CONSOLIDATED FINANCIAL STATEMENTS

INDEPENDENT AUDITORS' REPORT

To the Shareholders of Arab Insurance Group (B.S.C.)

Report on the consolidated financial statements

We have audited the accompanying consolidated financial statements of Arab Insurance Group B.S.C. ("the Company") and its subsidiaries (together the "Group"), which comprise the consolidated statement of financial position as at 31 December 2013, the consolidated statements of income, comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Responsibility of the board of directors for the consolidated financial statements

The board of directors of the Company is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as the board of directors determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2013, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards.

Report on other regulatory requirements

As required by the Bahrain Commercial Companies Law and the Central Bank of Bahrain (CBB) Rule Book (Volume 3), we report that the Company has maintained proper accounting records and the consolidated financial statements are in agreement therewith; the financial information contained in the directors' report is consistent with the consolidated financial statements; we are not aware of any violations of the Bahrain Commercial Companies Law, the Central Bank of Bahrain and Financial Institutions Law, the CBB Rule Book (Volume 3, applicable provisions of Volume 6 and CBB directives), the CBB Capital Markets Regulations and associated resolutions, rules and procedures of the Bahrain Bourse or the terms of the Company's memorandum and articles of association having occurred during the year that might have had a material adverse effect on the business of the Group or on its financial position; and satisfactory explanations and information have been provided to us by the management in response to all our requests.

KPMG

Kingdom of Bahrain
12 February 2014

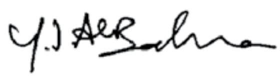
CONSOLIDATED STATEMENT OF FINANCIAL POSITION

AS AT 31 DECEMBER 2013

(US$ '000)

	Note	2013	2012 (restated)	1 January 2012 (restated)
ASSETS				
Cash and bank balances	5	273,231	348,354	359,297
Investments	6	366,707	316,128	305,894
Accrued income	8	84,482	101,560	121,200
Insurance receivables	9	114,332	97,385	101,707
Insurance deposits	10	46,538	45,592	51,478
Deferred policy acquisition costs		28,230	27,992	28,184
Reinsurers' share of technical provisions	11	59,082	59,292	61,496
Other assets	12	56,568	22,103	34,928
Property and equipment	14	27,472	27,675	27,657
		1,056,642	**1,046,081**	**1,091,841**
LIABILITIES				
Technical provisions	15	678,648	671,454	701,874
Insurance payables	18	45,588	31,043	27,252
Borrowings	19	-	20,000	40,000
Other liabilities	20	41,073	42,117	67,596
		765,309	764,614	836,722
EQUITY				
Attributable to shareholders of parent company	21			
Share capital		220,000	220,000	220,000
Treasury stock		(14,793)	(14,793)	(14,793)
Reserves		38,844	41,977	31,360
Retained earnings/(Accumulated deficit)		5,173	(11,955)	(28,323)
		249,224	235,229	208,244
Non-controlling interests	22	42,109	46,238	46,875
		291,333	281,467	255,119
		1,056,642	**1,046,081**	**1,091,841**

These consolidated financial statements were approved by the Board of Directors on 12 February 2014 and signed by:



Khalid A. Al Bustani
Chairman

Dr. Fouad A A Alfalah
Director

Yassir Albaharna
Chief Executive Officer

The accompanying notes 1 to 37 are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF INCOME

FOR THE YEAR ENDED 31 DECEMBER 2013

(US$ '000)

	Note		2013	2012 (restated)
Gross premiums written			261,988	276,517
Net earned premiums			237,712	254,718
Claims and related expenses			(150,103)	(153,353)
Policy acquisition costs			(66,854)	(70,808)
Investment income attributable to insurance funds	24		11,160	11,963
Operating expenses	25		(18,492)	(18,863)
Underwriting result	23		**13,423**	**23,657**
Investment income attributable to shareholders' funds	24		9,263	9,631
Operating expenses – non underwriting activities	25		(10,442)	(9,547)
Borrowing cost			(63)	(407)
Other income	26		4,887	3,891
Other expenses and provisions	27		(2,195)	(10,594)
Profit for the year			**14,873**	**16,631**
Attributable to:				
Non-controlling interests			(3,730)	(922)
Shareholders of Parent Company			18,603	17,553
			14,873	**16,631**
Earnings per share attributable to shareholders (basic and diluted):	28	US$	0.09	0.09

Khalid A. Al Bustani
Chairman

Dr. Fouad A A Alfalah
Director

Yassir Albaharna
Chief Executive Officer

The accompanying notes 1 to 37 are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

FOR THE YEAR ENDED 31 DECEMBER 2013

(US$ '000)

	2013	2012 (restated)
Profit for the year	14,873	16,631
Other comprehensive income		
Items that will be reclassified to profit or loss:		
Changes on remeasurement of available for sale investments	(4,275)	3,936
Transfers for recognition of (gains) / losses on disposal of available for sale investments	(732)	5,054
Items that will not be reclassified subsequently to profit or loss:		
Revaluation of property	-	727
Other comprehensive income for the year	(5,007)	9,717
Total comprehensive income for the year	**9,866**	**26,348**
Attributable to:		
Non-controlling interests	(4,129)	(637)
Shareholders of Parent Company	13,995	26,985
	9,866	**26,348**

The accompanying notes 1 to 37 are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 31 DECEMBER 2013

(US$ '000)

			Reserves							
	Share capital	Treasury stock	Legal	Investment revaluation	Property revaluation	Total	Retained earnings/ (Accumulated deficit)	Attributable to shareholders of parent company	Non-controlling interests	Total Equity
Restated balances at 31 December 2012	**220,000**	**(14,793)**	**29,759**	**5,378**	**6,840**	**41,977**	**(11,955)**	**235,229**	**46,238**	**281,467**
Net profit (loss) for the year	-	-	-	-	-	-	18,603	18,603	(3,730)	14,873
Changes on remeasurement of available for sale investments	-		-	(4,060)	-	(4,060)	-	(4,060)	(215)	(4,275)
Transfers for recognition of gains on disposal of available for sale investments	-	-	-	(548)	-	(548)	-	(548)	(184)	(732)
Total comprehensive income for the year	**-**	**-**	**-**	**(4,608)**	**-**	**(4,608)**	**18,603**	**13,995**	**(4,129)**	**9,866**
Transfer of net depreciation on revalued property	-	-	-	-	(387)	(387)	387	-	-	-
Transfer to non-distributable reserves	-	-	1,862	-	-	1,862	(1,862)	-	-	-
Balances at 31 December 2013	**220,000**	**(14,793)**	**31,621**	**770**	**6,453**	**38,844**	**5,173**	**249,224**	**42,109**	**291,333**
Balances at 1 January 2012 as previously reported	220,000	(14,793)	28,194	(3,327)	6,493	31,360	(14,179)	222,388	58,924	281,312
Impact of changes in accounting policies (note 34)	-	-	-	-	-	-	(14,144)	(14,144)	(12,049)	(26,193)
Restated balances as at 1 January 2012	220,000	(14,793)	28,194	(3,327)	6,493	31,360	(28,323)	208,244	46,875	255,119
Net profit (loss) for the year	-	-	-	-	-	-	17,553	17,553	(922)	16,631
Changes on remeasurement of available for sale investments	-	-	-	3,659	-	3,659	-	3,659	277	3,936
Transfers for recognition of losses on disposal of available for sale investment	-	-	-	5,046	-	5,046	-	5,046	8	5,054
Revaluation of property	-	-	-	-	727	727	-	727	-	727
Total comprehensive income for the year	-	-	-	8,705	727	9,432	17,553	26,985	(637)	26,348
Transfer of net depreciation on revalued property	-	-	-	-	(380)	(380)	380	-	-	-
Transfer to non-distributable reserves	-	-	1,565	-	-	1,565	(1,565)	-	-	-
Restated balances at 31 December 2012	**220,000**	**(14,793)**	**29,759**	**5,378**	**6,840**	**41,977**	**(11,955)**	**235,229**	**46,238**	**281,467**

Parent company balances at (note 37)										
31 December 2013	220,000	(14,793)	31,480	769	6,453	38,702	5,315	249,224	-	249,224
Restated 31 December 2012	220,000	(14,793)	29,620	4,900	6,840	41,360	(11,338)	235,229	-	235,229

The accompanying notes 1 to 37 are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

FOR THE YEAR ENDED 31 DECEMBER 2013

	Note	2013	(US$ '000) 2012 (restated)
CASH FLOWS FROM OPERATING ACTIVITIES			
Premiums received		278,901	297,709
Reinsurance premiums paid		(9,662)	(40,547)
Claims and acquisition costs paid		(247,767)	(276,517)
Reinsurance receipts in respect of claims		15,278	36,583
Investment income		600	307
Interest received		4,352	5,304
Dividends received		1,188	1,138
Operating expenses paid		(25,288)	(25,102)
Other income/expenses, net		(636)	(2,330)
Insurance deposits paid, net		(919)	6,075
Purchase of trading investments		(43,099)	(64,122)
Sale of trading investments		44,088	94,591
Net cash provided by operating activities	32	**17,036**	**33,089**
CASH FLOWS FROM INVESTING ACTIVITIES			
Maturity/sale of investments		112,928	193,214
Purchase of investments		(161,648)	(222,068)
Term deposit with bank		(32,988)	(9,251)
Interest received		5,779	6,024
Dividend received		-	24
Investment income		1,503	6,395
Collateralised cash deposits paid, net		(28,847)	(3,814)
Purchase of property and equipment		(928)	(150)
Purchase of intangible assets		(393)	(422)
Net cash used in investing activities		**(104,594)**	**(30,048)**
CASH FLOWS FROM FINANCING ACTIVITIES			
Borrowings		(20,000)	(20,000)
Interest on borrowings		(371)	(633)
Dividends paid		(43)	(2,501)
Net cash used in financing activities		**(20,414)**	**(23,134)**
Net decrease in cash and cash equivalents		(107,972)	(20,093)
Effect of exchange rate on cash and cash equivalents		(19)	(101)
Effect of assets held for sale on cash and cash equivalents		(120)	-
Cash and cash equivalents, beginning of year		232,196	252,390
Cash and cash equivalents, end of year		**124,085**	**232,196**
Term deposit with bank		149,146	116,158
Cash and bank balances, end of year		**273,231**	**348,354**

The accompanying notes 1 to 37 are an integral part of these consolidated financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2013

1. INCORPORATION AND PRINCIPAL ACTIVITY

Arab Insurance Group (B.S.C.) (the "Company", "parent company") is an international insurance company registered as a Bahraini Shareholding Company having its registered office at Arig House, Manama, Kingdom of Bahrain. The parent company and its subsidiaries (the "Group") are involved in provision of general (non-life) and life reinsurance and related service activities.

2. SIGNIFICANT ACCOUNTING POLICIES

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS), issued by the International Accounting Standards Board and are consistent with prevailing practice within the insurance industry.

The Group's financial statements are presented in U.S. Dollars, which is its functional currency as its share capital and a significant proportion of its business, assets and liabilities are denominated in that currency.

The consolidated financial statements are prepared under the historical cost convention as modified by the revaluation of land and building and certain investment assets.

