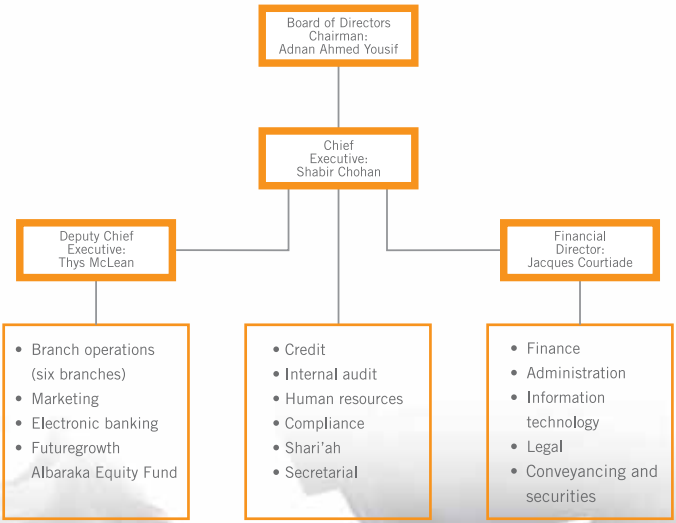
Albaraka Bank - Executive Management



Chairman's Statement

Economic summary

Despite the rising trend of interest rates and the uncertainty on global markets, the South African economy managed to sustain its 5%-plus growth trajectory of the previous three years in 2007. Growth in consumer spending remained quite buoyant at close to 7%, but it was the high growth in fixed investment, of more than 15%, which was geared towards building up the country's infrastructure ahead of the 2010 FIFA World Cup, that really helped to drive economic growth.

Unfortunately, the year 2008 began on a sobering note, with confidence in the South African economy receiving a major blow. Firstly, the cumulative effect of a 4% rise in interest rates between June 2006 and December 2007 clearly began manifesting itself in terms of a marked slowdown in the growth of retail sales and consumer spending generally. In the face of household debt which has kept rising to record levels, the proportionate increase in the debt servicing burden of individuals was even greater than that reflected by the rise in interest rates alone. In addition, the rate of growth in house prices slowed substantially and equity markets remained vulnerable, implying that the positive wealth effect which had also contributed towards a vigorous growth in consumer spending in recent years, began to dissipate. Sharply increased food inflation, coupled with steep increases in fuel costs, also had a marked impact on eroding disposable income. The adverse impact of rising debt servicing burden was naturally felt most severely in the durable goods sector, where credit plays a proportionately larger role than in respect of the purchase of non-durable goods and services.

Over and above these factors, the onset of the electricity crisis played a major role in knocking consumer confidence. As a consequence, the growth of consumer spending, which had fallen off sharply towards the end of 2007, could be expected to continue to remain under pressure through 2008. At the same time, one does not foresee a total collapse of consumer spending. Towards the end of 2008, it is likely that substantial wage increases, based on expectations formed by the sharp increase in inflation which took place towards the end of 2007 and in early 2008, should help to lift disposable income somewhat in relation to an expected slowdown in the rate of price increases. Unless the double-digit depreciation of the Rand since the beginning of 2008 gains still more momentum and, in so doing, boosts inflation a lot further, interest rate increases should be kept to a minimum. As a consequence, growth in consumer spending can be expected to remain positive, albeit at a much lower rate than that experienced last year. Hopefully, in 2009 and 2010, associated with the build-up to the World Cup, one could see some revival in the growth of consumer spending.

There is little doubt that the onset of the electricity crisis will compel investors to postpone some of the large investment projects envisaged as a consequence of the uncertainty of power supply over the next five years. At the same time, there could be some countervailing investment which takes place in search of alternative energy sources. In addition, consumers are likely to reduce their consumption of electricity in the face of rising electricity costs. The electricity problem is therefore by no means insurmountable. However, it does highlight the constraint on the South African economy's ability to sustain growth in excess of 4 to 5%. Infrastructural bottlenecks and a shortage of skills are likely to make the Accelerated and Shared Growth Initiative of South Africa goal of achieving a 6% sustainable growth rate from 2010 onwards, unattainable.

