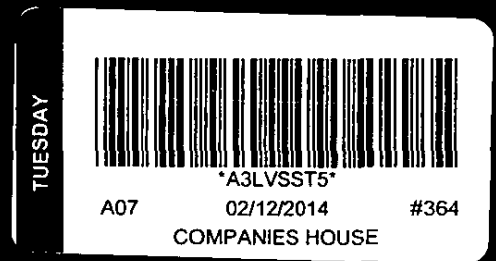


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Gulf International Bank

Annual Report and Accounts 2000



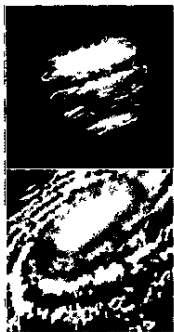
GIB
بنك الخليج الدولي

This year's GIB annual report draws inspiration from the cosmos, where inter-planetary forms, energy and movement combine to bring about dynamic synergy and strength.

The integration of Gulf International Bank and Gulf International Bank (UK) Limited has created a diverse financial services group offering customers a spectrum of wholesale commercial and investment banking services. "The new GIB" represents a new order, expanding into new territories, offering a wider range of products and services, and creating the capability and space for new opportunities.

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Gulf International Bank is a wholesale commercial and investment bank based in Bahrain. It is majority owned by Gulf Investment Corporation (GIC) [the international investment banking corporation owned equally by the governments of the six member states of the Gulf Cooperation Council (GCC) – Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and United Arab Emirates], the Saudi Arabian Monetary Agency (SAMA) and J.P. Morgan Overseas Capital Corporation.

The Bank's primary focus is on the GCC market and the associated trade and financial flows between this region and the rest of the world. Target clients include major indigenous private-sector corporations, Gulf-based financial institutions, multinational companies active in the region and the governments of the GCC states themselves. Its subsidiary, Gulf International Bank (UK) Limited, branches in Riyadh, London and New York and representative offices in Abu Dhabi, Beirut and Singapore assist in servicing this client base. GCC market knowledge, expertise in its industries, extensive product skills, international reach and a commitment to excellence are distinguishing features of the Bank.

Financial Highlights

	2000	1999	1998*
Earnings (US\$ millions)			
Net Income after Tax	118.1	67.6	82.1
Net Interest Revenue	169.7	139.6	115.3
Other Income	127.3	77.4	49.2
Operating Expenses	132.3	109.9	52.9
Financial Position (US\$ millions)			
Total Assets	15,119.5	15,679.4	10,209.0
Loans	3,923.1	4,038.0	4,000.7
Trading Securities	465.8	535.8	139.6
Investment Securities	7,062.1	5,451.4	3,229.6
Shareholders' Equity	1,205.8	1,137.7	731.0
Ratios (%)			
Profitability			
Return on Average Shareholders' Equity	10.1	6.5	11.2
Return on Average Assets	0.8	0.5	0.8
Capital			
BIS Risk Asset Ratio			
- Total	11.5	12.2	11.9
- Tier 1	10.2	10.9	10.7
Shareholders' Equity as % of Total Assets	8.0	7.3	7.2
Loans as a multiple of Equity (times)	3.3	3.5	5.5
Asset Quality			
Loans as % of Total Assets	25.9	25.8	39.2
Securities as % of Total Assets	49.8	38.2	33.0
GCC Country Risk as % of Total Assets	26.9	24.4	34.0
GCC & OECD Country Risk as % of Total Assets	91.6	92.6	86.6
Liquidity			
Liquid Assets Ratio	71.0	71.3	59.1
Deposits to Loans Cover (times)**	3.1	3.0	2.2
Long-Term Debt Ratings			
Fitch IBCA	BBB+	—	—
Moody's	Baa2	Baa2	Baa2
Standard & Poor's	BBB+	BBB+	BBB+

* GIB only (Prior to acquisition of GIBUK)

** Deposits include Term Financing

Net Income After Tax US\$ millions	2000	118.1
	1999	67.6
	1998	82.1
	1997	86.4
	1996	94.5

Total Assets US\$ millions	2000	15,120
	1999	15,679
	1998	10,209
	1997	9,524
	1996	8,983

Shareholders' Equity US\$ millions	2000	1,206
	1999	1,138
	1998	731
	1997	694
	1996	653



GIB unveiled its new corporate identity during 2000.

H.E. Abdulla H. Saif

Chairman

Minister of Finance & National Economy
State of Bahrain

Dr. Khaled Al-Fayez

Vice Chairman

Chief Executive Officer
Gulf Investment Corporation
State of Kuwait

Bader Abdullah Al-Rushaid Al-Bader *

Ex-Chairman & Managing Director
Kuwait Investment Company
State of Kuwait

Mohammed Bin Salf Al Shamsi *

Industrial Property Directorate
Ministry of Finance & Industry
United Arab Emirates

Saker Dhafer Al-Moraikhi

Consultant
Office of the Minister
Ministry of Finance, Economy & Commerce
State of Qatar

Dr. Yahya A. M. Al-Yahya

Advisor
The Governor's Office
Saudi Arabian Monetary Agency
Kingdom of Saudi Arabia

Dr. Hamad S Al-Bazai *

Deputy Minister for Economic Affairs
Ministry of Finance
& National Economy
Kingdom of Saudi Arabia

Rashid Ismaeel Al-Meer *

Assistant Under-Secretary for
Financial Affairs
Ministry of Finance & National Economy
State of Bahrain

Saud Nassir Al-Shukailly

Acting Director General of
Revenue & Investments
Ministry of Finance
Sultanate of Oman

Robert J McGinn

Managing Director
J P Morgan Overseas Capital Corporation
United Kingdom

* Audit Committee Members

On behalf of the Board of Directors, I am pleased to present the twenty-fourth annual report of Gulf International Bank B.S.C. (GIB) for the year ended 31st December 2000.

In my report last year I spoke of our objective of fully integrating the renamed Gulf International Bank (UK) Limited (GIBUK) so as to create "a bank that feels, acts and looks as one bank". In fact, this integration and the formalisation of the organisation structure across the GIB network has resulted in a successful synthesis of people and skills and provided our customer base with access to more products and services. In addition, certain senior management personnel from Bahrain have taken positions of responsibility in London, and certain London-based executives have assumed group-wide functions. Also, commercial banking has substantially been transferred from GIBUK to Bahrain and the branches. It is pleasing to note that referrals across all business units have been very satisfactory. This has significantly reinforced our stated long-term aim of being the leader in commercial and

investment banking in the Arab world, as well as a major Gulf and international financial institution. We will continue to re-evaluate our existing strategy and to proactively respond to changes in the environment where we conduct our business activities. We will also continue to pursue our objectives through the identification of suitable strategic alliances and the creation of more opportunities for expansion in our product range.

Financially and operationally, 2000 constituted a period of solid achievement for GIB. The year saw significant positive developments in virtually every sector of the Bank's activities. The first full year's contribution from GIBUK assisted in no small way towards a 74.7 per cent increase in the group's profits to a record US\$118.1 million. Importantly, the improvement in the financial

Abdulla H. Saif
Chairman



performance was accomplished with an enhanced return on equity whilst containing balance sheet growth. Shareholders' equity increased to US\$1,205.8 million. Both ongoing interest and non-interest earnings displayed a marked improvement. Trading revenue showed growth against prevailing weak market trends, primarily due to the continued implementation of sophisticated and disciplined risk management techniques. These excellent financial results – along with complementary and well-reasoned operational advances in many sectors – provide the Bank with an adequate base for further growth.

In this context, the opening of our branch in Riyadh, Saudi Arabia, constituted a milestone for the Bank. It places GIB in a key GCC onshore market, and introduces new customers to the spectrum of our wholesale commercial and investment banking services. The Bank is now represented in six countries and territories as well as Bahrain, which is significant when seen alongside our increasingly frequent role as a preferred partner

for international banks in high profile regional projects.

The Bank's improved regional presence was also enhanced by the restructuring of the Bank's activities. This has successfully provided the Bank with the ideal foundation to capitalise on strong core business activities in the Gulf, whilst making GIB's skills and expertise accessible to a wider audience interested in project and corporate finance, Islamic banking, trade finance and the syndication market. Our enhanced product mix places the Bank in a strong position to benefit from continuing penetration of the GCC market, and to build wider customer relationships.

This comprehensive range of services, and GIB's commitment to flexibility and co-operation, has seen the Bank involved in numerous major undertakings during 2000, in the capacity of either lead arranger or lead underwriter. GIB took a leading role in financing arrangements for several Gulf-based banks, in addition to being

a key player in deals for major GCC infrastructural investments. Our participation in large international projects underlines the Bank's premier position in key regional transactions, and also confirms our role as a significant driving force in the GCC's economic development. GIB is widely acknowledged as the area's prime financial 'facilitator' and economic 'enabler'.

Indeed, the Bank is strategically positioned to benefit from its efforts to create a premier Gulf Bank, amidst an economic environment offering an array of opportunities. The strengthening in oil prices has allowed the regional economies to sustain positive growth and encouraged the GCC governments to take the necessary steps to implement their privatisation programmes. Overall, economic policy remains aimed at making the private sector the main driver of economic growth, as an increasing number of parastatal organisations undergo restructuring. In this regard, the growing participation of the private sector in numerous


capital projects is testimony to the policy's success, while there is also a growing convergence of family-owned businesses into shareholding companies. Against this backdrop, the span of business prospects available to GIB is both broad and varied.

Internally, areas for improvement have been identified and relevant strategies put into place. The Bank's focus on a change-driven culture is demonstrated by an increased commitment to staff recruitment and training, exchange programmes and career development. Management fully realises that trained, qualified people are the Bank's key assets, and that efficient, 'user-friendly' and secure systems constitute a vital bridge between GIB's customers and our expertise and services.

This determination to create a solid ground for continued growth through a larger capital base, a strong and liquid asset profile and enhanced risk management techniques has seen a reaffirmation of our investment grade credit ratings by all three international rating agencies. Such continued confidence reinforces our belief in the importance of correct strategic choices, professionally timed and executed.

Finally, it remains for me to thank both the Board for their support, experience and cumulative expertise, and GIB's dedicated management and staff for their continued hard work. Teamwork is the cornerstone of commercial success in a competitive climate, and the Bank is fortunate to possess a blend of management with the ability to introduce opportune strategic initiatives, and competent people to implement them efficiently.

It has proved to be a memorable 2000 for GIB, and the Bank is firmly positioned to achieve continued growth in 2001 and beyond. This platform for sustained progress provides the Bank with the potential to further extend its range of activities, customer relationships and influence both within the GCC and well beyond.



Abdulla H. Saif
Chairman

GIB Corporate and Institutional Banking

GIB Assets and Liabilities Management and GIB Financial Markets

GIB Investment Banking

GIB Asset Management

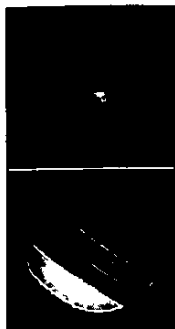
In order to mobilise staff expertise, technological resources and operational efficiency to the maximum, the Bank's operations have been divided into five mutually supportive and streamlined business units: GIB Corporate and Institutional Banking, GIB Assets and Liabilities Management, GIB Financial Markets, GIB Investment Banking and GIB Asset Management. As this is the first year of this operational structure, the responsibilities and services offered by each unit are detailed in the following pages, along with their respective achievements during the year.

The year 2000 constituted another significant year for Gulf International Bank as it continued to further improve and diversify its product range and enhance service levels in order to meet the evolving requirements of a steadily increasing client base. Headquartered in Bahrain, with branch offices in Riyadh, London and New York and representative offices in Abu Dhabi, Beirut and Singapore, the Bank is ideally placed to provide its primarily Gulf-based customers with a quality service through a comprehensive understanding of the region's economic and commercial environment, a fine product portfolio, excellent human and technological resources and broad international expertise.

The past year has been marked by steady progress in virtually every sector of the Bank's operations.

At a time when integration was a major priority internally, this proved especially gratifying. Simultaneously, GIB's strong track record and participation in both state and private sector projects throughout the GCC have enabled it to capitalise on opportunities both in the Gulf and further afield.

Evidence of GIB's position at the forefront of Gulf banking was forthcoming in the form of a prestigious award from the publication *Global Finance*. The Bank was ranked 'The Safest Bank in Bahrain' in the magazine's annual analysis. In the words of *Global Finance* publisher Joseph D Giarraputo, the featured banks were "recognised for their outstanding financial condition and management of market risk".



The experience and expertise throughout the GIB network enable the Bank to offer a wide spectrum of products and services designed to meet the commercial banking and financial requirements of its Gulf and international clients.

...GIB remained a creative and dependable banker to many corporate and institutional clients, primarily in the GCC region, reflecting the familiarity and understanding developed by the Bank over many years.

GIB's client base includes regional institutions, governments and private sector businesses. Services include corporate, financial institution and government sector financing, project and asset-based financing, structural and acquisition finance, Islamic finance, contract finance and guarantees, trade finance and syndications.

For GIB Corporate and Institutional Banking, 2000 was a year of achievement. GIB remained a creative and dependable banker to many corporate and institutional clients, primarily in the GCC region, reflecting the familiarity and understanding developed by the Bank over many years. Yet, GIB like its clients, has faced the challenges of change posed by modern market developments and the increased emphasis on adequacy of returns. GIB's response has been to intensify its focus on areas of specialisation.

Project finance activities enjoyed a highly successful year, evidenced by GIB's recognition by Project Finance International as the leading Arab bank in project finance in 2000, as well as

being the largest regional arranger of project financing.

Among the more notable transactions were the US\$1,015 million long term financing for the independent power project Taweelah A1 in the United Arab Emirates, and the US\$200 million supplementary facility for Arabian Industrial Fibres Company (Ibn Rushd) as lead arranger and underwriter.

The Bank's structured finance activities played an important role in arranging and financing deals for key players in shipping and aircraft leasing, both within GIB's natural market, the GCC countries, and beyond. Noteworthy examples of transactions include: a US\$110 million new ship building financing facility for Arab Maritime Petroleum Transport Company, for which GIB acted as sole Arranger and Underwriter; a US\$200 million umbrella facility for UAE-based Oasis International Leasing in relation to the purchase of aircraft, as Lead Arranger; and a US\$92 million aircraft acquisition financing for



*US\$110 million ship
building financing facility
for Arab Maritime Petroleum
Transport Company.*

Singapore Aircraft Leasing Enterprise,
as Lead Arranger

These achievements in project and structured finance drew upon GIB's continued leading position in regional syndications. In addition, the Bank played a senior role in several other regional syndicated facilities including those for Commercial Bank of Qatar, Bahrain International Bank, Bank Muscat and Sharjah Cement

*the leading Arab bank
in project finance in 2000,
as well as being the largest
regional arranger of
project financing*

Of particular note, 2000 also marked the extension of GIB's syndication capability to Islamic financing by arranging and underwriting a major murabaha financing for the Islamic Development Bank

The depth of GIB's relationships is proving to be a platform from which to offer the Bank's increasing range of asset management, corporate advisory

and other investment banking services

Similarly, the establishment of GIB's Riyadh branch has enabled the Bank to extend the scope of services offered to many longstanding clients in Saudi Arabia, as well as penetrating new areas of the marketplace

The flow of business opportunities from existing clients and new prospects alike remains strong, and the outlook for 2001 is therefore encouraging

With a wide range of treasury and capital market products and services, GIB Assets and Liabilities Management meets the diverse needs of a broad client base of regional corporate and financial institutions

The Bank's treasury assets performed strongly during 2000, despite significant market volatility.

Through dealing rooms in Bahrain, London, New York and Riyadh, the Bank implements hedging and investment strategies tailored to individual client requirements. It manages important proprietary investment and trading securities portfolios, in addition to assuming responsibility for the management of the Bank's balance sheet. The unit also makes selective investments in specialised markets through external fund managers to achieve effective risk diversification.

...hedging and investment strategies tailored to the individual client...

