

Capital Management House B.S.C. (c)

**Basel II, Pillar III Disclosures
for the six months period ended**

30 June 2011 (Reviewed)

Capital Management House B.S.C.(c)

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1 Back ground

Capital Management House B.S.C.(c) (the "Bank") was incorporated in the Kingdom of Bahrain in accordance with and subject to the provisions of the Bahrain Commercial Companies Law, Decree no (21) of 2001 and its Implementation Regulations issued as per Ministerial Order No (6) of 2002 and registered with the Ministry of Industry and Commerce under Commercial Registration (CR) number 61045 on 15 May 2006. Until 7 October 2009, the Bank operated under an Investment Firm (Category I) License issued by the Central Bank of Bahrain (CBB) and from 7 October 2009 the CBB has upgraded its license to a "Wholesale Islamic Bank". The Bank's registered office is at Office 81, Building B1, Road 365, Block 316, Bahrain World Trade Center, Manama, Kingdom of Bahrain. The principle activities of the Bank includes:

- Short term investments;
- Capital market: Sukuk securities, equity linked offering, initial public offering and rights issues;
- Advisory services: Mergers and acquisitions, private placement, divestures and real estate developments;
- Asset management; and
- Islamic deposits products and customers' current account

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

The Board of Directors seeks to optimize the Group's performance by enabling the various group business units to realize the Group's business strategies and meet agreed business performance targets by operating within the agreed capital and risk parameters and the Group's risk policy framework.

The Public Disclosures under this section have been prepared in accordance with the CBB's requirements outlined in the Public Disclosure Module Requirements ("PD:") Section PD - 1 requirements, CBB Rule Book, Volume II for Islamic Banks. For the purposes of guidance we have cross referenced every disclosure with the relevant paragraph number of the CBB's PD Requirement Module.

2 Capital Adequacy

The primary objectives of the Group's capital management are to ensure that the Group complies with regulatory capital requirements and that it maintains healthy capital ratios in order to support its business and to maximize shareholders' value.

The Group manages its capital structure and makes adjustments to it in the light of changes in economic conditions and risk characteristics of its activities. In order to maintain and adjust the capital structure, the Group may adjust the amount of dividend payment to shareholders, return capital to shareholders or issue capital securities.

The Bank's capital adequacy policy is to maintain a strong capital base to support the development and growth of the business. Current and future capital requirements are determined on the basis of growth expectations of the business and future sources and uses of funds. The Bank's regulator, CBB requires the Bank to maintain a ratio of 12% of total risk weighted assets as the minimum regulatory capital. To assess the capital adequacy requirements in accordance with the CBB requirements, the Group adopts the Standardized Approach for its credit risk, Basic Indicator Approach for its Operational Risk and the Standardized Measurement Approach for its Market Risk.

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Table 1 - Capital Structure (PD 1.3.12, 1.3.13, 1.3.15)

	<i>Tier 1</i> <i>USD'000</i>	<i>Tier 2</i> <i>USD'000</i>
Issued and fully paid ordinary shares	105,000	
Less: Employee stock incentive program funded by the bank	(4,432)	
Share premium	17,912	
General reserve	563	
Statutory reserve	2,180	
Other reserves	447	
Retained earnings brought forward	(9,038)	
Unrealized gains arising from fair valuing equity through statement of income 45% only	3,168	
Less: Current interim cumulative net losses	(5,822)	
Less: Unrealized gross losses arising from fair valuing equity securities	(2,235)	
Tier 1 Capital before PCD deductions	107,743	
Unrealized gains arising from fair valuing equity securities (45% only)		164
Tier 2 Capital before PCD deductions		164
Regulatory deductions		
Excess amount over maximum permitted large exposure limits	(12,818)	-
Total Deductions		-
Net Available capital	94,925	164
Total Eligible Capital Basel II (Tier 1 and Tier 2)		95,089

Table 2 - Capital Requirement by type of Islamic financing contracts (PD 1.3.17)

The following table summarizes the credit risk exposures as per the standardized approach and related capital requirements by type of Islamic financing contracts:

	<i>Amount of exposures</i> <i>USD'000</i>	<i>Risk weighted assets</i> <i>USD'000</i>	<i>Capital requirement 12%</i> <i>USD'000</i>
Commodity Murabaha receivables	2,000	500	60
Musharaka receivables	2,995	-	-
Mudaraba receivables	16,350	3,270	392
	21,345	3,770	452

