AmIslamic Bank Berhad

(Company No. 295576–U)
(Incorporated in Malaysia)

CAFIB - Pillar 3 Disclosures

31 March 2011

CAFIB - Pillar 3 Disclosures
31 March 2011

Table of Contents **Page**

1.0 Scope of Application

The Bank Negara Malaysia's ("BNM") Risk Weighted Capital Adequacy Framework - Basel II and Capital Adequacy Framework for Islamic Bank - CAFIB ("RWCAF") – Disclosure Requirements ("Pillar 3") is applicable to all banking institutions licensed under the Banking and Financial Institutions Act, 1989 ("BAFIA") and all Islamic banks licensed under section 3(4) of the Islamic Banking Act, 1983 ("IBA"). The Pillar 3 disclosure requirements aim to enhance transparency on the risk management practices and capital adequacy of banking institutions.

The RWCAF framework is applicable to the Bank, a subsidiary of AMMB Holdings Berhad ("AMMB"), which offers Islamic banking services.

The following information has been provided in order to highlight the capital adequacy of the Bank. The information provided has been verified by the Group internal auditors and certified by the Chief Executive Officer.

BNM guidelines on capital adequacy require regulated banking entities to maintain an adequate level of capital to withstand any losses which may result from credit and other risks associated with financing operations.

The capital adequacy ratios are computed in accordance with BNM's Risk Weighted Capital Adequacy Framework or Capital Adequacy Framework for Islamic Banks (as applicable), which are based on the Basel II capital accord. The Bank has adopted the Standardised Approach for Credit and Market Risks and the Basic Indicator Approach for Operational Risk.

The minimum regulatory capital adequacy requirement is 8.0% for the risk weighted capital ratio.

2.0 Capital Management

The capital and risk management of the banking subsidiaries of AMMB are managed collectively at Group level. The Group's capital management approach is driven by its desire to maintain a strong capital base to support the development of its businesses, to meet regulatory capital requirements at all times and to maintain good credit ratings.

Strategic, business and capital plans are drawn up annually covering a 5 year horizon and approved by the Board of Directors. The capital plan ensures that adequate levels of capital and an optimum mix of the different components of capital are maintained by the Group to support its strategy.

The capital plan takes the following into account:

(a) Regulatory capital requirements:
- forecast demand for capital to support the credit ratings; and
- increases in demand for capital due to business growth and market shocks.

(b) Or stresses:
- available supply of capital and capital raising options; and
- internal controls and governance for managing the Group's risk, performance and capital.

The Group uses internal models and other quantitative techniques in its internal risk and capital assessment. The models help to estimate potential future losses arising from credit, market and other risks, and using regulatory formulae the amount of capital required to support them. In addition, the models enable the Group to gain a deeper understanding of its risk profile, e.g. by identifying potential concentrations, assessing the impact of portfolio management actions and performing what-if analysis.

Stress testing and scenario analysis are used to ensure that the Group's internal capital assessment considers the impact of extreme but plausible scenarios on its risk profile and capital position. They provide an insight into the potential impact of significant adverse events on the Group and how these events could be mitigated. The Group's target capital levels are set taking into account its risk appetite and its risk profile under future expected and stressed economic scenarios.

The Group's assessment of risk appetite is closely integrated with the Group's strategy, business planning and capital assessment processes, and is used to inform senior management's views on the level of capital required to support the Group's business activities.

2.0 Capital Management (Contd.)

The Group uses a capital model to assess the capital demand for material risks, and support its internal capital adequacy assessment. Each material risk is assessed, relevant mitigants considered, and appropriate levels of capital determined. The capital modelling process is a key part of the Group's management disciplines.

The capital that the Bank is required to hold is determined by its balance sheet, off-balance sheet, counterparty and other risk exposures after applying collateral and other mitigants, based on the Group's risk rating methodologies and systems. We discuss these outcomes with BNM on a regular basis as part of our normal regulatory liaison activities. BNM has the right to impose further capital requirements on Malaysian Financial Institutions via its Financial Market Supervision remit.

The Group operates processes and controls to monitor and manage capital adequacy across the organisation. Where we operate in other jurisdictions, capital is maintained on the basis of the local regulator's requirements. It is overseen by the Group Asset and Liability Committee ("GALCO"), which is responsible for managing the Group's statement of financial position, capital and liquidity.

A strong governance and process framework is embedded in the capital planning and assessment methodology. Overall responsibility for the effective management of risk rests with the Board of Directors. The Risk Management Committee of Directors ("RMCD") is specifically delegated the task of reviewing all risk management issues including oversight of the Group's capital position and any actions impacting the capital levels. The Audit and Examination Committee ("AEC") reviews specific risk areas and the issues discussed at the key capital management committees.

GALCO proposes internal triggers and target ranges for capital management and operationally oversees adherence with these. These ranges are 7.5% to 8.5% for the Tier 1 capital ratio and 11.5% to 12.5% for the total capital ratio. The Group has been (knowingly) operating in excess of these ranges for the last 3 years as the Group was conservatively positioned for any repercussions from the Global Financial Crisis.

A dedicated team, the Capital and Balance Sheet Management Department, is responsible for the ongoing assessment of the demand for capital and the updating of the Group's capital plan.

In light of the uncertain economic environment and evolving regulatory debate on banking institutions' capital structures, we believe it is appropriate to remain strongly capitalised above our target ranges.

2.0 Capital Management (Contd.)

Appropriate policies are also in place governing the transfer of capital within the Group. These ensure that capital is remitted as appropriate, subject to complying with regulatory requirements and statutory and contractual restrictions.

There are no current material, practical or legal impediments to the prompt transfer of capital resources in excess of those required for regulatory purposes or repayment of liabilities between AMMB and its group entities when due.

Table 2.1: Capital Adequacy Ratio

The capital adequacy ratios of the Bank are as follows:

	Bank	
	2011	2010
Before deducting proposed dividends:		
Core capital ratio	8.0%	10.5%
Risk weighted capital ratio	12.5%	15.3%
After deducting proposed dividends:		
Core capital ratio	8.0%	10.5%
Risk weighted capital ratio	12.5%	15.3%

Table 2.2: Risk Weighted Assets and Capital Requirements

The breakdown of risk weighted assets (“RWA”) by exposures in major risk category of the Bank is as follows:

2011

Exposure Class		Gross Exposures/ EAD before Credit Risk Mitigation ("CRM")	Net Exposures/ EAD after CRM	Risk Weighted Assets	Minimum Capital Requirement at 8%
	RM'000	RM'000	RM'000	RM'000	RM'000
1. **Credit Risk**					
On Balance Sheet Exposures					
Sovereigns/Central Banks		4,376,818	4,376,818	-	-
Banks, Development Financial Institutions ("DFI") & Multilateral Development Banks ("MDBs")		1,150,629	1,150,629	230,126	18,410
Corporates		5,418,211	5,357,854	5,047,676	403,814
Regulatory Retail		8,099,780	8,085,710	6,113,478	489,078
Residential Mortgages		176,840	176,805	64,894	5,192
Other Assets		150,280	150,280	142,564	11,405
Defaulted Exposures		217,621	214,348	267,201	21,376
Total On Balance Sheet Exposures		**19,590,179**	**19,512,444**	**11,865,939**	**949,275**
Off-Balance Sheet Exposures					
Over the counter ("OTC") Derivatives		15,113	15,113	6,131	490
Off-balance sheet exposures other than OTC Derivatives or Credit Derivatives		2,992,328	2,925,378	2,494,708	199,577
Defaulted Exposures		8,971	8,970	12,940	1,035
Total Off-Balance Sheet Exposures		**3,016,412**	**2,949,461**	**2,513,779**	**201,102**
Total On and Off-Balance Sheet Exposures		**22,606,591**	**22,461,905**	**14,379,718**	**1,150,377**
2. **Large Exposure Risk Requirement**					
3. **Market Risk**	**Long Position**	**Short Position**			
Rate of Return Risk					
- General profit rate risk	1,332,171	59,852		340,368	27,229
- Specific profit rate risk	1,332,171	59,852		119,496	9,560
Total	**2,664,342**	**119,704**		**459,864**	**36,789**
4. **Operational Risk**				1,209,490	96,759
5. **Total RWA and Capital Requirements**				16,049,072	1,283,925

The Bank does not have Profit-Sharing Investment Account ("PSIA") that qualifies as a risk absorbent.

Table 2.2: Risk Weighted Assets and Capital Requirements (Contd.)

The breakdown of risk weighted assets (“RWA”) by exposures in major risk category of the Bank are as follows:

2010

Exposure Class		Gross Exposures/ EAD before Credit Risk Mitigation ("CRM")	Net Exposures/ EAD after CRM	Risk Weighted Assets	Minimum Capital Requirement at 8%
	RM'000	RM'000	RM'000	RM'000	RM'000
1. **Credit Risk**					
On Balance Sheet Exposures					
Sovereigns/Central Banks		3,968,110	3,968,110	-	-
Public Sector Entities		29,831	29,831	5,966	477
Banks, Development Financial Institutions ("DFI") & Multilateral Development Banks ("MDBs")		718,459	718,459	143,731	11,499
Corporates		3,418,971	3,367,269	3,179,488	254,359
Regulatory Retail		8,330,738	8,325,365	6,243,317	499,465
Residential Mortgages		198,113	198,060	79,736	6,379
Other Assets		94,806	94,806	91,253	7,300
Defaulted Exposures		274,924	259,821	365,502	29,240
Total On Balance Sheet Exposures		**17,033,952**	**16,961,721**	**10,108,993**	**808,719**
Off-Balance Sheet Exposures					
Over the counter ("OTC") Derivatives		9,501	9,501	1,900	152
Off-balance sheet exposures other than OTC Derivatives or Credit Derivatives		737,060	737,060	629,309	50,345
Total Off-Balance Sheet Exposures		**746,561**	**746,561**	**631,209**	**50,497**
Total On and Off-Balance Sheet Exposures		**17,780,513**	**17,708,282**	**10,740,202**	**859,216**
2. **Large Exposure Risk Requirement**					
3. **Market Risk**	**Long Position**	**Short Position**			
Rate of Return Risk					
- General profit rate risk	1,047,739	106,263		301,642	24,131
- Specific profit rate risk	1,047,739	106,263		154,688	12,375
Total	**2,095,478**	**212,526**		**456,330**	**36,506**
4. **Operational Risk**				1,090,009	87,201
5. **Total RWA and Capital Requirements**				12,286,541	982,923

The Bank does not have Profit-Sharing Investment Account ("PSIA") that qualifies as a risk absorbent.

3.0 Capital Structure

Table 3.1 Capital Structure summarises the capital position of the Bank. The capital structure of the Bank includes capital under the following headings:

- paid-up ordinary share capital and eligible reserves;
- qualifying subordinated liabilities; and
- collective allowance (netted against financing and advances).

