011 several measures to enhance its corporate governance practices.

Foremost among these was the adoption of the new Board Charter, which was approved by the Board in 2011. This Charter replaces the previous mandate of GIB's Board of Directors, the mandate of the directors, the Chairman's mandate and the mandate of the Committees' Chairmen. The Board Charter is posted in its entirety on the Bank's website (www.gibonline.com) and by itself largely reflects a substantial proportion of the corporate governance requirements contained in Module HC of the CBB Rulebook.

The mandates of the Board committees were also reviewed and updated where necessary during 2011. Most significantly, the Audit Committee's mandate was revised and expanded to also include corporate governance responsibilities.

Also in 2011, the former Human Resources & Compensation Committee was re-designated the Nomination & Remuneration Committee with a revised mandate as approved by the Board. The revised mandate includes updated responsibilities with regards to remuneration, retention and termination of senior management, performance reviews of individual directors and of the Board as a whole, of senior executives and of management, as well as succession planning for senior management.

In line with the Board-approved Code of Conduct, the Bank also instituted in 2011 an enhanced Whistle-blowing programme available to all staff on the Bank's intranet. During the year GIB continued to strengthen its corporate governance framework by increasing the awareness and understanding of directors, management and staff of this important topic through a series of presentations conducted by the Compliance unit.

The measures adopted by GIB in 2011 formally entrench a culture of professional corporate governance in the organisation. They also demonstrate GIB's commitment to financial transparency, fairness and disclosure of financial information that will benefit all users of such information, including regulators, customers, counterparties, rating agencies and other stakeholders.

STRATEGY & OBJECTIVES

Throughout 2011, the Board and management with the help of external consultants began the implementation phase of the new business model and strategy that were developed and articulated in 2010. Under the new strategy, GIB will be transforming itself into a pan-GCC universal bank, based on four main pillars: corporate banking, investment banking, asset management and retail banking. The new institution will benefit from more diversified and stable funding and additional revenue streams, thus reducing volatility and minimising the effects of external shocks.

A key objective of the Bank's new business model and strategy is to provide shareholders with an enhanced return on equity that will be competitive with the Bank's peers.

SHAREHOLDERS

The current shareholding structure of GIB is as follows:

Name of Shareholder	Percentage of Shareholding
Public Investment Fund, Kingdom of Saudi Arabia	97.226%
Kuwait Investment Authority, State of Kuwait	0.730%
Qatar Holding Company, State of Qatar	0.730%
Bahrain Mumtalakat Holding Company, Kingdom of Bahrain	0.438%
Ministry of Finance, Sultanate of Oman	0.438%
Emirates Investment Authority, United Arab Emirates	0.438%

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ORGANISATION – RULES AND ROLES

GIB maintains a corporate governance structure that delineates and segregates the functions, roles and responsibilities of the Board of Directors and management, and ensures that the requisite separate attribution of responsibilities between them is maintained:

- There is an effective and appropriately constituted Board of Directors responsible for the stewardship of the Bank and the supervision of its business; it receives from management all information required to properly fulfill its duties and the duties of the committees that assist it, and it delegates to management the authority and responsibility for managing the day-to-day business of the Bank.
- There is an effective and appropriately organised management structure responsible for the day-to-day management of the Bank and the implementation of Board-approved strategy, policies and controls.
- There is a clear division of roles and responsibilities between the Board of Directors and management, and between the Chairman and the Chief Executive Officer (CEO).
- There are defined and documented mandates and responsibilities (as well as delegated authorities where applicable) for senior management.

The Bank's corporate governance structure and organisation chart is set out on page 31 of this Annual Report.

BOARD OF DIRECTORS

In accordance with GIB's Articles of Association, directors are appointed by the Bank's shareholders who also have the right to terminate such appointments and replace the relevant directors.

The Board comprises seven non-executive directors, including the Chairman and Vice-Chairman, who together, bring a wide range of skills and experience to the Board. Their biographies are set out on page 32 of this Annual Report.

Independence of Directors

The independence or non-independence of the directors is subject to an annual review by the Board of Directors. As at 31st December 2011, two directors of the Bank were classified as non-independent in accordance with the CBB regulations, and the other directors were classified as independent (see table on page 24 of this Annual Report).

Board Responsibilities

The Board is responsible for the overall business performance and strategy of the Bank.

The Board establishes the objectives of the Bank, the adoption and annual review of strategy, the management structure and responsibilities, and the systems and controls framework. It monitors management performance, and the implementation of strategy by management, keeps watch over conflicts of interest and prevents abusive related party transactions.

The Board is also responsible for the preparation and fair representation of the consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal controls as the Board determines is necessary to enable the preparation of the consolidated financial statements that are free from material misstatement, whether due to fraud or error.

The Board also convenes and prepares the agenda for shareholders meetings, and assures equitable treatment of shareholders including minority shareholders.

Finally, the Board delegates to management the responsibility for the day-to-day management of the Bank in accordance with policies, guidelines and parameters set by the Board.

Letters of appointment are issued to newly appointed directors that iterate three important points:

- Reminding them that as directors they are responsible for contributing to the oversight of the Bank's affairs with professionalism and integrity, with the aim of achieving the strategic and financial objectives adopted by the Board.
- Pointing out that a key responsibility of the Board is to fill the gap between stakeholders (shareholders, creditors, employees, depositors, investment account holders, etc.) to whom the Board owes a duty of care, and executive management, by monitoring management closely on behalf of stakeholders.
- Drawing attention to the fact that a detailed description of directors' responsibilities is outlined in the Board Charter and that these responsibilities are to be carried out in line with the standards of the Code of Conduct adopted by the Board.

In preparation for Board and committees meetings, the directors receive, in a timely manner, regular reports and all other information required for such meetings, supplemented by any additional information specifically requested by the directors from time to time. The directors also receive monthly financial reports and other regular management reports that enable them to evaluate the Bank's and management's performance against agreed objectives. As prescribed in GIB's Articles of Association, the Board plans at least four meetings per year, with further meetings to occur at the discretion of the Board.

Corporate Governance (continued)

The details of Board membership and directors' attendance during 2011 are set out in the following table.

Directors Attendance: January to December 2011

Board Members	Board Meetings	Executive Committee Meetings	Audit Committee Meetings	Nomination & Remuneration Committee Meetings	Risk Policy Committee Meetings	Executive/ Non-Executive	Independent/ Non-Independent
H.E. Jammaz bin Abdullah Al-Suhaimi Chairman	6 (6)	1 (2)		1 (1)*		Non-Executive	Independent
Mr. Mansour bin Saleh Al Maiman Vice Chairman	6 (6)	2 (2)*		5 (5)		Non-Executive	Non-Independent
H.E. Dr. Hamad bin Sulaiman Al-Bazai	6 (6)	2 (2)			4 (4)*	Non-Executive	Non-Independent
Dr. Abdullah bin Hassan Al-Abdul-Gader	6 (6)		5(5)*	5 (5)		Non-Executive	Independent
Mr. Sulaiman bin Abdullah Al-Hamdan	5 (6)	2 (2)			4 (4)	Non-Executive	Independent
Mr. Abdulla bin Mohammed Al Zamil	6 (6)		5(5)		4 (4)	Non-Executive	Independent
Mr. Khaled bin Saleh Al-Mudaifer	5 (6)		5(5)	5 (5)		Non-Executive	Independent

* Committee Chairman
Figures in brackets indicate the maximum number of meetings during the period of membership.

On 26th August 2009, all the directors were appointed (or re-appointed in the case of H.E Jammaz Al-Suhaimi and H.E. Dr. Hamad Al-Bazai) for a three-year term.

In October 2011 the Board of Directors passed a resolution to reconstitute the membership of the Nomination and Remuneration Committee (NRC). As a result, H.E. Jammaz Al-Suhaimi joined the NRC as Chairman, and Mr. Mansour Al Maiman was appointed Chairman of the Executive Committee.

BOARD COMMITTEES

The committees of the Board of Directors derive their authorities and powers from the Board. Details of committees' memberships and attendance are listed in the tables below.

Board Committees' Memberships

Board Committees	Member Name	Member Position
Executive Committee	Mr. Mansour bin Saleh Al Maiman	Chairman
	H.E. Jammaz bin Abdullah Al-Suhaimi	Member
	H.E. Dr. Hamad bin Sulaiman Al-Bazai	Member
	Mr. Sulaiman bin Abdullah Al-Hamdan	Member
Audit Committee	Dr. Abdullah bin Hassan Al-Abdul-Gader	Chairman
	Mr. Abdulla bin Mohammed Al Zamil	Member
	Mr. Khaled bin Saleh Al-Mudaifer	Member
Nomination & Remuneration Committee	H.E. Jammaz bin Abdullah Al-Suhaimi	Chairman
	Mr. Mansour bin Saleh Al Maiman	Member
	Dr. Abdullah bi n Hassan Al-Abdul-Gader	Member
	Mr. Khaled bin Saleh Al-Mudaifer	Member
Risk Policy Committee	H.E. Dr. Hamad bin Sulaiman Al-Bazai	Chairman
	Mr. Abdulla bin Mohammed Al Zamil	Member
	Mr. Sulaiman bin Abdullah Al-Hamdan	Member

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Board and Committee Meetings: January to December 2011

Type of Meeting	Meeting Dates
Board of Directors	1. 12th February 2. 31st March 3. 28th April 4. 26th July 5. 20th October 6. 10th December
Executive Committee	1. 27th February 2. 15th October
Audit Committee	1. 10th February 2. 21st April 3. 25th July 4. 19th October 5. 1st December
Nomination & Remuneration Committee	1. 13th January 2. 12th February 3. 21st May 4. 20th August 5. 15th October
Risk Policy Committee	1. 30th March 2. 25th July 3. 19th October 4. 9th December

Executive Committee

The mandate of the Executive Committee requires it, among other things, to:

- Assist the Board in formulating the executive policy of the Bank and controlling its implementation.
- Assist the Board by reviewing, evaluating, and making recommendations to the Board with regard to key strategic issues or material changes in key strategic objectives or direction.
- Approve credit limits that exceed the authority of the CEO subject to the limits approved by the Board.
- Carry out additional responsibilities specifically mandated to it by the Board.
- Exercise the powers of the Board on matters for which the Board has not otherwise given specific direction, in circumstances in which it is impossible or impractical to convene a meeting of the Board (and subject to applicable law and GIB's Agreement of Establishment & Articles of Association). However, the Board may, acting unanimously, modify or amend any decision of the committee.

In all cases, the members of the committee must exercise their business judgement to act in what they reasonably believe to be in the best interests of the Bank and its shareholders.

Audit Committee

In 2011, the mandate of the Audit Committee was updated to include additional corporate governance responsibilities. The committee is also responsible for:

- Assisting the Board in its oversight of (i) the integrity and reporting of the Bank's quarterly and annual financial statements, (ii) compliance with legal and regulatory requirements; and (iii) the qualifications, independence and performance of the Bank's internal and external auditors.
- Assisting the Board in fulfilling its statutory and fiduciary responsibilities with respect to internal controls, accounting policies, auditing and financial reporting practices.
- Overseeing performance of the Bank's internal audit function, independent audits and regulatory inspections.
- Overseeing the Bank's compliance with the rules of good corporate governance.

The mandate of the Audit Committee provides further particulars on financial reporting processes, process improvements, and additional ethical and legal compliance overview responsibilities. The Group Chief Auditor reports functionally to the Audit Committee and administratively to the CEO.

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Corporate Governance (continued)

In December 2011, the Audit Committee conducted an evaluation of its performance and of its major activities during the year, and submitted its report to the Board.

Risk Policy Committee

In 2011, the mandate of the Risk Policy Committee was reviewed and updated. The committee assists the Board in fulfilling its oversight responsibilities in respect of setting the overall risk appetite, parameters and limits within which the Bank conducts its activities. On an on-going basis the committee:

- Ensures that realistic policies in respect of management of all significant risks are drafted and approved appropriately.
- Receives, reviews, challenges and recommends for approval by the Board any proposed amendments to the overall risk appetite for the Bank.
- Monitors whether management maintains a culture that rewards the recognition, communication and management of risks.
- Ensures that roles and responsibilities for risk management are clearly defined, with group and/or division heads directly responsible, and that heads of risk management and the control functions are in supporting or monitoring roles, independent of business development.
- Ensures that management reports significant excesses and exceptions, as and when they arise, to the committee for information and review.
- Ensures that, on a timely basis, management informs the committee of all significant risks arising and that it is comfortable with management's responses and actions taken to address such findings.
- Reviews the Bank's risk profile and significant risk positions and in so doing:
    - Receives reports on credit exposure by country, credit grade, industry/concentration and segment for the period under review.
    - Receives reports on the market risk positions (VaR) for the period under review.
    - Receives reports on changes to credit approvals or extension processes, credit risk measurement, market risk measurement and risk control measures.

Nomination & Remuneration Committee

In 2011, the Human Resources & Compensation Committee was re-named the Nomination & Remuneration Committee with a revised mandate approved by the Board. The principal objectives of the committee, as set out in its mandate, are to review and make recommendations to the Board in respect of:

Nomination Matters

- Assessing the skills and competencies required on the Board, the committees of the Board and senior management.
- Assessing from time to time the extent to which the required skills are represented on the Board and senior management.
- Establishing processes for reviewing the performance of the individual directors and the Board as a whole.
- Establishing processes for reviewing the performance of the individual senior executives and senior management as a whole.
- Establishing processes for the identification of suitable candidates for senior management and identifying and recommending individuals qualified to become members of senior management.
- Establishing a succession plan for senior management.

Remuneration Matters

The committee's objectives, as stated in its mandate, also include reviewing and making recommendations to the Board in respect of (among other things):

- The executive remuneration and incentive policy.
- The remuneration of the CEO.
- The executive incentive plan.
- The remuneration of directors.

EVALUATION OF THE BOARD OF DIRECTORS

The mandate of the Nomination & Remuneration Committee, as well as the Board Charter, reflect the requirement that the Board must conduct an evaluation of its performance and the performance of each committee and of each individual director at least annually. The Board reviewed independent performance reports from each of its Committees as well as a report on its own performance by evaluating the major activities undertaken during the year in comparison with the respective mandates. For individual Directors (as explained at the end of this section of the Annual Report), an evaluation tool was presented to the Nomination & Remuneration Committee for its review, which includes measurable rating scales, self-evaluations and the Chairman's input. The revised evaluation process of individual directors is expected to be implemented in 2012.

INDUCTION & CONTINUING EDUCATION OF DIRECTORS

When the current directors were appointed on 26 August 2009 (two of them were in fact re-appointed on that date) for a three-year term, they were provided with an orientation that included a presentation and a binder prepared by the Compliance Department containing their individual Letter of Appointment, the Mandates of the Board and of its Committees, the Mandate of Directors, the GIB Code of Conduct (Code on Conduct, Ethics and Avoiding Conflicts of Interest), the GIB Policy on Insider Trading, Chinese Walls & Personal Account Dealing, and the CBB Principles of Business.

When the CBB introduced new rules on Corporate Governance in October 2010 dealing specifically with Board responsibilities, the directors were provided in December 2010, in October 2011 and in December 2011 with progressive updates on this subject matter. This demonstrates the importance that the Board gives to this topic.

The Board also stresses the importance of providing training and development opportunities for the directors. In 2009 the Board passed a resolution to encourage directors to seek any training they deem necessary (with the Bank bearing the expenses of such training), and the directors are frequently briefed on the availability of training opportunities.

MANAGEMENT

The senior management team is responsible for the day-to-day management of the Bank entrusted to it by the Board. It is headed by the CEO, who is assisted by the Managing Director-Chief Financial Officer, the Managing Director-Chief Risk Officer, the Managing Director-Wholesale Banking, the Managing Director-Retail Banking, the Managing Director-Head of Operations, Administration and IT, the Chief Investment and Treasury Officer and the Chief Human Resources Officer. The biographies of the members of the senior management team are set out on page 33 of this Annual Report.

Eight committees assist the CEO in the management of the Bank:

- Management Committee
- Strategy Steering Committee
- Group Risk Committee
- Assets and Liabilities Committee (ALCO)
- Human Resources Committee
- Information Technology Steering Committee
- Information Security Management Committee
- Operational Risk Committee

These committees derive their authorities from the CEO, based on the authorities and limits delegated by the Board of Directors.

In fulfilling its principal responsibility for the day-to-day management of the Bank, the senior management team is required to implement Board-approved policies and effective controls, within the strategy and objectives set by the Board.

Letters of appointment are issued to members of the senior management team setting out their specific responsibilities and accountabilities that include assisting with and contributing to the following:

- Formulation of the Bank's strategic objectives and direction.

- Formulation of the Bank's annual budget and business plan.

- Ensuring that high-level policies are in place for all areas and that such policies are fully applied. The setting and management of risk/return targets in line with the Bank's overall risk appetite.

- Determining the Bank's overall risk-based performance measurement standards.

- Reviewing business units' performance and initiating appropriate action.

- Ensuring that the Bank operates to the highest ethical standards and complies with both the letter and spirit of the law, applicable regulations and codes of conduct.

- Ensuring that the Bank is an exemplar of good business practice and customer service.

Their attention is also drawn to the fact that these obligations are in addition to their specific functional responsibilities and objectives, and those set out in the Bank's Corporate Policy Manual.

COMPENSATION

The Bank remunerates its directors and officers fairly and responsibly. As per the Board Charter, the remuneration of directors and officers must be sufficient to attract, retain and motivate persons of the quality needed to run the Bank successfully, and the Bank must avoid paying more than is necessary for that purpose. The Board has approved a remuneration policy which includes a policy on performance-based incentive plans, for submission to Shareholder approval at the 2012 AGM.

Staff Compensation

GIB has established a comprehensive staff compensation policy based on total compensation that is in line with industry best practice. This was done in consultation with external independent remuneration consultants.

The scheme consists of the following for all staff except the CEO:

- A fixed component representing basic pay, allowances and benefits, which are reviewed and compared annually with market levels, based on an independent market survey and adjusted as appropriate.

- A variable component representing a performance-related award linked to the performance of the Bank, the contribution of the relevant unit and the individual's personal performance. The scheme is based on defined quantitative as well as qualitative measures.

- Based on established criteria, the performance bonus of senior management is recommended by the CEO for review and endorsement by the Nomination & Remuneration Committee, subject to Board approval.

CEO Compensation

- The CEO is appointed by the Board of Directors for a term of three years. Renewal is considered prior to the expiration of each term.

- The fixed compensation components are negotiated and determined at the time of renewal, with assistance and input from independent external compensation evaluation experts.

Corporate Governance (continued)

- The performance bonus of the CEO is recommended by the Nomination & Remuneration Committee, and approved by the Board-based on the established scheme mechanism approved by the Board.

Board of Directors Compensation
To assist with establishing the appropriate structure and level of compensation, independent external consultants advise on market practice and provide suggestions on Board compensation. The compensation is linked to actual attendance of meetings. The structure and level of the compensation for the members of the Board of Directors are approved by the AGM and consist of the following:

- Attendance fees payable to members attending different Board-related committees' meetings.

- Allowance to cover travelling, accommodation and subsistence, while attending Board and related committees' meetings.

- A pre-defined fixed amount representing an annual remuneration fee.

In 2011, the aggregate remuneration paid to Board members and senior management was US$7.0 million of which US$0.97 million was paid to the Board members.

CORPORATE COMMUNICATIONS

The Bank has in place a Corporate Communications Policy which ensures that the disclosures made by GIB are fair, transparent, comprehensive and timely, and reflect the character of the Bank and the nature, complexity and risks inherent in its business activities. Main communications channels include the Annual Report, corporate brochures, staff newsletters, and announcements in the appropriate media.

This transparency is also reflected in the Bank's website (www.gibonline.com) that provides substantial information on the Bank, including its profile and milestones; vision, mission, values, strategy and objectives; its financial statements; and its press releases.

CODE OF CONDUCT

The Bank's website also contains the Board-approved Code of Conduct that contains rules on conduct, ethics and on avoiding conflicts of interest, applicable to all the employees and directors of the Bank. The Code of Conduct is designed to guide all employees and directors through best practices to fulfill their responsibilities and obligations towards the Bank's stakeholders (shareholders, clients, staff, regulators, suppliers, the public, the host countries in which the Bank conducts business, etc.), in compliance with all applicable laws and regulations.

The Code addresses such issues as upholding the law and following best practices; acting responsibly, honestly, fairly and ethically; avoiding conflicts of interest; protecting Bank property and data; protecting client confidential information and safeguarding the information of others; complying with inside information rules and with the prohibition on insider trading; preventing money laundering and terrorism financing; rejecting bribery and corruption; avoiding compromising gifts; as well as speaking up and 'whistle-blowing.'

In addition, in 2011 GIB set up a new Whistle-blowing Programme that enhances the whistle-blowing provisions already existing in the GIB Code of Conduct, and the programme is easily accessible by members of staff on the Bank's intranet.

All employees and directors of the Bank are reminded every year of their obligations under the Code of Conduct by means of an email from the Bank that includes a copy of the Code of Conduct (in English and Arabic) and everyone is required to sign an Acknowledgment and Declaration confirming that they have received and read the Code of Conduct, understand its requirements, have followed and will continue to follow these requirements, and agree that if they have any concern about any possible misconduct or breach of the Code of Conduct they will raise the concern with the appropriate persons within the Bank as per the Code.

In addition, all employees of the Bank must sign an annual declaration on outside employment and other activities, to ensure that no conflicts of interest exist. These declarations are addressed to the Bank's Human Resources department. Similarly, all directors and members of the Management Committee must complete and sign a similar annual Declaration, addressed to the Audit Committee of the Board.

DISCLOSURES

The Bank's website also provides access to GIB's Annual Reports, and all the information contained in these reports is therefore accessible globally. That information includes management discussion on the business activities of the Bank, as well as discussion and analysis of the financial statements and risk management. The financial information reflects the latest international accounting standards requirements, including the increased level of disclosure resulting from the adoption of International Financial Reporting Standard No. 7 – Financial Instruments Disclosures, such as the disclosures on related party transactions in note 36 to the consolidated financial statements available on USB.

The Board-approved Disclosure Policy is in accordance with the requirements of Basel 2 Pillar 3, in compliance with CBB rules. The objective of this Policy is to ensure transparency in the disclosure of the financial and risk profiles of the Bank to all interested parties.

POLICY ON CONNECTED COUNTERPARTIES

The Board-approved Policy on Connected Counterparties governs GIB's dealings with such parties. The Policy defines which parties are considered to be connected with GIB within the criteria set by the CBB and imposes not only the limitations placed by the CBB but also additional criteria imposed by GIB. The policy sets out the internal responsibilities for reporting GIB's connected counterparties exposures to the CBB, and the disclosures to be made in GIB's financial statements and Annual Reports, in line with applicable disclosure requirements.

POLICY ON RELATED PARTY TRANSACTIONS

GIB has a Board-approved policy for the approval of related party transactions. The Bank's dealings with its shareholders are conducted on an arms-length basis in respect of its exposure to and deposits received from them. If loans are extended to related parties, these are approved on the basis of authorities delegated by the Board of Directors to the CEO. If the loans exceed these authorities, then further approval from the Executive Committee or the Board is requested. The Bank will not deal with any of its directors in a lending capacity. Any deposit received from GIB directors will be treated on an arms-length basis with rates of interest in line with those prevailing in the market. It should be noted that Article 16 of the Articles of Association prevents directors of the Bank from having any interest, directly or indirectly, in any contract with the Bank.

All loans to senior management members (including the CEO and his direct reports), as well as staff of GIB, are governed by the policies applicable to staff. These policies are reviewed by the Nomination & Remuneration Committee of the Board at least annually. No deposits are accepted from senior management. All dealings with companies associated with a GIB director or member of the senior management are referred to the Board of Directors for approval.

MATERIAL TRANSACTIONS THAT REQUIRE BOARD APPROVAL

The Bank has delegated credit authority to the CEO based on a risk-rating matrix. When considering transactions, any exposure to an entity that exceeds the CEO's limit will require the approval of the Board Executive Committee or the Board of Directors.

COMPLIANCE

The Compliance framework adopted by the Board reflects the principles for promoting sound compliance practices at GIB. It also demonstrates the Bank's adherence to applicable legal and regulatory requirements and to high professional standards. The role of the Compliance function is to assist senior management to ensure that the activities of GIB and its staff are conducted in conformity with applicable laws and regulations, and generally with sound practices pertinent to those activities. The Head of Compliance (Bahrain), who reports directly to the CEO, also has access to the Board of Directors through the Audit Committee, if required.

In ensuring that the tone emanates from the top, the CEO issues a yearly message to all of GIB employees reminding everyone of the importance of complying with all laws and regulations applicable to GIB's operations; good compliance behaviour is also rewarded by making it a mandatory measurement item in staff evaluations.

ANTI-MONEY LAUNDERING

The Bank's current anti-money laundering and combating the financing of terrorism (AML/CFT) procedures and guidelines in place at GIB conform to the legal and regulatory requirements of the Kingdom of Bahrain. These legal and regulatory requirements largely reflect the FATF recommendations on Money Laundering and special recommendations on terrorism financing. The GIB AML/CFT procedures and guidelines apply to all of the Bank's offices, branches and subsidiaries, wherever located. In addition, the GIB entities located outside Bahrain are subject to the laws and requirements of the jurisdictions where they operate, and if local standards differ, the higher standards apply.

Systems are in place to ensure that business relationships are commenced with clients whose identity and activities can reasonably be established to be legitimate, to collect and record all relevant client information, to monitor and report suspicious transactions, to provide periodic AML/CFT training to employees, and to review with external auditors the effectiveness of the AML/CFT procedures and controls. The GIB AML/CFT procedures prohibit dealing with shell banks.

A proactive structure of officers is in place to ensure group-wide compliance with AML/CFT procedures, and the timely update of the same to reflect the changes in regulatory requirements. This structure consists of the Head of Compliance (Bahrain) and the Group Money Laundering Reporting Officer, MLROs, and Deputy MLROs.

CORPORATE GOVERNANCE FRAMEWORK – AUDIT REVIEW

When the CBB introduced its new corporate governance rules in the Rulebook in October 2010, GIB's Internal Audit proactively added to its list of annual reviews the review of the GIB Corporate Governance framework which, until then, was reviewed by Internal Audit as part of other various examinations of business and control functions within the Bank.

Consequently, in October 2011 Internal Audit conducted a comprehensive review of the Bank's Corporate Governance framework. The purpose of the audit was to provide a level of assurance over the processes of corporate governance within the Bank. The scope of the audit included reviewing the existing policies, procedures and current practices followed by GIB in light of the CBB rules contained in the HC Module (High Level Controls) of the CBB Rulebook.

The overall conclusion of the audit review was that the Corporate Governance framework of GIB appears to be operating effectively and is providing a sound framework to control the risks inherent in GIB's current business activities.

The Internal Audit review of the GIB Corporate Governance framework is scheduled to be undertaken annually.

Corporate Governance (continued)

STATUS OF COMPLIANCE WITH THE NEW CBB RULES (MODULE HC)

GIB has implemented the new CBB rules on Corporate Governance outlined in Module HC of the CBB Rulebook, and instances of non-compliance in 2011 are explained as follows:

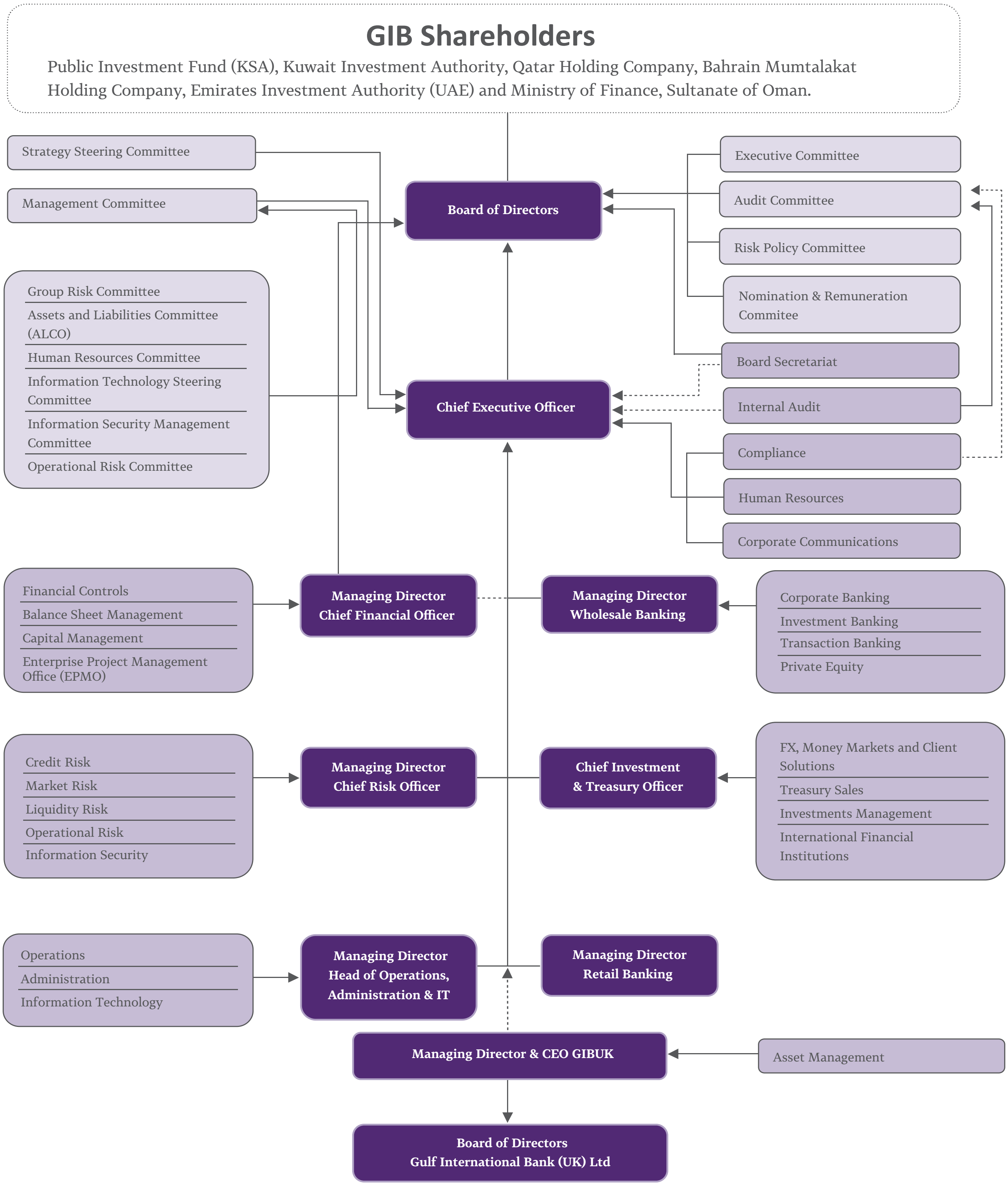
- Certain new Corporate Governance items will take effect by Q1 2012 (timed with the 2012 Annual General Meeting), namely the requirements under HC-5.2.1 and 5.6.6 that Shareholders' approval be obtained for the Bank's remuneration policy for approved persons and for the Bank's policy on performance-based incentives plans. Similarly, new written appointment agreements with each new or continuing Director will be issued at the time of their appointment or re-appointment, as required under HC-1.2.9.

- In response to the HC-1.9.1 requirement that at least annually the Board must conduct an evaluation of its performance and the performance of each committee and each individual director, this requirement has been reflected in the new Board Charter and in the Mandate of the Nomination & Remuneration Committee. The Board reviewed independent performance reports from each of its Committees as well as a report on its own performance by evaluating the major activities undertaken during the year in comparison with the respective mandates. For individual Directors, an evaluation tool was presented to the Nomination & Remuneration Committee for its review, and it includes measurables, rating scales, self-evaluations, and Chairman's input. The revised evaluation process is expected to be implemented in 2012.

