

FIRST INTERNATIONAL INVESTMENT BANK LIMITED ANNUAL REPORT 2003

COMPANY INFORMATION

Board of Directors	Managing Director & Chief Executive Chairman
Syed Babar All, Nasim Beg A. Saeed Siddiqui, Nadeem Karamat Kamal A. Chinoy Khalid Yacob Naveed Qazi Imran Butt Naveed Qazi, Audit Committee Kamal A. Chinoy Khalid Yacob	Company Secretary Chairman
Auditors	M/s Ford Rhodes Sidat Hyder & Co., Chartered Accountants
Legal Advisers	M/s Orr, Dignam & Co., Advocates M/s Mohsin Tayebaly & Co., Advocates & Legal Consultants
Bankers	American Express Bank Ltd. ABN-AMRO Bank N.V. Bank AL Habib Limited Citibank, N.A. Metropolitan Bank Limited Muslim Commercial Bank Limited Soneri Bank Limited
Shares Registrar	Noble Computer Services (Private) Limited 14, BangloreTown Housing Society, Main Shahrah-e-Faisal, Karachi. Telephones: (021) 452-0121, 454-6978 Fax: (021)431-4962 E-mail: ncsi@hoh.net
Lahore Registered Office	5 F.C.C., Ground Floor, Syed Maratib Ali Road, Gulberg, Lahore. Telephones: (042) 575-3414 (3 lines), 571-0597 Fax: (042)571-0598 E-mail: fiibl.lhr@interbank.com.pk
Karachi Office	7th Floor, Shaheen Commercial Complex, Dr. Ziauddin Ahmed Road, Karachi. Telephones: (021) 263-9042 (4 lines) Fax: (021)263-0678 E-mail: fiibl.khi@interbank.com.pk
Islamabad Office	Mezzanine Floor, Razia Sharif Plaza, 90, Blue Area, G / 7, Islamabad. Telephones: (051) 227-5256 (3 lines) Fax: (051)227-3861 E-mail: fiibl.isl @ interbank.com.pk
Universal Access	Telephone: 111-234-234 Fax: 111-567-567
Website	www.interbank.com.pk

DIRECTORS' REPORT TO THE SHAREHOLDERS

The Board of Directors of First International Investment Bank Limited (Interbank) is pleased to present the annual report and audited financial statements for the year ended June 30, 2003 to the thirteenth Annual General Meeting of the shareholders.

BUSINESS OPERATIONS

After-tax profit of Interbank for the year under review is Rs. 44.9 million as against Rs. 43.1 million for the previous year. Declining mark-up rates and excess liquidity in the market presented a challenge to Interbank, but we were able to bring about corresponding reduction in our financial charges and also took advantage of trading opportunities in marketable securities, particularly government securities, to generate trading income. Our income from lease finance also recorded substantial increase. Consequently, pre-tax profit increased to Rs. 89.9 million from Rs. 62.5 million. However, this is not fully reflected in after-tax profit because of a one-time adjustment of Rs. 18.7 million on account of income tax and deferred tax pertaining to earlier years.

Earnings per share for the year are Rs. 1.95 per share as against Rs. 1.87 for the previous year.

Total assets and liabilities of Interbank increased to Rs. 3.344 billion from Rs. 2.960 billion last year. Long-term local currency deposits have grown to Rs. 403.0 million from Rs. 223.6 million, in spite of reduction in deposit rates offered by us in line with prevailing market conditions. Mobilisation of long-term, low-cost funds will continue to be an important aspect of our business. Leasing portfolio has grown to Rs. 869.9 million from Rs. 624.0 million, and this has been achieved in an environment which is becoming increasingly competitive. However, term finance has declined to Rs. 367.5 million from Rs. 484.7 million; it has not been feasible to grow this business due to very low mark-up rates being offered by commercial banks. Short-term investments have grown to Rs. 1.292 billion from Rs. 1.051

billion, mainly on account of investment in government securities, while exposure to the stock market has been kept within prudent limits.

During the year, we developed a website for our Inter-car Financing Schemes, making it possible for clients to apply directly to us via the Internet. We are also launching a website for our Intersafe Saving Schemes, which will enable clients to know more about their investment options, calculate periodic profit, and also download the application form.

A summary of key operating and financial data for the last six years appears at the beginning of this annual report.