Comparative figures have been reclassified and restated, where necessary, to conform to the current year's presentation.

The Group has adopted the following new and revised IFRS and interpretations which became effective in 2013:

- IAS 1 - Presentation of items of other comprehensive income

  The amendment to IAS 1 requires that an entity present separately the items of other comprehensive income that would be reclassified to profit or loss in the future if certain conditions are met from those that would never be reclassified to profit or loss. The Group has applied the standard from 1 January 2013. The adoption of the amendment has no material impact on the financial statement.

- IAS 19 - Employee benefits

  The amendments mainly require recognition in other comprehensive income of any actuarial gains and losses resulting from increases or decreases in the present value of defined benefit obligations because of changes in actuarial assumptions and experience adjustments. The Group has applied the standard from 1 January 2013. The adoption of this amendment has no material impact on the financial statements.

- IAS 28 – Investment in associates and joint ventures

  The amended standard requires investments in joint ventures, determined on the basis of IFRS 11 - Joint Arrangements, to be accounted for using the equity method. The earlier standard applied only to investment in associates. The Group has applied the standard from 1 January 2013. This amendment requires that the Group's joint venture Hardy Arig Insurance Management W.L.L. be accounted using the equity method instead of the proportionate method of consolidation adopted earlier.

- IFRS 7 – Financial instruments: Disclosures

  Amendments to IFRS 7 introduce disclosures about the impact of netting arrangements on an entity's financial position requiring the Group to provide information about what amounts have been offset in the statement of financial position and the nature and extent of rights of set off under master netting arrangements or similar arrangements. The Group has applied the standard from 1 January 2013. The adoption of this amendment has no material impact on the financial statements.

- IFRS 10 - Consolidated financial statements

  The standard introduces a single control model that is applicable to all investees; it requires the consolidation of an investee if the Group controls the investee on the basis of:

  - power over the investee
  - exposure to variable returns from the investee
  - the ability to use its power to affect the amount of returns

  In accordance with the transitional provisions of IFRS 10, the Group reassessed the control conclusion for its subsidiaries as at 1 January 2013. As a consequence, the Group has changed its control conclusion in respect of the subsidiary, Takaful Re Limited's participants' (policyholders) funds. The Group has concluded that Takaful Re Limited has control over the participants' funds and as a result the participants' fund accounts have been consolidated retrospectively. Previously Takaful Re Limited's participants' fund accounts were not being consolidated into the Group financial statements. The effect of adopting the standard is disclosed in note 34.

- IFRS 11 – Joint arrangements

  As a result of the adoption of IFRS 11, the Group has changed its accounting policy with respect to its interests in joint arrangements. Under IFRS 11, the Group classifies its interests in joint arrangements as either joint operations or joint ventures depending on the Group's rights to the assets and obligations for the liabilities of the arrangements. The Group re-evaluated its involvement in its only joint venture and has assessed that it is in the nature of a joint venture, since it has a residual interest in the net assets, to be recognised by applying the equity method and is regarded as individually immaterial. There is no

FOR THE YEAR ENDED 31 DECEMBER 2013

2. SIGNIFICANT ACCOUNTING POLICIES (Contd.)

significant impact on the recognised assets, liabilities and comprehensive income of the Group. The effect of adopting the standard is disclosed in note 34.

- IFRS 12 - Disclosures of interests in other entities

  IFRS 12 contains the disclosure requirements for entities that have interests in subsidiaries, joint arrangements (i.e. joint operations or joint ventures), associates and/or unconsolidated structured entities, aiming to provide information to enable users to evaluate the nature of, and risks associated with, an entity's interests in other entities; and the effects of those interests on the entity's financial position, financial performance and cash flows. The Group has applied the standard from 1 January 2013. Necessary disclosures are presented in note 35.

- IFRS 13 - Fair value measurement

  IFRS 13 replaces the fair value measurement guidance contained in individual IFRSs with a single source of fair value measurement guidance. It defines fair value, establishes a framework for measuring fair value and sets out disclosure requirements for fair value measurements. It explains how to measure fair value when it is required or permitted by other IFRSs. It does not introduce new requirements to measure assets or liabilities at fair value nor does it eliminate the practicability exceptions to fair value measurements that currently exist in certain standards. The Group has applied the standard from 1 January 2013. The adoption of this standard has no material impact on the financial statements.

The following standards and interpretations have been issued but not yet effective for the year ended 31 December 2013:

- IAS 19 Employee benefits

  Amendments to IAS 19 apply to contributions from employees or third parties to defined benefit plans. The objective of the amendments is to simplify the accounting for contributions that are independent of the number of years of employee service. The amendments are effective for annual periods beginning on or after 1 January 2014. Early application is permitted. The Group is not expecting a significant impact from the adoption of this amendment.

- IAS 32 Financial instruments: Disclosure and presentation

  Amendments have been made to IAS 32 to clarify the offsetting criteria by explaining when an entity currently has a legally enforceable right to set off. The amendments are effective for annual periods beginning on or after 1 January 2014 and interim periods within those annual periods. Earlier application is permitted. The Group is not expecting a significant impact from the adoption of this amendment.

- IAS 36 Impairment of assets

  Amendments to IAS 36 have expanded disclosures of recoverable amounts for non-financial assets when the amounts are based on fair value less costs of disposals and impairment is recognized. The amendments are effective for annual periods beginning on or after 1 January 2014. Earlier application is permitted. An entity shall not apply those amendments in periods (including comparative periods) in which it does not also apply IFRS 13. The Group is not expecting a significant impact from the adoption of this amendment.

- IFRS 9 'Financial instruments'
  Standard issued October 2010 (IFRS9 (2010))

  IFRS 9 (2010) adds the requirements related to the classification and measurement of financial liabilities, and derecognition of financial assets and liabilities to the version issued in November 2009. It also includes those paragraphs of IAS 39 dealing with how to measure fair value and accounting for derivatives embedded in a contract that contains a host that is not a financial asset, as well as the requirements of IFRIC 9 "reassessment of Embedded Derivatives"

  The Group is yet to assess the impact of IFRS 9. However, initial indications are that it may affect the Group's accounting for its debt available for sale financial assets, as IFRS 9 only permits the recognition of fair value gains and losses in other comprehensive income if they relate to equity investments that are not held for trading. Fair value gains and losses on debt investments not carried at amortised cost will therefore have to be recognised in profit or loss.

  While adoption of IFRS 9 is mandatory from 1 January 2017, earlier adoption is permitted. Prior periods need not be restated. Instead additional transition disclosures will be required on the effect of initial application of IFRS 9 on the classification and measurement of financial instruments.

- Investment Entities (Amendments to IFRS 10 Consolidated Financial Statements and IFRS 12 Disclosure of Interests in Other Entities)

  Amendments to IFRS 10 and IFRS 12, grants certain relief from consolidation to investment entities. It requires qualifying investment entities to account for investment in controlled investees on a fair value basis. The effective date is annual periods beginning on or after 1 January 2014, but early adoption is permitted to enable alignment with the adoption of IFRS 10. The Group is not expecting a significant impact from the adoption of this amendment.

The Group did not early-adopt new or amended standards in 2013.

2. SIGNIFICANT ACCOUNTING POLICIES (Contd.)

The significant accounting policies of the Group are as follows:

Basis of consolidation

The consolidated financial statements include the accounts of the parent company and all of its subsidiaries made up to 31 December 2013.

Subsidiaries are defined as companies that are controlled by the Group, on the basis of

- power over the investee
- exposure to variable returns from the investee
- the ability to use its power to affect the amount of returns.

The purchase method is used to account for acquisitions.

As a result of adoption of IFRS 11, the Group has changed its accounting policy with respect to its interests in joint arrangements. Under IFRS 11, the Group classifies its interests in joint arrangements as either joint operations or joint ventures depending on the Group's rights to the assets and obligations for the liabilities of the arrangements. The Group has re-evaluated its involvement in its only joint venture and has assessed that it is in the nature of a joint venture to be recognised by applying the equity method and is regarded as individually immaterial. There is no significant impact on the recognised assets, liabilities and comprehensive income of the Group.

All intra-group transactions, balances and unrealised surpluses and deficits on transactions between group companies have been eliminated on consolidation. Where necessary, the accounts of subsidiaries have been restated to ensure consistency with the accounting policies adopted by the Group.

A listing of the principal subsidiaries is set out in note 35. In the parent company, these investments are accounted under IAS 39, Financial Instruments: Recognition and Measurement.

Investments

Investment securities are classified as 'at fair value through profit or loss', which includes financial assets held for trading and those designated at fair value on initial recognition, 'available for sale', 'held to maturity' or 'loans and receivables'. Management determines the appropriate classification of investments at the time of purchase.

Securities are classified as at fair value through profit or loss if they are acquired for the purpose of generating a profit from short-term fluctuations in price or if so designated by management. Derivative financial instruments that are not designated as accounting hedge are classified as at fair value through profit or loss. Investments with fixed or determinable payments and fixed maturity that the management has the intent and ability to hold to maturity are classified as held to maturity. Financial instruments with fixed or determinable payments and that are not quoted in an active market are categorised as loans and receivables. Securities intended to be held for an indefinite period of time and those that are not classified as at fair value through profit or loss, held to maturity or loans and receivables, which may be sold in response to needs for liquidity or changes in interest rates, are classified as available for sale.

All purchases and sales of investments are recognised at the settlement date. All investment assets are recognised initially at cost. After initial recognition, investments are valued using principles described below.

Investments at fair value through profit or loss and investments available for sale are carried at fair value. Held to maturity investments and loans and receivables are carried at amortised cost, less any adjustment necessary for impairment.

Fair values are measured using market observable data as far as possible. Fair values are categorised into different levels in a fair value hierarchy based on the inputs used in valuation (see note 33).

Provision for impairment of financial assets

A provision is made in respect of a financial asset that is impaired if its carrying amount is greater than its estimated recoverable amount.

Provisions for assets carried at amortised cost are calculated as the difference between the carrying amount of the assets and the present value of expected future cash flows discounted at their original effective interest rate. By comparison, the recoverable amount of an instrument carried at cost is the present value of expected future cash flows discounted at the current market rate of interest for a similar financial asset.

In the case of available for sale financial assets, the Group assesses at each statement of financial position date whether there is an objective evidence of impairment of such assets. If any such evidence exists, the impairment is recognised in income. Evidence of impairment considers among other factors significant or prolonged decline in market values and financial difficulties of the issuer. Impairment recognised is not reversed subsequently except in case of debt instruments.

Investment in associated companies

Investments in associated companies are accounted for using the equity method. Associated companies are defined as those companies over which the Group is

2. SIGNIFICANT ACCOUNTING POLICIES (Contd.)

able to exercise significant influence, being the power to participate in the financial and operating policy decisions of the company, but not the power to control such policy decisions. Generally, these are companies in which the Group owns 20% to 50% of the voting shares.

Insurance receivables

Insurance receivables are carried at anticipated realisable values after provision for impairment. A provision for impairment is established when there is evidence that the Group will not be able to collect all amounts due according to the terms of the receivables. In case of receivables not specifically impaired, a collective evaluation of impairment is carried out based on historical loss experience. Bad debts are written off during the year in which they are identified. The identification of bad debts is based on an analysis of the financial position of the counter party.