- In response to the HC-6.2.1 and HC-6.3.4 requirements that senior management must include a corporate secretary who should be given general responsibilities for reviewing the Bank's procedures and advising the Board directly on such matters, the Bank intends to widen in 2012 the current mandate of the Secretary to the Board.

- Under Article 2 of GIB's Agreement of Establishment approved by Decree Law No. (30) for the year 1975 (as amended from time to time), GIB is subject to the Agreement of Establishment and its Articles of Association (the "AoA") (together the "GIB Constitutional Documents"), and in the event of any conflict between the GIB Constitutional Documents and the internal law of the Kingdom of Bahrain, the terms of the Constitutional Documents shall prevail. As a result, certain Corporate Governance requirements under HC-1 and HC-4 that are in conflict with the AoA such as the nomination of Directors, the attendance requirements for Directors and the prohibition against proxies at Board Meetings, have not been adopted.

Organisation and Corporate Governance Chart



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Biographies of The Board and Senior Management

BOARD OF DIRECTORS

H.E. Jammaz bin Abdullah Al-Suhaimi ❶ ❹
Chairman
H.E. Al-Suhaimi joined GIB as Chairman of the Board of Directors in 2008 and was re-elected in 2009 for three more years. Prior to that, he served between 2004 and 2006 as Chairman and Chief Executive of the Saudi Arabia Capital Market Authority, the regulatory body for the capital market in the Kingdom of Saudi Arabia. During the period 1989-2004, he was Deputy Governor of the Saudi Arabian Monetary Agency. He initially joined SAMA as Director-General for Banking Control. He also served as Deputy Director General of the Saudi Industrial Development Fund from 1982 to 1984. In November 2009, he was appointed Vice Chairman and Member of the Board of Directors of the Saudi Arabian Investment Company (Sanabil Investments). He has also held Board memberships in many leading public and private organisations including, the Saudi Arabian General Investment Authority, the General Petroleum and Minerals Organisation, the National Company for Cooperative Insurance and the London-based Saudi International Bank (which merged with GIB in 1999). H.E. Al-Suhaimi holds a Bachelor's degree in Electrical Engineering from the University of Washington in Seattle, USA.

Mr. Mansour bin Saleh Al Maiman ❶ ❹
Vice Chairman
Mr. Al Maiman joined GIB's Board of Directors in 2009. He is currently the Secretary General of the Public Investment Fund in Saudi Arabia (since 1998). Prior to that he was Assistant Deputy Minister for Budget and Administration (1993-1998). Mr. Al Maiman is a Board member of the Saudi Arabian Mining Company (Ma'aden), the Saudi Stock Exchange and Saudi Arabian Railways Company. Mr. Al Maiman holds a BA in Accounting and Business Administration from King Saud University (1973), and an MBA from the University of Dallas, USA (1980).

H.E. Dr. Hamad bin Sulaiman Al-Bazai ❶ ❸
H.E. Dr. Al-Bazai was appointed to GIB's Board of Directors in 1999. He is currently the Vice Minister of Finance for the Kingdom of Saudi Arabia. Prior to that he served as Deputy Minister of Finance for Economic Affairs. Dr. Al-Bazai is a Board Member of the Southern Region Cement Company and Tatweer Education Holding Company. He holds a BA in Administrative Sciences from King Saud University in Saudi Arabia and an MS and a Ph.D. in Economics from Colorado State University, USA.

Professor Abdullah bin Hassan Al-Abdul-Gader ❷ ❹
Professor Al-Abdul-Gader joined GIB's Board of Directors in 2009. He has been a Professor at King Fahd University of Petroleum and Minerals since 1981. Between 2004 and 2009, he was a Commissioner at the Saudi Arabia Capital Market Authority. He serves on a number of Boards of Directors and Audit Committees of public companies, including the Saudi Company for Development and Technology Investment, the Saudi Telecom Company, Riyad Bank, and Ma'aden. He contributes to the accounting/auditing profession through the Saudi Arabia Organization of Certified Public Accountants. He holds a BSc degree in Business Administration, an MBA from King Fahd University of Petroleum and Minerals, and a Ph.D. in Business Administration from the University of Colorado, USA.

Mr. Sulaiman bin Abdullah Al-Hamdan ❶ ❸
Mr. Al-Hamdan joined GIB's Board of Directors in 2009. Mr. Al-Hamdan is the Chief Executive Officer of National Air Services (NAS) in Saudi Arabia (since 2008). Prior to that he held various positions at the Saudi British Bank, including that of Deputy Managing Director and General Manager Personal Banking. He worked at the Saudi Fund for Development between 1979 and 1985. Mr. Al-Hamdan is a member of the Board of Directors of Middle East Specialised Cables (MESC) and Al Ahlia Cooperative Insurance Company. He holds a Bachelor of Arts in Administrative Science from King Saud University (1979) and an MBA from the University of New Haven, USA (1985).

Mr. Abdulla bin Mohammed Al Zamil ❷ ❸
Mr. Al Zamil joined GIB's Board of Directors in 2009. He is the Chief Executive Officer and board member of Zamil Industrial Investment Company "Joint Stock Company." He was the company's Chief Operating Officer from 2004-2009. Prior to that he was Senior Vice President at Zamil Air Conditioners. He started his career at Zamil Air Conditioners in 1987 as an industrial engineer. Mr. Al Zamil is a Board member of many companies, including Zamil Hudson Company, Armacell Zamil Middle East Company, Arabian Fiberglass Insulation Company, Gulf Electronic Management Systems Company, Zamil New Delhi Infrastructure Private Ltd. and Middle East Air Conditioners Company, in addition to his membership of the Eastern Province Chamber of Commerce. He holds a BA in Industrial Engineering from the University of Washington in USA (1987) and an MBA in Financial and Business Administration from King Fahd University of Petroleum and Minerals (1992).

Mr. Khaled bin Saleh Al-Mudaifer ❷ ❹
Mr. Al-Mudaifer joined GIB's Board of Directors in 2009. He is the President & CEO of Ma'aden. He joined Ma'aden in March 2006 as Vice President for Industrial Affairs. In 2007, he became Vice President for Phosphate and New Business Development. Prior to that, he was the Managing Director of Qassim Cement Company (1993-2006). Between 1987 and 1993, he held various positions in Eastern Petrochemical Company (Sharq- a SABIC affiliate) last of which as Vice President-Finance. Currently, he is Board and Executive Committee Member of Ma'aden and Saudi Arabian Railroad Company (SAR). Mr. Al-Mudaifer holds a BSc in Engineering (1984) and MBA (1987) from King Fahd University of Petroleum and Minerals.

❶ Executive Committee Member
❷ Audit Committee Member
❸ Risk Policy Committee Member
❹ Nomination & Remuneration Committee Member

SENIOR MANAGEMENT

Dr. Yahya A. Alyahya
Chief Executive Officer
Dr. Alyahya served on the Board of The World Bank Group as Executive Director representing Saudi Arabia from 1999 to 2006. During that period he served in many capacities, most notably as Dean of Executive Directors and Chairman of the Board Steering Committee (03-06); Chairman of the Personnel Committee and Member of the Budget Committee (02-03); Vice Chairman of the Audit Committee and Member of the Governance Committee (00-02). Prior to that Dr. Alyahya served as Advisor to the Governor, Saudi Arabian Monetary Agency (99); General Manager of E.A. Juffali & Bros. in Riyadh (94-99); Founder and Director General, The Institute of Banking, SAMA, in Riyadh (89-94); Professor of Industrial and Systems Engineering at King Saud University, Riyadh (86-89) and the University of Michigan, USA (83-86); Lecturer on Matching Problems and Algorithms at the Indian Statistical Institute, Bangalore, India (82); and a Project Analyst at the Saudi Industrial Development Fund, Riyadh (75). Dr. Alyahya has also served on the Boards and Board Committees of many organisations, most notably Saudi Re (first reinsurer in SA) (07-08), Gulf Investment Corporation (GIC) (06-08), National Commercial Bank (NCB) (08), Gulf International Bank (GIB) (99-01); Saudi Engineering Society (79-99); Audit Committee of AlBank AlSaudi AlFaransi (97-99) and Saudi Agricultural Bank (92-95). Dr. Alyahya holds a PhD in Industrial and Systems Engineering from The University of Michigan, Ann Arbor (83) and a graduate of the UPM (75). Currently, Dr. Alyahya is Chief Executive Officer of Gulf International Bank since January, 2009. He also chairs the Board of Shuaibah Water and Electricity Company (first IWPP in SA) and Shuaibah Expansion Project Company (SA), and a member of the Group of Twenty (G-20) High Level Panel on Infrustructure Investment (HLPII).

Mr. Stephen Williams
Managing Director - Chief Financial Officer
Chartered Accountant, Member of the Institute of Chartered Accountants in England and Wales (ICAEW). BSc Economics, University College Cardiff, UK. Mr. Williams joined GIB in 1987. He was appointed Group Financial Controller in 2000 and Chief Financial Officer in 2008. He is directly responsible for Groupwide statutory, regulatory and management reporting; financial and balance sheet planning; capital management, and GIB's Enterprise Project Management Office (EPMO). Mr. Williams was responsible for GIB's Basel 2 implementation project and was a member of the Institute for International Finance's (IIF) Working Group on Capital Adequacy. Mr. Williams is a member of GIB's Management Committee and Group Risk Committee and is the chairman of the Assets and Liabilities Committee. Prior to joining GIB, Mr. Williams worked for KPMG in London and the Middle East.

Mr. Adel Al-Mangour
Managing Director - Wholesale Banking
Mr. Al-Mangour joined GIB as Managing Director-Wholesale Banking in 2010. Previously, he held several senior positions including Chief Credit Officer at Arab National Bank in Saudi Arabia (2001-2010) and Vice President-Corporate Finance at J. P. Morgan Chase in Bahrain (1999-2001). Mr. Al-Mangour started his banking career at GIB in 1987 after completing his MBA. During his 12 years of service at the Bank, he worked in many areas including heading the Structured Finance Division.

Mr. Chris Berry
Managing Director - Retail Banking
Mr. Berry joined GIB as Managing Director-Retail Banking in 2010. Previously, he held several senior positions including General Manager at SABB in Saudi Arabia (2005-2007) and Executive Vice President at Emirates NBD in the UAE (2008-2010). Mr. Berry started his banking career with Lloyds TSB in 1979 and during 22 years of service, he worked in many areas of their domestic and offshore retail banking divisions culminating in his appointment as senior executive responsible for Operations and Customer Service Strategy of the International & Private Banking Division.

Mr. Jose Maria Marigomen
Managing Director - Chief Risk Officer
Mr. Marigomen joined GIB as Managing Director-Chief Risk Officer in February 2011 and is primarily responsible for the overall enterprise risk management. He is an experienced banker with over 30 years of diverse international exposure including senior postings in the Middle East, Asia and Latin America. Immediately prior to joining GIB, he was the Chief Risk Officer at Alinma Bank, a Shari'ah compliant bank in Saudi Arabia, where he was a key member of the senior management team which launched the bank in 2008, spearheaded the development and implementation of the governance structure and risk management architecture and was a member of the Board of Directors of the Alinma Investment Company. In addition, he worked for Citibank/Citigroup in Saudi Arabia (Samba Financial Group), Turkey, South Korea and Mexico between 1984 and 2003, both in the relationship and risk management areas, as well as for 2 Indonesian banks (2005-2008) as Chief Risk Officer. Mr. Marigomen is a member of GIB's Management Committee and Assets and Liabilities Committee and chairman of the Group Risk Committee.

Mr. Matthew C. Snyder
Managing Director - CEO of GIBUK
BA in Political Science, CW Post College, USA and MA in International Politics, Long Island University, USA. Mr. Snyder first joined GIB's principal subsidiary Gulf International Bank (UK) Ltd. (then Saudi International Bank) in 1993. From 1982 to 1993 he was President and Chief Executive Officer of AI International, a US-based diversified, private industrial company. He previously worked for eleven years in the New York offices of Schroders, a London-based merchant bank. He is the CEO of Gulf International Bank (UK) Ltd.

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Financial Statements

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Independent Auditors' Report to the Shareholders

Report on the consolidated financial statements

We have audited the accompanying consolidated financial statements of Gulf International Bank B.S.C. ("the Bank") and its subsidiaries (together the "Group"), which comprise the consolidated statement of financial position as at 31 December 2011, and the consolidated statements of income, comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Responsibility of the board of directors for the consolidated financial statements

The board of directors of the Bank is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as the board of directors determines is necessary to enable the preparation of the consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2011, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards.

Report on other regulatory requirements

As required by the Bahrain Commercial Companies Law and the Central Bank of Bahrain (CBB) Rule Book (Volume 1), we report that: the Bank has maintained proper accounting records and the consolidated financial statements are in agreement therewith; the financial information contained in the chairman's statement is consistent with the consolidated financial statements; we are not aware of any violations of the Bahrain Commercial Companies Law, the Central Bank of Bahrain and Financial Institutions Law, the CBB Rule Book (Volume 1, applicable provisions of Volume 6), CBB directives, or the terms of the Bank's memorandum and articles of association having occurred during the year that might have had a material adverse effect on the business of the Bank or on its financial position; and satisfactory explanations and information have been provided to us by the management in response to all our requests.

KPMG
Public Accountants
Manama, Kingdom of Bahrain
16th February 2012

Consolidated Statement of Financial Position

	Note	At 31.12.11 US$ millions	At 31.12.10 US$ millions
ASSETS			
Cash and other liquid assets	5	**858.7**	863.9
Securities purchased under agreements to resell	6	**280.0**	180.0
Placements	7	**5,394.0**	3,576.3
Trading securities	8	**83.7**	79.7
Investment securities	9	**3,151.7**	3,067.8
Loans and advances	10	**6,751.8**	7,510.1
Other assets	11	**269.0**	249.9
Total assets		**16,788.9**	15,527.7
LIABILITIES			
Deposits from banks	13	**1,549.3**	2,224.4
Deposits from customers	13	**8,520.3**	6,479.2
Securities sold under agreements to repurchase	14	**283.3**	945.5
Other liabilities	15	**305.1**	273.0
Senior term financing	16	**3,690.3**	3,176.6
Subordinated term financing	17	**477.8**	511.0
Total liabilities		**14,826.1**	13,609.7
EQUITY			
Share capital	18	**2,500.0**	2,500.0
Reserves	19	**246.0**	288.7
Retained earnings		**(783.2)**	(870.7)
Total equity		**1,962.8**	1,918.0
Total liabilities & equity		**16,788.9**	15,527.7

The consolidated financial statements were approved by the Board of Directors on 16th February 2012 and signed on its behalf by:-

Jammaz bin Abdullah Al-Suhaimi
Chairman

Mansour bin Saleh Al Maiman
Vice Chairman

Yahya bin Abdullah Alyahya
Chief Executive Officer

The notes on pages 41 to 83 form an integral part of these consolidated financial statements.

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Consolidated Statement of Income

	Note	Year ended 31.12.11 US$ millions	Year ended 31.12.10 US$ millions
Interest income	21	**273.9**	272.4
Interest expense	21	**130.1**	116.2
Net interest income		**143.8**	156.2
Fee and commission income	22	**48.5**	42.2
Trading income	23	**17.6**	12.7
Other income	24	**17.0**	12.7
Total income		**226.9**	223.8
Staff expenses		**77.7**	61.4
Premises expenses		**9.9**	10.0
Other operating expenses	25	**32.2**	41.9
Total operating expenses		**119.8**	113.3
Net income before provisions and tax		**107.1**	110.5
Provisions for investment securities	9	**(4.8)**	5.0
Provisions for loans and advances	10	**6.7**	(9.0)
Net income before tax		**109.0**	106.5
Taxation charge on overseas activities		**(4.5)**	(6.1)
Net income		**104.5**	100.4
Earnings per share	38	***US$0.04***	*US$0.04*

Jammaz bin Abdullah Al-Suhaimi	Mansour bin Saleh Al Maiman	Yahya bin Abdullah Alyahya
Chairman	Vice Chairman	Chief Executive Officer

The notes on pages 41 to 83 form an integral part of these consolidated financial statements.

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Consolidated Statement of Comprehensive Income

	Year ended 31.12.11 US$ millions	Year ended 31.12.10 US$ millions
Net income	**104.5**	100.4
Other comprehensive income		
Cash flow hedges:-		
- net fair value gains	**0.5**	0.9
- net amount transferred to the consolidated statement of income	**(3.3)**	(5.7)
Available-for-sale securities:-		
- net fair value (losses) / gains	**(61.3)**	38.6
- net amount transferred to the consolidated statement of income	**4.4**	4.4
Total other comprehensive income	**(59.7)**	38.2
Total comprehensive income	**44.8**	138.6

The notes on pages 41 to 83 form an integral part of these consolidated financial statements.

Consolidated Statement of Changes in Equity

	Share capital US$ millions	Reserves US$ millions	Retained earnings US$ millions	Total US$ millions
At 1st January 2010	**2,500.0**	**230.1**	**(950.7)**	**1,779.4**
Net income for the year	-	-	100.4	100.4
Other comprehensive income:-				
- Cash flow hedges:				
net fair value gains	-	0.9	-	0.9
- Available-for-sale securities:				
net fair value gains	-	38.6	-	38.6
Transfers in the year:-				
- Transfers to consolidated statement of income	-	(1.3)	-	(1.3)
Total other comprehensive income	-	38.2	-	38.2
Total comprehensive income	-	38.2	100.4	138.6
Transfers from retained earnings	-	20.4	(20.4)	-
At 31st December 2010	**2,500.0**	**288.7**	**(870.7)**	**1,918.0**
Net income for the year	-	-	104.5	104.5
Other comprehensive income:-				
- Cash flow hedges:				
net fair value gains	-	0.5	-	0.5
- Available-for-sale securities:				
net fair value losses	-	(61.3)	-	(61.3)
Transfers in the year:-				
- Transfers to consolidated statement of income	-	1.1	-	1.1
Total other comprehensive income	-	(59.7)	-	(59.7)
Total comprehensive income	-	(59.7)	104.5	44.8
Transfers from retained earnings	-	17.0	(17.0)	-
At 31st December 2011	**2,500.0**	**246.0**	**(783.2)**	**1,962.8**

The notes on pages 41 to 83 form an integral part of these consolidated financial statements.

Consolidated Statement of Cash Flows

	Note	**Year ended 31.12.11 US$ millions**	Year ended 31.12.10 US$ millions
OPERATING ACTIVITIES			
Net income after tax		**104.5**	100.4
Adjustments to reconcile net income to net cash inflow from operating activities:			
Provisions for investment securities		**4.8**	(5.0)
Provisions for loans and advances		**(6.7)**	9.0
Realised profits on investment securities		**(5.0)**	(5.9)
Amortisation of investment securities		**20.7**	7.7
Net increase in securities purchased under agreements to resell		**(100.0)**	(180.0)
Net (increase) / decrease in placements		**(1,817.7)**	524.8
Net increase in trading securities		**(4.0)**	(29.5)
Net decrease in loans and advances		**765.0**	1,779.0
Increase in accrued interest receivable		**(8.5)**	(19.3)
Increase in accrued interest payable		**8.5**	8.8
Net increase in other net assets		**(4.6)**	(19.3)
Net decrease in deposits from banks		**(675.1)**	(329.8)
Net increase / (decrease) in deposits from customers		**2,041.1**	(1,016.1)
Net cash inflow from operating activities		**323.0**	824.8
INVESTING ACTIVITIES			
Purchase of investment securities		**(982.7)**	(1,800.9)
Sale and maturity of investment securities		**836.2**	782.6
Net cash outflow from investing activities		**(146.5)**	(1,018.3)
FINANCING ACTIVITIES			
Net (decrease) / increase in securities sold under agreements to repurchase		**(662.2)**	380.5
Net increase in senior term financing		**513.7**	168.7
Net decrease in subordinated term financing		**(33.2)**	-
Net cash (outflow) / inflow from financing activities		**(181.7)**	549.2
(Decrease) / increase in cash and cash equivalents		**(5.2)**	355.7
Cash and cash equivalents at 1st January		**863.9**	508.2
Cash and cash equivalents at 31st December	5	**858.7**	863.9

The notes on pages 41 to 83 form an integral part of these consolidated financial statements.

Notes to the Consolidated Financial Statements

For the year ended 31st December 2011

1. INCORPORATION AND REGISTRATION

The parent company of the Group (the Group), Gulf International Bank B.S.C. (the Bank), is a Bahraini Shareholding Company incorporated in the Kingdom of Bahrain by Amiri Decree Law No.30 dated 24th November 1975 and is registered as a conventional wholesale bank with the Central Bank of Bahrain. The registered office of the Bank is located at Al-Dowali Building, 3 Palace Avenue, Manama, Kingdom of Bahrain.

The Group is principally engaged in the provision of wholesale commercial and investment banking services. The Group operates through subsidiaries, branch offices and representative offices located in six countries worldwide. The total number of staff employed by the Group at the end of the financial year was 484.

2. ACCOUNTING POLICIES

The principal accounting policies adopted in the preparation of the consolidated financial statements are set out below:-

2.1 Basis of preparation

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards and in conformity with the Bahrain Commercial Companies Law and the Central Bank of Bahrain and Financial Institutions Law. The consolidated financial statements have been prepared under the historical cost convention as modified by the revaluation of trading securities, available-for-sale securities and derivative financial instruments as explained in more detail in the following accounting policies. Recognised assets and liabilities that are hedged by derivative financial instruments are also stated at fair value in respect of the risk that is being hedged. The accounting policies have been consistently applied by the Bank and its subsidiaries and are consistent with those of the previous year.

2.2 Consolidation principles

The consolidated financial statements include the accounts of Gulf International Bank B.S.C. and its subsidiaries. Subsidiary undertakings are companies and other entities, including special purpose entities, in which the Bank holds, directly or indirectly, more than one half of the voting rights, or otherwise has the power to exercise effective control over the financial and operating policies of the entity. All intercompany balances and transactions, including unrealised gains and losses on transactions between Group companies, have been eliminated.

2.3 Foreign currencies

Items included in the consolidated financial statements of the Bank and its principal subsidiaries are measured based on the currency of the primary environment in which the entity operates (the functional currency). The consolidated financial statements are presented in US Dollars, representing the Group's functional and presentation currency. Transactions in foreign currencies are converted to US Dollars at the rate of exchange prevailing at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into US Dollars at market rates of exchange prevailing at the balance sheet date. Realised and unrealised foreign exchange gains and losses are included in trading income.

2.4 Financial assets and liabilities

Financial assets and liabilities comprise all assets and liabilities reflected in the statement of financial position, although excluding investments in subsidiaries, associated companies and joint ventures, employee benefit plans, property and equipment, deferred taxation and taxation payable.

a) Initial recognition and measurement

Financial assets are classified at inception into one of the following four categories:-

- held-for-trading
- held-to-maturity
- loans and receivables
- available-for-sale financial assets

Notes to the Consolidated Financial Statements (continued)

For the year ended 31st December 2011

2. ACCOUNTING POLICIES (continued)

2.4 Financial assets and liabilities (continued)

a) Initial recognition and measurement (continued)

Financial assets, other than those classified as held-for-trading, are initially recognised at fair value, including transaction costs that are directly attributable to the acquisition of the financial asset.

Financial liabilities are initially recognised at fair value, representing the proceeds received net of premiums, discounts and transaction costs that are directly attributable to the financial liability.

All regular way purchases and sales of financial assets and liabilities held-for-trading are recognised on the trade date, i.e. the date on which the Group commits to purchase or sell the financial asset or liability. All regular way purchases and sales of other financial assets and liabilities are recognised on the settlement date, i.e. the date on which the asset or liability is received from or delivered to the counterparty. Regular way purchases or sales are purchases or sales of financial assets that require delivery within the time frame generally established by regulation or convention in the market place.

b) Subsequent measurement

Subsequent to initial measurement, financial assets and liabilities are measured at either fair value or amortised cost, depending on their classification:-

Held-for-trading

Held-for-trading financial assets and liabilities are assets or liabilities acquired or incurred for the purpose of generating a profit from short-term fluctuations in price or are included in a portfolio in which a pattern of short-term profit taking exists.

Held-for-trading financial assets and liabilities are measured at fair value. The fair value of financial assets and liabilities traded in active markets is based on quoted prices, including quotations obtained from lead managers, brokers and dealers. The bid price is used to measure financial assets and the offer price is used to measure financial liabilities. Mid-market prices are used to measure fair value only to the extent that the Group has financial assets and liabilities with offsetting risk positions.

Realised and unrealised gains and losses, interest earned or incurred, and dividends received on held-for-trading financial assets and liabilities are included in trading income.

Held-to-maturity

Held-to-maturity assets are non-derivative financial assets with fixed or determinable payments and a fixed maturity that have been acquired with the intention of being held until maturity.

Financial assets classified as held-to-maturity are stated at amortised cost using the effective interest rate method as described in note 2.7(a), less provision for impairment, with interest revenue recognised in the consolidated statement of income.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than those classified as held-for-trading. The majority of the Group's loans and receivables are included in the loans and advances category.

Financial assets classified as loans and receivables are stated at amortised cost using the effective interest rate method as described in note 2.7(a), less provision for impairment, with interest revenue recognised in the consolidated statement of income.

Available-for-sale financial assets

Available-for-sale financial assets are assets which are intended to be held for an indefinite period of time and may be sold in response to needs for liquidity, changes in interest rates, or concerns with respect to credit deterioration. Available-for-sale financial assets are measured at fair value. The fair value of available-for-sale financial assets in active markets is based on quoted

2. ACCOUNTING POLICIES (continued)

2.4 Financial assets and liabilities (continued)

b) Subsequent measurement (continued)

Available-for-sale financial assets (continued)

prices, including quotations obtained from lead managers, brokers and dealers. The fair value of available-for-sale financial assets in inactive markets is determined using appropriate valuation techniques. Valuation techniques include comparison to similar instruments for which there are observable prices, and discounted cash flow techniques. Unquoted and illiquid equity investments for which fair values cannot be reliably measured are stated at cost less provision for impairment.

Unrealised gains and losses arising from changes in the fair values of available-for-sale financial assets are recognised in other comprehensive income. The cumulative fair value adjustments on available-for-sale financial assets which are sold or otherwise disposed or become impaired, and which had previously been recognised in other comprehensive income are transferred to the consolidated statement of income.

Non-trading financial liabilities

All financial liabilities, other than those designated as held-for-trading, are classified as non-trading financial liabilities and are measured at amortised cost using the effective interest rate method as described in note 2.7(a).

c) Derecognition of financial assets and liabilities

Financial assets are derecognised and removed from the consolidated statement of financial position when the right to receive cash flows from the assets has expired; the Group has transferred its contractual right to receive the cash flows from the assets, and substantially all the risks and rewards of ownership; or where control is not retained. Financial liabilities are derecognised and removed from the consolidated statement of financial position when the obligation is discharged, cancelled, or expires.

2.5 Impairment of financial assets

A provision for impairment is established where there is objective evidence that the Group will not collect all amounts due, including both principal and interest, in accordance with the contractual terms of the credit facility. Objective evidence that a financial asset is impaired may include a breach of contract, such as default or delinquency in interest or principal payments, the granting of a concession that, for economic or legal reasons relating to the borrower's financial difficulties, would not otherwise be considered, indications that it is probable that the borrower will enter bankruptcy or other financial reorganisation, the disappearance of an active market, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlate with defaults in the group. For equity securities classified as available-for-sale, a significant or prolonged decline in fair value below cost is considered in determining whether a security is impaired. Where such evidence exists, the cumulative net loss that has been previously recognised in other comprehensive income is transferred to the consolidated statement of income. The amount of the cumulative loss that is removed from other comprehensive income and recognised in the consolidated statement of income is the difference between the acquisition cost and current fair value, less any impairment loss on that security previously recognised in the consolidated statement of income.

With the exception of provisions for the impairment of available-for-sale financial assets, provisions for impairment are determined based on the difference between the net carrying amount and the recoverable amount of the financial asset. The recoverable amount is measured as the present value of expected future cash flows, including amounts recoverable from guarantees and collateral, discounted based on the interest rate at the inception of the credit facility or, for debt instruments remeasured to fair value, at the current market rate of interest for a similar financial asset. Provisions for the impairment of available-for-sale financial assets are determined based on the difference between the acquisition cost, net of principal repayments and amortisation adjustments, and the fair value of the financial asset, less any impairment loss previously recognised in the consolidated statement of income. Cumulative losses previously recognised in other comprehensive income, are reclassified from the available-for-sale securities revaluation reserve in equity to the consolidated statement of income.

Notes to the Consolidated Financial Statements (continued)

For the year ended 31st December 2011

2. ACCOUNTING POLICIES (continued)

2.5 Impairment of financial assets (continued)

Provisions for impairment are also measured and recognised on a collective basis in respect of impairments that exist at the balance sheet date but which will only be individually identified in the future. Future cash flows for financial assets that are collectively assessed for impairment are estimated based on contractual cash flows and historical loss experiences for assets with similar credit risk characteristics. Historical loss experience is adjusted, based on current observable data, to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based.

Provisions for impairment are recognised in the consolidated statement of income and are reflected in an allowance account against loans and advances and investment securities.

Financial assets are written off after all restructuring and collection activities have taken place and the possibility of further recovery is considered to be remote. Subsequent recoveries are included in other income.

With the exception of provisions for the impairment of available-for-sale equity investments, provisions for impairment are released and transferred to the consolidated statement of income where a subsequent increase in the recoverable amount is related objectively to an event occurring after the provision for impairment was established. Impairment provisions for available-for-sale equity investments are only released and transferred to the consolidated statement of income on the redemption or sale of the investment.

Financial assets which have been renegotiated are no longer considered to be past due and are replaced on performing status when all principal and interest payments are up-to-date and future payments are reasonably assured. Financial assets subject to individual impairment assessment and whose terms have been renegotiated, are subject to ongoing review to determine whether they remain impaired or should be considered past due.

2.6 Offsetting financial assets and liabilities

Financial assets and financial liabilities are only offset and the net amount reported in the consolidated statement of financial position when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis, or to realise the asset and settle the liability simultaneously.

2.7 Revenue recognition

a) Interest income and interest expense

Interest income and interest expense for all interest-bearing financial assets and liabilities except those classified as held-for-trading are recognised using the effective interest rate method. The effective interest rate method is a method of calculating the amortised cost of a financial asset or liability and of allocating the interest income or interest expense over the expected life of the asset or liability. The effective interest rate is the rate that exactly discounts estimated future cash flows through the expected life of the financial asset or liability or, where appropriate, a shorter period, to the net carrying amount of the financial asset or liability. The application of the effective interest rate method has the effect of recognising interest income and interest expense evenly in proportion to the amount outstanding over the period to maturity or repayment. In calculating the effective interest rate, cash flows are estimated taking into consideration all contractual terms of the financial asset or liability but excluding future credit losses. Fees, including loan origination fees and early redemption fees, are included in the calculation of the effective interest rate to the extent that they are considered to be an integral part of the effective interest rate.

Interest income is suspended when either interest or principal on a credit facility is overdue by more than 90 days whereupon all unpaid and accrued interest is reversed from income. Interest on non-accrual facilities is included in income only when received. Credit facilities are restored to accrual status only after all delinquent interest and principal payments have been brought current and future payments are reasonably assured.