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Table 3 - Capital requirement for market risk (PD 1.3.18)

The following table summaries the exposures subject to standardized measurement approach of market risk and related capital requirements:

	Self Financed USD'000	Capital requirement 12% USD'000
Market Risk - Standardized measurement approach		
Price risk	300	36
Equity position risk	974	117
Sukuk risk	468	56
Foreign Exchange risk	1,796	216
Total of Market Risk - Standardized Measurement Approach	3,538	425
Multiplier	12.5	12.5
	44,225	5,307
Eligible portion for the purpose of the calculations	100%	100%
Risk weighted exposures to be used in CAR calculation	44,225	5,307

Table 4 - Capital requirements for operational risk (PD 1.3.19 & PD 1.3.30 (a and b))

The following table summaries the operational risk exposures subject to basic indicator approach of operational risk and related capital requirements:

	Capital Charge USD'000
Indicators of Operational risk	
Average gross income (three previous years)	9,045
Multiplier	12.5
	113,063
Eligible portion for purposes of calculation	15%
Risk Weighted Exposures	16,959

Table 5 - Capital adequacy ratios (PD 1.3.20)

The following table summarizes the Capital Adequacy Ratios for Total Capital and Tier 1 Capital

	Total capital adequacy ratio	Tier 1 capital adequacy ratio
Top consolidated level	35.59%	35.65%

3 Risk Management

3.1 Group wide Risk Management Objectives

The risk management objective of the Group is to identify, capture, monitor and manage various dimensions of risk with the objective of protecting asset values and income streams such that the interest of Group's shareholders (and others to whom the Group owes liability) are safeguarded, while the returns are intended to optimize the Group's shareholder return, with the risk exposure maintained within the self-imposed parameters.

The Group has defined its risk appetite within the parameters of its risk strategies. The Group reviews and realigns its risk appetite as per the evolving business plan of the Group with changing economic and market scenarios. The Group also assesses its tolerance for specific risk categories and its strategies to manage these risks.

In addition to satisfying the minimum regulatory capital requirements of the CBB, the Group seeks to constantly identify and quantify, to the extent possible, the various risks that are inherent in the normal course of its business and maintain appropriate internal capital levels and consequently is in the process of developing an Internal Capital Adequacy assessment Plan ("ICAAP") framework. The main objective of the Group's ICAAP would be to ensure that adequate capital is retained at all times to support the risk the Group undertakes in the course of its business.

3.2. Strategies, Processes and Internal Controls

3.2.1 Group's risk strategy

The 'Capital Management Policy and Risk Charter' of the Group defines the risk strategies. These are also supported by appropriate limit structures. These policies provide an enterprise wide integrated risk management framework for the Group.

The 'Risk Charter' identifies risk objectives, policies, strategies and risk governance both at the Board of Directors ("Board") and management level. The 'Capital Management Policy' is aimed at ensuring financial stability by allocating enough capital to cover the unexpected losses.

The limit structure serves as a key component in articulating risk strategy in quantifiable risk appetite. In addition the Group is in the process of implementing various risk systems to help quantify not just the regulatory capital but also the economic capital allocated to various investment portfolios.

The Group is exposed to various types of risks, such as market, credit, profit rate, liquidity and operational, all of which require the comprehensive controls and ongoing oversight. The risk management framework summarizes the spirit behind Basel II, which includes management oversight and control, risk culture and ownership, risk recognition and assessment, control activities, segregation of duties, adequate information and communication channels, monitoring risk management activities and correcting deficiencies.

The Group has established an independent Internal Audit Function headed by a professional accountant as the Head of Internal Audit. The Internal Audit Charter has been approved by the Board and a Risk Based Internal Audit approach has been implemented. The Internal Audit Function reports to the Audit and Risk Committee of the Board.

3.2.2 Credit risk

Credit risk is the risk that one party to a financial contract may fail to discharge an obligation and cause the other party to incur financial loss. The Group controls credit risk by monitoring credit exposures with reference to limits structure and concentration of risks for counterparties, sector and geography and by continually assessing the creditworthiness of counterparties.

3.2.3 Market risk

Market risk is the risk that the fair value or future cash flows of financial instruments may fluctuate due to changes in market variables such as profit rates, foreign exchange rates and equity prices. The Group has set limits on the risk that may be accepted.