Insurance deposits

Insurance deposits comprise premium and claim deposits with cedants in accordance with policy terms and are carried at anticipated realisable values after provision for impairment. A provision for impairment is established when there is evidence that the Group will not be able to collect all amounts due according to the terms of the deposits. In case of deposits not specifically impaired, a collective evaluation of impairment is carried out based on historical loss experience. Irrecoverable deposits are written off during the year in which they are identified. Irrecoverable deposits are identified on an analysis of the financial position of the counter party.

Intangible assets

Expenditure on software, patents, present value of future profits on acquisition of portfolio and licenses are capitalised and amortised using the straight line basis over their expected useful lives, not exceeding a period of 5 years.

Costs associated with developing computer software programmes are recognised as an expense when incurred. However, costs that are clearly associated with an identifiable and unique product, which will be controlled by the Group and has a probable benefit exceeding the costs beyond one year, are recognised as intangible assets. Costs include staff costs of the development team and an appropriate portion of relevant overheads.

Expenditure, which enhances and extends the benefits of computer software programmes beyond their original specifications and lives is recognised as a capital improvement and added to the original cost of the software. The carrying amount of intangible assets is reviewed annually and adjusted for impairment where it is considered necessary.

Property & equipment and related depreciation

Property & equipment are stated at cost less accumulated depreciation except for the head office land and building which are stated at their revalued amount being fair value on date of valuation by independent external valuers, less accumulated depreciation on buildings. On revaluation, any increase in the carrying amount of the asset is carried in the shareholders' equity as Property Revaluation Reserve and any decrease is recognised as an expense, except to the extent that it reverses decreases or increases previously recognised through income or shareholders' equity. The balance in the Property Revaluation Reserve is transferred directly to Retained Earnings on sale of property and realization of surplus. Further, the difference between depreciation based on the revalued carrying amounts and the depreciation based on original cost of the property is transferred directly from Property Revaluation Reserve to Retained Earnings.

The cost of additions and major improvements are capitalised; maintenance and repairs are charged to expense as incurred. Gains or losses on disposal are reflected in other income. Depreciation is provided on straight-line basis over the expected useful lives of the assets, which are as follows:

Building	40 years
Electrical and mechanical	20 years
Information systems, furniture, equipment and others	3-5 years

Useful lives and residual values are reassessed at each reporting period and adjusted accordingly.

Assets held for sale

Non-current assets, or disposal groups comprising assets and liabilities, are classified as held-for-sale if it is highly probable that they will be recovered primarily through sale rather than through continuing use.

Such assets, or disposal groups, are generally measured at the lower of their carrying amount and fair value less costs to sell. Any impairment loss on a disposal group is allocated first to goodwill, and then to the remaining assets and liabilities on a pro-rata basis, except that no loss is allocated to inventories, financial assets, deferred tax assets, employee benefit assets, investment property or biological assets, which continue to be measured in accordance with the Group's other accounting policies. Impairment losses on initial classification as held-for-sale or held-for-distribution and subsequent gains or losses on remeasurement are recognised in profit or loss.

Once classified as held-for-sale, intangible assets and property, plant and equipment are no longer amortised or depreciated, and any equity-accounted investee is no longer equity accounted.

FOR THE YEAR ENDED 31 DECEMBER 2013

2. SIGNIFICANT ACCOUNTING POLICIES (Contd.)

Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation and a reliable estimate of the amount of the obligation can be made. Employee entitlements are recognised when they accrue to employees, with a provision being carried for the estimated liability as a result of services rendered upto the statement of financial position date.

Post employment obligations

The Group operates a number of defined benefit plans for its employees.

For defined benefit plans, the accounting cost except for actuarial gains or losses, is charged to the income statement so as to spread it over the expected service lives of employees. The accounting costs under these plans are measured as the present value of the estimated future cash outflows using interest rates of government securities, which have terms to maturity approximating the terms of the related liability. Actuarial gains or losses are carried in the comprehensive income statement.

Employee share scheme

The Group operates a cash settled, share-based compensation scheme. The fair value of the employee services received in exchange for virtual shares is recognised as an expense.

The shares are awarded based on the performance during the financial year (scheme year) and is expensed over the scheme year and the vesting period of two years from the end of Scheme year.

At each statement of financial position date, the liability is revalued with reference to the book value of the virtual shares allocated and the impact of the revaluation is recognised in the income statement with a corresponding adjustment to the liability.

Treasury stock

Treasury stock representing shares purchased by the parent company or its consolidated subsidiaries are carried at cost with the exception of holdings as on the date of capital reduction, 4 July 2002, which are carried at nominal value. All treasury stock is presented as a deduction from shareholders' equity and gains and losses from sale of these shares are presented as a change in shareholders' equity.

Recognition of underwriting result

Insurance business is accounted for in a manner consistent with prevailing practice within the insurance industry, more specifically, on an annual accounting basis. Specific accounting policies relating to individual items of insurance revenues and costs and technical provisions are explained below for each relevant item.

Premiums

Gross premiums written comprise the total premiums in relation to contracts incepting during the financial year, together with adjustments arising in the financial year to premiums receivable in respect of business written in previous financial years. It includes an estimate of pipeline premiums, being those premiums written but not reported to the Group at the statement of financial position date. Pipeline premiums are reported as accrued insurance premiums.

Premiums, net of reinsurance, are taken to income over the terms of the related contracts or policies. Unearned premiums are those proportions of the premiums accounted for, which relate to periods of risk that extend beyond the end of the financial year; they are calculated based on a time apportionment basis. A provision for unexpired risks is made for estimated amounts required over and above provisions for unearned premiums to meet future claims and related expenses on business in force at the statement of financial position date. Such provision, where necessary, is made on the basis of an assessment of segments in which policies with similar risk profile are grouped together.

Claims and related expenses

Claims and related expenses are accounted for based on reports received and subsequent review on an individual case basis. Provision is made to cover the estimated ultimate cost of settling claims arising out of events, which have occurred by the end of the financial year, including unreported losses, and claims handling expenses. Provision for unreported claims is established based on actuarial analysis and application of underwriting judgment having regard to the range of uncertainty as to the eventual outcome for each category of business.

Policy acquisition costs

Commissions, taxes, brokerages and other variable underwriting costs directly associated with acquiring business are amortised over the period in which the related premiums are earned. Policy acquisition costs that relate to periods of risk that extend beyond the end of the financial year are reported as deferred policy acquisition costs.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2013

2. SIGNIFICANT ACCOUNTING POLICIES (Contd.)

Reinsurance arrangements

As part of managing its insurance risks, the Group enters into contracts with other reinsurers for compensation of losses on insurance contracts issued by the Group.

Compensations receivable from reinsurers are estimated in a manner consistent with the corresponding claim liability. The benefits and obligations arising under reinsurance contracts are recognised in income and the related assets and liabilities are recognised as accounts receivable, reinsurers' share of technical reserves and accounts payable.

Liability adequacy test

At each statement of financial position date, liability adequacy tests are performed to ensure adequacy of the contractual liabilities net of related deferred acquisition costs. In performing these tests, current best estimates of future contractual undiscounted cash flows and claims handling and administrative expenses are considered. The tests are performed on a portfolio basis where policies with similar risk profile are grouped together as a portfolio.

Investment income

Investment income comprises interest and dividend receivable for the financial year. Gains and losses arising from changes in the fair value of investments at fair value through profit or loss are included in the income statement in the period in which they arise. Gains and losses arising from changes in the fair value of available for sale investments are recognised in other comprehensive income and carried in investment revaluation income as part of equity. When available for sale investments are disposed or are impaired, the related fair value adjustments are included in the income statement.

Investment income arising from insurance business investment assets are allocated to the underwriting results of insurance businesses based on the proportion of their respective insurance funds to shareholders' funds during the financial year.

Foreign currency translation

Transactions denominated in currencies other than U.S. Dollars are recorded at the rates ruling at the date of the transaction. All monetary and non-monetary assets carried at fair value denominated in currencies other than U.S. Dollars are translated at year-end exchange rates.

Unrealised gains or losses on translation are taken to income except in respect of non-monetary available for sale investments, which are taken to equity until they are disposed.

Unrealised gains and losses on translation of financial statements of subsidiaries are included in equity. Other foreign currency gains and losses are taken to income.

Derivative financial instruments and hedging

In the ordinary course of its business, the Group uses forward foreign exchange contracts as fair value hedges to protect its exposures in respect of foreign currency denominated investments and insurance liabilities and these contracts are carried at fair value.

Where a fair value hedge meets the conditions prescribed by International Financial Reporting Standards for qualifying as an effective hedge, gains or losses from remeasuring forward foreign exchange contracts and gains or losses on hedged assets attributable to the hedged risk are recognised in income.

Where the hedge is not effective, gains or losses from remeasuring forward foreign exchange contracts are recognised in income. Gains or losses on hedged assets are recognised in income except in respect of non-monetary available for sale investments, which are taken to equity until they are disposed.

The gain or losses from remeasuring insurance liabilities and related foreign exchange contracts are recognised in income.

FOR THE YEAR ENDED 31 DECEMBER 2013

3. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

In the process of applying its accounting policies, the Group makes estimates and judgements that have an impact on the amounts recognised and reported in the financial statements. These estimates and judgements are based on historical experience, observable market data, published information and other information including expectations of future events that are believed to be reasonable under the circumstances. The estimates and judgements that have a significant impact on the recognised amounts in the financial statements and the processes used to determine these estimates and judgements are described below:

Claims and related expenses

The estimate of ultimate losses arising from existing insurance contracts include unreported claims. Provisions for unreported claims are estimated based on actuarial analysis and application of underwriting judgment having regard to the range of uncertainty as to the eventual outcome for each category of business. The ultimate insurance liability also includes the costs to administer the claims.

Ultimate premiums

The estimate of ultimate premiums is based on premium income estimates provided by cedants which is then adjusted to reflect underwriters' judgement taking into account market conditions and historical data. This estimate is subject to review by underwriters and actuaries.

Other significant estimates include fair value measurement and impairment of financial assets as disclosed in note 2

4. MANAGEMENT OF INSURANCE RISKS

Risks under insurance contracts arise from uncertainty regarding the occurrence of the insured event and the amount of the resulting claim. In addition to underwriting risks, the Group is also exposed to other related risks such as credit, currency and liquidity risks.

The following is a summary of policies adopted to mitigate the key insurance risks facing the Group:

Underwriting risks

The group manages its underwriting risks principally through policies and guidelines for accepting risks and reinsurance arrangements.

Risks are accepted based on an evaluation of pricing and prior underwriting experience in accordance with underwriting guidelines that have been laid out for each line of business. Underwriting guidelines are constantly reviewed and updated to take account of market developments, performance and opportunities. Accumulation limits are set to control exposures to natural hazards and catastrophes. Various underwriting and approval limits are specified for accepting risks.

Acceptance of risks that do not meet specified minimum criteria are subject to agreement of an Underwriting Review Committee comprising representatives from the Marketing, Underwriting and Actuarial functions.

The reinsurance strategy of the Group is designed to protect exposures to individual and event risks based on current risk exposures through cost effective reinsurance arrangements.

