

TAIB Bank B.S.C (c)

Pillar 3 - Market Discipline

Disclosures

30 June 2008

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1 Introduction

The Basel II frame work (“frame work”)developed by the Basel Committee on Banking Supervision (Basel Committee) seeks to improve the existing capital adequacy rules by aligning regulatory capital requirements more closely to the underlying risks that banks face, or may face.

The legislative framework, under the Basel II, governing how much capital the banks in Bahrain must hold to protect their members, depositors, shareholders, was introduced by Central Bank of Bahrain (“CBB”) for all banks licensed in the Kingdom of Bahrain with effect from 1 January 2008.

The CBB guidelines are in consistent with the framework and guideline developed by the Basel Committee and is based on the following three pillars.

Basel II framework		
Pillar 1	Pillar 2	Pillar 3
Minimum Capital Requirements	Supervisory Review Process, including the Internal Capital Adequacy Assessment Process (ICAAP).	Market Discipline

Each bank, under CBB’s Basel II frame work, is required to be individually assessed by the CBB and an individual minimum Capital Adequacy Ratio is to be determined for each bank. The new Capital Adequacy Module of the CBB Rule provides a more risk sensitive approach to the assessment of risk and the calculation of regulatory capital, i.e. the minimum capital that a bank is required to maintain.

Since the first quarter of 2007, TAIB Bank B.S.C (c) (“the Bank” or “the Group”) has routinely been monitoring capital adequacy for internal capital management purposes based on the Basel II Standardized Approach. This report encompasses the Pillar 3 disclosure requirements prescribed by CBB based on the Basel Committee’s Pillar 3 guidelines as at 30 June 2008.

All figures presented in this report are in thousands of United States Dollars as at 30 June 2008 unless otherwise stated.

1.1 Pillar 1

Pillar 1 prescribes the basis for the calculation of the regulatory Capital Adequacy Ratio. Credit Risk and Market Risk are two essential risk types that were included under Basel I, while Operational Risk was introduced as a new risk type in the CBB’s Basel II capital adequacy framework.

The table below summarises the approaches available for calculating Risk Weighted Assets (RWA) for each risk type in accordance with the framework:-

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 approaches followed by TAIB for calculation of each risk type are:

- 1) **Credit Risk:** The Bank uses Standardised Approach for calculation of Credit Risk. The standardised approach relies on credit ratings of borrowers assigned by external credit assessment institutions” (ECAIs). TAIB is currently using International rating (Fitch, S&P, Moody’s) rating to compute banks regulatory capital 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 ratings, where available. This RWA is reduced by the Credit Risk Mitigant (CRM) if any, to arrive at the net exposure.
- 2) **Market Risk:** The Group uses the standardised approach for exposures in the Bank’s trading book to measure the market risk capital charge to cover interest rate risk, equity risk and foreign exchange risk. Total risk weighted assets are determined by multiplying the capital charge arrived above by 12.5
- 3) **Operational Risk:** Bank uses the standardised approach for calculating operational risk capital charges. In this approach, bank’s activities are divided into eight business lines. The capital charge for each business line is calculated by multiplying gross income by a factor (denoted by beta) assigned to that business line. Total risk weighted assets are determined by multiplying the capital charged arrived by 12.5. The bank has obtained the necessary approvals to use the above approach.

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 CBB’s Basel II frame work, each bank is required to be individually assessed by the CBB and an individual minimum capital adequacy ratio is to be determined for each bank. The CBB is currently undertaking the assessment exercises for all banks including TAIB through approved external specialists in order to determine minimum capital ratios in excess of 8.5 per cent, based on the 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 continue to maintain a 12 per cent minimum Capital Adequacy Ratio as under the previous Basel 1 framework.

Pillar 2 comprises two processes:

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

The ICAAP incorporates a review and evaluation of risk management and capital relative to the risks to which the bank is exposed.

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 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

The objective of Pillar 3 is to improve market discipline through effective public disclosures to complement requirements under Pillar 1 and Pillar 2. It introduces substantial new public disclosure requirements and represents a significant increase in the amount of information made publicly available by the banks around capital structure, capital adequacy, risk management and risk measurement.