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2. ACCOUNTING POLICIES (continued)

2.7 Revenue recognition (continued)

b) Fees and commissions

Fees and commissions that are integral to the effective interest rate of a financial asset or liability are included in the calculation of the effective interest rate.

Other fees and commissions are recognised as the related services are performed or received, and are included in fee and commission income.

c) Trading income

Trading income arises from earnings generated from customer business and market making, and from changes in fair value resulting from movements in interest and exchange rates, equity prices and other market variables. Changes in fair value and gains and losses arising on the purchase and sale of trading instruments are included in trading income, together with the related interest income, interest expense and dividend income.

d) Dividend income

Dividend income is recognised as follows:-

- dividends from equity instruments classified as held-for-trading are recognised when the right to receive the dividend is established and are included in trading income.
- dividends from equity instruments classified as available-for-sale are recognised when the right to receive the dividend is established and are included in other income.

2.8 Securities financing arrangements

Securities purchased under agreements to resell (reverse repurchase agreements) and securities sold under agreements to repurchase (repurchase agreements) are treated as collateralised lending and borrowing transactions and are recorded in the consolidated statement of financial position at the amounts the securities were initially acquired or sold. Interest earned on reverse repurchase agreements and interest incurred on repurchase agreements are included in interest income and interest expense respectively.

2.9 Premises and equipment

Land is stated at cost. Other premises and equipment are stated at cost less accumulated depreciation. The residual values and useful lives of premises and equipment are reviewed at each balance sheet date, and adjusted where appropriate. Where the carrying amount of premises or equipment is greater than the estimated recoverable amount, the carrying amount is reduced to the recoverable amount.

Generally, costs associated with the maintenance of existing computer software are recognised as an expense when incurred. However, expenditure that enhances and extends the benefits of computer software programmes beyond their original specifications and lives is recognised as a capital improvement and capitalised as part of the original cost of the software.

2.10 Other provisions

Other provisions are recognised when the Group has a present legal or constructive obligation 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.

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Notes to the Consolidated Financial Statements (continued)

For the year ended 31st December 2011

2. ACCOUNTING POLICIES (continued)

2.11 Derivative financial instruments and hedge accounting

Derivative financial instruments are contracts, the value of which is derived from one or more underlying financial instruments or indices, and include futures, forwards, swaps and options in the interest rate, foreign exchange, equity and credit markets.

Derivative financial instruments are recognised in the consolidated statement of financial position at fair value. Fair values are derived from prevailing market prices, discounted cash flow models or option pricing models as appropriate. In the consolidated statement of financial position, derivative financial instruments with positive fair values (unrealised gains) are included in other assets and derivative financial instruments with negative fair values (unrealised losses) are included in other liabilities.

The changes in the fair values of derivative financial instruments entered into for trading purposes or to hedge other trading positions are included in trading income.

The recognition of changes in the fair values of derivative financial instruments entered into for hedging purposes is determined by the nature of the hedging relationship. For the purposes of hedge accounting, derivative financial instruments are designated as a hedge of either: (i) the fair value of a recognised asset or liability (fair value hedge), or (ii) the future cash flows attributable to a recognised asset or liability or a firm commitment (cash flow hedge).

The Group's criteria for a derivative financial instrument to be accounted for as a hedge include:-

- the hedging instrument, the related hedged item, the nature of the risk being hedged, and the risk management objective and strategy must be formally documented at the inception of the hedge,
- it must be clearly demonstrated that the hedge is expected to be highly effective in offsetting the changes in fair values or cash flows attributable to the hedged risk in the hedged item,
- the effectiveness of the hedge must be capable of being reliably measured, and
- the hedge must be assessed on an ongoing basis and determined to have actually been highly effective throughout the financial reporting period.

Changes in the fair values of derivative financial instruments that are designated, and qualify, as fair value hedges and that prove to be highly effective in relation to the hedged risk, are included in trading income together with the corresponding change in the fair value of the hedged asset or liability that is attributable to the risk that is being hedged. Unrealised gains and losses arising on hedged assets or liabilities which are attributable to the hedged risk are adjusted against the carrying amounts of the hedged assets or liabilities in the consolidated statement of financial position. If the hedge no longer meets the criteria for hedge accounting, any adjustment to the carrying amount of a hedged interest-bearing financial instrument is amortised to income over the remaining period to maturity.

Changes in the fair values of derivative financial instruments that are designated, and qualify, as cash flow hedges and that prove to be highly effective in relation to the hedged risk, are recognised in other comprehensive income. Unrealised gains or losses recognised in other comprehensive income are transferred to the consolidated statement of income at the same time that the income or expense of the corresponding hedged item is recognised in the consolidated statement of income and are included in the same income or expense category as the hedged item. Unrealised gains or losses on any ineffective portion of cash flow hedging transactions are included in trading income.

The interest component of derivatives that are designated, and qualify, as fair value or cash flow hedges is included in interest income or interest expense relating to the hedged item over the life of the derivative instrument.

Hedge accounting is discontinued when the derivative hedging instrument either expires or is sold, terminated or exercised, or no longer qualifies for hedge accounting. Gains and losses arising on the termination of derivatives designated as cash flow hedges are recognised in interest income or interest expense over the original tenor of the terminated hedge transaction.

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2. ACCOUNTING POLICIES (continued)

2.11 Derivative financial instruments and hedge accounting (continued)

Some hybrid instruments contain both a derivative and non-derivative component. In such cases, the derivative is categorised as an embedded derivative. If the economic characteristics and risks of the embedded derivative are not closely related to those of the host contract, and the overall contract itself is not carried at fair value, the embedded derivative is bifurcated and measured at fair value. If it is not practically possible to bifurcate the embedded derivative, the entire hybrid instrument is categorised as held-for-trading and measured at fair value. Changes in fair value are included in trading income.

2.12 Financial guarantees

Financial guarantees are contracts that require the Group to make specified payments to reimburse the holder for a loss it incurs because a specific debtor fails to make payment when due in accordance with the terms of a debt instrument. Financial guarantees are issued to financial institutions and other counterparties on behalf of customers to secure loans, overdrafts and other banking facilities, and to other parties in relation to the performance of customers under obligations related to contracts, advance payments made by other parties, tenders and retentions.

Financial guarantees are initially recognised at fair value on the date the guarantee is issued. The guarantee liability is subsequently measured at the higher of the initial measurement, less amortisation to recognise the fee income earned over the period, or the present value of any expected financial obligation arising as a result of an anticipated non-recoverable payment under a guarantee. Any increase in a liability relating to guarantees is recognised in the consolidated statement of income. In the consolidated statement of financial position, financial guarantees are included in other liabilities.

2.13 Post-retirement benefits

The majority of the Group's employees are eligible for post-retirement benefits under either defined benefit or defined contribution pension plans which are provided through separate trustee-administered funds or insurance plans. The Group also pays contributions to Government-defined contribution pension plans in accordance with the legal requirements in each location.

The Group's contributions to defined contribution pension plans are expensed in the year to which they relate.

The pension costs for defined benefit pension plans are assessed using the projected unit credit method. The cost of providing pensions is charged to income so as to spread the regular cost of pensions over the service lives of the employees, in accordance with the advice of an independent qualified actuary who conducts a full valuation of the plan every three years. The pension obligation is measured as the present value of the estimated future cash flows using interest rates of government securities which have terms to maturity approximating the terms of the related liability.

Actuarial gains and losses are recognised in income when the net cumulative unrecognised actuarial gain or loss at the end of the previous financial year exceeds 10 per cent of the higher of: (i) the fair value of the plan assets, or (ii) the present value of the fund obligations. That portion of the net cumulative unrecognised actuarial gain or loss is recognised in income over the expected average remaining working lives of the employees participating in the plan. Otherwise, the actuarial gain or loss is not recognised.

2.14 Taxation

a) Current tax

Current taxation is the expected tax payable on the taxable income for the year, using tax rates enacted at the balance sheet date, and includes any adjustments to tax payable in respect of previous years.

b) Deferred tax

Deferred tax is provided, using the liability method, for temporary differences arising between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. A deferred tax asset is recognised only to the extent that it is probable that future taxable income will be available against which the unutilised tax losses and credits can be utilised. Currently enacted tax rates are used to determine deferred taxes.

Notes to the Consolidated Financial Statements (continued)

For the year ended 31st December 2011

2. ACCOUNTING POLICIES (continued)

2.15 Cash and cash equivalents

In the consolidated statement of cash flows, cash and cash equivalents comprise cash and other liquid assets.

2.16 Segment reporting

An operating segment is a distinguishable component of the Group that is engaged in business activities from which revenues are earned and expenses are incurred, including revenues and expenses that relate to transactions with any of the Group's other operating segments. All segments have discrete financial information which is regularly reviewed by the Group's Management Committee, being the Group's chief operating decision maker, to make decisions about resources allocated to the segment and to assess its performance.

2.17 Fiduciary activities

The Group administers and manages assets owned by clients which are not reflected in the consolidated financial statements. Asset management fees are earned for providing investment management services and for managing mutual fund products. Asset administration fees are earned for providing custodial services. Fees are recognised as the services are provided and are included in fee and commission income.

2.18 Dividends

Dividends on issued shares are recognised as a liability and deducted from equity when they are approved by the Bank's shareholders.

2.19 Comparatives

Where necessary, comparative figures have been adjusted to conform with changes in presentation in the current year.

2.20 Future accounting developments

The International Accounting Standards Board (IASB) have issued a number of new standards, amendments to standards, and interpretations that are not yet effective and have not been applied in the preparation of the consolidated financial statements for the year ended 31st December 2011. The relevant new standards, amendments to standards, and interpretations, are as follows:-

- IAS 19 - Employee Benefits (revised). The amendments to the existing standard are effective for financial years beginning on or after 1st January 2013. The standard amends the methodology for recognising actuarial gains and losses, the current corridor method will be eliminated and all actuarial gains and losses will be immediately recognised in other comprehensive income. The revised standard also amends the calculation methodology for the reported expected returns. The Group is currently evaluating the potential effect of this revision.
- IFRS 10 - Consolidated Financial Statements. The new standard is effective for financial years beginning on or after 1st January 2013. The standard supersedes SIC 12 and elements of IAS 27 and introduces a new approach to determine which investees should be consolidated as part of the Group. The Group is currently evaluating the potential effect of this new standard and the minor revisions to the remaining elements of IAS 27 - Separate Financial Statements (2011).
- IFRS 12 - Disclosure of Interests in Other Entities. The new standard is effective for financial years beginning on or after 1st January 2013. The new standard contains the disclosure requirements for organisations that have interests in subsidiaries, associates or other unconsolidated entities. The Group is currently evaluating the potential impact on presentation that this standard could require.
- IFRS 13 - Fair Value Measurement. The new standard is effective for financial years beginning on or after 1st January 2013. The new standard provides a single source of fair value measurement guidance. The standard does not introduce new measurement requirements, but does provide new techniques on how to measure fair value and the related disclosures. The adoption of this standard is not expected to have any material impact on the consolidated financial statements.

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2. ACCOUNTING POLICIES (continued)

2.20 Future accounting developments (continued)

- IFRS 9 - Financial Instruments. The new standard is effective for financial years beginning on or after 1st January 2015. The standard amends the measurement categories currently defined under IAS 39, specifically, held-to-maturity, loans and receivables and available-for-sale categories are eliminated. The standard also amends the accounting for embedded derivatives and the rules regarding derecognition of financial assets and liabilities. The Group is currently evaluating the potential effect of this standard which is expected to require certain valuation and associated presentational changes.

3. ACCOUNTING ESTIMATES AND ASSUMPTIONS

The preparation of the consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of certain financial assets, liabilities, income and expenses.

The use of estimates and assumptions is principally limited to the determination of provisions for impairment, the valuation of financial instruments, and the valuation of the Group's defined benefit pension plan as explained in more detail below:-

Provisions for impairment

Financial assets are evaluated for impairment on the basis set out in note 2.5.

In determining provisions for impairment, judgement is required in the estimation of the amount and timing of future cash flows.

In addition to provisions for impairment against specific assets, the Group also maintains provisions that are measured and recognised on a collective basis. Key assumptions included in the measurement of the portfolio provisions include data on the probability of default and the eventual recovery amount in the event of a forced sale or write off. These assumptions are based on observed historical data and updated as considered appropriate to reflect current conditions. The accuracy of the portfolio provisions would therefore be affected by unexpected changes in these assumptions.

Equity securities classified as available-for-sale are considered to be impaired when there has been a significant or prolonged decline in fair value below cost. The determination of significant or prolonged requires judgement. In making the judgement, a number of factors are taken into account including the normal volatility in valuation, evidence of a deterioration in the financial condition of the investee, industry and sector performance, and operational and financing cash flows.

Fair value of financial assets and liabilities

Where the fair value of financial assets and liabilities cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The input to these models is derived from observable markets where available, but where this is not feasible, a degree of judgement is required in determining assumptions used in the models. Changes in assumptions used in the models could affect the reported fair value of financial assets and liabilities.

Retirement benefit obligations

Management, in coordination with an independent qualified actuary, are required to make assumptions regarding the defined benefit pension plan, changes in which could affect the reported liability, service cost and expected return on pension plan assets. The principal actuarial assumptions for the defined benefit pension plan are set out in note 12 and include assumptions on the discount rate, expected return on pension plan assets, mortality, future salary increases, and inflation. Changes in the assumptions could affect the reported asset, service cost and expected return on pension plan assets.

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Notes to the Consolidated Financial Statements (continued)

For the year ended 31st December 2011

4. CLASSIFICATION OF ASSETS AND LIABILITIES

The classification of assets and liabilities by accounting categorisation was as follows:-

	Held-to-maturity US$ millions	Loans and receivables US$ millions	Held-for-trading US$ millions	Available-for-sale US$ millions	Financial liabilities at amortised cost US$ millions	Non-financial assets & liabilities US$ millions	Total US$ millions
At 31st December 2011							
Cash and other liquid assets	**763.9**	**94.8**	-	-	-	-	**858.7**
Securities purchased under agreements to resell	**280.0**	-	-	-	-	-	**280.0**
Placements	**5,394.0**	-	-	-	-	-	**5,394.0**
Trading securities	-	-	**83.7**	-	-	-	**83.7**
Investment securities	-	-	-	**3,151.7**	-	-	**3,151.7**
Loans and advances	-	**6,751.8**	-	-	-	-	**6,751.8**
Other assets	-	**154.0**	**81.1**	-	-	**33.9**	**269.0**
Total assets	**6,437.9**	**7,000.6**	**164.8**	**3,151.7**	-	**33.9**	**16,788.9**
Deposits from banks	-	-	-	-	**1,549.3**	-	**1,549.3**
Deposits from customers	-	-	-	-	**8,520.3**	-	**8,520.3**
Securities sold under agreements to repurchase	-	-	-	-	**283.3**	-	**283.3**
Other liabilities	-	-	**112.5**	-	-	**192.6**	**305.1**
Senior term financing	-	-	-	-	**3,690.3**	-	**3,690.3**
Subordinated term financing	-	-	-	-	**477.8**	-	**477.8**
Equity	-	-	-	-	-	**1,962.8**	**1,962.8**
Total liabilities & equity	-	-	**112.5**	-	**14,521.0**	**2,155.4**	**16,788.9**
At 31st December 2010							
Cash and other liquid assets	747.6	116.3	-	-	-	-	863.9
Securities purchased under agreements to resell	180.0	-	-	-	-	-	180.0
Placements	3,576.3	-	-	-	-	-	3,576.3
Trading securities	-	-	79.7	-	-	-	79.7
Investment securities	-	-	-	3,067.8	-	-	3,067.8
Loans and advances	-	7,510.1	-	-	-	-	7,510.1
Other assets	-	145.7	67.1	-	-	37.1	249.9
Total assets	4,503.9	7,772.1	146.8	3,067.8	-	37.1	15,527.7
Deposits from banks	-	-	-	-	2,224.4	-	2,224.4
Deposits from customers	-	-	-	-	6,479.2	-	6,479.2
Securities sold under agreements to repurchase	-	-	-	-	945.5	-	945.5
Other liabilities	-	-	86.2	-	-	186.8	273.0
Senior term financing	-	-	-	-	3,176.6	-	3,176.6
Subordinated term financing	-	-	-	-	511.0	-	511.0
Equity	-	-	-	-	-	1,918.0	1,918.0
Total liabilities & equity	-	-	86.2	-	13,336.7	2,104.8	15,527.7

The held-for-trading category includes the fair values of derivatives designated as fair value and cash flow hedges.

The Group did not have any financial assets or financial liabilities classified as fair value through the statement of income, other than those classified as held-for-trading, at either 31st December 2011 or 31st December 2010.

5. CASH AND OTHER LIQUID ASSETS

	31.12.11	31.12.10
	US$ millions	US$ millions
Cash and balances with banks	**94.8**	116.3
Certificates of deposit	**604.3**	721.0
Government bills	**159.6**	26.6
	858.7	863.9

6. SECURITIES PURCHASED UNDER AGREEMENTS TO RESELL

The Group enters into collateralised lending transactions (reverse repurchase agreements) in the ordinary course of its operating activities. The collateral is in the form of highly rated debt securities. The collateralised lending transactions are conducted under standardised terms that are usual and customary for such transactions.

7. PLACEMENTS

Placements at 31st December 2011 included placements with central banks amounting to US$1,008.8 million (2010: US$633.5 million). The placements with central banks represented the placement of surplus liquid funds.

8. TRADING SECURITIES

	31.12.11	31.12.10
	US$ millions	US$ millions
Debt securities	**56.9**	53.0
Managed funds	**26.8**	26.4
Listed equities	-	0.3
	83.7	79.7

Debt securities comprise investments in debt securities issued by emerging market governments, quasi-government entities, and government-owned entities.

Managed funds comprise funds placed for investment with specialist managers.

9. INVESTMENT SECURITIES

a) Composition

The credit rating profile of investment securities, based on the lowest rating assigned by the major international rating agencies, was as follows:-

	31.12.11		31.12.10	
	US$ millions	**%**	US$ millions	%
AAA to A- / Aaa to A3	**2,610.1**	**91.6**	2,435.8	89.4
BBB+ to BBB- / Baa1 to Baa3	**163.6**	**5.8**	207.6	7.6
Other debt securities	**75.1**	**2.6**	81.5	3.0
Total debt securities	**2,848.8**	**100.0**	2,724.9	100.0
Equity investments	**302.9**		342.9	
	3,151.7		3,067.8	

Investment securities principally comprise investment-grade rated debt securities issued by major international financial institutions and government-related entities. The Group did not have any direct exposure to troubled European government debt impacted by the eurozone crisis at either 31st December 2011 or 31st December 2010.

At 31st December 2011, 91.6 per cent of debt securities were rated A- / A3 or above (2010: 89.4 per cent).

Notes to the Consolidated Financial Statements (continued)

For the year ended 31st December 2011

9. INVESTMENT SECURITIES (continued)

b) Provisions for impairment

The movements in the provisions for the impairment of investment securities were as follows:-

	2011 US$ millions	2010 US$ millions
At 1st January	**67.8**	97.5
Exchange rate movements	**(0.1)**	(0.5)
Amounts utilised	**(0.6)**	(24.2)
Charge / (Release) for the year	**4.8**	(5.0)
At 31st December	**71.9**	67.8

The amounts utilised during the year ended 31st December 2010 principally comprised amounts written off on the redemption of externally managed funds. The redemptions resulted in the release of unutilised provisions for impairment and no incremental losses arose as a result of the redemptions.

c) Impaired securities

Impaired securities represent securities for which there is objective evidence that the Group will not collect all amounts due, including both principal and interest, in accordance with the contractual terms of the security.

Impaired investment securities and the related specific provisions for impairment were as follows:-

	31.12.11			31.12.10		
	Gross US$ millions	**Impairment provisions US$ millions**	**Carrying amount US$ millions**	Gross US$ millions	Impairment provisions US$ millions	Carrying amount US$ millions
Equity investments	**74.5**	**58.2**	**16.3**	57.7	44.2	13.5
Non-specific / portfolio provisions		**13.7**			23.6	
Total provisions for impairment		**71.9**			67.8	

Total specific provisions for impairment at 31st December 2011 represented 78.1 per cent of gross impaired investment securities (2010: 76.6 per cent).

There were no past due debt securities at 31st December 2011 or 31st December 2010.

d) Unquoted equity investments

Investment securities at 31st December 2011 included US$107.0 million (2010: US$106.9 million) of unquoted equity investments for which fair values cannot be reliably measured. These investments are stated at cost less provision for impairment. They principally represent private equity investments and investments in managed entities, the underlying investments of which are primarily of either a corporate debt or private equity nature, managed by external specialist managers and international investment banks. There are no active markets or other appropriate methods from which to derive reliable fair values for these investments. The Group intends to exit these investments principally by means of IPOs or private placements.

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9. INVESTMENT SECURITIES (continued)

e) Reclassified securities

In accordance with the amendments to IAS 39 - Financial Instruments: Recognition and Measurement, a number of externally managed funds that were no longer held for the purpose of sale in the short term were reclassified from held-for-trading to available-for-sale on 1st October 2008. Due to the adverse impact of the severe market conditions prevailing at the time, which was considered to meet the IAS 39 amendment definition of a rare event, the managed funds are closed to redemptions for the foreseeable future. The funds were reclassified at their net asset values on the date of transfer on 1st October 2008. The movements in the carrying amount of the reclassified funds were as follows:-

	Carrying amount US$ millions
At 1st October 2008	60.8
Provisions for impairment	(37.7)
Net movement	4.2
At 31st December 2008	27.3
Net movement	(8.3)
At 31st December 2009	19.0
Net movement	(2.1)
At 31st December 2010	16.9
Net movement	0.4
At 31st December 2011	**17.3**

During 2011, realised gains of US$0.1 million (2010: US$0.7 million) were recognised as realised profits on investment securities in other income in the consolidated statement of income. These profits would have been recognised as trading income had the assets not been reclassified.

10. LOANS AND ADVANCES

	31.12.11 US$ millions	31.12.10 US$ millions
Gross loans and advances	**7,371.0**	8,152.4
Provisions for impairment	**(619.2)**	(642.3)
Net loans and advances	**6,751.8**	7,510.1

Notes to the Consolidated Financial Statements (continued)

For the year ended 31st December 2011

10. LOANS AND ADVANCES (continued)

a) Industrial classification

The classification of loans and advances by industry was as follows:-

	31.12.11 US$ millions	31.12.10 US$ millions
Energy, oil and petrochemical	2,791.6	3,010.8
Financial	1,277.5	1,103.7
Trading and services	1,002.5	1,192.5
Transportation	782.5	812.9
Manufacturing	546.3	595.7
Communication	329.1	266.8
Construction	308.5	533.3
Real estate	191.5	361.5
Government	21.7	185.9
Other	119.8	89.3
	7,371.0	8,152.4
Provisions for impairment	(619.2)	(642.3)
	6,751.8	7,510.1

The classification of loans and advances by industry reflects the Group's historical strategic focus on project and structured finance in the Gulf Cooperation Council (GCC) states.

Gross loans at 31st December 2011 included Shariah-compliant transactions amounting to US$1,011.9 million (2010: US$1,582.4 million).

b) Provisions for impairment

The movements in the provisions for the impairment of loans and advances were as follows:-

	2011			2010		
	Specific US$ millions	Non-Specific US$ millions	Total US$ millions	Specific US$ millions	Non-Specific US$ millions	Total US $ millions
At 1st January	397.3	245.0	642.3	394.1	240.0	634.1
Exchange rate movements	(0.1)	-	(0.1)	-	-	-
Amounts utilised	(16.3)	-	(16.3)	(0.8)	-	(0.8)
Amounts reallocated	35.0	(35.0)	-	-	-	-
(Release) / Charge for the year	(6.7)	-	(6.7)	4.0	5.0	9.0
At 31st December	409.2	210.0	619.2	397.3	245.0	642.3

The level of non-specific loan provisions reflect the application of stressed probabilities of default in the calculation of provisions for impairment measured on a collective basis. Stressed probabilities of default are anticipated to result from the impact of the global recession on the regional economic environment. The probabilities of default applied in the calculation of the collective provisions of impairment equate to a speculative-grade mean default rate of 13.9 per cent, exceeding the previous historical high corporate default levels witnessed in July 1991.

Non-specific provisions at 31st December 2011 represented 3.1 per cent of non-specifically provisioned loans (2010: 3.3 per cent).

The gross amount of specifically provisioned loans at 31st December 2011 was US$686.0 million (2010: US$641.1 million). Total specific provisions at 31st December 2011 represented 59.7 per cent of loans against which a specific provision had been made (2010: 54.9 per cent).

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10. LOANS AND ADVANCES (continued)

b) Provisions for impairment (continued)

Amounts utilised during the years ended 31st December 2011 and 31st December 2010 represented provisions utilised on the settlement or sale of the related loans. No incremental losses arose on the settlement or sale of the loans.

The provision release during the year ended 31st December 2011 arose on the repayment of the related loans.

c) Past due loans

The gross and carrying amounts of loans for which either principal or interest was over 90 days past due were as follows:-

	31.12.11				31.12.10			
	Gross		**Carrying amount**		Gross		Carrying amount	
	Corporates US$ millions	**Financial institutions US$ millions**	**Corporates US$ millions**	**Financial institutions US$ millions**	Corporates US$ millions	Financial institutions US$ millions	Corporates US$ millions	Financial institutions US$ millions
Secured	**86.4**	-	**86.4**	-	84.3	-	84.3	-
Unsecured								
Under restructuring and current	**99.2**	-	**99.2**	-	477.2	-	381.6	-
Other	**196.8**	**200.1**	**77.5**	**61.3**	154.7	169.4	41.3	23.7
Total Unsecured	**296.0**	**200.1**	**176.7**	**61.3**	631.9	169.4	422.9	23.7

Corporates include loans extended for investment purposes.

Net unsecured past due loans at 31st December 2011 of US$238.0 million included US$99.2 million of loans that were subject to restructuring programmes and for which interest was current and being paid on due dates. The restructurings were expected to be finalised within the six months ended 30th June 2012, following which the loans will revert to performing status. The restructuring programmes are not anticipated to result in an economic loss for the Group.

The overdue status of past due but not impaired loans based on original contractual maturities was as follows:-

	31.12.11 US$ millions	31.12.10 US$ millions
Less than 1 year	**146.7**	235.7
Years 2 to 5	**86.8**	26.7
	233.5	262.4

At 31st December 2011 interest-in-suspense on past due loans amounted to US$79.1 million (2010: US$59.5 million).

d) Renegotiated loans

During the year ended 31st December 2011, the Group renegotiated two loans amounting to US$100.2 million (2010: nil) that were restructured due to a deterioration in the borrowers' financial position and where the Group made concessions that it would not have otherwise considered. In addition, a number of other loans were restructured on improved terms.

e) Collateral

During the year ended 31st December 2011, no collateral was received in settlement of past due loans. During the year ended 31st December 2010, the Group took possession of listed equities received in settlement of a secured past due loan. The equities are classified as investment securities. At 31st December 2011, the carrying amount of the equities was US$148.6 million.

Notes to the Consolidated Financial Statements (continued)

For the year ended 31st December 2011

11. OTHER ASSETS

	31.12.11 US$ millions	31.12.10 US$ millions
Accrued interest, fees and commissions	**85.6**	77.1
Derivative financial instruments	**81.1**	67.1
Premises and equipment	**33.9**	37.1
Prepaid pension cost	**17.9**	16.5
Prepayments	**8.9**	8.0
Deferred items	**3.1**	4.8
Other, including accounts receivable	**38.5**	39.3
	269.0	249.9

Derivative financial instruments represent the positive fair values of derivative financial instruments entered into for trading purposes, or designated as fair value or cash flow hedges. An analysis of the fair value of derivative financial instruments is set out in note 31(d).

An analysis of the prepaid pension cost is set out in note 12.

12. POST-RETIREMENT BENEFITS

The Group contributes to defined benefit and defined contribution pension plans which cover substantially all of its employees.

The Bank maintains defined contribution pension plans for the majority of its employees. Contributions are based on a percentage of salary. The amounts to be paid as retirement benefits are determined by reference to the amounts of the contributions and investment earnings thereon. The total cost of contributions to defined contribution pension plans for the year ended 31st December 2011 amounted to US$4.8 million (2010: US$5.1 million).

The Bank's principal subsidiary, Gulf International Bank (UK) Limited (GIBUK), maintains a defined benefit pension plan for a number of its employees. The assets of the plan are held independently of the subsidiary's assets in a separate trustee administered fund. The pension costs are charged to income so as to spread the regular cost of the pensions over the service lives of the employees, in accordance with the advice of an independent qualified actuary who conducts a full valuation of the plan every three years using the projected unit credit method. In the intervening years the calculation is updated based on information received from the actuary. The latest full actuarial valuation was carried out at 1st January 2010.

a) The amount recognised in the consolidated statement of financial position is analysed as follows:-

	31.12.11 US$ millions	31.12.10 US$ millions
Fair value of plan assets	**157.1**	148.0
Present value of fund obligations	**151.5**	152.5
Plan surplus / (deficit)	**5.6**	(4.5)
Unrecognised actuarial loss	**12.3**	21.0
Net asset in the consolidated statement of financial position	**17.9**	16.5

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12. POST-RETIREMENT BENEFITS (continued)

b) The movements in the fair value of plan assets were as follows:-

	2011 **US$ millions**	2010 US$ millions
At 1st January	**148.0**	144.8
Expected return on plan assets	**9.5**	7.3
Contributions paid by the Group	**1.6**	0.8
Benefits paid by the plan	**(5.4)**	(3.6)
Actuarial gains	**4.0**	5.3
Exchange rate movements	**(0.6)**	(6.6)
At 31st December	**157.1**	148.0

The plan assets at 31st December 2011 comprise equity and debt securities in the ratio of 26 per cent and 74 per cent respectively (2010: 34 per cent and 66 per cent respectively). Cash holdings within the plan assets are included in debt securities.

The expected and actual returns on the plan assets for the year ended 31st December 2011 were US$9.5 million and US$13.5 million respectively (2010: US$7.3 million and US$12.9 million respectively). The overall expected rate of return on the plan assets is determined based on market prices, applicable to the period over which the obligation is to be settled. The expected return is determined separately for equity and debt securities.

c) The movements in the present value of fund obligations were as follows:-

	2011 **US$ millions**	2010 US$ millions
At 1st January	**152.5**	149.8
Current service cost	**0.8**	0.9
Interest cost	**8.8**	8.1
Actuarial (gains) / losses	**(4.6)**	4.1
Benefits paid by the plan	**(5.4)**	(3.6)
Exchange rate movements	**(0.6)**	(6.8)
At 31st December	**151.5**	152.5

d) The movements in the net asset recognised in the consolidated statement of financial position were as follows:-

	2011 **US$ millions**	2010 US$ millions
At 1st January	**16.5**	17.6
Net expense included in staff expenses	**(0.1)**	(3.0)
Contributions paid by the Group	**1.6**	0.8
Exchange rate movements	**(0.1)**	1.1
At 31st December	**17.9**	16.5

The Group paid US$1.6 million in contributions to the plan during 2011 and expects to pay US$0.8 million during 2012.