Reserving risks are addressed by ensuring prudent and appropriate reserving for business written by the Group, thus ensuring that sufficient funds are available to cover future claims. Reserving practices involve the use of actuarial analysis and application of underwriting judgement. These are supplemented by periodical independent actuarial reviews for determining the adequacy of reserves.

Credit risks

Credit risk under insurance contracts is the risk that a counterparty will be unable to pay amounts in full when due.

Credit risk is controlled through terms of trade for receipt of premium and in certain cases enforcement of premium warranty conditions. Most of the counterparties are insurance companies that are generally not rated. However, there are no significant exposures from any one counterparty.

Reinsurance arrangements are effected with reinsurers whose creditworthiness is assessed on the basis of satisfying minimum rating and financial strength criteria. Exposure to any single reinsurer generally does not exceed a maximum of 25% of total exposure and risks are generally placed with counterparties with minimum investment grade rating except for proportional treaty arrangements placed on reciprocal basis.

FOR THE YEAR ENDED 31 DECEMBER 2013

4. MANAGEMENT OF INSURANCE RISKS (Contd.)

Credit risks relating to reinsurance arrangements are analysed as follows:

(US$ '000)

2013	Receivables	Share of technical provisions	Total
Balance relating to reinsurers:			
- With investment grade rating	2,215	39,693	41,908
- Other	20,056	5,922	25,978
	22,271	**45,615**	**67,886**
2012			
Balance relating to reinsurers:			
- With investment grade rating	2,136	30,647	32,783
- Other	21,613	11,946	33,559
	23,749	**42,593**	**66,342**

Currency risks

As the Company writes business in various currencies, it is exposed to currency risk. Foreign exchange currency risks are hedged where exposures are significant and facility to hedge is available.

(US$ '000)

2013	Euro	Pound Sterling	Indian Rupee	Canadian Dollar	Other
Reinsurance Assets (Liabilities), net	(2,205)	2,662	(9,838)	(475)	(99,490)
Hedged	(2,413)	(1,065)	-	959	-
2012					
Reinsurance Assets (Liabilities), net	(3,930)	(451)	(10,778)	(610)	(97,363)
Hedged	(2,815)	(870)	-	(1,011)	-

Liquidity risks

Liquidity risk is the risk that cash may not be available to pay obligations when due. Limits have been specified in the investment policy and guidelines that requires a significant portion of investment funds representing insurance liabilities to be held in cash or readily marketable debt securities.

Sensitivity analysis

The sensitivity of the Group's income and equity to market risks is as follows:

(US$ '000)

	2013	2012
5% increase in loss ratio	(11,886)	(12,736)
5% decrease in loss ratio	11,886	12,736
10% increase in US Dollar exchange rate	10,935	11,071
10% decrease in US Dollar exchange rate	(10,498)	(10,624)

FOR THE YEAR ENDED 31 DECEMBER 2013

5. CASH AND BANK BALANCES

(US$ '000)

	2013	2012
Cash and bank balances	80,506	82,331
Deposits with maturity within 3 months	43,579	149,865
Deposits with maturity over 3 months	149,146	116,158
	273,231	**348,354**

Bank deposits amounting to US$ Nil (2012: US$: 24.8 million) have been pledged against borrowings.

Details of significant terms and conditions, exposures to credit, interest rate and currency risks are as follows:

Credit risk

Bank balances and deposits with short term maturities are held with leading financial institutions. The Group limits its concentration of time deposits with any one financial institution to a maximum of 10% of shareholders' equity.

Interest rate risk

	2013	2012
Interest receivable basis:		
- Bank balances	Daily/Monthly	Daily/Monthly
- Deposits with short term maturities	On maturity	On maturity
Effective rates	0.01% to 2.70 %	0.125% to 2.50 %

As the deposits are short term maturities, there is no sensitivity to interest rate fluctuation.

Currency risk

(US$ '000)

	2013	2012
U.S. Dollar	141,926	154,313
Bahraini Dinar	69,992	83,368
UAE Dirham	32,712	66,142
Qatari Riyal	19,471	32,941
Other	9,130	11,590
	273,231	**348,354**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2013

6. INVESTMENTS

		(US$ '000)
	2013	2012
At fair value through profit or loss		
Held for trading		
Common stock of listed companies	53,934	45,476
	53,934	45,476
Designated at fair value on initial recognition		
Debt Securities		
- Other investment grade	24,206	23,851
- Other	17,737	8,449
	41,943	32,300
Held to maturity		
Debt securities		
- Supra-nationals and OECD country governments	22,973	36,975
- Other investment grade	20,024	26,045
- Non OECD country government	2,663	2,655
- Other	9,850	-
	55,510	65,675
Available for sale		
Debt securities		
- Supra-nationals and OECD country governments	32,694	21,995
- Other investment grade	118,796	73,104
- Non-OECD country governments	2,648	6,803
- Other	38,342	44,584
Common stock of listed companies	-	813
Common stock of unlisted companies	7,160	6,808
Other	15,542	18,164
	215,182	172,271
Investment in joint venture	119	127
Investment in associate	19	279
	366,707	**316,128**

FOR THE YEAR ENDED 31 DECEMBER 2013

6. INVESTMENTS (Contd.)

Movements in the Group's impairment recognised on available for sale investments are as follows:

		(US$ '000)
	2013	2012
At 1 January	18,660	17,460
Impairment recognised during the year		
- Unlisted companies	312	86
- Others	1,291	1,416
Reversal on sale of investments	(318)	(302)
At 31 December	**19,945**	**18,660**

Debt securities amounting to US$ 72.7 million (2012: US$ 66.3 million) have been pledged as security for reinsurance trust agreements, letters of credit and guarantees.

Details of significant exposures to credit, interest rate and currency risks on investments are as follows:

Credit risk

The Group limits its investment concentration in debt securities in any one investee and in any one industry group to 10% and 20% respectively, of the total debt securities portfolio.

The Group also limits its investment concentration in common stock of listed companies of any one issue and any one issuer to 5% and 10% respectively, of its total common stock portfolio.

Debt securities - interest rate risk

2013	Interest receivable basis	Effective rates	Coupon rates
Supra-nationals and OECD country government securities	Monthly/Semi-annual/ Annual	0.125% - 2.875%	0.125% - 2.875%
Other investment grade debt securities	Semi-annual/Annual	1.6% - 7.25%	1.6% - 7.25%
Non-OECD country government securities	Semi-annual/Annual	3.6% - 4.3%	3.6% - 4.3%
Other securities	Monthly/Semi-Annual	1.357% - 4.61%	1.357% - 4.718%

2012			
Supra-nationals and OECD country government securities	Monthly/Semi-annual/ Annual	0.13% - 4.14%	0.125% - 4.25%
Other investment grade debt securities	Semi-annual/Annual	1.25% - 6.81%	1.25% - 7.38%
Non-OECD country government securities	Semi-annual/Annual	1.8 % - 4.3%	1.80% - 4.3%
Other securities	Monthly/Semi-Annual	2.08% - 4.02%	2.10% - 4.15%

FOR THE YEAR ENDED 31 DECEMBER 2013

6. INVESTMENTS (Contd.)

Debt securities – currency risk

(US$ '000)

2013	U.S. Dollar	Euro	Bahraini Dinar	Other	Total
Supra-nationals and OECD country government securities	55,667	-	-	-	55,667
Other investment grade debt securities	152,964	7,270	-	2,792	163,026
Non-OECD country governments	-	-	5,311	-	5,311
Other debt securities	65,929	-	-	-	65,929
	274,560	**7,270**	**5,311**	**2,792**	**289,933**
2012					
Supra-nationals and OECD country government securities	58,970	-	-	-	58,970
Other investment grade debt securities	110,902	8,964	-	3,134	123,000
Non-OECD country governments	-	-	8,098	1,360	9,458
Other debt securities	53,033	-	-	-	53,033
	222,905	**8,964**	**8,098**	**4,494**	**244,461**

Debt securities - remaining term to maturity

The principal amount and book values of debt securities are shown in the table below by contractual maturity.

(US$ '000)

	2013		2012	
	Principal amount	Book value	Principal amount	Book value
Supra-nationals and OECD country government securities:				
- Due in one year or less	14,000	14,001	18,000	18,023
- One to five years	35,000	35,147	39,000	39,255
- More than five years	7,000	6,519	2,000	1,692
	56,000	55,667	59,000	58,970
Debt securities of other investment grade issuers:				
- Due in one year or less	9,739	10,365	10,200	10,420
- One to five years	96,539	98,735	85,343	90,658
- More than five years	54,452	53,926	20,488	21,922
	160,730	163,026	116,031	123,000
Non-OECD country government securities:				
- Due in one year or less	-	-	1,360	1,360
- One to five years	2,658	2,663	5,316	5,505
- More than five years	2,658	2,648	2,658	2,593
	5,316	5,311	9,334	9,458
Other debt securities :				
- Due in one year or less	-	-	1,000	999
- One to five years	38,651	38,044	36,139	36,085
- More than five years	21,394	27,885	15,975	15,949
	60,045	65,929	53,114	53,033
	282,091	**289,933**	**237,479**	**244,461**

FOR THE YEAR ENDED 31 DECEMBER 2013

6. INVESTMENTS (Contd.)

Common stock

Common stocks have no fixed maturity dates and are generally not exposed to interest rate risk. Dividends are generally declared on an annual basis.

The book value of common stock classified by currencies in which they are denominated are as follows:

(US$ '000)

	2013	2012
U.S. Dollar	35,250	27,685
Euro	2,574	2,065
Bahraini Dinar	489	593
Saudi Riyal	6,004	7,117
Pound Sterling	3,276	2,777
Japanese Yen	2,040	2,168
Other	11,461	10,692
	61,094	**53,097**

Commitments

The Group has commitments in respect of uncalled capital in available for sale investments amounting to US$ 8.0 million (2012: US$ 6.4 million).