The CBB's Basel 2 framework has prescribed partial disclosure consisting of mainly quantitative analysis during the half year reporting (period ended 30 June 2008), where as fuller disclosure is required to coincide with the financial year end reporting.

The following sections of this report provide minimum regulatory requirements and disclosures in accordance with Public Disclosure Module of the CBB's rule book. .

2 Pillar 3 Disclosures

2.1 Table 1 – Group Structure

Subsidiary	Domicile	Ownership
Everest Fund	Luxembourg	64%
TAIB Income Fund	British Virgin Islands	92%
Golden Horn Fund	British Virgin Islands	81%
TAIB Explorer Fund	Cayman Islands	59%
TAIB GCC Blue Chip Fund	Kingdom of Bahrain	90%
TAIB Yatirim Bank A.S	Turkey	100%
PDF Corporate Finance	Turkey	100%
TAIB Kazak Bank	Kazakhstan	100%
TAIB Yatirim A.S	Turkey	100%
TAIB Securities W.L.L	Kingdom of Bahrain	100%
TAIB Capital Corporation Limited	India	74%
TAIB Securities (India) Limited	India	74%
TAIB Asset Management Company E.C	Kingdom of Bahrain	100%
TAIB Securities Maturities Limited	Mauritius	100%
TAIB Investments N.V	Netherlands Antilles	100%
TAIB Securities Limited	United Kingdom	100%
TAIB (Suisse) S.A	Switzerland	100%
TAIB Asia Limited	Hong Kong	100%
TAIB Securities Inc	USA	100%
TAIB Invest Inc.	Cayman Islands	100%
TAIB Bank Qatar LLC	Qatar	100%
TAIB Securities LLC	United Arab Emirates	80%
TAIB Investment Company Ltd	Mauritius	100%
TAM Holding Inc	USA	100%
Delray Property Investments Inc	USA	100%
SOSQ Property Investments Inc	USA	100%

2.2 Table 2 – Capital Structure

	Tier 1	Tier 2	Total
Share Capital	107,205	-	107,205
Share Premium	1,623	-	1,623
Statutory Reserve	22,953	-	22,953
General Reserve	6,714	-	6,714
Retained profit brought forward	46,932	-	46,932
Minority Interest in consolidated subsidiaries	1,778	-	1,778
Goodwill on acquisition	(5,632)	-	(5,632)
Current interim cumulative net losses	(6,015)	-	(6,015)
Unrealised gross losses arising from fair valuing equity securities	(2,170)	-	(2,170)
Asset revaluation reserve - Property, plant & equipment	-	5,885	5,885
Unrealised gains arising from fair valuing equities	-	1,157	1,157
Total	173,388	7,042	180,430
Consolidated Capital Adequacy Ratio (%):			
	Tier 1		27.0
	Total		28.1

The Bank does not have Tier 3 capital as at 30 June 2008.

2.3 Table 3 – Top Consolidated group in Bahrain

	Tier 1	Tier 2	Total
Share Capital	109,460	-	109,460
Share Premium	1,623	-	1,623
Statutory Reserve	21,016	-	21,016
General Reserve	6,879	-	6,879
Retained profit brought forward	14,078	-	14,078
Current interim cumulative net losses	(5,438)	-	(5,438)
Unrealised gross losses arising from fair valuing equity securities	(1,930)	-	(1,930)
Asset Revaluation Reserve - Property, plant ,equipment	-	5,328	5,328
Unrealised gains arising from fair valuing equities	-	1,065	1,065
Available capital	145,688	6,393	152,081
Less: Deductions from Capital			(97,695)
Regulatory Capital			54,386
Total Risk Weighted Assets			404,802
Capital Adequacy Ratio (%)			13.44

2.4 Table 4 – Capital Adequacy Ratio

Subsidiaries

	TAIB Kazak Bank JSE, Kazakhstan	TAIB Yatirim Bank A.S, Turkey
Tier 1 – Capital Adequacy Ratio (%)	125.57	308.08
Total – Capital Adequacy Ratio (%)	126.83	209.57