(Rupees in thousands)				
For the year ended				
June 30, 2002	June 30, 2001	June 30, 2000	June 30, 1999	June 30, 1998
200,000	200,000	180,000	180,000	180,000
204,382	161,263	165,322	157,122	150,215
404,382	361,263	345,322	337,122	330,215
29,414	2,632	—	—	—
484,738	686,246	891,711	1,009,755	1,571,525
623,972	458,957	338,719	250,776	74,740
1,108,710	1,145,203	1,230,430	1,260,531	1,646,265
862,924	515,139	1,216,368	534,970	474,969
246,403	188,628	109,439	26,849	9,284
-	-	3,333	6,666	9,999
26,047	23,718	6,097	39,901	70,287
1,135,374	727,485	1,335,237	608,386	564,539
358,281	405,361	579,565	837,235	554,981
1,131,609	1,585,143	1,796,046	2,385,643	2,715,019
355,433	243,861	325,179	325,440	-
62,500	71,940	32,053	10,907	28,499
43,119	45,940	26,200	6,907	20,999
-	15.00%	10.00%	-	7.50%
15.00%	-	11.11%	-	-

APPROPRIATIONS The Directors recommend the following appropriations:

	Rupees
Profit for the year from ordinary activities after taxation	44,850,785
Unappropriated profit brought forward	58,182
Available for appropriation	44,908,967
Appropriations:	
Transfer to special reserve	8,970,157
Transfer to general reserve	21,000,000
Transfer to reserve for issue of bonus shares	14,500,000
	44,470,157
Unappropriated profit carried forward	438,810

SUMMARY OF KEY OPERATING AND FINANCIAL DATA FOR THE LAST SIX YEARS

	June 30, 2003
Share capital and reserves	
Paid-up capital	230,000
Reserves	219,233
	449,233
Surplus on revaluation of investments - net	47,088
Finance provided	
Term finance	367,469
Lease finance	869,942
	1,237,411
Investments (Including repos and excluding reverse repos)	
Government securities	1,111,973
Term finance certificates (listed)	225,314
Term finance certificates (unlisted)	-
Listed shares, units and modaraba certificates	24,348
	1,361,635
Balances and placements with	

banks/ financial institutions (excluding balances with SBP and reverse repos)	241,494
Certificates of deposit issued	1,114,415
Term finance certificates issued	274,106
Profit before taxation	89,936
Profit after taxation	45,851
Cash dividend	' -
Bonus shares issue	15.00%

STATEMENT OF COMPLIANCE WITH THE BEST PRACTICES OF THE CODE OF CORPORATE GOVERNANCE

This statement is being presented to comply with the Code of Corporate Governance contained in Regulation No. 37 (Chapter XI) and No. 43 (Chapter XIII) of listing regulations of the Karachi and Lahore Stock Exchanges respectively for the purpose of establishing a framework of good governance, whereby a listed company is managed in compliance with the best practices of corporate governance.

The Company has applied the principles contained in the Code in the following manner:

1. The Company encourages representation of independent non-executive directors and directors representing minority interests on its Board of Directors. At present the Board includes six non-executive Directors, including two independent Directors, and there is no director representing minority shareholders.
2. The Directors have confirmed that none of them is serving as a director in more than ten listed companies, including this Company.
3. All the resident Directors of the Company are registered as taxpayers and none of them has defaulted in payment of any loan to a banking company, a Development Finance Institution or a Non-Banking Finance Company or, being a member of a stock exchange, has been declared as a defaulter by that stock exchange.
4. A casual vacancy occurring in the Board on January 25, 2003 was filled up by the Directors on the same day.
5. The Company has prepared a 'Statement of Ethics and Business Practices', which has been signed by all the Directors and employees of the Company.
6. The Board has developed a statement of main purpose and guiding principles (vision/mission statement), overall corporate strategy and significant policies of the Company. A complete record of particulars of significant policies along with the dates on which they were approved or amended has been maintained.
7. All the powers of the Board have been duly exercised and decisions on material transactions, including appointment and determination of remuneration and terms and conditions of employment of the Chief Executive /executive Director, have been taken by the Board.
8. The meetings of the Board were presided over by the Chairman and the Board met at least once in every quarter. Written notices of the Board meetings, along with agenda and working papers, were circulated at least seven days before the meetings. The minutes of the meetings were appropriately recorded and circulated.
9. The Board arranged an orientation course for its Directors during the year to apprise them of their duties and responsibilities. Furthermore, the Chief Executive also attended a course on the Code of Corporate Governance arranged by the Securities and Exchange Commission of Pakistan.
10. The Board has approved appointment of Chief Financial Officer, Company Secretary and Head of Internal Audit, including their remuneration and terms and conditions of employment, as determined by the Chief Executive.