There can also be no doubt that political considerations have regained their importance after many years of being subservient to economic considerations. The election of Jacob Zuma as president of the ANC in December has elicited concerns in certain quarters regarding the possibility of a shift in economic policy increasingly towards helping lesser privileged sections of society. Whilst such policies are unlikely to be introduced so long as the Mbeki regime remains in office until mid-2009, the risk is that economic policy will become increasingly interventionist.

Such a prospect is not conducive towards attracting foreign capital to the country. Furthermore, irrespective of the regime in power, the problem of service delivery by the public sector will not dissipate until such time as the sector absorbs sufficient skilled personnel, whose availability is, in any case, in short supply.

Overriding all these considerations regarding the economic outlook is the threat of a major slowdown in global economic

Economic summary (continued)

activity. South Africa's economic growth has been intimately linked with that of the global economy over many decades and to a far greater extent than is frequently perceived.

The US sub-prime mortgage crisis and the resultant credit crunch within the US financial system carries the threat of taking the global economy, including South Africa, down with it. Weakness in the Rand since the New Year has been a reflection of anxiety and rising risk aversion towards emerging markets amongst international investors. However, that very weakness in the South African currency should act as a shock absorber in insulating the productive side of the economy from the full effects of the global slowdown, by rendering exports significantly more competitive than previously.

Furthermore, in recent years, emerging markets, led by China and India, have managed to substantially outperform the more advanced economies. Intra-regional trade, especially in East Asia, has increased substantially and has provided additional stimuli to growth in such markets.

This has raised the question as to whether or not the fortunes of emerging markets might not have become decoupled from those of advanced economies. In the event of China and other emerging market economies managing to withstand the impact of a slowdown in more advanced economies, South Africa's economic performance might not yet be adversely affected.

In such an environment, commodity prices would sustain their strength, assisting the domestic economy to limit the widening of the current account deficit and succeed in paying for imports of oil and capital equipment necessary to drive economic growth in the longer term. However, there is as yet no certainty that the decoupling theory will indeed hold water.

In conclusion, the South African economy faces its biggest challenges in several years. However, in the same way as the economy had displayed resilience on previous occasions, there is significant hope that it will meet with success in the future in facing up to challenges posed.

Albaraka Banking Group

Albaraka Bank in South Africa is a subsidiary of the international Albaraka Banking Group B.S.C. (ABG), which has its headquarters in the Kingdom of Bahrain and is widely regarded as being the pioneer of Islamic banking world-wide.

Indeed, ABG, the world's leading Islamic banking group, has assets in excess of US$10,0 billion and has achieved a BBB- rating with Standards and Poor's. The group, listed on the Bahrain Stock Exchange and Dubai International Financial Market, has declared profits of US$200,8 million for the 2007 financial year. ABG is represented in 10 countries and has recently established a presence in a further two countries, namely Syria and Indonesia.

The group, having gained a significant foothold in Africa with its 51,7% shareholding in the Durban-based Albaraka Bank, is intent on increasing its African footprint, expanding into select countries to the north of South Africa.

South African performance

The 2007 financial year proved to be a period of impressive growth for Albaraka Bank South Africa. The bank excelled in meeting a range of challenging financial targets, while operating in a highly charged, though niche-based business sector.

Indeed, I am pleased to report that we successfully met all our strategic objectives for the review period and have posted excellent financial results, which auger well in future for the bank's continued growth within the community it serves. Net profit before taxation increased by 75,5% from R15,3 million in 2006 to a most gratifying R26,9 million in 2007.

Corporate governance

Our board remains committed to adhering to the best practice ideal, so living the principles espoused in the King Report for Corporate Governance for South Africa (King II).

As a significant role-player in South Africa's financial sector, we recognise and acknowledge the need for transparency and accountability in any and all our business dealings. Accordingly, we strive for the continuous strengthening of our governance policies and procedures.

