

Chairman and Chief Executive's Statement

Economic overview

The 2010 financial year saw the international and South African economies recovering from the recession of 2008/09.

Assisted by record low interest rates and the injection of massive doses of liquidity into the global financial system, together with fiscal stimulus in several leading countries, economic growth recovered to levels in line with the average of the past two decades, both internationally and domestically.

Resurgence in the growth of emerging markets, led by China, contributed to the economic recovery. In South Africa, a further moderate boost was provided following the successful hosting of the FIFA World Cup.

The lagged benefits of low interest rates saw an improvement in the financial health of individuals and businesses, while the maintenance of low-level interest rates for the foreseeable future will generate a further increase in domestic economic growth in 2011.

With inflationary pressures subdued on the back of the Rand's strength, instigated by substantial capital inflows to emerging markets, including South Africa, a continued boost to consumer spending is likely, although the downward trend in interest rates may have run its course.

It is likely that economic growth would be even stronger if the public authorities had been able to embark upon massive infrastructural investment spending, designed to be the main driver of economic growth and employment creation going forward.

This raises questions about the stated objective, contained in the New Growth Path and announced in November 2010, of generating 500 000 jobs per annum during the coming decade. To achieve this, education and skills need to be rapidly and passionately developed. Furthermore, the stranglehold over the economy by the so-called Golden Triangle of government, big business and powerful trade unions needs to be lessened, allowing small business activity to thrive more effectively.

Public-private partnerships should be encouraged in order to imbue the economic system with greater human resource capacity in the decision-making processes, so maximising efficiencies and successful outcomes from the, theoretically, noble employment creation programmes.

Al Baraka Banking Group

During the 2010 financial year the Bahrain-based Al Baraka Banking Group showed its mettle as a leading Islamic financial institution, expanding its global footprint and world-wide presence, in line with rapidly increasing demand for Shariah-compliant banking products and services.

Al Baraka Banking Group also entered a growth phase, geared towards being better able to serve its numerous clients across the world.

The review period saw a new representative office under formation in Libya, bringing to thirteen the number of business units in the group's stable, while another subsidiary, Al Baraka Bank Pakistan Limited, successfully completed a merger, creating the second largest Islamic bank in Pakistan with a network of 89 branches in 35 cities. In addition, Al Baraka Türk Participation Bank, relocated to a new corporate office, so enhancing its ability to meet demand.

Al Baraka Banking Group awarded a contract for the commencement of the construction of its own new building in Bahrain, designed to better reflect the group's image as a highly-acclaimed banking operation and one of the world's largest Islamic banking groups within the burgeoning international financial sector.

The group, now with a shareholding in uniformly branded banking operations in thirteen countries and employing well in excess of 7 000 members of staff, has assets totalling more than US\$16,0 billion and achieved net income of US\$193,0 million during the 2010 financial year.

The group, originally created to meet the need for Islamic banking services around the world, has rapidly evolved to clearly indicate its standing in the international banking community. In addition, two major awards were conferred on Al Baraka Banking Group during the 2010 financial year. The group was presented with the Hawkamah-UAB Corporate Governance Award in recognition of its leadership role in and high standards applied to corporate governance. The group also won the 'Best Regional Bank' Award at the prestigious 2010 annual Islamic Business & Finance Awards ceremony.

The group, humbled by these business accolades, will use such recognition to continue implementing its strategies so as to serve the development needs of the countries in which it operates, while providing innovative banking products and services in line with the evolving needs of its customers.

Shariah banking

We place great store in the fact that Al Baraka Bank is this country's only fully-fledged Islamic banking institution.

We remain committed to continuously strengthening our structures and controls, and to the ongoing training of staff, so as to further enhance Shariah compliance throughout our business activities for the benefit of our valued customers.