The Group is in the process of developing techniques to carry out stress testing to assess the impact of adverse market conditions on its market risk sensitive portfolio. The Group's management believes that the Group is not exposed to material market risk sensitive assets.

3.2.4 Equity Price risk

Equity price risk is the risk that the fair values of equities decrease as a result of changes in the levels of equity indices and the value of individual stocks. The Group manages this risk through diversification of investments in terms of geographical distribution and industry concentration.

3.2.5 Profit rate risk

Profit rate risk arises from the possibility that changes in profit rates may affect future profitability or the fair values of financial instruments. The Group's management believes that the Group is not exposed to material profit rate risk as a result of mismatches in profit rate repricing.

3.2.6 Foreign exchange risk

Foreign exchange risk is the risk that the value of financial instruments may fluctuate due to changes in foreign exchange rates. The currency positions are monitored on a daily basis to ensure positions are maintained within established limits.

3.2.7 Operational risk

Operational risk is the risk of loss arising from system failure, human error, fraud or external events. When controls fail to perform, operational risk can cause damage to reputation, have legal or regulatory implications, or lead to financial loss. The Bank cannot expect to eliminate all operational risks, but through a control frame work and by monitoring and responding to potential risks, the Group is able to manage the operational risks. Controls include effective segregation of duties, access, authorization and reconciliation procedures. Maker checker concept and dual eye principles are also applied across the Group, where possible.

3.2.8 Prepayment risk

Prepayment risk is the risk that the Group will incur a financial loss because its counterparties may repay or request repayment earlier or later than expected maturity. The Group is not exposed to any significant prepayment risk.

3.2.9 Displaced commercial risk

Displaced commercial risk ("DCR") refers to the market pressure to pay returns that exceeds the rate that has been earned on the assets financed by liabilities, when the return on assets is underperforming as compared to Competitor's rates. The Group is not exposed to any displaced commercial risk.

3.3 Structure and organization of Risk Management Function

Risk Management Structure includes all levels of authorities, organizational structure, people and systems required for smooth functioning of risk management processes in the Group. The responsibilities associated with each level of risk management structure and authority include the following:

The Board retains ultimate responsibility and authority for all risk matters, including:

- a) Establishing overall policies and procedures;
- b) Delegating authority to Investment Committee, Audit, Risk and Governance Committee and the management to review and approve any risk related issues; and
- c) Risk Management Committee (comprising of senior officials of the Group) is responsible to review new products and facilities from risk perspective, and review on an ongoing basis all risk related issues pertaining to all assets of the Group and submit its risk assessment and recommendations to the Management Committee (comprising of executive management and senior officers of the Group) in all risk related issues.

3.4 Risk Measurement and Reporting Systems

Based on the risk appetite of the Group, the Group has put in place various exposure limits (both global limits for consolidated exposure to currency, industry and geography and specific investment limits for individual assets). These limits are approved by the Board. Any limit breaches are reported to the Management Committee and to the Board. The limits are reviewed and revised at least on an annual basis or when it is deemed necessary.

The Group has developed a risk measurement and reporting mechanism that translates various system generated reports into a risk assessment report to monitor all limits and exposure on various types of risk.

3.5 Credit risk

3.5.1 Types of credit risk

Contracts entered into by the Group comprise of Murabaha receivables, Mudaraba receivables and Wakala receivables.

Murabaha receivables

These are basically sales on deferred terms.

The Bank arranges a Murabaha transaction by buying a commodity (which represents the object of the Murabaha) and then sells this commodity to the Murabeh (beneficiary) after adding a margin of profit over the cost. The sale price (cost plus profit margin) is repaid by the Murabeh over the agreed period.

Mudaraba receivables

Mudaraba receivables is a partnership whereby the Bank ("rabbalmaal") gives money to another institutions ("Mudarib") for investing in a commercial enterprise for a definite period of time.

Wakala receivables

Wakala receivables is an investment product similar to Mudaraba receivables. However under an wakala agreement the investor ("Wakil") receives only an agreed ratio of profit derived from the investment and all excess are for the benefit of "Muwakkil".

3.5.2 Past Due and impaired islamic facilities

The Group defines facility (including investments) as non-performing facility when it is overdue for a period of 90 days or more. Non-performing facilities are placed on non-accrual basis and any income on such facilities are recognized on receipts basis only. It is the Group's policy that when an exposure is overdue for a period of 90 days or more, the whole of the facility extended or investment made is considered as past due and impaired and not only the overdue installments / payments.

