

European Islamic Investment Bank Plc

**Pillar 3 Disclosures
December 2010**

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1. Overview

Background

The European Union Capital Requirements Directive came into effect on 1 January 2007. This was introduced in the UK by the Financial Services Authority (FSA) based on the Basel 2 rules. Basel 3 comprises new regulatory standards on capital adequacy and liquidity to be adopted during 2011 for full implementation by 2019.

Pillar 3 requirements are designed to promote market discipline and disclosure by providing information on a firm's risk exposures and risk management processes.

European Islamic Investment Bank Plc (EIIB) uses the Standardised approach to risk and capital management.

Basis and frequency of disclosures

Disclosures have been prepared by EIIB in accordance with Pillar 3. All figures relate to the 31 December 2010 Consolidated Financial Statements and are in GBP 000 unless otherwise stated.

Disclosures are on an annual basis or more frequently in the event of material changes.

Scope

EIIB is an EEA parent institution and is regulated by the FSA.

There is a requirement to calculate, maintain and report regulatory capital ratios on an unconsolidated basis. Full details of subsidiary undertakings are included in Note 31 of the Annual Report.

Location and verification

These disclosures are subject to review by the Executive Management Committee following Board approval of the financial statements and are published on the company website. These disclosures are not subject to audit although certain disclosures are included in the audited or reviewed financial statements.

2. Risk management objectives and policies

Strategies and processes to manage risk

The Bank is an Islamic Finance Institution which operates in accordance with Sharia'a law. The Board has set risk appetite and tolerances within the overall risk framework, documented within a set of risk management policies which are approved by mandated Risk Committees. Ultimate responsibility for risk resides with the Board of Directors.

Risk management framework

Primary responsibility for the identification, control, monitoring and mitigation of risk lies with the business origination and operational support areas. A specialist risk support function independently identifies, measures, monitors, controls and reports risk with oversight provided by a number of committees covering various aspects of risk. Assurance is provided by Internal Audit with governance provided by the Audit Committee.

Risks are reviewed at least annually via the Internal Capital Adequacy Assessment Process (ICAAP). The most significant risks are considered to be credit risk, market risk, operational risk and liquidity risk. Risk management practices include risk policies, risk measurement, risk monitoring and control, risk reporting, and risk mitigation.

Risk is managed by a set of comprehensive limits, triggers and processes. Internal risk ratings are assigned to exposures which are assessed using quantitative and qualitative methodologies. All exposures are reviewed at least annually. Risk mitigation techniques are used where permitted and are also considered when losses may materialise.

Risk is measured and reported against capital and liquidity requirements, limits, triggers and mandates as contained in the various policy statements. Information is provided to management and risk committees via daily and monthly risk reports and includes stress testing using an appropriate level of severity. Summary information is provided quarterly to the Board.