The bank is a member of the Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI), an organisation internationally acclaimed for the standards it lays down and to which we adhere in our day-to-day business operations. We also take direction from the Shariah Supervisory Board, an independent body of specialist jurists in Islamic commercial jurisprudence. In this regard, therefore, we confidently display our Shariah Certificates in all our branches and corporate offices for the information of customers, prospective customers and stakeholders, certain in the knowledge that we remain totally dedicated to absolute and ongoing compliance with Shariah.

During the course of the 2010 financial year, Shariah compliance was confirmed through no fewer than five meetings undertaken by the Shariah Supervisory Board or its sub-committee, confirming our bank having successfully met AAOIFI standards.

South African financial performance

Our 2010 financial results proved disappointing, although it should be conceded that they follow in the wake of the recent crippling world-wide economic crash and on the back of the resultant extremely sluggish economic recovery in South Africa.

Of particular concern was the pedestrian rate of growth in income, even though we are pleased to be able to report that we achieved agreeably consistent growth in deposits and assets during the period under review.

Encouragingly, it is noted that since the opening in 2009 of our new and iconic head office, together with the Kingsmead and Overport branches in Durban – and coupled with the birth of our striking new corporate branding – our bank has registered flattering increases in business. Indeed, our Overport branch has exceeded expectations since opening, its prime location on the Berea being a particular customer draw-card. Meanwhile, customer growth in Lenasia has rendered our branch there woefully inadequate, resulting in a decision during the 2010 financial year to relocate the facility from its present Trade Route Mall location to a more central position. The new Lenasia branch commenced operations on 28 February 2011 at Signet Terrace.

There can be no doubt that demand for Shariah-compliant financial products is steadily increasing and we have accordingly utilised our position of consolidation to extract maximum returns from the bank's achievements to date.

While demand for credit was relatively slow in the first two quarters of the year, the third quarter ushered in a welcome change in tempo. The increase in demand for credit gained momentum in the fourth quarter, thereby enabling the bank to grow its gross advances book by a commendable 21,5% (R341,9 million) for the year. However, the relatively late surge in advances growth did little to compensate for the overall effects of the downward pressure in yields and, as a result, income earned from advances decreased by 3,0% to R180,4 million for the year.

It is pleasing to report that due to the evenly paced 20,7% (R441,0 million) growth in the deposit book, the bank experienced a significant increase in excess liquidity which ultimately led to an equivalent increase in the bank's investment in equity finance for the better part of the year, before declining by R8,4 million to R471,7 million at the end of the year. As a result, the bank's income from equity finance increased by 33,4% to R37,1 million in spite of generally lower yields which prevailed during the year.

We maintained a tight rein on credit control and our diligence paid dividends in this regard with credit provisions at a low R14,7 million (2009: R17,1 million) and an arrears ratio of just 1,3% of our

advances book at year-end.

Net profit for the 2010 financial year, after accounting for operating expenses, amounted to R16,7 million (2009: R18,3 million).

Following the 2008 financial crisis, the Basel III Committee of the Bank of International Settlements moved to develop Basel III to actively address identified flaws and weaknesses which had played a part in the crisis. Such flaws included liquidity management deficiencies, inadequate capital adequacy and quality levels, overly liberal gearing in the banking industry and weak points in the fields of corporate governance, risk management and market transparency. The purpose of Basel III is to enhance bank and sector resilience, so creating improved financial stability.

In essence, Basel III focuses intensely on new capital and liquidity requirements, while also effectively addressing corporate governance problems which came to the fore during the international financial turmoil of 2008. The requirements of Basel III, especially those pertaining to liquidity, are onerous and pose new and daunting challenges within the South African banking environment. In fact, industry experts predict that bank returns on equity will decrease as a consequence of the introduction of Basel III. In order to ensure a seamless transition to Basel III, our bank convened a Basel III committee comprising representatives of various disciplines, including credit, finance, information technology, risk and human resources, under the chairmanship of the financial director.

It is anticipated that the bank will be in a position to meet the Basel III implementation date of 01 January 2012.