In line with this thinking, the 2007 financial year saw our implementation and completion of a comprehensive series of evaluations involving myself, as chairman of the board, our directors and our chief executive. The evaluations, which are in accordance with recommendations contained in the King II Report, are specifically designed to ensure that the individuals concerned constantly improve their overall effectiveness within their respective capacities.

Allied to this is our commitment to appropriate director training, a concept we actively support as a means of keeping all our directors abreast of evolving developments in the South African business arena generally and the country's financial sector specifically. I can report that during the 2007 financial year our directors attended – together with directors of a number of other financial institutions – a training programme, delivered by the Gordon Institute of Business Science in Durban, tailored to meeting the needs of directors of banks.

I would like to congratulate Shabir Randeree on his appointment as vice chairman of our board and take this opportunity to wish him well in fulfilling the commitments of this important role.

Importantly for the bank and in line with the regulatory compliance requirements of the Reserve Bank, we made great strides as regards ensuring our readiness to comply with the Basel II reporting system by January 2008.

Previously completed work on this new system made it possible for us to successfully participate in parallel runs during the period under review and to introduce certain refinements which have effectively led to an improvement in our own internal business processes.

Critically, our efforts have paid dividends insofar as the bank was ready to accommodate Basel II returns and 'go live' by the end of December 2007, thus meeting the Reserve Bank deadline.

Shari'ah banking

We have long prided ourselves on being the only fully-fledged Islamic bank in South Africa and, by definition therefore, can also take great pride in the fact that we offer our clients the assurance and peace-of-mind that Albaraka Bank is a fully Shari'ah-compliant financial institution.

So seriously do we take our Shari'ah compliance responsibility that we continuously invest in vital staff training regarding adherence to Shari'ah standards in our everyday business and, especially, dealings with clients.

In this regard, Albaraka Bank is a member of the internationally respected Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI), which is based in the Kingdom of Bahrain and which lays down the Shari'ah Standards by which we conduct our business in South Africa.

Similarly, we place great store in the knowledge of and expertise displayed by the local Shari'ah Supervisory Board, an independent body of specialist jurists in Islamic commercial jurisprudence entrusted with the responsibility

Chairman's Statement *(Continued)*

of directing, reviewing and supervising the business activities of our bank, so ensuring compliance with Shari'ah. I take this opportunity to congratulate our local Shari'ah Supervisor on having successfully attained an additional international qualification recently, namely that of Certified Islamic Professional Accountant.

I would further like to welcome Mufti Shafique Jakhura onto the Shari'ah Supervisory Board. I feel sure that his specialist knowledge will contribute still further to the valued work of this august body. Albaraka Bank wishes him well in his position on the board.

Corporate social investment

As a concerned and responsible social citizen, the bank recognises the critical importance of meeting socio-economic development needs in South Africa. We acknowledge, too, that business has a meaningful role to play in meeting such needs. Our corporate social investment programme accordingly focuses on four specific fields in which we believe our business can provide a positive impact. These include humanitarianism, education, poverty alleviation and health.This is a responsibility we take most seriously.

During the past financial year we committed some R5,9 million by way of donations and advances to a variety of different charities and charitable organisations throughout South Africa.

Future prospects

Looking to the future, there is every indication – in spite of a slowing economy – that our bank's growth trend of recent years will be sustained going forward, albeit at a much slower rate.

Continued growth in market share, coupled with our growing bouquet of product offerings and significant improvement in the bank's overall performance and attendant return on equity will give effect to the growth we seek within our niche business environment.

Appreciation

The 2007 financial year proved to be an encouragingly successful year in the history of Albaraka Bank, and for this I must thank all those who have played a role in ensuring such success.

I thank my board colleagues for the expertise they bring to the bank and for the commitment they have displayed in giving impetus to our strategic objectives, leading to the phenomenal growth we have realised. In addition, I am most grateful to our executive management team and all our members of staff for their unstinting dedication to our business operations each and every day. Their efforts are reflected in the fine financial results achieved in the 2007 financial year.