3.5.3 Definition of Geographical area

The geographical distribution of the exposures are monitored by the Group's Financial Control Department and reported to the Management Committee on an ongoing basis and the Audit, Risk and Governance Committee of the Board on a quarterly basis. The Group's classification of geographical area is according to its business needs and the distribution of its portfolio.

3.5.4 Concentration Risk

Concentration risk is the credit risk stemming from not having a well diversified credit portfolio, i.e. being overexposed to a single customer, industry or geographic region. As per CBB's single obligor regulations, banks incorporated in the Kingdom of Bahrain and licensed by CBB are required to obtain the CBB's prior approval for any planned exposure to a single counterparty, or a group of connected counterparties, exceeding 15% of the regulatory capital base.

The Group's policy and procedures include specific guidelines to focus on maintaining a diversified portfolio and all identified concentration of risks are controlled and managed accordingly.

3.5.5 Large Exposure

Large exposure is any exposure whether direct or indirect to a counterparty or a group of closely related counterparties which is greater than or equal to 10% of the Group's regulatory capital base.

Prior written approval from the CBB is required in the following cases:

- a) If any counterparty (single/group) exposure exceeds 15% of Group's regulatory capital base; and
- b) If any facility (new/extended) to an employee is equal to or above BD 100,000 (or equivalent).

3.5.6 Related party transactions

The disclosure relating to related party transactions has been made in the interim condensed consolidated financial statements for the period ended 30 June 2011. These statements are also included on the website of the Group. All related party transactions have been made on arm's length basis.

It is the policy of the Group to request and obtain Board representation in the Investment Special Purpose Vehicles ("SPV") and the Board representation is primarily to monitor and manage the investments to the best interest of the shareholders of the Group. These investments are included in the above disclosure in the interim condensed consolidated financial statements for the period ended 30 June 2011.

3.5.7 Credit Risk Mitigation

Credit risk mitigation refers to use of a number of techniques, such as collaterals, guarantees, credit derivatives (Shari'a compliant contract) to mitigate the credit risks that the Group is exposed to. Credit risk mitigants reduce the credit risk by allowing the Group to protect against counterparty non-performance of credit contracts through collateral, netting agreements, guarantees and credit derivatives (Shari'a compliant contract). Refer to Table 19

The Group generally extends Islamic facilities or initiates equity investments only when supported by adequate underlying collateral assets and / or audited financial statements. Investments and facilities without adequate tangible collateral assets are considered only when audited financial statements reveal satisfactory financial position/ repayment ability and the facility are properly structured supported by cash flow projections, fair value projections, assignments, guarantees, etc. as appropriate. Additionally significant equity investments in new ventures are supported by Board representations to monitor the investment through its holding period. Facilities to non corporate entities without audited financial statements is discouraged and is approved only on an exceptional basis after careful analysis of the quality of customer, market reputation etc.

Generally the Group ensures the following with respect to an acceptable collateral or underlying asset for facilities granted by the Group.

- a. The assets must be maintaining their value during the holding period of the investment,
- b. Such assets should be easily convertible into cash, if required (liquidity),
- c. There should be reasonable market for the assets (marketability), and
- d. The group should be able to enforce its rights over the asset if necessary (enforceability).

The Legal department ensures the satisfactory evidences of legal and physical ownership of the underlying assets supporting the investment or the facility.

The Financial Control Department with the assistance of Investment Department ensures periodic valuation of the underlying assets (including real estate) and obtain external valuations where applicable and submit periodic reports on the adequacy or otherwise of the underlying assets to the Management Committee.

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Table 6 - Credit risk exposure (PD 1.3.23)

The following table summarizes: (a) the amount of gross funded credit exposure (before any risk mitigation) as at 30 June 2011 (b) average gross exposure for the period ended on 30 June 2011 and (c) exposure funded by own capital.