7. SENSITIVITY ANALYSIS

The sensitivity of the Group's profit or loss and total equity to market risks on its cash and cash equivalents and investments is as follows:

(US$ '000)

	2013		2012	
	Income	Equity	Income	Equity
Interest rate				
+ 100 basis points shift in yield curves- debt instruments	(846)	(5,305)	(859)	(4,233)
– 100 basis points shift in yield curves- debt instruments	851	5,488	888	3,972
Currency risk				
10% increase in US Dollar exchange rate	(10,413)	132	(16,570)	215
10% decrease in US Dollar exchange rate	21,450	123	20,253	(176)
Equity price				
10% increase in equity prices	1,060	134	4,614	212
10% decrease in equity prices	(1,060)	(134)	(4,614)	(212)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2013

8. ACCRUED INCOME

(US$ '000)

	2013	2012
Accrued insurance premiums		
Expected to be received :		
- Within 12 months	60,322	71,828
- After 12 months	21,860	26,661
	82,182	98,489
Accrued interest		
- Expected to be received within 12 months	2,300	3,071
	84,482	**101,560**

9. INSURANCE RECEIVABLES

(US$ '000)

	2013	2012
Balances due :		
- Within 12 months	113,777	97,028
- After 12 months	555	357
	114,332	**97,385**

Movements in the Group's provision for impaired receivables are as follows:

(US$ '000)

	2013	2012
At 1 January	20,791	18,398
Provision for impairment	385	2,393
31 December	**21,176**	**20,791**

The individually impaired receivables mainly relate to counter party in financial difficulty. The ageing of these receivables is as follows:

(US$ '000)

	2013	2012
Over two years	5,385	10,869
	5,385	**10,869**

Receivables that are less than 12 months past due are not considered impaired. The ageing analysis of these receivables is as follows:

(US$ '000)

	2013	2012
Upto 6 months	12,124	12,012
6 to 12 months	13,628	15,322
	25,752	**27,334**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2013

10. INSURANCE DEPOSITS

(US$ '000)

	2013	2012
Balances due :		
- Within 12 months	31,502	32,453
- After 12 months	15,036	13,139
	46,538	**45,592**

Movements in the Group's provision for impaired deposits are as follows:

(US$ '000)

	2013	2012
At 1 January	4,693	5,882
Provision for impairment written back	(485)	(1,189)
31 December	**4,208**	**4,693**

The individually impaired deposits mainly relate to counter parties in financial difficulty. The ageing of these deposits is as follows:

(US$ '000)

	2013	2012
Under ten years	893	891
Over ten years	6,460	6,278
	7,353	**7,169**

Deposits that are less than 3 years past due are not considered impaired. The ageing analysis of these deposits is as follows:

(US$ '000)

	2013	2012
Up to 1 year	7,855	6,596
1 to 3 years	25,875	26,267
	33,730	**32,863**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2013

11. REINSURERS' SHARE OF TECHNICAL PROVISIONS

		(US$ '000)
	2013	2012
General insurance business		
- Claims outstanding	45,420	42,036
- Unreported claims	8,388	13,021
- Deferred retrocession premium reserve	5,079	3,644
	58,887	58,701
Life insurance business		
- Claims outstanding	195	573
- Deferred retrocession premium reserve	-	18
	195	591
	59,082	**59,292**

12. OTHER ASSETS

		(US$ '000)
	2013	2012
Intangible assets :		
- Computer software	11,336	10,944
	11,336	10,944
Less : accumulated amortisation	(10,167)	(9,796)
Net intangible assets	1,169	1,148
Disposal group held for sale (Note 13)	543	-
Other assets due within 12 months:		
- Collateralised cash deposits	45,353	16,506
- Prepayments and other receivables	9,503	4,449
	55,399	20,955
	56,568	**22,103**

		(US$ '000)
	2013	2012
Movement in intangible assets:		
Net book value at 1 January	1,148	1,088
- Additions	393	422
- Amortisation charge	(372)	(362)
Net book value at 31 December	**1,169**	**1,148**

Collateralised cash deposits have been pledged as security for reinsurance letters of credit and guarantees.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2013

13. DISPOSAL GROUP HELD FOR SALE

In December 2013, management committed to a plan to sell 51% of its equity stake in ARIMA Insurance Solutions W.L.L. Accordingly, ARIMA is presented as a disposal group held for sale. Sale is expected to be completed during 2014. The arrangement was approved by the board of directors at the meeting held on 8 December 2013. An impairment of US$ 55 thousand has been recorded as the sale price is lower than the carrying amount.

At 31 December, the disposal group include:

	(US$ '000)
	2013
Assets of disposal group held for sale:	
- Cash	20
- Accounts receivables	757
	777
Liabilities of disposal group held for sale:	
- Accrued expenses and other payables	234
	234

The results relating to assets held-for-sale included in the consolidated statement of income are as follows:

		(US$ '000)
	2013	2012
Income	1,945	2,176
Expenses	(1,918)	(1,939)
	27	**237**

The cash flow relating to assets held-for-sale included in the consolidated statement of cash flows are as follows:

		(US$ '000)
	2013	2012
Net cash used in operating activities	(100)	(124)
	(100)	**(124)**

The fair value has been measured on the indicative price multiple expected from the buyer for this disposal group and classified as level 1 in fair value hierarchy.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2013

14. PROPERTY AND EQUIPMENT

(US$ '000)

	2013	2012
Land	1,340	1,340
Building	26,741	7,221
Work in progress	50	19,058
Information systems, furniture, equipment and other	14,217	13,941
	42,348	41,560
Less: accumulated depreciation	(14,876)	(13,885)
	27,472	**27,675**
Movements in property and equipment		
Net book value at 1 January	27,675	27,657
- Revaluation of property	-	727
- Additions	928	150
- Disposals	(6)	(1)
- Depreciation charge	(1,125)	(858)
Net book value at 31 December	**27,472**	**27,675**

Land and Building comprises the head office property owned and occupied by the Company since 1984. The property was revalued in March 2012 by independent external valuers and classified as level 2 in the fair value measurement hierarchy as it has been valued using indicative transaction prices for similar payments and adjusted to reflect the characteristics of the property. Building also includes office premises of the subsidiary Takaful Re Limited in Dubai, U.A.E; US$ 19.1 million. This property, earlier carried as work in progress, was brought into use during the year and carried at cost.

15. TECHNICAL PROVISIONS

Technical provisions comprise

(US$ '000)

	2013	2012
General insurance business		
Claims outstanding	323,420	301,039
Unreported losses	156,667	174,235
Unearned premiums	117,642	109,740
	597,729	**585,014**
Life insurance business		
Claims outstanding	15,271	15,141
Unreported losses	58,828	65,333
Unearned premiums	6,820	5,966
	80,919	86,440
	678,648	**671,454**

The mean term of reserves is 2.9 years and 2.7 years for non-life and life business respectively.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2013

16. CLAIMS DEVELOPMENT

The table below shows the incurred gross and net claims including unreported losses computed with reference to earned premiums, compared with previous estimates for the last 5 years:

(US$ '000)

	Underwriting year						
	2008	2009	2010	2011	2012	2013	Total
Gross							
Estimate of incurred claims costs:							
- At end of underwriting year	113,740	123,596	119,232	128,402	113,735	112,367	
- One year later	209,160	209,836	210,700	205,558	178,609	-	
- Two years later	216,027	208,488	227,383	210,058	-	-	
- Three years later	221,811	203,983	229,046	-	-	-	
- Four years later	219,615	198,608	-	-	-	-	
- Five years later	217,642	-	-	-	-	-	
Current estimate of incurred claims	217,642	198,608	229,046	210,058	178,609	112,367	1,146,330
Cumulative payments to date	(186,955)	(161,723)	(182,616)	(125,349)	(80,814)	(5,021)	(742,478)
Liability recognised	30,687	36,885	46,430	84,709	97,795	107,346	403,852
Liability in respect of prior years							150,334
Total liability included in the statement of financial position							**554,186**

Net							
Estimate of incurred claims costs:							
- At end of underwriting year	111,183	121,438	103,286	112,047	108,594	110,213	
- One year later	204,736	207,630	189,981	175,123	166,667	-	
- Two years later	211,446	204,279	187,265	181,617	-	-	
- Three years later	216,730	199,358	186,509	-	-	-	
- Four years later	214,641	193,791	-	-	-	-	
- Five years later	212,684	-	-	-	-	-	
Current estimate of incurred claims	212,684	193,791	186,509	181,617	166,667	110,213	1,051,481
Cumulative payments to date	(182,517)	(157,892)	(140,529)	(107,101)	(74,225)	(2,944)	(665,208)
Liability recognised	30,167	35,899	45,980	74,516	92,442	107,269	386,273
Liability in respect of prior years							113,910
Total liability included in the statement of financial position							**500,183**

FOR THE YEAR ENDED 31 DECEMBER 2013

17. MOVEMENTS IN INSURANCE LIABILITIES AND ASSETS

(US$ '000)

	Gross	Reinsurance	Net
2013			
Claims			
Claims outstanding	316,180	42,609	273,571
Unreported losses	239,568	13,021	226,547
Total at beginning of year	555,748	55,630	500,118
Change in provision during the year	161,963	11,599	150,364
Claims settled during the year	(163,525)	(13,226)	(150,299)
Balance at end of year	**554,186**	**54,003**	**500,183**
Unearned premium			
At beginning of year	115,706	3,662	112,044
Change in provision during the year	8,756	1,417	7,339
Balance at end of year	**124,462**	**5,079**	**119,383**
Accrued insurance premium			
At beginning of year	103,201	4,712	98,489
Movement during the year	(16,994)	(687)	(16,307)
Balance at end of year	**86,207**	**4,025**	**82,182**
Deferred policy acquisitions costs			
At beginning of year	28,178	186	27,992
Movement during the year	174	(64)	238
Balance at end of year	**28,352**	**122**	**28,230**

2012			
Claims			
Claims outstanding	319,372	50,758	268,614
Unreported losses	260,411	5,978	254,433
Total at beginning of year	579,783	56,736	523,047
Change in provision during the year	184,290	31,524	152,766
Claims settled during the year	(208,325)	(32,630)	(175,695)
Balance at end of year	**555,748**	**55,630**	**500,118**
Unearned premium			
At beginning of year	120,595	4,760	115,835
Change in provision during the year	(4,889)	(1,098)	(3,791)
Balance at end of year	**115,706**	**3,662**	**112,044**
Accrued insurance premium			
At beginning of year	123,853	5,867	117,986
Movement during the year	(20,652)	(1,155)	(19,497)
Balance at end of year	**103,201**	**4,712**	**98,489**
Deferred policy acquisitions costs			
At beginning of year	28,499	316	28,183
Movement during the year	(321)	(130)	(191)
Balance at end of year	**28,178**	**186**	**27,992**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2013

18. INSURANCE PAYABLES

(US$ '000)

	2013	2012
Due Within 12 months	45,588	31,043
	45,588	**31,043**

19. BORROWINGS

(US$ '000)

	2013	2012
Balances Due:		
- Within 12 months	-	20,000
	-	**20,000**

Borrowings amounting to US$ Nil (2012: US$ 20 million) are secured by bank deposits. The effective interest rate on the borrowings was 1.3% (2012: 1.7%).

20. OTHER LIABILITIES

(US$ '000)

	2013	2012
Post-employment benefits (note 30)	14,058	12,484
Reinsurance premiums accrued	8,619	8,619
Dividends payable	1,928	1,971
Accrued expenses	7,245	8,882
Employee share scheme (note 29)	3,440	2,480
Other	5,783	7,681
	41,073	**42,117**
Balances due:		
- Within 12 months	23,575	27,153
- After 12 months	17,498	14,964
	41,073	**42,117**

21. SHAREHOLDERS' EQUITY

Share capital

a) Composition

(US$ '000)

	2013	2012
Authorised 500 million ordinary shares of US$ 1 each	500,000	500,000
Issued, Subscribed & Fully Paid-up 220 million (2012: 220 million) ordinary shares of US$ 1 each	220,000	220,000

FOR THE YEAR ENDED 31 DECEMBER 2013

21. SHAREHOLDERS' EQUITY (Contd.)

b) Major Shareholders

Shareholders who have an interest of 5% or more of the outstanding shares are as shown below:

Name	Nationality	No. of shares (in millions)		% of total outstanding shares	
		2013	2012	**2013**	2012
Central Bank of Libya	Libya	31.8	31.8	16.1	16.1
Emirates Investment Authority	UAE	30.5	30.5	15.4	15.4
General Pension & Social Security Authority	UAE	27.5	27.5	13.9	13.9
Kuwait Investment Authority	Kuwait	20.0	20.0	10.1	10.1
Real Estate Bank	UAE	11.0	11.0	5.6	5.6

c) Shareholding pattern

The shareholding pattern in the outstanding shares of the Company is as follows:

Shares	No. of shares (in millions)		No. of shareholders		% of total outstanding shares	
	2013	2012	**2013**	2012	**2013**	2012
Less than 1%	42.7	46.3	4,677	4,779	21.5	23.3
1% to 5%	34.5	30.9	8	6	17.4	15.6
5% to 10%	11.0	11.0	1	1	5.6	5.6
10% and above	109.8	109.8	4	4	55.5	55.5

Treasury stock

The company held 21,967,818 of its own shares at 31 December 2013 (2012: 21,967,818 shares) and is carried at cost US$ 14,793,000 (2012: US$ 14,793,000).