Structure and organisation of risk management

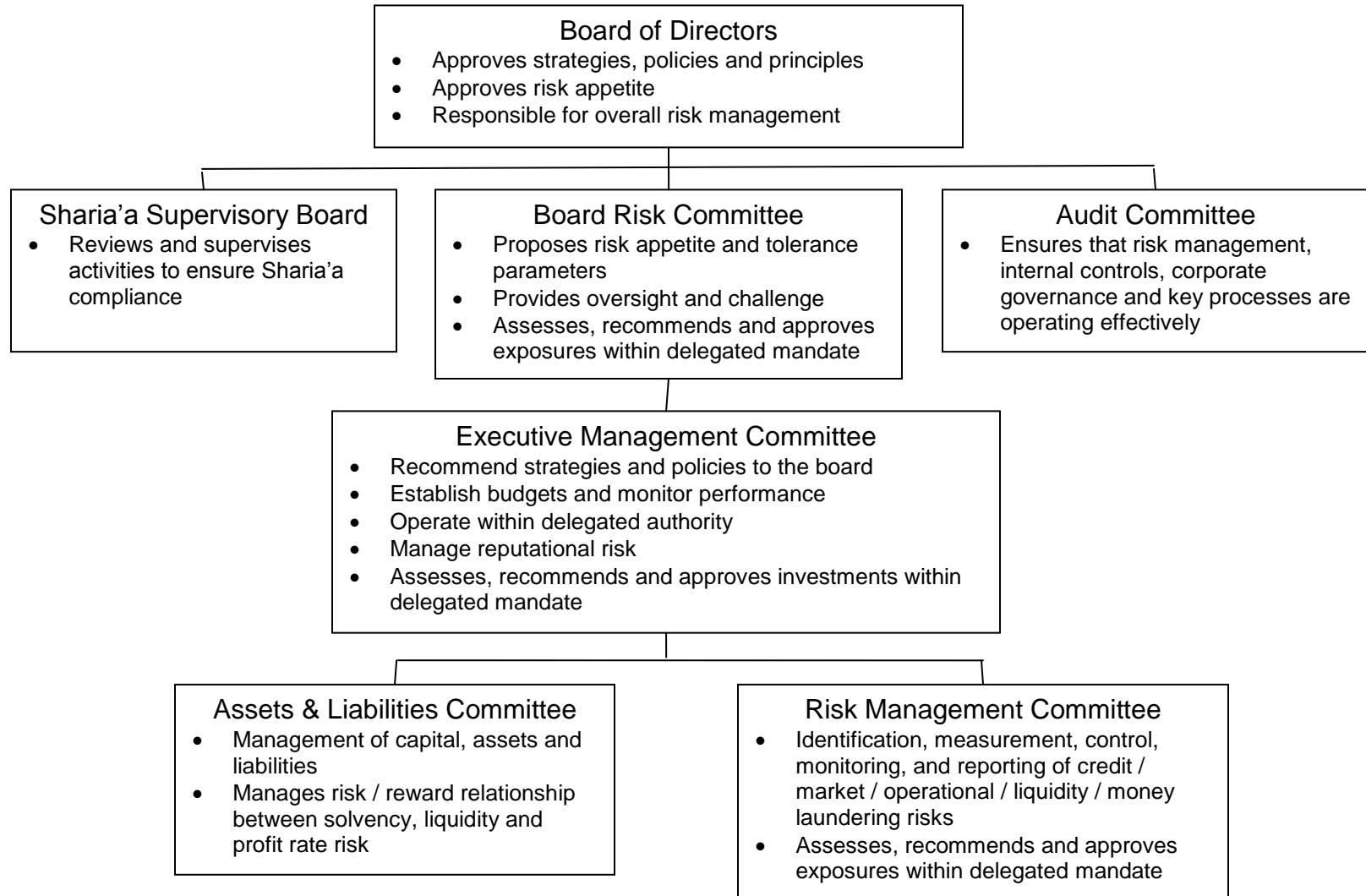
Responsibilities for the main risks are allocated as follows:

Key Risk	Risk Management	Risk Oversight	Risk Governance
Credit / Investment risk	Treasury & Capital Markets and Private Equity	Risk Department	Risk Management Committee / Executive Management Committee
Market risk	Treasury & Capital Markets and Private Equity	Risk Department	Risk Management Committee
Operational risk	All business areas	Operations Dept and Risk Dept	Risk Management Committee
Liquidity risk	Treasury & Capital Markets	Risk Department	Asset & Liability Committee

The Board Risk Committee oversees all Risk Committees.

Internal Audit is responsible for scheduling a programme of reviews to provide assurance that internal controls are in place, assets are safeguarded, compliance with policies and procedures as well as regulations and laws, and accuracy and reliability of records and reports. The Audit Committee approves the annual audit plan and considers subsequent audit reports.

The Risk Committees structure is as follows:



3. Capital resources

Total available capital

The Bank complied with the capital requirements set out by the FSA. Total regulatory capital available was:

GBP 000	Unconsolidated
Share capital	17,657
Share premium	116,220
Retained earnings	10,846
Other reserves	735
Investment in own shares	(2,117)
Fair value reserves on available-for-sale securities	(265)
Total Tier 1 Capital	143 076
Investments in qualifying holdings and subsidiaries	(63,109)
Illiquid assets	(354)
Total regulatory capital available	79,613

No part of available capital comprises Tier 2 or Tier 3 capital.