The average gross funded exposure is calculated on the month end balances:

	<i>Total gross credit exposure USD '000</i>	<i>Average gross exposure over the period USD '000</i>
Funded		
Cash and bank balances	1,292	2,378
Due from financial institutions	16,850	16,160
Investments	108,988	116,079
Non-current assets held for sale	1,326	1,326
Fixed assets	1,086	1,193
Other assets	1,020	1,051
Sub total	<u>130,562</u>	<u>138,187</u>
Unfunded / commitments		
Investment commitments	11,785	11,785
Foreign Exchange commitments	478	482
Other commitments	916	983
Sub total	<u>13,179</u>	<u>13,250</u>
Total credit risk exposure	<u><u>143,741</u></u>	<u><u>151,437</u></u>

Table 7 - Credit risk - Geographical breakdown (PD 1.3.23 (b))

The following table summarizes the geographical distribution of exposures, broken down into significant areas by major types of credit exposures:

	<i>GCC and Middle East USD '000</i>	<i>Europe USD '000</i>	<i>Africa and Asia USD '000</i>	<i>North America USD '000</i>	<i>Total USD '000</i>
Funded					
Cash and bank balances	202	20	1	1,069	1,292
Due from financial institutions	16,850	-	-	-	16,850
Investments	83,431	10,230	15,327	-	108,988
Non-current assets held for sale	1,326	-	-	-	1,326
Fixed assets	1,086	-	-	-	1,086
Other assets	1,020	-	-	-	1,020
	<u>103,915</u>	<u>10,250</u>	<u>15,328</u>	<u>1,069</u>	<u>130,562</u>
Unfunded / commitments					
Investment commitments	11,406	-	379	-	11,785
Foreign Exchange commitments	-	478	-	-	478
Other commitments	916	-	-	-	916
	<u>12,322</u>	<u>478</u>	<u>379</u>	<u>-</u>	<u>13,179</u>

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Table 8 - Credit risk - Industry breakdown (PD 1.3.23 (c))

The following table summarizes the distribution of exposures by industry, broken down by major types of credit exposures:

	<i>Trading and manufact uring</i> USD '000	<i>Banks and financial institutions</i> USD '000	<i>Real Estate</i> USD '000	<i>Others</i> USD '000	<i>Total</i> USD '000
Funded					
Cash and bank balances	-	1,292	-	-	1,292
Due from financial institutions	-	16,850	-	-	16,850
Investments	24,273	28,833	33,802	22,080	108,988
Non-current assets held for sale	-	-	-	1,326	1,326
Fixed assets	-	-	-	1,086	1,086
Other assets	641	133	53	193	1,020
	24,914	47,108	33,855	24,685	130,562
Unfunded / commitments					
Investment commitments	-	379	-	11,406	11,785
Foreign Exchange commitments	-	478	-	-	478
Other Commitments	-	-	-	916	916
	-	857	-	12,322	13,179

Table 9 - Credit Risk - concentration of risk (PD 1.3.23(f))

The following table summarizes the disclosure for concentration of risk to individual counterparties or group of connected counterparties in excess of 15% of regulatory capital:

	<i>USD '000</i>	<i>% of total eligible capital</i>
Counterparty 1	18,482	17.13%

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Table 10 - Credit risk - Residual contractual maturity (own capital (PD 1.3.23 g))

The following table summarizes the residual contractual maturity of the Bank's own capital breakdown of the whole credit portfolio, broken down by major type of credit exposure:

	<i>Up to 1 month USD'000</i>	<i>1 to 3 months USD'000</i>	<i>3 to 6 months USD'000</i>	<i>6 months to 1 year USD'000</i>	<i>1 to 3 years USD'000</i>	<i>Over 3 years USD'000</i>	<i>No fixed Maturity USD'000</i>	<i>Total USD'000</i>
ASSETS								
Cash and bank balances	1,292	-	-	-	-	-	-	1,292
Due from financial institutions	8,850	7,500	-	-	-	-	500	16,850
Investments	107	6,299	331	681	1,660	4,837	95,073	108,988
Non-current assets held for sale	-	-	-	-	-	-	1,326	1,326
Other assets	251	300	469	-	-	-	-	1,020
Fixed assets	-	-	-	-	-	-	1,086	1,086
Total assets	10,500	14,099	800	681	1,660	4,837	97,985	130,562
LIABILITIES								
Due to financial institutions	2,000	13,000	2,350	-	-	-	-	17,350
Customers current accounts	318	338	-	-	-	-	-	656
Other liabilities	399	-	-	-	-	-	-	399
Equity	-	-	-	-	-	-	112,157	112,157
Total liabilities and equity	2,717	13,338	2,350	-	-	-	112,157	130,562

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Table 11 - Credit Risk - Impaired facilities and allowances (PD 1.3.23 (h and i))