The foreign exchange and money market activities of the business unit encompass deposits and placements, Euro-commercial paper, spot and forward foreign exchange transactions, margin trading facilities, and foreign exchange and interest rate derivative instruments. During a period typified by general currency uncertainty, GIB Assets

and Liabilities Management turned in a strong performance, especially through its treasury and capital markets units based in Bahrain. The foreign exchange, derivatives and fixed income functions also made impressive contributions.

As GIB continues to operate in a market that is becoming both more competitive and acutely time sensitive, the Bank is well positioned to take further advantage of the best global and local conditions.

GIB's participation in the international financial markets encompasses a wide range of specialist asset classes, products and investment strategies

Based in Gulf International Bank (UK) Limited (GIBUK), the unit's trading and investment teams apply a range of analytical approaches including relative value based strategic investments, arbitrage activities and directional trading. Risk is actively managed in a diverse range of markets including equities and convertibles, corporate fixed income, high yield debt, emerging market debt, currencies, interest rates and related derivatives.

strong trading revenues were achieved in all markets despite difficult and challenging conditions

GIB's sophisticated capital management skills played a vital role during the year, a period of significant volatility in the international capital markets. 2000 was a record year for GIB Financial Markets in a number of respects. Led by an exceptional performance from the equities team, strong trading revenues were achieved in all markets despite difficult and challenging conditions.

Furthermore, the performance of the funds managed by the unit exceeded their relevant benchmarks.

Our strategy of transferring in-house skills into client business continued during 2000, which saw the launch of the Bank's Falcon Collateralised Bond Obligation (CBO), with GIBUK acting as the manager for US\$300 million of high yield corporate securities. The CBO was a significant addition to the growing range of funds managed by GIBUK. These include funds in US and European high yield as well as managed futures. With further client initiatives planned, GIB will continue to benefit from a blend of product capability and client focus.

performance of the funds managed by the unit exceeded their relevant benchmarks



GIB Investment Banking, based in Riyadh, New York and London, provides specialist advice to clients conducting business in the GCC markets and internationally.

Jarir also represented the first private equity investment by GIB in the GCC

These clients include governments, government owned organisations, corporates and family owned establishments. The principal business focus is on providing and implementing advice on

- Mergers, acquisitions and disposals, including valuations
- Restructuring, valuing and placing shares in companies, including those which are family owned, in order to meet the challenges imposed by generational change, market developments and the desire or need to introduce specific new investors. This process can involve either private placements or Initial Public Offerings (IPOs)
- Project financing involving the review of feasibility studies through to the raising of equity and/or debt
- Restructuring and privatisation of governmental corporations

During 2000, GIB Investment Banking continued the development of its franchise in a number of areas, resulting in higher retainer and success

fees than the previous year. Highlights included the successful placement of a significant minority stake in, and conversion to joint stock company status of, Jarir Marketing Company, the leading bookstore and wholesale and retail stationery supplier in Saudi Arabia. Jarir also represented the first private equity investment by GIB in the GCC. In addition, the Bank acted as financial adviser to the Arabian Petrochemical Company Ltd, a wholly owned subsidiary of SABIC, in the successful raising of US\$600 million of debt from a syndicate of local, regional and international banks. The Bank was also appointed to the team acting as advisers on the privatisation of Saudi Arabian Airlines, the second mandate of its kind to be awarded to GIB in Saudi Arabia.

Corporate restructuring continues to present opportunities for GIB Investment Banking in both mergers and acquisitions, as well as with family companies across the GCC. Furthermore, as GCC companies mature, they are seeking financial and strategic investment opportunities.



In 2000, GIB Investment Banking continued the development of its franchise in a number of areas, serving an expanding and more diverse client base

outside their traditional markets where the Bank's regional and international presence and experience are vital in providing a customised capability. The continuing flow of new projects in the region has resulted in significant new project finance mandates being signed and these should be concluded during 2001 and 2002.

In addition, GIB Investment Banking offers clients co-investment opportunities in direct private equity investments as well as specialist private equity fund products. During 2000, we saw significant growth in the size and number of our direct private equity investments. We continued to focus on small and medium sized companies, and our deal flow accelerated dramatically over the year. We also achieved a successful first close of the Global Rights Fund II. This fund focuses on investments in brands, content and enabling technology in the media sector.

The direct private equity investment environment continues to offer interesting and rewarding opportunities.

Investment valuations became increasingly attractive during 2000 and continued to favour our focused bottom-up investment approach. Investments during the year focused on areas of core expertise including:

- speciality chemicals
- media technology
- enterprise software applications and telecoms

The investment banking market in the GCC continues to expand. Given GIB's track record and strong relationships in the region, the Bank is well positioned to capitalise on this growth.

...GIB Investment Banking offers clients co-investment opportunities in direct private equity investments...

GIB Asset Management is based in London and is regulated by the UK's Financial Services Authority and the Securities and Futures Authority

The unit concentrates on providing clients with an innovative but focused range of products and services and has established a reputation for delivering strategies consistent with clients' needs. This philosophy is founded on consistency of performance delivered by a clear and repeatable process.

GIB Asset Management provides a range of products and services which cover a wide spectrum of investment opportunities designed to meet the varying risk parameters of our client base. Such products include cash management and multi-currency fixed income portfolios for conservative mandates. Increasingly, a trend has been observed for investors to accept more risk with a longer-term investment horizon, and this has led to a number of balanced portfolio mandates which incorporate both bond and equity investments. For other clients, the unit manages a number of pure equity mandates including global, regional, single country and Islamic equity portfolios. Within the 'alternative assets' arena, designed for those clients with an even higher level of risk tolerance,

products and services include emerging market debt portfolios and hedge funds.

The year 2000 saw a number of new accounts being established, resulting in an increase in assets under management to US\$5.7 billion. This represents an important achievement given the volatility in capital markets during 2000 which resulted in broadly negative returns for most market indices.

this philosophy is founded on consistency of performance delivered by a clear and repeatable process

The Bank's policy of developing a wider range of products continued with GIB Asset Management and GIB Financial Markets working to establish and promote a range of 'alternative asset' funds. The CBO offering and the newly launched Falcon Euro High Yield Fund added to the growing stable of Falcon Funds, the brand name for our range of alternative fund products. The Falcon Relative Value Fund, an equity market neutral hedge fund, returned 48 per cent over the



*The launch of the Falcon
Euro High Yield Fund
enhanced GIB's growing
portfolio of alternative
fund products.*

year 2000 and is now attracting significant attention from a wide audience of investors both within and outside the GCC area. The Falcon Trend Selection Fund, the managed futures fund, also produced strong returns in a difficult environment

*...a trend has been
observed for investors
to accept more risk
with a longer-term
investment horizon...*

during the year and is similarly attracting considerable interest from an international investor base.

GIB Asset Management's marketing capabilities were significantly enhanced last year by the establishment of a marketing presence in Bahrain. This represented another step towards promoting asset management services to GIB's wider audience.



2000 saw growth in GIB's Saudi Arabian operations, including the opening of a branch in Riyadh.

Branches and Representative Offices

The opening of the Riyadh branch in September 2000 was one of the most significant events in GIB's history. As the first non-local bank in Saudi Arabia, the branch's inaugural year saw it laying firm foundations, especially in investment, institutional and corporate banking. The year has seen encouraging growth in the Bank's Saudi Arabian operations, and it continues to retain the leading position in mergers and acquisitions, and IPO activity. This position will be reinforced by enhancing service and marketing capabilities, the introduction of 'value added' products and increased client awareness of GIB's growing range of products and services.

the opening of the Riyadh branch in September 2000 was one of the most significant events in GIB's history

Treasury and trade finance, with related services for European exporters, remained the core activities of London branch during 2000. In addition, the

branch selectively participated in syndicated structured finance transactions, principally in the UK but also in other European Union countries. These transactions continue to support corporate mergers and acquisitions, and more recently the increasing securitisation of financial assets such as mortgages.

In dealing with clients in North Africa, the London branch played a leading role in a large syndicated term loan for Tunisia's electricity company and in the financing of basic commodities such as cereal, sugar and crude oil exports to several Arab countries.

During the second half of the year, the branch successfully integrated its operations and other support functions with GIBUK, which is already producing significant cost savings on a consolidated basis. The branch moved to new premises shared with GIBUK without disruption of its services to clients.

Elsewhere, 2000 has been a year of operational restructuring in the

New York branch, with no adverse impact on business, whilst the Abu Dhabi, Beirut and Singapore representative offices continued to develop successful relationships with key international clients.

Technology

The year saw a number of developments of a technological nature for GIB. Highlights included

- an in-house policy review encompassing all aspects of the Bank's technology and operations
- the transfer of operational processing from New York to Bahrain
- the complete installation of advanced IT and communication systems for Riyadh Branch and the linking of these systems to Bahrain
- implementation of a standardised technology strategy utilising integration and 'best of breed' hardware and software
- planning and preparation for the introduction of IAS-39 accounting procedures on 1st January 2001

The Bank has undertaken a policy review, coordinated by the Shared Services Committee. The review initiated important changes in procedures and systems with the objective of ensuring that Bank systems are flexible and capable of supporting new product requirements and an expansion in the customer base. It also covered the Bank's contingency disaster back-up plans, incorporating 'catch-all backup', local and off-country facilities. GIB views technology as part of its total resource capability, playing an important role in maintaining the Bank's competitive edge.

Human Resources

The guiding principle of GIB's human resources strategy is the development of policies and practices that allow the Bank to gain competitive advantage via our human resources. The overriding human resources objective is to attract, motivate and retain high quality employees at all levels. This is achieved through a combination of sound management, open communication, appropriate

remuneration and the provision of excellent training and development opportunities. From a cultural perspective, individual creativity is encouraged and valued within the context of promoting teamwork.

The management and development of GIB's human resources is fundamental to the continued success of the Bank. The Bank remains fully committed to the training and development of employees as evidenced by the significant training activity undertaken during the year. This is increasingly important given the principle that the Bank employs suitably qualified, competent employees.

In addition to building on the skills of existing employees, GIB has increased by 66 per cent the number of graduates joining the Bank Executive Trainee programme in Bahrain. The aim of this programme is to identify and develop the Bank's potential future leaders.

a combination of sound management, open communication, appropriate remuneration and the provision of excellent training and development opportunities

Consolidated Net Income for the year was at a record level. Net Income after Provisions and Tax at US\$118.1 million was US\$50.5 million or 74.7 per cent up against the prior year. The consolidated prior year result, however, only incorporated the profit of GIB's wholly owned investment banking subsidiary, Gulf International Bank (UK) Limited (GIBUK), for the nine month period since the date of acquisition in April 1999. The strong advance in the 2000 consolidated profit was attributable to significant year-on-year increases in both interest and non-interest earnings. This reflected the implementation of business initiatives to both focus on higher value-added customer-related banking services and to capitalise on the Group's pre-eminent investment banking franchise in the GCC.

Net Interest Income

Net Interest Income at US\$169.7 million was US\$30.1 million or 21.6 per cent up on the prior year. Net Interest Income is principally derived from four sources: earnings on the Group's net free capital, the commercial banking portfolio, the investment securities portfolio, and the money book. Net Interest Income is also reported net of the funding cost of externally managed funds for which income is derived in the form of dividends and capital gains.

Year-on-year increases were recorded in interest earnings from all of the Group's principal business activities. A lower interest rate environment prevailed in most economies in 2000. The Group was nevertheless able to enhance the level of interest earnings on the investment of its net free capital funds. Prudent management contributed to the maximisation of the yield generated on the investment of the net free capital funds and a higher amount of capital was also available for investment. A 13 per cent year-on-year increase was recorded in

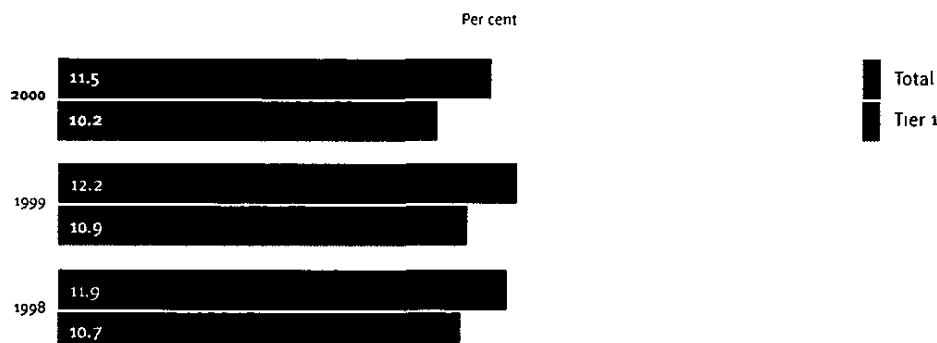
net interest earnings from the Group's core commercial banking portfolio, reflecting a further improvement in margins with average volumes being almost 10 per cent lower than the previous year. The increase in margins was attributable to a continued focus on higher value-added, skill-based commercial banking facilities, including project financings and lead manager roles in syndicated facilities. Margin income derived from the investment securities portfolio benefited from a substantial widening in credit spreads during the second half of the year with maturing assets being replaced at higher margins. In addition, there was an almost 20 per cent year-on-year increase in the average volume of investment securities. The Group continued to increase, on a selective basis, its investment securities portfolio, taking advantage of particularly attractive investment opportunities afforded by the general widening in credit spreads, even at the higher end of the rating spectrum. The credit quality of the investment securities portfolio continued to be emphasised with 85.5 per cent of

investment debt securities at the 2000 year end being investment grade-rated. A year-on-year increase was also recorded in the net interest earnings generated by the money book, reflecting the benefit derived from short interest repricing mismatch positions maintained during a period of declining interest rates. Net interest earnings in the prior year had also been negatively impacted by the maintenance of an exceptionally high level of liquidity over the 1999 year end for Year 2000 contingency purposes.

Other Income

Other Income at US\$127.3 million for the year was US\$49.9 million or 64.4 per cent up on the prior year. An analysis of Other Income with prior year comparatives is set out in Note 16 to the Consolidated Financial Statements. Trading activities were the largest contributor to non-interest earnings, recording a US\$38.9 million profit for the year. This represented a US\$15.3 million or 64.8 per cent increase over the prior year. The strong trading revenues were achieved despite the extremely difficult and

BIS Risk Asset Ratio



challenging market environment in 2000, particularly during the second half of the year. Revenue generation was assisted by the strict application of disciplined risk management techniques. A disciplined and prudent approach to risk taking enabled the Group to anticipate and react swiftly to adverse market changes. Strong trading revenues were generated from equity trading in particular although material contributions were also made by the Group's trading activities in the corporate debt, fixed income, interest rate derivative and emerging markets. Equity trading revenues benefited from relative value, arbitrage and non-directional trading strategies. Dividend Income of US\$28.5 million was received from equity investments of a structured finance nature and from externally managed funds. The funding cost of these investments is reported in Net Interest Income. A 6.3 per cent year-on-year increase in dividend income reflected a higher level of investment in 2000. Profits on Investment Securities were US\$27.6 million for the year. This included profits of US\$18.0 million arising on

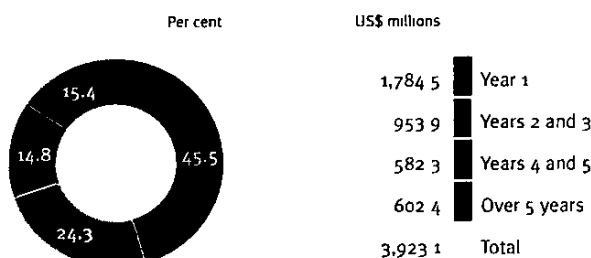
certain long term equity holdings that were liquidated in anticipation of a deterioration in market conditions. All marketable equity activities, other than certain long term investments in managed funds, subsequently took place in the trading portfolio. The remaining profits on investment securities comprised profits realised on either long term private equity investments or on the early maturity of debt securities which were called by the issuers. Longer term debt security holdings are generally only liquidated in anticipation of a potential deterioration in the creditworthiness of the security issuer. Investment Banking and Management Fees at US\$13.9 million were at almost twice the prior year level. Strong advances were recorded in fee income generated from the Group's corporate finance, asset management and fund management activities. The very significant year-on-year increase reflected the Group's successful efforts in diversifying revenues through the development of a wider range of customer-related products and services, and the associated benefits

derived from the integration with GIBUK. As commented on in more detail in the Management Review section, the Group was awarded a number of important corporate finance mandates during the year. Fund management fee income also benefited from higher performance-related fees resulting from the strong returns generated by the various funds managed by the Group. Profits on Foreign Exchange of US\$7.5 million were 36.4 per cent up on the prior year and reflected a continued strong customer demand. Commissions on letters of credit and guarantees at US\$6.6 million continued to make an important contribution to non-interest income. A US\$3.0 million profit was realised on the partial sale of an associated company through an IPO. The company, a Singapore-based stockbroker, undertook an IPO in the second quarter of the year in which part of the Bank's shareholding was included. GIB continues to have an investment in the company, although following the IPO the investment no longer meets the criteria for an associated company.