CAR of TAIB Yatirim Bank, Turkey is reported under Basel 1

2.5 Table 5 – Capital requirement for Credit Risk

Asset Classification	Rated	Unrated	Total Exposure	Average risk weight	RWA	Capital charge
Claims on Sovereigns	18,318	515	18,833	3%	515	62
Claims on Banks	180,759	36,937	217,696	34%	73,068	8,768
Claims on Corporates	1,100	45,504	46,604	98%	45,729	5,487
Investment in equity portfolio	-	3,985	3,985	111%	4,417	530
Investment in Funds	-	26,345	26,345	145%	38,143	4,577
Holding of Real Estate including premises occupied by the bank	-	115,514	115,514	190%	219,786	26,374
Underwriting of Non-trading book items	-	38,010	38,010	100%	38,010	4,561
Others Assets	-	24,651	24,651	100%	24,651	2,958
Total Credit Risk under Standardised Approach	200,177	291,461	491,638	90%	444,318	53,318

2.6 Table 6 – Gross Credit Exposure

Balance sheet Items:	Gross credit exposure	Average Gross credit exposure
Cash and balances with central banks	63,854	63,578
Placements with banks	160,798	152,035
Loans and advances	18,182	18,439
Available-for-sale financial assets	136,662	110,403
Investment in associate	11,467	9,822
Investment property	42,725	51,696
Property and equipment	17,357	20,638
Other assets	13,549	16,115
Total On balance sheet credit exposure	464,594	442,726
Off balance sheet items:		
Direct credit substitutes	14,946	11,344
Notes Issuance and Revolving Underwriting Facilities	12,350	13,208
Derivative - Foreign exchange contracts	1,126	750
Total Off balance sheet credit exposure	28,422	25,301
Total credit exposure	493,016	468,027

The average gross credit exposure is calculated based on balances as at 31 December 2007, March 2008 and 30 June 2008. 31

2.7 Table 7 – Credit Exposure by Geographical segments

Credit Exposure	North America	Europe	Middle East	Rest of Asia	Total
Cash and balances with central banks	810	3,929	42,672	16,445	63,856
Placements with banks	27,858	75,498	48,377	9,064	160,797
Loans and advances	18	539	14,113	3,512	18,182
Available-for-sale financial assets	30,596	77,486	474	28,106	136,662
Investment in associate	-	11,467	-	-	11,467
Investment property	24,941	-	16,909	875	42,725
Property and equipment	317	1,314	14,379	1,346	17,356
Other assets	5,828	1,010	6,028	682	13,548
Off Balance sheet items	1,126	12,390	13,615	1,292	28,423
Total	91,494	183,633	156,567	61,322	493,016

Exposure to Europe comprises of Cayman Islands, Cyprus, Guernsey, Luxembourg, Netherlands, Turkey, United Kingdom and British Virgin Islands

Exposure to North America comprises of Bahamas & United States of America

Exposure to Rest of Asia comprises of China, India, Mauritius and Thailand

2.8 Table 8 – Credit Exposure by Sectoral segments

	Cash, Balances with Central Banks & placements	Loans & advances	Investment	Other assets	Off-Balance Sheet Items	Total
Financial Services	224,064	133	388	17,354	16,033	257,972
Government	591	-	-	-	-	591
Structured Finance	-	-	18,242	-	-	18,242
Energy	-	-	771	-	-	771
Trade & Transport	-	3,370	177	-	-	3,547
Real Estate	-	-	142,282	-	12,390	154,672
Equity Funds	-	-	26,534	-	-	26,534
Others	-	14,678	2,461	13,548	-	30,687
Total	224,655	18,182	190,855	30,902	28,423	493,016