NOTES:

1. The share transfer books of the Company will remain closed from October 14, 2003 to October 21, 2003 (both days inclusive).
2. A member entitled to attend and vote at the Annual General Meeting is entitled to appoint a proxy in writing to attend the meeting and to vote on a member's behalf. A proxy need not be a member of the Company.
3. Duly completed form of proxy must be received at the Registered Office of the Company not later than forty-eight hours before the time appointed for the Meeting.
4. Account holders and sub-account holders holding book entry securities of the Company in the Central Depository Company of Pakistan Limited, who wish to attend the Annual General Meeting, are requested to bring original National Identity Cards with copies thereof duly attested by their bankers for identification purposes.
5. A statement under Section 160(1)(b) of the Companies Ordinance, 1984 pertaining to the special business along with the special resolutions to be passed at the Annual General Meeting is being sent to the members along with this Notice. The existing Memorandum and Articles of Association of the Company and the special resolutions are available at the Registered Office of the Company for perusal and inspection of the members during office hours.
6. The shareholders are requested to notify any change in their addresses.

NOTICE OF THE THIRTEENTH ANNUAL GENERAL MEETING

Notice is hereby given that the Thirteenth Annual General Meeting of First International Investment Bank Limited will be held at Ground Floor, 5 F.C.C., Gulberg, Lahore, on Tuesday, October 21, 2003 at 4.00 p.m. to transact the following businesses:

ORDINARY BUSINESS:

1. To receive and consider the Financial Statements of the Company for the financial year ended June 30, 2003 together with the Directors' and Auditors' Reports thereon.
2. To declare issuance of bonus shares in the proportion of 3 shares for every 20 shares held.
3. To appoint auditors and to fix their remuneration. M/s Ford Rhodes Sidat Hyder & Co., Chartered Accountants, being eligible offer themselves for re-appointment.

4. To elect Directors in accordance with the provisions of section 178 of the Companies Ordinance, 1984 for a term of three years commencing from the date of their appointment.

As decided by the Board of Directors, the number of Directors to be elected would be seven.

The names of the present Directors retiring at the Annual General Meeting are as follows:

1. Syed Babar AN
2. Mr. Nasim Beg
3. Mr. A. Saeed Siddiqui
4. Mr. Nadeem Karamat
5. Mr. Kamal A. Chinoy
6. Mr. Khalid Yacob
7. Mr. Naveed Qazi

Any person who seeks to contest election of the office of Director shall file a notice of his intention along with an affidavit as required under the State Bank of Pakistan's BPRD Circular No. 12, dated June 2, 2000 at the Registered Office in terms of Section 178(3) of the Companies Ordinance 1984, not later than fourteen days before the date of the Meeting.

In terms of the criteria prescribed by the State Bank of Pakistan, association of the following persons as director is undesirable and against the public interest: (a) a person who is/has been associated with any illegal activity, especially relating to banking business; and (b) a person who in his individual capacity or a proprietary concern or any partnership firm or any private limited company or any unlisted public company or any listed public company (of which he has been a proprietor, partner, director or shareholder), has been in default of payment of dues owed to any financial institution and/or in default of payment of any taxes. Furthermore, a person is not permitted to be a director of more than one financial institution. The term "financial institution" will include any bank, investment finance company, venture capital company, housing finance company, leasing company or modaraba company.

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STAFF RETIREMENT BENEFITS

interbank operates a contributory provident fund for all its permanent employees. Equal monthly contributions are made, both by Interbank and the employee, to the fund at 10% of basic salary. Based on the audited financial statements of the provident fund as of June 30, 2002, the investments of the fund amount to Rs. 12,545,809.

Interbank also has a staff gratuity scheme, which was approved by the income tax authorities on July 31, 2002, for its permanent employees who complete the qualifying period of service. Provision in the books of account has been made in accordance with actuarial recommendations.

CODE OF CORPORATE GOVERNANCE

The Board has adopted the Code of Corporate Governance, which was inserted in the listing regulations of the stock exchanges as directed by the Securities and Exchange Commission of Pakistan (SECP). As required by the Code, it is stated that:

- These financial statements, prepared by the management of the company, present fairly its state of affairs, the result of its operations, cash flows, and changes in equity.
- Proper books of account of the company have been maintained.
- Appropriate accounting policies have been consistently applied in preparation of financial statements and accounting estimates are based on reasonable and prudent judgment.
- International Accounting Standards, as applicable in Pakistan, have been followed in preparation of financial statements and there has been no departure from them.
- The system of internal control is sound in design and has been effectively implemented and monitored. Timely corrective action is taken to address any exceptions that are identified.
- There are no doubts upon the company's ability to continue as a going concern.
- There has been no material departure from the best practices of corporate governance, as detailed in the listing regulations of the Karachi and Lahore Stock Exchanges.