4. Capital adequacy

Capital management

Capital is managed with a view to balancing prudence and efficiency. The Board decided to adopt a cautious approach given the recent market turmoil and the need to establish a reputation in the financial services industry. Improved capital efficiency is being achieved through the deployment of assets.

The minimum Capital Resource Requirement (CRR) is determined in accordance with BIPRU rules. The Bank has adopted the Standardised Approach to credit risk and market risk, and the Basic Indicator Approach to operational risk for calculation of the Basel 2 Pillar 1 minimum capital requirement.

Economic capital covers other material risks (Pillar 2 risks) in addition to Pillar 1 risks. A Standard Approach is used to determine an economic value for these risks.

In line with FSA requirements, a capital planning buffer is also available to absorb losses and/or to cover increased capital requirements in adverse or unforeseen circumstances that are outside the Bank's normal and direct control. Regulatory capital is sufficient to cover all Pillar 1 and Pillar 2 requirements.

Regulatory capital is reported daily, while economic capital and is reported monthly to management and risk committees.

Internal capital adequacy assessment process

An internal assessment of capital needs (Internal Capital Adequacy Assessment Process) (ICAAP) is undertaken at least annually.

The outcome of the ICAAP is used to determine the Internal Capital Assessment (ICA). The ICA covers all material risks to determine the capital requirement over a three year horizon and includes stress testing. The ICA is presented to the Board for approval. The FSA assesses the ICA and sets Individual Capital Guidance (ICG) for the Bank.

Minimum capital requirement: credit risk

The overall minimum capital requirement for credit risk using the Standardised Approach (8 % of the risk weighted exposure amounts for each exposure class) was: (unconsolidated)

Exposure class GBP 000	
Sovereigns	128
Financial Institutions	2,329
Corporates and other	1,330
Equity	128
Credit risk minimum capital requirement	3,915

Minimum capital requirement: Pillar 1

The overall minimum capital requirement under Pillar 1 is determined by adding the credit capital requirement above to that required for market and operational risk. Market risk includes a Position Risk Requirement (PRR) being the regulatory capital required to cover the risk of losses on profit rate, foreign currency and equity positions calculated in accordance with FSA rules. There were no commodity positions.

The overall minimum capital requirement under Pillar 1 was: (unconsolidated)

GBP 000	Pillar 1 Capital	Risk weighted exposure
Credit risk	3,915	48,932
Market risk	1,017 ¹	12,713
Operational risk	1,424	17,804
Total Pillar 1 minimum capital requirement	6,356	
Total Risk weighted exposure		79,449
Total regulatory capital available	79,613	N/A
Excess over Pillar 1 minimum capital requirement	73,257	N/A

¹ Includes foreign currency PRR of GBP 377k

Capital adequacy: 100 %

5. Credit risk

Credit risk overview

Credit risk is the risk of loss arising from counterparty failure to pay capital or income or failure to perform on due date. For disclosure purposes credit risk is sub divided into sovereign, financial institutions, corporate, private equity and quoted equity.

Risk arising from changes in credit quality and the recoverability of advances are inherent in the Bank's activities. Adverse changes in the credit quality of counterparties and in the economies where the Bank takes risk can affect the value of assets. Risk management processes have been established as part of the overall risk framework to measure, manage and mitigate risk.

Equity investments are held for medium term capital gain at fair value. Unrealised gains or losses are taken into account for the Tier 1 Capital calculation.

The gross credit risk exposures were as follows: GBP 000

Sovereigns	7,997
Financial institutions	102,159
Corporate and other	16,683
Private equity	40,699
Quoted equity	11,915
Total	179,453

The geographical distribution of these exposures was as follows:

GBP 000	Europe	Middle East	Rest of world	Total
Sovereigns	-	7,997	-	7,997
Financial institutions	41,368	55,697	5,094	102,159
Corporate and other	11,303	5,380	-	16,683
Private equity	-	-	40,699	40,699
Quoted equity	-	3,560	8,355	11,915
	52,671	72,634	54,148	179,453

The residual maturity of exposures was as follows:

	0 – 1 months	2 – 3 months	4 – 6 months	7 – 12 months	1 - 5 years	5+ years	Total
Sovereigns	45	9	22	-	4,699	3,222	7,997
Financial institutions	76,218	1,664	7	4,075	20,195	-	102,159
Corporate and other	-	13	3,236	-	11,250	2,184	16,683
Private equity	-	-	26,363	-	-	40,699	40,699
Quoted equity	-	-	-	-	-	-	11,915
	76,263	1,686	3,265	4,075	36,144	58,020	179,453

The industry sector distribution of these exposures was as follows: GBP 000

Financial services & other financial	106,340
Government	7,996
Manufacturing & engineering	13,630
Oil & gas	27,780
Mining	5,939
Real estate	6,764
Food	2,826
Agricultural	350
Healthcare	280
Information & communication technology	1,924
Telecommunication	2,249
Media & entertainment	2,584
Other	791
	179,453

Credit risks are managed in accordance with the Credit Policy approved by the Board. Limits are placed on business volumes, industry sector, geography and size of exposures. Exposure limits are subjected to both objective and subjective analysis criteria with the primary focus placed on the ability and willingness to repay, track record, financial strength and transaction structure.

Security may be taken to add comfort where required although exposures are not based solely on security provided. Security may cover various forms, is valued at regular intervals and is assessed for concentration risk. Other credit risk mitigants may be used such as third party guarantees and netting, supported by robust legal documentation. Guarantors are assessed for creditworthiness. The use of derivatives is generally not permitted by Sharia'a scholars.

Gross exposures subject to credit risk mitigants were: GBP 000

Netting	8,500
Collateral (mainly land, buildings, plant & equipment)	14,482

All exposures are given an internal rating which is used in the calculation of capital. Ratings by External Credit Assessment Institutions (ECAIs), comprising Moody's, Standard and Poor's and Fitch, are taken into account where applicable.

Transactions are priced in accordance with the level of risk taken.

The Board delegates authority to approve exposures by means of a formal mandate taking ratings, type of risk and tenors into account.

Ongoing monitoring of credit exposures is undertaken by the Business Units, with separate monitoring by Operations Department and Risk Department with monthly reports to management and the Risk Management Committee. In the event of adverse trends, covenant breaches or arrears, Risk Department becomes actively involved in resolving the situation.

The tables below shows the value of exposures for each credit quality step: GBP 000

Sovereigns:

Credit quality step	Risk weight %	ECAI Rating	Exposure Value	Exposure Value after mitigation
1	0	AAA to AA-	-	-
2	20	A+ to A-	4,480	4,480
3	50	BBB+ to BBB-	-	-
4	100	BB+ to BB-	1,323	1,323
Not Rated	100	Not Rated	2,193	2,193

Financial Institutions:

Credit quality step	Risk weight %	Rating	Exposure Value	Exposure Value after mitigation
1	20	AAA to AA-	33,721	33,721
2	20 (under 3 months) 50 (over 3 months)	A+ to A-	11,928	11,928
3	20 (under 3 months) 50 (over 3 months)	BBB+ to BBB-	22,555	22,555
4	50 (under 3 months) 100 (over 3 months)	BB+ to BB-	1,627	1,627
Not Rated	20 (under 3 months) 50 (over 3 months)	Not Rated	32,164	32,164

Corporates and other:

Credit quality step	Risk weight %	Rating	Exposure Value	Exposure Value after mitigation
1	20	AAA to AA-		
2	50	A+ to A-	-	-
3	100	BBB+ to BBB-	2,187	2,187
4	100	BB+ to BB-	-	-
Not Rated	100	Not Rated	14,443	14,443

Private and Quoted Equity:

Credit quality step	Risk weight %	Exposure Value	Exposure Value after mitigation
Sufficiently diversified Portfolios	190	-	-
Quoted	290	16,051	16,051
Unquoted	370	36,563	36,563

Impairment provisions

At each reporting date an objective assessment is made whether a financial asset or group of assets are impaired. Evidence will include financial difficulties, default in payments, breach of financial covenants and restructuring as well as macroeconomic and geopolitical risk factors.

If there is evidence that an impairment loss has been incurred, the amount of the impairment is measured as the difference between the carrying value of the asset and the present value of estimated future cash flows discounted at the asset's original effective interest rate. Impairments have been deducted from the corresponding asset value in the balance sheet. Where subsequent events indicate the impairment allowance is not required, or not required in full, the allowance is reversed.