2.9 Table 9 – Credit Exposure by Maturity

	below 1 month	1 to 3 months	3 to 12 months	1 to 5 Years	5 to 10 Years	10 to 20 Years	Over 20 Years	Total
Exposures								
Cash and balances with central banks	63,857	-	-	-	-	-	-	63,857
Placements with banks	155,493	5,305	-	-	-	-	-	160,798
Loans and advances	9,875	2,719	5,588	-	-	-	-	18,182
Available-for-sale financial assets	-	62,169	58,267	16,227	-	-	-	136,663
Investment in associate	-	-	-	-	11,467	-	-	11,467
Investment property	8,000	-	-	24,941	875	-	8,909	42,725
Property and equipment	-	133	-	4,891	419	-	11,911	17,354
Other assets	3,128	4,709	4,107	1,604	-	-	-	13,548
Total	240,353	75,035	67,962	47,663	12,761	-	20,820	464,594

2.10 Table 10 – Provision for investments- Sectoral segments

	Property interest held for sale- Equity	Private Equity	Total
At 1 January 2008	4,769	6,282	11,051
Charge for the period	1,394	863	2,257
Amounts utilised	(220)	-	(220)
Exchange rate movement	(45)	-	(45)
At 30 June 2008	5,898	7,145	13,043

2.11 Table 11 – Provision for investments and related exposures

	Gross exposure	Provisions	Net Exposure
Property interests held for sale - equity	6,163	6,163	-
Private equity investments	6,880	6,880	-
Total	13,043	13,043	-

2.12 Table 12 – Provision for investments and related exposure - Geographical segments

	North America	Europe	Middle East	Rest of Asia	Total
Exposure	5,902	4,769	355	2,017	13,043
Specific impairment provision	5,902	4,769	355	2,017	13,043

Bank does not have any collective impairment provision at 30 June 2008.

2.13 Table 13 – Provision for loans and advances- Sectoral segments

	Impaired loans	Specific provision
Financial Services	4,953	4,820
Trade	1,286	-
Corporate	4,625	4,625
Total	10,864	9,445

No provision has been made on impaired loans amounting to US\$ 1.2 million as the Bank holds cash collateral.

Impaired loans are past due over 3 years.

2.14 Table 14 – Provisions for loans and advances - Geographical segments

	North America	Europe	Middle East	Rest of Asia	Total
Exposure	1,802	3,887	1,988	3,187	10,864
Specific impairment provision	1,725	3,848	702	3,170	9,445

2.15 Table 15 – Provision for loans and advances - Sectoral segments

	Financial Institutions	Corporates	Total
At 1 January 2008	4,820	4,630	9,450
Other Movements	-	(5)	(5)
At 30 June 2008	4,820	4,625	9,445

2.16 Table 16 – Counterparty Credit Risk in derivative transaction

	Notional amount	Credit Exposure	Capital Requirement
Direct Credit Substitutes	14,947	14,947	1,794
Notes Issuance and Revolving Underwriting Facilities	24,699	12,349	1,482
Total	39,646	27,296	3,276

2.17 Table 17 – Capital requirement for components of Market Risk

	RWA	Capital requirement	Maximum Value	Minimum Value
Interest rate position risk	595	48	48	32
Equities position risk	22,526	1,802	2,482	1,802
Foreign exchange risk	81,162	6,493	6,511	6,493
Total general market risk	104,283	8,343	9,025	8,343
Total specific market risk	5,926	474	474	340
Total	110,209	8,817	9,499	8,683

2.18 Table 18 – Interest Rate Risk

Assets	Less than 3 months	3 months to 1 Year	Over 1 Year	Non-Interest bearing	Total
Cash and balances with central banks	63,857	-	-	-	63,857
Placements with banks	160,798	-	-	-	160,798
Financial Assets at Fair value	7,370	3,923	-	17,160	28,453
Loans and advances	12,593	5,588	-	-	18,181
Available-for-sale financial assets	58,971	21,150	10,650	47,304	138,075
Investment in associate	-	-	-	11,467	11,467
Investment property	-	-	-	43,379	43,379
Property and equipment	-	-	-	23,895	23,895
Goodwill	-	-	-	11,934	11,934
Other assets	-	-	-	7,246	7,246
Total	303,589	30,661	10,650	162,385	507,285
Liabilities					
Deposits from Banks	93,902	5,000	-	367	99,269
Deposit from Customers	45,832	20,123	1,108	104,546	171,609
Securities Sold under REPO	988	-	-	-	988
Other liabilities	-	-	-	28,573	28,573
Long term debt	-	-	6,389	-	6,389
Total	140,722	25,123	7,497	133,486	306,828
Interest rate sensitivity gap	162,867	5,538	3,153		
Cumulative Interest rate	162,867	168,405	171,558		