During the review period, the bank took a decision to raise additional share capital in the amount of R105,0 million. This will have the effect of growing the capital base of the company from R233,3 million to R338,3 million. The capital injection was completed in March 2011 thereby gearing the bank for increased capital reserve requirements and providing the platform for continued growth. Al Baraka Banking Group increased its holding to 61,8% as a result of the foregoing.

Following hard on the heels of our bank's introduction in 2009 of an instantly successful limited foreign exchange facility, we have since applied for a full licence which would effectively allow us to provide foreign exchange products across the spectrum, while also enabling us to conduct foreign exchange transactions with other subsidiaries within Al Baraka Banking Group.

The advent of a full foreign exchange service would impact positively on our already wide-ranging bouquet of Shariah-compliant banking products.

The bank constantly strives to improve existing offerings and to identify, develop and introduce new and innovative products for the benefit of customers. During the period under review Old Mutual became involved in our Shariah-compliant unit trust, resulting in

Chairman and Chief Executive's Statement

(continued)

the name of the product being changed to the Old Mutual Al Baraka Equity Fund. In addition, a new unit trust, known as the Old Mutual Al Baraka Balanced Fund, was introduced, providing a more stable return for investors in a volatile market.

Building on our 2009 launch of electronic banking, which included the introduction of a debit card and provision of a number of ATMs around the country, we have subsequently established the Al Baraka Business Banking Account which provides owners of sole proprietorships, close corporations and proprietary companies with simple, secure, affordable and convenient banking, with the added ability to make in-store purchases using a card instead of cash.

The dawn of electronic banking, at both a personal and business level, is soon to be augmented by the emergence of our all-new electronic corporate banking product.

We are very encouraged by the tremendous uptake of and demand for electronic banking products and foresee this form of banking going from strength-to-strength as increasingly customers embrace the electronic age in which we live.

Dividends

The bank is pleased to confirm that the board approved a dividend of 45 cents per share for the 2010 financial year against the backdrop of a slowly improving economy.

This is the fifth consecutive year that we have paid a dividend to shareholders.

Corporate Governance

With the King Report on Governance for South Africa (King III) coming into effect in March 2010, we dedicated a great deal of time and effort to diligently working towards various deadlines and ensuring that we were appropriately positioned to correctly apply the principles contained in King III in our day-to-day business.

We paid particular attention to matters of sustainability, especially as regards environmental considerations during the review period and in this regard established a sub-committee specifically charged with the duty of enhancing our existing sustainability reporting, in line with King III principles.

Compliance with the principles contained in King III requires close and constant attention and whilst we fully recognise and acknowledge the need for such attention, it comes at a price. The cost of compliance is having an impact on the bank, given the greatly increased internal resources we must deploy to ensure that we fully comply with regulations.

The year under review also brought with it a number of legislative changes to the Companies Act, changes which we carefully reviewed and are in the process of bringing into effect.

Information technology

The 2010 financial year saw the bank's introduction of its new Equation Banking and Branch Automation System, which followed an intensive two-year implementation process.

We are especially pleased to finally have the new system in place and operational, as this brings our business more closely in line with Al Baraka Banking Group in Bahrain, as well as a number of other subsidiaries within the group. Importantly, the banking system creates the opportunity for consistency and standardisation of operation which will, in turn, enhance our efficiency levels, thereby improving the bank's competitive edge in the market.

The introduction of the Equation Banking and Branch Automation System is one more building block in the provision of additional systems for the future of the bank.

Corporate social investment

We at Al Baraka Bank recognise and acknowledge that there exists in South Africa a myriad of social challenges which must be overcome if this country is to prosper.

A concerted and sustained effort by both the public and private sectors is required if we are to make a positive impact on such barriers to growth and development.

The bank has, since 1994, played an active role in helping to address a range of socio-economic issues. Our extensive Corporate Social Investment Programme sets out to tackle the plight of disadvantaged communities in South Africa in five broad fields, including education, humanitarianism, health, security and poverty alleviation. During the 2010 financial year we made a total of 253 donations, with a combined value of almost R11,2 million, to worthy organisations throughout South Africa. Of this amount, R3,2 million was committed to educational initiatives, inclusive of school extensions and upgrades, library facilities and computer centres, in the belief that the provision of sound education is the true and long-term key to eradicating poverty in this country.