Asset Mix by Category



Loan Maturity Profile



Operating Expenses

Operating Expenses at US\$132.3 million compared to US\$109.9 million in the prior year. Prior year expenses, however, only included GIBUK's expenses for the nine months since acquisition. On a comparable proforma basis, including GIBUK's full year expenses for 1999, Operating Expenses were only US\$7.6 million or 6.1 per cent up on the prior year. Prior year expenses did, however, include an exceptional pre-tax charge of US\$11.7 million in respect of restructuring costs associated with the GIBUK acquisition. At the end of the third quarter of 2000, GIB's London branch physically integrated with GIBUK, with branch personnel moving to GIBUK's premises. The London branch's back office and support functions have subsequently been

outsourced to GIBUK with the approval of the relevant regulators. At the same time, certain back office functions were transferred from GIB's New York branch to Head Office in Bahrain. These actions resulted in reductions in staffing levels. The cost savings associated with the restructuring of the overseas activities will only be fully realised from the beginning of 2001, although will be offset to a certain extent by the incremental costs associated with the new Riyadh branch which opened in the third quarter of the year.

The Group continues to focus on further improving cost efficiencies through the use of technology and to take measures to contain recurring costs while making the necessary investments for the future.

Capital Strength

Shareholders' Equity increased to US\$1,205.8 million at 31st December 2000. At the 2000 year end Shareholders' Equity and Tier 1 Capital both represented 8.0 per cent of Total Assets, ratios that are high by international comparison. The average Tier 1 capital to total assets ratio of the top 1,000 banks in 2000 was 4.86 per cent according to a survey published in *The Banker* in July 2000.

With a total regulatory capital base of US\$1,353.0 million and total risk-weighted exposure of US\$11,777.3 million, the risk asset ratio calculated in accordance with the guidelines of the Basel Committee on Banking Supervision was 11.5 per cent. The risk asset ratio incorporates market risk-weighted exposure. Exposure to

general market risk is calculated utilising a Value-at-Risk model in accordance with the provisions of the Amendment to the Capital Accord to Incorporate Market Risk. 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 Bahrain Monetary Agency (BMA). The high proportion of Shareholders' Equity within the total capital base resulted in a Tier 1 ratio of 10.2 per cent. This ratio is particularly high by international standards. Note 27 to the Consolidated Financial Statements provides further details on capital adequacy. The risk asset ratio calculated in accordance with the guidelines of the Bank's regulatory authority, the BMA, was 12.3 per cent at the 2000 year end (1999 13.1 per cent). Under the BMA guidelines, GCC governments and government-owned entities are accorded the same preferential risk weighting as for OECD governments. The BMA applies a minimum risk asset ratio of 12 per cent compared to a minimum of 8 per cent prescribed by the Basel Committee.

Factors which contribute to the favourable capital adequacy position are the strong capital base, the level of general provisions and significant exposure to major OECD country governments and to the banking community.

Asset Quality

The Bank's principal strategic focus is on the GCC states and their major trading partners in the industrialised world. Geographical diversification of risk therefore occurs to a large degree naturally. An assessment of the geographical diversification of risk assets may be made by reference

to Note 22 to the Consolidated Financial Statements. Further assessment of asset quality can be facilitated by reference to Note 30 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 were lower than their net book values at 31st December 2000 by only US\$64.6 million. The shortfall reflected a general widening in credit spreads that took place during the second half of the year. The shortfall has substantially reduced in the early part of 2001 as a result of a subsequent narrowing of credit spreads.

At the 2000 year end, Loans and Advances represented 25.9 per cent of Total Assets while Investment Securities accounted for 46.7 per cent.

Loans and Advances

Loans and Advances were relatively unchanged at US\$3,923.1 million at the 2000 year end. Based on contractual maturities at the balance sheet date, 45.5 per cent of the portfolio was due to mature within one year while 69.8 per cent was due to mature within three years. Details of exposure within the portfolio to GCC and OECD country governments are contained in Note 7 to the Consolidated Financial Statements, while the geographic distribution of Loans and Advances is set out in Note 22. 60.6 per cent, or a little over half, of the portfolio represented lending within GIB's core market in the GCC states while the balance was largely made up of exposure to the GCC countries' major trading partners in Europe, North America and Asia. The portfolio contained no significant concentrations

by industrial sector. As discussed in Note 30, the net fair value of loans and advances exceeded their net book value by US\$24.8 million. Total loan loss provisions at 31st December 2000 amounted to US\$792.9 million. Country and counterparty specific provisions amounted to US\$602.2 million while general provisions were US\$190.7 million. The loan loss provision charge for the year of US\$22.4 million comprised the net of an increase in specific provisions of US\$26.5 million and a decrease in general provisions of US\$4.1 million. Specific provision utilisations during 2000 totalled US\$53.3 million. The utilisations principally arose on the settlement of an exposure to a Korean conglomerate in accordance with the terms of a debt restructuring agreement concluded with the foreign bank steering committee, and on the conversion of a Russian loan facility to a debt obligation. The loan was transferred to the investment security portfolio at its net book value resulting in the write off of the related specific country provision.

The decrease in general loan provisions arose in GIB's investment banking subsidiary, GIBUK, and resulted from a further reduction in GIBUK's loan portfolio during the year to a level where it was deemed appropriate to release part of the general provision which exceeded the level of expected loss. A US\$14.7 million decrease in specific provisions resulting from exchange rate movements was offset by an equivalent decrease in the related impaired loan exposures. Specific provisions are maintained in the currencies of the related exposures. The general provision at the year end represented 4.6 per cent of loans net of specific provisions.

Specific provisions in respect of troubled sovereign exposures are determined with reference to the guidelines of the relevant regulatory authorities. Specific provisions in respect of other loans are made to the full extent of the estimated potential loss, while general provisions are maintained to cover possible future losses which as yet have not been specifically identified. Specific provisions are maintained for individually significant, non-homogenous loans and 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. General provisions are determined based on historical patterns of losses for each group of similar loans and the applicable credit ratings, and reflect the current economic and business environment and other pertinent indicators.

The basis on which provisions were determined at the 2000 year end was consistent with the requirements of International Accounting Standard (IAS) No. 39 – Financial Instruments Recognition and Measurement. The adoption of IAS 39 on 1st January 2001 therefore had no impact on the Group's overall level of provisions for impairment at that date. Loans are written off only after all reasonable restructuring and collection activities have taken place and the possibility of further recovery is considered to be remote.

The gross and net book values of non-performing loans amounted to US\$561.0 million and US\$57.6 million respectively. The average provisioning

coverage for non-performing loans was therefore 89.7 per cent. An ageing analysis of non-performing loans is set out in Note 7 (c) to the Consolidated Financial Statements. US\$464.9 million, or 82.9 per cent, of gross non-performing loans were overdue by more than five years and are therefore historical in nature. These are all fully provided against. Only US\$66.1 million of non-performing loans at 31st December 2000 had been placed on non-accrual status during the preceding twelve months. This represented only 1.4 per cent of gross loans. The gross volume of non-performing loans also continued to be substantially below the total of specific and general provisions. Total provisions for loan losses exceeded the gross volume of non-performing loans by US\$231.9 million. This means that rather than earnings being impaired by the funding cost of the net book value of non-performing loans, there is a positive earnings enhancement. Non-performing loans at their net book value of US\$57.6 million represented just 1.5 per cent of net loans. Non-performing loans at their net book value also represented only 4.8 per cent of Shareholders' Equity. Loans on which interest or principal is 90 days or more overdue are without exception placed on a non-accrual basis and all unpaid and accrued interest is reversed from income. Interest on non-accrual loans is accounted for only when received.

Investment Securities

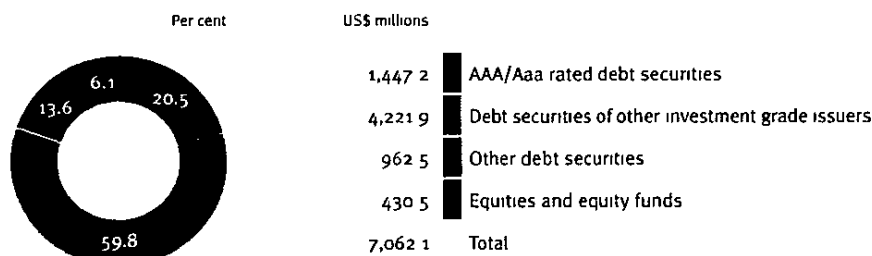
Investment Securities totalled US\$7,062.1 million at 31st December 2000. The investment securities portfolio is used as a means of providing effective geographical diversification of the Group's risk assets with 82.9 per cent of the

portfolio comprising securities of North American and European issuers.

Investment Securities principally comprise two types of debt security portfolios and a more 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 floating to yield constant spreads over LIBOR. These accounted for 88.6 per cent of the total investment securities portfolio. The smaller debt security portfolio is made up of fixed income securities, principally OECD government or government-guaranteed bonds, representing the investment of part of the Group's net free capital. This portfolio amounted to US\$377.6 million at the 2000 year end.

An analysis of the investment securities portfolio by rating category is contained in Note 6 to the Consolidated Financial Statements. US\$1,447.2 million or 20.5 per cent of the portfolio at the 2000 year end represented AAA-rated securities. Based on the rating of the issuer a further US\$4,221.9 million or 59.8 per cent of the portfolio represented investment grade debt securities. Thus 80.3 per cent of the total portfolio comprised investment grade securities. Other Debt Securities at the end of 2000 amounted to US\$962.5 million. These securities are largely of a loan substitution nature and as such are not necessarily rated. The credit risk associated with these securities is rigorously monitored within the overall credit risk management process. The securities are therefore subject to the same stringent credit requirements as standard lending and credit-related contingent transactions.

Investment Securities Rating Profile



Equities and equity funds at 31st December 2000 amounted to US\$430.5 million. The equity and equity fund portfolio is principally invested in equity investments of a structured finance nature and also a wide range of externally managed fund-type investments which provide a diversified exposure to private equity, debt and real estate markets.

Total investment security provisions at 31st December 2000 amounted to US\$24.2 million. Specific investment security provisions at the 2000 year end comprised provisions for impairment against unquoted and illiquid investments and sovereign-related provisions determined with reference to regulatory authority matrix-based guidelines. In preparation for the implementation of IAS 39 on 1st January 2001, the unutilised general security provision of US\$21.3 million was transferred to specific security provisions and allocated to individual security holdings which were deemed to be impaired. The carrying amounts, or book values, of the impaired marketable securities

were written down to their recoverable amounts determined with reference to quoted market prices.

Other Interest-bearing Asset Categories Cash and Other Liquid Assets, which amounted to US\$137.3 million at the 2000 year end, are analysed in Note 3 to the Consolidated Financial Statements. In addition to Cash and Balances with Banks, which were at a particularly high level at the previous year end due to Year 2000 considerations, Other Liquid Assets included Certificates of Deposit held for Balance Sheet management purposes.

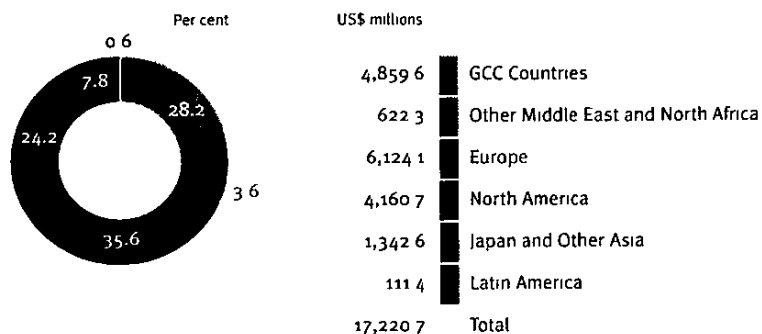
Placements with Banks totalled US\$3,065.0 million at the 2000 year end and were well diversified by geography as illustrated in Note 22 to the Consolidated Financial Statements. Placements were at an exceptionally high level over the 1999 year end reflecting the placement of a substantial volume of additional funds raised prior to the year end as part of the Group's Year 2000 contingency plan. As demonstrated in the Average

Balance Sheet set out in Note 34 to the Consolidated Financial Statements, Placements with Banks at the 2000 year end were not materially dissimilar to the average of US\$3,500.4 million during 2000.

Trading Securities at US\$465.8 million largely comprised listed debt securities and government bonds amounting to US\$236.8 million and US\$69.9 million respectively. Trading Securities also included US\$108.7 million of managed funds. The funds, which are managed by international institutions with acknowledged expertise in their field, provide diversified exposure to foreign exchange and international debt markets. Trading Securities are accounted for at market value.

Risk Asset and Commitment Exposure Risk assets and commitments at 31st December 2000 amounted to US\$17,220.7 million. Risk assets and commitments comprise all assets included in the balance sheet (with the exception of Fixed and Other Assets) and Credit-related Contingent Items. As alluded to earlier, an analysis of risk

Risk Asset and Commitment Exposure



asset and commitment exposure by category and geography is contained in Note 22 to the Consolidated Financial Statements. An analysis of derivatives and foreign exchange products is set out in Note 25(a), while a further analysis of Credit-related Contingent Items together with their risk-weighted equivalents is contained in Note 25(b).

Funding

Bank and Customer Deposits at 31st December 2000 totalled US\$11,414.5 million. This was much the same level as at the end of 1999, although deposits at the 1999 year end were at an exceptionally high level due to Year 2000 factors. As reported in Note 34 to the Consolidated Financial Statements, total deposits averaged US\$11,185.6 million during 2000 compared to an average of US\$10,701.9 million during 1999. Customer deposits at the 2000 year end represented 42.9 per cent of total deposits compared to 48.0 per cent at the end of 1999. Customer deposits were, however, at an exceptionally high level over the 1999 year end. Customer deposits averaged US\$4,868.9 million during 2000, being US\$487.5

million or 11.1 per cent higher than the average during 1999. Securities Sold under Agreements to Repurchase (Repos) decreased to US\$1,164.6 million at 31st December 2000. Repos were used to generate additional liquidity over the 1999 year end as part of the Bank's Year 2000 liquidity contingency arrangements. Term Financing at 31st December 2000 totalled US\$850 million. In the second quarter of the year, the Bank replaced a maturing US\$300 million term loan with a new US\$400 million 5-year floating rate loan facility. The new term loan was increased from an original US\$300 million to US\$400 million on syndication due to a very substantial oversubscription. The new term facility was also raised at a lower all-in cost than the maturing facility despite the general widening in spreads that took place in the international credit markets during the year. Further commentary on liquidity and funding is provided in the Risk Management section of the Financial Review.

Future Change in Accounting Policies

As commented on in more detail in

Note 36 to the Consolidated Financial Statements, GIB adopted IAS 39 – Financial Instruments Recognition and Measurement on 1st January 2001. The adoption of IAS 39 resulted in changes in the Group's accounting policies in respect of the recognition and measurement of derivative financial instruments, securities, loans and advances, and provisions for impairment.