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Notes to the Consolidated Financial Statements (continued)

For the year ended 31st December 2011

12. POST RETIREMENT BENEFITS (continued)

e) The amounts recognised in the consolidated statement of income were as follows:-

	2011 US$ million	2010 US$ millions
Current service cost	**0.8**	0.9
Interest cost	**8.8**	8.1
Expected return on plan assets	**(9.5)**	(7.3)
Amortisation of actuarial loss	**-**	1.3
Net expense included in staff expenses	**0.1**	3.0

f) The principal actuarial assumptions used for accounting purposes were as follows:-

	2011	2010
Discount rate	**5.1%**	5.6%
Expected return on plan assets - equities	**6.5%**	7.7%
Expected return on plan assets - bonds	**4.7%**	5.4%
Future salary increases	**4.4%**	4.8%
Future increases to pensions in payment	**3.2%**	3.6%

g) Historical information

	2011 US$ millions	2010 US$ millions	2009 US$ millions	2008 US$ millions	2007 US$ millions
Fair value of plan assets	**157.1**	148.0	144.8	117.5	169.9
Present value of fund obligations	**151.5**	152.5	149.8	101.5	162.5
Plan surplus / (deficit)	**5.6**	(4.5)	(5.0)	16.0	7.4
Experience gains on plan assets	**4.5**	4.8	10.0	3.2	4.2
Experience losses on plan liabilities	**(4.7)**	(3.5)	(2.6)	(14.6)	(1.2)

13. DEPOSITS

Deposits from customers include deposits from central banks.

The geographical composition of total deposits was as follows:-

	31.12.11 US$ millions	31.12.10 US$ millions
GCC countries	**7,387.4**	6,749.6
Other Middle East and North Africa countries	**364.3**	654.8
Other countries	**2,317.9**	1,299.2
	10,069.6	8,703.6

GCC deposits comprise deposits from GCC country governments and central banks and other institutions headquartered in the GCC states.

At 31st December 2011, GCC deposits represented 73.4 per cent of total deposits (2010: 77.5 per cent).

The significant increase in deposits from other countries during the year ended 31st December 2011 reflected a higher level of deposit activity by the Group's London-based subsidary, Gulf International Bank (UK) Limited.

13. DEPOSITS (continued)

Total deposits at 31st December 2011 included Shariah-compliant transactions amounting to US$1,188.5 million (2010: US$2,022.8 million). Shariah-compliant transactions comprise murabaha contracts. The decrease in Shariah-compliant deposits during the year ended 31st December 2011 reflected a generally lower funding requirement associated with a lower loan volume.

14. SECURITIES SOLD UNDER AGREEMENTS TO REPURCHASE

The Group enters into collateralised borrowing transactions (repurchase agreements) in the ordinary course of its financing activities. Collateral is provided in the form of securities held within the investment securities portfolio. At 31st December 2011, the fair value of investment securities that had been pledged as collateral under repurchase agreements was US$294.0 million (2010: US$1,002.0 million). The collateralised borrowing transactions are conducted under standardised terms that are usual and customary for such transactions.

15. OTHER LIABILITIES

	31.12.11 US$ millions	31.12.10 US$ millions
Derivative financial instruments	**112.5**	86.2
Deferred items	**69.7**	62.1
Accrued interest	**56.9**	48.4
Other, including accounts payable and accrued expenses	**66.0**	76.3
	305.1	273.0

Derivative financial instruments represent the negative fair values of derivative financial instruments entered into for trading purposes, or designated as fair value or cash flow hedges. An analysis of the fair value of derivative financial instruments is set out in note 31(d).

16. SENIOR TERM FINANCING

	Maturity	**31.12.11 US$ millions**	31.12.10 US$ millions
Floating rate loan	2012	**1,173.5**	1,200.0
Floating rate note	2012	**533.3**	533.3
Murabaha term facility	2012	**50.0**	50.0
Murabaha term facility	2013	**100.0**	100.0
Murabaha term facility	2014	**300.0**	-
Floating rate repurchase agreements	2014	**64.9**	-
Floating rate note	2015	**933.2**	933.3
Floating rate repurchase agreements	2015	**35.4**	-
Floating rate loan	2016	**500.0**	-
Floating rate loans	2011	**-**	360.0
		3,690.3	3,176.6

During the year ended 31st December 2011, the Group raised US$900.3 million of new senior term finance (2010: US$1,033.3 million) and repurchased US$26.5 million of the senior floating rate loan maturing in 2012 (2010: nil).

The US$500.0 million floating rate loan maturing in 2016 was provided by the Group's majority shareholder, the Public Investment Fund. The loan was based on market rates and standardised terms that are usual and customary for such transactions.

At 31st December 2011, the fair value of investment securities that had been pledged as collateral under term repurchase agreements was US$145.3 million.

Notes to the Consolidated Financial Statements (continued)

For the year ended 31st December 2011

17. SUBORDINATED TERM FINANCING

	Maturity	31.12.11 US$ millions	31.12.10 US$ millions
Floating rate note	2015	**327.8**	361.0
Floating rate loans	2016	**150.0**	150.0
		477.8	511.0

The subordinated term financing facilities represent unsecured obligations of the Group and are subordinated in right of payment to the claims of depositors and other creditors of the Group that are not also subordinated. The subordinated financing facilities have been approved for inclusion in tier 2 capital for capital adequacy purposes by the Bank's regulator, the Central Bank of Bahrain.

During the year ended 31st December 2011, the Group repurchased US$33.2 million of the subordinated floating rate note maturing in 2015 (2010: nil).

18. SHARE CAPITAL

The authorised share capital at 31st December 2011 comprised 3.0 billion shares of US$1 each (2010: 3.0 billion shares of US$1 each). The issued share capital at 31st December 2011 comprised 2.5 billion shares of US$1 each (2010: 2.5 billion shares of US$1 each). All issued shares are fully paid.

19. RESERVES

	Share premium US$ millions	Compulsory reserve US$ millions	Voluntary reserve US$ millions	Cash flow hedge reserve US$ millions	Available-for-sale securities revaluation reserve US$ millions	Total US$ millions
At 1st January 2010	**7.6**	**169.2**	**106.7**	**11.1**	**(64.5)**	**230.1**
Arising in the year:-						
- Cash flow hedges:						
net fair value gains	-	-	-	0.9	-	0.9
- Available-for-sale securities:						
net fair value gains	-	-	-	-	38.6	38.6
Transfers in the year:-						
- Transfers to consolidated						
statement of income	-	-	-	(5.7)	4.4	(1.3)
Net (decrease) / increase	-	-	-	(4.8)	43.0	38.2
Transfers from retained earnings	-	10.2	10.2	-	-	20.4
At 31st December 2010	**7.6**	**179.4**	**116.9**	**6.3**	**(21.5)**	**288.7**
Arising in the year:-						
- Cash flow hedges:						
net fair value gains	-	-	-	0.5	-	0.5
- Available-for-sale securities:						
net fair value losses	-	-	-	-	(61.3)	(61.3)
Transfers in the year:-						
- Transfers to consolidated						
statement of income	-	-	-	(3.3)	4.4	1.1
Net decrease	-	-	-	(2.8)	(56.9)	(59.7)
Transfers from retained earnings	-	8.5	8.5	-	-	17.0
At 31st December 2011	**7.6**	**187.9**	**125.4**	**3.5**	**(78.4)**	**246.0**

19. RESERVES (continued)

In accordance with the Bank's articles of association, 10 per cent of the Bank's net profit for the year is required to be transferred to each of the compulsory and voluntary reserves. Transfers to the non-distributable compulsory reserve are required until such time as this reserve represents 50 per cent of the issued share capital of the Bank. The voluntary reserve may be utilised at the discretion of the Board of Directors.

20. DIVIDENDS

No dividend is proposed in respect of the financial year ended 31st December 2011.

21. NET INTEREST INCOME

	2011 US$ millions	2010 US$ millions
Interest income		
Placements and other liquid assets	**37.9**	28.1
Investment securities	**49.4**	36.9
Loans and advances	**186.6**	207.4
Total interest income	**273.9**	272.4
Interest expense		
Deposits from banks and customers	**60.9**	61.5
Securities sold under agreements to repurchase	**6.1**	3.4
Term financing	**63.1**	51.3
Total interest expense	**130.1**	116.2
Net interest income	**143.8**	156.2

Interest income on loans and advances includes loan origination fees that form an integral part of the effective interest rate of the loan.

Accrued but uncollected interest on impaired loans included in interest income for the year ended 31st December 2011 amounted to US$1.6 million (2010: US$0.5 million). There was no accrued but uncollected interest included in interest income on past due loans or past due investment securities for either the year ended 31st December 2011 or 31st December 2010.

22. FEE AND COMMISSION INCOME

	2011 US$ millions	2010 US$ millions
Fee and commission income		
Investment banking and management fees	**24.6**	24.4
Commissions on letters of credit and guarantee	**22.7**	16.0
Loan commitment fees	**1.2**	1.2
Other fee and commission income	**1.5**	1.5
Total fee and commission income	**50.0**	43.1
Fee and commission expense	**(1.5)**	(0.9)
Net fee and commission income	**48.5**	42.2

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For the year ended 31st December 2011

22. FEE AND COMMISSION INCOME (continued)

Investment banking and management fees comprise fees relating to the provision of investment management and financial services, including asset and fund management, underwriting activities, and services relating to structured financing, privatisations, IPOs, and mergers and acquisitions.

Investment banking and management fees for the year ended 31st December 2011 included fee income relating to the Group's fiduciary activities amounting to US$19.6 million (2010: US$15.2 million).

Fee and commission expense principally comprises security custody fees.

23. TRADING INCOME

	2011 US$ millions	2010 US$ millions
Foreign exchange	**10.3**	8.7
Debt securities	**3.7**	-
Managed funds	**3.2**	3.5
Interest rate derivatives	**0.4**	0.5
	17.6	12.7

Trading income comprises gains and losses arising both on the purchase and sale, and from changes in the fair value, of trading instruments, together with the related interest income, interest expense and dividend income. Trading income accordingly incorporates all income and expenses related to the Group's trading activities.

Foreign exchange includes spot and forward foreign exchange contracts, and currency futures and options. Foreign exchange income principally comprised income generated from customer-related activities.

Interest rate derivatives includes interest rate swaps, forward rate agreements, interest rate options, interest rate futures and credit derivatives.

An analysis of the basis used for determining the fair values of held-for-trading financial assets and liabilities is set out in note 37.

24. OTHER INCOME

Other income principally comprised dividends on available-for-sale equity investments, profits realised on the sale of investment securities and profits arising on the repurchase of the Group's senior and subordinated term financing.

25. OTHER OPERATING EXPENSES

Other operating expenses for the year ended 31st December 2010 included US$15.0 million of non-recurring costs associated with the implementation of the Group's new business strategy. No such costs were incurred during the year ended 31st December 2011.

26. SEGMENTAL INFORMATION

Segmental information is presented in respect of the Group's business and geographical segments. The primary reporting format, business segments, reflects the manner in which financial information is evaluated by the Board of Directors and the Group Management Committee.

a) Business segments

For financial reporting purposes, the Group is organised into four main operating segments:-

- Wholesale banking: the provision of wholesale commercial financing and other credit facilities for corporate and institutional customers, and the provision of financial advisory services relating to structured financing, privatisations, IPOs and mergers and acquisitions.

26. SEGMENTAL INFORMATION (continued)

a) Business segments (continued)

- Treasury: the provision of a broad range of treasury and capital market products and services to corporate and financial institution clients, money market, proprietary investment and trading activities and the management of the Group's balance sheet, including funding.
- Financial markets: the provision of asset and fund management services.
- Corporate and support units: income arising on the investment of the Group's net free capital funds and expenses incurred by support units.

The results reported for the business segments are based on the Group's internal financial reporting systems. The accounting policies of the segments are the same as those applied in the preparation of these consolidated financial statements and are set out in note 2. Transactions between business segments are conducted on normal commercial terms and conditions. Transfer pricing between the business units is based on the market cost of funds.

Segment results, assets and liabilities comprise items directly attributable to the business segments. Liabilities reported for corporate and support units comprise senior and subordinated term finance facilities and related accrued interest, the cost of which is recharged to the relevant operating business segments.

The business segment analysis is as follows:-

	Wholesale banking US$ millions	Treasury US$ millions	Financial markets US$ millions	Corporate and support units US$ millions	Total US$ millions
2011					
Net interest income	**49.1**	**41.6**	**-**	**53.1**	**143.8**
Total income	**81.1**	**59.6**	**23.2**	**63.0**	**226.9**
Segment result	**25.0**	**53.1**	**16.2**	**14.7**	**109.0**
Taxation charge on overseas activities					**(4.5)**
Net income after tax					**104.5**
Segment assets	**6,884.9**	**9,599.4**	**25.9**	**278.7**	**16,788.9**
Segment liabilities	**-**	**11,067.1**	**9.9**	**3,749.1**	**14,826.1**
Total equity					**1,962.8**
Total liabilities and equity					**16,788.9**
2010					
Net interest income	107.6	20.1	-	28.5	156.2
Total income	135.8	35.3	18.1	34.6	223.8
Segment result	106.5	38.9	10.5	(49.4)	106.5
Taxation charge on overseas activities					(6.1)
Net income after tax					100.4
Segment assets	7,961.0	7,298.0	9.6	259.1	15,527.7
Segment liabilities	-	10,357.3	8.8	3,243.6	13,609.7
Total equity					1,918.0
Total liabilities and equity					15,527.7

During the year ended 31st December 2011, the Group implemented, as part of its liquidity management framework, a new funds transfer pricing methodology based on the marginal cost of funds (matched maturity cost of funds) to replace the previous average cost of funds transfer pricing methodology. This resulted in a year-on-year decrease in wholesale banking net interest income and an increase in corporate net interest income.

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For the year ended 31st December 2011

26. SEGMENTAL INFORMATION (continued)

b) Geographical segments

Although the Group's three main business segments are managed on a worldwide basis, they are considered to operate in two geographical markets: the GCC and the rest of the world.

The geographical composition of total income and total assets based on the location in which transactions are booked and income is recorded was as follows:-

	2011		2010	
	Total income US$ millions	**Total assets US$ millions**	Total income US$ millions	Total assets US$ millions
GCC	**178.6**	**13,805.1**	188.4	13,470.2
Other countries	**48.3**	**2,983.8**	35.4	2,057.5
	226.9	**16,788.9**	223.8	15,527.7

The geographical analyses of deposits and risk assets are set out in notes 13 and 28 respectively.

27. RISK MANAGEMENT

The principal risks associated with the Group's businesses are credit risk, market risk, liquidity risk and operational risk. The Group has a comprehensive risk management framework in place for managing these risks which is constantly evolving as the business activities change in response to credit, market, product and other developments. The risk management framework is guided by a number of overriding principles including the formal definition of risk management governance, an evaluation of risk appetite expressed in terms of formal risk limits, risk oversight independent of business units, disciplined risk assessment and measurement including Value-at-Risk (VaR) methodologies and portfolio stress testing, and risk diversification. The Board of Directors set the Group's overall risk parameters and risk tolerances, and the significant risk management policies. A Board Risk Policy Committee reviews and reports to the Board of Directors on the Group's risk profile and risk taking activities. A Management Committee, chaired by the Group Chief Executive Officer, has the primary responsibility for sanctioning risk taking activities and risk management policies within the overall risk parameters and tolerances defined by the Board of Directors. A Group Risk Committee, under the chairmanship of the Chief Risk Officer and comprising the Group's most senior risk professionals, provides a forum for the review and approval of risk measurement methodologies, risk control processes and the approval of new products. The Group Risk Committee also reviews all risk policies and limits that require the formal approval of the Management Committee. The risk management control process is based on a detailed structure of policies, procedures and limits, and comprehensive risk measurement and management information systems for the control, monitoring and reporting of risks. Periodic reviews by internal and external auditors and regulatory authorities subject the risk management processes to additional scrutiny which help to further strengthen the risk management environment.

The principal risks associated with the Group's businesses and the related risk management processes are described in detail in the Basel 2 Pillar 3 disclosure report in the Annual Report, and are summarised below together with additional quantitative analysis:-

a) Credit risk

Credit risk is the risk that counterparties will be unable to meet their obligations to the Group. Credit risk arises principally from the Group's lending and investment activities in addition to other transactions involving both on- and off-balance sheet financial instruments. Disciplined processes are in place at both the business unit and corporate level that are intended to ensure that risks are accurately assessed and properly approved and monitored. Formal credit limits are applied at the individual transaction, counterparty, country and portfolio levels. Overall exposures are also evaluated to ensure a broad diversification of credit risk. The credit management process involves the monitoring of concentrations by product, industry, single obligor, risk grade and geography, and the regular appraisal of counterparty credit quality through the analysis of qualitative and quantitative information.

27. RISK MANAGEMENT (continued)

a) Credit risk (continued)

Credit risk is actively managed and rigorously monitored in accordance with well-defined credit policies and procedures. Prior to the approval of a credit proposal, a detailed credit risk assessment is carried out which includes an analysis of the obligor's financial condition, market position, business environment and quality of management. The risk assessment generates an internal credit risk rating for each exposure, which affects the credit approval decision and the terms and conditions of the transaction. For cross border transactions an analysis of country risk is also conducted. The Group bases its credit decision for an individual counterparty on the aggregate Group exposure to that counterparty and all its related entities. Groupwide credit limit setting and approval authorisation requirements are conducted within Board approved guidelines, and the measurement, monitoring and control of credit exposures are done on a Groupwide basis in a consistent manner.

The Group also mitigates its credit exposures on foreign exchange and derivative financial instruments through the use of master netting agreements and collateral arrangements.

Maximum exposure to credit risk

The gross maximum exposure to credit risk before applying collateral, guarantees and other credit enhancements was as follows:-

	31.12.11 **US$ millions**	31.12.10 US$ millions
Balance sheet items:		
Cash and other liquid assets	**858.7**	863.9
Securities purchased under agreements to resell	**280.0**	180.0
Placements	**5,394.0**	3,576.3
Trading securities	**83.7**	79.7
Investment securities	**3,151.7**	3,067.8
Loans and advances	**6,751.8**	7,510.1
Other assets, excluding derivative-related items	**85.6**	77.1
Total on-balance sheet credit exposure	**16,605.5**	15,354.9
Off-balance sheet items:		
Credit-related contingent items	**3,569.0**	2,149.9
Foreign exchange-related items	**31.4**	11.9
Derivative-related items	**77.7**	90.1
Total off-balance sheet credit exposure	**3,678.1**	2,251.9
Total gross credit exposure	**20,283.6**	17,606.8

Credit Risk Profile

The Group monitors, manages and controls credit risk exposures based on an internal credit rating system that rates individual obligors based on a rating scale from 1 to 10, subject to positive (+) and negative (-) modifiers for rating grades 2 to 6. The internal credit rating is a measure of the credit-worthiness of a single obligor, based on an assessment of the credit risk relating to senior unsecured, medium term, foreign currency credit exposure. The primary objectives of the internal credit rating system are the maintenance of a single uniform standard for credit quality measurement, and to serve as the primary basis for Board-approved risk parameters and delegated credit authority limits. The internal credit rating system also serves as a key input into the Group's risk-adjusted return on capital (RAROC) performance measurement system. Ratings are assigned to obligors, rather than facilities, and reflect a medium term time horizon, thereby rating through an economic cycle.

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For the year ended 31st December 2011

27. RISK MANAGEMENT (continued)

a) Credit risk (continued)

The internal ratings map directly to the rating grades used by the international credit rating agencies as follows:-

Internal rating grade	Internal classification	Historical default rate range	External Rating Fitch and Standard & Poor's	Moody's
		%		
Investment grade				
Rating grade 1	Standard	0.00 - 0.00	AAA	Aaa
Rating grade 2	Standard	0.00 - 0.04	AA	Aa
Rating grade 3	Standard	0.07 - 0.08	A	A
Rating grade 4	Standard	0.16 - 0.38	BBB	Baa
Sub-investment grade				
Rating grade 5	Standard	0.55 - 1.30	BB	Ba
Rating grade 6	Standard	2.60 - 9.12	B	B
Rating grade 7	Standard	27.39	CCC	Caa
Classified				
Rating grade 8	Substandard	27.39	CC	Ca
Rating grade 9	Doubtful	27.39	C	C
Rating grade 10	Loss	-	D	-

The historical default rates represent the range of probability of defaults between the positive and negative modifiers for each rating grade based on Standard & Poor's one year default rates for the 30 years from 1981 to 2010 for senior unsecured obligations. The default rates represent the averages over the 30-year period and therefore reflect the full range of economic conditions over that period.

27. RISK MANAGEMENT (continued)

a) Credit risk (continued)

The credit risk profile, based on internal credit ratings, was as follows:-

	31.12.11			31.12.10		
	Placements, reverse repos & other liquid assets US$ millions	**Securities US$ millions**	**Loans and advances US$ millions**	Placements, reverse repos & other liquid assets US$ millions	Securities US$ millions	Loans and advances US$ millions
Neither past due nor impaired						
Rating grades 1 to 4-	**6,519.7**	**2,776.7**	**4,224.1**	4,570.2	2,646.4	4,668.3
Rating grades 5+ to 5-	**13.0**	**96.6**	**1,809.5**	50.0	101.5	1,514.0
Rating grades 6+ to 6-	-	**32.4**	**281.5**	-	30.0	654.4
Rating grade 7	-	-	-	-	-	84.7
Equity investments	-	**313.4**	-	-	356.1	-
Carrying amount	**6,532.7**	**3,219.1**	**6,315.1**	4,620.2	3,134.0	6,921.4
Past due but not impaired						
Rating grades 1 to 7	-	-	**159.9**	-	-	262.4
Carrying amount	-	-	**159.9**	-	-	262.4
Past due and individually impaired						
Rating grade 7	-	-	**33.7**	-	-	67.4
Rating grade 8	-	-	**14.4**	-	-	79.9
Rating grade 9	-	-	**42.8**	-	-	121.2
Carrying amount	-	-	**90.9**	-	-	268.5
Individually impaired but not past due						
Rating grades 1 to 7	-	-	**128.2**	-	-	45.3
Rating grade 8	-	-	-	-	-	12.5
Rating grade 9	-	-	**57.7**	-	-	-
Equity investments	-	**16.3**	-	-	13.5	-
Carrying amount	-	**16.3**	**185.9**	-	13.5	57.8
Total	**6,532.7**	**3,235.4**	**6,751.8**	4,620.2	3,147.5	7,510.1

The above analysis is reported net of the following provisions for impairment:-

Provisions for impairment	-	**(71.9)**	**(619.2)**	-	(67.8)	(642.3)

Individually impaired financial assets represent assets for which there is objective evidence that the Group will not collect all amounts due, including both principal and interest, in accordance with the contractual terms of the obligation.

Unimpaired financial assets are stated net of allocated non-specific provisions for impairment.

The Group holds collateral against loans and advances in the form of physical assets, cash deposits, securities and guarantees. The amount and type of collateral is dependent upon the assessment of the credit risk of the counterparty. The market / fair 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. Collateral is not usually held against securities or placements and no such collateral was held at either 31st December 2011 or 31st December 2010.

Notes to the Consolidated Financial Statements (continued)

For the year ended 31st December 2011

27. RISK MANAGEMENT (continued)

a) Credit risk (continued)

An analysis of the credit risk in respect of foreign exchange and derivative financial instruments is set out in note 31 while the notional and risk-weighted exposures for off-balance sheet credit-related financial instruments are set out in note 32.

Credit risk concentration

The Group monitors concentrations of credit risk by sector and by geographic location. The industrial classification of loans and advances is set out in note 10(a). The geographical distribution of risk assets is set out in note 28. An analysis of the credit risk in respect of foreign exchange and derivative financial instruments is set out in note 31.

Settlement risk

Settlement risk is the risk of loss due to the failure of a counterparty to honour its obligations to deliver cash, securities, or other assets as contractually agreed.

For certain types of transactions, the Group mitigates this risk by conducting settlements through a settlement or clearing agent to ensure that a trade is settled only when both parties have fulfilled their contractual settlement obligations. Settlement limits form part of the credit approval and limit monitoring process.

b) Market risk

Market risk is the risk of loss due to adverse changes in interest rates, foreign exchange rates, equity prices and market conditions, such as liquidity. The principal market risks to which the Group is exposed are interest rate risk, foreign exchange risk and equity price risk associated with its trading, investment and asset and liability management activities. The portfolio effects of holding a diversified range of instruments across a variety of businesses and geographic areas contribute to a reduction in the potential negative impact on earnings from market risk factors.

- **Trading market risk:** The Group's trading activities principally comprise trading in debt and equity securities, foreign exchange and derivative financial instruments. Derivative financial instruments include futures, forwards, swaps and options in the interest rate, foreign exchange, equity, credit and commodity markets. The Group manages and controls the market risk within its trading portfolios through limit structures of both a VaR and non-VaR nature. Non-VaR based constraints relate, inter alia, to positions, volumes, concentrations, allowable losses and maturities. VaR is a risk measurement concept which uses statistical models to estimate, within a given level of confidence, the maximum potential negative change in the market value of a portfolio over a specified time horizon resulting from an adverse movement in rates and prices. It is recognised that there are limitations to the VaR methodology. These limitations include the fact that the historical data may not be the best proxy for future price movements. The Group performs regular back testing exercises to compare actual profits and losses with the VaR estimates to monitor the statistical validity of the VaR model. VaR is calculated based on the Group's market risk exposures at the close of the business each day. Intra-day risk levels may vary from those reported at the end of the day. In addition, losses beyond the specified confidence level are not captured by the VaR methodology. VaR is not a measure of the absolute limit of market risk and losses in excess of the VaR amounts will, on occasion, arise. To manage the risk associated with extreme market movements, the Group conducts stress testing which measures the impact of simulated abnormal changes in market rates and prices on the market values of the portfolios. The composition of the debt and equity trading securities is set out in note 8. An analysis of derivative financial instruments, including the VaR of foreign exchange and derivative trading contracts, is set out in note 31.

27. RISK MANAGEMENT (continued)

b) Market risk (continued)

- **Trading market risk:** (continued)

The VaR by risk class for the Group's trading positions, as calculated in accordance with the basis set out in note 34, was as follows:-

	2011				2010			
	31.12.11	Average	High	Low	31.12.10	Average	High	Low
	US$ millions	US$ millions	US$ millions	US$ millions	US$ millions	US$ millions	US$ millions	US$ millions
Interest rate risk	1.2	1.2	1.5	0.9	1.3	0.2	1.3	0.1
Foreign exchange risk	-	0.1	0.2	-	0.1	0.1	0.2	-
Equity risk	0.1	0.1	0.2	0.1	0.1	0.3	0.7	0.1
Total diversified risk	1.3	1.3	1.6	1.0	1.3	0.5	1.4	0.2

- **Non-trading market risk:** Structural interest rate risk arises in the Group's core balance sheet as a result of mismatches in the repricing of interest rate sensitive financial assets and liabilities. The associated interest rate risk is managed within VaR limits and through the use of models to evaluate the sensitivity of earnings to movements in interest rates. The repricing profile and related interest rate sensitivity of the Group's financial assets and liabilities are set out in note 30. The Group is exposed to the impact of changes in credit spreads on the fair value of available-for-sale debt securities. Movements in the fair value of available-for-sale securities are accounted for in equity. Credit spread risk is managed within VaR limits and through the use of models to evaluate the sensitivity of changes in equity to movements in credit spreads. Based on the available-for-sale debt securities held at 31st December 2011, a 1 b.p. increase in credit spreads would result in a US$0.8 million decrease in fair value (2010: US$0.8 million). The Group does not maintain material foreign currency exposures. In general, the Group's policy is to match financial assets and liabilities in the same currency or to mitigate currency risk through the use of currency swaps. Details of significant foreign currency net open positions are set out in note 31(e).

The more significant market risk-related activities of a non-trading nature undertaken by the Group, the related risks associated with those activities, and the types of derivative financial instruments used to manage and mitigate such risks are summarised as follows:-

Activity	Risk	Risk Mitigant
Management of the return on variable rate assets funded by shareholders' funds	Reduced profitability due to a fall in short-term interest rates	Receive fixed interest rate swaps
Fixed rate assets funded by floating rate liabilities	Sensitivity to increases in short-term interest rates	Pay fixed interest rate swaps
Investment in foreign currency assets	Sensitivity to strengthening of US$ against other currencies	Currency swaps
Profits generated in foreign currencies	Sensitivity to strengthening of US$ against other currencies	Forward foreign exchange contracts and purchased currency options

c) Liquidity risk

Liquidity risk is the risk that sufficient funds are not available to meet the Group's financial obligations on a punctual basis as they fall due.

Liquidity management policies are designed to ensure that funds are available at all times to meet the funding requirements of the Group, even in adverse conditions. In normal conditions the objective is to ensure that there are sufficient funds available not only to meet current financial commitments but also to facilitate business expansion. These objectives are met through the

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For the year ended 31st December 2011

27. RISK MANAGEMENT (continued)

c) Liquidity risk (continued)

application of prudent liquidity controls. These controls provide security of access to funds without undue exposure to increased costs from the liquidation of assets or the aggressive bidding for deposits. The Group's liquidity controls ensure that, over the short-term, the future profile of cash flows from maturing assets is adequately matched to the maturity of liabilities. Liquidity controls also provide for the maintenance of a stock of liquid and readily realisable assets and a diversified deposit base in terms of both maturities and range of depositors.

The management of liquidity and funding is primarily conducted in the Group's individual geographic entities within limits set and approved by the Board of Directors. The limits take account of the depth and liquidity of the market in which the entity operates. It is the Group's general policy that each geographic entity should be self-sufficient in relation to funding its own operations.

The Group's liquidity management policies include the following:-

- the monitoring of (i) future contractual cash flows against approved limits, and (ii) the level of liquid resources available in a stress event
- the monitoring of balance sheet liquidity ratios
- the monitoring of the sources of funding in order to ensure that funding is derived from a diversified range of sources
- the monitoring of depositor concentrations in order to avoid undue reliance on individual depositors
- the maintenance of a satisfactory level of term financing
- the maintenance of appropriate standby funding arrangements; and
- the maintenance of liquidity and funding contingency plans. These plans identify early indicators of stress conditions and prescribe the actions to be taken in the event of systemic or other crisis, while minimising adverse long-term implications for the Group's business activities.

The Group has established limits which restrict the volume of liabilities maturing in the short-term. An independent risk management function monitors the future cash flow maturity profile against approved limits on a daily basis. The cash flows are monitored against limits applying to both daily and cumulative cash flows occurring over a 30-day period. The liquidity limits ensure that the net cash outflows over a 30-day period do not exceed the eligible stock of available liquid resources. The cash flow analysis is also monitored on a weekly basis by the Assets and Liabilities Committee (ALCO).

Customer deposits form a significant part of the Group's funding. The Group places considerable importance on maintaining the stability of both its customer and interbank deposits. The stability of deposits depends on maintaining confidence in the Group's financial strength and financial transparency.

The maturity profile of assets and liabilities is set out in note 29. An analysis of debt investment securities by rating classification is set out in note 27(a).

d) Operational risk

Operational risk is the risk of unexpected losses resulting from inadequate or failed internal controls or procedures, systems failures, fraud, business interruption, compliance breaches, human error, management failure or inadequate staffing.

A framework and methodology has been developed to identify and control the various operational risks. While operational risk cannot be entirely eliminated, it is managed and mitigated by ensuring that the appropriate infrastructure, controls, systems, procedures, and trained and competent people are in place throughout the Group. A strong internal audit function makes regular, independent appraisals of the control environment in all identified risk areas. Adequately tested contingency arrangements are also in place to support operations in the event of a range of possible disaster scenarios.

27. RISK MANAGEMENT (continued)

e) Capital management

The Group's lead regulator, the Central Bank of Bahrain (CBB), sets and monitors capital requirements for the Group as a whole. The parent company and individual banking operations are directly supervised by their local regulators.

As referred to in more detail in note 34, the Group adopted the Basel 2 capital adequacy framework with effect from 1st January 2008.