Where an exposure is not recoverable it is written off against the related impairment provision after all recovery actions have been taken and the amount of the loss has been determined. Subsequent recoveries are recognised in the income statement.

Past due amounts are defined as one day overdue and include the full amount outstanding. There were no amounts classified as past due.

Impairments and charges to the income statement, which relate to exposures in the UK and Saudi Arabia, were:

GBP 000	Sovereign	Financial Institutions	Corporate and other	Quoted equity	Private equity	Total
Impairments:						
Opening balance at 1 January 2010	-	-	17,133	-	-	17,133
Charge / (credit) for the period:						
Recoveries	-	-	(1,041)	-	-	(1,041)
Amounts written off	-	-	(5,989)	-	-	(5,989)
Foreign exchange						

movements	-	-	372	-	-	372
Closing balance at 31 Dec 2010	-	-	10,475	-	-	10,475

Available for sale assets (AFS)

At each reporting date, the AFS financial assets are assessed for fair value. If there is evidence of a credit loss embedded in the reduced value, the credit loss is accounted for in the income statement as an impairment charge, and the balance of the fair value loss is charged to the AFS Reserve.

Factors taken into account in assessing impairments include volatility in markets, deterioration in financial position and cash flows, and industry and sector performance.

AFS reserves and changes were:

GBP 000	Sovereign	Financial Institutions	Corporate and other	Quoted equity	Private equity	Total
Fair value reserve – AFS securities:						
Opening balance at 1 January 2010	171	109	(119)	-	-	161
Charge / (credit) for the period:	(232)	27	308	-	-	103
Closing balance at 31 Dec 2010	(61)	136	189	-	-	264

Credit risk concentrations

Concentration limits are set within policy. Limits for geographic, industry sector and large exposures to counterparty or connected counterparty concentrations are set and monitored.

Credit risk mitigation

Credit risk is mitigated where possible using collateral, netting, third party guarantees, securitisations and syndications. Most financing structures are unsecured although certain securities have recourse to pools of tangible assets. Robust and enforceable documentation is maintained with standard documentation subject to internal legal review and bespoke documentation prepared by independent solicitors.

No speculative derivatives have been permitted by the Bank's Sharia'a Supervisory Board.

6. Market risk

Market risk overview

Market risk is defined as the risk of loss arising from adverse changes in market prices.

Profit rate risk arises from changes in profit rates and credit spreads. The Bank is not exposed to interest rate risk on its financial assets as no interest is charged or earned. However the fair value of financial instruments may be affected by market forces including interest rates. Profit rate risk is mainly allocated between GBP and USD.

Foreign exchange risk arises from assets and liabilities denominated in foreign currency where the value or net income changes as a result of changes in foreign exchange rates.

Equity risk arises from movements in equity prices. Equities are accounted for using Fair Value Through the Income Statement. Fair values are derived from quoted prices in active markets or valuation techniques based on recent arms length transactions, reference to similar instruments, discounted cash flow analysis or option pricing models.

Equity positions together with gains and losses were:

GBP 000	Private Equity	Quoted Equity
Balance sheet values	40,699	11,915
Fair values	40,699	11,915
Realised – gains	-	193
- Losses	(676)	(496)
Unrealised – gains	15 266	71
- losses	-	-
Amounts included in capital resources		
Realised	-	(303)
Unrealised	-	71

All market risks are monitored and regularly considered by ALCO and the Risk Management Committee.

Monitoring market risks

The following metrics are used to monitor market risk:

Sensitivity analysis (PV01). This is used to assess the change in value of net worth against a one basis point (0.01 %) rise in profit rates and credit spreads. Results are reported on a daily basis.

Stress Testing (PV200). This is a similar calculation to PV01 but against a more severe 200 basis point (2.0 %) rise in profit rates. Results are reported daily.

Trigger limits. These limits are set to allow a certain pre-determined movement in the investment portfolio, open foreign exchange positions and equity prices. Movements in excess of the trigger limits must be reported to the relevant committee for further decision. Trigger limits are monitored daily.