The overall financial effect of the adoption of IAS 39 was to reduce Shareholders' Equity at 1st January 2001 by a net US\$88.7 million. This almost entirely represented the remeasurement of investments to fair value following their recategorisation as 'available-for-sale' securities. Further details on the effect of the changes in accounting policies is provided in Note 36 to the Consolidated Financial Statements.

Credit Ratings

During the year under review, GIB's investment grade ratings were reaffirmed by Standard & Poor's and Moody's. In addition, at the beginning

Asset Mix by Geography

	Per cent			
2000	64.7	26.9	8.4	OECD Countries
1999	68.2	24.4	7.4	GCC Countries
1998	53.5	34.6	11.9	Other Countries

of the year GIB's ratings were further enhanced by the assignment of investment grade ratings by Fitch IBCA. As a result, GIB was the first GCC bank to be assigned long term debt ratings by all three major international credit rating agencies. Individual and Financial Strength ratings, which are specific to Fitch IBCA and Moody's respectively, are awarded on a scale from A to E. Following a recalibration by Moody's of its Financial Strength ratings scale early in 2001, GIB's Financial Strength rating was adjusted up from D+ to C-. GIB's credit ratings are as follows:

	Fitch IBCA	Moody's	Standard & Poor's
Long-term	BBB+	Baa2	BBB+
Short-term	F2	P3	A2
Individual	C	-	-
Financial Strength	-	C-	-

Standard & Poor's investment grade ratings reflect 'the bank's ownership, its adequate capitalisation at both bank and shareholder level, and adequate asset quality'. In addition, Standard & Poor's state 'the bank has a good quality

of service and highly experienced senior management' and, with reference to asset quality, comment 'GIB's conservative loan loss provisioning policy enhances the bank's credit standing'. Moody's ratings 'reflect a strong wholesale commercial banking franchise in the Arabian Gulf' and 'take account of the strong shareholding and high likelihood of support in case of need' and conclude 'GIB plays a leading role in arranging and providing finance for public and private borrowers in the Arabian Gulf'. Fitch IBCA state that their ratings reflect 'GIB's ownership and likely shareholder support regional expertise and client relationships'.

It is an objective of GIB to manage itself in such a manner as to retain and enhance the assigned ratings.

Risk Management

The GIB Group maintains a prudent and professional approach to risk-taking. A risk management culture is actively promoted that accords high value to disciplined and effective risk management and employs professionally qualified people with appropriate risk management skills. Comprehensive

risk management processes have been developed which effectively identify, measure, monitor, and control risk exposures and that are subject to oversight by the Board of Directors and senior management.

The Group is constantly seeking to strengthen these processes, particularly through investment in technology and training. Periodic review by internal and external auditors and regulators subject these processes to additional scrutiny and help to further strengthen risk management practices. GIB is also fully supportive of the risk management recommendations of the Basel Committee on Banking Supervision and the actions taken by national supervisory authorities with respect to the application of appropriate and adequate risk management principles.

The risk management control process is based upon a detailed structure of policies, procedures and limits, a comprehensive risk measurement process and a strong management information system for the control,

monitoring and reporting of risks

All significant policies are approved by the Board of Directors. Policies are consistent with corporate strategy, capital strength and management expertise, and together with procedures, are reviewed regularly in order to ensure their continued appropriateness. An integrated limit structure is an essential component of the risk management process. This permits management to control exposures and to monitor the assumption of risk against predetermined approved tolerances. Global limits are established for each major type of risk. These are generally sub-allocated to individual business units.

A Risk Management Committee is the senior authority within the integrated risk management hierarchy and oversees the active management of all risks involved in the Group's business. The committee comprises the organisation's most senior professionals and is chaired by the Group Chief Executive. The role of the committee includes the strategic management of the overall risk profile, ensuring the adequacy of the risk management infrastructure, the coordination of the various specialist risk control areas and assessing solutions for specific risk issues. The Risk Management Committee provides a forum for the discussion of risk issues by senior management as well as ensuring that the Group is aware of the latest developments in risk management practice within the financial services industry.

A fundamental risk management tenet within GIB is the clear segregation of duties and reporting lines between personnel transacting business and personnel processing

that business. Key elements of the processing environment are clearly defined procedures, adequate systems infrastructure and a comprehensive system of internal controls.

An independent market risk management function possessing market risk management skills and capable of informative interpretation of management information contributes positively to the overall effectiveness of the risk management process. It is ensured that all risks associated with a product or line of business are clearly understood and are monitored and reported to senior management by professionally qualified and experienced personnel outside the business unit responsible for transacting that business.

A strong internal audit function is also considered to be of particular importance. The internal audit function conducts periodic reviews of the adequacy and integrity of the risk management process. Auditing procedures are designed to ensure the integrity of the measurement, control and reporting systems and compliance with approved policies and procedures. The Group Chief Auditor reports regularly to the Audit Committee of the Board of Directors.

Recommendations from both the internal and external auditors are considered positively by senior management. In cases where remedial action is deemed appropriate, such action is undertaken promptly.

The Asset and Liability Committee (ALCO), which comprises members of senior management, provides a forum for treasury risk management. ALCO meets on a weekly basis to review

matters relating to both the asset and liability management function and trading strategies.

Risks associated with off-balance sheet derivative instruments are managed as part of the overall risk management framework. Financial and risk management disclosures with respect to off-balance sheet financial instruments are set out in Note 25 to the Consolidated Financial Statements. The disclosure provides details of derivative and foreign exchange transactions at 31st December 2000 analysed by type of product, counterparty and maturity. The major risks associated with GIB's business are credit, market, liquidity and operational risks. These risks and the related risk management processes are commented on in Note 21 to the Consolidated Financial Statements and discussed in detail in the following sections.

Credit Risk

Credit risk represents the risk that a counterparty may fail to perform according to agreed terms and conditions, thus causing the bank to suffer a loss in terms of cash flow or market value. This risk is measured in relation to banking and treasury products both on and off the balance sheet.

Credit risk is actively managed and rigorously monitored in accordance with well-defined credit policies and procedures. The creditworthiness of each counterparty is assessed, and appropriate credit limits are established within delegated authority by the Credit Committee. Credit limits are also established for countries, utilising a country risk review system. Overall exposures are also evaluated to ensure a broad diversification of credit risk.

Per cent

Liquid Assets Ratio

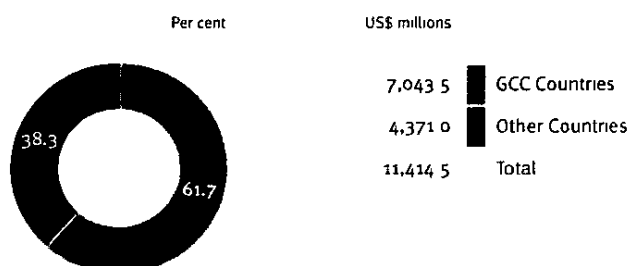


Times

Deposits to Loans Cover



Deposits – Geographic Profile



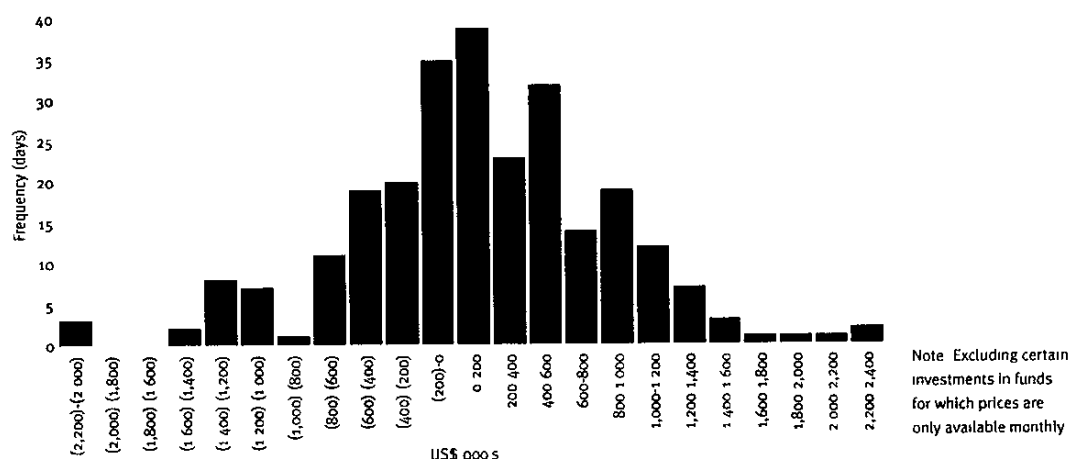
Potential concentration risks by product, industry, single obligor, risk grade and geography are regularly assessed with a view to improving overall portfolio diversification. Established limits and actual levels of exposure are regularly reviewed by the Chief Credit Officer and senior management. Credit policies and procedures are designed to identify, at an early stage, exposures which require more detailed monitoring and review. A credit risk rating system together with an associated watch list and classification system are used in the determination of the appropriate level of specific and general provisions for credit losses.

The credit risk associated with foreign exchange and derivative instruments is assessed in a manner similar to that associated with on-balance sheet activities. However, 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 derivatives instruments is therefore more appropriately considered to be their replacement cost at current market rates, should the counterparty default prior to the settlement date.

The gross positive market values or credit risk amounts of foreign exchange and derivative transactions are set out in Note 25 to the Consolidated Financial Statements. The total credit risk amount in respect of all such transactions outstanding at the 2000 year end amounted to US\$314.3 million before taking account of the risk-reducing benefits of any collateral held or legally enforceable netting agreements.

The note highlights that 92.5 per cent of the total credit risk was concentrated on major OECD-based banks and was predominantly short-term in nature with 65.2 per cent,

Histogram of Daily Trading Gains & Losses



or two thirds, of transactions outstanding at the end of 2000 due to mature within one year. Transactions maturing beyond one year represented either hedging transactions entered into for asset and liability management purposes or fully offset customer transactions.

Market Risk

Market risk is the risk that the value of a financial instrument or a portfolio of financial instruments will change as a result of a change in market prices and rates. This risk arises from the Group's trading, asset and liability management and investment activities in the interest rate, foreign exchange, security and equity markets. Limit structures incorporate both VaR-based and non-VaR-based limits with respect to market risk. There are a variety of non-VaR-based constraints. These relate, inter alia, to positions, volumes, concentrations, maximum allowable losses and maturities. Exposures are monitored against the range of limits and regularly reported to, and reviewed by, senior management. A key element in the Group's market

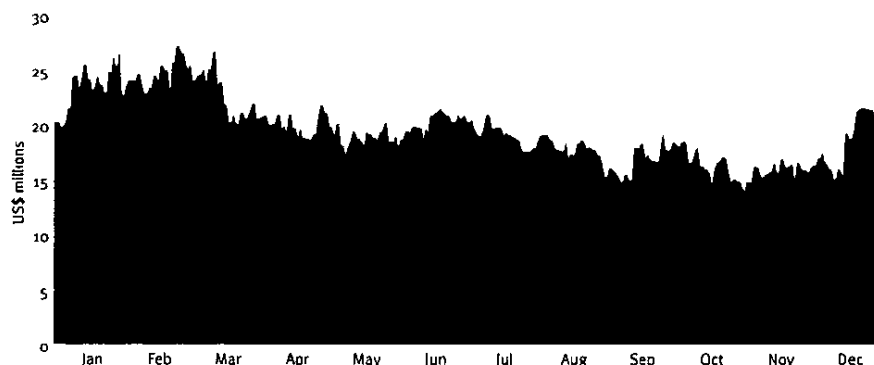
risk management framework is the estimation of potential losses that may arise from adverse market movements. GIB utilises Value-at-Risk (VaR) to estimate such losses. VaR takes account of variables that may cause a change in portfolio value. These include interest rates, foreign exchange rates, security and equity prices, their respective volatilities and the correlations between these variables. GIB uses exponentially weighted historical one-day movements in these variables from the DataMetrics™ data set in estimating potential future losses from its trading and asset and liability activities as well as from its investment portfolios. These estimates assume normal market conditions and take account of potential diversification benefits of different positions both within each and across different portfolios.

For internal risk management purposes, GIB measures losses that are anticipated to occur within a 95 per cent confidence level. This implies that there is a 5 per cent or 1 in 20 chance of a loss exceeding the VaR over the prescribed time horizon or holding period.

A one-day horizon is relevant for trading activities while a longer horizon is more appropriate for both asset and liability management and investment activities. GIB consolidates VaR utilising a one month holding period. The graph opposite sets out the total Value-at-Risk of all activities for the Group in both the banking and investment books at the close of business each day throughout the year. The figures are calculated at the 5 per cent risk level (1.65 standard deviations) and at the one month horizon based on the DataMetrics™ data set. On this basis, VaR over the year averaged US\$19.7 million and varied within the range of US\$14.1 million to US\$27.3 million. (At a one-day rather than a one-month horizon but at the same 5 per cent risk level average VaR was US\$3.9 million and varied between US\$2.8 million and US\$5.5 million.) At the 2000 year end VaR at the one month horizon amounted to US\$21.0 million.

GIB conducts daily VaR backtesting for both regulatory compliance with the Basel Committee on Banking

Consolidated Value-at-Risk (VaR) Daily Development



Supervision market risk capital rules and for internal evaluation of VaR against trading revenues. During 2000, a daily trading loss exceeded the trading VaR at the close of business on the previous business day on only three occasions. This is within the maximum of five excesses permitted under the Basel Committee's guidelines on backtesting beyond which the multiplication factor determined by the regulator must be increased.

GIB believes that the stability of revenues from market risk activities is enhanced through the measurement, control and management of risk exposures to extreme stress events. Whereas VaR captures exposures in normal market conditions, stress testing is used to determine the risk of unlikely but plausible events in abnormal markets. Portfolio stress testing is an integral market risk measurement and control tool. Stress tests are built around changes in market rates and prices that result from pre-specified economic scenarios, including both actual historical and hypothetical market

events. Historical scenarios include the 1994 bond market sell-off, the 1995 Mexican Peso crisis and the 1998 Russian crisis. Stress test calculations are performed for all material trading and investment portfolios.

A major 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. Nominal gap and VaR-based limits are utilised to control fluctuations in interest earnings resulting from changes in interest rate levels. The asset and liability repricing profile and details of the effective interest rates prevailing at the year end on the various asset and liability categories are set out in Note 24 to the Consolidated Financial Statements.

The repricing profiles of securities and loans incorporate the effect of interest rate swaps used to modify the interest rate characteristics of specific transactions. By contrast, interest rate swaps and forward rate agreements

that have been used for asset and liability management purposes to hedge overall exposure to interest rate risk are included separately as Off-Balance Sheet Items. As illustrated in Note 24, the substantial majority of assets and liabilities reprice within one year. The volume of net interest-bearing assets repricing over one year amounted to only US\$527.1 million or 3.5 per cent of Total Assets. This largely represented the investment of the Group's net free capital through fixed rate securities, the modified duration of which was 1.45 at the year end.

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 measure of market risk across all applicable products and activities based on the assumption of normal market conditions. Market risk is therefore assumed on a prudent basis in recognition of the fact that market shocks may result in losses in excess of those anticipated from VaR. A broad mix of limits are thus employed. This notwithstanding limits

in themselves are recognised as an aid to – rather than a substitute for – sound judgement. Sound judgement is recognised as the cornerstone of effective market risk management.

Liquidity Risk and Funding

Liquidity risk management ensures that funds are available at all times to meet the funding requirements of the Group.

GIB's liquidity management policies are designed to ensure that it has access to adequate funds to meet its obligations, even under 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 provide the flexibility to capitalise on opportunities for business expansion. These objectives are met through the application of a prudent mix of liquidity controls. These controls provide security of access to liquidity without undue exposure to increased costs from the liquidation of assets or the aggressive bidding for deposits. The 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 is managed and monitored on a daily basis at the parent company and subsidiary levels, enabling senior management to identify changes and to react accordingly to fluctuations in market conditions. Liquidity controls also provide for the maintenance of a stock of liquid and marketable assets and also an adequately diversified deposit base in terms of both maturities and range of counterparties. The funding base is enhanced through term financing of US\$850 million.