In applying current capital requirements, the CBB requires the Group to maintain a prescribed minimum ratio of total regulatory capital to total risk-weighted assets. The CBB's minimum risk asset ratio is 12 per cent compared to a minimum ratio of 8 per cent prescribed by the Basel Committee on Banking Supervision. The Group calculates regulatory capital requirements for general market risk in its trading portfolios using a Value-at-Risk model and uses the CBB's prescribed risk weightings under the standardised approach to determine the risk-weighted amounts for credit risk and specific market risk. Operational risk is calculated in accordance with the standardised approach. The regulatory capital requirement is calculated by applying the CBB's prescribed range of beta coefficients, ranging from 12 to 18 per cent, to the average gross income for the preceding three financial years for each of eight predefined business lines.

The Group's regulatory capital is analysed into two tiers:-

- Tier 1 capital, comprising issued share capital, share premium, retained earnings and reserves, adjusted to exclude revaluation gains and losses arising on the remeasurement to fair value of available-for-sale securities and derivative cash flow hedging transactions with the exception of unrealised losses arising on the remeasurement to fair value of equity securities classified as available-for-sale securities.
- Tier 2 capital, comprising qualifying subordinated term finance, collective impairment provisions and 45 per cent of unrealised gains arising on the remeasurement to fair value of equity securities classified as available-for-sale securities.

The CBB applies various limits to elements of the capital base. The amount of innovative tier 1 securities cannot exceed 15 per cent of total tier 1 capital; qualifying tier 2 capital cannot exceed tier 1 capital; and qualifying subordinated term finance cannot exceed 50 per cent of tier 1 capital. There are also restrictions on the amount of collective impairment provisions that may be included as part of tier 2 capital. Collective impairment provisions cannot exceed 1.25 per cent of total risk-weighted assets.

The Group's risk exposures are categorised as either trading book or banking book, and risk-weighted assets are determined according to specified requirements that seek to reflect the varying levels of risk attached to assets and off-balance sheet exposures.

The Group's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain the future development of the business. The impact of the level of capital on shareholders' return is also recognised as well as the need to maintain a balance between the higher returns that might be possible with greater gearing and the advantages and security afforded by a sound capital position. The Group manages its capital structure and makes adjustments to the structure taking account of changes in economic conditions and strategic business plans. The capital structure may be adjusted through the dividend payout and the issue of new shares.

The Group complied with all externally imposed capital requirements throughout the years ended 31st December 2011 and 31st December 2010.

There have been no material changes in the Group's management of capital during the years ended 31st December 2011 and 31st December 2010.

The capital adequacy ratio calculation is set out in note 34.

Notes to the Consolidated Financial Statements (continued)

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28. GEOGRAPHICAL DISTRIBUTION OF RISK ASSETS

	31.12.11					31.12.10
	Placements, reverse repos & other liquid assets US$ millions	Securities US$ millions	Loans and advances US$ millions	Credit-related contingent items US$ millions	Total US$ millions	Total US$ millions
GCC	1,982.0	1,362.2	6,354.5	3,168.7	12,867.4	11,589.7
Other Middle East & North Africa	13.0	24.3	69.2	13.9	120.4	305.5
Europe	3,798.6	842.9	311.3	161.8	5,114.6	3,940.2
North America	385.8	705.8	0.2	201.8	1,293.6	807.2
Asia	353.3	277.5	16.6	22.8	670.2	756.2
Latin America	-	22.7	-	-	22.7	28.9
	6,532.7	3,235.4	6,751.8	3,569.0	20,088.9	17,427.7

At 31st December 2011, risk exposures to customers and counterparties in the GCC represented 64.1 per cent (2010: 66.5 per cent) of total risk assets. The risk asset profile reflects the Group's strategic focus on wholesale banking activities in the GCC states.

Placements, reverse repos and other liquid assets exposure to Europe principally comprised exposure to financial institutions located in Germany, France, Switzerland, the United Kingdom and Holland.

An analysis of derivative and foreign exchange instruments is set out in note 31.

29. MATURITIES OF ASSETS AND LIABILITIES

The maturity profile of the carrying amount of assets and liabilities, based on the contractual maturity dates, was as follows:-

	Within 3 months US$ millions	4 months to 1 year US$ millions	Years 2 and 3 US$ millions	Years 4 and 5 US$ millions	Over 5 years and other US$ millions	Total US$ millions
At 31st December 2011						
Cash and other liquid assets	559.5	299.2	-	-	-	858.7
Securities purchased under agreements to resell	150.0	130.0	-	-	-	280.0
Placements	5,270.0	124.0	-	-	-	5,394.0
Trading securities	56.9	-	-	-	26.8	83.7
Investment securities	151.5	288.6	982.2	1,259.3	470.1	3,151.7
Loans and advances	1,562.4	1,192.4	1,306.1	814.6	1,876.3	6,751.8
Other assets	70.7	31.2	7.2	-	159.9	269.0
Total assets	7,821.0	2,065.4	2,295.5	2,073.9	2,533.1	16,788.9
Deposits	8,671.5	1,398.1	-	-	-	10,069.6
Securities sold under agreements to repurchase	283.3	-	-	-	-	283.3
Other liabilities	97.0	19.5	8.4	-	180.2	305.1
Term financing	-	1,756.8	464.9	1,946.4	-	4,168.1
Equity	-	-	-	-	1,962.8	1,962.8
Total liabilities & equity	9,051.8	3,174.4	473.3	1,946.4	2,143.0	16,788.9
At 31st December 2010						
Total assets	5,881.9	1,867.5	2,704.7	1,987.9	3,085.7	15,527.7
Total liabilities & equity	7,597.0	2,521.8	1,898.2	1,295.5	2,215.2	15,527.7

29. MATURITIES OF ASSETS AND LIABILITIES (continued)

The asset and liability maturities presented in the table above are based on contractual repayment arrangements and as such do not take account of the effective maturities of deposits as indicated by the Group's deposit retention records. Formal liquidity controls are nevertheless based on contractual asset and liability maturities.

The gross cash flows payable by the Group under financial liabilities, based on contractual maturity dates, was as follows:-

	Within 3 months US$ millions	4 months to 1 year US$ millions	Years 2 and 3 US$ millions	Years 4 and 5 US$ millions	Over 5 years US$ millions
At 31st December 2011					
Deposits	**8,684.7**	**1,411.5**	-	-	-
Securities sold under agreements to repurchase	**285.7**	-	-	-	-
Term financing	**8.0**	**1,794.6**	**530.1**	**1,986.5**	-
Derivative financial instruments:					
- contractual amounts payable	**46.5**	**73.6**	**170.0**	**115.0**	**49.6**
- contractual amounts receivable	**(40.3)**	**(59.3)**	**(140.1)**	**(97.5)**	**(46.4)**
Total undiscounted financial liabilities	**8,984.6**	**3,220.4**	**560.0**	**2,004.0**	**3.2**
At 31st December 2010					
Deposits	6,728.0	1,994.9	9.6	-	-
Securities sold under agreements to repurchase	779.1	169.4	-	-	-
Term financing	2.1	401.5	1,991.2	1,401.9	157.0
Derivative financial instruments:					
- contractual amounts payable	35.4	94.8	203.8	169.1	112.8
- contractual amounts receivable	(15.1)	(63.3)	(167.9)	(142.9)	(100.9)
Total undiscounted financial liabilities	7,529.5	2,597.3	2,036.7	1,428.1	168.9

Information on the contractual terms for the drawdown of gross loan commitments is set out in note 32.

The figures in the table above do not agree directly to the carrying amounts in the consolidated statement of financial position as they incorporate all cash flows, on an undiscounted basis, related to both principal as well as those associated with future coupon and interest payments. Coupons and interest payments for periods for which the interest rate has not yet been determined have been calculated based on the relevant forward rates of interest prevailing at the balance sheet date.

A maturity analysis of derivative and foreign exchange instruments based on notional amounts is set out in note 31(c).

Notes to the Consolidated Financial Statements (continued)

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30. INTEREST RATE RISK

The repricing profile of assets and liabilities categories were as follows:-

	Within 3 months US$ millions	Months 4 to 6 US$ millions	Months 7 to 12 US$ millions	Over 1 year US$ millions	Non-interest bearing items US$ millions	Total US$ millions
At 31st December 2011						
Cash and other liquid assets	824.9	33.8	-	-	-	858.7
Securities purchased under agreements to resell	150.0	50.0	80.0	-	-	280.0
Placements	5,369.0	25.0	-	-	-	5,394.0
Trading securities	56.9	-	-	-	26.8	83.7
Investment securities:-						
- Fixed rate	-	126.1	107.9	713.8	-	947.8
- Floating rate	1,810.4	104.3	-	-	(13.7)	1,901.0
- Equities & equity funds	-	-	-	-	302.9	302.9
Loans and advances	4,741.9	2,095.3	112.8	11.8	(210.0)	6,751.8
Other assets	-	-	-	-	269.0	269.0
Total assets	12,953.1	2,434.5	300.7	725.6	375.0	16,788.9
Deposits	9,742.9	251.5	75.2	-	-	10,069.6
Securities sold under agreements to repurchase	283.3	-	-	-	-	283.3
Other liabilities	-	-	-	-	305.1	305.1
Term financing	4,103.2	64.9	-	-	-	4,168.1
Equity	-	-	-	-	1,962.8	1,962.8
Total liabilities & equity	14,129.4	316.4	75.2	-	2,267.9	16,788.9
Interest rate sensitivity gap	(1,176.3)	2,118.1	225.5	725.6	(1,892.9)	-
Cumulative interest rate sensitivity gap	(1,176.3)	941.8	1,167.3	1,892.9	-	-
At 31st December 2010						
Cumulative interest rate sensitivity gap	(13.9)	842.6	1,030.5	1,840.1	-	-

The repricing profile is based on the remaining period to the next interest repricing date. Derivative financial instruments that have been used for asset and liability management purposes to hedge exposure to interest rate risk are incorporated in the repricing profiles of the related hedged assets and liabilities. The non-specific investment security and loan provisions are classified in non-interest bearing items.

The substantial majority of assets and liabilities reprice within one year. Accordingly there is limited exposure to interest rate risk. The principal interest rate risk beyond one year as set out in the asset and liability repricing profile, represents the investment of the Group's net free capital in fixed rate government securities. At 31st December 2011 the modified duration of these fixed rate securities was 2.27. Modified duration represents the approximate percentage change in the portfolio value resulting from a 100 basis point change in yield. More precisely in dollar terms, the price value of a basis point of the fixed rate securities was US$175,000.

Based on the repricing profile at 31st December 2011, and assuming that the financial assets and liabilities were to remain until maturity or settlement with no action taken by the Group to alter the interest rate risk exposure, an immediate and sustained one per cent increase in interest rates across all maturities would result in a reduction in net income before tax for the following

30. INTEREST RATE RISK (continued)

year and in the Group's equity by approximately US$11.3 million and US$30.4 million respectively (2010: US$11.1 million and US$32.2 million respectively). The impact on the Group's equity represents the cumulative effect of the increase in interest rates over the entire duration of the mismatches in the repricing profile of the interest rate sensitive financial assets and liabilities.

The Value-at-Risk by risk class for the Group's trading positions is set out in note 27. The market risk relating to foreign exchange and derivative trading instruments is set out in note 31.

31. DERIVATIVE AND FOREIGN EXCHANGE INSTRUMENTS

The Group utilises derivative and foreign exchange instruments to meet the needs of its customers, to generate trading revenues and as part of its asset and liability management (ALM) activity to hedge its own exposure to market risk. Derivative instruments are contracts whose value is derived from one or more financial instruments or indices. They include futures, forwards, swaps and options in the interest rate, foreign exchange, equity, credit and commodity markets. Derivatives and foreign exchange are subject to the same types of credit and market risk as other financial instruments. The Group has appropriate and comprehensive Board-approved policies and procedures for the control of exposure to both market and credit risk from its derivative and foreign exchange activities.

In the case of derivative transactions, the notional principal typically does not change hands. It is simply a quantity which is used to calculate payments. While notional principal is a volume measure used in the derivative and foreign exchange markets, it is neither a measure of market nor credit risk. The Group's measure of credit exposure is the cost of replacing contracts at current market rates should the counterparty default prior to the settlement date. Credit risk amounts represent the gross unrealised gains on non-margined transactions before taking account of any collateral held or any master netting agreements in place.

The Group participates in both exchange traded and over-the-counter (OTC) derivative markets. Exchange traded instruments are executed through a recognised exchange as standardised contracts and primarily comprise futures and options. OTC contracts are executed between two counterparties who negotiate specific agreement terms, including the underlying instrument, notional amount, maturity and, where appropriate, exercise price. In general, the terms and conditions of these transactions are tailored to the requirements of the Group's customers although conform to normal market practice. Industry standard documentation is used, most commonly in the form of a master agreement. The existence of a master netting agreement is intended to provide protection to the Group in the event of a counterparty default.

The Group's principal foreign exchange transactions are forward foreign exchange contracts, currency swaps and currency options. Forward foreign exchange contracts are agreements to buy or sell a specified quantity of foreign exchange on a specific future date at an agreed rate. A currency swap involves the exchange, or notional exchange, of equivalent amounts of two currencies and a commitment to exchange interest periodically until the principal amounts are re-exchanged on a specified future date. Currency options provide the buyer with the right, but not the obligation, either to purchase or sell a fixed amount of a currency at a specified exchange rate on or before a specified future date. As compensation for assuming the option risk, the option seller (or writer) receives a premium at the start of the option period.

The Group's principal interest rate-related derivative transactions are interest rate swaps, forward rate agreements, futures and options. An interest rate swap is an agreement between two parties to exchange fixed rate and floating rate interest by means of periodic payments based upon a notional principal amount and the interest rates defined in the contract. Certain agreements combine interest rate and foreign currency swap transactions, which may or may not include the exchange of principal amounts. In a forward rate agreement, two parties agree a future settlement of the difference between an agreed rate and a future interest rate, applied to a notional principal amount for an agreed period. The settlement, which generally occurs at the start of the contract period, is the discounted present value of the payment that would otherwise be made at the end of that period. An interest rate future is an exchange traded contract for the delivery of a standardised amount of a fixed income security or time deposit at a future specified date. Interest rate options, including caps, floors and collars, provide the buyer with the right, but not the obligation, either to purchase or sell an interest rate financial instrument at a specified price or rate on or before a specified future date.

Notes to the Consolidated Financial Statements (continued)

For the year ended 31st December 2011

31. DERIVATIVE AND FOREIGN EXCHANGE INSTRUMENTS (continued)

The Group's principal equity-related derivative transactions are equity and stock index options. An equity option provides the buyer with the right, but not the obligation, either to purchase or sell a specified stock or index at a specified price or level on or before a specified future date.

The Group buys and sells credit protection through credit default swaps. Credit default swaps provide protection against the decline in value of a referenced asset as a result of credit events such as default or bankruptcy. It is similar in structure to an option whereby the purchaser pays a premium to the seller of the credit default swap in return for payment related to the deterioration in value of the referenced asset. Credit default swaps purchased and sold by the Group are classified as derivative financial instruments.

a) Product analysis

The table below summarises the aggregate notional and credit risk amounts of foreign exchange, interest rate, credit and equity-related derivative contracts.

	Notional amounts			Credit risk
	Trading	Hedging	Total	amounts
	US$ millions	US$ millions	US$ millions	US$ millions
At 31st December 2011				
Foreign exchange contracts:-				
Unmatured spot, forward and futures contracts	**1,088.8**	**3,267.8**	**4,356.6**	**31.4**
Interest rate contracts:-				
Interest rate swaps	**1,364.0**	**5,003.0**	**6,367.0**	**77.7**
Cross currency swaps	-	**533.3**	**533.3**	-
Options, caps and floors purchased	**24.3**	-	**24.3**	-
Options, caps and floors written	**24.3**	-	**24.3**	-
	1,412.6	**5,536.3**	**6,948.9**	**77.7**
Credit contracts:-				
Protection sold	**25.0**	-	**25.0**	-
Total	**2,526.4**	**8,804.1**	**11,330.5**	**109.1**
At 31st December 2010				
Total	2,409.3	7,568.2	9,977.5	102.0

There is no credit risk in respect of options, caps and floors written, and protection sold on credit contracts as they represent obligations of the Group.

At 31st December 2011 the Value-at-Risk of the foreign exchange, interest rate and credit derivative trading contracts analysed in the table above, as calculated in accordance with the basis set out in note 34, was US$0.1 million, nil and nil respectively (2010: US$0.1 million, US$0.1 million and nil). Value-at-Risk is a measure of market risk exposure and is accordingly separate and in addition to the credit risk exposure represented by the credit risk amounts in the table above.

b) Counterparty analysis

		31.12.11		31.12.10
Credit risk amounts	Banks	Corporates	Total	Total
	US$ millions	US$ millions	US$ millions	US$ millions
OECD countries	**31.3**	-	**31.3**	34.6
GCC countries	**0.2**	**58.5**	**58.7**	54.3
Other countries	**0.4**	**18.7**	**19.1**	13.1
	31.9	**77.2**	**109.1**	102.0

Credit risk is concentrated on major OECD-based banks and GCC-related customers.

31. DERIVATIVE AND FOREIGN EXCHANGE INSTRUMENTS (continued)

c) Maturity analysis

	Year 1 US$ millions	Years 2 & 3 US$ millions	Years 4 & 5 US$ millions	Over 5 years US$ millions	Total US$ millions
At 31st December 2011					
Foreign exchange contracts	**4,356.6**	**-**	**-**	**-**	**4,356.6**
Interest rate contracts	**3,762.0**	**706.3**	**1,669.3**	**811.3**	**6,948.9**
Credit contracts	**-**	**25.0**	**-**	**-**	**25.0**
Total	**8,118.6**	**731.3**	**1,669.3**	**811.3**	**11,330.5**
At 31st December 2010					
Total	6,711.0	981.7	1,140.6	1,144.2	9,977.5

The Group's derivative and foreign exchange activities are predominantly short-term in nature. Transactions with maturities over one year principally represent either fully offset trading transactions or transactions that are designated, and qualify, as fair value and cash flow hedges.

d) Fair value analysis

	31.12.11		31.12.10	
	Positive fair value US$ millions	**Negative fair value US$ millions**	Positive fair value US$ millions	Negative fair value US$ millions
Derivatives held for trading:-				
Forward foreign exchange contracts	**15.5**	**(2.1)**	2.2	(2.1)
Interest rate swaps and swaptions	**65.5**	**(63.1)**	64.9	(61.4)
	81.0	**(65.2)**	67.1	(63.5)
Derivatives held as cash flow hedges:-				
Interest rate swaps	**0.1**	**-**	-	-
Derivatives held as fair value hedges:-				
Interest rate swaps	**-**	**(47.3)**	-	(22.7)
Amount included in other assets / (other liabilities)	**81.1**	**(112.5)**	67.1	(86.2)

e) Significant net open positions

There were no significant derivative trading or foreign currency net open positions at either 31st December 2011 or at 31st December 2010.

f) Hedge effectiveness

Gains and losses recognised in the consolidated statement of income relating to fair value hedging relationships were as follows:-

	2011 US$ millions	2010 US$ millions
Net (losses) / gains on derivative fair value hedging instruments	**(32.7)**	28.9
Net (gains) / losses on hedged items attributable to the hedged risk	**(32.7)**	28.9

There were no ineffective portions of derivative fair value or cash flow hedging transactions recognised in the consolidated statement of income in either the year ended 31st December 2011 or 31st December 2010.

Certain derivative cash flow hedging transactions were unwound during the year ended 31st December 2009. The resultant realised profits are being recognised in the consolidated statement of income over the respective tenors of the original transactions for periods to 2014.

Notes to the Consolidated Financial Statements (continued)

For the year ended 31st December 2011

32. CREDIT-RELATED FINANCIAL INSTRUMENTS

Credit-related financial instruments include commitments to extend credit, standby letters of credit and guarantees which are designed to meet the financing requirements of customers. The credit risk on these transactions is generally less than the contractual amount. The table below sets out the notional principal amounts of outstanding credit-related contingent items and the risk-weighted exposures calculated in accordance with the capital adequacy guidelines of the Basel Committee on Banking Supervision.

	31.12.11		31.12.10	
	Notional principal amount US$ millions	**Risk-weighted exposure US$ millions**	Notional principal amount US$ millions	Risk-weighted exposure US$ millions
Direct credit substitutes	**309.2**	**285.0**	164.0	147.6
Transaction-related contingent items	**2,618.9**	**907.2**	1,237.2	474.3
Short-term self-liquidating trade-related contingent items	**189.0**	**30.3**	209.2	42.9
Commitments, including undrawn loan commitments and underwriting commitments under note issuance and revolving facilities	**451.9**	**186.4**	539.5	224.8
	3,569.0	**1,408.9**	2,149.9	889.6

Commitments may be drawndown on demand.

Direct credit substitutes at 31st December 2011 included financial guarantees amounting to US$242.0 million (2010: US$101.8 million). Financial guarantees may be called on demand.

The notional principal amounts reported above are stated gross before applying credit risk mitigants, such as cash collateral, guarantees and counter-indemnities. At 31st December 2011, the Group held cash collateral, guarantees, counter-indemnities or other high quality collateral in relation to credit-related contingent items amounting to US$732.9 million (2010: US$178.7 million).

33. CONTINGENT LIABILITIES

Litigation

The Bank and its subsidiaries are engaged in litigation in various jurisdictions. The litigation involves claims by and against Group companies which have arisen in the ordinary course of business. The directors of the Bank, after reviewing the claims pending against Group companies and based on the advice of relevant professional legal advisors, are satisfied that the outcome of these claims will not have a material adverse effect on the financial position of the Group.

34. CAPITAL ADEQUACY

The CBB's Basel 2 guidelines became effective on 1st January 2008 as the common framework for the implementation of the Basel Committee on Banking Supervision's (Basel Committee) Basel 2 capital adequacy framework for banks incorporated in the Kingdom of Bahrain.

34. CAPITAL ADEQUACY (continued)

The risk asset ratio calculated in accordance with the CBB's Basel 2 guidelines was as follows:-

	31.12.11 US$ millions	31.12.10 US$ millions
Regulatory capital base		
Tier 1 capital:		
Total equity	**1,962.8**	1,918.0
Tier 1 adjustments	**6.5**	12.0
Tier 1 capital	**1,969.3**	1,930.0
Tier 2 capital:		
Subordinated term financing	**316.7**	438.8
Non-specific provisions subject to 1.25% risk weighted exposure limitation	**128.4**	129.0
Tier 2 adjustments	**(25.1)**	11.0
Tier 2 capital	**420.0**	578.8
Total regulatory capital base	**2,389.3**	2,508.8

Risk-weighted exposure

	31.12.11		31.12.10	
	Notional principal amount US$ millions	**Risk-weighted exposure US$ millions**	Notional principal amount US$ millions	Risk-weighted exposure US$ millions
Credit risk				
Balance sheet items:				
Cash and other liquid assets	**858.7**	**190.1**	863.9	271.2
Securities purchased under agreements to resell	**280.0**	**1.8**	180.0	-
Placements	**5,394.0**	**923.5**	3,576.3	671.5
Investment securities	**3,151.7**	**1,203.8**	3,067.8	1,211.2
Loans and advances	**6,751.8**	**5,704.8**	7,510.1	6,394.8
Other assets	**269.0**	**183.4**	249.9	185.5
		8,207.4		8,734.2
Off-balance sheet items:				
Credit-related contingent items	**3,569.0**	**1,408.9**	2,149.9	889.6
Foreign exchange-related items	**4,356.6**	**27.2**	2,493.0	9.0
Derivative-related items	**6,973.9**	**14.1**	7,484.5	15.9
Forward placements	**39.5**	**7.9**	118.9	23.8
Repo counterparty risk	**-**	**8.6**	-	28.9
		1,466.7		967.2
Credit risk-weighted exposure		**9,674.1**		9,701.4
Market risk				
General market risk		**49.5**		61.2
Specific market risk		**65.9**		67.9
Market risk-weighted exposure		**115.4**		129.1
Operational risk				
Operational risk-weighted exposure		**483.2**		491.2
Total risk-weighted exposure		**10,272.7**		10,321.7
Tier 1 risk asset ratio		**19.2%**		18.7%
Total risk asset ratio		**23.3%**		24.3%

Notes to the Consolidated Financial Statements (continued)

For the year ended 31st December 2011

34. CAPITAL ADEQUACY (continued)

For regulatory Basel 2 purposes, the Group has initially adopted the standardised approach for credit risk. In time and subject to approval by the CBB, the Group plans to adopt the foundation internal ratings-based (FIRB) approach for credit risk as it is more closely aligned to the Group's internal risk and capital management methodologies. For market risk, the Group uses the internal models approach. GIB applies the standardised approach for determining the capital requirement for operational risk.

In accordance with the capital adequacy guidelines of the CBB, revaluation gains and losses arising on the remeasurement to fair value of available-for-sale securities and derivative cash flow hedging transactions are excluded from tier 1 capital with the exception of losses arising on the remeasurement to fair value of equity securities classified as available-for-sale. In accordance with the CBB's guidelines, gains arising on the remeasurement to fair value of equity securities classified as available-for-sale are included in tier 2 capital, although limited to 45 per cent of the unrealised revaluation gain.

The Group's subordinated term financing facilities have been approved for inclusion in tier 2 capital by the CBB. During the last five years before maturity, a cumulative amortisation (discount) factor of 20 per cent per year is to be applied to the facilities. As at 31st December 2011, the amortisation amount excluded from tier 2 capital amounted to US$161.1 million (2010: US$72.2 million).

The Group calculates the regulatory capital requirement for general market risk using a Value-at-Risk model. The use of the internal model approach for the calculation of the capital requirement for general market risk has been approved by the Bank's regulator, the CBB. The multiplication factor to be applied to the Value-at-Risk calculated by the internal model has been set at 3.0 (2010: 3.5) by the CBB.

Value-at-Risk is calculated based on a 99 per cent confidence level, a ten-day holding period and a twelve-month historical observation period of unweighted data from the DataMetrics regulatory data set. Correlations across broad risk categories are excluded. Prescribed additions in respect of specific risk are made to the general market risk. The resultant measure of market risk is multiplied by 12.5, the reciprocal of the 8 per cent international minimum capital ratio, to give market risk-weighted exposure on a basis consistent with credit risk-weighted exposure.

The capital requirement for operational risk is calculated by the Group in accordance with the standardised approach. The regulatory capital requirement is calculated based on a range of beta coefficients, ranging from 12 to 18 per cent, applied to the average gross income for the preceding three financial years for each of eight predefined business lines.

35. FIDUCIARY ACTIVITIES

The Group conducts investment management and other fiduciary activities on behalf of clients. Assets held in trust or in a fiduciary capacity are not assets of the Group and accordingly have not been included in the consolidated financial statements. The aggregate amount of the funds concerned at 31st December 2011 was US$8,139.5 million (2010: US$18,206.5 million).

36. RELATED PARTY TRANSACTIONS

The Group is owned by the six Gulf Cooperative Council governments, with the Public Investment Fund holding a majority (97.2 per cent) controlling stake. The Public Investment Fund is an investment body of the Saudi Arabian Ministry of Finance. There were no individual or collectively significant transactions with the Public Investment Fund during the years ended 31st December 2011 or 31st December 2010, other than the senior term loan referred to in note 16.

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36. RELATED PARTY TRANSACTIONS (continued)

The Group's related party transactions are limited to the compensation of its directors and executive officers.

The compensation of key management personnel was as follows:-

	2011	2010
	US$ millions	US$ millions
Short-term employee benefits	**6.5**	6.8
Post-employment benefits	**0.5**	0.4
	7.0	7.2

Key management personnel comprise members of the Board of Directors, the Group Chief Executive Officer and the Managing Directors of the Group.

Post-employment benefits principally comprise compensation paid to personnel on retirement or resignation from the services of the Group.

37. FAIR VALUE OF FINANCIAL INSTRUMENTS

The Group's financial instruments are accounted for under the historical cost method with the exception of trading securities, available-for-sale securities and derivative financial instruments. By contrast the fair value represents the amount at which an asset could be exchanged, or a liability settled, in a transaction between knowledgeable, willing parties in an arm's length transaction. Differences therefore can arise between book values under the historical cost method and fair value estimates. Underlying the definition of fair value is the presumption that the Group is a going concern without any intention or requirement to curtail materially the scale of its operation or to undertake a transaction on adverse terms. Generally accepted methods of determining fair value include reference to quoted prices or to the pricing prevailing for similar financial instruments and the use of estimation techniques such as discounted cash flow analysis.

Based on the valuation methodologies outlined below, the fair values of all on- and off-balance sheet financial instruments were not significantly different to their carrying amounts.

a) Trading and investment securities

The fair values of securities are based on quoted prices or valuation techniques with the exception of investments in unquoted equity investments for which fair values cannot be reliably measured, the fair values of which are based on their carrying amount.

b) Loans and advances

The fair values of loans held for trading are based on quoted market prices. The fair values of other loans on a floating interest rate basis are principally estimated at book value less provisions for impairment. The fair values of impaired loans are estimated at the recoverable amount, measured as the present value of expected future cash flows discounted based on the interest rate at the inception of the loan. The fair values of fixed-rate loans are estimated on a discounted cash flow basis utilising discount rates equal to prevailing market rates of interest in the respective currencies for loans of similar residual maturity and credit quality.

c) Term financing

The fair value of term financing is based on observable market data, including quoted market prices for debt instruments issued by similarly rated financial institutions and with similar maturities, or estimated on a discounted cash flow basis utilising currently prevailing spreads for borrowings with similar maturities. The fair values of senior term financing and subordinated term financing at 31st December 2011 were US$3,569.9 million and US$437.4 million respectively (2010: US$3,163.1 million and US$446.6 million respectively).

Notes to the Consolidated Financial Statements (continued)

For the year ended 31st December 2011

37. FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

d) Other on-balance sheet items

The fair values of foreign exchange and derivative financial instruments are based on market prices, discounted cash flow techniques or option pricing models as appropriate. The fair values of all other on-balance sheet financial assets and liabilities approximate their respective book values due to their short term nature.

e) Credit-related contingent items

There was no material fair value excess or shortfall in respect of credit-related off-balance sheet financial instruments, which include commitments to extend credit, standby letters of credit and guarantees, as the related future income streams reflected contractual fees and commissions actually charged at the balance sheet date for agreements of similar credit standing and maturity. Specific provisions made in respect of individual transactions where a potential for loss has been identified are included in provisions for the impairment of loans and advances.

The valuation basis for financial assets and financial liabilities carried at fair value was as follows:-

	Quoted prices (level 1) US$ millions	Valuation based on observable market data (level 2) US$ millions	Other valuation techniques (level 3) US$ millions
At 31st December 2011			
Financial assets:			
Trading securities	**83.7**	-	-
Investment securities	**3,016.5**	-	**28.2**
Derivative financial instruments	-	**81.1**	-
Financial liabilities:			
Derivative financial instruments	-	**112.5**	-
At 31st December 2010			
Financial assets:			
Trading securities	79.7	-	-
Investment securities	2,933.8	-	27.1
Derivative financial instruments	-	67.1	-
Financial liabilities:			
Derivative financial instruments	-	86.2	-

Quoted prices include prices obtained from lead managers, brokers and dealers. Investment securities valued based on other valuation techniques comprise private equity investments that have been valued based on price / earnings ratios for similar entities. The majority of the Group's financial assets and liabilities that are carried at fair value are valued based on quoted market prices. At 31st December 2011, 96.6 per cent of financial assets carried at fair value were valued based on quoted prices (2010: 97.0 per cent).

During the year ended 31st December 2011, the value of investment securities whose measurement was determined by other valuation techniques (level 3 measurement) increased by US$1.1 million (2010: US$2.2 million). The increase comprised the provisioning of a security, and changes in assigned valuations as recognised in other comprehensive income. No transfers out of, or into, the level 3 measurement classification occurred during the year ended 31st December 2011 or 31st December 2010.