All capital instruments included in the capital base have been issued in accordance with the Bank Negara Malaysia rules and guidelines.

For regulatory purposes, capital is categorised into two main categories, or tiers, depending on the degree of permanency and loss absorbency exhibited. These are Tier 1 and Tier 2 capital which are described below.

3.1 Tier 1 Capital

Tier 1 capital comprises paid-up ordinary share capital, retained earnings and eligible reserves, after the deduction of certain regulatory adjustments.

Paid-up Ordinary Share Capital

Paid-up ordinary share capital is an item of capital issued by an entity to an investor, which is fully paid-up and where the proceeds of issue are immediately and fully available. There is no obligation to pay a coupon or dividend to the equity holder of ordinary shares. The capital is available for unrestricted and immediate use to cover risks and losses, and enable the entity to continue trading. It can only be redeemed on the winding-up of the entity.

Retained Earnings

Retained earnings at the end of the financial year and eligible reserves are accumulated resources included in the shareholders' funds in an entity's statement of financial position, with certain regulatory adjustments applied.

Eligible Reserves

Eligible reserves comprise the following:

- **Share Premium**
  Share premium is used to record premium arising from new shares issued in the group entity.

3.1 Tier 1 Capital (Contd.)

- **Statutory Reserve**
  Statutory reserve is maintained in compliance with the provisions of IBA and is not distributable as cash dividends.

3.2 Tier 2 capital

The main components of Tier 2 capital are collective allowance for bad and doubtful debts and Subordinated Sukuk Musyarakah.

Subordinated Sukuk Musyarakah
On 21 December 2006, the Bank issued RM400,000,000 Subordinated Sukuk Musyarakah ("Sukuk Musyarakah") for the purpose of increasing the Bank's capital funds.

The salient features of the Sukuk Musyarakah are as follows:

(i) The Sukuk Musyarakah carries a profit rate of 4.80% per annum for the first five (5) years and shall be stepped up by 0.50% per annum for every subsequent year to maturity date. The profit is payable on a semi-annual basis.

(ii) The Sukuk Musyarakah is for a period of ten (10) years. The Bank may exercise its call option and redeem in whole (but not in part) the Sukuk Musyarakah on the 5th anniversary of the issue date or on any anniversary date thereafter at 100% of the principal amount together with the expected profit payments.

Table 3.1: Capital Structure

The components of Tier 1 and Tier 2 Capital of the Bank are as follows:

	The Bank	
	2011	2010
	RM'000	RM'000
Tier 1 capital		
Paid-up ordinary share capital	403,038	403,038
Share premium	534,068	534,068
Statutory reserve	304,316	265,169
Retained earnings	162,515	133,719
	1,403,937	1,335,994
Less : Deferred tax asset	(116,298)	(42,218)
Total Tier 1 capital	1,287,639	1,293,776
Tier 2 capital		
Subordinated Sukuk Musyarakah	400,000	400,000
Collective/general allowance #	324,004	184,803
Total Tier 2 capital	724,004	584,803
Capital base	2,011,643	1,878,579

Excludes collective allowance on impaired financing restricted from Tier 2 capital of the Bank of RM155,006,000 as at 31 March 2011.

4.0 Risk Management Framework

The Risk Management Framework takes its lead from the Board of Directors' Approved Risk Appetite Framework which provides the catalyst to setting the risk/reward profile required by the Board of Directors, together with the related business strategies, limit framework and policies required to enable successful execution.

The Risk Appetite Framework is approved annually by the Board of Directors taking into account the Bank's desired external rating and targeted profitability/return on equity ("ROE") and is reviewed periodically throughout the financial year by both the executive management and the Board of Directors to consider any fine tuning/amendments taking into account prevailing or expected changes to the operational environment.

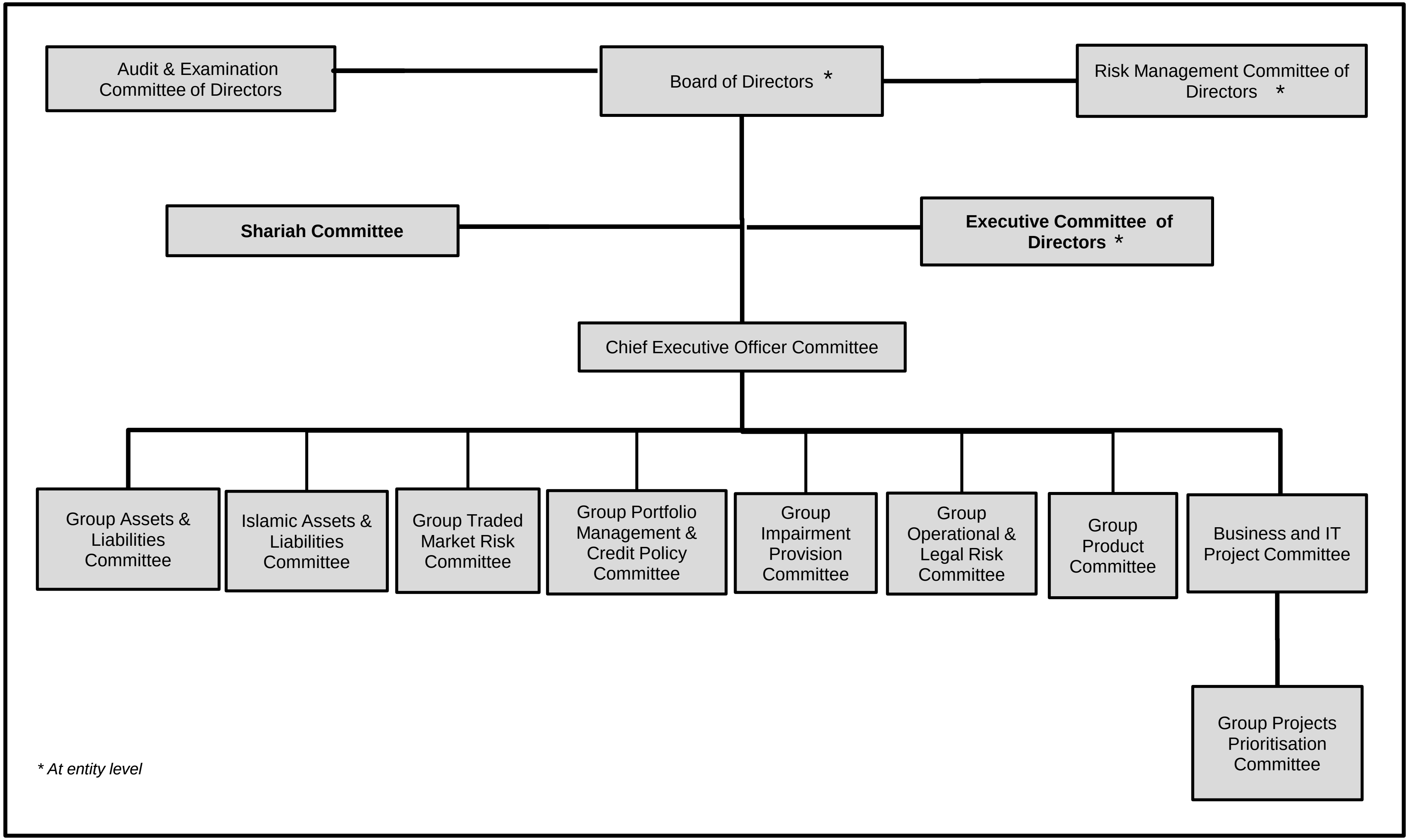
The Risk Appetite Framework provides portfolio parameters for Credit Risk, Traded Market Risk, Non-Traded Market Risk and Operational Risk incorporating, inter alia, limit structures for countries, industries, single counterparty, value at risk, capital at risk, earnings at risk, stop loss, stable funding ratio and liquidity. Each Business Unit has asset writing strategies which tie into the overall Risk Appetite Framework providing detailed strategies of how the Business Units will execute their business plans in compliance with the Risk Appetite Framework.

Risk Management Governance

The Board of Directors is ultimately responsible for the management of risks within the Bank. The Risk Management Committee of Directors is formed to assist the Board of Directors in discharging its duties in overseeing the overall management of all risks covering market risk management, liquidity risk management, credit risk management and operational risk management.

The Board of Directors has also established various Management Committees at the Group level to assist it in managing the risks and businesses of the Bank. The following chart sets out the organisational structure of the risk management committees and an overview of the respective committee's roles and responsibilities:

4.0 Risk Management Framework (Contd.)



4.0 Risk Management Framework (Contd.)

Committee	Roles and Responsibilities
Risk Management Committee of Directors ("RMCD")	- Oversee senior management activities in managing risk (covering credit, market, funding, operational, legal, regulatory capital and strategic risk) and to ensure that the risk management process is in place and functioning. - Report and advise the Board of Directors on risk issues.
Audit & Examination Committee of Directors ("AEC")	- Provide assistance to the Board in relation to fulfilling fiduciary responsibilities and monitoring of the accounting and financial reporting practices of the Group. - Provide assistance to Board of Directors in ensuring the Islamic Banking operations of the Group are Shariah compliant.
Shariah Committee	- Responsible and accountable on matters related to Shariah, which includes advising Board of Directors and management on Shariah matters and endorsing and validating products and services, and the relevant documentations in relation to Islamic Banking operations of the Group.
Executive Committee of Directors ("EXCO")	- Responsible to consider and approve credit facilities and commitments that are not in accordance with the policies approved by the Board for which EXCO has been granted powers to exempt. - Review credit facilities and commitments that exceeds certain thresholds.
Chief Executive Officer Committee ("CEO Committee")	- Responsible for overall day to day operations of the Group such as oversee management's activities in managing risk, review high level risk exposures, portfolio composition and risk strategies; and evaluate the existence and effectiveness of the control and risk management infrastructure. - Report and advise the Board of Directors on risk issues.
Group Assets and Liabilities Committee (Conventional and Islamic) ("GALCO")	- Responsible for the development of capital and balance sheet management policy, approve and oversee non-traded rate of return risk exposures, liquidity and funding framework and hedging and management of structural foreign exposure. Ensure fund transfer pricing is effective and fair and capital is managed.
Islamic Assets and Liabilities Committee	- Responsible for the development of Islamic capital and balance sheet management policy, approve and oversee rate of return risk exposures, liquidity and funding framework and hedging and management of structural foreign exposure. Ensure fund transfer pricing is effective and fair and capital is managed.