	Own Capital							
	Ageing Past Due				Specific allowances			
	Less than 90 days USD'000	3 to 12 months USD'000	1 to 3 years USD'000	Over 3 years USD'000	Balance at the beginning of the period USD'000	Charges during the period USD'000	Charge off during the period USD'000	Balance at the end of the period USD'000
Impaired facilities USD'000								
2,000	-	-	2,000	-	1,500	-	-	1,500
4,346	-	-	-	4,346	3,694	652	-	4,346
1,065	-	-	-	1,065	781	-	-	781
4,900	-	-	4,900	-	1,709	916	-	2,625
4,123	-	-	4,123	-	1,647	281	-	1,928
16,434	-	-	11,023	5,411	9,331	1,849	-	11,180

Due from financial institutions (Bahrain)
 Unquoted equity shares (USA) (note below)
 Quoted equity securities (UK)
 Quoted equity securities (Bahrain)
 Unquoted equity securities (Bahrain)

Collective provisions represent provisions against exposures which, although not specifically identified, have a greater risk of default than when originally granted. As per management's assessment the amount of collective provision was increased during the period by USD 250 thousands making the total collective provision to USD 1,650 thousands as at 30 June 2011.

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Table 11 - Credit Risk - Specific allowances by industry and geographic sector (PD 1.3.23 (h and i)) continued

	Own Capital						
	Industry Sector			Geographic Sector			
	Banks and Financial institutions USD'000	Trading and Manufacturing USD'000	Real Estate USD'000	North America USD'000	Europe USD'000	GCC and other Middle East USD'000	Total USD'000
Due from financial institutions	1,500	-	-	-	-	1,500	1,500
Unquoted equity shares - International	-	4,346	-	4,346	-	-	4,346
Quoted equity securities - International	781	-	-	-	781	-	781
Quoted equity securities - Local	2,625	-	-	-	-	2,625	2,625
Unquoted equity securities - Local	1,366	562	-	-	-	1,928	1,928
	6,272	4,908	-	4,346	781	6,053	11,180

Credit Risk - Restructured islamic financing contracts (PD 1.3.23(j))

There were no restructured islamic financing contracts during the period ended 30 June 2011. However, one of the Bank's investment in unquoted Sukuk which was restructured during April 2010 have been fully provided for during the current period.

3.6 MARKET RISK

3.6.1 Introduction

The Group has adopted the definition of market risk as defined per CBB rulebook which is "the risk of losses in on- and off- balance sheet positions arising from movements in market prices".

3.6.2. Sources of market risk

For the Group, market risk may arise from movements in profit rates, foreign exchange markets or equity markets. A single transaction or financial product may be subject to any number of these risks.

Profit rate risk

Profit rate risk arises from the possibility that changes in profit rates will affect future profitability or the fair values of the financial instruments.

Foreign exchange risk

Foreign exchange risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The currency positions are monitored on daily basis to ensure positions are maintained within established limits.

Equity price risk

Equity price risk is the risk that the fair values of equities may decrease as a result of changes in the levels of equity indices and the value of individual equities.

3.6.3. Market risk strategy

The Group's Board is responsible for approving and reviewing the risk strategies and significant amendments to the risk policies and the senior management is responsible for implementing the risk strategy approved by the Board.

Inline with the Group's risk management objectives and risk tolerance levels, the specific strategies for market risk management include:

1. The Group manages its market risk exposure by evaluating each new product / activity with respect to the market risk associated with it;
2. The Group proactively measures and continually monitors the market risk in its portfolio;
3. The Group at all times holds sufficient capital in line with CBB Pillar 1 regulatory capital requirements;
4. The Group has established a market risk appetite which is quantified and established as market risk limit structure;
5. The Group has established a limit structure to monitor and control the market risk in its portfolio. These limits will include position limits, maximum / stop loss limits, factor sensitivity limits, VaR limits and maturity limits; and
6. The Group clearly identifies the foreign currencies in which it wishes to deal in and actively manage its market risk in all foreign currencies in which it has significant exposure.

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Table 12 - Market Risk capital requirements (PD 1.3.27 (b))

The following table summarizes the capital requirement for foreign exchange risk as of 30 June 2011:

	<i>Equity Price risk USD'000</i>	<i>Foreign exchange risk USD'000</i>	<i>Capital requirement 8%</i>
Equity price capital requirements	-	-	460*
Foreign exchange capital requirements	-	-	1,796*
Maximum value	6,458	22,933	-
Minimum value	5,756	22,455	-

* The capital requirement is as per the supplementary schedule to form PIRI.