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38. EARNINGS PER SHARE

Basic earnings per share is calculated by dividing the net income attributable to the shareholders by the weighted average number of shares in issue during the year.

	2011	2010
Net income after tax (US$ millions)	**104.5**	100.4
Weighted average number of shares in issue (millions)	**2,500**	2,500
Basic earnings per share	**US$0.04**	US$0.04

The diluted earnings per share is equivalent to the basic earnings per share set out above.

39. PRINCIPAL SUBSIDIARIES

The principal subsidiary companies were as follows:-

	Country of incorporation	Ownership interest 31.12.11	31.12.10
Gulf International Bank (UK) Limited	United Kingdom	**100%**	100%
GIB Capital L.L.C.	Kingdom of Saudi Arabia	**100%**	100%
GIB Investment S.P.C.	Kingdom of Bahrain	**100%**	100%

40. AVERAGE CONSOLIDATED STATEMENT OF FINANCIAL POSITION

The average consolidated statement of financial position was as follows:-

	31.12.11 US$ millions	31.12.10 US$ millions
Assets		
Cash and other liquid assets	**996.2**	644.0
Securities purchased under agreements to resell	**157.7**	143.2
Placements	**4,931.5**	4,206.3
Trading securities	**81.3**	38.6
Investment securities	**3,219.6**	2,525.5
Loans and advances	**7,131.7**	8,340.4
Other assets	**198.8**	170.3
Total assets	**16,716.8**	16,068.3
Liabilities		
Deposits from banks	**2,087.4**	2,904.4
Deposits from customers	**7,912.4**	6,697.5
Securities sold under agreements to repurchase	**450.8**	660.2
Other liabilities	**251.2**	255.9
Senior term financing	**3,552.3**	3,155.1
Subordinated term financing	**507.4**	511.0
Total liabilities	**14,761.5**	14,184.1
Total equity	**1,955.3**	1,884.2
Total liabilities & equity	**16,716.8**	16,068.3

Basel 2
Pillar 3 Report

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Basel 2 Pillar 3 Report

EXECUTIVE SUMMARY

The Central Bank of Bahrain (CBB) Basel 2 guidelines prescribe the capital adequacy framework for banks incorporated in the Kingdom of Bahrain.

This Risk Management and Capital Adequacy report encompasses the Basel 2 Pillar 3 disclosure requirements prescribed by the CBB based on the Basel Committee's Pillar 3 guidelines. The report contains a description of GIB's risk management and capital adequacy policies and practices, including detailed information on the capital adequacy process.

Since 2006, GIB (the Group) has routinely been monitoring capital adequacy for internal capital management purposes based on both the Basel 2 standardised and the foundation internal ratings based (FIRB) approaches for credit risk, and the basic indicator and standardised approaches for operational risk, in addition to the internal models approach for market risk.

For regulatory purposes, GIB has initially adopted the standardised approach for credit risk. In time and subject to approval by the CBB, GIB plans to adopt the FIRB approach for credit risk, as it is more closely aligned to the Group's internal capital management methodologies. GIB uses the internal models approach for market risk and the standardised approach for determining the capital requirement for operational risk.

The disclosed tier 1 and total capital adequacy ratios comply with the minimum capital requirements under the CBB's Basel 2 framework.

GIB's total risk-weighted assets at 31st December 2011 amounted to US$10,272.7 million. Credit risk accounted for 94.2 per cent, market risk 1.1 per cent and operational risk 4.7 per cent of the total risk-weighted assets. Tier 1 and total regulatory capital were US$1,969.3 million and US$2,389.3 million respectively.

At 31st December 2011, GIB's tier 1 and total capital adequacy ratios were 19.2 per cent and 23.3 per cent respectively. GIB aims to maintain a tier 1 capital ratio above 8 per cent and a total capital ratio in excess of 12 per cent.

GIB views the Basel 2 Pillar 3 disclosures as an important contribution to increased risk transparency within the banking industry, and particularly important during market conditions characterised by high uncertainty. In this regard, GIB has provided more disclosure in this report than is required in accordance with the CBB's Pillar 3 guidelines in order to provide the level of transparency that is believed to be appropriate and relevant to the Group's various stakeholders and market participants.

All figures presented in this report are as at 31st December 2011 unless otherwise stated.

1. THE BASEL 2 FRAMEWORK

The CBB's Basel 2 framework is based on three pillars, consistent with the Basel 2 framework developed by the Basel Committee, as follows:-

- Pillar 1: the calculation of the risk weighted amounts (RWAs) and capital requirement.
- Pillar 2: the supervisory review process, including the Internal Capital Adequacy Assessment Process (ICAAP).
- Pillar 3: the disclosure of risk management and capital adequacy information.

1.1 Pillar 1

Pillar 1 prescribes the basis for the calculation of the regulatory capital adequacy ratio. Pillar 1 sets out the definition and calculations of the RWAs, and the derivation of the regulatory capital base. The capital adequacy ratio is calculated by dividing the regulatory capital base by the total RWAs.

The resultant ratio is to be maintained above a predetermined and communicated level. Under the previously applied Basel 1 Capital Accord, the minimum capital adequacy ratio for banks incorporated in Bahrain was 12 per cent compared to the Basel Committee's minimum ratio of 8 per cent.

Basel 2 Pillar 3 Report (continued)

1. THE BASEL 2 FRAMEWORK (continued)

1.1 Pillar 1 (continued)

With the introduction of Pillar 2, the CBB will implement a minimum ratio threshold to be determined for each institution individually, as described in more detail in the Pillar 2 section of this report. As at 31st December 2011, and pending the finalisation of the CBB's Pillar 2 guidelines, all banks incorporated in Bahrain were required to maintain a minimum capital adequacy ratio of 12 per cent.

The CBB also requires banks incorporated in Bahrain to maintain a buffer of 0.5 per cent above the minimum capital adequacy ratio. In the event that the capital adequacy ratio falls below 12.5 per cent, 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 GIB to maintain an effective minimum capital adequacy ratio of 12.5 per cent. No separate minimum tier 1 ratio is required to be maintained under the CBB's Basel 2 capital adequacy framework. However, the maintenance of a strong tier 1 ratio is nevertheless a focus of GIB's internal capital adequacy assessment process, as it represents the core capital of the Bank.

The table below summarises the approaches available for calculating RWAs for each risk type in accordance with the CBB's Basel 2 capital adequacy framework:-

Approaches for determining regulatory capital requirements		
Credit Risk	**Market Risk**	**Operational Risk**
Standardised Approach	Standardised Approach	Basic Indicator Approach
Foundation Internal Ratings Based Approach (FIRB)	Internal Models Approach	Standardised Approach

The approach applied by GIB for each risk type is as follows:-

i) Credit Risk

For regulatory reporting purposes, GIB applies the standardised approach for credit risk.

The RWAs are determined by multiplying the credit exposure by a risk weight factor dependent on the type of counterparty and the counterparty's external rating, where available.

Internally, GIB also calculates the capital requirement under the more risk-sensitive and complex FIRB approach, although the resultant ratio is not being used for regulatory compliance purposes at present.

ii) Market Risk

For the regulatory market risk capital requirement, GIB applies the internal models approach based on a Value-at-Risk (VaR) model. The use of the internal models approach for the calculation of regulatory market risk capital has been approved by the CBB.

iii) Operational Risk

Under the CBB's Basel 2 capital adequacy framework, all banks incorporated in Bahrain are required to apply the basic indicator approach for operational risk unless approval is granted by the CBB to use the standardised approach. The CBB's Basel 2 guidelines do not currently permit the use of the advanced measurement approach (AMA) for operational risk. For regulatory reporting purposes, GIB received approval from the CBB to use the standardised approach for the calculation of regulatory operational risk capital in 2011.

Under the standardised approach, the regulatory capital requirement is calculated based on a range of beta coefficients, ranging from 12 to 18 per cent, applied to the average gross income for the preceding three financial years for each of eight predefined business lines.

1. THE BASEL 2 FRAMEWORK (continued)

1.2 Pillar 2

Pillar 2 defines the process of supervisory review of an institution's risk management framework and, ultimately, its capital adequacy.

Under the CBB's Pillar 2 guidelines, each bank is to be individually assessed by the CBB and an individual minimum capital adequacy ratio is to be determined for each bank. The CBB is yet to undertake the assessment exercises, which will allow their setting of minimum capital ratios in excess of 8 per cent, based on the CBB's assessment of the financial strength and risk management practices of the institution. Currently, pending finalisation of the assessment process, all banks incorporated in Bahrain are required to maintain a 12 per cent minimum capital adequacy ratio.

Pillar 2 comprises two processes:-

- an Internal Capital Adequacy Assessment Process (ICAAP), and
- a supervisory review and evaluation process.

The ICAAP incorporates a review and evaluation of risk management and capital relative to the risks to which the bank is exposed. GIB's ICAAP has been developed around its economic capital framework which is designed to ensure that the Group has sufficient capital resources available to meet regulatory and internal capital requirements, even during periods of economic or financial stress. The ICAAP addresses all components of GIB's risk management, from the daily management of more material risks to the strategic capital management of the Group.

The supervisory review and evaluation process represents the CBB's review of the Group's capital management and an assessment of internal controls and corporate governance. The supervisory review and evaluation process is designed to ensure that institutions identify their material risks and allocate adequate capital, and employ sufficient management processes to support such risks.

The supervisory review and evaluation process also encourages institutions to develop and apply enhanced risk management techniques for the measurement and monitoring of risks in addition to the credit, market and operational risks addressed in the core Pillar 1 framework. Other risk types which are not covered by the minimum capital requirements in Pillar 1 include liquidity risk, interest rate risk in the banking book, business risk and concentration risk. These are covered either by capital, or risk management and mitigation processes under Pillar 2.

1.3 Pillar 3

In the CBB's Basel 2 framework, the third pillar prescribes how, when, and at what level information should be disclosed about an institution's risk management and capital adequacy practices.

The disclosures comprise detailed qualitative and quantitative information. The purpose of the Pillar 3 disclosure requirements is to complement the first two pillars and the associated supervisory review process. The disclosures are designed to enable stakeholders and market participants to assess an institution's risk appetite and risk exposures and to encourage all banks, via market pressures, to move toward more advanced forms of risk management.

Under the current regulations, partial disclosure consisting mainly of quantitative analysis is required during half year reporting, whereas fuller disclosure is required to coincide with the financial year end reporting.

In this report, GIB's disclosures are beyond the minimum regulatory requirements and provide disclosure of the risks to which it is exposed, both on- and off-balance sheet. The disclosures in this report are in addition to the disclosures set out in the consolidated financial statements presented in accordance with International Financial Reporting Standards (IFRS).

Basel 2
Pillar 3 Report (continued)

2. GROUP STRUCTURE AND OVERALL RISK AND CAPITAL MANAGEMENT

This section sets out the consolidation principles and the capital base of GIB as calculated in accordance with the Pillar 1 guidelines, and describes the principles and policies applied in the management and control of risk and capital.

2.1 Group structure

The Group's financial statements are prepared and published on a full consolidation basis, with all subsidiaries being consolidated in accordance with IFRS. For capital adequacy purposes, all subsidiaries are included within the Gulf International Bank B.S.C. Group structure. However, the CBB's capital adequacy methodology accommodates both normal and aggregation forms of consolidation.

Under the CBB capital adequacy framework, subsidiaries reporting under a Basel 2 framework in other regulatory jurisdictions may, at the bank's discretion, be consolidated based on that jurisdiction's Basel 2 framework, rather than based on the CBB's guidelines. Under this aggregation consolidation methodology, the risk weighted assets of subsidiaries are consolidated with those of the rest of the Group based on the guidelines of their respective regulator to determine the Group's total risk weighted assets.

GIB's principal subsidiary, GIBUK, is regulated by the Financial Services Authority (FSA) of the United Kingdom, and has calculated its risk weighted assets in accordance with the FSA's guidelines.

The principal subsidiaries and basis of consolidation for capital adequacy purposes are as follows:-

Subsidiary	Domicile	Ownership	Consolidation basis
Gulf International Bank (UK) Limited	United Kingdom	100%	Aggregation
GIB Capital LLC	Saudi Arabia	100%	Full Consolidation
GIB Investment SPC	Bahrain	100%	Full Consolidation

No investments in subsidiaries are treated as a deduction from the Group's regulatory capital.

2.2 Risk and capital management

GIB maintains a prudent and disciplined approach to risk taking by upholding a comprehensive set of risk management policies, processes and limits, employing professionally qualified people with the appropriate skills, investing in technology and training, and actively promoting a culture of sound risk management at all levels. A key tenet of this culture is the clear segregation of duties and reporting lines between personnel transacting business and personnel processing that business. The Group's risk management is underpinned by its ability to identify, measure, aggregate and manage the different types of risk it faces.

The Board of Directors has created from among its members a Board Risk Policy Committee to review the Group's risk taking activities and report to the Board in this regard. The Board has the ultimate responsibility for setting the overall risk parameters and tolerances within which the Group conducts its activities, including responsibility for setting the capital ratio targets. The Board reviews the Group's overall risk profile and significant risk exposures as well as the Group's major risk policies, processes and controls.

The Management Committee, chaired by the Chief Executive Officer (CEO), has the primary responsibility for sanctioning risk taking policies and activities within the tolerances defined by the Board. The Group Risk Committee assists the Management Committee in performing its risk related functions.

The Group Risk Committee, under the chairmanship of the Chief Risk Officer (CRO) and comprising the Group's most senior risk professionals, provides a forum for the review and approval of new products, risk measurement methodologies and risk control processes. The Group Risk Committee also reviews all risk policies and limits that require approval by the Management Committee. The Assets and Liabilities Committee (ALCO), chaired by the Chief Financial Officer (CFO), provides a forum for the review of asset and liability activities within GIB. It co-ordinates the asset and liability functions and serves as a link between the funding sources and usage in the different business areas.

From a control perspective, the process of risk management is facilitated through a set of independent functions, which report directly to senior management. These functions include Credit Risk, Market Risk, Operational Risk, Financial Control and Internal Audit. This multi-faceted approach aids the effective management of risk by identifying, measuring and monitoring risks from a variety of perspectives.

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2. GROUP STRUCTURE AND OVERALL RISK AND CAPITAL MANAGEMENT (continued)

2.2 Risk and capital management (continued)

Internal Audit is responsible for carrying out a risk-based programme of work designed to provide assurance that assets are being safeguarded. This involves ensuring that controls are in place and working effectively in accordance with Group policies and procedures as well as with laws and regulations. The work carried out by Internal Audit includes providing assurance on the effectiveness of the risk management functions, as well as that of controls operated by the business units. The Audit Committee approves the annual audit plan and also receives regular reports of the results of audit work.

The Group's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future business development. The Group manages its capital structure and makes adjustments to the structure taking account of changes in economic conditions and strategic business plans. The capital structure may be adjusted through the dividend payout and the issue of new shares.

The CFO is responsible for the capital planning process. Capital planning includes capital adequacy reporting, economic capital and parameter estimation, i.e. probability of default (PD) and loss given default (LGD) estimates, used for the calculation of economic capital. The CFO is also responsible for the balance sheet management framework.

The governance structure for risk and capital management is set out in the table below:-

<table>
<tr><th colspan="3">Board of Directors</th></tr>
<tr><td colspan="2">Audit Committee</td><td>Board Risk Policy Committee</td></tr>
<tr><th colspan="3">Chief Executive Officer</th></tr>
<tr><td>Management Committee
(Chairman: CEO)</td><td>Group Risk Committee
(Chairman: CRO)</td><td>Assets and Liabilities Committee
(Chairman: CFO)</td></tr>
</table>

The risk, liquidity and capital management responsibilities are set out in the table below:-

<table>
<tr><th colspan="2">Chief Executive Officer</th></tr>
<tr><td>Chief Financial Officer
(CFO)</td><td>Chief Risk Officer
(CRO)</td></tr>
<tr><td>Balance sheet management framework
Capital management framework</td><td>Risk management framework and policies
Group credit control
Credit risk
Market risk
Operational risk
Liquidity risk</td></tr>
</table>

2.3 Risk types

The major risks associated with the Group's business activities are credit, market, operational and liquidity risk. These risks together with a commentary on the way in which the risks are managed and controlled are set out in the following sections, based on the Basel 2 pillar in which the risks are addressed.

2.4 Risk in Pillar 1

Pillar 1, which forms the basis for the calculation of the regulatory capital requirement, addresses three specific risk types: credit, market and operational risk.

i) Credit risk

Credit risk is the risk that a customer, counterparty or an issuer of securities or other financial instruments fails to perform under its contractual payment obligations thus causing the Group to suffer a loss in terms of cash flow or market value. Credit risk is the predominant risk type faced by the Group in its banking, investment and treasury activities, both on- and off-balance sheet. Where appropriate, the Group seeks to minimise its credit exposure using a variety of techniques including, but not limited to, the following:-

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Basel 2
Pillar 3 Report (continued)

2. GROUP STRUCTURE AND OVERALL RISK AND CAPITAL MANAGEMENT (continued)

2.4 Risk in Pillar 1 (continued)

i) Credit risk (continued)

- entering netting agreements with counterparties that permit the offsetting of receivables and payables
- obtaining collateral
- seeking third party guarantees of the counterparty's obligations
- imposing restrictions and covenants on borrowers

Credit risk is actively managed and rigorously monitored in accordance with well-defined credit policies and procedures. Prior to the approval of a credit proposal, a detailed credit risk assessment is undertaken which includes an analysis of the obligor's financial condition, market position, business environment and quality of management. The risk assessment generates an internal credit risk rating for each counterparty, which affects the credit approval decision and the terms and conditions of the transaction. For cross-border transactions, an analysis of country risk is also conducted. The credit decision for an individual counterparty is based on the aggregate Group exposure to that counterparty and all its related entities. Groupwide credit limit setting and approval authorisation requirements are conducted within Board approved guidelines, and the measurement, monitoring and control of credit exposures are done on a Groupwide basis in a consistent manner. Overall exposures are evaluated to ensure broad diversification of credit risk. Potential concentration risks by product, industry, single obligor, credit risk rating and geography are regularly assessed with a view to improving overall portfolio diversification. Established limits and actual levels of exposure are regularly reviewed by the Chief Risk Officer, Chief Credit Officer and other members of senior management. All credit exposures are reviewed at least once a year. Credit policies and procedures are designed to identify, at an early stage, exposures which require more detailed monitoring and review. The credit risk associated with foreign exchange and derivative instruments is assessed in a manner similar to that associated with on-balance sheet activities. The Group principally utilises derivative transactions to facilitate customer transactions and for the management of interest and foreign exchange risks associated with the Group's longer-term lending, borrowing and investment activities. Unlike on-balance sheet products, where the principal amount and interest generally represent the maximum credit exposure, the notional amount relating to a foreign exchange or derivative transaction typically exceeds the credit exposure by a substantial margin. The measure of credit exposure for foreign exchange and derivative instruments is therefore more appropriately considered to be the replacement cost at current market rates plus an add-on amount commensurate with the position's size, volatility and remaining life. Derivative contracts may also carry legal risk; the Group seeks to minimise these risks by the use of standard contract agreements.

ii) Market risk

Market risk is the risk of loss of value of a financial instrument or a portfolio of financial instruments as a result of adverse changes in market prices and rates, and market conditions such as liquidity. Market risk arises from the Group's trading, asset and liability management, and investment activities.

The categories of market risk to which the Group is exposed are as follows:-

Interest rate risk results from exposure to changes in the level, slope, curvature and volatility of interest rates and credit spreads. The credit spread risk is the risk that the interest yield for a security will increase, with a reduction in the security price, relative to benchmark yields as a result of the general market movements for that rating and class of security. Interest rate risk is the principal market risk faced by the Group and arises from the Group's investment activities in debt securities, asset and liability management, and the trading of debt and off-balance sheet derivative instruments.

Foreign exchange risk results from exposure to changes in the price and volatility of currency spot and forward rates. The principal foreign exchange risk arises from the Group's foreign exchange forward and derivative trading activities.

Equity risk arises from exposures to changes in the price and volatility of individual equities or equity indices.

The Group seeks to manage exposure to market risk through the diversification of exposures across dissimilar markets and establishment of hedges in related securities or off-balance sheet derivative instruments. To manage the Group's exposures, in addition to the exercise of business judgement and management experience, the Group utilises limit structures including those

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2. GROUP STRUCTURE AND OVERALL RISK AND CAPITAL MANAGEMENT (continued)

2.4 Risk in Pillar 1 (continued)

ii) Market risk (continued)

relating to positions, portfolios, maturities and maximum allowable losses. A key element in the Group's market risk management framework is the estimation of potential future losses that may arise from adverse market movements. The Group utilises Value-at-Risk (VaR) to estimate such losses. The VaR is derived from quantitative models that use statistical and simulation methods that take account of all market rates and prices that may cause a change in a position's value. These include interest rates, foreign exchange rates and equity prices, their respective volatilities and the correlations between these variables. The Group's VaR is calculated on a Monte Carlo simulation basis using historical volatilities and correlations to generate a profit and loss distribution from several thousand scenarios.

The VaR takes account of potential diversification benefits of different positions both within and across different portfolios. Consistent with general market practice, VaR is computed for all financial instruments for which there are readily available daily prices or suitable proxies. VaR is viewed as an effective risk management tool and a valuable addition to the non-statistically based limit structure. It permits a consistent and uniform measurement of market risk across all applicable products and activities. Exposures are monitored against a range of limits both by risk category and portfolio and are regularly reported to and reviewed by senior management and the Board of Directors.

An inherent limitation of VaR is that past market movements may not provide an accurate prediction of future market losses. Historic analyses of market movements have shown that extreme market movements (i.e. beyond the 99 per cent confidence level) occur more frequently than VaR models predict. Stress tests are regularly conducted to estimate the potential economic losses in such abnormal markets. Stress testing combined with VaR provides a more comprehensive picture of market risk. The Group regularly performs stress tests that are constructed around changes in market rates and prices resulting from pre-defined market stress scenarios, including both historical and hypothetical market events. Historical scenarios include the 1997 Asian crisis, the 1998 Russian crisis, the events of 9/11 and the 2008 credit crisis. In addition, the Group performs stress testing based on internally developed hypothetical market stress scenarios. Stress testing is performed for all material market risk portfolios.

iii) Operational risk

Operational risk is the risk of loss arising from inadequate or failed internal processes, people and systems or from external events, whether intentional, unintentional or natural. It is an inherent risk faced by all businesses and covers a large number of potential operational risk events including business interruption and systems failures, internal and external fraud, employment practices and workplace safety, customer and business practices, transaction execution and process management, and damage to physical assets.

Whilst operational risk cannot be eliminated in its entirety, the Group endeavours to minimise the risk by ensuring that a strong control infrastructure is in place throughout the organisation. The various procedures and processes used to manage operational risk include effective staff training, appropriate controls to safeguard assets and records, regular reconciliation of accounts and transactions, close monitoring of risk limits, segregation of duties, and financial management and reporting. In addition, other control strategies, including business continuity planning and insurance, are in place to complement the control processes, as applicable.

The Group has an independent operational risk function. As part of the Group's Operational Risk Management Framework (ORMF), comprehensive risk assessments are conducted, which identify operational risks inherent in the Group's activities, processes and systems. The controls in place to mitigate these risks are also reviewed, and enhanced if necessary.

2.5 Risk in Pillar 2

Other risk types are measured and assessed in Pillar 2. GIB measures and manages these risk types although they are not included in the calculation of the regulatory capital adequacy ratio. Most of the Pillar 2 risks are included in GIB's calculation of internal economic capital. Pillar 2 risk types include liquidity risk, interest rate risk in the banking book, business risk and concentration risk.

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Basel 2 Pillar 3 Report (continued)

2. GROUP STRUCTURE AND OVERALL RISK AND CAPITAL MANAGEMENT (continued)

2.5 Risk in Pillar 2 (continued)

i) Liquidity risk

Liquidity risk is the risk that sufficient funds are not available to meet the Group's financial obligations on a punctual basis as they fall due. The risk arises from the timing differences between the maturity profiles of the Group's assets and liabilities. It includes the risk of losses arising from the following:-

- Forced sale of assets at below normal market prices
- Raising of deposits or borrowing funds at excessive rates
- The investment of surplus funds at below market rates

Liquidity management policies are designed to ensure that funds are available at all times to meet the funding requirements of the Group, even in adverse conditions. In normal conditions, the objective is to ensure that there are sufficient funds available not only to meet current financial commitments but also to facilitate business expansion. These objectives are met through the application of prudent liquidity controls. These controls provide access to funds without undue exposure to increased costs from the liquidation of assets or the aggressive bidding for deposits.

The Group's liquidity controls ensure that, over the short-term, the future profile of cash flows from maturing assets is adequately matched to the maturity of liabilities. Liquidity controls also provide for the maintenance of a stock of liquid and readily realisable assets and a diversified deposit base in terms of both maturities and range of depositors.

The management of liquidity and funding is primarily conducted in the Group's individual geographic entities within approved limits. The limits ensure that contractual net cash flows occurring over the following 30-day period do not exceed the eligible stock of available liquid resources.

It is the Group's general policy that each geographic entity should be self-sufficient in relation to funding its own operations.

The Group's liquidity management policies include the following:-

- the monitoring of (i) future contractual cash flows against approved limits, and (ii) the level of liquid resources available in a stress event
- the monitoring of balance sheet liquidity ratios
- the monitoring of the sources of funding in order to ensure that funding is derived from a diversified range of sources
- the monitoring of depositor concentrations in order to avoid undue reliance on individual depositors
- the maintenance of a satisfactory level of term financing
- the maintenance of appropriate standby funding arrangements; and
- the maintenance of liquidity and funding contingency plans. These plans identify early indicators of stress conditions and prescribe the actions to be taken in the event of a systemic or other crisis, while minimising adverse long-term implications for the Group's business activities.

ii) Interest rate risk in the banking book

Structural interest rate risk arises in the Group's core balance sheet as a result of mismatches in the repricing of interest rate sensitive financial assets and liabilities. The associated interest rate risk is managed within VaR limits and through the use of models to evaluate the sensitivity of earnings to movements in interest rates.

iii) Business risk

Business risk represents the earnings volatility inherent in all businesses due to the uncertainty of revenues and costs associated with changes in the economic and competitive environment. Business risk is evaluated based on the observed volatility in historical profits and losses.

iv) Concentration risk

Concentration risk is the risk related to the degree of diversification in the credit portfolio, i.e. the risk inherent in doing business with large customers or not being equally exposed across industries and regions.

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2. GROUP STRUCTURE AND OVERALL RISK AND CAPITAL MANAGEMENT (continued)

2.5 Risk in Pillar 2 (continued)

iv) Concentration risk (continued)

Concentration risk is captured in GIB's economic capital framework through the use of a credit risk portfolio model which considers single-name concentrations in the credit portfolio. Economic capital add-ons are applied where counterparty exposures exceed specified thresholds.

Potential concentration risks by product, industry, single obligor, and geography are regularly assessed with a view to improving overall portfolio diversification. Established limits and actual levels of exposure are regularly reviewed by senior management and the Board of Directors.

2.6 Monitoring and reporting

The monitoring and reporting of risk is conducted on a daily basis for market and liquidity risk, and on a monthly or quarterly basis for credit and operational risk.

Risk reporting is regularly made to senior management and the Board of Directors. The Board of Directors receives internal risk reports covering market, credit, operational and liquidity risks.

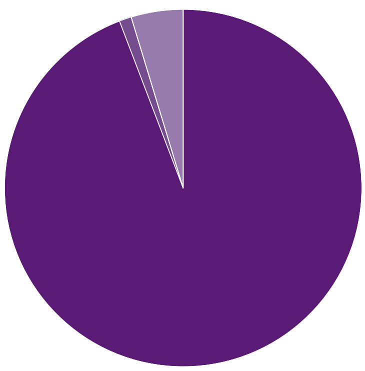
Capital management, including regulatory and internal economic capital ratios, is reported to senior management and the Board of Directors on a monthly basis.

3. REGULATORY CAPITAL REQUIREMENTS AND THE CAPITAL BASE

This section describes the Group's regulatory capital requirements and capital base.

The composition of the total regulatory capital requirement was as follows:-

Regulatory capital requirements



	%
Credit risk capital	94.2
Market risk capital	1.1
Operational risk capital	4.7
Total	**100.0**

Basel 2
Pillar 3 Report (continued)

3. REGULATORY CAPITAL REQUIREMENTS AND THE CAPITAL BASE (continued)

3.1 Capital requirements for credit risk

For regulatory reporting purposes, GIB calculates the capital requirements for credit risk based on the standardised approach. Under the standardised approach, on- and off-balance sheet credit exposures are assigned to exposure categories based on the type of counterparty or underlying exposure. The exposure categories are referred to in the CBB's Basel 2 capital adequacy framework as standard portfolios. The primary standard portfolios are claims on sovereigns, claims on banks and claims on corporates. Following the assignment of exposures to the relevant standard portfolios, the RWAs are derived based on prescribed risk weightings. Under the standardised approach, the risk weightings are provided by the CBB and are determined based on the counterparty's external credit rating. The external credit ratings are derived from eligible external rating agencies approved by the CBB. GIB uses ratings assigned by Standard & Poor's, Moody's and Fitch.

An overview of the exposures, RWAs and capital requirements for credit risk analysed by standard portfolio is presented in the table below:-

	Rated exposure US$ millions	Unrated exposure US$ millions	Total exposure US$ millions	Average risk weight %	RWA US$ millions	Capital requirement US$ millions
Sovereigns	2,993.6	-	2,993.6	1%	17.5	2.1
PSEs	-	5.4	5.4	100%	5.4	0.6
Banks	9,890.4	320.1	10,210.5	24%	2,445.8	293.5
Corporates	1,017.7	5,819.1	6,836.8	92%	6,315.5	757.9
Equities	-	306.9	306.9	126%	386.1	46.3
Past due loans	-	263.9	263.9	133%	350.4	42.0
Other assets	20.0	153.0	173.0	89%	153.4	18.4
Total	**13,921.7**	**6,868.4**	**20,790.1**	**47%**	**9,674.1**	**1,160.8**

Exposures are stated after taking account of credit risk mitigants where applicable. The treatment of credit risk mitigation is explained in more detail in section 4.4(vii) of this report.

The unrated exposure to banks principally represents unrated subordinated loans to rated banks.

The definitions of each standard portfolio and the related RWA requirements are set out in section 4 of this report.

3.2 Capital requirements for market risk

GIB uses a Value-at-Risk (VaR) model to calculate the regulatory capital requirements relating to general market risk.

The VaR calculated by the internal model is subject to a multiplication factor determined by the CBB. GIB's multiplication factor has been set at the regulatory minimum of 3.0 by the CBB.

Prescribed additions in respect of specific risk are made to general market risk. The resultant measure of market risk is multiplied by 12.5, the reciprocal of the theoretical 8 per cent minimum capital ratio, to give market risk-weighted exposure on a basis consistent with credit risk-weighted exposure.

3. REGULATORY CAPITAL REQUIREMENTS AND THE CAPITAL BASE (continued)

3.2 Capital requirements for market risk (continued)

The RWAs and capital requirements for market risk are presented in the table below:-

	RWA US$ millions	Capital requirement US$ millions
Interest rate risk	44.9	5.4
Equity risk	1.3	0.1
Foreign exchange risk	3.3	0.4
Total general market risk	49.5	5.9
Total specific market risk	65.9	7.9
Total	**115.4**	**13.8**

3.3 Capital requirements for operational risk

For regulatory reporting purposes, the capital requirement for operational risk is calculated according to the standardised approach. Under this approach, the Group's average gross income over the preceding three financial years is multiplied by a range of beta coefficients. The beta coefficients are determined based on the business line generating the gross income and are prescribed in the CBB's Basel 2 capital adequacy framework and range from 12 to 18 per cent.