Deposits from Customers provide a further stable source of funding. Contingency plans also exist and could be implemented on a timely basis to minimise the risk associated with dramatic changes in market conditions.

The asset and liability maturity profile by individual asset and liability category based on contractual repayment arrangements is set out in Note 23 to the Consolidated Financial Statements. At the 2000 year end 43.9 per cent, or a little under half, of Total Assets were due to mature within one year. A significant portion of assets with longer term maturities comprised readily realisable securities. With regard to deposits, retention records demonstrate that there is considerable divergence between their contractual and effective maturities. By way of example, average deposits in 2000 from those counterparties with deposits over US\$10 million at the 2000 year end amounted to US\$8,511 million. Thus, these deposits of a core nature, together with Shareholders' Equity and Term Financing, were two and a half times, and thus more than adequately funded, the least liquid asset category, Loans and Advances. The loan portfolio is also comfortably exceeded by the more stable deposits from the GCC region. Deposits from GCC country governments and central banks and other institutions headquartered in the GCC states at 31st December 2000 amounted to US\$7,043.5 million. GCC deposits to total loans cover was therefore 1.8 times. Total deposits and term financing coverage to loans was 3.1 times while the liquid assets ratio, which expresses bank balances, money market instruments, placements with banks and securities as a percentage of total assets, was a very high 71.0 per cent.

Operational Risk

The bank views operational risk as the risk of loss resulting from inadequate or failed internal policies or processes, systems failures, internal or external criminal acts, business interruption, compliance breaches, human error, management failure or inadequate staffing.

While operational risk cannot be eliminated in entirety, the Group endeavours to minimise it by ensuring that the appropriate infrastructure, controls, systems and trained and competent people are in place throughout the organisation. The various procedures used to manage operational risk include segregation of duties, effective training, performance management, communication of risk tolerance, risk monitoring and financial management and reporting. The Group also possesses back-up capabilities to support ongoing business operations in the event of adverse conditions.

To reinforce the comprehensive controls and procedures in place, a department has been established with specific responsibility for ensuring adequate protection against operational risk. A database of risks has been compiled using a risk assessment process and the controls required to mitigate these risks are constantly under review. Business units monitor risk indicators on a regular basis and a reporting methodology to senior management is currently being developed.

In addition, the Group has a strong Internal Audit function which makes regular, independent appraisals of the actual functioning of the controls in all the identified risk areas.

Gulf International Bank is committed to the ongoing enhancement of its financial reporting. The Bank's objective is to provide clear, comprehensive and relevant disclosure in order to facilitate financial appraisal and risk assessment. Accounting and reporting policies comply with the requirements of International Accounting Standards and conform with best practice in the banking industry.

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Auditors' Report to the Shareholders

We have audited the consolidated financial statements of Gulf International Bank B.S C. and its subsidiaries (the Group) as at, and for the year ended, 31st December 2000 as set out on pages 35 to 67.

Respective responsibilities of directors and auditors

These consolidated financial statements are the responsibility of the directors. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

Basis of opinion

We conducted our audit in accordance with International Standards on Auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as at 31st December 2000, and the results of its operations and its cash flows for the year then ended, in accordance with International Accounting Standards.

Other regulatory matters

In addition, in our opinion, the Group has maintained proper accounting records and the consolidated financial statements are in agreement therewith. We have reviewed the accompanying Chairman's Statement and confirm that the information contained therein is consistent with the consolidated financial statements.

To the best of our knowledge and belief, no violations of the provisions of the Bahrain Commercial Companies Law 1975 (as amended), or the Bahrain Monetary Agency Law 1973 (as amended), or the terms of the banking licence or Agreement of Establishment and Articles of Association have occurred during the year that might have had a material adverse effect on the business of Gulf International Bank B.S.C. or on its financial position. Satisfactory explanations and information were provided by management in response to all our requests.



KPMG

Public Accountants

Manama, Bahrain

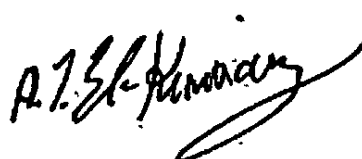
7th February 2001

	Note	At 31 12 00 US\$ millions	At 31 12 99 US\$ millions
Assets			
Cash and Other Liquid Assets	3	137.3	502.1
Placements with Banks	4	3,065.0	4,694.6
Trading Securities	5	465.8	535.8
Investment Securities	6	7,062.1	5,451.4
Loans and Advances	7	3,923.1	4,038.0
Fixed Assets	8	27.2	29.5
Other Assets	9	439.0	428.0
Total Assets		15,119.5	15,679.4
Liabilities			
Deposits from Banks	11	6,514.5	5,959.0
Deposits from Customers	11	4,900.0	5,503.4
Securities Sold under Agreements to Repurchase		1,164.6	1,707.7
Securities Sold but not yet Purchased		44.5	107.1
Other Liabilities	12	440.1	514.5
Term Financing	13	850.0	750.0
Total Liabilities		13,913.7	14,541.7
Shareholders' Equity			
Share Capital	14	1,000.0	1,000.0
Reserves	14	205.8	137.7
Shareholders' Equity		1,205.8	1,137.7
Total Liabilities & Shareholders' Equity		15,119.5	15,679.4

The consolidated financial statements were approved by the Board of Directors on 7th February 2001 and signed on their behalf by



Abdulla Hassan Salf
Chairman



Dr. Abdullah I El-Kuwaiz
General Manager

The notes on pages 38 to 67 form part of these consolidated financial statements

Consolidated Statement of Income

		Year Ended 31 12 00 US\$ millions	Year Ended 31 12 99 US\$ millions
Note			
	Interest Income		
	Interest and Fees on Loans	319.2	285.2
	Interest on Securities	424.3	293.4
	Interest on Placements and Other Liquid Assets	230.6	180.7
		974.1	759.3
	Interest Expense	804.4	619.7
	Net Interest Income	169.7	139.6
	Provision for Investment Securities	6 (13.8)	(0.4)
	Provision for Loan Losses	7 (22.4)	(24.6)
	Net Interest Income after Provisions	133.5	114.6
	Other Income	16 127.3	77.4
	Net Interest and Other Income	260.8	192.0
	Operating Expenses		
	Staff	83.5	60.1
	Premises	10.8	9.5
	Restructuring Costs	17 –	11.7
	Other	38.0	28.6
		132.3	109.9
	Net Income before Tax and effect of change in accounting policy	128.5	82.1
	Net effect of change in accounting policy	18 –	(13.9)
	Net Income before Tax	128.5	68.2
	Taxation on Overseas Activities	19 (10.4)	(0.6)
	Net Income after Tax	118.1	67.6
	Earnings per share	31 US\$0.12	US\$0.07

The notes on pages 38 to 67 form part of these consolidated financial statements

Consolidated Statement of Cash Flows

37

		Year Ended 31.12.00 US\$ millions	Year Ended 31.12.99 US\$ millions
	Note		
Operating Activities			
Net Income		118.1	67.6
Adjustments to reconcile Net Income to Net Cash Inflow from Operating Activities			
Provision for Loan Losses		22.4	24.6
Provision for Investment Securities		13.8	0.4
Restructuring Provision	17	–	10.0
Profit on Investment Securities		(27.6)	(3.9)
Amortisation of Investment Securities		6.9	9.6
Depreciation of Fixed Assets		13.0	7.8
Increase in accrued interest receivable		(59.4)	(77.8)
Increase in accrued interest payable		9.8	84.3
(Increase)/decrease in other net assets		(35.8)	58.7
Net decrease/(increase) in Trading Securities		70.0	(19.9)
Net Cash Inflow from Operating Activities		131.2	161.4
Investing Activities			
Net decrease/(increase) in Placements with Banks		1,629.6	(1,318.7)
Net decrease in Loans and Advances		92.5	396.2
Purchase of Investment Securities		(4,039.3)	(1,764.0)
Sale and maturity of Investment Securities		2,435.5	1,215.6
Acquisition of Subsidiary	32	–	52.1
Purchase of Fixed Assets		(10.7)	(11.6)
Net Cash Inflow/(Outflow) from Investing Activities		107.6	(1,430.4)
Financing Activities			
Net increase/(decrease) in Deposits from Banks		555.5	(604.6)
Net (decrease)/increase in Deposits from Customers		(603.4)	979.1
Net (decrease)/increase in Securities Sold under Agreements to Repurchase		(543.1)	1,220.8
Net decrease in Securities Sold but not yet Purchased		(62.6)	(140.8)
Net increase in Term Financing		100.0	–
Dividends paid		(50.0)	(45.0)
Net Cash (Outflow)/Inflow from Financing Activities		(603.6)	1,409.5
(Decrease)/increase in Cash and Cash Equivalents		(364.8)	140.5
Cash and Cash Equivalents at 1st January		502.1	361.6
Cash and Cash Equivalents at 31st December		137.3	502.1

Cash and Cash Equivalents comprise Cash and Other Liquid Assets

The notes on pages 38 to 67 form part of these consolidated financial statements

Notes to the Consolidated Financial Statements

for the year ended 31st December 2000

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 State of Bahrain by Amiri Decree Law No 30 dated 24th November 1975 and is registered as an offshore banking unit with the Bahrain Monetary Agency. The registered office of the Bank is located at Al-Dowali Building, 3 Palace Avenue, Manama, 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 seven countries worldwide. The total number of staff employed by the Group at the end of the financial year was 615.

The ultimate parent company of the Group is Gulf Investment Corporation G S C (GIC), an international investment company registered in the State of Kuwait and owned equally by the governments of the six member states of the Gulf Cooperation Council (GCC) - Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates. The issued share capital of the Bank is owned by GIC (72.5 per cent), the Saudi Arabian Monetary Agency (22.2 per cent) and JP Morgan Overseas Capital Corporation (5.3 per cent).

2 Accounting Policies

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

2.1 Basis of Presentation

The consolidated financial statements have been prepared in accordance with International Accounting Standards (IAS) and Interpretations of the Standing Interpretations Committee. The consolidated financial statements have been prepared under the historical cost convention as modified by the revaluation of trading instruments as explained in more detail in the following accounting policies. 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. A subsidiary is an entity in which the Bank holds, directly or indirectly, more than one half of the voting rights, or in which it otherwise exercises effective control. The results of subsidiaries acquired during the year are consolidated from the effective date of acquisition. The acquisition of subsidiaries are accounted for using the purchase method. Where necessary, accounting policies for subsidiaries are changed to ensure consistency with the policies applied by the Bank. All inter-company balances and transactions, including unrealised gains and losses on transactions between Group companies, have been eliminated.

The financial effect of the acquisition of subsidiaries is set out in Note 32. A listing of the principal subsidiaries is set out in Note 33.

2.3 Trade and Settlement Date Accounting

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

2.4 Foreign Currencies

The reporting currency of the Group is the US Dollar. The share capitals of the Bank and its principal subsidiaries are also denominated in US Dollars. Transactions in foreign currencies are converted to US Dollars at the rate of exchange prevailing at the date of the transaction. Foreign currency monetary assets and liabilities are translated into US Dollars at market rates of exchange prevailing on the balance sheet date. Realised and unrealised foreign exchange profits and losses are included in Other Income.

2.5 Offsetting

Financial assets and liabilities are only offset and the net amount reported in the Balance Sheet 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.

2.6 Derivative Financial Instruments

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 and equity markets. Derivative financial instruments are used to satisfy the requirements of customers, for proprietary trading purposes and to hedge exposures to interest rate, currency and other risks. In order for a derivative instrument to be classified as a hedge it must match or eliminate the market risk inherent in the asset or liability being hedged. Details of the Group's risk management policies in respect of derivative financial instruments are set out in Note 25.

Derivative financial instruments entered into for trading purposes or to hedge other trading positions are marked-to-market with associated gains and losses included in Other Income. Market values are obtained from quoted market prices, discounted cash flow models and option pricing models as appropriate.

Gains and losses on derivative financial instruments entered into for hedging purposes, other than those referred to above, are deferred and recognised in Interest Income or Interest Expense on an amortisation basis over the lives of the hedged assets or liabilities.

2.7 Interest Income and Interest Expense

Interest income and interest expense are recognised on an accruals basis. Interest income is suspended when 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.

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 Balance Sheet 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. Securities Purchased under Agreements to Resell are reported in Cash and Other Liquid Assets.

2 Accounting Policies continued

2.9 Securities

Trading Securities and Securities Sold but not yet Purchased are stated at fair value. Realised and unrealised gains and losses are reported in Other Income. Interest earned on Trading Securities and interest incurred on Securities Sold but not yet Purchased are included in Interest Income and Interest Expense respectively.

Investment Securities, which comprise debt and equity securities which are intended to be held for the long term, are stated at cost, adjusted for the amortisation of premiums and accretion of discounts, less provisions for credit losses. Premiums and discounts on debt securities are amortised and accreted respectively to Interest Income over the period to the maturity of the related securities.

Dividends received on Trading and Investment Securities are included separately in Other Income.

Bonds received in settlement of sovereign debt interest and principal claims are capitalised at the same net book value as other debt obligations of that country. The capitalised amount of bonds received in settlement of interest claims is included in Interest Income.

2.10 Loans and Advances

Loans and Advances are stated net of provisions for credit losses.

Loans 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.

2.11 Provisions for Credit Losses

Provisions for credit losses comprise both specific and general provisions. Specific provisions are maintained to cover identified potential losses and diminution in the value of investments which is other than temporary. Specific provisions in respect of troubled sovereign exposures are determined with reference to relevant regulatory authority guidelines. Specific provisions in respect of other credit exposures are made to the full extent of the estimated potential loss or diminution in value which is other than temporary. General provisions are maintained to cover potential losses which are considered to be present in the credit portfolio although as yet have not been specifically identified. Provisions for credit losses are deducted from the relevant asset category.

2.12 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.

2.13 Fixed Assets

Land is stated at cost. Other fixed assets are stated at cost less accumulated depreciation. Depreciation is computed on a straight line basis over the estimated useful life of each asset category as follows:

Buildings	–	Ten years
Installations	–	Four years or period of lease if longer
Office Furniture	–	Six years
Office Equipment	–	Four years
Motor Vehicles	–	Three years

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 programs beyond their original specifications and lives is recognised as a capital improvement and capitalised as part of the original cost of the software.

2.14 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 charged to income in the year to which they relate.

The pension contributions 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. The contributions are determined by a qualified actuary on the basis of a full valuation of the plan conducted every three years. Net balance sheet assets, representing the excess of the fair value of the plan assets over the present value of the defined benefit obligation, are limited to the present value of reductions in future contributions to the plan.

2.15 Deferred Income Taxes

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

2.16 Fiduciary Activities

The Group administers and manages assets owned by clients which are not reflected in the Consolidated Balance Sheet. Asset management fees are earned for providing investment management services and mutual fund products. Asset administration fees are earned for providing custodial services. Fees are recognised as the services are provided and are included in Other Income.