3.7 Operational Risk

3.7.1 Introduction

Operational risk is the risk of loss arising from system failure, human error, fraud or external events. When controls fail to operate, operational risk can cause damage to reputation, have legal or regulatory implications, or lead to financial losses. The Group cannot expect to eliminate all operational risks, but through a control framework and by monitoring and responding to potential risks, the Group is able to manage these risks. Controls include effective segregation of duties, access, authorization and reconciliation procedures. Maker checker function and dual eye principles are applied across the Group, where applicable.

Table 13 - Equity position risk in banking book (PD 1.3.31 (b), (c) and (d))

	<i>Total Gross exposure USD'000</i>	<i>Average Gross exposure * USD'000</i>	<i>Publically traded USD'000</i>	<i>Risk weighted assets USD'000</i>	<i>Capital requirement 12% on RWA USD'000</i>
Equity investments	117,262	108,998	6,083	191,647	22,998
Sukuks **	4,837	8,407	3,207	7,683	922
Total	122,099	117,405	9,290	199,330	23,920

* Average balances are computed on month end balances

** Sukuks are considered as tradeable based on bid offer quotes in Bloomberg

Table 14 - Equity gains or losses in banking book (PD 1.3.31 (d) and (e))

	USD'000
Cumulative realized loss arising from sales or liquidations in the reporting period	-
Cumulative realized gain arising from sales or liquidations in the reporting period	46
Total unrealized losses recognized in the balance sheet but not through statement of income	2,235
Total unrealized gains recognized in the balance sheet but not through statement of income	364
Total unrealized losses included in Tier 1 capital	2,235
Total unrealized gains included in Tier 1 capital	3,168
Unrealized gains included in Tier 2 capital	164

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3.8 Liquidity risk

Liquidity risk is the risk that an institution will be unable to meet its funding requirements. Liquidity risk can be caused by market disruptions or credit downgrades which may cause certain sources of funding to cease immediately. To guard against this risk, the Group is targeting to build a large customer base with sound credit standing and assets are managed with liquidity in mind, maintaining a healthy balance of cash, cash equivalents, and commodity murabaha. Liquidity position is monitored on an ongoing basis by the Group's Asset Liability Committee ("ALCO") and is also compared to the limits set by the Group's Board. All exceptions are reported for adequate corrective actions.

Table 15 - Liquidity ratios (PD 1.3.37)

The following table summarizes the liquidity ratios:

	30-Jun-11	2010	2009	2008	2007
Short term assets less than 1 Year / Short term Liability less than 1 Year	1.59	1.33	2.00	5.88	1.00
Commodities Murabaha / Total assets	0.01%	10.04%	2.71%	23.60%	23.09%
Liquid Assets / Total Assets	13.90%	24.16%	8.72%	36.36%	31.14%
Liquid Assets / Total Assets	18.55%	32.91%	28.18%	38.73%	31.74%

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Table 16 - Maturity analysis of assets and liabilities and equity (PD 1.3.38)

The table below shows an analysis of assets, liabilities and equity analyzed according to when they are expected to be recovered or settled:

	<i>Up to 1 month USD'000</i>	<i>1 to 3 months USD'000</i>	<i>3 to 6 months USD'000</i>	<i>6 months to 1 year USD'000</i>	<i>1 to 3 years USD'000</i>	<i>Over 3 years USD'000</i>	<i>Total USD'000</i>
ASSETS							
Cash and bank balances	1,292	-	-	-	-	-	1,292
Due from financial institutions	8,850	7,500	-	-	-	500	16,850
Investments	107	6,299	331	2,481	86,377	13,393	108,988
Non-current assets held for sale	-	-	-	1,326	-	-	1,326
Fixed assets	-	-	-	-	-	1,086	1,086
Other assets	251	300	469	-	-	-	1,020
Total assets	10,500	14,099	800	3,807	86,377	14,979	130,562
LIABILITIES AND EQUITY							
Due to financial institutions	7,500	7,500	2,350	-	-	-	17,350
Customers current accounts	318	338	-	-	-	-	656
Other liabilities	399	-	-	-	-	-	399
Equity	-	-	-	-	-	112,157	112,157
Total liabilities and equity	8,217	7,838	2,350	-	-	112,157	130,562
Liquidity gap	2,283	6,261	(1,550)	3,807	86,377	(97,178)	-
Cumulative liquidity gap	2,283	8,544	6,994	10,801	97,178	-	-

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3.9 Profit rate risk

Profit rate risk is the potential impact of the mismatch between the rate of return on assets and the expected rate of funding due to the sources of finance (e.g. deposits etc.)