Legal reserve

In accordance with applicable legal provisions, the Group is required to set aside 10% of net profits each year to build a Legal Reserve up to a maximum of 100% of the paid up value of its share capital.

Investment revaluation reserve

Investment Revaluation Reserve comprises gains or losses arising from remeasurement of available for sale investment assets. These gains or losses are carried in the reserve until the assets are disposed of, at which time the gains or losses are included in income.

Property revaluation reserve

Property Revaluation Reserve represents the difference between the cost of buildings less accumulated depreciation and their fair values. Further, the difference between depreciation based on the revalued carrying amounts and the depreciation based on original cost of the property is transferred directly from Property Revaluation Reserve to Retained Earnings.

FOR THE YEAR ENDED 31 DECEMBER 2013

21. SHAREHOLDERS' EQUITY (Contd.)

Capital management

The Group's total capital comprises paid-up capital, legal reserve and retained earning less treasury shares. The Group's policy is to maintain a strong capital base so as to maintain client, investor and market confidence and to sustain future development of the business. The parent company is regulated by Central Bank of Bahrain, which sets and monitors capital requirement for the parent company. Central Bank of Bahrain (CBB) requires the parent company to compute the solvency margin requirement in accordance with provisions of the CBB Rule Book. The Company is in compliance with the required margin of solvency.

Additionally, the Company manages its capital adequacy on an evaluation of its capital requirement through risk based capital models.

22. NON-CONTROLLING INTERESTS

(US$ '000)

	2013	2012
At 1 January	46,238	58,924
Impact of changes in accounting policies (note 34)	-	(12,049)
Restated at 1 January	46,238	46,875
Share of comprehensive income	(4,129)	(637)
At 31 December	**42,109**	**46,238**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2013

23. SEGMENT INFORMATION

Analysis of revenue by primary business segment

The Group's reinsurance business consists of two main business segments, Non-life and Life. Non-life business primarily consists of Property, Engineering, Marine, Accident, Whole Account & other classes. Life business mainly involves short term group life policies and long term life policies. Life portfolio does not contain investment linked policies.

(US$ '000)

	Non-life						Life		Total
2013	Property	Engineering	Marine	Accident	Whole Account	Others	Short term	Long term	
REVENUES									
Gross premiums written	77,319	34,351	19,075	19,846	54,867	31,510	24,616	404	261,988
Outward reinsurance premiums	(4,895)	(6,683)	4,937	778	(8,336)	(827)	(286)	(424)	(15,736)
Change in unearned premiums - gross	5,174	2,329	1,586	(153)	(13,476)	(4,182)	(1,071)	223	(9,570)
Change in unearned premiums - reinsurance	(18)	(111)	(86)	(33)	1,567	(270)	(19)	-	1,030
Net earned premiums	77,580	29,886	25,512	20,438	34,622	26,231	23,240	203	237,712
Investment income attributable to insurance funds	2,449	1,145	553	1,588	1,403	1,853	873	1,296	11,160
	80,029	31,031	26,065	22,026	36,025	28,084	24,113	1,499	248,872
COSTS AND EXPENSES									
Gross claims paid	(61,567)	(19,204)	(16,657)	(9,442)	(4,839)	(29,583)	(15,368)	(6,865)	(163,525)
Claims recovered from reinsurers	11,084	1,198	(750)	710	(1,441)	2,234	191	-	13,226
Change in provision for outstanding claims - gross	(9,190)	(5,230)	699	(549)	(13,567)	3,853	466	(539)	(24,057)
Change in provision for outstanding claims - reinsurance	151	(500)	(230)	143	5,355	(375)	(378)	-	4,166
Change in provision for unreported losses - gross	2,188	5,595	5,398	(38)	(958)	7,875	(904)	7,380	26,536
Change in provision for unreported losses - reinsurance	(2,045)	688	(103)	(305)	(3,764)	(948)	32	(4)	(6,449)
Claims and related expenses	(59,379)	(17,453)	(11,643)	(9,481)	(19,214)	(16,944)	(15,961)	(28)	(150,103)
Policy acquisition costs	(21,940)	(11,628)	(5,184)	(6,252)	(12,479)	(3,897)	(2,270)	412	(63,238)
Policy acquisition costs recovered from reinsurers	(1,434)	(320)	(1,959)	575	4	(54)	307	-	(2,881)
Change in deferred policy acquisition costs - gross	(929)	(578)	(768)	147	354	1,002	(11)	(61)	(844)
Change in deferred policy acquisition costs - reinsurance	(1)	39	30	9	-	26	6	-	109
Policy acquisition costs	(24,304)	(12,487)	(7,881)	(5,521)	(12,121)	(2,923)	(1,968)	351	(66,854)
Operating expenses	(6,963)	(2,826)	(1,900)	(1,042)	(463)	(2,469)	(2,264)	(565)	(18,492)
Underwriting result	**(10,617)**	**(1,735)**	**4,641**	**5,982**	**4,227**	**5,748**	**3,920**	**1,257**	**13,423**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2013

23. SEGMENT INFORMATION (Contd.)

(US$ '000)

	Non-life						Life		
2012	Property	Engineering	Marine	Accident	Whole Account	Others	Short term	Long term	Total (restated)
REVENUES									
Gross premiums written	78,056	36,943	25,780	18,242	53,790	37,836	20,204	5,666	276,517
Outward reinsurance premiums	(7,258)	(1,965)	(1,030)	(484)	(13,347)	(868)	(2,189)	(11)	(27,152)
Change in unearned premiums - gross	4,807	2,259	2,915	(6)	(9,873)	3,230	1,382	(270)	4,444
Change in unearned premiums - reinsurance	(945)	23	(8)	(351)	2,024	147	19	-	909
Net earned premiums	74,660	37,260	27,657	17,401	32,594	40,345	19,416	5,385	254,718
Investment income attributable to insurance funds	2,713	1,345	727	1,893	480	2,180	986	1,639	11,963
	77,373	38,605	28,384	19,294	33,074	42,525	20,402	7,024	266,681
COSTS AND EXPENSES									
Gross claims paid	(79,433)	(20,727)	(18,103)	(12,483)	(13,563)	(35,846)	(17,901)	(10,269)	(208,325)
Claims recovered from reinsurers	25,620	828	526	2,020	3,200	210	226	-	32,630
Change in provision for outstanding claims - gross	930	1,091	1,820	(1,139)	(9,262)	6,620	1,739	2,002	3,801
Change in provision for outstanding claims - reinsurance	(9,431)	(462)	(953)	(262)	4,403	(2,385)	(20)	(1)	(9,111)
Change in provision for unreported losses - gross	11,931	1,065	163	5,264	(10,521)	9,256	2,817	4,021	23,996
Change in provision for unreported losses - reinsurance	(329)	1,367	10	1,126	4,561	(3,184)	112	(7)	3,656
Claims and related expenses	(50,712)	(16,838)	(16,537)	(5,474)	(21,182)	(25,329)	(13,027)	(4,254)	(153,353)
Policy acquisition costs	(19,439)	(12,188)	(9,329)	(5,520)	(11,570)	(6,009)	(3,136)	225	(66,966)
Policy acquisition costs recovered from reinsurers	141	344	388	132	-	65	594	-	1,664
Change in deferred policy acquisition costs - gross	(1,778)	(693)	(878)	(188)	(2,894)	678	100	57	(5,596)
Change in deferred policy acquisition costs - reinsurance	30	(1)	-	87	-	(21)	(5)	-	90
Policy acquisition costs	(21,046)	(12,538)	(9,819)	(5,489)	(14,464)	(5,287)	(2,447)	282	(70,808)
Operating expenses	(7,123)	(2,703)	(2,195)	(1,520)	(617)	(2,131)	(1,532)	(1,042)	(18,863)
Underwriting result	**(1,508)**	**6,526**	**(167)**	**6,811**	**(3,189)**	**9,778**	**3,396**	**2,010**	**23,657**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2013

23. SEGMENT INFORMATION (Contd.)

Analysis of premiums and non-current asset based on geographical location of the risk insured and location of the asset respectively

(US$ ’000)

	2013		2012	
	Premium	Non-current assets	Premium	Non-current assets
from:				
- Middle East	103,181	43,391	123,654	48,020
- Africa	30,668	4,384	38,293	5,877
- Asia	68,174	9,745	59,461	9,074
- Others	59,965	8,572	55,109	8,357
	261,988	**66,092**	**276,517**	**71,328**

Analysis of segment assets and liabilities

(US$ ’000)

	Non-Life						Life			
2013	Property	Engineering	Marine	Accident	Whole	Others	Short Term	Long term	Corporate	Total
Reinsurance assets	81,823	54,075	33,677	23,564	88,093	75,915	18,079	4,699	-	379,925
Cash	40,651	20,109	12,361	5,854	7,851	20,030	10,164	15,078	141,133	273,231
Investments	58,549	28,627	17,793	8,452	12,735	27,720	12,830	25,378	174,623	366,707
Others	-	-	-	-	-	-	-	-	36,779	36,779
	181,023	102,811	63,831	37,870	108,679	123,665	41,073	45,155	352,535	1,056,642
Reinsurance liabilities	183,620	108,882	70,113	37,905	115,842	138,660	34,560	47,063	-	736,645
Others	-	-	-	-	-	-	-	-	28,664	28,664
	183,620	**108,882**	**70,113**	**37,905**	**115,842**	**138,660**	**34,560**	**47,063**	**28,664**	**765,309**
2012										
Reinsurance assets	87,903	60,900	37,265	22,221	28,237	63,487	12,619	7,077	-	319,709
Cash	46,542	25,287	17,581	7,282	4,801	36,579	10,248	22,806	177,228	348,354
Investments	45,921	24,837	17,508	7,092	6,102	33,311	9,907	24,487	146,963	316,128
Others	-	-	-	-	-	-	-	-	61,890	61,890
	180,366	111,024	72,354	36,595	39,140	133,377	32,774	54,370	386,081	1,046,081
Reinsurance liabilities	183,410	113,964	79,193	48,685	69,974	134,677	32,711	54,131	-	716,745
Others	-	-	-	-	-	-	-	-	47,949	47,949
	183,410	**113,964**	**79,193**	**48,685**	**69,974**	**134,677**	**32,711**	**54,131**	**47,949**	**764,694**