2.17 Comparatives

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

3 Cash and Other Liquid Assets

	31.12.00 US\$ millions	31.12.99 US\$ millions
Cash and Balances with Banks	67.8	156.6
Certificates of Deposit	68.0	169.2
Treasury Bills	1.5	123.0
Securities Purchased under Agreements to Resell	—	47.3
Money Market Funds	—	6.0
	137.3	502.1

Notes to the Consolidated Financial Statements continued

for the year ended 31st December 2000

4 Placements with Banks

Placements with Banks at 31st December 2000 included placements with non-bank financial institutions amounting to US\$146.9 million (1999 US\$154.9 million)

5 Trading Securities

	31.12.00 US\$ millions	31.12.99 US\$ millions
Government bonds	69.9	10.0
Listed debt securities	236.8	338.1
Unlisted debt securities	11.2	84.9
Managed funds	108.7	86.8
Equities	39.2	16.0
	465.8	535.8

The externally managed funds provide a diversified exposure to foreign exchange and international debt markets

6 Investment Securities

a) Classification of Investment Securities

	31.12.00		31.12.99	
	Book Value US\$ millions	Market Value US\$ millions	Book Value US\$ millions	Market Value US\$ millions
AAA/Aaa rated debt securities	1,447.2	1,444.5	1,122.6	1,111.6
Debt securities of other investment grade issuers	4,221.9	4,190.6	3,188.0	3,183.4
Other debt securities	962.5	904.4	765.3	768.9
Equities and equity funds	430.5	433.2	375.5	392.2
	7,062.1	6,972.7	5,451.4	5,456.1

The market value of Investment Securities at 31st December 2000 included net unrealised losses on securities of US\$45.2 million (1999 US\$23.5 million loss) and net unrealised losses of US\$44.2 million (1999 US\$28.2 million gain) on interest rate swaps used to convert fixed rate securities to a floating rate basis

Debt securities of other investment grade issuers at 31st December 2000 included GCC country government securities of US\$588.4 million (31st December 1999 US\$324.9 million)

b) Provisions for Investment Securities

The movements in the provisions for investment securities were as follows

	2000			1999		
	Specific US\$ millions	General US\$ millions	Total US\$ millions	Specific US\$ millions	General US\$ millions	Total US\$ millions
At 1st January	27.4	22.2	49.6	37.5	22.1	59.6
Transfer	21.3	(21.3)	—	—	—	—
Amounts utilised	(38.3)	(0.9)	(39.2)	—	—	—
Transfer to loan provisions	—	—	—	(10.4)	—	(10.4)
Charge for the year	13.8	—	13.8	0.3	0.1	0.4
At 31st December	24.2	—	24.2	27.4	22.2	49.6

In preparation for the implementation of IAS No 39 – Financial Instruments Recognition and Measurement on 1st January 2001, the unutilised general security provision was transferred to specific security provisions and allocated to individual security holdings which were deemed to be impaired. Concurrently, the carrying amounts of impaired marketable securities were written down to their recoverable amounts. The recoverable amounts were determined with reference to quoted market prices. Specific investment security provisions at 31st December 2000 comprised provisions for impairment against unquoted and illiquid investments and sovereign-related provisions determined with reference to regulatory authority guidelines.

During 1999, specific investment security provisions of US\$10.4 million were transferred to specific loan provisions on the reclassification of the related exposures following the finalisation of a formal refinancing agreement.

7 Loans and Advances

	31 12 00 US\$ millions	31 12 99 US\$ millions
Gross Loans and Advances	4,716.0	4,876.5
Provisions for Loan Losses	(792.9)	(838.5)
Net Loans and Advances	3,923.1	4,038.0

a) Concentrations of Loans and Advances

Net Loans and Advances at 31st December 2000 included exposure to GCC country governments of US\$520.6 million (1999 US\$753.5 million) and OECD country central government and agency risk of US\$205.4 million (1999 US\$262.5 million). There were no significant concentrations by industrial sector at 31st December 2000 and at 31st December 1999.

b) Provisions for Loan Losses

The movements in the provisions for loan losses were as follows:

	2000			1999		
	Specific US\$ millions	General US\$ millions	Total US\$ millions	Specific US\$ millions	General US\$ millions	Total US\$ millions
At 1st January	643.7	194.8	838.5	601.8	177.6	779.4
Arising on Acquisition	–	–	–	5.9	15.3	21.2
Exchange rate and other movements	(14.7)	–	(14.7)	3.5	0.4	3.9
Amounts utilised	(53.3)	–	(53.3)	(1.0)	–	(1.0)
Transfer from investment security provisions	–	–	–	10.4	–	10.4
Charge for the year	26.5	(4.1)	22.4	23.1	1.5	24.6
At 31st December	602.2	190.7	792.9	643.7	194.8	838.5

During 1999, specific investment security provisions of US\$10.4 million were transferred to specific loan provisions on the reclassification of the related exposures following the finalisation of a formal refinancing agreement.

Notes to the Consolidated Financial Statements continued

for the year ended 31st December 2000

7 Loans and Advances continued

c) Non-Performing Loans

The gross and net book values of loans on which interest was not being accrued were as follows

	31 12 00		31 12 99	
	Gross	Net Book Value	Gross	Net Book Value
	US\$ millions	US\$ millions	US\$ millions	US\$ millions
Sovereign	417.6	0.7	461.5	3.3
Corporate	132.6	54.5	121.5	54.5
Financial Institutions	10.8	2.4	12.2	3.0
	561.0	57.6	595.2	60.8

The overdue status of non-performing loans based on original contractual maturities was as follows

	31 12 00	31 12 99
	US\$ millions	US\$ millions
Within 6 months	60.0	48.1
Month 7 to 1 year	6.1	8.5
2 to 5 years	30.0	31.0
Over 5 years	464.9	507.6
	561.0	595.2

d) Interest in Suspense

The movements in interest in suspense were as follows

	2000	1999
	US\$ millions	US\$ millions
At 1st January	414.6	379.0
Arising on Acquisition	—	1.3
Net interest suspended	21.5	39.3
Interest written off	(4.3)	(1.7)
Exchange rate movements	1.1	(3.3)
At 31st December	432.9	414.6

8 Fixed Assets

	Freehold Land	Buildings	Premises and Equipment	Total
	US\$ millions	US\$ millions	US\$ millions	US\$ millions
At 31st December 2000				
Cost	8.9	27.2	63.5	99.6
Accumulated Depreciation	—	26.8	45.6	72.4
Net Book Value	8.9	0.4	17.9	27.2
At 31st December 1999				
Net Book Value	8.9	0.5	20.1	29.5

9 Other Assets

	31 12 00	31 12 99
	US\$ millions	US\$ millions
Accrued interest, fees and commissions	267.5	208.1
Derivative related amounts	106.7	140.8
Prepaid pension cost	19.5	21.3
Other prepayments	3.2	6.4
Other, including accounts receivable	42.1	51.4
	439.0	428.0

Derivative related amounts represent the positive fair values of derivative financial instruments entered into for trading purposes and deferred losses on derivatives designated as hedges

10 Post-Retirement Benefits

The Group contributes to defined benefit and defined contribution pension plans which cover substantially all 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 2000 amounted to US\$3.5 million (1999: US\$3.5 million).

The Bank's principal subsidiary, Gulf International Bank (UK) Limited (GIBUK), maintains a defined benefit pension plan for substantially all its employees. The assets of the plan are held independently of the subsidiary's assets in a separate trustee administered fund. The pension contributions are charged to the income statement so as to spread the regular cost of the pensions over the service lives of employees. The contributions are determined on the basis of a full valuation of the plan conducted by an independent, qualified actuary every three years using the projected unit credit method. The latest actuarial valuation was carried out at 1st January 2001.

The amount recognised in the Consolidated Balance Sheet is analysed as follows:

	31.12.00	31 12 99
	US\$ millions	US\$ millions
Fair value of plan assets	76.0	86.0
Present value of fund obligations	61.4	53.5
	14.6	32.5
Unrecognised actuarial loss / (gain)	4.9	(11.2)
Net Asset in the Consolidated Balance Sheet	19.5	21.3

The net asset recognised in the Consolidated Balance Sheet is limited to the present value of the estimated benefits available in the form of reductions in future contributions to the plan.

Notes to the Consolidated Financial Statements continued

for the year ended 31st December 2000

10 Post-Retirement Benefits continued

The movement in the net asset recognised in the Consolidated Balance Sheet was as follows

	2000 US\$ millions	1999 US\$ millions
At 1st January	21.3	—
Arising on Acquisition	—	21.8
Net expense included in Staff Expenses	(1.8)	(0.5)
At 31st December	19.5	21.3

The amounts recognised in the Consolidated Income Statement were as follows

	2000 US\$ millions	1999 US\$ millions
Current service cost	4.5	3.6
Interest cost	3.3	2.0
Expected return on plan assets	(6.0)	(5.1)
Total included in Staff Expenses	1.8	0.5

The principal actuarial assumptions used for accounting purposes were as follows

	2000	1999
Discount rate	5.5%	5.5%
Expected return on plan assets	7.0%	7.0%
Future salary increases	4.5%	4.5%

11 Deposits

The geographical composition of total deposits was as follows

	31.12.00 US\$ millions	31.12.99 US\$ millions
GCC countries	7,043.5	7,413.5
Other countries	4,371.0	4,048.9
	11,414.5	11,462.4

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

Deposits from Customers include deposits from central banks

12 Other Liabilities

	31.12.00 US\$ millions	31.12.99 US\$ millions
Accrued interest	195.0	185.2
Derivative related amounts	148.9	137.9
Deferred items	28.6	17.7
Overseas taxation	9.3	3.2
Outstanding security settlements	7.1	124.0
Restructuring provision	5.8	10.0
Other, including accounts payable and accrued expenses	45.4	36.5
	440.1	514.5

Derivative related amounts represent the negative fair values of derivative financial instruments entered into for trading purposes and deferred profits on derivatives designated as hedges

13 Term Financing

	31.12.00 US\$ millions	31.12.99 US\$ millions
US\$ Floating rate loan due between 2001 and 2003	250.0	250.0
US\$ Floating rate note due in 2002	200.0	200.0
US\$ Floating rate loan due in 2005	400.0	–
US\$ Floating rate loan due in 2000	–	300.0
	850.0	750.0

14 Shareholders' Equity

The movements in Shareholders' Equity were as follows

	Share Capital US\$ millions	Share Premium US\$ millions	Compulsory Reserve US\$ millions	Voluntary Reserve US\$ millions	Retained Earnings US\$ millions	Total US\$ millions
At 1st January 1999	450.0	–	62.5	62.5	201.0	776.0
Dividends for 1998	–	–	–	–	(45.0)	(45.0)
Capitalisation of Reserves	218.5	–	–	(62.5)	(156.0)	–
Issue of new shares	254.0	85.1	–	–	–	339.1
Capitalisation of Share Premium	77.5	(77.5)	–	–	–	–
Net Income for the year	–	–	–	–	67.6	67.6
Transfers from Retained Earnings	–	–	6.9	6.9	(13.8)	–
At 31st December 1999	1,000.0	7.6	69.4	6.9	53.8	1,137.7
Dividends for 1999	–	–	–	–	(50.0)	(50.0)
Net Income for the year	–	–	–	–	118.1	118.1
Transfers from Retained Earnings	–	–	8.7	8.7	(17.4)	–
At 31st December 2000	1,000.0	7.6	78.1	15.6	104.5	1,205.8

Notes to the Consolidated Financial Statements continued

for the year ended 31st December 2000

14 Shareholders' Equity continued

The Authorised Share Capital at 31st December 2000 comprised 3.0 billion shares of US\$1 each (31st December 1999 3.0 billion shares of US\$1 each). The Issued Share Capital at 31st December 2000 comprised 1.0 billion shares of US\$1 each (31st December 1999 1.0 billion shares of US\$1 each). All issued shares are fully paid.

On 8th April 1999 the Bank acquired all the issued shares in Gulf International Bank (UK) Limited (GIBUK), formerly Al-Bank Al-Saudi Al-Alami Limited (Saudi International Bank – SIB), a bank incorporated in the United Kingdom. In conjunction with the acquisition, 224.1 million shares of US\$1 each were issued in exchange for GIBUK's shares held by the Saudi Arabian Monetary Agency and JP Morgan Overseas Capital Corporation. The remaining shares in GIBUK were acquired for cash. An additional 29.9 million shares of US\$1 each were also issued in consideration for the transfer of a subordinated loan extended to GIBUK by one of its previous shareholders. The 254.0 million new shares were issued at a premium of US\$0.335 per share, amounting in total to US\$85.1 million. Immediately prior to the acquisition, the Voluntary Reserve and Retained Earnings at 1st January 1999, amounting to US\$62.5 million and US\$156.0 million respectively, were capitalised in the form of 218.5 million shares of US\$1 each. Following the acquisition, US\$77.5 million of the Share Premium arising on the issue of the new shares was capitalised in the form of 77.5 million shares of US\$1 each.

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. No transfers are made in respect of the net profit of the Bank's principal subsidiary, GIBUK. Transfers to the non-distributable Compulsory Reserve are required until such time as this reserve represents 25 per cent of the issued share capital of the Bank. The Voluntary Reserve may be utilised at the discretion of the Board of Directors.

15 Dividends

Dividends are not accounted for until they have been ratified at the General Assembly meeting. The dividend ratified in respect of 2000 will be accounted for in Shareholders' Equity as an appropriation of Retained Earnings in the year ending 31st December 2001.

16 Other Income

	2000 US\$ millions	1999 US\$ millions
Profit on Trading Securities	38.9	23.6
Dividend Income	28.5	26.8
Profit on Investment Securities	27.6	3.9
Investment Banking and Management Fees	13.9	7.0
Profit on Foreign Exchange	7.5	5.5
Commissions on Letters of Credit and Guarantee	6.6	7.5
Profit on partial sale of Associated Company	3.0	–
Fee and Sundry Income	1.3	0.9
Loan Recoveries	–	2.2
	127.3	77.4

17 Restructuring Costs

Net Income for the year ended 31st December 1999 included a pre-tax charge of US\$11.7 million in connection with initiatives to reorganise and streamline support functions and realign certain business activities following the acquisition of GIBUK. The charge included a US\$10.0 million provision in respect of costs that were anticipated to be incurred on the basis of a formal plan approved by the Bank's Board of Directors. These costs related to planned staff reductions and the write-off of certain fixed assets. The full amount of costs estimated to be incurred was recognised as a restructuring provision in 1999. The restructuring process was substantially completed during 2000. However, certain related costs are to be incurred in 2001. The restructuring provision is included in Other Liabilities in the Consolidated Balance Sheet.

18 Change in Accounting Policy of Subsidiary

During 1999 a newly acquired subsidiary, GIBUK, changed its accounting policy in respect of interest rate-related derivative financial instruments in order to conform with the policy applied by the Bank. Under the previous policy applied by GIBUK, the net interest on interest rate-related derivative financial instruments entered into for longer-term investment objectives was recognised in Interest Income or Interest Expense over the life of the instruments. Following the change in policy, all derivative financial instruments, other than those utilised for hedging purposes, are marked-to-market. The change in accounting policy was applied retrospectively. The impact of the change, had it been adopted prior to the date of acquisition on 8th April 1999, would not have been material to the results of operation or financial position of GIBUK as at that date. The cumulative net effect of the change, which is reported as a separate component in the income statement, was to reduce the pre-tax operating profit for 1999 by US\$13.9 million.

19 Deferred Income Taxes

Deferred income tax assets are recognised for tax loss carry forward purposes only to the extent that the realisation of the related tax benefit is probable. A Group subsidiary company has tax losses carried forward to apply against future taxable income. The benefit of these tax losses has not been recognised in the consolidated financial statements due to the uncertainty of their recovery.

20 Segmental Information

Segmental information is presented in respect of the Group's business and geographical segments. The primary reporting format, business segments, is based on the products and services provided or the type of customer serviced and reflects the manner in which financial information is evaluated by management and the Board of Directors.

a) Business Segments

For financial reporting purposes the Group is organised into three main business segments:

- Corporate and Institutional Banking – the provision of wholesale commercial financing and other credit facilities for corporate and institutional customers
- Treasury and Financial Markets – the provision of a broad range of treasury and capital market products and services to corporate and financial institution clients, money market, proprietary trading and investment activities and the management of the Group's balance sheet, including funding
- Investment Management and Banking – the provision of investment management and financial advisory services, including asset management and services relating to structured financing, privatisations, IPO's and mergers and acquisitions

Notes to the Consolidated Financial Statements continued

for the year ended 31st December 2000

20 Segmental Information continued

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 the Group's consolidated financial statements as 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. The 'Corporate and Other' category comprises items which are not directly attributable to specific business segments, including investments of a strategic nature and the investment of, and earnings on, the Group's net free capital. Unallocated overheads and exceptional charges are reported separately.