4.0 Risk Management Framework (Contd.)

Committee	Roles and Responsibilities
Group Traded Market Risk Committee (“GTMRC”)	- Responsible for the development of traded market risk policy framework, oversee the trading book portfolio, approve new trading products and ensure the compliance with the internal and regulatory requirements throughout the Group.
Group Portfolio Management and Credit Policy Committee (“GPMCP”)	- Responsible for the development of credit policy framework, oversee credit portfolio, endorse asset writing strategies, review credit provisioning policies and process and ensure the compliance with the internal and regulatory requirements throughout the Group.
Group Impairment Provision Committee	- Responsible for the development of key policies relating to impairment provisions, ensure provisions are assessed and made in accordance with Board approved policies and FRS 139 and FRS 137 standards and establish adequate management governance for the determination of provisions.
Group Operational and Legal Risk Committee (“GOLRC”)	- Responsible for endorsing operational risk, legal risk and regulatory compliance framework, oversee operational risk and legal risk management and reviews regulatory actions or any incidences that may give rise to operational and legal risk along with the actions taken to mitigate such risks.
Group Product Committee (“GPC”)	- Responsible for ensuring adequate infrastructure and resources are in place for product management, endorse proposal for new product and product launching strategies, approve proposal for product variation and reactivation of dormant product, and review post implementation activities and product performance.
Business and IT Project Committee (“BITPC”)	- Responsible to review and approve (or where required recommend for approval) requests relating to the Group’s major Business and Information Technology ("IT") investments. - To ensure all projects are aligned to the Business and IT plans, appropriate prioritisation of Business and IT projects, and the allocation of resources.
Group Projects Prioritisation Committee	- Responsible to optimise the allocation of shared resources and change capacity to programmes, projects and initiatives across the Group.

4.1 Internal Capital Adequacy Assessment Process (“ICAAP")

The core objectives of the Group’s ICAAP Policy are to:

- Protect the interests of depositors, creditors and shareholders;
- Ensure the safety and soundness of the Group’s capital position; and
- Ensure that the capital base supports the Group’s Risk Appetite, and strategic business objectives, in an efficient and effective manner.

4.1 Internal Capital Adequacy Assessment Process (“ICAAP") (Contd.)

The requirements of the ICAAP Policy are consistent and calibrated with the Group’s Risk Appetite as set and approved by the Board.

The following key principles underpin the ICAAP.

4.1.1 The Group must maintain an approved, documented, risk based and auditable ICAAP. The aim is to ensure the Group maintains, on a continuous basis, an adequate level of capitalisation which is sized following the identification, measurement, monitoring, and effective management and oversight of material risks across the Group, consistent with:

- Group Risk Appetite, including the Bank’s target credit rating category;
- Regulatory Capital requirements (basic Economic Capital methodologies to be introduced in FY 2013);
- The Board and Management’s targeted financial performance, and
- The Group’s planned asset growth and strategic business objectives.

4.1.2 Management Oversight

The ICAAP must be subject to Board and senior management oversight, form an integral part of the Group’s capital management and decision making processes, and will:

- Undergo regular, effective and comprehensive review;
- Satisfy regulatory requirements;
- Be capable of independent assessment and validation;
- Be incorporated into the Bank’s overall risk management strategy and governance frameworks.

4.1.3 Capital Management Plan and Framework

The ICAAP must include an approved Capital Management Framework and Plan including:

- A strategy for maintaining capital resources over time;
- Measures that would be taken in the event capital falls below a targeted level;
- Measures to ensure that the Group is in compliance with minimum regulatory standards; and
- Stressed capital plans; with clearly documented assumptions consistent with the Group’s strategic planning cycles.

4.1.4 The Group’s quality and level of capital must be commensurate with the level of risks in the business. Sufficient capital should be maintained to:

- Meet minimum prudential requirements in all jurisdictions in which the Group operates, also any ratings agency requirements, including maintaining appropriate buffers over minimum capital levels.
- Be consistent with the Group’s overall risk profile and financial positions, taking into account its strategic focus and business plan.

4.1 Internal Capital Adequacy Assessment Process (“ICAAP") (Contd.)

- Ensure there is sufficient capital to support the regulatory capital requirements of the business, including those resulting from the outcomes of stress testing.

The Group will have appropriately established capital targets for each major capital type; including:

- Minimums;
- Triggers; and
- Target operating ranges

The relationship between regulatory targets and economic capital will be clearly articulated and documented as part of the Group’s Economic Capital initiatives, targeted for basic introduction in FY 2013.

4.1.5 Capital allocation:

- The Group’s capital, excluding any amount held centrally for strategic contingencies (e.g. acquisitions) should be allocated to individual business units using regulatory capital allocation principles (basic Economic Capital methodologies to be introduced in FY 2013);
- Capital allocation should be consistent with the Group’s Regulatory Capital measurement framework (basic Economic Capital methodologies to be introduced in FY 2013) and risk adjusted performance requirements; and
- The Group should only retain capital that is required to meet its economic, operational, prudential and strategic requirements. Consideration should be given to returning capital in excess of that required to shareholders.

4.1.6 Material Risks

- The Group must have clearly articulated definitions of each material risk type to be included in the ICAAP; and
- Processes to identify and determine the materiality of current risk types, change to existing risk types and new risk types must be established.

4.1.7 Economic Capital Model

- The Group will develop a fully documented, Board approved comprehensive and credible internal economic capital model, targeted for basic introduction in FY 2013;
- In advance of the introduction of an economic capital model, regulatory capital will be used as a proxy in order to ease the transition process;
- While capital may not be required for every material risk, the economic capital framework must consider the capital required for each material risk type. The reason for the inclusion or exclusion of any material risk types from the economic capital model must be documented.

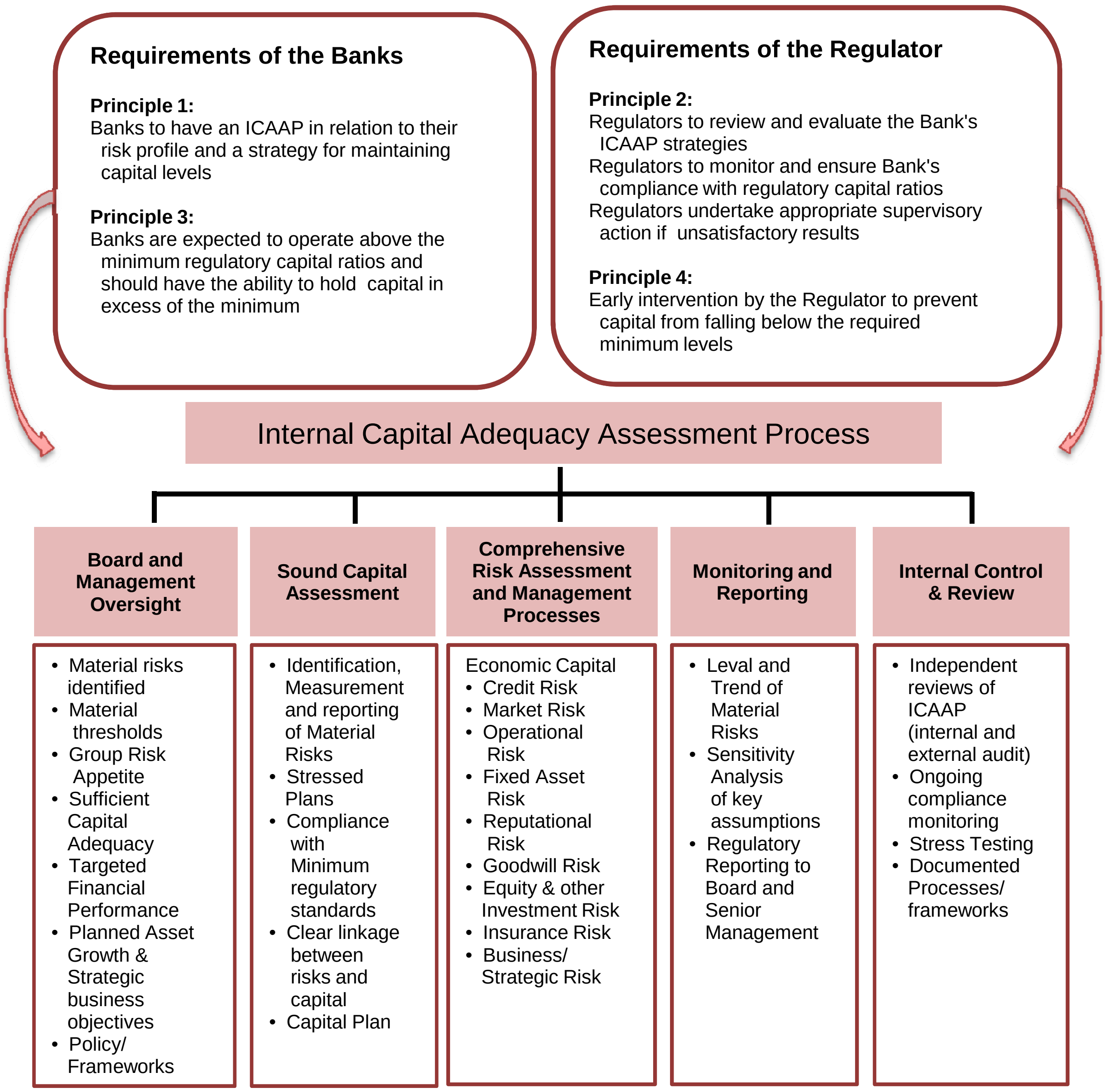
4.1 Internal Capital Adequacy Assessment Process ("ICAAP") (Contd.)

4.1.8 The Board must be notified and the regulator advised as soon as practicable of any:

- Significant departure from its ICAAP;
- Concerns that the Board has about its capital adequacy along with proposed measures to address those concerns; and
- Significant changes in its capital.

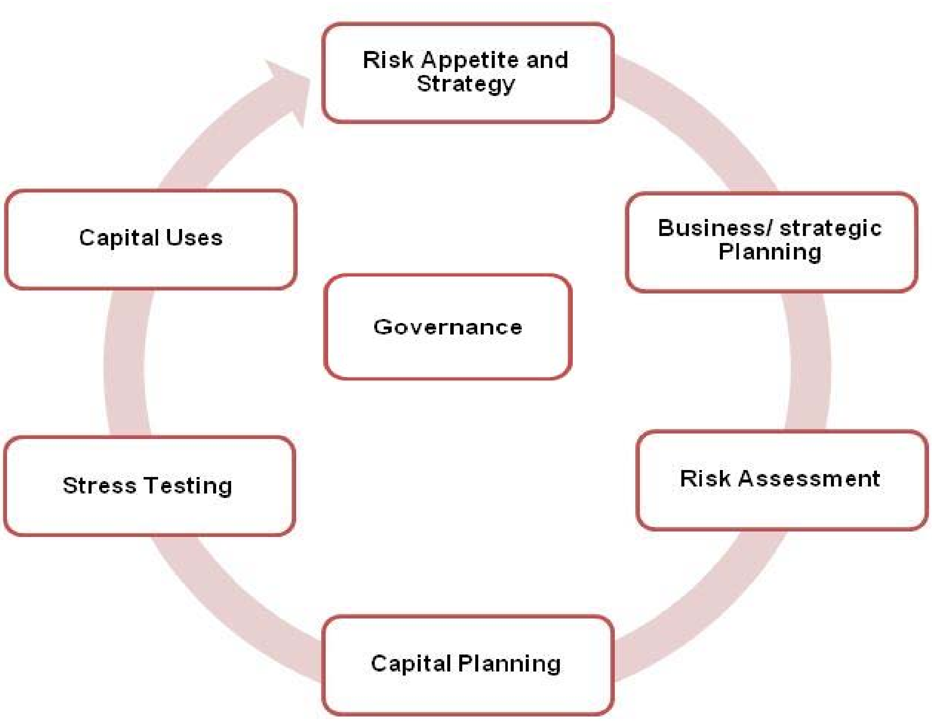
4.1.9 The cost of capital should be reviewed annually. The cost of capital should be set with reference to the Group's long term Return on Equity objectives.