FOR THE YEAR ENDED 31 DECEMBER 2013

24. INVESTMENT INCOME

(US$ '000)

2013	Insurance funds	Shareholders' funds	Total
Interest income			
- Investments designated at fair value through profit or loss	564	345	909
- Others	4,843	4,379	9,222
Dividends	649	539	1,188
Realised gains (loss)			
- Trading investments	1,569	1,463	3,032
- Investment designated at fair value through profit or loss	(35)	(21)	(56)
- Available for sale	1,119	1,288	2,407
Gain (loss) on remeasurement of investments at fair value through profit & loss			
- Trading investments	3,456	2,960	6,416
- Investments designated at fair value through profit or loss	(206)	(127)	(333)
Impairment loss-available for sale	(402)	(1,200)	(1,602)
Other	(397)	(363)	(760)
	11,160	**9,263**	**20,423**

2012			
Interest income			
- Investments designated at fair value through profit or loss	546	333	879
- Others	5,745	5,041	10,786
Dividends	622	539	1,161
Realised gains			
- Trading investments	843	428	1,271
- Investment designated at fair value through profit or loss	482	293	775
- Available for sale	2,528	2,357	4,885
Gain on remeasurement of investments at fair value through profit & loss			
- Trading investments	2,172	2,224	4,396
- Investments designated at fair value through profit or loss	20	12	32
Impairment loss – available for sale	(354)	(1,148)	(1,502)
Other	(641)	(448)	(1,089)
	11,963	**9,631**	**21,594**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2013

25. OPERATING EXPENSES

(US$ '000)

	Underwriting	Non-Underwriting	Total	2012
2013				
Salaries and benefits	13,404	7,052	20,456	20,127
General and administration	5,088	3,390	8,478	8,283
	18,492	**10,442**	**28,934**	**28,410**

26. OTHER INCOME

(US$ '000)

	2013	2012
Software sales and related services	1,945	2,176
Third party administration services	2,317	1,338
Other	625	377
	4,887	**3,891**

27. OTHER EXPENSES AND PROVISIONS

(US$ '000)

	2013	2012
Foreign exchange loss	941	4,641
Provision for doubtful receivable & deposits	30	4,177
Other	1,224	1,776
	2,195	**10,594**

28. EARNINGS PER SHARE ATTRIBUTABLE TO SHAREHOLDERS

Basic and diluted earnings per share has been computed as follows:

		2013	2012
Weighted average number of shares outstanding	'000	198,032	198,032
Net profit	US$'000	18,603	17,553
Earnings per share	US$	0.09	0.09

29. EMPLOYEE SHARE SCHEME

The Group operates a cash-settled, share based compensation scheme. Awards under the scheme are subject to the Company achieving specified minimum rates of return to shareholders and are determined based on an evaluation of employee performance against objectives agreed in advance. Virtual shares are allocated at the end of the financial year, being the allotment date, based on the book value of the Company's shares at the beginning of the financial year. These virtual shares will vest in the employees after two years from the allotment date.

The effect of the Scheme on the consolidated financial statements is presented below:

(US$ '000)

	2013	2012
Liability	3,440	2,480
Expense	1,141	1,809

30. POST EMPLOYMENT BENEFITS

The Group operates a number of post-employment plans on defined benefit basis. Eligibility for participation in the defined benefit plans is based on completion of a specified period of continuous service or date of hire. Benefits are based on the employee's years of service.

The principal assumptions used for accounting purposes were:

	2013	2012
Discount rate	2.2%	2.0%
Expected return on assets	2.2%	2.0%
Future salary increases	3.3%	3.3%

The movements in the liability recognised in the statement of financial position are:

(US$ '000)

	2013	2012
Balance at 1 January	12,484	14,696
Accruals for the year	2,528	962
Payments during the year	(954)	(3,174)
Balance at 31 December	**14,058**	**12,484**

FOR THE YEAR ENDED 31 DECEMBER 2013

31. FORWARD FOREIGN EXCHANGE CONTRACTS

In the ordinary course of its business, the Group uses forward foreign exchange contracts to hedge its exposure in respect of foreign currency denominated investments and insurance liabilities. In the event that the item being hedged is sold or settled prior to maturity of the forward foreign exchange contract, it is generally the Group's policy to enter into another offsetting forward foreign exchange contract of the same amount and maturity date. The notional amounts of these financial instruments are not recognised in the Group's consolidated financial statements but their fair values are recognised as assets or liabilities, as appropriate, with changes in fair value being taken to the statement of income. The contracts oblige the Group to exchange cash flows to be received in the future from foreign currency denominated investments for U.S. Dollars at predetermined exchange rates. The counter parties in respect of these transactions are leading financial institutions.

Forward foreign exchange contracts – by currency

(US$ '000)

	2013		2012	
	Notional amount purchases	Notional amount sales	Notional amount purchases	Notional amount sales
Euro	2,413	9,484	2,815	10,606
Pound Sterling	1,065	5,842	5,565	10,599
Japanese yen	-	2,343	-	2,026
Canadian Dollar	959	2,596	1,011	1,728
	4,437	**20,265**	**9,391**	**24,959**

Notional amounts are the contract amounts used to calculate the cash flows to be exchanged. They are a common measure of the volume of outstanding transactions, but do not represent credit or market risk exposures.

Forward foreign exchange contracts - remaining term to maturity

All of the forward foreign exchange contracts outstanding are due in one year or less.

Forward foreign exchange contracts – unrealised gains and losses

The following table summarises the fair value of the Group's hedging portfolio of forward foreign exchange contracts at the statement of financial position date, segregating the items between those that are in an unrealised gain position from those that are in an unrealised loss position.

(US$ '000)

	2013		2012	
	Purchases	Sales	Purchases	Sales
Unrealised gains	154	64	277	91
Unrealised losses	(17)	(353)	(3)	(607)
	137	**(289)**	**274**	**(516)**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2013

32. RECONCILIATION OF NET RESULT TO CASH FLOWS FROM OPERATING ACTIVITIES

(US$ '000)

	2013	2012
Profit for the year	14,873	16,631
Increase (decrease) in insurance funds	6,220	(14,669)
Change in insurance receivable/payable, net	(2,402)	708
Change in accrued insurance premiums	17,078	15,115
Change in other assets/liabilities, net	(18,733)	15,304
Net cash provided by operating activities	**17,036**	**33,089**

33. FAIR VALUE DISCLOSURE

The following table presents the fair values of the Group's financial instruments

(US$ '000)

	Book Value						Fair value
2013	At fair value through profit & loss	Loans and receivables	Held to maturity	Available for sale	Amortised Cost	Total	
ASSETS							
Cash and bank balances	-	273,231	-	-	-	273,231	273,231
Investments	95,877	-	55,510	215,182	-	366,569	367,631
Accrued income	-	421	82,908	1,153	-	84,482	84,482
Insurance receivables	-	114,332	-	-	-	114,332	114,332
Insurance deposits	-	46,538	-	-	-	46,538	46,538
Other assets	-	55,399	-	-	-	55,399	55,399
LIABILITIES							
Insurance payables	-	-	-	-	45,588	45,588	45,588
Other liabilities	-	-	-	-	33,828	33,828	33,828

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33. FAIR VALUE DISCLOSURE (Contd.)

(US$ '000)

	Book Value						Fair value
2012	At fair value through profit & loss	Loans and receivables	Held to maturity	Available for sale	Amortised Cost	Total	
ASSETS							
Cash and bank balances	-	348,354	-	-	-	348,354	348,354
Investments	77,776	-	65,675	172,271	-	315,722	318,432
Accrued income	-	1,118	99,424	1,018	-	101,560	101,560
Insurance receivables	-	97,385	-	-	-	97,385	97,385
Insurance deposits	-	45,592	-	-	-	45,592	45,592
Other assets	-	20,955	-	-	-	20,955	20,955
LIABILITIES							
Insurance payables	-	-	-	-	31,043	31,043	31,043
Borrowings	-	-	-	-	20,000	20,000	20,000
Other liabilities	-	-	-	-	33,235	33,235	33,235

The information disclosed in the table above is not indicative of the net worth of the Group.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal, or in its absence, the most advantageous market to which the Group has access at that date. The fair value of a liability reflects its non-performance risk.

When available, the Group measures the fair value of an instrument using the quoted price in an active market for that instrument. A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

When there is no quoted price in an active market, the Group uses valuation techniques that maximize the use of relevant observable inputs and minimize the use of unobservable inputs. The chosen valuation technique incorporates all the factors that market participants would take into account in pricing a transaction.

The following methods and assumptions were used to estimate the fair value of the financial instruments:

General

The book values of the Group's financial instruments except investments and forward foreign exchange contracts were deemed to approximate fair value due to the immediate or short term maturity of these financial instruments.

Hence, the fair value measurement details are not disclosed.

Investments

The Company measures fair values using the following fair value hierarchy that reflects the significance of the inputs used in making the measurements:

- Level 1: quoted prices (unadjusted) in active markets for identical assets and liabilities

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33. FAIR VALUE DISCLOSURE (Contd.)

- Level 2: Valuation techniques based on observable inputs, either directly (i.e. as prices) or indirectly (i.e. as derived from prices). This category includes instruments valued using: quoted market prices in active markets for similar instruments; quoted prices for identical or similar instruments in markets that are considered less active; or other valuation techniques where all significant inputs are directly or indirectly observable from market data.

- Level 3: Valuation techniques using significant unobservable inputs. This category includes all instruments where the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted market prices for similar instruments where significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

The table below analyses financial instruments, measured at fair value as at the end of the year, by level in the fair value hierarchy into which the fair value measurement is categorized:

(US$ '000)

2013	Level 1	Level 2	Level 3	Total
Held for maturity				
Debt securities	56,572	-	-	56,572
At fair value through profit or loss				
Held for trading				
Common stock of listed companies	53,934	-	-	53,934
Designated at fair value on initial recognition				
Debt Securities	41,943	-	-	41,943
Available for sale				
Debt securities	192,480	-	-	192,480
Common stock of unlisted companies	-	1,514	5,646	7,160
Other	-	1,935	13,607	15,542
	344,929	**3,449**	**19,253**	**367,631**

2012				
Held for maturity				
Debt securities	68,385	-	-	68,385
At fair value through profit or loss				
Held for trading				
Common stock of listed companies	45,476	-	-	45,476
Designated at fair value on initial recognition				
Debt Securities	32,300	-	-	32,300
Available for sale				
Debt securities	146,486	-	-	146,486
Common stock of listed companies	813	-	-	813
Common stock of unlisted companies	-	1,721	5,087	6,808
Other	-	2,628	15,536	18,164
	293,460	**4,349**	**20,623**	**318,432**

FOR THE YEAR ENDED 31 DECEMBER 2013

33. FAIR VALUE DISCLOSURE (Contd.)

The tables below show movements in the Level 3 financial assets measured at fair value:

(US$ '000)

	Unlisted equity	Others	Total
Balance at 1 January 2013	5,087	15,536	20,623
Gain (loss) recognised in:			
- Income statement	(538)	(1,037)	(1,575)
- Other comprehensive income	(8)	(178)	(186)
Investments made during the year	1,231	1,274	2,505
Investments redeemed during the year	(126)	(1,988)	(2,114)
Balance at 31 December 2013	**5,646**	**13,607**	**19,253**
Balance at 1 January 2012	6,073	16,892	22,965
Gain (loss) recognised in:			
- Income statement	(86)	(1,302)	(1,388)
- Other comprehensive income	(122)	445	323
Investments made during the year	1,307	1,000	2,307
Investments redeemed during the year	(2,085)	(1,499)	(3,584)
Balance at 31 December 2012	**5,087**	**15,536**	**20,623**

The carrying values of the investment held in level 3 are based on unobservable inputs and reflects proportional share of the fair values of the respective companies and their underlying net assets. The Group does not expect the fair value of assets under level 2 & level 3 to change significantly on changing one or more of the unassumable inputs. The valuations of these investments are reviewed quarterly and updated as necessary on the basis of information received from investee and investment managers. For the year ended December 31, 2013, there were no transfers in and out of level 1, level 2 and level 3 (2012: none). The fair values are estimates and do not necessarily represent the price at which the investment would sell. As the determination of fair values involve subjective judgments, and given the inherent uncertainty of assumptions regarding capitalization rates, discount rates, leasing and other factors, the amount which will be realized by the company on the disposal of its investments may differ significantly from the values at which they are carried in the consolidated financial statements, and the difference could be material.