REGULATORY MATTERS

Effective December 2, 2002, the regulatory supervision of investment banks was transferred from the State Bank of Pakistan (SBP) to SECP. We thank SBP for their support and guidance in the past, and look forward to working with SECP in the years ahead for bringing about further improvement and innovation in the financial sector of the country.

On April 1, 2003, SECP published new rules for establishment and regulation of Non-Banking Finance Companies (NBFCs), including investment banks. These rules have considerably widened the scope of business of investment banks. We at Interbank look forward to making use of the new opportunities that have now become available to us, and we are in the process of making corresponding changes in our Memorandum and Articles of Association.

The new rules prescribe separate tiers of minimum "equity" (capital) for various types of businesses undertaken by an NBFC. As Interbank provides investment banking and leasing services, minimum equity prescribed for us is Rs. 500 million, and this requirement is to be met by December 31, 2003. Interbank's equity as of June 30, 2003 was Rs. 449.2 million, and we are taking necessary steps to meet the minimum equity requirement.

BONUS SHARES

The Directors recommend issue of bonus shares in the proportion of 3 shares for every 20 shares held. The bonus shares are proposed to be issued out of the share premium account (Rs. 20 million) and the remaining balance (Rs. 14.5 million) from the amount available for appropriation, as shown

above.

CREDIT RATING

Based on financial results for the year ended June 30, 2002, the Pakistan Credit Rating Agency (PACRA) maintained the long-term credit rating of Interbank at 'A1 and the short-term rating at 'A1'.

Credit rating of our secured TFC issue of December 1998 was maintained at 'A+1, while the rating of our unsecured TFC issue of October 2001 was also maintained at 'A'.

DIRECTORS

During the year, Mr. Azhar Ahmed retired, and the Board appointed Mr. Naveed Qazi as Director to fill the casual vacancy thus created. The Board welcomes Mr. Naveed Qazi, and records its appreciation of the valuable services rendered by Mr. Azhar Ahmed during his tenure of office as Director of Interbank.

During the year under review, the Board met six times. The meetings were held on August 20, 2002, October 16, 2002, January 25, 2003, March 20, 2003, April 22, 2003, and June 20, 2003. The attendance of each Director at the Board meetings is given below:

Directors	Number of Board meetings attended
Syed Babar All (Chairman)	6
Nasim Beg	4
A. Saeed Siddiqui (Managing Director and Chief Executive)	6
Nadeem Karamat	6
Kamal A. Chinoy	3
Azhar Ahmed (<i>resigned during the year</i>)	2
Khalid Yacob	5
Naveed Qazi (<i>appointed during the year</i>)	4

REVIEW REPORT TO THE MEMBERS ON STATEMENT OF COMPLIANCE WITH BEST PRACTICES OF CODE OF CORPORATE GOVERNANCE

We have reviewed the Statement of Compliance with the best practices contained in the Code of Corporate Governance prepared by the Board of Directors of First International Investment Bank Limited to comply with Listing Regulations No. 43 (Chapter XIII) and No. 37 (Chapter XI) of the Lahore and Karachi stock exchanges where the company is listed.

The responsibility for compliance with the Code of Corporate Governance is that of the Board of Directors of the company. Our responsibility is to review, to the extent where such compliance can be objectively verified, whether the Statement of Compliance reflects the status of the company's compliance with the provisions of the Code of Corporate Governance and report if it does not. A review is limited primarily to inquiries of the company personnel and review of various documents prepared by the company to comply with the Code.

As part of our audit of financial statements we are required to obtain an understanding of the accounting and internal control systems sufficient to plan the audit and develop an effective audit approach. We have not carried out any special review of the internal control system to enable us to express an opinion as to whether the Board's statement on internal control covers all controls and the effectiveness of such internal controls.

Based on our review nothing has come to our attention which causes us to believe that the Statement of Compliance does not appropriately reflect the company's compliance, in all material respects, with the best practices contained in the Code of Corporate Governance for the year ended June 30, 2003.

FUTURE

As regards the future, we will remain dedicated to our core purpose of promoting saving and investment in Pakistan and our core values of integrity, innovation, fairness, and effectiveness. Our corporate purpose and values translate into a set of guiding principles, which govern all aspects of our business.