ICAAP Framework



4.1 Internal Capital Adequacy Assessment Process ("ICAAP") (Contd.)

Overview of ICAAP process and setting Internal Capital Targets



5.0 Credit Risk Management

The credit risk management process is depicted in the table below:

Identification	• Accurate identification/recognition of credit risk on transactions and/ or positions • Selection of asset and portfolio mix
Assessment/ Measurement	• Internal credit rating system • Probability of default ("PD") • Loss given default ("LGD") • Exposure at default ("EAD")
Control/ Mitigation	• Portfolio Limits, Counterparty Limits, Benchmark Returns • Collateral and tailored facility structures
Monitoring/ Review	• Monitoring of portfolio and reporting • Watchlist review • Post mortem review

Credit risk is the risk of loss due to the inability or unwillingness of a counterparty to meet its payment obligations. Exposure to credit risk arises from financing, securities and derivative exposures. The identification of credit risk is done by assessing the potential impact of internal and external factors on the Bank's transactions and/or positions.

The primary objective of credit risk management is to maintain accurate risk recognition - identification and measurement, to ensure that credit risk exposure is in line with the Group's Risk Appetite Framework and related credit policies.

For non-retail credits, risk recognition begins with an assessment of the financial standing of the customer or counterparty using an internally developed credit rating model. The model consists of quantitative and qualitative scores that are then translated into a rating grade, ranging from "AAA" (representing the lowest risk grade) to "C" (that is the highest risk grade). The assigned credit rating grade forms a crucial part of the credit analysis undertaken for each of the Bank's credit exposures.

To support credit risk management's observation of disciplines governed by the Basel II Framework and Financial Reporting Standards ("FRS"), our rating models pertaining to credit risk (obligor's PD, LGD and EAD) are in the process of being upgraded. These new models are scheduled to be operational during 2012 and will:

5.0 Credit Risk Management (Contd.)

- improve the accuracy of individual obligor risk ratings and calculation of expected loss;
- enhance pricing models;
- facilitate financing loss provision calculation;
- automate stress-testing; and
- enhance portfolio management.

For retail credits, third generation credit-scoring systems to better differentiate the quality of customers are being used to complement the credit assessment and approval processes. New LGD and EAD models have also been recently developed which will also become operational during 2012.

Financing activities are guided by internal credit policies and Risk Appetite Framework that are approved by the Board of Directors. The Banks's Risk Appetite Framework is refreshed at least annually and with regard to credit risk, provides direction as to portfolio management strategies and objectives designed to deliver the Bank's optimal portfolio mix. Credit Risk portfolio management strategies include, amongst others:

- Concentration limits:
  - single counterparty credit;
  - industry sector;
  - country; and
  - portfolio composition (by risk grade).
- Asset writing strategies for industry sectors and individual customers;
- Setting Financing to Value limits for asset backed financing (that is, property exposures and other collateral);
- Watchlist processes for identifying, monitoring and managing customers exhibiting signs of weakness and higher risk customers; and
- Setting Benchmark Returns which serve as a guide to the minimum returns the Bank requires for the risk undertaken, taking into account operating expenses and cost of capital.

Individual credit risk exposure is reported to Credit and Commitment Committee ("CACC"). In the event such exposure exceeds CACC authority, it will be reported to EXCO. Portfolio credit risk is reported to the relevant management and board committees.

The GPMCP regularly meets to review the quality and diversification of the Bank's financing portfolio, approve new and amended credit risk policy, review watchlist reports and post mortem review of financing (to extract lessons learned for facilitating credit training and refinement of credit policies or guidelines, towards enhancing risk identification and control).

Group Risk prepares monthly Risk Reports which detail important portfolio composition and trend analysis incorporating asset growth, asset quality, impairments, flow rates of financing delinquency buckets and exposures by industry sectors are reported monthly by Group Risk to executive management and to all meetings of the Board.

5.0 Credit Risk Management (Contd.)

The Bank applies the Standardised Approach to determine the regulatory capital charge related to credit risk exposure.

The Bank determines a list of all types of applicable and approved Shariah transactions and financing. The approved list includes formal exclusions from any engagement by the Bank in certain prohibited industries, such as pork meat, alcohol, and gambling. The approved list is kept up to date and communicated to the relevant personnel within Bank.

The Bank had engaged appropriate experts, including a Shariah advisor to review and ensure that new financing proposals that have not been proposed before or amendments to existing contracts are Shariah-compliant at all times.

5.1 Impairment

5.1.1 Definition of Past Due and Impaired Financing

All financing and advances are categorised as either:

- Neither past due nor impaired;
- Past due but not impaired; or
- Impaired

An asset is considered past due when any payment (whether principal and/or profit) due under the contractual terms are received late or missed.

A financing is classified as impaired under the following circumstances:

(a) where the principal or profit or both[1] is past due or the amount outstanding is in excess of approved limit (for revolving facilities), each for more than 90 days or 3 months; or

(b) the financing exhibits weaknesses that render a classification appropriate to the Bank's Credit Risk Rating Framework, which requires it to fall under the "unlikeliness to repay" category under the Bank's Watchlist Policy.

(c) for financing with repayment schedules on quarterly basis or longer intervals to be classified as impaired as soon as default[2] occurs, unless it does not exhibit any weakness that would render it classified according to the Bank's Credit Risk Rating Framework. Notwithstanding that, these financing shall be classified as impaired when the principal or profit or both is past due for more than 90 days or 3 months.

(d) for distressed rescheduled and restructured ("R/R") facilities, these financing are categorised as "unlikeliness to repay" and classified as impaired. Non-performing R/R facilities remain impaired until re-aged.

[1] For credit card facilities, an account is "past due" when the cardmember fails to settle the minimum monthly repayment due before the next billing date.

[2] "Default" is defined for financings with repayment schedules on a quarterly basis or longer as 1-day past due + 30 days

5.1 Impairment (Contd.)

5.1.2 Methodology for Determination of Individual and Collective Allowances

An assessment is performed to determine whether objective evidence of impairment exists individually for financial assets that are individually significant, and collectively for financial assets that are not individually significant or not individually impaired.

Individual Assessment

Individual assessment is divided into 2 main processes – detection of an event(s) and an assessment of impairment:

(a) Trigger management
In trigger management, financial assets which are above the pre-set individual assessment threshold are assessed using the relevant impairment triggers for objective evidence of impairment.

(b) Valuation of assets
Financial assets which are triggered by the impairment triggers will be measured for evidence of high likelihood of impairment, that is, estimated recoveries (based on the discounted cash flow projection method and taking into account economic conditions) is less than carrying value or fair value is less than the carrying value.

Collective Assessment

All financial assets below the significant threshold and those not assessed to be individually impaired, will be subject to collective assessment and a collective allowance will be computed accordingly.

As a transitional arrangement up to 2012, BNM has given banking institutions the choice of applying either one of the following approaches in computing the required collective assessment:

(a) Transitional approach – where, banking institutions may maintain an allowance of at least 1.5% of total outstanding financing net of individual impairment allowance; or

(b) Full FRS 139 compliance approach – where collective allowances are computed using models based on the banking institutions' historical experience.

The Bank has opted for the transitional approach and has modified it to reflect the Bank's historical loss experience.

Table 5.1: Distribution of gross credit exposures by sector

The distribution of credit exposures by sector of the Bank are as follows:

2011	Primary Agriculture RM'000	Mining and Quarrying RM'000	Manufacturing RM'000	Electricity, Gas and Water RM'000	Construction RM'000	Wholesale, Retail Trade, Restaurant and Hotel RM'000	Transport, Storage and Communication RM'000	Finance, Insurance, Real Estate and Business Activities RM'000	Education and Health RM'000	Household RM'000	Others RM'000	Total RM'000
On Balance Sheet Exposures												
Sovereigns/Central Banks	-	-	-	-	-	-	-	4,376,818	-	-	-	4,376,818
Banks, Development Financial Institutions & Multilateral Development Banks	-	-	-	-	-	-	-	1,150,629	-	-	-	1,150,629
Corporates	86,196	57,284	1,279,919	244,850	811,253	378,010	680,533	1,132,848	308,109	340,658	98,551	5,418,211
Regulatory Retail	6,616	-	25,739	423	8,887	15,930	3,761	25,766	13,708	7,998,950	-	8,099,780
Residential Mortgages	-	-	-	-	-	-	-	-	-	176,840	-	176,840
Other Assets	-	-	-	-	-	-	-	-	-	-	150,280	150,280
Defaulted Exposures	-	20	10,150	-	2,721	23,701	-	12,538	-	168,491	-	217,621
Total On Balance Sheet Exposures	92,812	57,304	1,315,808	245,273	822,861	417,641	684,294	6,698,599	321,817	8,684,939	248,831	19,590,179
Off-Balance Sheet Exposures												
OTC Derivatives	-	-	-	-	-	-	-	15,113	-	-	-	15,113
Off-balance sheet exposures other than OTC Derivatives or Credit Derivatives	28,085	2,420	171,407	25,007	488,836	70,956	91,858	269,095	2,456	1,701,389	140,819	2,992,328
Defaulted Exposures	-	3,511	696	-	400	645	-	212	-	3,402	105	8,971
Total Off-Balance Sheet Exposures	28,085	5,931	172,103	25,007	489,236	71,601	91,858	284,420	2,456	1,704,791	140,924	3,016,412
Total On and Off-Balance Sheet Exposures	**120,897**	**63,235**	**1,487,911**	**270,280**	**1,312,097**	**489,242**	**776,152**	**6,983,019**	**324,273**	**10,389,730**	**389,755**	**22,606,591**

Table 5.2: Impaired and past due financing, individual and collective allowances by sector

The amounts of impaired and past due financing, individual and collective allowances, charges for individual impairment allowances and write offs during the year by sector of the Bank are as follows:

2011	Primary Agriculture RM'000	Mining and Quarrying RM'000	Manufacturing RM'000	Electricity, Gas and Water RM'000	Construction RM'000	Wholesale, Retail Trade, Restaurant and Hotel RM'000	Transport, Storage and Communication RM'000	Finance, Insurance, Real Estate and Business Activities RM'000	Education and Health RM'000	Household RM'000	Others RM'000	Not Allocated RM'000	Total RM'000
Impaired financing	429	106	28,397	1	5,201	23,584	1,714	2,948	1,834	256,119	85	-	**320,418**
Past due financing	23,482	4,008	64,746	635	46,830	64,614	25,011	27,097	18,626	3,561,237	329	-	**3,836,615**
Individual allowances	-	-	13,453	-	1,342	10,652	-	-	-	-	-	-	**25,447**
Collective allowances	-	-	-	-	-	-	-	-	-	-	-	479,010	**479,010**
Charges for individual allowances	-	-	13,040	-	1,342	9,957	-	-	-	-	-	-	**24,339**
Write-offs against individual allowances	-	-	-	-	-	-	-	-	-	-	-	-	**-**

Table 5.3: Geographical distribution of credit exposures

The geographic distribution of credit exposures of the Bank is as follows:

2011	In Malaysia	Outside Malaysia	Total
	RM'000	RM'000	RM'000
On Balance Sheet Exposures			
Sovereigns/Central Banks	4,376,818	-	4,376,818
Banks, Development Financial Institutions & Multilateral Development Banks	1,150,629	-	1,150,629
Corporates	5,418,211	-	5,418,211
Regulatory Retail	8,099,780	-	8,099,780
Residential Mortgages	176,840	-	176,840
Other Assets	150,280	-	150,280
Defaulted Exposures	217,621	-	217,621
Total On Balance Sheet Exposures	19,590,179	-	19,590,179
Off-Balance Sheet Exposures			
OTC Derivatives	15,113	-	15,113
Off-balance sheet exposures other than OTC Derivatives or Credit Derivatives	2,992,328	-	2,992,328
Defaulted Exposures	8,971	-	8,971
Total Off-Balance Sheet Exposures	3,016,412	-	3,016,412
Total On and Off-Balance Sheet Exposures	**22,606,591**	**-**	**22,606,591**

Table 5.4: Geographical distribution of impaired and past due financing, individual and collective allowances

The amounts of impaired and past due financing, individual and collective allowances by geographic distribution of the Bank are as follows:

2011	In Malaysia	Outside Malaysia	Total
	RM'000	RM'000	RM'000
Impaired financing	320,418	-	320,418
Past due financing	3,836,615	-	3,836,615
Individual allowances	25,447	-	25,447
Collective allowances	479,010	-	479,010

Table 5.5: Residual contractual maturity by major types of credit exposure

The residual contractual maturity by major types of gross credit exposures of the Bank is as follows:

2011	Up to 1 month RM'000	>1 to 3 months RM'000	>3 to 6 months RM'000	>6 to 12 months RM'000	>1 to 3 years RM'000	>3 to 5 years RM'000	> 5 years RM'000	No Maturity specified RM'000	Total RM'000
On Balance Sheet Exposures									
Sovereigns/Central Banks	4,186,056	-	-	-	25,501	115,231	50,030	-	4,376,818
Banks, Development Financial Institutions & Multilateral Development Banks	551,584	599,045	-	-	-	-	-	-	1,150,629
Corporates	2,342,911	138,950	75,763	43,834	823,749	399,973	1,593,031	-	5,418,211
Regulatory Retail	295,566	14,642	15,181	86,188	620,275	1,908,685	5,159,243	-	8,099,780
Residential Mortgages	24	19	10	82	1,681	2,817	172,207	-	176,840
Other Assets	42,778	-	-	-	-	-	-	107,502	150,280
Defaulted Exposures	13,892	9,678	3,704	4,230	15,434	54,841	115,842	-	217,621
Total On Balance Sheet Exposures	7,432,811	762,334	94,658	134,334	1,486,640	2,481,547	7,090,353	107,502	19,590,179
Off-Balance Sheet Exposures									
OTC Derivatives	-	-	-	-	10,674	4,439	-	-	15,113
Off-balance sheet exposures other than OTC Derivatives or Credit Derivatives	253,945	141,687	114,681	374,494	176,776	323,375	1,607,370	-	2,992,328
Defaulted Exposures	4,363	244	646	-	211	52	3,455	-	8,971
Total Off-Balance Sheet Exposures	258,308	141,931	115,327	374,494	187,661	327,866	1,610,825	-	3,016,412
Total On and Off-Balance Sheet Exposures	**7,691,119**	**904,265**	**209,985**	**508,828**	**1,674,301**	**2,809,413**	**8,701,178**	**107,502**	**22,606,591**

Table 5.6: Reconciliation of changes to financing impairment allowances

The reconciliation of changes to financing impairment allowances of the Bank are as follows:

2011	Individual impairment allowances RM'000	Collective impairment allowances RM'000
Balance at 1 April	1,108	287,844
Charge for the year – net	24,339	281,169
Amount written-off	-	(90,003)
Balance at 31 March	25,447	479,010

2011	(Charge off)/recoveries RM'000
Bad debts written off during the year	(14,373)
Bad debt recoveries during the year	72,090

6.0 Credit Risk Exposure under the Standardised Approach

The Bank adopts the list of eligible External Credit Assessment Institutions ("ECAIs”) that is allowed by BNM for the following exposure classes:

- Sovereigns and Central Banks
- Banking Institutions
- Corporate
- Securitisations

Depending on the exposure class, the following ratings by the following ECAIs are allowed:

- Standard & Poor’s Rating Services ("S&P")
- Moody’s Investors Service ("Moodys")
- Fitch Rating ("Fitch")
- Rating and Investment Information, Inc
- RAM Rating Services Berhad ("RAM")
- Malaysian Rating Corporation Berhad ("MARC")

Table 6.1: Credit exposures by risk weights under the Standardised Approach

The breakdown of credit risk exposures by risk weights of the Bank is as follows:

2011

Risk Weights	Exposures after Netting and Credit Risk Mitigation										
	Sovereigns and Central Banks	Public Sector Entities	Banks, MDBs and FDIs	Insurance Cos, Securities Firms and Fund Managers	Corporates	Regulatory Retail	Residential Mortgages	Higher Risk Assets	Other Assets	Total Exposures after Netting and Credit Risk Mitigation	Total Risk Weighted Assets
	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000
0%	4,376,818	-	-	-	200,000	-	-	-	7,713	4,584,531	-
20%	-	-	1,155,681	-	111,075	-	-	-	5	1,266,761	253,352
35%	-	-	-	-	-	-	156,735	-	-	156,735	54,857
50%	-	-	14,711	-	51,297	18,394	20,082	-	-	104,484	52,242
75%	-	-	-	-	-	9,591,708	-	-	-	9,591,708	7,193,781
100%	-	-	-	26,650	6,191,450	255,993	5,432	-	142,562	6,622,087	6,622,087
150%	-	-	-	-	66,827	67,734	-	1,038	-	135,599	203,399
Average Risk Weight											
Total	4,376,818	-	1,170,392	26,650	6,620,649	9,933,829	182,249	1,038	150,280	22,461,905	14,379,718
Deduction from Capital Base	-	-	-	-	-	-	-	-	-	-	

Table 6.1: Credit exposures by risk weights under the Standardised Approach (Contd.)

The breakdown of credit risk exposures by risk weights of the Bank is as follows:

2010

Risk Weights	Exposures after Netting and Credit Risk Mitigation										
	Sovereigns and Central Banks	Public Sector Entities	Banks, MDBs and FDIs	Insurance Cos, Securities Firms and Fund Managers	Corporates	Regulatory Retail	Residential Mortgages	Higher Risk Assets	Other Assets	Total Exposures after Netting and Credit Risk Mitigation	Total Risk Weighted Assets
	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000
0%	3,968,110	-	-	-	-	-	-	-	3,549	3,971,659	-
20%	-	29,831	727,831	-	209,137	-	-	-	5	966,804	193,361
35%	-	-	-	-	-	-	128,622	-	-	128,622	45,018
50%	-	-	1,129	-	44,250	10,808	69,457	-	-	125,644	62,822
75%	-	-	-	-	-	8,761,036	-	-	-	8,761,036	6,570,777
100%	-	-	-	303	3,409,241	12,841	13,463	-	91,252	3,527,100	3,527,099
150%	-	-	-	-	137,421	87,086	-	2,910	-	227,417	341,125
Average Risk Weight											
Total	3,968,110	29,831	728,960	303	3,800,049	8,871,771	211,542	2,910	94,806	17,708,282	10,740,202
Deduction from Capital Base	-	-	-	-	-	-	-	-	-	-	

Table 6.2: Rated Exposures according to Ratings by ECAIs

2011

Exposure Class		Ratings of Corporate by Approved ECAIs			
	Moodys	Aaa to Aa3	A1 to A3	Baa1 to Ba3	Unrated
	S&P	AAA to AA-	A+ to A-	BBB+ to BB-	Unrated
	Fitch	AAA to AA-	A+ to A-	BBB+ to BB-	Unrated
	RAM	AAA to AA3	A to A3	BBB1 to BB3	Unrated
	MARC	AAA to AA-	A+ to A-	BBB+ to BB-	Unrated
	Rating & Investment information, Inc.	AAA to AA-	A+ to A-	BBB+ to BB-	Unrated
		RM'000	RM'000	RM'000	RM'000
On and Off-Balance Sheet Exposures					
Credit Exposures (using Corporate Risk Weights)					
Insurance Cos., Securities Firms & Fund managers	**26,650**	-	-	-	26,650
Corporates	**6,620,649**	110,780	47,740	11,308	6,450,821
Total	**6,647,299**	**110,780**	**47,740**	**11,308**	**6,477,471**

Table 6.2: Rated Exposures according to Ratings by ECAIs (Cont'd)

2011

Exposure Class	Ratings of Sovereigns and Central Banks by Approved ECAIs				
	Moodys	Aaa to Aa3	A1 to A3	Baa1 to Baa3	Unrated
	S&P	AAA to AA-	A+ to A-	BBB+ to BBB-	Unrated
	Fitch	AAA to AA-	A+ to A-	BBB+ to BBB-	Unrated
	Rating & Investment information, Inc.	AAA to AA-	A+ to A-	BBB+ to BBB-	Unrated
		RM'000	RM'000	RM'000	RM'000
On and Off-Balance Sheet Exposures					
Sovereigns and Central Banks	4,376,818	-	-	-	4,376,818
Total	4,376,818	-	-	-	4,376,818

2011

Exposure Class	Ratings of Banking Institutions by Approved ECAIs				
	Moodys	Aaa to Aa3	A1 to A3	Baa1 to Baa3	Unrated
	S&P	AAA to AA-	A+ to A-	BBB+ to BBB-	Unrated
	Fitch	AAA to AA-	A+ to A-	BBB+ to BBB-	Unrated
	RAM	AAA to AA3	A1 to A3	BBB1 to BBB3	Unrated
	MARC	AAA to AA-	A+ to A-	BBB+ to BBB-	Unrated
	Rating & Investment information, Inc.	AAA to AA-	A+ to A-	BBB+ to BBB-	Unrated
		RM'000	RM'000	RM'000	RM'000
On and Off-Balance Sheet Exposures					
Banks, MDBs and FDIs	1,170,392	305,921	1,793	301,601	561,077
Total	1,170,392	305,921	1,793	301,601	561,077

7.0 Credit Risk Mitigation

Main types of collateral taken by the Bank

Collateral is generally taken as security for credit exposures as a secondary source of payment in case the counterparty cannot meet its contractual payment obligations from cash flow generation. Types of collateral typically taken by the Bank include:

- Cash and term deposits
- Exchange traded shares, sukuk and marketable securities
- Non-exchange traded debt securities/sukuk
- Unit trusts (including Amanah Saham Nasional, Amanah Saham Bumiputera and mutual funds)
- Non-exchange traded shares
- Residential and non-residential property
- Plantation land, mining land, quarry land and vacant land
- Passenger vehicle, commercial vehicle, construction vehicle and vessel
- Plant and machineries

The Bank can only accept Shariah approved asset as collateral.