The business segment analysis is as follows:

	Corporate and Institutional Banking US\$ millions	Treasury and Financial Markets US\$ millions	Investment Management and Banking US\$ millions	Corporate and Other US\$ millions	Total US\$ millions
2000					
Net Interest and Other Income	60.1	111.4	10.0	79.3	260.8
Segment result	46.1	85.7	0.6	79.3	211.7
Unallocated Overhead					(83.2)
Taxation on Overseas Activities					(10.4)
Net Income after Tax					118.1
Segment Assets	5,228.6	9,478.0	3.1	409.8	15,119.5
Segment Liabilities	—	12,967.5	—	946.2	13,913.7
Shareholders' Equity					1,205.8
Total Liabilities and Shareholders' Equity					15,119.5
1999					
Net Interest and Other Income	50.9	73.2	6.4	61.5	192.0
Segment result	38.7	52.6	(0.7)	61.5	152.1
Unallocated Overhead					(58.3)
Restructuring Costs					(11.7)
Net effect of change in accounting policy					(13.9)
Taxation on Overseas Activities					(0.6)
Net Income after Tax					67.6
Segment Assets	5,017.8	10,207.0	5.0	449.6	15,679.4
Segment Liabilities	—	13,301.2	—	1,240.5	14,541.7
Shareholders' Equity					1,137.7
Total Liabilities and Shareholders' Equity					15,679.4

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 Net Interest and Other Income based on the location in which transactions are booked and income is recorded was as follows:

	2000 US\$ millions	1999 US\$ millions
GCC countries	129.6	126.0
Other countries	131.2	66.0
	260.8	192.0

The geographical analyses of deposits and risk assets are set out in Notes 11 and 22 respectively.

21 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. All significant risk management policies are approved by the Board of Directors. A Group Risk Committee oversees the management and control of all the risks involved in the Group's businesses. 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 review 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 commented on as follows:

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

The geographical distribution of risk assets is set out in Note 22. An analysis of the credit risk in respect of foreign exchange and derivative financial instruments is set out in Note 25 (a) while the notional and risk-weighted exposures for credit-related financial instruments are detailed in Note 25 (b).

21 Risk Management continued

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 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. 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. The Group supplements daily VaR calculations with portfolio stress testing which measures the impact of simulated abnormal changes in market rates and prices on the market values of the portfolios. It is recognised that VaR is not a measure of the absolute limit of market risk and that losses in excess of the VaR amounts will, on occasion, arise. The composition of the debt and equity trading securities is set out in Note 5. An analysis of derivative financial instruments, including the VaR of foreign exchange and derivative trading contracts, is set out in Note 25 (a).

The VaR by risk class for the Group's trading positions, as calculated in accordance with the basis set out in Note 27, was as follows:

	31.12.00	2000 Average
	US\$ millions	US\$ millions
Interest rate risk	3.5	4.2
Foreign exchange risk	1.1	1.7
Equity risk	8.5	4.3

- **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 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 assets and liabilities is set out in Note 24. The Group does not maintain material non-trading foreign currency open positions. In general, the policy is to match 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 25 (a).

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

Liquidity Risk

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 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 maturity profile of assets and liabilities is set out in Note 23. An analysis of investment securities by rating classification is set out in Note 6 (a).

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.

Notes to the Consolidated Financial Statements continued

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22 Geographical Distribution of Risk Assets

	31 12 00				31 12 99	
	Placements & Other Liquid Assets	Securities	Loans and Advances	Credit-related Contingent Items	Total	Total
	US\$ millions	US\$ millions	US\$ millions	US\$ millions	US\$ millions	US\$ millions
GCC	938.5	626.4	2,376.4	918.3	4,859.6	4,670.1
Other Middle East & North Africa	123.8	100.9	298.2	99.4	622.3	677.0
Europe	1,402.5	3,630.4	600.0	491.2	6,124.1	7,039.1
North America	280.7	2,612.8	348.4	918.8	4,160.7	3,969.4
Japan & Other Asia	456.8	455.6	290.6	139.6	1,342.6	1,469.2
Latin America	—	101.8	9.5	0.1	111.4	141.5
	3,202.3	7,527.9	3,923.1	2,567.4	17,220.7	17,966.3

An analysis of derivative and foreign exchange instruments is set out in Note 25 (a)

23 Maturities of Assets and Liabilities

The maturity profile of assets and liabilities based on the remaining period to the contractual maturity date was as follows

	Within 3 months	Month 4 to 1 year	Years 2 and 3	Years 4 and 5	Over 5 years and other	Total
	US\$ millions	US\$ millions	US\$ millions	US\$ millions	US\$ millions	US\$ millions
At 31st December 2000						
Cash and Other Liquid Assets	84.3	53.0	—	—	—	137.3
Placements	2,795.4	269.6	—	—	—	3,065.0
Securities	563.6	703.4	1,128.8	1,210.6	3,921.5	7,527.9
Loans and Advances	1,058.7	725.8	953.9	582.3	602.4	3,923.1
Fixed & Other Assets	309.8	70.4	—	—	86.0	466.2
Total Assets	4,811.8	1,822.2	2,082.7	1,792.9	4,609.9	15,119.5
Deposits	9,796.6	1,481.5	136.4	—	—	11,414.5
Securities Sold under						
Agreements to Repurchase	1,164.6	—	—	—	—	1,164.6
Securities Sold but not						
yet Purchased	44.5	—	—	—	—	44.5
Other Liabilities	321.9	33.2	0.1	—	84.9	440.1
Term Financing	—	100.0	350.0	400.0	—	850.0
Shareholders' Equity	—	—	—	—	1,205.8	1,205.8
Liabilities & Shareholders' Equity	11,327.6	1,614.7	486.5	400.0	1,290.7	15,119.5
At 31st December 1999						
Total Assets	7,460.2	1,556.1	1,996.9	1,743.1	2,923.1	15,679.4
Liabilities & Shareholders' Equity	12,033.9	1,823.5	301.8	250.0	1,270.2	15,679.4

The asset and liability maturities 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. Counterparties each with deposits over US\$10 million at 31st December 2000 had average deposits throughout 2000 amounting to US\$8,511 million (1999 US\$8,171 million). Formal liquidity controls are nevertheless based on contractual asset and liability maturities.

24 Interest Rate Risk

The repricing profile and effective interest rates of the various asset and liability categories were as follows

	Within 3 months	Months 4 to 6	Months 7 to 12	Over 1 year	Non-interest bearing items	Total	Effective interest rates %
	US\$ millions	US\$ millions	US\$ millions	US\$ millions	US\$ millions	US\$ millions	
At 31st December 2000							
Cash and Other Liquid Assets	84.3	3.0	50.0	–	–	137.3	3.39
Placements	2,333.4	161.8	244.8	325.0	–	3,065.0	6.33
Trading Securities	317.9	–	–	–	147.9	465.8	2.83
Investment Securities							
– Fixed Rate	35.2	67.1	4.1	271.2	–	377.6	5.32
– Floating Rate	5,118.5	1,092.5	43.0	–	–	6,254.0	7.04
– Equities & Equity Funds	–	–	–	–	430.5	430.5	–
Loans and Advances	2,979.9	1,044.1	82.5	7.3	(190.7)	3,923.1	8.14
Fixed & Other Assets	–	–	–	–	466.2	466.2	–
Total Assets	10,869.2	2,368.5	424.4	603.5	853.9	15,119.5	
Deposits	9,784.0	987.3	566.8	76.4	–	11,414.5	6.28
Securities Sold under Agreements to Repurchase	1,164.6	–	–	–	–	1,164.6	6.42
Securities Sold but not yet Purchased	44.5	–	–	–	–	44.5	3.45
Other Liabilities	–	–	–	–	440.1	440.1	–
Term Financing	850.0	–	–	–	–	850.0	7.17
Shareholders' Equity	–	–	–	–	1,205.8	1,205.8	–
Liabilities & Shareholders' Equity	11,843.1	987.3	566.8	76.4	1,645.9	15,119.5	
Balance Sheet Items	(973.9)	1,381.2	(142.4)	527.1	(792.0)	–	
Off-Balance Sheet Items	(496.5)	141.0	306.7	48.8	–	–	
Interest Rate Sensitivity Gap	(1,470.4)	1,522.2	164.3	575.9	(792.0)	–	
Cumulative Interest Rate							
Sensitivity Gap	(1,470.4)	51.8	216.1	792.0	–	–	
At 31st December 1999							
Cumulative Interest Rate							
Sensitivity Gap	(1,647.6)	(51.8)	(46.9)	933.4	–	–	

The repricing profile is based on the remaining period to the next interest repricing date. The repricing profiles of securities and loans incorporate the effect of interest rate swaps used to modify the interest rate characteristics of specific transactions. The repricing profile of Placements incorporates the effect of interest rate swaps used to lock-in a return on the Group's net free capital funds. Interest rate swaps and forward rate agreements that have been used for asset and liability management purposes to hedge overall exposure to interest rate risk are included separately as Off-Balance Sheet Items. Their impact on effective interest rates is reflected in Deposits. The general provisions for securities and loan losses are deducted from non-interest bearing assets.

24 Interest Rate Risk continued

The substantial majority of assets and liabilities reprice within one year. Accordingly there is a limited exposure to interest rate risk. The investment of the Group's net free capital by means of fixed receive interest rate swaps or fixed rate securities represents the principal interest rate risk beyond one year. At 31st December 2000 the modified duration of these portfolios was 1.45 (1999 2.47). 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 portfolios was US\$137,000 (1999 US\$349,000).

The market risk relating to derivative and foreign exchange instruments is set out in Note 25 (a).

25 Off-Balance Sheet Financial Instruments

a) 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) activities 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 and equity 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 exposures 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 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.

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

Product Analysis

	Trading	Notional Amounts		Credit Risk
	US\$ millions	ALM US\$ millions	Total US\$ millions	Amounts US\$ millions
At 31st December 2000				
Foreign Exchange Contracts				
Unmatured Spot, Forward and Futures contracts	2,537.1	1,235.6	3,772.7	88.7
Options purchased	196.5	—	196.5	6.2
Options written	186.3	—	186.3	—
Total	2,919.9	1,235.6	4,155.5	94.9
Interest Rate Contracts				
Futures and Forward Rate Agreements	20,340.1	240.0	20,580.1	3.4
Interest Rate Swaps	10,832.4	3,304.0	14,136.4	161.8
Options, Caps and Floors purchased	10,112.8	16.0	10,128.8	54.2
Options, Caps and Floors written	11,094.5	5.0	11,099.5	—
Total	52,379.8	3,565.0	55,944.8	219.4
Equity Contracts				
Options purchased	8.9	—	8.9	—
Options written	—	—	—	—
Total	8.9	—	8.9	—
Total	55,308.6	4,800.6	60,109.2	314.3
At 31st December 1999				
Total	80,737.6	4,298.2	85,035.8	351.3

Financial Futures are exchange traded and therefore not subject to credit risk. There is no credit risk in respect of options, caps and floors written as they represent obligations of the Group.

Notes to the Consolidated Financial Statements continued

for the year ended 31st December 2000

25 Off-Balance Sheet Financial Instruments continued

a) Derivative and Foreign Exchange Instruments continued

Product Analysis continued

At 31st December 2000 the Value-at-Risk of the foreign exchange and interest rate-related derivative trading contracts analysed in the table set out on page 57, as calculated in accordance with the basis set out in Note 27, was US\$0.1 million and US\$2.3 million respectively (31st December 1999 US\$0.1 million and US\$3.0 million respectively). 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 set out on page 57.

Counterparty Analysis

			31.12.00	31.12.99
	Banks	Other	Total	Total
Credit Risk Amounts	US\$ millions	US\$ millions	US\$ millions	US\$ millions
OECD countries	290.8	9.8	300.6	332.0
GCC countries	7.7	5.6	13.3	19.3
Other countries	0.4	—	0.4	—
	298.9	15.4	314.3	351.3

Credit risk is concentrated on major OECD-based banks.

Maturity Analysis

	Year 1	Years 2 & 3	Years 4 & 5	Over 5 years	Total
Notional Amounts	US\$ millions	US\$ millions	US\$ millions	US\$ millions	US\$ millions
At 31st December 2000					
Foreign Exchange contracts	4,028.5	26.7	100.3	—	4,155.5
Interest Rate contracts	35,188.4	14,255.1	1,204.2	5,297.1	55,944.8
Equity contracts	8.9	—	—	—	8.9
Total	39,225.8	14,281.8	1,304.5	5,297.1	60,109.2
At 31st December 1999					
Total	60,545.1	12,430.3	7,734.2	4,326.2	85,035.8

The Group's derivative and foreign exchange activities are predominantly short-term in nature. Transactions with maturities over one year either represent hedging transactions entered into for asset and liability management purposes or fully offset customer transactions.

Significant Net Open Positions

At 31st December 2000 the Group had a US\$24.0 million long (1999: US\$26.2 million long) Omani Riyal net open currency position. This related to Omani Government investment security holdings.

There were no other significant derivative trading or foreign currency net open positions at 31st December 2000 and at 31st December 1999.

b) 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 Basle Committee on Banking Supervision.

	31.12.00		31.12.99	
	Notional Principal Amount US\$ millions	Risk- Weighted Exposure US\$ millions	Notional Principal Amount US\$ millions	Risk- Weighted Exposure US\$ millions
Direct credit substitutes	159.2	81.7	65.7	47.4
Transaction-related contingent items	762.3	357.4	1,031.1	448.2
Short term self-liquidating trade-related contingent items	146.8	20.9	366.7	44.0
Commitments, including undrawn loan commitments and note underwriting commitments under issuance and revolving facilities	1,499.1	503.4	1,280.9	467.3
	2,567.4	963.4	2,744.4	1,006.9

26 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.

Notes to the Consolidated Financial Statements continued

for the year ended 31st December 2000

27 Capital Adequacy

The risk asset ratio calculated in accordance with the capital adequacy guidelines of the Basle Committee on Banking Supervision was as follows

	31.12.00		31.12.99	
	US\$ millions		US\$ millions	
Capital Base				
Tier I Capital				
Shareholders' Equity	1,205.8		1,137.7	
Tier II Capital				
General provision subject to 1.25% risk-weighted exposure limitation	147.2		130.4	
Total Capital Base	(a) 1,353.0		1,268.1	
Risk-Weighted Exposure				
	Notional	Risk-	Notional	Risk-
	Principal	Weighted	Principal	Weighted
	Amount	Exposure	Amount	Exposure
	US\$ millions	US\$ millions	US\$ millions	US\$ millions
Credit Risk				
Balance Sheet Items				
Cash and Other Liquid Assets	137.3	27.1	502.1	87.2
Placements	3,065.0	694.5	4,694.6	1,031.6
Securities	7,527.9	5,520.0	5,987.2	3,985.7
Loans and Advances	3,923.1	3,279.3	4,038.0	3,336.3
Fixed & Other Assets	466.2	204.0	457.5	160.3
	15,119.5	9,724.9	15,679.4	8,601.1
Off-Balance Sheet Items				
Credit-related Contingent Items	2,567.4	963.4	2,744.4	1,006.9
Foreign Exchange-related Items	4,155.5	28.9	6,397.7	33.5
Interest Rate-related Items	55,944.8	79.1	78,636.5	100.1
Equity-related Items	8.9	—	—	—
	62,676.6	1,071.4	87,778.6	1,140.5
Credit Risk-weighted Exposure		10,796.3		9,741.6
Market Risk				
General market risk		576.7		412.2
Specific market risk		404.3		275.1
Market Risk-weighted Exposure		981.0		687.3
Total Risk-weighted Exposure		(b) 11,777.3		10,428.9
Risk Asset Ratio [(a)/(b) x 100]		11.5%		12.2%

The Group calculates the capital requirement for general market risk using a Value-at-Risk model in accordance with the provisions of the Amendment to the Capital Accord to Incorporate Market Risks issued by the Basle Committee in January 1996. 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 Bahrain Monetary Agency (BMA). The minimum multiplication factor to be applied to the Value-at-Risk calculated by the internal model has been set at 3.5 (31st December 1999/4) by the BMA.

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 calculated using the internal model. The resultant measure of market risk is multiplied by 12.5, the reciprocal of the 8 per cent minimum capital ratio, to give Market Risk-weighted Exposure on a basis consistent with Credit Risk-weighted Exposure.