May Allah Ta'ala continue to shower us with His mercy and blessings in the time ahead.

Adnan Ahmed Yousif
Chairman
14 March 2008
Durban

Chief Executive's Review

Unprecedented growth in advances and record profits marked our 2007 financial year as a highly significant period in the history of Albaraka Bank in South Africa and effectively placed our bank in a most favourable position going forward.

Financial performance

I am especially pleased to be able to report superb financial performance by the bank during the period under review, due in large part to initiatives implemented in support of our overall corporate strategy.

Profit for the year increased by an impressive 84,5% to R18,2 million, equating to an increase of 19,3% in basic and diluted earnings per share to 121,2 cents. This significant improvement in performance is attributable primarily to the achievement of the objective, set by the board and management in the latter part of 2006, of espousing a more aggressive, but nonetheless responsible approach towards growing the bank's advances book. As a result, the advances book grew by 43,1% to exceed R1,3 billion at the end of the year. Our new approach to growing the advances book was implemented in tandem with enhanced credit control, approval and monitoring processes.

The growth of R401,8 million in advances was funded partly by the increase of 15,1% or R189,8 million in deposits and partly by way of the conscious reduction of R217,5 million in excess liquid funds invested in equity finance to a more appropriate level of R166,3 million. As a consequence, yields and margins increased significantly, resulting in an overall increase of 44,8% in net income earned.

After taking into account the charge for impairment losses of R1,4 million in 2007 as opposed to a release of R2,0 million to the income statement in 2006 and the smaller increase of 18,6% in fee, commission and other operating income, the bank's total income increased by 33,4% to R81,2 million. With the increase in operating expenditure having been contained at the relatively lower level of 19,2%, the increase in profit before taxation surged by 75,5% to R26,9 million. The growth in advances, offset by the reduction in excess liquid fund investments, combined to limit the overall growth in total assets to 14,7%, or R215,9 million, to R1,7 billion.

In addition, much effort was invested in the ground-work necessary for the appropriate extension of our product offering. Pleasingly, a major and long-time product milestone is now set to be realised as a result of our efforts in the 2007 financial year. We have successfully developed a limited foreign exchange product, to be introduced in 2008 opening the door for the bank to buy and sell foreign currency. Our foreign exchange services will be initially limited to the buying and selling of notes and traveller's cheques, so servicing the international travel needs of our clients.

Shari'ah compliance

As a pioneer of Islamic banking in South Africa, Albaraka Bank maintains strict adherence to Shari'ah in day-to-day business dealings and transactions.

During the year under review our bank's continued compliance was ensured through a series of Shari'ah audits, undertaken by the Shari'ah Supervisory Board, indicating that rules and principles – as set by the international Accounting and Auditing Organisation for Islamic Financial Institutions (AAIOFI) - had been complied with. Increased awareness of our commitment to strict compliance with Shari'ah and the interventions in place to monitor adherence to the principles of Shari'ah have undoubtedly led to increased interest in and support for our Islamic banking approach.

The Shari'ah Supervisory Board's hand was further strengthened during the 2007 financial year with the appointment of an additional member, Mufti Shafique Jakhura. Albaraka Bank welcomes his appointment as a means of intensifying the Shari'ah audit process. We therefore look forward to enhanced interaction with our Shari'ah Supervisory Board as we continue striving to entrench continuous adherence to Shari'ah principles throughout every element of our business.

Dividends

For the second consecutive year, Albaraka Bank has declared a dividend.

In the 2006 financial year we declared a dividend of 20c per share. Pleasingly, during the review period we were in a position to declare a dividend of 25c per share to all shareholders recorded in the register as at 12 October 2007.

Rating – Financial Sector Charter

During the 2007 financial year we were delighted to have received an exceptional rating in terms of the Financial Sector Charter.

Our bank was given an 'A' rating, equating to 83,1%, giving credence to our long-held belief in and unswerving commitment to the implementation of Black Economic Empowerment principles throughout the bank.