Where the customer risk profile is considered very sound (or by nature of the product, for instance small limit products such as credit cards), a transaction may be provided on an “unsecured” basis, that is, not be supported by collateral.

In addition to rating customer’s probability of default via an internal risk rating system, the Bank uses Security Indicators (“SIs”) in its non-retail portfolio to assess the strength of collateral supporting its exposures. Thus both the PD and LGD estimates are used in assessing and monitoring exposures.

Processes for collateral management

To support the development of processes around collateral valuation and management, the concept of legal enforceability and certainty are central to collateral management. In order to achieve legal enforceability and certainty, the Bank has standard collateral instruments, and where applicable, security interest are registered.

Guarantee Support

Guarantee support for financing proposals are an integral component in transaction structuring for the Bank. The guarantee of a financially strong party can help improve the Probability of Default of a transaction through its explicit support of the customer, where customer’s risk grade will be replaced with guarantor’s risk grade.

7.0 Credit Risk Mitigation (Contd.)

Guarantees that are recognised for risk grading purposes may be provided by parties that include associated entities, banks or sovereigns. Credit policy provides threshold parameters to determine acceptable counterparties in achieving risk grade enhancement of the transaction. Guarantee by a counterparty with lower rating than the customer is not recognised as part of the risk grade enhancement.

Use of credit derivatives and netting for risk mitigation

Currently, the Bank does not use credit derivatives and netting for risk mitigation.

Transaction structuring to mitigate credit risk

Besides tangible security and guarantee support described above, credit risk mitigation techniques are used in structuring transactions. These include duration limits managing the number of years the financing is extended, amortisation schedules and financing covenants. These assist in managing credit risk and in providing early warning signals, whereby should financing covenants be breached, the Bank and the customer can work together to address the underlying causes and as appropriate, restructure facilities.

Concentrations of credit risk mitigation

The Bank carefully monitors collateral concentrations via portfolio management reporting and amendments as necessary to its Risk Appetite Framework and related policies governing Financing to Value metrics.

The main types of collateral undertaken by the Bank are properties, motor vehicles and exchange traded shares.

Table 7.1: Credit Risk Mitigation

The total exposures and eligible guarantees, credit derivatives and collateral of the Bank are as follows:

Exposures	Exposures before Credit Risk Mitigation ("CRM") RM'000	Exposures covered by Guarantees / Credit Derivatives RM'000	Exposures covered by Eligible Financial Collateral RM'000
Credit Risk			
On Balance Sheet Exposures			
Sovereigns/Central Banks	4,376,818	-	-
Banks, Development Financial Institutions and Multilateral Development Banks	1,150,629	-	-
Corporates	5,418,211	202,894	60,357
Regulatory Retail	8,099,780	-	14,070
Residential Mortgages	176,840	-	35
Other Assets	150,280	-	-
Defaulted Exposures	217,621	-	3,273
Total On Balance Sheet Exposures	19,590,179	202,894	77,735
Off-Balance Sheet Exposures			
OTC Derivatives	15,113	-	-
Off Balance sheet exposures other than OTC Derivatives or Credit Derivatives	2,992,328	1,190	66,950
Defaulted Exposures	8,971	-	1
Total Off-Balance Sheet Exposures	3,016,412	1,190	66,951
Total On and Off-Balance Sheet Exposures	**22,606,591**	**204,084**	**144,686**

8.0 Off-Balance Sheet Exposures and Counterparty Credit Risk

8.1 Off-Balance Sheet exposures

The Bank's off-balance sheet exposure consists of the following:

- Credit related exposures, e.g. direct credit substitute, certain transaction-related contingent items, short term self liquidating trade-related contingencies, Islamic financing sold to Cagamas, obligations under underwriting agreements, irrevocable commitment to extend credit and unutilised credit card.

- Derivatives Financial Instruments, e.g. equity and commodity related contract (option).

Off-balance sheet exposure is mitigated by setting of credit limit for the respective counterparty and exposure limit for industry sectors which are governed under the Group Risk Appetite Framework.

8.2 Counterparty Credit Risk

Market related credit risk is present in market instruments (derivatives and forward contracts), and comprises counterparty risk (default at the end of contract) and pre-settlement risk (default at any time during the life of contract). Market related credit risk requires a different method in calculating the pre-settlement risk because actual and potential market movements impact the Bank's exposure. The markets covered by this treatment for transactions entered by the Bank include profit rates, foreign exchange, and equities.

For each individual contract, the pre-settlement risk exposure is normally calculated based on the sum of the mark-to-market (MTM) value of the exposure, plus the notional principal multiplied by the potential credit risk exposure (PCRE) factor for the exposure; if the sum of each individual contract is negative, the pre-settlement risk exposure for this contract is deemed to be zero.

Pre-settlement risk exposure = MTM + PCRE factor (or known as add-on factor) x Notional Principal

- The MTM is essentially the current replacement cost of the contract, and can be positive or negative. Where it is positive, that is in the money, the Bank has credit exposure against the counterparty; if it is negative, that is out of the money, the negative value will be used.

- The PCRE factors recognise that prices change over the remaining period to maturity, and that risk increases with time. The PCRE factors are mandated for regulatory capital purposes.

8.2 Counterparty Credit Risk (Contd.)

Maximum pay out method is used for back to back and structured products where the underlying instrument structures are dynamic, that is not confine to a standardised underlying instruments. Where the maximum payout is known, it is taken as the pre-settlement risk amount. However, in situations where the maximum payout is not observable, a Monte Carlo simulation method is used.

Exposure to the counterparty is governed by the counterparty credit limit under the Group Risk Appetite Framework.

Other than credit limit setting and related duration setting of such limits, the Bank's primary tool to mitigate counterparty credit risk by taking collateral.

For derivative exposures, collateral is generally managed via standard market documentation which governs the amount of collateral required and the re-margining frequency between counterparties, including the impact on collateral requirements should either the Bank or the counterparty's credit risk rating be upgraded or downgraded.

Table 8.1: Off-Balance Sheet Exposures

The off-balance sheet exposures and counterparty credit risk of the Bank are as follows:

2011

Description	Principal Amount RM'000	Positive Fair Value of Derivative Contracts RM'000	Credit Equivalent Amount RM'000	Risk Weighted Assets RM'000
Direct credit substitutes	247,796		247,797	247,797
Transaction related contingent items	413,461		206,730	207,212
Short term self liquidating trade related contingencies	148,770		29,754	29,754
Assets sold with recourse	1,589,790		1,588,126	1,193,405
Forward asset purchases	145,137		4,650	2,235
Obligations under an on-going underwriting agreement	192,500		-	-
Equity related contracts	74,822	1,446	4,439	2,220
One year or less			-	-
Over one year to five years	74,822	1,446	4,439	2,220
Over five years			-	-
Other commodity contracts	147,704	1,812	10,674	3,911
One year or less			-	-
Over one year to five years	147,704	1,812	10,674	3,911
Over five years			-	-
Other commitments, such as formal standby facilities and credit lines, with an original maturity of over one year	1,520,857		304,174	300,562
Other commitments, such as formal standby facilities and credit lines, with an original maturity of up to one year	2,636,090		527,218	457,220
Any commitments that are unconditionally cancelled at any time by the bank without prior notice or that effectively provide for automatic cancellation due to deterioration in a borrower's creditworthiness	14,804		-	-
Unutilised credit card lines	464,251		92,850	69,463
Off-balance sheet items for securitisation exposures			-	-
Total	7,595,982	3,258	3,016,412	2,513,779

2010

Description	Principal Amount RM'000	Positive Fair Value of Derivative Contracts RM'000	Credit Equivalent Amount RM'000	Risk Weighted Assets RM'000
Direct credit substitutes	184,794		184,794	184,794
Transaction related contingent items	130,228		65,114	65,772
Short term self liquidating trade related contingencies	90,357		18,071	18,372
Assets sold with recourse	335,852		335,852	253,809
Sell and buy back agreements	306,538		6,286	5,786
Obligations under an on-going underwriting agreement	391,000		-	-
Other commodity contracts	75,500	3,461	9,501	1,900
One year or less	-	-	-	-
Over one year to five years	75,500	3,461	9,501	1,900
Over five years	-	-	-	-
Other commitments, such as formal standby facilities and credit lines, with an original maturity of over one year	160,507		37,415	33,823
Other commitments, such as formal standby facilities and credit lines, with an original maturity of up to one year	1,987,102		-	-
Any commitments that are unconditionally cancelled at any time by the bank without prior notice or that effectively provide for automatic cancellation due to deterioration in a borrower's creditworthiness	8,424		-	-
Unutilised credit card lines	447,639		89,528	66,953
Off-balance sheet items for securitisation exposures			-	-
Total	4,117,941	3,461	746,561	631,209

9.0 Securitisation

The Bank does not have any securitisation exposure in its trading book and banking book nor does it undertake any securitisation activities during the year.

10.0 Operational Risk

The operational risk management process is depicted in the table below:

Identification	• Identify and analyse risks in key processes/activities within Line of Business (including new products)
Assessment/ Measurement	• Incident Management and Data Collection • Risk and Control Self Assessment • Key Risk Indicators
Control/ Mitigation	• Policies addressing control & governance requirements to mitigate specific operational risk • Advisory on establishment of internal control • Contingency planning
Monitoring/ Review	• Monitoring and reporting of loss incidents by Event Type, Portfolio and Line of Business • Periodical review of risk profile within Line of Business

Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external incidents which includes legal risk and Shariah compliance risk (please refer to Chapter 14 for discussion on Shariah Governance). It excludes strategic, systemic and reputational risk.

The strategy for managing operational risk in the Bank is anchored on the three lines of defence concept which are as follows:

- The first line of defence is accountable for implementing the operational risk framework and policies, embedding appropriate internal controls into processes and maintaining business resilience for key activities. The responsibility for managing day-to-day operational risk rests with each Line of Business.