Senior management identifies the source of profit rate risk exposures based upon the current as well as forecasted statement of financial position structure of the Group. The profit rate risk may arise due to transactions relating to Murabaha, mudaraba, wakala and investment in Sukuks.

The management believe that the Group is not exposed to any significant profit rate risk as a result of mismatches of profit rate repricing of assets and liabilities as the repricing of assets and liabilities occur at similar intervals.

Table 17 - Profit rate risk in Banking book (PD 1.3.40 (b))

The following table summarizes the effect on the value of assets, liabilities and economic capital for a benchmark change of 200 basis point in profit rates:

	<i>Balances as at 30 June 2011 USD'000</i>	<i>Effect on value of asset and income USD'000</i>	<i>Effect on value of liability and expense USD'000</i>	<i>Effect on value of economic capital and net income USD'000</i>
Rate sensitive assets				
Due from financial institutions (inter bank profit rates)	16,850	337	-	
Rate sensitive liabilities				
Due to financial institutions (interbank profit rates)	(17,350)	-	(347)	
Net upward rate shocks on Rate sensitive assets & liabilities	(500)	337	(347)	(10)
Net downward rate shocks on Rate sensitive assets & liabilities	(500)	(337)	347	10

The others assets and liabilities are not rate sensitive

Table 18 - Quantitative indicators of Financial Performance and position (PD 1.3.9 (b))

	30-Jun-11*	2010	2009	2008	2007
Return on average equity	(10.26%)	(9.94%)	1.08%	27.71%	11.81%
Return on average assets	(8.43%)	(6.55%)	0.75%	12.26%	7.20%
Cost to Income ratio	(99.29%)	482.41%	57.97%	31.01%	44.56%

*Percentages are annualised on the basis of half yearly results.

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Table 19 - Disclosures for exposures related to counterparty credit risk

General Disclosure (PD-1.3.26 (b))

<i>Current credit exposure by types of islamic financing contracts</i>	<i>Gross positive fair value USD'000</i>	<i>Netting benefit USD'000</i>	<i>Netted current credit exposure USD'000</i>	<i>Eligible collaterals held USD'000</i>
Commodity Murabaha receivables	500	-	500	-
Musharka receivables	2,995	-	2,995	-
Mudaraba receivables	16,350	-	16,350	-

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4 Unrestricted Investment Accounts (PD 1.3.32 & PD 1.3.33)

The CBB upgraded the Bank's license from 'Investment Firm - Category 1 license' to 'Wholesale Islamic Investment Bank License' on 7 October 2009. Under its previous license, The Bank did not offer any Unrestricted Investment account product in accordance with the Investment Firm license and intends to structure Unrestricted Investment products.

CBB requires the Group to maintain capital to cover the price risk arising from 30% of the assets funded by Unrestricted Investment Accounts (URIA) on a pro-rata basis. As at 30 June 2011 the Bank has no exposure under this requirement.

The Group is currently in the process of developing written policies and procedures applicable to Unrestricted Investment Accounts. URIA funds are intended to be invested and managed in accordance with Shari'a requirements.

5 Restricted Investment accounts ("RIA") (PD 1.3.34)

The Bank holds Investments of portfolio customers under fiduciary relationship and thus RIA assets and liabilities, are held Off- Balance sheet and separate portfolio accounts are maintained for each client. The Bank currently holds only custody accounts and performs only custodian duties.

Although the underlying investments are held in the name of the Bank, these assets are not consolidated in the Group's financial statements. During the period ended 30 June 2011 the management received an amount of USD 3,000 as mudarib fee from restricted investment.

6 Investment in foreign subsidiaries (PD 1.3.42)

The Group has a foreign subsidiary incorporated in Cayman Island with share capital of USD 50,000. During the period there has been no change in the Group's holding in the above mentioned investment. The other subsidiaries of the Group are incorporated in Bahrain. Refer note-2 of the interim condensed consolidated financial statements for six-month period ended 30 June 2011.