As a responsible corporate organisation, we remain loyal to the ideal behind social investment and continue identifying appropriate and relevant projects which will give effect to community upliftment into the future.

Future prospects

With economic conditions in South Africa and internationally showing signs of slow improvement, Al Baraka Bank has emerged from the trying conditions of the past several years with a sound base for another period of cautious growth.

Having consolidated our position, it is our intention now to extract maximum return against our past achievements. Our focus for the future is to further improve profitability, especially in terms of income generation.

Complementary to this endeavour is our unswerving commitment to continuously investigating, developing and introducing new Shariah-compliant products and services to meet the growing needs and – indeed – expectations of customers and prospective customers.

Central to the bank's future growth is the necessity for the delivery of customer service excellence. It is our goal to revisit and rekindle the relationships we have formed with our customers – private, business and corporate – cementing true and meaningful partnerships for the mutual benefit of the bank and its highly valued customers. Equally, we will vigorously pursue the need to instigate the formation of partnerships with prospective new customers so as to significantly grow our customer base across the country.

Appreciation

It is our sad duty to bid farewell to one of the bank's stalwarts, Mr Thys McLean, our deputy chief executive. The 2010 financial year was his last before retiring in March 2011. Mr McLean devoted some 40 years to working in the banking industry, 10 of which were spent with Al Baraka Bank in Durban.

Mr McLean is vastly experienced and has amassed a wealth of banking knowledge which he constantly drew on to the benefit of the bank. The energy and dedication he displayed was an inspiration to every member of our staff. Although now retired, we are fortunate not to have lost Mr McLean's banking skills and industry insights, as he has accepted a position as a non-executive director on our board. We look forward to the contribution he will make at this level.

We also bid farewell and recognise the contribution of Professor S Cassim, who served as an advisor to the board and resigned in September 2010. We thank her and wish her everything of the best for the future.

During the 2010 financial year, South Africa's Professional Management Review (PMR) undertook a comprehensive assessment of this country's Islamic business community, gauging its development and economic contribution on various levels,



.....
Adnan Ahmed Yousif

Chairman

17 March 2011

Durban

business competencies, brand awareness and the Islamic business community as potential partners for both local and international investors.

Our bank was placed first in the Banking: Business category and second in the Banking: Personal category. This was a tremendous tribute to the efforts of everyone involved with Al Baraka Bank and their commitment to ensuring our institution's standing as a leading Islamic business entity in this country. We greatly appreciate these accolades; accolades which will inspire us to ever greater business heights going forward.

The 2010 financial year was characterised by numerous challenges, the legacy of the previous recession and global financial crisis. Pleasingly, the resilience and expertise displayed by our board in giving strategic direction to the bank, coupled with the dedication and sheer determination of our executive and staff saw us successfully overcome the various business challenges we met as we charted a new course; a course designed to put behind us the negativity associated with the economic down-turn, instead looking to a further period of pragmatic growth.

We accordingly take this opportunity to thank most sincerely Al Baraka Banking Group for its continued belief in and support of Al Baraka Bank in South Africa. We are also particularly grateful to the members of our board whose individual skills and collective expertise have, in no small measure, been responsible for our success in understandably difficult business conditions. Thanks, too, are due to our executive and all our members of staff for their steadfastness in the face of adversity and their loyalty to the bank and its customer commitments.

Lastly, we extend our most sincere thanks to our numerous private, business and corporate customers who support Al Baraka Bank and the Islamic banking ideal. We greatly value such support and reaffirm our commitment to being *your* partner bank.

We thank Almighty Allah, Most Gracious, and pray that He will continue guiding us to success in the future.



.....
Shabir Chohan

Chief Executive