- In the second line, Group Operational Risk is responsible for exercising governance over operational risk through the management of the operational risk framework, policy development, quality assurance of internal controls, operational risk measurement and capital allocation, fraud strategy and reporting of operational risk issues to GOLRC, CEO Committee and RMCD.

10.0 Operational Risk (Contd.)

- Group Internal Audit acts as the third and final line of defence by providing independent assurance on the internal control effectiveness through periodic audit programme.

Group Operational Risk maintains close working relationships with all Line of Business, continually assisting in the identification of operational risks inherent in their respective business activities, assessing the impact and significance of these risks and ensuring that satisfactory risk mitigation measures and controls are in place. Various tools and methods are employed to identify, measure, control and monitor/ report operational risk issues within the Bank. The Operational Risk Management System ("ORMS") contains the following modules:

- The Incident Management and Data Collection ("IMDC") module provides a common platform for reporting an operational risk incident that falls within one of the seven Event Types as stated in Basel II. IMDC also serves as a centralised database of operational risk incidents to model the potential exposure to future operational risks and estimate the amount of economic capital charge.
- The Risk and Control Self Assessment ("RCSA") is a process of continual assessment of risks and controls effectiveness. By using structured questionnaires to assess and measure key risk and its corresponding controls effectiveness, RCSA provides risk profiling across the Bank.
- The Key Risk Indicators ("KRI") module provides early warning of increasing risk and/or control failures by monitoring the changes of the underlying risk measurements.

As part of the risk transfer strategy, the Bank obtains third party protection to cover the Bank's major operational risks. In addition, a comprehensive Business Continuity Management is established to ensure critical business functions can be maintained, or restored in a timely manner, in the event of material disruptions from internal or external events.

The ultimate authority for all operational risk management matters is delegated by the Board of Directors to the CEO Committee. It is in turn, supported by the GOLRC, comprising senior management members of various business divisions and support units. The RMCD, CEO Committee and the GOLRC are the main reporting and escalation committees for operational risk matters. These matters include significant operational risk incidences or findings, deliberations on regulatory and supervisory changes and their impact on operational risk and deliberation and endorsement of operational risk mitigation measures and risk management strategies.

The Bank adopts Basic Indicator Approach for the operational risk capital charge computation.

11.0 Market Risk

Market risk is the risk of losses due to adverse changes in the level or volatility of market rates or prices, such as rates of return, credit spreads, equity prices and foreign exchange rates. The Bank differentiates between two types of market risk: Traded Market Risk ("TMR") and Rate of Return Risk in the Banking Book ("RORBB"). Assessment, control and monitoring of these risks are the responsibility of the Market Risk Unit ("MRU").

11.1 Traded Market Risk ("TMR")

The Traded Market Risk ("TMR") management process is depicted in the table below. Please refer to Section 8 for off-balance sheet exposures and counterparty credit risk arising from market risk.

Identification	• Identify market risks within existing and new products. • Review market-related information such as market trend and economic data.
Assessment/ Measurement	• Recommend / validate methodologies to calculate: o Value-at-Risk ("VaR") o Profit-at-Risk ("PaR") o Capital-at-Risk ("CaR")
Controls/ Mitigation	• Recommend: - VaR limits - PaR limits - CaR limits - Annual and Monthly Loss limits - Greeks (Delta/Gamma/Vega/Theta) limits - Dollar Value of One Basis Point ("DV01") - Position Size - Maximum Tenor - Maximum Holding Period - Stealth Concentration
Monitoring/ Review	• Monitor limits • Periodical review and reporting

TMR arises from transactions in which the Bank acts as principal with clients or the market. It involves taking positions in fixed income, equity or foreign exchange. The objectives of TMR management are to understand, accurately measure and to work with the business to ensure exposures are managed within Board and Executive Management approved limit structures. This is done via robust measurement, setting of limits, limit monitoring and collaboration and agreement with business units on business strategies.

11.1 Traded Market Risk ("TMR") (Contd.)

VaR, PaR, CaR and sensitivity analysis are used to measure, monitor and control TMR exposures. VaR is a quantitative measure which applies recent historic market conditions to estimate potential losses in market value, at a certain confidence level and over a specified holding period. PaR comprises VaR and a loss limit threshold. Loss limit thresholds are intended to trigger management discussion on appropriate mitigation measures to be taken, once certain loss levels are reached.

To complement VaR, CaR is used as a measure of the potential impact on portfolio values of more extreme, albeit plausible, market movements. In addition, CaR is used to gauge and ensure that the Bank is able to absorb extreme, unanticipated market movements.

Apart from VaR, PaR and CaR, additional sensitivity analysis limits (i.e. Greeks/DV01) and indicators are used to monitor changes in portfolio value under potential market conditions such as shifts in currency rates, equity prices and profit rates.

MRU monitors and reports risk exposures against limits on a daily basis. Portfolio market risk positions are also reported to GTMRC, RMCD and the Board of Directors. Furthermore, policies and procedures are in place to ensure prompt action is taken in the event of limit breaches. Business Units exposed to traded market risk are required to maintain risk exposures within their respective thresholds. When risk limits are exceeded, Business Units are required to reduce their exposures immediately to a level below the thresholds unless senior management are consulted and approve alternative strategies to minimise potential losses.

The Bank adopts the Standardised Approach for market risk capital charge computation. This serves as a financial buffer to withstand adverse market movements.

MRU is committed to on-going improvements in market risk processes and systems, and allocates substantial resources to this endeavour.

12.0 Equities (Banking Book Positions)

Equity risk is the potential loss that may be incurred on equity investments in the banking book. The Bank's equity exposures in the banking book are primarily categorised as follows:

- Equity investments that are taken for strategic and other objectives – Where an equity investment is undertaken for a strategic purpose, such investment will be made only after extensive analysis and due diligence. Equity investments undertaken for other business objectives are principally in conjunction with initiatives or measures promoted by the relevant regulatory authorities or trade bodies in which the Bank will jointly with other financial institutions invest in such entities to attain various objectives, such as socio-economic development, promoting the further development of the financial market, the provision of facilities to improve customer service, and support for human capital development for the betterment of the Malaysian banking industry. The Board of Directors' approvals are required prior to committing to all forms of equity investment under this category and, where relevant, the necessary regulatory approval or notification will be obtained or met.

- Equity investments on which capital gains are expected – These transactions are originated and managed by dedicated equity finance teams. These transactions represent funding solutions for known customers of the Bank and are governed by specific policies. The Bank ensures that the investment in these entities does not constitute a controlling interest in the relevant business.

- Equity investments made as the result of a work out of a problem exposure – From time to time, the Bank will take an equity stake in a customer as part of a work out arrangement for problem exposures. These investments are made only where there is no other viable option available and form an immaterial part of the Bank's equity exposures.

12.1 Valuation for and accounting of equity investments in the banking book

Measurement of equity securities – Equity securities that have a quoted market price are carried at their fair value. Fair value is determined based upon current bid prices. If a market for a financial asset is not active, fair value is determined based upon a valuation technique. This includes the use of recent arms-length transactions, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants to price similar instruments. Where fair value is not determined based upon an actively traded market price, judgement is required to take into consideration the impact of liquidity, concentration, uncertainty of market factors, pricing assumptions and other risks affecting the specific instrument. In the event that the fair value of an unlisted security cannot be measured reliably, these investments are measured at cost.

12.1 Valuation for and accounting of equity investments in the banking book (Contd.)

Where the investment is held for long term strategic purposes, these investments are accounted for either as available for sale, with changes in fair value being recognised in equity, or at fair value through profit or loss.

For the periods reported the book value of certain unlisted investments are measured at cost because the fair value cannot be reliably measured. These investments represent minority interests in companies for which active markets do not exist and quote prices are not available. For all other equity exposures book value equals fair value.

Fair value should not differ to the quoted share price. Should a quoted share price not be available, it is estimated using the techniques referred to above.

Table 12.1: Equity investments and capital requirement

An analysis of equity investments by appropriate equity groupings and risk weighted assets of the Bank are as follows:

Non Traded Equity Investments	**2011 RM'000**
Value of quoted (publicly traded) equities	10,000
Value of unquoted (privately held) equities	-
Total	10,000
Net Realised and Unrealised Gains/(Losses)	
Cumulative realised gains/(losses) from sales and liquidations	-
Total unrealised gains/(losses)	-
Total	-
Risk Weighted Assets	
Equity investments subject to a 100% risk weight	10,000
Equity investments subject to a 150% risk weight	-
Total	10,000
Total Minimum Capital Requirement (8%)	800

13.0 Non-Traded Market Risk

13.1 Rate of Return Risk in the Banking Book

The Rate of Return Risk in the Banking Book ("RORBB") risk management process is depicted in the table below:

Identification	• Identify rate of return risks within existing and new products. • Review market-related information such as market trend and economic data.
Assessment/ Measurement	• Non-Traded Value-at-Risk ("VaR") • Earnings-at-Risk ("EaR")
Control/ Mitigation	• Establish non-traded VaR limit and EaR limit.
Monitoring/ Review	• Monitor limits • Periodical review and reporting

RORBB arises from changes in market rates of return that impact core net profit income, future cash flows or fair values of financial instruments. This risk arises from mismatches between repricing dates of assets and liabilities, changes in yield curves, volatilities in profit margin and implied volatilities on rate of return options. The provision of retail and wholesale banking products and services (primarily lending and deposit taking activities) creates rate of return sensitive positions in the Bank's statement of financial position.

The principal objectives of balance sheet risk management are to manage net fund income sensitivity while maintaining acceptable levels of rate of return and funding risk, and to manage the market value of the Bank's capital.

The Board's oversight of RORBB is supported by the Group Asset & Liability Committee ("GALCO"). GALCO is responsible for the alignment of Group-wide risk appetite and funding needs, taking into consideration Group-wide business strategies. GALCO consistently manages the Group's gapping positions, asset growth and liability mix against the rate of return outlook. It also reviews strategies to ensure a comfortable level of rate of return risk is maintained. The Bank has successfully engaged long-term funding to reduce longer tenor rate of return risk, and maintained a comfortable gapping profile as a result. In accordance with Group's policy, positions are monitored on a monthly basis and hedging strategies are used to ensure risk exposures are maintained within board-established limits.

13.1 Rate of Return Risk in the Banking Book (Contd.)

The Bank measures the risk of losses arising from potential adverse movements in market rate of return and volatilities using VaR. VaR is a quantitative measure of rates of return risk which applies recent historic market conditions to estimate the potential loss in market value, at a certain confidence level and over a specified holding period.

The Bank complements VaR by stress testing rate of return risk exposures to highlight potential risk that may arise from extreme market events that are rare but plausible.

Key assumptions in the gap and sensitivity analysis relate to the behaviour of rates of return and spreads, changes in financing and deposit product balances due to behavioural characteristics under different rate of return environments. Material assumptions include the repricing characteristics and the stickiness of indeterminate or non-maturity deposits.