The market is expected to be characterized by low mark-up rates and excess liquidity in the medium term. This provides us an opportunity to raise long-term funds at low rates. At the same time, in order to enhance income from financing activities, we have been shifting our focus from large companies to small and medium enterprises (SMEs), particularly medium-size enterprises. Two potential areas of substantial business in future are housing finance services and asset management services. We have already initiated a feasibility study on housing finance, which is nearing completion. In order to diversify our revenue stream, we are training a team of 2-3 persons to market advisory services to corporate clients. We have also undertaken process re-engineering exercises for improving the efficiency of our operations and productivity of our people. Towards this end, we will continue to explore new applications of information technology in our business.

PATTERN OF SHAREHOLDING

The pattern of shareholding, disclosing the aggregate number of shares held by various categories of shareholders, appears at the end of this annual report. There were no trades in the shares of Interbank during the year, carried out by its Directors, Chief Executive, Chief Financial Officer, Company Secretary, and their spouses and minor children.

ACKNOWLEDGEMENT

The Directors thank all members of the staff for their dedication and commitment.

11. The Directors' Report for this year has been prepared in compliance with the requirements of

the Code and fully describes the salient matters required to be disclosed.

12. The financial statements of the Company were duly endorsed by Chief Executive and Chief Financial Officer before approval of the Board.

13. The Directors, Chief Executive and executives do not hold any interest in the shares of the Company other than that disclosed in the pattern of shareholding.

14. The Company has complied with all the corporate and financial reporting requirements of the Code.

15. The Board has formed an Audit Committee. It comprises three members, all of whom are non-executive Directors including the Chairman of the Committee.

16. The meetings of the Audit Committee were held at least once every quarter prior to approval of interim and final results of the Company and as required by the Code. The terms of reference of the Committee have been formed and advised to the Committee for compliance.

17. The Board has hired an internal auditor who is considered suitably qualified and experienced for the purpose and is conversant with the policies and procedures of the Company and is involved in the internal audit function on a full time basis.

18. The statutory auditors of the Company have confirmed that they have been given a satisfactory rating under the quality control review programme of the Institute of Chartered Accountants of Pakistan, that they or any of the partners of the firm, their spouses and minor children do not hold shares of the Company and that the firm and all its partners are in compliance with International Federation of Accountants (IFAC) guidelines on code of ethics as adopted by Institute of Chartered Accountants of Pakistan.

Other income	Note	2003 Rupees	2002 Rupees
EXPENDITURE			
Financial charges	33	21,373,218	-167,375,368
Administration and operating expenses	34		
		11,908,036	—
Operating profit before provisions	32	-8,860,920	-4,770,699
Provision for doubtful finance / potential lease losses - general		1,886,483	941,152
		4,933,599	-3,829,547
Provision / (reversal of provision) under SBP's NBFIs Regulations against finance / lease losses - specific		-62,782,238	115,821,911
		2,694,701	26,713,676
		-5,553	-29,743,573
Profit for the year from ordinary activities before taxation		-60,093,090	112,792,014
Taxation	35	-33,786,273	-58,412,901
		55,613,427	114,337,703
Profit for the year from ordinary activities after taxation			
		-66,096	-311,375
Unappropriated profit brought forward		21,761,058	55,613,427
Available for appropriation			
APPROPRIATIONS		39,865,958	55,613,427
Transfer to special reserve	17.2	-18,104,900	—
Transfer to general reserve	44.1	21,761,058	55,613,427
Transfer to reserve for issue of bonus shares			
Unappropriated profit carried forward			
Earnings per share - Basic			

respect of deferred tax liability on revaluation of investments. Comparative figures have been restated in respect of deferred tax liability on surplus on revaluation of investments, which has been taken to the same account.

This change in accounting policy has reduced Interbank's net assets by Rs. 7,885,920 (2002: Rs. 1 0,498,91 8). There is no impact on the net profit after tax for the current or prior years.

Investments

The management of Interbank determines the appropriate classification of its investments at the time of purchase and classifies these investments as held for trading, available-for-sale or held-to-maturity.

Held for trading

Investments which are acquired principally for the purpose of generating profit from short-term fluctuations in price or dealer's margin are classified as held for trading.

Available-for-sale

Investments intended to be held for an indefinite period of time which may be sold in response to needs for liquidity or changes to interest rates, exchange rates or equity prices are classified as available-for-sale.

Held-to-maturity

Investment securities with fixed maturity where management has both the intent and ability to hold to maturity, are classified as held-to-maturity.

All investments are initially recognised at cost, being the fair value of the consideration given.