With regard to credit risk, the risk-weighted exposures for foreign exchange transactions and interest rate-related off-balance sheet items are determined using the current exposure method. A credit conversion factor as determined by the Basle Committee is applied to the replacement cost of these contracts. The resultant amounts are then risk-weighted according to the classification of the counterparty.

28 Related Party Transactions

Banking transactions are conducted with the Group's ultimate parent company, Gulf Investment Corporation, in the normal course of business. These comprise standard wholesale money market and foreign exchange transactions that are conducted on an arm's length basis on commercial terms and conditions and at market rates.

	2000 US\$ millions	1999 US\$ millions
The following transactions were outstanding at 31st December of each year		
Placements with GIC	91.3	3.8
Deposits from GIC	43.1	32.8
Floating rate notes held by GIC	10.0	10.0
Forward foreign exchange transactions	–	20.0
Interest on transactions during the year was as follows		
Interest on Placements with GIC	4.1	2.3
Interest on Deposits from GIC	0.7	0.9
Interest on floating rate notes held by GIC	0.7	0.6

29 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 consolidated. The aggregate amount of the funds concerned at 31st December 2000 was US\$5,334.1 million (1999: US\$5,498.9 million).

30 Fair Value of Financial Instruments

The table set out on the next page compares the estimated fair values of all on- and off-balance sheet financial instruments with their respective book values. The Group's financial instruments are accounted for principally under the historical cost method. 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 can therefore 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 market prices or to the pricing prevailing for similar financial instruments and the use of estimation techniques such as discounted cash flow analysis.

Notes to the Consolidated Financial Statements continued

for the year ended 31st December 2000

30 Fair Value of Financial Instruments continued

	Book Value US\$ millions	Fair Value US\$ millions	(Shortfall)/ Excess US\$ millions
At 31st December 2000			
Assets			
Cash and Other Liquid Assets	137.3	137.3	-
Placements with Banks	3,065.0	3,065.0	-
Trading Securities	465.8	465.8	-
Investment Securities	7,062.1	6,972.7	(89.4)
Loans and Advances	3,923.1	3,947.9	24.8
Fixed & Other Assets	466.2	466.2	-
Liabilities			
Deposits	11,414.5	11,414.5	-
Securities Sold under Agreements to Repurchase	1,164.6	1,164.6	-
Securities Sold but not yet Purchased	44.5	44.5	-
Other Liabilities	440.1	440.1	-
Term Financing	850.0	850.0	-
Off-Balance Sheet Financial Instruments	-	-	-
Shortfall in Net Fair Values against Net Book Values			(64.6)
At 31st December 1999			
Excess of Net Fair Values over Net Book Values			42.7

Based on the valuation methodologies outlined below, the net fair values of all on- and off-balance sheet financial instruments were lower than their net book values as at 31st December 2000 by US\$64.6 million (1999 US\$42.7 million excess). The decrease in the fair value of Investment Securities reflected a general widening in credit spreads during 2000. The resultant shortfall in fair value represents only 1.3 per cent of the book value of Investment Securities. The classification of Investment Securities by credit rating category is set out in Note 6 (a). 80.3 per cent of Investment Securities at 31st December 2000 comprised debt securities of investment grade issuers.

a) Securities

The fair value of securities was based on quoted market prices with the exception of investments in unquoted equity investments, the fair values of which were estimated at attributable net asset value determined with reference to the most recent audited financial statements and the latest unaudited financial information available to shareholders.

b) Loans and Advances

The fair value of floating rate loans was principally estimated at book value less attributable specific provisions and the general provision for loan losses. The fair value of troubled sovereign debt was based on market bid prices. The fair value of fixed rate loans was 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. The repricing profile of Loans and Advances is set out in Note 24. All but US\$7.3 million (1999 US\$7.2 million) of Loans and Advances repriced within one year.

c) Term Financing

The fair value of term financing was based on book value as the financing is on a floating rate basis and as the applicable margins approximate the current spreads that would apply for borrowings with similar maturities. The term financing reprices at least semi-annually.

d) Other On-Balance Sheet Financial Instruments

The fair values of all other on-balance sheet financial instruments approximated their respective book values due to their short term nature.

e) Off-Balance Sheet Financial Instruments

Derivative financial instruments utilised for asset and liability management purposes were valued based on market prices and incorporated in the fair values of Placements, Securities, Loans and Advances and Deposits. The net unrealised loss on these contracts at 31st December 2000 amounted to US\$40.8 million (1999: US\$2.4 million loss).

The fair values of derivative trading and foreign exchange instruments were based on market prices. The market values of derivative trading and foreign exchange instruments are included in the book values of Other Assets and Other Liabilities.

No fair value adjustment was made with respect to 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 materially reflect contractual fees and commissions actually charged at the balance sheet date for agreements of similar credit standing and maturity. Specific provisions have been made in respect of individual transactions, where a potential for loss has been identified. Such provisions are included in provisions for loan losses.

31 Earnings Per Share

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

	2000	1999
Net Income after Tax (US\$ millions)	118.1	67.6
Weighted average number of shares in issue (millions)	1,000.0	911.9
Basic earnings per share	US\$0.12	US\$0.07

32 Acquisition of Subsidiary

a) Acquisition

On 8th April 1999 the Bank acquired all the issued shares of Gulf International Bank (UK) Limited (GIBUK), formerly Al-Bank Al-Saudi Al-Alami Limited, a bank incorporated in the United Kingdom, for a total consideration of US\$397.9 million. The purchase consideration was satisfied by the issue of US\$299.1 million of new shares and cash paid of US\$98.8 million. The acquisition cost equated to the fair values of the identified net assets acquired and accordingly no goodwill arose on the acquisition.

Notes to the Consolidated Financial Statements continued

for the year ended 31st December 2000

32 Acquisition of Subsidiary continued

b) Cash Flow on Acquisition

The fair value of the assets and liabilities acquired were as follows

	US\$ millions
Cash and Cash Equivalents	150.9
Placements with Banks	1,069.5
Trading Securities	376.3
Investment Securities	1,679.5
Loans and Advances	458.1
Fixed & Other Assets	127.2
	3,861.5
Deposits from Banks	(1,441.0)
Deposits from Customers	(1,642.7)
Securities Sold but not yet Purchased	(217.1)
Other Liabilities	(82.8)
Subordinated Loan	(80.0)
Total Purchase Consideration	397.9
Less	
Shares Issued	(299.1)
Cash and Cash Equivalents acquired	(150.9)
Cash inflow on acquisition	(52.1)

c) Consolidation

The Consolidated Income Statement for the year ended 31st December 1999 included GIBUK's income and expenses for the nine months from 8th April 1999. The amounts incorporated in respect of GIBUK in the Consolidated Income Statement are as follows

	2000 US\$ millions	1999 US\$ millions
Net Interest and Other Income	118.2	62.9
Operating Expenses	73.5	46.1
Net effect of change in accounting policy	–	(13.9)
Net Income after Tax	30.7	2.8

33 Principal Subsidiaries

The principal subsidiary companies were as follows

	Country of Incorporation	Ownership Interest	
		31.12.00	31.12.99
		%	%
Gulf International Bank (UK) Limited	United Kingdom	100	100
GIB Export Finance Limited	United Kingdom	100	100
SIB Financial Advisory Services Limited	United Kingdom	100	100
SIB Investment Holdings Limited	United Kingdom	100	100
GIBINVEST E C	Bahrain	100	100

34 Average Consolidated Balance Sheet

The average Consolidated Balance Sheet was as follows

	2000	1999
	US\$ millions	US\$ millions
Assets		
Cash and Other Liquid Assets	202.7	331.1
Placements with Banks	3,500.4	3,152.8
Trading Securities	452.9	513.4
Investment Securities	6,196.1	5,170.8
Loans and Advances	3,927.0	4,299.7
Fixed & Other Assets	508.5	425.2
Total Assets	14,787.6	13,893.0
Liabilities & Shareholders' Equity		
Deposits from Banks	6,316.7	6,320.5
Deposits from Customers	4,868.9	4,381.4
Securities Sold under Agreements to Repurchase	1,024.9	834.0
Securities Sold but not yet Purchased	91.2	174.2
Other Liabilities	406.4	396.2
Term Financing	896.2	750.0
Total Liabilities	13,604.3	12,856.3
Shareholders' Equity	1,183.3	1,036.7
Total Liabilities & Shareholders' Equity	14,787.6	13,893.0

Notes to the Consolidated Financial Statements continued

for the year ended 31st December 2000

35 Parent Company

The condensed unconsolidated financial statements of Gulf International Bank B S C were as follows

a) Condensed Balance Sheet

	At 31.12.00 US\$ millions	At 31 12 99 US\$ millions
Assets		
Cash and Other Liquid Assets	70.8	199 6
Placements with Banks	2,508 1	2,454 6
Trading Securities	117 3	236 9
Investment Securities	4,400.8	3,649 9
Investment in GIBUK	395 2	400 2
Loans and Advances	3,888.2	3,915 2
Fixed & Other Assets	275.6	227 7
Total Assets	11,656.0	11,084 1
Liabilities & Shareholders' Equity		
Deposits from Banks	5,085 5	4,263 9
Deposits from Customers	3,141.5	3,102 0
Securities Sold under Agreements to Repurchase	1,159 8	1,563 6
Securities Sold but not yet Purchased	—	45 3
Other Liabilities	242.8	220 3
Term Financing	850 0	750 0
Total Liabilities	10,479.6	9,945 1
Shareholders' Equity	1,176.4	1,139 0
Total Liabilities & Shareholders' Equity	11,656.0	11,084 1

The investment in GIBUK is stated at cost less pre-acquisition dividends received

b) Condensed Income Statement

	Year Ended 31.12.00 US\$ millions	Year Ended 31 12 99 US\$ millions
Interest Income	743 8	586 0
Interest Expense	627.0	479 0
Net Interest Income	116 8	107 0
Provision for Investment Securities	(2.9)	(0 4)
Provision for Loan Losses	(27.1)	(24 6)
Net Interest Income after Provisions	86.8	82 0
Other Income	55 8	47 1
Net Interest and Other Income	142.6	129 1
Operating Expenses	(58 7)	(52 5)
Restructuring Costs	—	(7 3)
Net Income before Tax	83 9	69 3
Taxation on Overseas Activities	3 5	(0 4)
Net Income after Tax	87.4	68 9

36 Future Changes in Accounting Policies

On 1st January 2001 the Group adopted IAS No 39 – Financial Instruments Recognition and Measurement. This resulted in changes in the accounting policies of the Group in respect of the recognition and measurement of derivative financial instruments entered into for hedging purposes and the measurement of certain non-derivative financial instruments. The changes in accounting policies are summarised as follows:

a) Derivative Financial Instruments

The Group recognised for the first time the fair value of all derivative financial instruments in the Balance Sheet as either assets (positive fair values) or liabilities (negative fair values). The fair value of a derivative financial instrument represents the unrealised gain or loss derived using quoted market prices or internal pricing models as appropriate. The recognition of unrealised gains and losses on derivative financial instruments entered into for hedging purposes is dependent on the nature of the hedging relationship as follows:

- **Fair value hedges** Fair value hedges represent derivative transactions entered into for the purpose of hedging exposure to changes in the fair value of a recognised asset or liability. Gains and losses on fair value derivative hedging instruments are recognised in the income statement. The hedged asset or liability is also stated at fair value in respect of the risk being hedged, with any gain or loss recognised in the income statement. On the adoption of IAS 39, unrealised gains and losses on fair value hedges and the related hedged assets and liabilities were accounted for as an adjustment to the opening balance of Retained Earnings at 1st January 2001.
- **Cash flow hedges** Cash flow hedges represent derivative transactions entered into for the purpose of hedging exposure to variability in cash flows that is attributable to a particular risk associated with a recognised asset or liability. On the adoption of IAS 39, unrealised gains and losses on cash flow hedges were accounted for as a separate component of Shareholders' Equity.

b) Non-Derivative Financial Instruments

Prior to the adoption of IAS 39, debt and equity securities which were intended to be held for the long term were stated at amortised cost less provisions for impairment. On the adoption of IAS 39, all such securities were reclassified as 'available-for-sale' and remeasured to fair value. The unrealised gains and losses arising on the remeasurement of 'available-for-sale' securities to fair value were accounted for as an adjustment to the opening balance of Retained Earnings at 1st January 2001.

Effect of changes in accounting policies

The more significant effects on Shareholders' Equity of the changes in accounting policies arising on the adoption of IAS 39 are summarised as follows:

	Share Capital US\$ millions	Share Premium US\$ millions	Retained Earnings US\$ millions	Other Reserves US\$ millions	Total US\$ millions
At 1st January 2001, as set out in Note 14	1,000.0	7.6	104.5	93.7	1,205.8
Impact of adopting IAS 39					
– Investments remeasured to fair value	–	–	(45.2)	–	(45.2)
– Fair value derivative hedges remeasured to fair value	–	–	(40.8)	–	(40.8)
– Hedged loans, placements and deposits remeasured to fair value	–	–	(3.4)	–	(3.4)
Cash flow hedges remeasured to fair value	–	–	–	0.7	0.7
Opening balances restated	1,000.0	7.6	15.1	94.4	1,117.1

Group Corporate Directory

Gulf International Bank B.S.C.

General Management

Dr Khaled Al-Fayez
Vice Chairman & Group Chief
Executive Officer

Dr Abdullah El-Kuwaiz
General Manager, GIB

Matthew Snyder
Managing Director &
Chief Executive Officer,
GIB (UK) Ltd

Mohannad T Farouky
Deputy Managing Director,
GIB (UK) Ltd

**Assets & Liabilities
Management GIB**
Bachir A. Barbir
Assistant General Manager &
Head of Assets & Liabilities
Management

Anthony James
Global Treasurer

Adel Al-Dosseri
FX & Money Markets

Sunil Dattani
Investment and Fixed Income &
Derivatives Trading

Salman Al-Zayani
Treasury Sales

**Financial Markets
GIB (UK) Ltd**
Mohab Mufti
Head of Financial Markets

John Benfield
Derivatives

Chris Baker
Corporate Debt

Woody Patnaik
Emerging Markets

Simon English
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**Corporate & Institutional
Banking GIB**
Andrew L I Pocock
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Corporate Banking
Abbas Ameer
Area Head

Muthuswamy Chandrasekaran
Project Finance

Ali Rahimi
Saudi Corporate

Cherif Malik
Gulf Corporate

Srinivas Vemparala
Multinational Unit

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Hassan Abdul-Ghani
Area Head

Munawar Ihsan
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Abdul Karim Bucheery
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A. Rahman Kooheji
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Sharlar Khoshabi
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GIB (UK) Ltd
Gregga Baxter
Michael Parkhouse
Heads of Investment Banking

Salman Al-Deghalther
Senior Manager, Riyadh

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GIB (UK) Ltd.**
David Waite
Head of Asset Management

Shared Services

Dr Fouad Al Sinan
Group Administrative Officer &
Head of Group Shared Services

GIB
Antony Maw
Head of Operations &
Administration

Ahmed Saleh
Head of Human Resources

Abdulla Janahi
Administrative Services

Ali Buheji
Product Processing

Jameel Al-Sairafi
Information Technology

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Gordon Brooker
Operations and Administration

Leslie Shepherd
Information Technology

Staff Functions
Audit
Masood Zafar
Group Chief Auditor

Julian Anthony
Chief Auditor, GIB (UK) Ltd

HR Policy
Gareth Hughes
Group HR Policy

Credit & Risk Control
Atef Sakr
Chief Credit Officer, GIB

Mohammed Al-Barwani
International Credit, GIB

K Venkataraman
Middle East Credit, GIB

Peter Robinson
Head of Credit, GIB (UK) Ltd

Mobin Chowdhury
Head of Market
Risk Management, GIB

Kwesson Quarshie
Head of Risk Control,
GIB (UK) Ltd

Corporate Centre

Financial Control
Stephen D Williams
Group Financial Controller

John Bridger
Financial Controller,
GIB (UK) Ltd

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