The rate scenarios may include rapid ramping of rates of return, gradual ramping of rate of return, and narrowing or widening of spreads. Usually each analysis incorporates what management deems the most appropriate assumptions about customer behaviour in a rate of return scenario. However, in certain cases, assumptions are deliberately changed to test the Bank's exposure to a specified event.

The Bank's strategy seeks to optimise exposure to rate of return risk within Board-approved limits. This is achieved through the ability to reposition the rate of return exposure of the balance sheet using dynamic product and funding strategies, supported by FRS 139-compliant rate of return hedging activities using profit rate swaps and other derivatives. These approaches are governed by the Bank's policies in the areas of product and liquidity management as well as the banking book policy statements and hedging policies.

RORBB is calculated monthly and reported to GALCO.

13.2 Market Risk Sensitivity – Rate of Return Risk Sensitivity in the Banking Book

The RORBB sensitivity for the Bank is as follows:

MYR	**Rate of Return + 100 bps RM'000**	**Rate of Return - 100 bps RM'000**
Impact on profit before taxation	(29,091)	29,091
Impact on equity	(217,817)	233,984

13.3 Liquidity and Funding Risk

Liquidity risk is the risk that the organisation either does not have sufficient financial resources available to meet all its obligations and commitments as they fall due, or can only access these financial resources at an unreasonable cost. Liquidity risk exposure arises mainly from the deposit taking and borrowing activities, and to a lesser extent, significant drawdown of funds from previously contracted financing and purchase commitments.

The primary objective of the Bank's liquidity risk management is to ensure the availability of sufficient funds at a reasonable cost to honour all financial commitments when they fall due. The secondary objective is to ensure an optimal funding structure and to balance the key liquidity risk management objectives, which includes diversification of funding sources, customer base and maturity period.

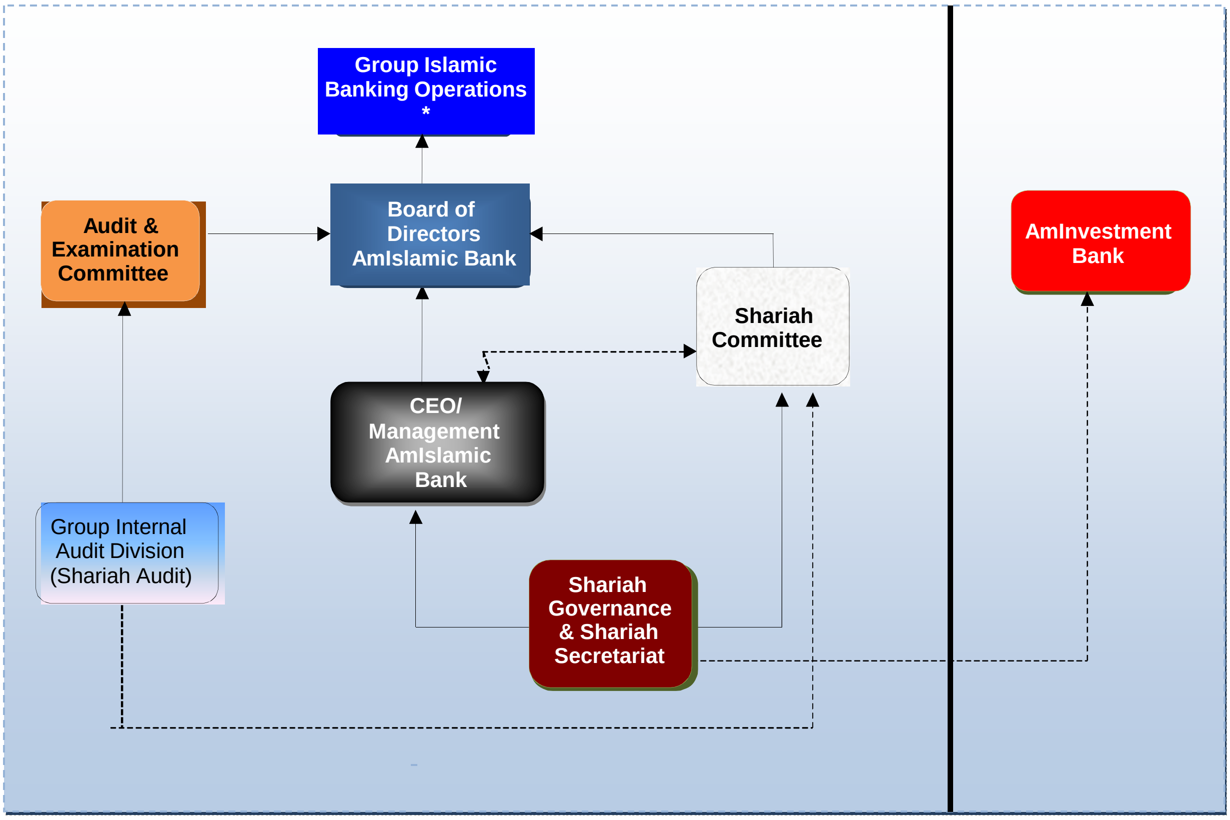
The Group Asset & Liability Committee ("GALCO") is the responsible governing body that approves the Group's liquidity management and strategies policies, and is responsible for setting liquidity limits, proposing liquidity risk policies and contingency funding plan, and practices to be in compliance with local regulatory requirements, and monitor liquidity on an ongoing basis. The Capital and Balance Sheet Management division and Group Risk functions propose and oversee the implementation of policies and other controls relating to the above risks.

In the event of actual liquidity crisis occurring, a Contingency Funding Plan provides a formal process to identify a liquidity crisis and detailing responsibilities among the relevant departments to ensure orderly execution of procedures to restore the liquidity position and confidence in the organisation.

Stress testing is undertaken to assess and plan for the impact for various scenarios which may put the Bank's liquidity at risk. The stress testing output contributes to the development of the liquidity risk limits and the Bank's contingence funding plan.

The Bank stresses the importance of customer deposit accounts as a source of funds to finance lending to customers. They are monitored using the advances to deposit ratio, which compares financing and advances to customers as a percentage of customer deposit accounts, together with term funding with a remaining term to maturity in excess of one year.

14.0 Shariah Governance Structure



* refers to the banking subsidiaries of AMMB.

A Shariah governance framework is put in place in the organisational structure of the Group for its Islamic banking operations, which includes establishment of the Shariah Committee in line with the requirement of Section 3(5)(b) of Islamic Banking Act, 1983 and Bank Negara Malaysia's "Shariah Governance Framework for Islamic Financial Institutions".

AmInvestment Bank Berhad leverages on AmIslamic Bank Berhad's infrastructure on Shariah governance, including the Shariah Committee and the Shariah Secretariat.

14.0 Shariah Governance Structure (Contd.)

Board of Directors

The Board of Directors ("The Board") is accountable and responsible for the overall oversight on Shariah governance structure, including the appointment of Shariah Committee members. The Board performs its oversight through various committees such as Audit & Examination Committee ("AEC"), and Shariah Committee.

Audit Examination Committee

The Audit & Examination Committee is a Board committee responsible for assisting the Board in discharging its responsibilities for the integrity of the Group's financial statements, assessment of the effectiveness of the systems of internal controls and monitoring the effectiveness and objectivity of the internal and external auditors. The Audit & Examination Committee, upon consultation with the Shariah Committee shall determine the deliverables of the Shariah audit function.

Shariah Committee

The Shariah Committee has been established to advise the Group on Shariah matters in business operations in order to ensure compliance with Shariah. The Shariah Committee reports functionally to the Bank's Board of Directors and this provides for the independence of the Shariah Committee in exercising their duties. The main duties and responsibilities of the Shariah Committee are:

(i) to advise Board of Directors on Shariah matters and provide input to the Group Islamic banking operations in order to ensure that the Islamic business operations comply with the Shariah principles at all times;

(ii) to endorse and validate the Group Islamic banking operations products and relevant documentations to ensure compliance with Shariah principles;

(iii) to advice the Group Islamic banking operations on matters to be referred to the Shariah Advisory Council of Bank Negara Malaysia; and

(iv) to advice the Group Islamic banking operations on business zakat, charity and other social programmes.

Management

The management is responsible to make reference to the Shariah Committee on Shariah issues and to take necessary measures for implementation of Shariah Committee's advice and decisions. The management is also responsible to put in place adequate systems and controls in order to ensure compliance with Shariah.

14.0 Shariah Governance Structure (Contd.)

Management shall:

(i) take into account Shariah compliance considerations whenever the Group Islamic banking operations accepts deposits and investment funds, provides financing and carries out investment services for customers;
(ii) ensure that contract documentation complies with Shariah principles;
(iii) ensure that Shariah review and Shariah audit are undertaken periodically; and
(iv) keep track of income not recognised arising out of Shariah non-compliance and assess the probability of similar cases arising in the future.

The Group Islamic banking operations practices first-level check on Shariah requirements by Business Units through Shariah guides and awareness programmes. Each department in the Bank is also designed to interface with Business Units and shared services of the Group. These departments function to bridge the understanding of Shariah requirements and are the frontline to disseminate Shariah requirements as advised by the Shariah Committee. References are made from existing Shariah guides issued by the Shariah Governance section and endorsed by the Shariah Committee.

Shariah Governance section

The Shariah Governance section operates as Secretariat to the Shariah Committee and shall be responsible to ensure all Shariah requirements are met. Amongst the functions of the Shariah Governance section are as follows:

(i) acting under the supervision and guidance of the Shariah Committee, to advice on Shariah compliance in the Group Islamic banking operations;
(ii) to conduct review and provide day-to-day Shariah advice and consultancy to relevant parties;
(iii) to help formulate relevant Shariah guidelines and policies needed to support / guide the Group Islamic banking business operations;
(iv) to conduct research on Shariah matters; and
(v) to provide and assist in Shariah awareness programmes.

14.0 Shariah Governance Structure (Contd.)

Group Internal Audit Division

A designated team within the Group Internal Audit Division is responsible to conduct independent assessment on the level of Shariah compliance of Islamic banking operations as follows:

(i) documents utilised are Shariah compliant and in line with the relevant Shariah concepts applied to a deposit or financing facility;
(ii) Shariah concepts are fully complied with and assets are identifiable, carry adequate value, owned by the Group Islamic banking operations, free from encumbrance and permissible; and
(iii) marketing and customer support staff are competent with the products and corresponding Shariah concepts applied.

The Shariah Committee is responsible to advise the designated audit team on all Shariah audit processes and activities.

14.1 Non-Shariah compliant income

All business activities, products and services offered, and legal documentations are implemented and executed based on legal provisions and Shariah requirements to ensure no occurrence of non-Shariah compliant income. However, should such non-Shariah compliant income exist, it will be channelled to specific charitable bodies. The Shariah Committee is responsible to oversee the management and distribution of the charity fund.