Subsequent to initial recognition, investments in quoted securities are marked to market, in accordance with the guidelines contained in the State Bank of Pakistan's BSD Circular No. 20 dated August 4, 2000, using rates quoted on Reuters, stock exchange quotes and brokers' quotations. Any difference between the carrying amount (representing cost adjusted for amortisation of premium or discount, if any) and revalued amount is taken to surplus / (deficit) on revaluation of investments account and shown separately in the balance sheet below shareholders' equity. At the time of disposal the respective surplus or deficit is transferred to income currently.

Registered Special US Dollar Bonds are stated at cost translated at the exchange rates prevailing at the balance sheet date. Any exchange difference on translation is taken to income currently.

Unquoted investments are carried at cost in accordance with the above mentioned circular. Provision for impairment in value, if any, is taken to income currently.

Trade and settlement date accounting

All "regular way" purchases and sales of financial assets are recognised on the settlement date, i.e. the date on which the asset is delivered to or by Interbank. Regular way purchases or sales of financial assets are those, the contract for which requires delivery of assets within the time frame generally established by regulation or convention in the market place.

Financial instruments

All the financial assets and financial liabilities are recognised at the time when Interbank becomes a party to the contractual provisions of the instrument. Any gain or loss on derecognition of the financial assets and financial liabilities is taken to income currently.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED JUNE 30, 2003

1. LEGAL STATUS AND OPERATIONS

First International Investment Bank Limited (Interbank) is a public limited company incorporated in Pakistan on February 7, 1990 under the Companies Ordinance, 1984. Its shares are quoted on the Karachi and Lahore Stock Exchanges. The registered office of Interbank is situated at 5 F.C.C., Gulberg, Lahore.

Interbank is licensed to carry out all investment finance activities and leasing operations as a Non-Banking Finance Company under Section 282C of the Companies Ordinance, 1984 and Non-Banking Finance Companies (Establishment and Regulation) Rules, 2003 [previously it was licensed to carry out all investment finance activities described under SRO 585(1)/87 dated July 13, 1987, issued by the Ministry of Finance and leasing operations under permission granted by the Corporate Law Authority (now Securities and Exchange Commission of Pakistan (SECP)) on December 31, 1996].

Based on financial results for the year ended June 30, 2002, the Pakistan Credit Rating Agency (PACRA) maintained the long-term credit rating of Interbank at 'A' and the short-term rating at 'AT'.

2. STATEMENT OF COMPLIANCE

These financial statements have been prepared in accordance with approved International Accounting Standards (IASs) as applicable in Pakistan and the requirements of the Companies Ordinance, 1984. Approved accounting standards comprise of such International Accounting Standards as notified under the provisions of the Companies Ordinance, 1984. Wherever, the requirements of the Companies Ordinance, 1984 or directives issued by the Securities and Exchange Commission of Pakistan (SECP) differ with the requirements of these standards, the requirements of the Companies Ordinance, 1984 or the requirements of the said directives take precedence.

3. BASIS OF MEASUREMENT

These financial statements have been prepared under the historical cost convention, except for held for trading and available-for-sale investments and derivative financial instruments. The carrying amounts of recognised assets and liabilities that are hedged are adjusted to record changes in fair values attributable to the risks that are being hedged.

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

4.1 Change in accounting policy

During the year, Interbank has adopted International Accounting Standard 12 - Income Taxes (revised 2000) [IAS 12] which has become effective for all periods beginning on or after January 1, 2002 as notified by the Institute of Chartered Accountants of Pakistan vide their circular No.8/99 dated August 8, 1999. Consequently, Interbank now recognises deferred tax assets or liabilities on all temporary differences and unused tax losses as described in note 4.9 to these financial statements. Previously, deferred tax assets or liabilities on items credited or charged directly to surplus on revaluation of investments were not accounted for.

Effect of change in accounting policy

This policy has been applied retrospectively in accordance with International Accounting Standard 8 - "Net Profit and Loss for the Period, Fundamental Errors and Changes in Accounting Policies", benchmark treatment, which requires that any resulting adjustment should be reported as an adjustment in the opening balance of retained earnings and comparative information should be restated as if the accounting policy had always been in use. No adjustments were required to the opening balances of retained earnings in

Deferred

Deferred tax is calculated using the liability method on all temporary differences at the balance sheet date, between the tax base of the assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax assets are recognised for all deductible temporary differences and unused tax losses, if any, to the extent that it is probable that sufficient taxable income will be available against which the deductible temporary differences and unused tax losses can be utilised.

The carrying amount of all deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the deferred tax assets to be utilised.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on the tax rates (and tax laws) that have been enacted at the balance sheet date.