The capital requirement for operational risk at 31st December 2011 amounted to US$58.0 million.

3.4 Capital base

The regulatory capital base is set out in the table below:-

	Tier 1 US$ millions	Tier 2 US$ millions	Total US$ millions
Share capital	2,500.0	-	2,500.0
Share premium	7.6	-	7.6
Compulsory reserve	187.9	-	187.9
Voluntary reserve	125.4	-	125.4
Retained earnings	(783.2)	-	(783.2)
Unrealised (losses) / gains on fair valuing AFS equity investments	(32.9)	10.4	(22.5)
Collective impairment provisions (subject to 1.25% RWA limitation)	-	128.4	128.4
Subordinated term finance	-	316.7	316.7
Regulatory capital deductions	(35.5)	(35.5)	(71.0)
Tier 1 and tier 2 capital base	**1,969.3**	**420.0**	**2,389.3**

Tier 1 capital is defined as capital of the same or close to the character of paid-up capital and comprises share capital, share premium, retained earnings and eligible reserves. Retained losses, after inclusion of profits for the current year, are included in tier 1 following the external audit. Eligible reserves exclude revaluation gains and losses arising on the remeasurement to fair value of available-for-sale securities and derivative cash flow hedging transactions, with the exception of unrealised gains and losses arising on the remeasurement to fair value of equity securities classified as available-for-sale. Unrealised losses on equity securities classified as available-for-sale are included in tier 1 capital. Unrealised gains on equity securities classified as available-for-sale are included in tier 2 capital.

Tier 2 capital comprises qualifying subordinated term finance, collective impairment provisions and 45 per cent of unrealised gross gains arising on the remeasurement to fair value of equity securities classified as available-for-sale.

The subordinated term finance facilities, amounting to US$316.7 million, represent unsecured obligations of the Group and are subordinated in right of payment to the claims of depositors and other creditors of the Group that are not also subordinated. The subordinated term finance facilities have been approved for inclusion in tier 2 capital for regulatory capital adequacy purposes by the CBB. During the last five years before maturity, a cumulative amortisation (discount) factor of 20 per cent per year is to be applied to the facilities. At 31st December 2011, the amortisation amount excluded from tier 2 capital amounted to US$161.1 million.

Basel 2 Pillar 3 Report (continued)

3. REGULATORY CAPITAL REQUIREMENTS AND THE CAPITAL BASE (continued)

3.4 Capital base (continued)

In accordance with the CBB single obligor regulations, certain large single obligor exposures that were pre-approved by the CBB are required to be treated as regulatory capital deductions. The deductions are applied 50 per cent against tier 1 and 50 per cent against tier 2. At 31st December 2011, the large single obligor exposures deducted from regulatory capital amounted to US$71.0 million.

The CBB applies various limits to elements of the regulatory capital base. The amount of innovative tier 1 securities cannot exceed 15 per cent of total tier 1 capital; qualifying tier 2 capital cannot exceed tier 1 capital; and qualifying subordinated term finance cannot exceed 50 per cent of tier 1 capital. There are also restrictions on the amount of collective impairment provisions that may be included as part of tier 2 capital.

In accordance with the CBB's Basel 2 capital adequacy framework, securitisation exposures that are rated below BB- or that are unrated are to be deducted from regulatory capital rather than included in RWAs. At 31st December 2011, the Group had no exposure to securitisations.

There are no impediments on the transfer of funds or regulatory capital within the Group other than restrictions over transfers to ensure minimum regulatory capital requirements are met for subsidiary companies.

4. CREDIT RISK – PILLAR THREE DISCLOSURES

This section describes the Group's exposure to credit risk and provides detailed disclosures on credit risk in accordance with the CBB's Basel 2 framework in relation to Pillar 3 disclosure requirements.

4.1 Definition of exposure classes

GIB has a diversified on- and off-balance sheet credit portfolio, the exposures of which are divided into the counterparty exposure classes defined by the CBB's Basel 2 capital adequacy framework for the standardised approach for credit risk. A high-level description of the counterparty exposure classes, referred to as standard portfolios in the CBB's Basel 2 capital adequacy framework, and the generic treatments, i.e. the risk weights to be used to derive the RWAs, are as follows:-

Sovereigns Portfolio

The sovereigns portfolio comprises exposures to governments and their respective central banks. The risk weights are 0 per cent for exposures in the relevant domestic currency, or in any currency for 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 sovereigns portfolio and treated as exposures with a 0 per cent risk weighting.

PSE Portfolio

Public sector entities (PSEs) are risk weighted according to their external ratings with the exception of Bahrain PSEs, and domestic currency claims on other PSEs which are assigned a 0 per cent risk weight by their respective country regulator.

Banks Portfolio

Claims on banks are risk weighted based on their external credit ratings. A preferential risk weight treatment is available for qualifying short-term exposures. Short-term exposures are defined as exposures with an original tenor of three months or less.

The Banks portfolio also includes claims on investment firms, which are risk weighted based on their external credit ratings although without any option for preferential treatment for short-term exposures.

Corporates Portfolio

Claims on corporates are risk weighted based on their external credit ratings. A 100 per cent risk weight is assigned to unrated corporate exposures. 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 0 per cent risk weight.

4. CREDIT RISK – PILLAR THREE DISCLOSURES (continued)

4.1 Definition of exposure classes (continued)

Equities Portfolio

The equities portfolio comprises equity investments in the banking book, i.e. the investment securities 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 per cent risk weight is assigned to listed equities and funds. Unlisted equities and funds are risk weighted at 150 per cent. Investments in rated funds are risk weighted according to their external credit rating. Equity investments in securitisations are deducted from the regulatory capital base.

In addition to the standard portfolios, other exposures are assigned to the following exposure classes:-

Past due exposures

All past due loan exposures, irrespective of the categorisation of the exposure if it were performing, are classified separately under the past due exposures asset class. A risk weighting of either 100 per cent or 150 per cent is applied depending on the level of provision maintained against the loan.

Other assets and holdings of securitisation tranches

Other assets are risk weighted at 100 per cent.

Securitisation tranches are risk weighted based on their external credit ratings. Risk weightings range from 20 per cent to 350 per cent. Exposures to securitisation tranches that are rated below BB- or are unrated are deducted from regulatory capital rather than being subject to a risk weight.

4.2 External rating agencies

GIB uses ratings issued by Standard & Poor's, Moody's and Fitch to derive the risk weightings under the CBB's Basel 2 capital adequacy framework. Where ratings vary between rating agencies, the highest rating from the lowest two ratings is used to represent the rating for regulatory capital adequacy purposes.

4.3 Credit risk presentation under Basel 2

The credit risk exposures presented in much of this report differ from the credit risk exposures reported in the consolidated financial statements. Differences arise due to the application of different methodologies, as illustrated below:-

- Under the CBB's Basel 2 framework, off-balance sheet exposures are converted into credit exposure equivalents by applying a credit conversion factor (CCF). The off-balance sheet exposure is multiplied by the relevant CCF applicable to the off-balance sheet exposure category. Subsequently, the exposure is treated in accordance with the standard portfolios referred to in section 4.1 of this report in the same manner as on-balance sheet exposures.
- Credit risk exposure reporting under Pillar 3 is frequently reported by standard portfolios based on the type of counterparty. The financial statement presentation is based on asset class rather than the relevant counterparty. For example, a loan to a bank would be classified in the Banks standard portfolio under the capital adequacy framework although is classified in loans and advances in the consolidated financial statements.
- Certain eligible collateral is applied to reduce exposure under the Basel 2 capital adequacy framework, whereas no such collateral netting is applicable in the consolidated financial statements.
- Based on the CBB's Basel 2 guidelines, certain exposures are either included in, or deducted from, regulatory capital rather than treated as an asset as in the consolidated financial statements.
- Under the CBB's Basel 2 capital adequacy framework, external rating agency ratings are based on the highest rating from the lowest two ratings, while for internal credit risk management purposes the Group uses the lowest rating.

Basel 2
Pillar 3 Report (continued)

4. CREDIT RISK – PILLAR THREE DISCLOSURES (continued)

4.4 Credit exposure

i) Gross credit exposure

The gross and average gross exposure to credit risk before applying collateral, guarantees, and other credit enhancements was as follows:-

	Gross credit exposure US$ millions	Average gross credit exposure US$ millions
Balance sheet items:		
Cash and other liquid assets	858.7	996.2
Securities purchased under agreements to resell	280.0	157.7
Placements	5,394.0	4,931.5
Trading securities	83.7	81.3
Investment securities	3,151.7	3,219.6
Loans and advances	6,751.8	7,131.7
Other assets, excluding derivative-related items	85.6	85.5
Total on-balance sheet credit exposure	**16,605.5**	**16,603.5**
Off-balance sheet items:		
Credit-related contingent items	3,569.0	3,183.5
Derivative and foreign exchange instruments	109.1	95.1
Total off-balance sheet credit exposure	**3,678.1**	**3,278.6**
Total credit exposure	**20,283.6**	**19,882.1**

The average gross credit exposure is based on daily averages during the year ended 31st December 2011.

Other assets comprise accrued interest, fees and commissions.

The gross credit exposure for derivative and foreign exchange instruments is the replacement cost (current exposure) representing the cost of replacing the contracts at current market rates should the counterparty default prior to the settlement date. The gross credit exposure reported in the table above does not include potential future exposure. Further details on the counterparty credit risk relating to off-balance sheet exposures are set out in section 7.3(i) of this report.

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4. CREDIT RISK – PILLAR THREE DISCLOSURES (continued)

4.4 Credit exposure (continued)

ii) Credit exposure by geography

The classification of credit exposures by geography, based on the location of the counterparty, was as follows:-

	Placements, reverse repos & other liquid assets US$ millions	Securities US$ millions	Loans and advances US$ millions	Other assets US$ millions	Off balance sheet items US$ millions	Total US$ millions
GCC	1,982.0	1,362.2	6,354.5	38.2	3,236.4	12,973.3
Other MENA	13.0	24.3	69.2	0.6	13.9	121.0
Europe	3,798.6	842.9	311.3	36.5	194.5	5,183.8
North America	385.8	705.8	0.2	7.2	210.5	1,309.5
Asia	353.3	277.5	16.6	3.1	22.8	673.3
Latin America	-	22.7	-	-	-	22.7
Total exposure	**6,532.7**	**3,235.4**	**6,751.8**	**85.6**	**3,678.1**	**20,283.6**

The MENA region comprises the Middle East and North Africa.

iii) Credit exposure by industry

The classification of credit exposures by industry was as follows:-

	Placements, reverse repos & other liquid assets US$ millions	Securities US$ millions	Loans and advances US$ millions	Other assets US$ millions	Off balance sheet items US$ millions	Total US$ millions
Financial services	5,523.9	1,802.8	982.2	49.6	201.9	8,560.4
Energy, oil and petrochemical	-	222.9	2,701.7	9.5	428.6	3,362.7
Construction	-	-	272.2	0.7	2,399.2	2,672.1
Government	1,008.8	865.2	21.0	10.7	0.3	1,906.0
Trading and services	-	-	969.0	2.7	243.8	1,215.5
Transportation	-	14.8	751.3	1.7	128.6	896.4
Manufacturing	-	-	448.2	1.9	213.2	663.3
Communication	-	-	319.1	3.0	28.5	350.6
Real estate	-	-	170.9	3.2	1.3	175.4
Equity investments	-	329.7	-	-	3.3	333.0
Other	-	-	116.2	2.6	29.4	148.2
Total exposure	**6,532.7**	**3,235.4**	**6,751.8**	**85.6**	**3,678.1**	**20,283.6**

Basel 2
Pillar 3 Report (continued)

4. CREDIT RISK – PILLAR THREE DISCLOSURES (continued)

4.4 Credit exposure (continued)

iv) Credit exposure by internal rating

The credit risk profile based on internal credit ratings was as follows:-

	Placements, reverse repos & other liquid assets US$ millions	Securities US$ millions	Loans and advances US$ millions	Other assets US$ millions	Off balance sheet items US$ millions	Total US$ millions
Neither past due nor impaired						
Rating grades 1 to 4-	6,519.7	2,776.7	4,224.1	71.3	1,029.2	14,621.0
Rating grades 5+ to 5-	13.0	96.6	1,809.5	10.9	2,602.9	4,532.9
Rating grades 6+ to 6-	-	32.4	281.5	2.6	30.2	346.7
Rating grade 7	-	-	-	0.3	11.5	11.8
Rating grade 8	-	-	-	-	1.0	1.0
Equity investments	-	313.4	-	-	3.3	316.7
Carrying amount	6,532.7	3,219.1	6,315.1	85.1	3,678.1	19,830.1
Past due but not impaired						
Rating grades 1 to 7	-	-	159.9	-	-	159.9
Carrying amount	-	-	159.9	-	-	159.9
Past due and individually impaired						
Rating grade 7	-	-	33.7	-	-	33.7
Rating grade 8	-	-	14.4	-	-	14.4
Rating grade 9	-	-	42.8	-	-	42.8
Carrying amount	-	-	90.9	-	-	90.9
Individually impaired but not past due						
Rating grades 1 to 7	-	-	128.2	-	-	128.2
Rating grade 9	-	-	57.7	0.5	-	58.2
Equity investments	-	16.3	-	-	-	16.3
Carrying amount	-	16.3	185.9	0.5	-	202.7
Total	**6,532.7**	**3,235.4**	**6,751.8**	**85.6**	**3,678.1**	**20,283.6**

The analysis is presented prior to the application of credit risk mitigation techniques.

The Group’s internal rating system is commented on in more detail in section 8.1 of this report.

Basel 2
Pillar 3 Report (continued)

4. CREDIT RISK – PILLAR THREE DISCLOSURES (continued)

4.4 Credit exposure (continued)

v) Credit exposure by maturity

The maturity profile of funded credit exposures based on contractual maturity dates was as follows:-

	Placements reverse repos & other liquid assets US$ millions	Securities US$ millions	Loans and advances US$ millions	Other assets US$ millions	Total US$ millions
Within 3 months	5,979.5	208.4	1,562.4	51.1	7,801.4
4 months to 1 year	553.2	288.6	1,192.4	27.3	2,061.5
Years 2 to 5	-	2,241.5	2,120.7	7.2	4,369.4
Years 6 to 10	-	109.6	1,089.3	-	1,198.9
Years 11 to 20	-	57.6	496.8	-	554.4
Over 20 years and other	-	329.7	290.2	-	619.9
Total exposure	**6,532.7**	**3,235.4**	**6,751.8**	**85.6**	**16,605.5**

An analysis of off-balance sheet exposure is set out in section 7 of this report.

Securities exposure over 20 years comprises equity investments.

vi) Equities held in the banking book

Equity investments included in investment securities in the consolidated balance sheet are included in the equities standard portfolio in the Pillar 1 credit risk capital adequacy framework. Such equity investments principally comprise listed equities received in settlement of a past due loan, investments of a private equity nature, and investments in funds managed by specialist managers.

At 31st December 2011, equity investments held in the banking book amounted to US$302.9 million, of which US$148.6 million comprised listed equities received in settlement of a secured past due loan and US$33.5 million comprised managed funds. Unlisted equities, which principally represent private equity investments, are primarily stated at cost less provision for impairment. There are no active markets or other appropriate methods from which to derive reliable fair values for the majority of these investments. The Group intends to exit these investments principally by means of IPOs or private placements.

During the year ended 31st December 2011, the total realised gains on equity investments amounted to US$0.1 million. At 31st December 2011, unrealised gains on equity investments amounted to US$23.2 million. 45 per cent of the unrealised gains, or US$10.4 million, was included in tier 2 capital. Unrealised losses on equity investments amounted to US$32.9 million and were deducted from tier 1 capital in accordance with the CBB's Basel 2 capital adequacy framework.

vii) Credit risk mitigation

The credit exposure information presented in section 4 of this report represents gross exposures prior to the application of any credit risk mitigation techniques. Collateral items and guarantees which can be used for credit risk mitigation under the capital adequacy framework are referred to as eligible collateral. Only certain types of collateral and some issuers of guarantees are eligible for preferential risk weights for regulatory capital adequacy purposes. Furthermore, the collateral management process and the terms in the collateral agreements have to fulfil the CBB's prescribed minimum requirements (such as procedures for the monitoring of market values, insurance and legal certainty) set out in their capital adequacy regulations.

4. CREDIT RISK – PILLAR THREE DISCLOSURES (continued)

4.4 Credit exposure (continued)

vii) Credit risk mitigation (continued)

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 follows:-

- Adjusted exposure amount: GIB uses the comprehensive method for financial collateral such as cash, bonds and stocks. The exposure amount is adjusted with regard to the financial collateral. The size of the adjustment depends on the volatility of the collateral and the exposure. GIB uses volatility adjustments specified by the CBB, known as supervisory haircuts, to reduce the benefit of collateral and to increase the magnitude of the exposure.

- Substitution of counterparty: The substitution method is used for guarantees, whereby the rating of the counterparty is substituted with the rating of the guarantor. This means that the credit risk in respect of the customer is substituted by the credit risk of the guarantor and the capital requirement is thereby reduced. Hence, a fully guaranteed exposure will be assigned the same capital treatment as if the loan was initially granted to the guarantor rather than to the customer.

Description of the main types of risk mitigation

GIB uses a variety of risk mitigation techniques in several different markets which contribute to risk diversification and credit protection. The different credit risk mitigation techniques such as collateral, guarantees, credit derivatives, netting agreements and covenants are used to reduce credit risk. All credit mitigation activities are not necessarily recognised for capital adequacy purposes since they are not defined as eligible under the CBB's Basel 2 capital adequacy framework, e.g. covenants and non-eligible tangible collateral such as unquoted equities.

Exposures secured by eligible financial collateral, guarantees and credit derivatives, presented by standard portfolio were as follows:-

		Of which secured by:	
	Exposure before credit risk mitigation US$ millions	Eligible collateral US$ millions	Eligible guarantees or credit derivatives US$ millions
Sovereigns	403.1	-	403.1
Banks	1,578.0	559.1	988.4
Corporates	434.1	252.4	4.1

Guarantees and credit derivatives

Only eligible providers of guarantees and credit derivatives may be recognised in the standardised approach for credit risk. Guarantees issued by corporate entities may only be taken into account if their rating corresponds to A- or higher. The guaranteed exposures receive the risk weight of the guarantor.

GIB uses credit derivatives as credit risk protection only to a limited extent as the credit portfolio is considered to be well diversified.

Collateral and valuation principles

The amount and type of collateral is dependent upon the assessment of the credit risk of the counterparty. The market / fair 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 customer's repayment capacity rather than the collateral value. However, collateral is considered the secondary alternative if the repayment capacity proves inadequate. Collateral is not usually held against securities or placements.

Types of eligible collateral commonly accepted

The Group holds collateral against loans and advances in the form of physical assets, cash deposits, securities and guarantees.

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Basel 2
Pillar 3 Report (continued)

4. CREDIT RISK – PILLAR THREE DISCLOSURES (continued)

4.5 Impaired credit facilities and provisions for impairment

Individually impaired financial assets represent assets for which there is objective evidence that the Group will not collect all amounts due, including both principal and interest, in accordance with the contractual terms of the obligation. Objective evidence that a financial asset is impaired may include: a breach of contract, such as default or delinquency in interest or principal payments, the granting of a concession that, for economic or legal reasons relating to the borrower's financial difficulties, would not otherwise be considered, indications that it is probable that the borrower will enter bankruptcy or other financial re-organisation, the disappearance of an active market, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlate with defaults in the group. For equity securities classified as available-for-sale, a significant or prolonged decline in fair value below cost is considered in determining whether a security is impaired.

Provisions for impairment are determined based on the difference between the net carrying amount and the recoverable amount of a financial asset. The recoverable amount is measured as the present value of expected future cash flows, including amounts recoverable from guarantees and collateral.

Provisions for impairment are also measured and recognised on a collective basis in respect of impairments that exist at the reporting date but which will only be individually identified in the future. Future cash flows for financial assets that are collectively assessed for impairment are estimated based on contractual cash flows and historical loss experiences for assets with similar credit risk characteristics. Historical loss experience is adjusted, based on current observable data, to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based. Provisions for impairment are recognised in the consolidated statement of income and are reflected in an allowance account against loans and advances and investment securities.

i) Impaired loan facilities and related provisions for impairment

Impaired loan facilities and the related provisions for impairment were as follows:-

	Gross exposure US$ millions	Impairment provisions US$ millions	Net exposure US$ millions
Corporates	466.4	245.1	221.3
Financial institutions	219.6	164.1	55.5
Total	**686.0**	**409.2**	**276.8**

Impaired loan facilities of US$686.0 million include loans amounting to US$336.8 million that were not past due, but for which specific provisions had been established as a matter of prudency. 49.1 per cent of impaired loan facilities were therefore current in terms of both principal and interest.

The impaired loan facilities were principally to counterparties in the GCC.

ii) Provisions for impairment – loans and advances

The movements in the provisions for the impairment of loans and advances were as follows:-

	Specific provisions				
	Corporates US$ millions	Financial institutions US$ millions	Total US$ millions	Collective provisions US$ millions	Total provisions US$ millions
At 1st January 2011	239.1	158.2	397.3	245.0	642.3
Exchange rate movements	-	(0.1)	(0.1)	-	(0.1)
Amounts utilised	(7.3)	(9.0)	(16.3)	-	(16.3)
Amounts reallocated	20.0	15.0	35.0	(35.0)	-
Release for the year	(6.7)	-	(6.7)	-	(6.7)
At 31st December 2011	**245.1**	**164.1**	**409.2**	**210.0**	**619.2**

4. CREDIT RISK – PILLAR THREE DISCLOSURES (continued)

4.5 Impaired credit facilities and provisions for impairment (continued)

ii) Provisions for impairment – loans and advances (continued)

Stressed probabilities of default are anticipated to result from the impact of the global recession on the regional economic environment. The probabilities of default applied in the calculation of the collective provisions of impairment equated to a speculative-grade mean default rate of 13.9 per cent, exceeding the previous historical high corporate default levels witnessed in July 1991.

iii) Impaired investment securities and related provisions for impairment

Impaired investment securities and related provisions for impairment were as follows:-

	Gross exposure US$ millions	Impairment provisions US$ millions	Net exposure US$ millions
Equity investments	74.5	58.2	16.3
Total	**74.5**	**58.2**	**16.3**

Total specific impairment provisions of US$58.2 million represented 78.1 per cent of the gross impaired investment securities exposure.

There were no past due or impaired debt securities at 31st December 2011.

iv) Provisions for impairment – investment securities

The movements in the provisions for the impairment of investment securities were as follows:-

	Specific provisions US$ millions	Collective provisions US$ millions	Total provisions US$ millions
At 1st January 2011	44.2	23.6	67.8
Exchange rate movements	(0.1)	-	(0.1)
Amounts utilised	(0.6)	-	(0.6)
Charge / (Release) for the year	14.7	(9.9)	4.8
At 31st December 2011	**58.2**	**13.7**	**71.9**

4.6 Past due facilities

In accordance with guidelines issued by the CBB, credit facilities are placed on non-accrual status and interest income suspended when either principal or interest is overdue by 90 days whereupon unpaid and accrued interest is reversed from income. Interest on non-accrual facilities is included in income only when received. Credit facilities classified as past due are assessed for impairment in accordance with the IFRS guidelines as set out in section 4.5 of this report. A specific provision is established only where there is objective evidence that a credit facility is impaired.

i) Loans

The gross and carrying amount of loans for which either principal or interest was over 90 days past due were as follows:-

	Gross		Carrying amount	
	Corporates US$ millions	Financial institutions US$ millions	Corporates US$ millions	Financial institutions US$ millions
Secured	**86.4**	**-**	**86.4**	**-**
Unsecured				
Under restructuring and current	99.2	-	99.2	-
Other	196.8	200.1	77.5	61.3
Total unsecured	**296.0**	**200.1**	**176.7**	**61.3**

Basel 2
Pillar 3 Report (continued)

4. CREDIT RISK – PILLAR THREE DISCLOSURES (continued)

4.6 Past due facilities (continued)

i) Loans (continued)

Net unsecured past due loans of US$238.0 million included US$99.2 million of loans that were subject to restructuring programmes and for which interest was current and being paid on due dates. The restructurings were expected to be finalised within the six months ended 30th June 2012, following which, the loans will revert to performing status. The restructuring programmes are not expected to result in an economic loss for the Group.

Non-specific loan provisions of US$210.0 million represented 1.5 times the net carrying amount of other unsecured past due loans.

The overdue status of gross past due loans based on original contractual maturities were as follows:-

	Less than 1 year US$ millions	Years 2 and 3 US$ millions	Over 3 years US$ millions	Total US$ millions
Corporates	146.7	231.7	4.0	382.4
Financial institutions	67.2	132.9	-	200.1
Total	**213.9**	**364.6**	**4.0**	**582.5**

Subsequent to 31st December 2011, the past due loan over 3 years has been settled.

ii) Investment securities

There were no debt securities for which either principal or interest was over 90 days past due.

5. MARKET RISK – PILLAR THREE DISCLOSURES

5.1 Market risk

Market risk is the risk of loss due to adverse changes in interest rates, foreign exchange rates, equity prices and market conditions, such as liquidity. The principal market risks to which the Group is exposed are interest rate risk, foreign exchange risk and equity price risk associated with its trading, investment and asset and liability management activities. The portfolio effects of holding a diversified range of instruments across a variety of businesses and geographic areas contribute to a reduction in the potential negative impact on earnings from market risk factors.

The Group's trading activities principally comprise trading in debt and equity securities, foreign exchange and derivative financial instruments. Derivative financial instruments include futures, forwards, swaps and options in the interest rate, foreign exchange, and equity markets. The Group manages and controls the market risk within its trading portfolios through limit structures of both a VaR and non-VaR nature. Non-VaR based constraints relate, inter alia, to positions, volumes, concentrations, allowable losses and maturities.

5. MARKET RISK – PILLAR THREE DISCLOSURES (continued)

5.2 VaR model

A key element in the Group's market risk management framework is the estimation of potential future losses that may arise from adverse market movements. Exposure to general market risk is calculated utilising a VaR model. The use of the internal model approach for the calculation of the capital requirement for general market risk has been approved by the CBB. The multiplication factor to be applied to the Value-at-Risk calculated by the internal model has been set at the regulatory minimum of 3.0 by the CBB.

An inherent limitation of VaR is that past market movements may not provide an accurate prediction of future market losses. Historic analyses of market movements have shown that extreme market movements (i.e. beyond the 99 per cent confidence level) occur more frequently than VaR models predict. Stress tests are therefore regularly conducted to estimate the potential economic losses in such abnormal markets. Stress testing combined with VaR provides a more comprehensive picture of market risk. The Group regularly performs stress tests that are constructed around changes in market rates and prices resulting from pre-defined market stress scenarios, including both historical and hypothetical market events. Historical scenarios include the 1997 Asian crisis, the 1998 Russian crisis, the events of 9/11 and the 2008 credit crisis. In addition, the Group performs stress testing based on internally developed hypothetical market stress scenarios. Stress testing is performed for all material market risk portfolios.

A key objective of asset and liability management is the maximisation of net interest income through the proactive management of the asset and liability repricing profile based on anticipated movements in interest rates. VaR-based limits are utilised to control fluctuations in interest earnings resulting from changes in interest rates. The asset and liability repricing profile of the various asset and liability categories are set out in section 8 of this report.

For internal risk management purposes, the Group measures losses that are anticipated to occur within a 95 per cent confidence level. Internally, the Group measures VaR utilising a one month assumed holding period for both trading and banking book positions. For regulatory capital adequacy purposes, the figures are calculated using the regulatory VaR basis at a 99 per cent confidence level (2.33 standard deviations) and a ten-day holding period using one-year unweighted historical daily movements in market rates and prices. Correlations across broad risk categories are excluded for regulatory capital adequacy purposes.

The VaR by risk class for the Group's trading positions as calculated in accordance with the regulatory parameters set out above, was as follows:-

	31.12.11 US$ millions	Average US$ millions	High US$ millions	Low US$ millions
Interest rate risk	1.2	1.2	1.5	0.9
Foreign exchange risk	-	0.1	0.2	-
Equity risk	0.1	0.1	0.2	0.1
Total diversified risk	1.3	1.3	1.6	1.0

The Group conducts daily VaR back testing both for regulatory compliance purposes and for the internal evaluation of VaR against actual trading profits and losses. During the year ended 31st December 2011, there were no instances of a daily trading loss exceeding the trading VaR at the close of business on the previous business day.

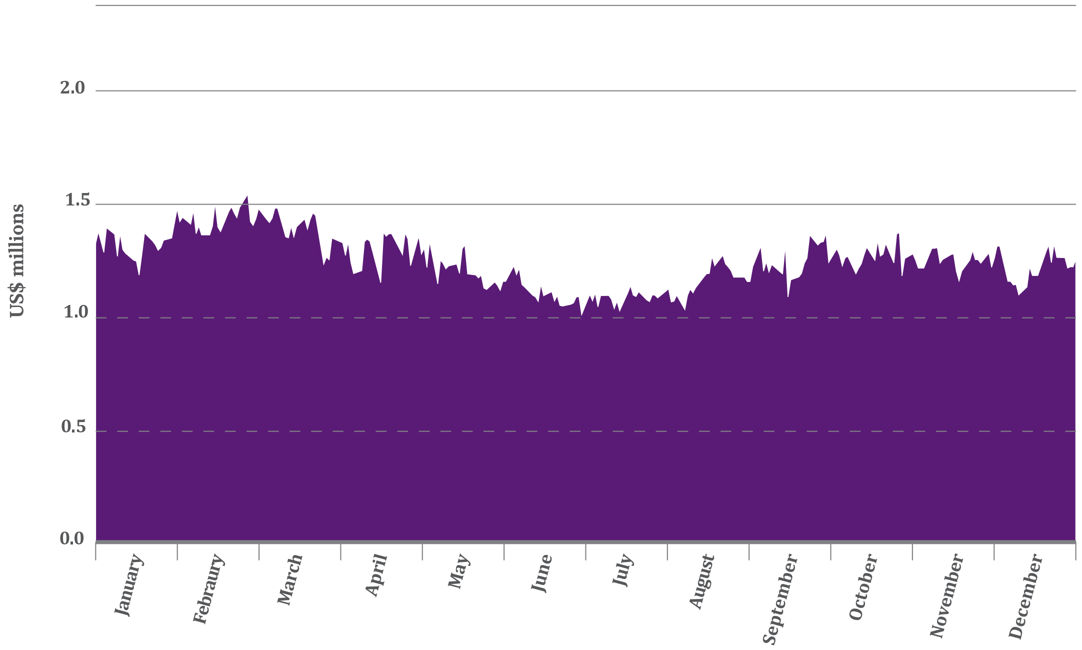
Basel 2
Pillar 3 Report (continued)

5. MARKET RISK – PILLAR THREE DISCLOSURES (continued)

5.2 VaR model (continued)

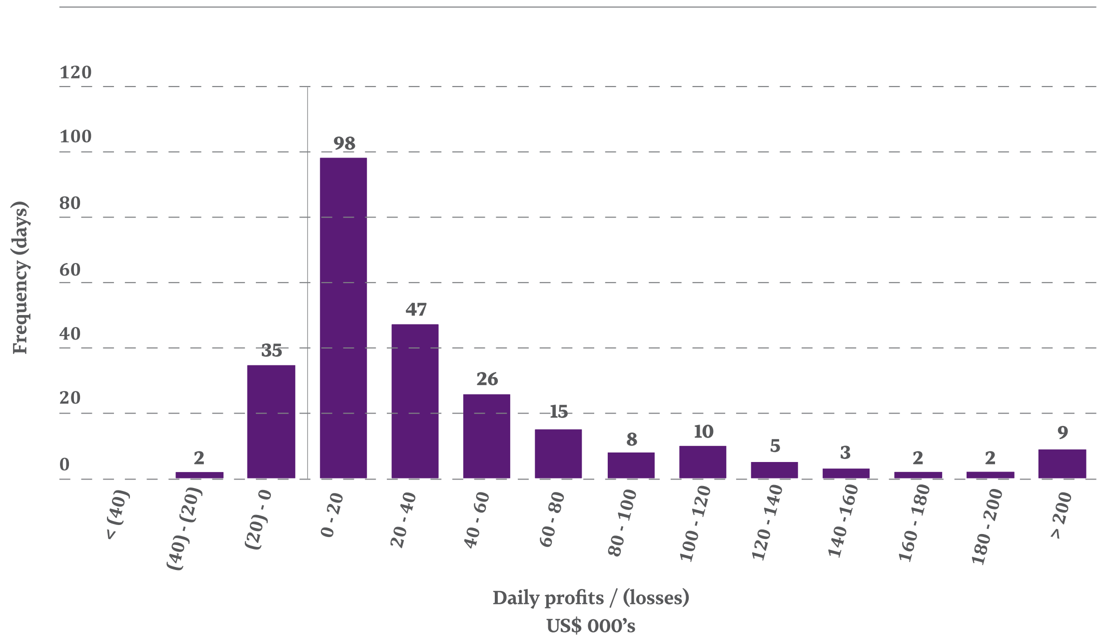
The graph below sets out the total VaR for all the Group's trading activities at the close of each business day throughout the year ended 31st December 2011:-

Trading Value-at-Risk (VaR) daily development
2011



The daily trading profits and losses during the year ended 31st December 2011 are summarised as follows:-

Histrogram of daily trading profits & losses



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5. MARKET RISK – PILLAR THREE DISCLOSURES (continued)

5.3 Sensitivity analysis

The sensitivity of the interest rate risk in the banking book to changes in interest rates is set out in section 8.2(iii) of this report.