The Group does not expect the fair value of assets under level 3 to change significantly on changing one or more of the measurable / observable inputs.

Forward foreign exchange contracts

The fair value of forward foreign exchange contracts, used for hedging purposes, is based on quoted market prices.

Fair value less than carrying amounts

The fair value of fixed interest debt securities fluctuates with changes in market interest rates. The book value of financial assets held to maturity has not been reduced to fair value where lower, because such market rate variations are considered temporary in nature and management intends, and has the financial resources and capacity, to generally hold such investments to maturity.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2013

34. CHANGES IN ACCOUNTING POLICIES

The following tables summarise the cumulative effect, of adopting IFRS 10 and IFRS 11 on the Group's financial statements as described in Note 2.

Consolidated statement of financial position

As at 31 December 2012

(US$ '000)

	Effect of changes in accounting policies		
	As previously reported	Subsidiaries	As restated
ASSETS			
Cash and bank balances	334,345	14,009	348,354
Investments	316,001	127	316,128
Accrued income	79,595	21,965	101,560
Insurance receivables	91,008	6,377	97,385
Insurance deposits	42,225	3,367	45,592
Deferred policy acquisition costs	23,876	4,116	27,992
Reinsurers' share of technical provisions	57,248	2,044	59,292
Other assets	27,959	(5,856)	22,103
Property and equipment	27,675	-	27,675
	999,932	**46,149**	**1,046,081**
LIABILITIES			
Technical provisions	600,990	70,464	671,454
Insurance payables	30,015	1,028	31,043
Borrowings	20,000	-	20,000
Other liabilities	45,513	(3,396)	42,117
	696,518	68,096	764,614
EQUITY			
Attributable to shareholders of Parent Company			
Share capital	220,000	-	220,000
Treasury stock	(14,793)	-	(14,793)
Reserves	41,977	-	41,977
Accumulated deficit	(104)	(11,851)	(11,955)
	247,080	(11,851)	235,229
Non-controlling interests	56,334	(10,096)	46,238
	303,414	(21,947)	281,467
	999,932	**46,149**	**1,046,081**
Earnings per share attributable to shareholders (basic & diluted) US$	0.08	0.01	0.09

FOR THE YEAR ENDED 31 DECEMBER 2013

34. CHANGES IN ACCOUNTING POLICIES (Contd.)

As at 1 January 2012

(US$ '000)

	Effect of changes in accounting policies		
	As previously reported	Subsidiaries	As restated
ASSETS			
Cash and bank balances	343,844	15,453	359,297
Investments	305,728	166	305,894
Accrued income	94,583	26,617	121,200
Insurance receivables	89,404	12,303	101,707
Insurance deposits	48,938	2,540	51,478
Deferred policy acquisition costs	23,523	4,661	28,184
Reinsurers' share of technical provisions	53,889	7,607	61,496
Other assets	34,520	408	34,928
Property and equipment	27,657	-	27,657
	1,022,086	**69,755**	**1,091,841**
LIABILITIES			
Technical provisions	618,660	83,214	701,874
Insurance payables	27,703	(451)	27,252
Borrowings	40,000	-	40,000
Other liabilities	54,411	13,185	67,596
	740,774	95,948	836,722
EQUITY			
Attributable to shareholders of Parent Company			
Share capital	220,000	-	220,000
Treasury stock	(14,793)	-	(14,793)
Reserves	31,360	-	31,360
Accumulated deficit	(14,179)	(14,144)	(28,323)
	222,388	(14,144)	208,244
Non-controlling interests	58,924	(12,049)	46,875
	281,312	(26,193)	255,119
	1,022,086	**69,755**	**1,091,841**
Earnings per share attributable to shareholders (basic & diluted) US$	(0.10)	(0.01)	(0.11)

FOR THE YEAR ENDED 31 DECEMBER 2013

34. CHANGES IN ACCOUNTING POLICIES (Contd.)

Consolidated statement of income

For the year ended 31 December 2012

(US$ '000)

	Effect of changes in accounting policies		
	As previously reported	Subsidiaries	As restated
Gross premiums written	238,642	37,875	276,517
Net earned premiums	218,231	36,487	254,718
Claims and related expenses	(129,714)	(23,639)	(153,353)
Policy acquisition costs	(61,513)	(9,295)	(70,808)
Investment income attributable to insurance funds	11,740	223	11,963
Operating expenses	(18,863)	-	(18,863)
Underwriting result	**19,881**	**3,776**	**23,657**
Investment income attributable to shareholders' funds	9,631	-	9,631
Operating expenses - non underwriting activities	(9,638)	91	(9,547)
Borrowing cost	(407)	-	(407)
Other income	8,128	(4,237)	3,891
Other expenses and provisions	(15,210)	4,616	(10,594)
Profit for the year	**12,385**	**4,246**	**16,631**
Attributable to:			
Non-controlling interests	(2,875)	1,953	(922)
Shareholders of Parent Company	15,260	2,293	17,553
	12,385	**4,246**	**16,631**

35. PRINCIPAL SUBSIDIARIES, JOINT VENTURES & ASSOCIATES

1. Subsidiaries

At 31 December 2013, the principal subsidiaries of the Company were:

	Country of incorporation	Ownership	Non-controlling Interests	Principal Activities
Arig Capital Limited	United Kingdom	100%	Nil	Reinsurance
Arima Insurance Software W.L.L.	Kingdom of Bahrain	100%	Nil	Software
Gulf Warranties W.L.L.	Kingdom of Bahrain	100%	Nil	Warranty
Takaful Re Limited	United Arab Emirates	54%	46%	Retakaful

All holdings are in the ordinary share capital of the subsidiaries concerned and are unchanged from 31 December 2012. The Company also continues to hold 50% of the Joint Venture Hardy Arig Insurance Management W.L.L which is incorporated in the Kingdom of Bahrain. The Group also holds 25% of the equity shares in Globemed Bahrain W.L.L., Bahrain

FOR THE YEAR ENDED 31 DECEMBER 2013

35. PRINCIPAL SUBSIDIARIES, JOINT VENTURES & ASSOCIATES (Contd.)

2. Interest in Subsidiaries: Takaful Re

(US$ '000)

	2013	2012
Non-controlling interest	46%	46%
Other assets	167,227	179,234
Other liabilities	75,685	78,719
Net Assets	91,542	100,515
Revenue	23,637	40,174
Loss for the year	(8,099)	(2,005)
Total comprehensive income	(8,975)	(1,388)
Comprehensive income attributable to non-controlling interests	4,129	639
Net cash (used in) provided by operating activities	(2,584)	8,982
Net cash used in investing activities	(2,248)	(4,911)
Net (decrease) increase in cash and cash equivalents	(4,832)	4,071

The subsidiary's policyholder funds are consolidated as these funds are controlled and managed by the subsidiary which is in a position to direct activities and operations.

3. Interests in joint arrangements and associates

a) The following table summarizes the financial information in all individually immaterial associates that are accounted for using the equity method

(US$ '000)

	2013	2012
Carrying amount of interest in associates	19	279
Total comprehensive income	(260)	(96)

b) The following table summarizes the financial information in all individually immaterial joint ventures that are accounted for using the equity method

(US$ '000)

	2013	2012
Carrying amount of interest in joint ventures	119	127
Total comprehensive income	(8)	(39)

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36. RELATED PARTY TRANSACTIONS

Related parties represent the Company's major shareholders, subsidiary companies, associates, joint ventures, directors and key management personnel.

The following is the summary of transactions with related parties.

1. Subsidiary companies

(US$ '000)

	2013	2012
a) Gross premium retroceded by subsidiary to parent company	34,932	31,433
b) Service fees for administration services provided by parent company	4,889	6,014
c) Balances outstanding		
- Receivables	40,193	12,468
d) Software royalty fees	61	114
e) Sale/purchase of intangible assets between subsidiaries	-	250

2. Joint Venture

(US$ '000)

	2013	2012
a) Service fees for administration services provided	123	74
b) Balances receivable	315	64

3. Compensation to directors and key management personnel

US$ '000

	2013	2012
a) Directors		
- Remuneration (attendance fees)	96	108
- Travel Expenses	116	148
b) Key management compensation		
- Salaries and other short-term employee benefits	2,144	1,525
- Post-employment benefits	719	261
- Share-based compensation	463	404
c) Balances payable (net)		
Key management		
- Maximum balance	6,036	4,496
- Closing balance	6,036	4,496

All transactions with related parties are conducted on an arm's length basis. All outstanding balances from related parties are expected to be settled within 12 months. No provisions have been required in 2013 and 2012 for any outstanding amounts due from related parties.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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37. PARENT COMPANY

The unconsolidated statement of financial position of the parent company, Arab Insurance Group (B.S.C.), is presented below.

(US$ '000)

	2013	2012
ASSETS		
Cash and bank balances	185,199	260,336
Investments	315,657	279,525
Accrued income	71,767	103,205
Insurance receivables	64,908	63,780
Insurance deposits	43,107	42,225
Deferred policy acquisition costs	18,203	18,233
Reinsurers' share of technical provisions	36,801	40,004
Other assets	89,137	35,861
Investment in subsidiaries and associates	51,183	52,174
Property and equipment	8,084	8,566
	884,046	**903,909**
LIABILITIES		
Technical provisions	576,323	584,875
Insurance payables	20,653	24,430
Borrowings	-	20,000
Other liabilities	37,846	39,375
	634,822	668,680
SHAREHOLDERS' EQUITY (note 21)		
Share capital	220,000	220,000
Treasury stock	(14,793)	(14,793)
Reserves	38,702	41,360
Retained earnings (accumulated deficit)	5,315	(11,338)
	249,224	235,229
	884,046	**903,909**