Deferred tax assets / liabilities on unrealised losses / gains on revaluation of investments

are recorded as an adjustment to the same account, where the unrealised losses / gains are recognised.

4.10 Term finance

Term finances are stated at cost less any write-offs and provision for doubtful finance, if any.

4.11 Net investment in lease finance

Leases where Interbank transfers substantially all the risks and rewards incidental to ownership of the assets to the lessee are classified as finance leases. Net investment in lease finance is stated at an amount equal to the aggregate of the minimum lease payments receivable, including any guaranteed residual value and excluding any unearned income, write-offs and provision for potential lease losses, if any.

4.12 Provision for doubtful finance / potential lease losses

The specific provision for doubtful finance / potential lease losses, if any, is made quarterly in accordance with the State Bank of Pakistan's Non-Banking Financial Institutions (SBP's NBFIs) Regulations.

The general provision for finance / lease losses is maintained at a level which is considered reasonably adequate at the time of execution of the finance / lease to provide for potential losses on Interbank's finance / lease portfolio.

Once a financial asset has been classified, income is not recognised in accordance with the SBP's NBFIs Regulations.

4.13 Assets acquired in satisfaction of claims

Interbank occasionally acquires certain vehicles and assets in settlement of non-performing finances / leases provided to its customers. These are stated at lower of the original cost of the related asset, exposure to Interbank and net realisable value. Gains and losses on disposal are taken to income unless recoverable from / payable to the customer.

4.14 Fixed assets

Tangible

These are stated at cost less accumulated depreciation and accumulated impairment losses, if any. Depreciation charge is based on the straight line method whereby the cost of an asset is written-off over its estimated useful life.

Derivatives

Interbank purchases forward exchange cover from the State Bank of Pakistan. These are stated at fair value. The fair value is equivalent to the unrealised gain or loss from remeasuring the derivative using prevailing exchange rates. Remeasurements with positive market values are included in other receivables and remeasurements with negative market values are included in other liabilities in the balance sheet. The resultant gains and losses are taken to the income currently.

Hedging

For the purposes of hedge accounting, hedges existing at Interbank are classified as fair value hedges which hedge the exposure to changes in the fair value of a recognised asset or liability.

Where a fair value hedge meets the conditions for special hedge accounting, the hedged instrument is remeasured to fair value and the resultant gain or loss is immediately recognised in the profit and loss account. Similarly, any gain or loss on the hedged item attributable to the hedged risk is adjusted against the carrying amount of the hedged item and is taken to income currently.

Securities' repurchase / resale agreements

Transactions of repurchase / resale of investment securities are entered into at contracted rates for specified periods of time and are accounted for as follows :

Securities sold under repurchase agreements (repo)

Investments sold with a simultaneous commitment to repurchase at a specified future date continue to be recognised in the balance sheet and are measured in accordance with accounting policies for investments. Amounts received under these agreements are included in borrowings from institutions. The difference between sale and repurchase price is amortised as expense over the life of the repo agreement.

Securities purchased under resale agreements (reverse repo)

Investments purchased with a corresponding commitment to resell at a specified future date are not recognised in the balance sheet. Amounts paid under these obligations are included in fund placements. The difference between purchase and resale price is accrued as income over the life of the reverse repo agreement.

Revenue recognition

Mark-up / return on investments, finances provided, term finance certificates (TFCs), bills receivable, demand promissory notes (DPNs), bankers' acceptances and fund placements are recognised on a time proportion basis.

Interbank follows the finance method in accounting for recognition of lease income. Under this method, the unearned lease income, i.e., the excess of aggregate lease rentals and the residual value over the cost of leased asset is deferred and then amortised to income over the term of the lease, applying the annuity method to produce a constant rate of return on the net investment in the lease finance.

Dividend from equity securities is recognised when the right to receive payment is established.

Commission and fees are taken to income when the service is provided.

Taxation

Current

Provision for current taxation is based on taxable income at the current rate of tax after taking into account applicable tax credits, rebates and exemptions available, if any, or on 0.5% of the turnover whichever is higher.

4.20 Offsetting of financial assets and financial liabilities

A financial asset and a financial liability is offset and the net amount is reported in the balance sheet if Interbank has a legally enforceable right to set-off the recognised amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

4.21 Cash and cash equivalents

Cash and cash equivalents comprise of cash and bank balances, net of running finance.	Total
	4,296,780

5. FIXED ASSETS

Tangible	196,240
Intangible	

5.1 Tangible

Maintenance and normal repairs are charged to income as and when incurred. Major renewals and improvements are capitalised and the parts so replaced, if any, are retired. Gains and losses on disposal of fixed assets are taken to income currently.