The Group is also exposed to the impact of changes in credit spreads on the fair value of available-for-sale debt securities. Credit spread risk is managed within VaR limits and through the use of models to evaluate the sensitivity of changes in equity to movements in credit spreads. Based on the available-for-sale debt securities held at 31st December 2011, a one basis point increase in credit spreads would result in a US$0.8 million decrease in fair value.

6. OPERATIONAL RISK – PILLAR THREE DISCLOSURES

6.1 Operational risk

Whilst operational risk cannot be eliminated in its entirety, the Group endeavours to minimise it by ensuring that a strong control infrastructure is in place throughout the organisation. The various procedures and processes used to manage operational risk include effective staff training, appropriate controls to safeguard assets and records, regular reconciliation of accounts and transactions, close monitoring of risk limits, segregation of duties, and financial management and reporting. In addition, other control strategies, including business continuity planning and insurance, are in place to complement the procedures, as applicable.

As part of the Group's Operational Risk Management Framework (ORMF), comprehensive risk self-assessments are conducted, which identify the operational risks inherent in the Group's activities, processes and systems. The controls in place to mitigate these risks are also reviewed, and enhanced as necessary. A database of measurable operational risk events is maintained, together with a record of key risk indicators, which can provide an early warning of possible operational risk.

The capital requirement for operational risk is calculated for regulatory purposes according to the standardised approach, in which the regulatory capital requirement is calculated based on a range of beta coefficients, ranging from 12 to 18 per cent, applied to the average gross income for the preceding three financial years for each of eight predefined business lines. Consequently, the operational risk capital requirement is updated only on an annual basis.

7. OFF-BALANCE SHEET EXPOSURE AND SECURITISATIONS

Off-balance sheet exposures are divided into two exposure types in accordance with the calculation of credit risk RWAs in the CBB's Basel 2 capital adequacy framework:-

- Credit-related contingent items: Credit-related contingent items comprise guarantees, credit commitments and unutilised approved credit facilities.
- Derivative and foreign exchange instruments: Derivative and foreign exchange instruments are contracts, the value of which is derived from one or more underlying financial instruments or indices, and include futures, forwards, swaps and options in the interest rate, foreign exchange, equity and credit markets.

In addition to counterparty credit risk measured within the Basel 2 credit risk framework, derivatives also incorporate exposure to market risk and carry a potential market risk capital requirement, as commented on in more detail in section 5 of this report.

For the two off-balance exposure types, there are different possible values for the calculation base of the regulatory capital requirement, as commented on below:-

7.1 Credit-related contingent items

For credit-related contingent items, the nominal value is converted to an exposure at default (EAD) through the application of a credit conversion factor (CCF). The CCF factor is 50 per cent or 100 per cent depending on the type of contingent item, and is intended to convert off-balance sheet notional amounts into an equivalent on-balance sheet exposure.

Basel 2
Pillar 3 Report (continued)

7. OFF-BALANCE SHEET EXPOSURE AND SECURITISATIONS (continued)

7.1 Credit-related contingent items (continued)

Credit commitments and unutilised approved credit facilities represent commitments that have not been drawndown or utilised at the reporting date. The nominal amount provides the calculation base to which a CCF is applied for calculating the EAD. The CCF ranges between 0 per cent and 100 per cent depending on the approach, product type and whether the unutilised amounts are unconditionally cancellable or irrevocable.

The table below summarises the notional principal amounts, RWAs and capital requirements for each credit-related contingent category:-

	Notional principal amount US$ millions	RWA US$ millions	Capital requirement US$ millions
Direct credit substitutes	309.2	285.0	34.2
Transaction-related contingent items	2,618.9	907.2	108.9
Short-term self-liquidating trade-related contingent items	189.0	30.3	3.6
Commitments, including undrawn loan commitments and underwriting commitments under note issuance and revolving facilities	451.9	186.4	22.4
Total	**3,569.0**	**1,408.9**	**169.1**

Commitments may be drawndown on demand.

The notional principal amounts reported above are stated gross before applying credit risk mitigants, such as cash collateral, guarantees and counter-indemnities. At 31st December 2011, the Group held cash collateral, guarantees, counter-indemnities or other high quality collateral in relation to credit-related contingent items amounting to US$732.9 million.

7.2 Derivative and foreign exchange instruments

The Group utilises derivative and foreign exchange instruments to meet the needs of its customers, to generate trading revenues and as part of its asset and liability management activity to hedge its own exposure to market risk. Derivatives and foreign exchange instruments are subject to the same types of credit and market risk as other financial instruments. The Group has appropriate and comprehensive Board-approved policies and procedures for the control of exposure to both market and credit risk from its derivative and foreign exchange activities.

In the case of derivative transactions, the notional principal typically does not change hands. It is simply a quantity which is used to calculate payments. While notional principal is a volume measure used in the derivative and foreign exchange markets, it is neither a measure of market nor credit risk. The Group's measure of credit exposure is the cost of replacing contracts at current market rates should the counterparty default prior to the settlement date. Credit risk amounts represent the gross unrealised gains on non-margined transactions before taking account of any collateral held or any master netting agreements in place.

The Group participates in both exchange traded and over-the-counter (OTC) derivative markets. Exchange traded instruments are executed through a recognised exchange as standardised contracts and primarily comprise futures and options. OTC contracts are executed between two counterparties who negotiate specific agreement terms, including the underlying instrument, notional amount, maturity and, where appropriate, exercise price. In general, the terms and conditions of these transactions are tailored to the requirements of the Group's customers although conform to normal market practice. Industry standard documentation is used, most commonly in the form of a master agreement. The existence of a master netting agreement is intended to provide protection to the Group in the event of a counterparty default.

The Group's derivative and foreign exchange activities are predominantly short term in nature. Transactions with maturities over one year principally represent either fully offset trading transactions or transactions that are designated, and qualify, as fair value or cash flow hedges.

7. OFF BALANCE SHEET EXPOSURE AND SECURITISATIONS (continued)

7.2 Derivative and foreign exchange instruments (continued)

The aggregate notional amounts for derivative and foreign exchange instruments at 31st December 2011 are set out below:-

	Trading US$ millions	Hedging US$ millions	Total US$ millions
Interest rate contracts:-			
Interest rate swaps	1,364.0	5,003.0	6,367.0
Cross currency swaps	-	533.3	533.3
Options, caps and floors purchased	24.3	-	24.3
Options, caps and floors written	24.3	-	24.3
	1,412.6	5,536.3	6,948.9
Foreign exchange contracts:-			
Unmatured spot, forward and futures contracts	1,088.8	3,267.8	4,356.6
Credit contracts:-			
Protection sold	25.0	-	25.0
Total	**2,526.4**	**8,804.1**	**11,330.5**

7.3 Counterparty credit risk

Counterparty credit risk is the risk that a counterparty to a contract in the interest rate, foreign exchange, equity or credit markets defaults prior to the maturity of the contract. The counterparty credit risk for derivative and foreign exchange instruments is subject to credit limits on the same basis as other credit exposures. Counterparty credit risk arises in both the trading book and the banking book.

i) Counterparty credit risk calculation

For regulatory capital adequacy purposes, GIB uses the current exposure method to calculate the exposure for counterparty credit risk for derivative and foreign exchange instruments in accordance with the credit risk framework in the CBB's Basel 2 capital adequacy framework. Credit exposure comprises the sum of current exposure (replacement cost) and potential future exposure. The potential future exposure is an estimate, which reflects possible changes in the market value of the individual contract during the remaining life of the contract, and is measured as the notional principal amount multiplied by a risk weight. The size of the risk weight depends on the risk categorisation of the contract and the contract's remaining life. Netting of potential future exposures on contracts within the same legally enforceable netting agreement is done as a function of the gross potential future exposure.

The EAD, RWAs and capital requirements for the counterparty credit risk of derivative and foreign exchange instruments analysed by standard portfolio, is presented in the table below:-

	Exposure at Default (EAD)				
	Current exposure US$ millions	Future exposure US$ millions	Total exposure US$ millions	RWA US$ millions	Capital requirement US$ millions
Banks	41.9	68.4	110.3	40.1	4.8
Corporates	67.2	0.3	67.5	1.2	0.2
Total	**109.1**	**68.7**	**177.8**	**41.3**	**5.0**

Basel 2 Pillar 3 Report (continued)

7. OFF BALANCE SHEET EXPOSURE AND SECURITISATIONS (continued)

7.3 Counterparty credit risk (continued)

ii) Mitigation of counterparty risk exposure

Risk mitigation techniques are widely used to reduce exposure to single counterparties. The most common risk mitigation technique for derivative and foreign exchange-related exposure is the use of master netting agreements, which allow the Group to net positive and negative replacement values of contracts under the agreement in the event of default of the counterparty.

The reduction of counterparty credit risk exposure for derivative and foreign exchange instruments through the use of risk mitigation techniques is demonstrated as follows:-

	Current exposure US$ millions	Effect of netting agreements US$ millions	Netted current exposure US$ millions
Counterparty credit risk exposure	109.1	(19.5)	89.6

7.4 Securitisations

Securitisations are defined as structures where the cash flow from an underlying pool of exposures is used to secure at least two different stratified risk positions or tranches reflecting different degrees of credit risk. Payments to the investors depend upon the performance of the underlying exposures, as opposed to being derived from an obligation of the entity originating those exposures.

At 31st December 2011, the Group had no exposure, net of specific provisions, to securitisation tranches.

The Group provides collateral management services to five collateralised debt obligations (CDOs) issued between 2002 and 2006. The CDOs are intended to extract relative value from a wide range of asset classes across a broad spectrum of credit ratings. The underlying collateral of the CDOs includes leveraged loans, residential and commercial real estate, consumer finance, lending to small and medium-sized enterprises, and other receivables. Each CDO holds up to 85 individual investments.

At 31st December 2011 the underlying investments in the CDOs for which the Group acted as collateral manager amounted to US$1.1 billion. At 31st December 2011, GIB did not hold any exposure to CDOs managed by the Group.

8. INTERNAL CAPITAL INCLUDING OTHER RISK TYPES

GIB manages and measures other risk types that are not included under Pillar 1 in the CBB's Basel 2 framework. These are principally covered in the Group's internal economic capital model.

This section describes GIB's economic capital model and discusses the treatment of the other risk types that are not addressed in Pillar 1 of the CBB's Basel 2 framework.

8.1 Economic capital model

For many years, GIB has applied economic capital and risk-adjusted return on capital (RAROC) methodologies which are used for both decision making purposes and performance reporting and evaluation.

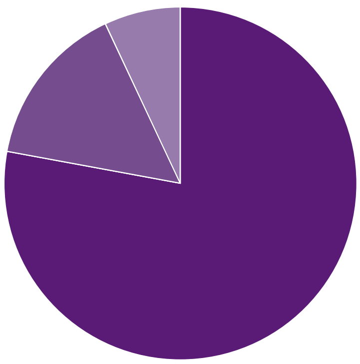
GIB calculates economic capital for the following major risk types: credit, market and operating risk. Operating risk includes business risk. Additionally, the economic capital model explicitly incorporates concentration risk, interest rate risk in the banking book and business risk.

8. INTERNAL CAPITAL INCLUDING OTHER RISK TYPES (continued)

8.1 Economic capital model (continued)

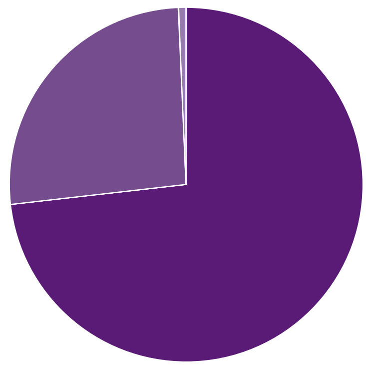
The composition of economic capital by risk type and business unit was as follows:-

Risk type



	%
Credit risk capital	77.9
Market risk capital	15.1
Operational risk capital	7.0
Total	**100.0**

Business unit



	%
Wholesale banking	73.2
Treasury	26.1
Financial markets	0.7
Total	**100.0**

The primary differences between economic capital and regulatory capital under the CBB's Basel 2 framework are summarised as follows:-

- In the economic capital methodology, the confidence level for all risk types is set at 99.88 per cent, compared to 99.0 per cent in the CBB's Basel 2 framework.
- Credit risk is calculated using GIB's estimates of probability of default, loss given default and exposures at default, rather than the regulatory values in the standardised approach.
- The economic capital model utilises GIB's embedded internal rating system, as described in more detail later in this section of the report, to rate counterparties rather than using the ratings of credit rating agencies or the application of a 100 per cent risk weighting for unrated counterparties.
- Concentration risk is captured in the economic capital model through the use of an internal credit risk portfolio model and add-on factors where applicable.
- The economic capital model applies a capital charge for interest rate risk in the banking book.
- The economic capital model applies a business risk capital charge where applicable.

Internal rating system

The economic capital model is based on an internal credit rating system. The internal credit rating system is used throughout the organisation and is inherent in all business decisions relating to the extension of credit. A rating is an estimate that exclusively reflects the quantification of the repayment capacity of the customer, i.e. the risk of customer default.

Basel 2
Pillar 3 Report (continued)

8. INTERNAL CAPITAL INCLUDING OTHER RISK TYPES (continued)

8.1 Economic capital model (continued)

Internal rating system (continued)
The Group monitors, manages and controls credit risk exposures based on an internal credit rating system that rates individual obligors based on a rating scale from 1 to 10, subject to positive (+) and negative (-) modifiers for rating grades 2 to 6. The internal credit rating is a measure of the credit-worthiness of a single obligor, based on an assessment of the credit risk relating to senior unsecured, medium-term, foreign currency credit exposure. The primary objectives of the internal credit rating system are the maintenance of a single uniform standard for credit quality measurement, and to serve as the primary basis for Board-approved risk parameters and delegated credit authority limits. The internal credit rating system also serves as a key input into the Group's RAROC performance measurement system. Ratings are assigned to obligors, rather than facilities, and reflect a medium-term time horizon, thereby rating through an economic cycle.

The internal ratings map directly to the rating grades used by the international credit rating agencies as illustrated below:-

Internal rating grade	Internal classification	Historical default rate range (percentage)	Fitch and Standard & Poor's	Moody's
Investment grade				
Rating grade 1	Standard	0.00 - 0.00	AAA	Aaa
Rating grade 2	Standard	0.00 - 0.04	AA	Aa
Rating grade 3	Standard	0.07 - 0.08	A	A
Rating grade 4	Standard	0.16 - 0.38	BBB	Baa
Sub-investment grade				
Rating grade 5	Standard	0.55 - 1.30	BB	Ba
Rating grade 6	Standard	2.60 - 9.12	B	B
Rating grade 7	Standard	27.39	CCC	Caa
Classified				
Rating grade 8	Substandard	27.39	CC	Ca
Rating grade 9	Doubtful	27.39	C	C
Rating grade 10	Loss	-	D	-

The external rating mapping does not intend to reflect that there is a fixed relationship between GIB's internal rating grades and those of the external agencies as the rating approaches differ.

The historical default rates represent the range of probability of defaults (PDs) between the positive and negative modifiers for each rating grade based on Standard & Poor's one year default rates for the 30 years from 1981 to 2010 for senior unsecured obligations. The default rates represent the averages over the 30-year period and therefore reflect the full range of economic conditions prevailing over that period.

8.2 Other risk types

i) Liquidity risk
The Group has established approved limits which restrict the volume of liabilities maturing in the short term. An independent risk management function monitors the future cash flow maturity profile against approved limits on a daily basis. The cash flows are monitored against limits applying to both daily and cumulative cash flows occurring over a 30-day period. The cash flow analysis is also monitored on a weekly basis by the Assets and Liabilities Committee (ALCO).

Customer deposits form a significant part of the Group's funding. The Group places considerable importance on maintaining the stability of both its customer and interbank deposits. The stability of deposits depends on maintaining confidence in the Group's financial strength and financial transparency.

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8. INTERNAL CAPITAL INCLUDING OTHER RISK TYPES (continued)

8.2 Other risk types (continued)

i) Liquidity risk (continued)

The funding base is enhanced through term financing, amounting to US$4,168.1 million at 31st December 2011. Access to available but uncommitted short-term funding from the Group's established Middle East and international relationships provides additional comfort. In addition to the stable funding base, the Group maintains a stock of liquid and marketable securities that can be readily sold or repoed.

Contractual standby facilities are available to the Group, providing access to US$500.0 million of collateralised funding based on pre-determined terms. The facilities are available to be drawn, in full or in part, at the Group's discretion up to 31st January 2013.

At 31st December 2011, 58.9 per cent of total assets were contracted to mature within one year. With regard to deposits, retention records demonstrate that there is considerable divergence between their contractual and effective maturities.

US$7,387.4 million or 73.4 per cent of the Group's deposits at 31st December 2011 were from GCC countries. Historical experience has shown that GIB's deposits from counterparties in the GCC region are more stable than deposits derived from the international interbank market. At 31st December 2011, placements with counterparties in non-GCC countries were 1.7 times the deposits received, demonstrating that the Group is a net lender of funds in the international interbank market.

ii) Concentration risk

Concentration risk is the credit risk stemming from not having a well-diversified credit portfolio, i.e. the risk inherent in doing business with large customers or being overexposed in particular industries or geographic regions. GIB's internal economic capital methodology for credit risk addresses concentration risk through the application of a single-name concentration add-on.

Under the CBB's single obligor regulations, banks incorporated in Bahrain are required to obtain the CBB's approval for any planned exposure to a single counterparty, or group of connected counterparties, exceeding 15 per cent of the regulatory capital base. At 31st December 2011, the following single obligor exposures exceeded 15 per cent of the Group's regulatory capital base (i.e. exceeded US$358.4 million):-

	On-balance sheet exposure US$ millions	Off-balance sheet exposure US$ millions	Total exposure US$ millions
Counterparty A	561.2	26.0	587.2
Counterparty B	357.5	215.8	573.3
Counterparty C	-	524.3	524.3
Counterparty D	268.7	180.0	448.7

These exposures had been approved by the CBB in accordance with the CBB's single obligor regulations. Under the CBB's regulations, single obligors include entities in which there is an ownership interest of 20 per cent or more. This is a significantly lower threshold than that used to determine control under IFRS.

In accordance with the CBB single obligor regulations, certain excess exposures that were pre-approved by the CBB are required to be treated as regulatory capital deductions. The deductions are to be applied 50 per cent against tier 1 and 50 per cent against tier 2.

Basel 2
Pillar 3 Report (continued)

8. INTERNAL CAPITAL INCLUDING OTHER RISK TYPES (continued)

8.2 Other risk types (continued)

iii) Interest rate risk in the banking book

Structural interest rate risk arises in the Group's core balance sheet as a result of mismatches in the repricing of interest rate sensitive financial assets and liabilities. The associated interest rate risk is managed within VaR limits and through the use of models to evaluate the sensitivity of earnings to movements in interest rates.

The repricing profile of the Group's financial assets and liabilities is set out in the table below:-

	Within 3 months US$ millions	Months 4 to 6 US$ millions	Months 7 to 12 US$ millions	Over 1 year US$ millions	Non-interest bearing items US$ millions	Total US$ millions
Cash and other liquid assets	824.9	33.8	-	-	-	858.7
Securities purchased under agreements to resell	150.0	50.0	80.0	-	-	280.0
Placements	5,369.0	25.0	-	-	-	5,394.0
Trading securities	56.9	-	-	-	26.8	83.7
Investment securities:-						
- Fixed rate	-	126.1	107.9	713.8	-	947.8
- Floating rate	1,810.4	104.3	-	-	(13.7)	1,901.0
- Equities and equity funds	-	-	-	-	302.9	302.9
Loans and advances	4,741.9	2,095.3	112.8	11.8	(210.0)	6,751.8
Other assets	-	-	-	-	269.0	269.0
Total assets	12,953.1	2,434.5	300.7	725.6	375.0	16,788.9
Deposits	9,742.9	251.5	75.2	-	-	10,069.6
Securities sold under agreements to repurchase	283.3	-	-	-	-	283.3
Other liabilities	-	-	-	-	305.1	305.1
Term financing	4,103.2	64.9	-	-	-	4,168.1
Equity	-	-	-	-	1,962.8	1,962.8
Total liabilities & equity	14,129.4	316.4	75.2	-	2,267.9	16,788.9
Interest rate sensitivity gap	**(1,176.3)**	**2,118.1**	**225.5**	**725.6**	**(1,892.9)**	**-**
Cumulative interest rate sensitivity gap	**(1,176.3)**	**941.8**	**1,167.3**	**1,892.9**	**-**	**-**

The repricing profile is based on the remaining period to the next interest repricing date. Derivative financial instruments that have been used for asset and liability management purposes to hedge exposure to interest rate risk are incorporated in the repricing profiles of the related hedged assets and liabilities. The non-specific investment security and loan provisions are classified in non-interest bearing items.

The substantial majority of assets and liabilities reprice within one year.

Interest rate exposure beyond one year amounted to only US$725.6 million or 4.3 per cent of total assets. This exposure principally represented the investment of the net free capital funds in fixed rate government securities. At 31st December 2011 the modified duration of these fixed rate government securities was 2.27. Modified duration represents the approximate percentage change in the portfolio value resulting from a 100 basis point change in yield. More precisely in dollar terms, the price value of a basis point of the fixed rate securities was US$175,000.

8. INTERNAL CAPITAL INCLUDING OTHER RISK TYPES (continued)

8.2 Other risk types (continued)

iii) Interest rate risk in the banking book (continued)

Based on the repricing profile at 31st December 2011, and assuming that the financial assets and liabilities were to remain until maturity or settlement with no action taken by the Group to alter the interest rate risk exposure, an immediate and sustained one per cent (100 basis points) increase in interest rates across all maturities would result in a reduction in net income before tax for the following year and in the Group's equity by approximately US$11.3 million and US$30.4 million respectively. The impact on the Group's equity represents the cumulative effect of the increase in interest rates over the entire duration of the mismatches in the repricing profile of the interest rate sensitive financial assets and liabilities.

iv) Foreign exchange risk

The Group does not maintain material foreign currency exposures. In general, the Group's policy is to match financial assets and liabilities in the same currency or to mitigate currency risk through the use of currency swaps.

v) Business risk

Business risk represents the earnings volatility inherent in all businesses due to the uncertainty of revenues and costs due to changes in the economic and competitive environment.

For economic capital purposes, business risk is calculated based on the annualised cost base of applicable business areas.

9. CAPITAL ADEQUACY RATIOS AND OTHER ISSUES

9.1 Capital adequacy ratios

The Group's policy is to maintain a strong capital base so as to preserve investor, creditor and market confidence and to sustain the future development of the business. The impact of the level of capital on shareholders' return is also recognised as well as the need to maintain a balance between the higher returns that might be possible with greater gearing and the advantages and security afforded by a sound capital position. The Group manages its capital structure and makes adjustments to the structure taking account of changes in economic conditions and strategic business plans. The capital structure may be adjusted through the dividend payout and the issue of new shares.

The capital adequacy ratios of GIB's principal subsidiary, GIBUK, and the Group were as follows:-

	GIBUK	Group
Total RWAs (US$ millions)	759.1	10,272.7
Capital base (US$ millions)	208.6	2,389.3
Tier 1 capital (US$ millions)	208.6	1,969.3
Tier 1 ratio (per cent)	**27.5%**	**19.2%**
Total ratio (per cent)	**27.5%**	**23.3%**

GIB aims to maintain a minimum tier 1 ratio in excess of 8 per cent and a total capital adequacy ratio in excess of 12 per cent. The CBB's current minimum total capital adequacy ratio for banks incorporated in Bahrain is set at 12 per cent. The CBB does not prescribe a minimum ratio requirement for tier 1 capital.

Basel 2 Pillar 3 Report (continued)

9. CAPITAL ADEQUACY RATIOS AND OTHER ISSUES (continued)

9.1 Capital adequacy ratios (continued)

Strategies and methods for maintaining a strong capital adequacy ratio

GIB prepares multi-year strategic projections on a rolling annual basis, which include an evaluation of short-term capital requirements and a forecast of longer-term capital resources.

The evaluation of the strategic planning projections has historically given rise to capital injections. The capital planning process triggered the raising of additional tier 2 capital through a US$400 million subordinated debt issue in 2005 to enhance the total regulatory capital adequacy ratio, and a US$500 million capital increase in March 2007 to provide additional tier 1 capital to support planned medium-term asset growth. A further US$1.0 billion capital increase took place in December 2007 to enhance capital resources and compensate for the impact of provisions relating to exposures impacted by the global credit crisis.

9.2 ICAAP considerations

Pillar 2 in the CBB's Basel 2 framework covers two main processes: the ICAAP and the supervisory review and evaluation process. The ICAAP involves an evaluation of the identification, measurement, management and control of material risks in order to assess the adequacy of internal capital resources and to determine an internal capital requirement reflecting the risk appetite of the institution. The purpose of the supervisory review and evaluation process is to ensure that institutions have adequate capital to support the risks to which they are exposed and to encourage institutions to develop and apply enhanced risk management techniques in the monitoring and measurement of risk.

GIB's regulatory capital base exceeded the CBB's minimum requirement of 12 per cent throughout the year ended 31st December 2011. Based on the results of capital adequacy stress testing and capital forecasting, GIB considers that the buffers held for regulatory capital adequacy purposes are sufficient and that GIB's internal minimum capital targets of 8 per cent for tier 1 capital and 12 per cent for total capital are adequate given its current risk profile and capital position. The Group's regulatory capital adequacy ratios set out in section 9.1 of this report significantly exceeded the minimum capital targets and are high by international comparison.

GIB uses its internal capital models, economic capital, and capital adequacy calculations based on the CBB's FIRB approach for credit risk when considering internal capital requirements both with and without the application of market stress scenarios. As a number of Pillar 2 risk types exist within GIB's economic capital framework (i.e. interest rate risk in the banking book, concentration risk and business risk), GIB uses its existing internal capital measurements as the basis for determining additional capital buffers. GIB considers the results of its capital adequacy stress testing, along with economic capital and RWA forecasts, to determine its internal capital requirement and to ensure that the Group is adequately capitalised in stress scenarios reflecting GIB's risk appetite.

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10. GLOSSARY OF ABBREVIATIONS

ALCO	Assets and Liabilities Committee
AMA	Advanced Measurement Approach
Basel Committee	Basel Committee for Banking Supervision
CBB	Central Bank of Bahrain
CCF	Credit Conversion Factor
CDO	Collateralised Debt Obligation
CEO	Chief Executive Officer
CFO	Chief Financial Officer
CI&TO	Chief Investment and Treasury Officer
CRO	Chief Risk Officer
EAD	Exposure at Default
FIRB Approach	Foundation Internal Ratings Based Approach
FSA	Financial Services Authority (of the United Kingdom)
GCC	Gulf Cooperation Council
GIB	Gulf International Bank B.S.C.
GIBUK	Gulf International Bank (U.K.) Limited
The Group	Gulf International Bank B.S.C. and subsidiaries
ICAAP	Internal Capital Adequacy Assessment Process
IFRS	International Financial Reporting Standards
LGD	Loss Given Default
MENA	Middle East and North Africa
ORMF	Operational Risk Management Framework
OTC	Over-The-Counter
PD	Probability of Default
PSE	Public Sector Entities
RAROC	Risk-adjusted Return on Capital
RWA	Risk Weighted Amount
VaR	Value-at-Risk

Group Corporate Directory

General Management

Dr. Yahya Alyahya
Chief Executive Officer
Stephen Williams
Managing Director – Chief Financial Officer
Adel Al-Mangour
Managing Director – Wholesale Banking
Christopher Berry
Managing Director – Retail Banking
Jose Marigomen
Managing Director – Chief Risk Officer
Matthew Snyder
Managing Director & CEO – GIBUK

Wholesale Banking

Relationship Management

Layth Al Shaiban
Head of KSA Relationship Management
Ali Al-Derazi
GCC Relationship Management
Asghar Ali Baba
International Banking & GCC FIs

Investment Banking

Srinivas Vemparala
Head of Investment Banking
Khalid Al-Ghamdi
Corporate Finance – KSA
Fakhre Fazli
Equity Capital Markets
Iftikhar Ali
Debt Capital Markets &
Sharia-Compliant Banking

Credit Products

Ravi Krishnan
Head of Credit Products
Salman Hasan Usmani
Loans & Trade Credit
Udit N. Mishra
Project & Structured Finance

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Maneesh Ajmani
Head of Private Equity

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Uday Patnaik
Chief Investment Officer
Peter Carey
Equity Portfolio Management
Kay Turner
Fund Product Manager
Malcolm Taylor
Investor Relations

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Abdulla Alzahrani
Chief Investment & Treasury Officer
Steven Moulder
Head of FX & Money Markets and Client Solutions
Ali Al-Qaseer
Head of International Financial Institutions & Funding Relationship Programme

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Russell Bennett
Group Financial Controller
Rahul Thomas
Head of Balance Sheet Management
Julian Anthony
Chief Financial Officer – GIBUK

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Chief Credit Officer
Michael Cowling
Head of Information Security &
Operational Risk
Shane Panjvani
Head of Operational Risk – Bahrain
Sameer Al-Jishi
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Rajan Malik
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Head of Enterprise Project - Management Office

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Khalid Mahmood
Head of Compliance
Ramnath Narayanan
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Abdulla Naneesh
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