2.19 Table 19 – Sensitivity analysis – Interest Rate Risk

Annualised	Up to 3 Months	3 Months to 1 Year	Over 1 Year	Total
at 50 bps increase	814	28	16	858
at 100 bps increase	1,629	55	32	1,716
at 200 bps increase	3,257	111	63	3,431

2.20 Table 20 – Capital requirement for Operation Risk

	2005	2006	2007
Gross Income	43,634	49,402	44,694
Capital charge	7,033	7,269	6,716
Average of capital charges for 3 years			7,006
Operational Risk Weighted Exposure			87,573

2.21 Table 21 – Credit concentration greater than 15%

	Amount
Total exposure in excess of 15 % individual obligor limit	NIL

2.22 Table 22 – Equity position in banking books

	Gross risk-weighted exposures	Capital requirement
Listed	3,121	375
Unlisted	864	104
Total	3,985	479

2.23 Table 23 – Unrealised gains and losses

	Amount	
Total unrealized gains and losses recognised in the balance sheet but not through the P&L		
Fair value reserve (net)		401
Unrealised gains and losses included in Tier One and Tier Two capital		
	Tier 1	Tier 2
Fair Value reserve:		
Unrealized gross losses arising from fair valuing equity securities	2,170	
Unrealized gains arising from fair valuing equities		1,157
Asset revaluation reserve:		
Property, plant, and equipment		5,885

2.24 Table 24 – Related party transaction

	Associates	Directors & Senior Management	Total
Deposits with the banks	6,022	8,122	14,144
Interest Income	245	-	245
Interest Expense	22	234	256
Fee & Commission Income	750	-	750
Key management compensation	-	6,150	6,150
Total	7,039	14,506	21,545

2.25 Credit Risk Mitigant (CRM):

Bank is currently in the process of implementing the new Basel II software which will cater to its CRM requirements. This implementation is expected to be completed by the end of year 2008.

2.26 Discussion on impact of acquisition:

On 25 March 2008, TAIB Yatirim Menkul Degerler A.S (Subsidiary of the Bank) has acquired 100% controlling stake in PDF Kurusmal Finasman Danismanlik Hizmetleri A.S (the “entity” or “PDF”). PDF is a corporate finance company specialized in providing financial advisory services to Turkish and international clients. The assets and liabilities as at 30 June 2008 and the results of the operations of the entity for the three months ended 30 June 2008 has been included in these interim condensed consolidated financial information.

As at 30 June 2008, the Group is in the process of assessing the fair values of the acquired entity’s tangible and intangible assets, liabilities and contingent liabilities. The acquired entity has been consolidated with effect from the date of acquisition and the excess of consideration over the book value of the net tangible assets acquired amounting to US\$ 5.4 million has been recorded as goodwill in these interim condensed consolidated balance sheet.

The carrying value of assets and liabilities acquired are as follows:

	<i>US\$</i>
Property and equipment	7,325
Other assets	100,347
Intangible assets	247
Other liabilities	<u>(443,462)</u>
Total assets and liabilities acquired	(335,543)
Purchase consideration settled in cash and equity shares of the parent	<u>5,100,000</u>
Goodwill on acquisition	<u>5,435,543</u>

The acquired business of PDF contributed revenues of US\$ 1.7 million and net profit of US\$ 1.4 million to the group for the period from acquisition date to 30 June 2008.

2.27 Discussion on changes in the capital structure:

The shareholders of the Bank and the regulatory authorities have accorded approval for an increase in the paid up capital of the Bank to US\$ 250 million. The processes for such increase are under internal examination and review.

2.28 Discussion on lending to highly leveraged and other high risk counterparties:

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