Intangible	2003 Rupees	2002 Rupees
These are stated at cost less accumulated amortisation and accumulated impairment losses, if any. Amortisation charge is based on the straight line method whereby the cost of an asset is written-off over its estimated useful life.	13,710,360	14,304,849
Deferred costs		
Expenditure incurred in obtaining long-term borrowings, issuance of term finance certificates and equity shares are being amortised on a straight line basis over the term of the instrument or five years, whichever is less.	224,886,760	305,788,143
	5,050,227	4,493,020
	229,936,987	310,281,163
Redeemable capital - term finance certificates (TFCs)	243,647,347	324,586,012
Term finance certificates issued by Interbank are shown net of own TFCs purchased and held for resale by Interbank, in its role as a market maker for such TFCs. Any premium paid or discount received on TFCs purchased and held for resale is recorded as other receivable or payable and amortised over the remaining life of the TFCs. The differential between the amortised cost and proceeds at the time of resale is amortised over the remaining life of the TFCs.	5,050,227	4,493,020
	238,597,120	320,092,992
	104,054,980	203,248,334
	134,542,140	116,844,658
	—	—
	134,542,140	116,844,658
Staff retirement benefits	134,542,140	116,844,658

Defined contribution plan

Interbank operates a contributory provident fund for all its permanent employees. Equal monthly contributions are made, both by Interbank and the employee, to the fund at 10% of basic salary.

Defined benefit plan

Interbank also has a staff gratuity scheme which was approved by the Income-tax authorities on July 31, 2002 for its permanent employees who complete the qualifying period of service. Provisions are made in accordance with actuarial recommendations. The latest actuarial valuation was carried out as of June 30, 2002.

Transitional liability in respect of defined benefit obligation is being written-off over a period of five years beginning from July 01, 1999, as allowed by International Accounting Standard 19 - "Employee Benefits" (IAS 19).

Actuarial gains and losses are amortised over the average expected remaining lives of the employees participating in the plan, in accordance with IAS 19.

Exchange risk cover fee

The fee for exchange risk cover obtained in respect of foreign currency certificates of deposit is amortised over the term of the respective forward exchange contracts.

Foreign currency transactions

Foreign currency transactions during the year are recorded at the exchange rates approximating those ruling on the date of the transactions. Assets and liabilities in foreign currencies are translated into Pakistan Rupees at the rates approximating those prevailing on the balance sheet date. Gains and losses on translation are taken to income currently.

LONG-TERM CERTIFICATES OF DEPOSIT - unsecured	Note	2003	2002
Local currency		965,322	1,156,372
Foreign currency		3,500	36,346
	21.1	3,532,237	7,891,878
	21.2		
Less: Current portion of long-term certificates of deposit	24	12,654,180	5,842,057
		22,897,730	22,491,090
		6,766,876	6,258,699
21.1 Foreign currencies have been exchanged for Pakistan Rupees with the SBP which provided the foreign exchange risk cover.		3,028,487	162,742
		784,661	790,214
21.2 These represent certificates of deposit of customers having contractual maturities over one year from the balance sheet date. Expected rates of return payable on long-term deposits are 4.25% to 17.75% (2002: 9% to 17.75%) per annum for local currency deposits and 7.75% (2002: 7% to 7.75%) per annum for US Dollar deposits.		2,688,559	737,189
		7,279,171	6,414,532
		277,317	832,782
		27,040	—
DEPOSITS ON LEASE CONTRACTS			
Deposits on lease contracts	22.1	4,147,287	4,428,856
Less: Current portion of deposits on lease contracts	24	65,052,367	57,042,757

In respect of assessment years 1998-1999 to 2000-2001 the appeals filed against the assessment orders with the CIT(A) are pending adjudication. Based on the previous decisions, Interbank is confident that the above matters would be decided in its favour and the possibility of any liability arising there against is considered remote.

(a) **Finances and certificates of deposit**

For all finances, including leases, and certificates of deposit, the fair values have been taken at carrying amounts as these are not considered materially different from their fair values based on the current yields / market rates and repricing profiles of similar finance and deposit portfolios.

(b) **Investments**

The fair values of quoted investments are based on quoted market prices or average of quotations received from the brokers. Unquoted local currency investments are stated at cost which approximates to their fair value in the absence of an active market. Fair value of unquoted foreign currency bonds which carry a floating rate of return is considered to be the same as their carrying amount as the same can only be redeemed at their carrying amount from designated banks.



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