Head office relocation

Continued business growth and an ever-increasing demand for Shari'ah-compliant banking facilities in South Africa prompted the finalisation in 2007 of plans to relocate the bank's Durban-based head office to bigger operating premises. The move is in line with the bank's strategy to grow its footprint in the country's Islamic financial sector.

Construction of a R63 million, 4 000 square metre iconic building at Durban's Kingsmead Office Park was initiated during the latter part of the review period. Project completion is currently scheduled for late 2008. The new development will result in the accommodation under one roof of the bank's head office, its corporate division – currently located at Musgrave – and a new Kingsmead Branch. The existing Durban Branch will be retained, thus providing Albaraka Bank with a national network of six branches countrywide.

Futuregrowth Albaraka Equity Fund

This partnered Shari'ah-compliant unit trust fund continued as one of the country's most consistent general equity sector performers in 2007.

This investment option, which continued attracting significant investment inflows during the review period, has been regarded as especially attractive to investors because it offers the ability to ensure that non-permissible income is deducted at source – consistent with the Accounting and Auditing Organisation for Islamic Financial Institutions rulings. This is a first for Shari'ah-compliant unit trusts in this country. Accordingly, this has proved popular and continues to be so with major investors who recognise that the Futuregrowth Albaraka Equity Fund is indeed a highly competitive investment vehicle within the market, posting most favourable returns.

The year ahead

I believe that we will continue our period of sustained growth into the year ahead, although at a lower level, taking into account current economic conditions, and that our new product offering will stimulate further interest by clients and prospective clients in Islamic banking.

In looking to the future with confidence, we are conscious of the need to keep abreast of developments within our business environment and, indeed, of competition within the niche market in which we operate. In line with such concerns, we have developed a four-point strategy for the year ahead which is consistent with the Albaraka Banking Group's international strategy going forward and which is designed to develop uniformity amongst all the operations within the world-wide group.

Our new strategic goals are clear. We aim to significantly increase returns in the forthcoming period, to entrench customer

service excellence in every facet of our business, to deliver product innovation to the benefit of our clients and to enhance our use of available technology so as to remain at the cutting edge of financial services provision in South Africa.

In addition and as a financial institution which has the best interests of our clients at heart, we will continually strive to improve our own profitability and return on assets, so ensuring higher returns to our valued depositors.

Given our current growth trend, we aim to give careful consideration to further expand the bank's national footprint into the future. We currently have six branches country-wide and, as indicated, will open an additional branch at our new head office site, Durban's Kingsmead Office Park, at the end of 2008. We do, however, recognise the need to look to the feasibility of opening branches in other parts of the country so as to better reach the communities we exist to serve.

Importantly too, we intend utilising our international link, through the Albaraka Banking Group, to leverage an ever greater range of products, bringing improved choice of product to our South African client-base and to adopt service standards which are truly considered world-class by virtue of their currently being applied in a range of highly discerning communities globally.

Appreciation

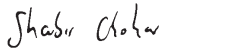
The challenge we faced in the 2007 financial year was to establish a solid foundation on which to develop the bank as a dynamic force within the Islamic financial sector.

The growth and development we have attained in the past year is testimony to the fact that we have made great strides towards the achievement of this ideal.

Our bank's impressive financial performance, growth in advances and enhanced appeal to clients have combined to take the bank to a new and exciting level in the South African financial sector. However, none of this would have been possible without the unstinting support of all those involved with the bank.

I would, therefore, extend my sincere thanks to our chairman, Mr Adnan Ahmed Yousif, members of our board, executive management and members of our staff for their unswerving dedication to our common goal….the growth and development of our bank for the benefit of our clients. Equally, I am grateful to the Albaraka Banking Group for its ongoing support of our business activities and for the guidance it has provided as regards the strategic direction, goals and objectives of the bank, given the niche market within which we operate.

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



Shabir Chohan
Chief Executive
14 March 2008
Durban