A set of limits and triggers to cover market risks has been set by the Board and are reported daily.

Value at Risk (VaR). This technique estimates the potential losses as a result of movements in market rates and prices over a specified time horizon and a given level of confidence. A 10 day horizon and a 99 % confidence level are used. The VaR model used incorporates underlying volatilities and correlations. Potential movements in market prices are calculated by reference to daily market data from the last two years equally weighted. Results are reviewed daily by management. Actual outcomes are checked periodically to test the validity of assumptions used. VaR methodology is limited by historical data not necessarily being a guide to the future, changes beyond the level of confidence used, and no account being taken of intra day positions.

Profit rate and foreign exchange rate risk summary:

GBP 000	Average 2010	High 2010	Low 2010
Gross PV01 profit rate exposure	3	5	2
Gross foreign exchange exposure	9,198	12,211	4,122

The Net Open Foreign Exchange position on 31 December 2010 was GBP 6,688,265.

There were no contractual obligations to provide collateral.

7. Operational risk

Operational risk overview

Operational risk is defined as the risk of loss arising from inadequate or failed internal processes, people and systems or from external events.

The Basic Indicator Approach to operational risk is followed. Gross income is used as a proxy for operational risk exposure with the capital charge based on gross income over the preceding three years.

Monitoring and control

Oversight and governance for setting and managing operational risk policy and culture are the responsibility of the Board, the Board Risk Committee, the Executive Management Committee and the Risk Management Committee with oversight in the following key risk areas:

Financial management
Information technology
Premises and safeguarding of physical assets.
Internal and external fraud
People
Employment practices and workplace safety
Business continuity
Information security
Legal & regulatory
Clients, products and business practices
Execution, delivery and process management
Third parties

Responsibility for each area is allocated to a risk owner being a senior member of management. Management includes monitoring and control of regular quality self assessments, incident reporting and analysis, material losses and control failures.

8. Liquidity risk

Liquidity risk overview

Liquidity risk is defined as the inability to repay liabilities when due at an acceptable cost within a reasonable time period.

Monitoring and control

Cash flows are managed on a daily basis and a portfolio of liquid assets is maintained consisting of cash, short term bank deposits and liquid instruments. Liquidity risk management is the responsibility of ALCO.

An internal assessment of liquidity (Internal Liquidity Adequacy Assessment) (ILAA) is undertaken at least annually.. The ILAA covers all material risks and includes stress testing . The results are used to determine minimum liquidity ratios and the minimum liquid asset buffer.

Liquidity is managed within the FSA's prudential limits as follows:

	Limit %	Actual %
Sight (up to 8 days)	0	19
Up to 1 month	-5	70

9. Remuneration

The Bank operates a Remuneration Committee in accordance with the principles of the UK Corporate Governance Code. The Remuneration Committee comprises three non executive directors and approves remuneration policies and practices. The Committee ensures that an acceptable balance exists between the interests of employees and shareholders and that the Bank attracts and retains the required expertise. External surveys are used and expert opinions may be sought.

Annual performance reviews are conducted and achievement of both financial and non financial goals is assessed.

The Bank operates a Staff Incentive Scheme. The purpose of the Scheme is to align the interests of employees and shareholders by rewarding performance. Variable remuneration is based on profits after meeting a pre-determined hurdle amount. Individual, team and company performance is taken into account and adjusted for risk where appropriate. The Scheme is subject to deferral.

In addition the Bank operates a Company Share Option Plan. Share options were granted to staff with the number of shares linked to levels of fixed remuneration.

Aggregate remuneration broken down by business area was: (GBP 000)

Executive	3 108
Front Office	1 386
Back Office	1 364

Aggregate remuneration for senior management and staff whose actions have a material impact on the risk profile of the Bank was: (GBP 000)

Fixed	1 574
Variable	2 100
Number of beneficiaries	10

Variable remuneration comprised:

Cash	100 %
Shares	Nil
Other instruments	Nil

Deferred remuneration comprised:

Vested	50 %
Unvested	50 %
Paid out	50 %
Amount reduced	Nil

The Bank's policy is to avoid sign on payments for new staff. No payments were made in the past year.

No severance payments were awarded during the year.