

MCB
ISLAMIC INCOME FUND

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FUND'S INFORMATION

Management Company	Arif Habib Investments Limited 8th Floor, Techno City, Corporate Tower, Hasrat Mohani Road, Karachi	
Board of Directors of the Management Company	Mian Mohammad Mansha Mr. Nasim Beg Mr. Yasir Qadri Syed Salman Ali Shah Mr. Haroun Rashid Mr. Ahmed Jahangir Mr. Samad A. Habib Mr. Mirza Mahmood Ahmad	Chairman(subject to the approval of SECP) Executive Vice Chairman Chief Executive (subject to the approval of SECP) Director (subject to the approval of SECP) Director (subject to the approval of SECP) Director (subject to the approval of SECP) Director Director (subject to the approval of SECP)
Company Secretary & CFO of the Management Company	Mr. Muhammad Saqib Saleem	
Audit Committee	Mr. Nasim Beg Mr. Haroun Rashid Mr. Samad A. Habib Mr. Ali Munir	
Trustee	Central Depository Company of Pakistan Limited CDC House, 990B, Block 'B', S.M.C.H.S, Main Shahrah-e-Faisal, Karachi-74400	
Bankers	MCB Bank Limited Bank Alfalah Limited Standard Chartered Bank (Pakistan) Limited United Bank Limited A.F. Ferguson & Co. - Chartered Accountants State Life Building No. 1-C, I.I. Chundrigar Road, Karachi-74000.	
Auditors	Bawaney & Partners 404, 4th Floor, Beaumont Plaza, Beaumont Road, Civil Lines, Karachi-75530	
Legal Advisor	Arif Habib Investments Limited 8th Floor, Techno City Corporate Tower, Hasrat Mohani Road, Karachi.	
Transfer Agent	AM2 (Positive Outlook) – Management Quality Rating assigned by PACRA	
Rating		

REPORT OF THE DIRECTORS OF THE MANAGEMENT COMPANY FOR THE QUARTER ENDED SEPTEMBER 30, 2011

Dear Investor,

On behalf of the Board of Directors, I am pleased to present MCB Islamic Income Fund's accounts review for the first quarter ended September 30th 2011.

ECONOMY AND MONEY MARKET OVERVIEW

On the macroeconomic front, inflation has remained lower during the period with CPI inflation averaging 11.5% amid change in CPI methodology as well as high base-effect of last year. Like the major part of last year, external current account has also remained comfortable with a marginal deficit of US\$ 189 million during first two months of FY12. Fiscal side, on the other hand, has remained a cause of concern for the economic managers with FY11 deficit touching a level of 6.6% of the GDP (Rs. 1.2 trillion deficit size in absolute term). The government, however, has been able to keep its borrowing from SBP at lower levels, which coupled with lower inflation and contained current account deficit has compelled the central bank to lower its policy discount rate by 50 bps in Jul'11 monetary policy to bring it down to 13.5%.

In the money market, short term market rates remained on the higher side amid tight liquidity scenario in the system. Due to depletion in net foreign assets (NFA) as well as net retirement in government borrowing from SBP, money supply (M2) has witnessed contraction during the period under review, thereby keeping market liquidity tight almost throughout the period. The SBP has constantly been injecting significant amount of money in the system through OMOs in order to calm down the market.

FUND PERFORMANCE

During the quarter under review, the fund generated an annualized return of 11.5% as against its benchmark return of 6.0%, a significant out performance by 5.5%.

Since the launch of fund in June 2011, the fund has gradually increased its exposure towards GoP Ijarah Sukuk, which stood at around 68% at quarter-end, on the back of decent yield as well as capital gains potential. The fund has kept its remaining exposure in cash and bank deposits at decent rates.

FUTURE OUTLOOK

Given declining trend in CPI inflation coupled with a comfortable external account position, the Central bank has decided to lower its policy DR further by 150 bps to 12.0% for Oct'11 - Nov'11 period to trigger growth stimulus in the economy. We continue to flag foreign inflow as the single most important variable especially in the backdrop of sustained oil prices, downward trend in cotton prices and debt repayments including IMF. In our opinion, the absence of foreign flows and government's greater reliance on domestic sources for fiscal funding could result in rebound of inflation and interest rates going forward.

We believe that well-timed accumulation of GoP Ijarah Sukuk should contribute towards healthy fund returns going forward, while the fund would remain cognizant of the changes in the macroeconomic environment in order to deploy assets efficiently in Shariah compliant instruments.

ACKNOWLEDGMENT

The Board is thankful to the Fund's valued investors, the Securities and Exchange Commission of Pakistan and the Trustees of the Fund for their continued cooperation and support. The Directors also appreciate the efforts put in by the management team.

On behalf of Directors,

Yasir Qadri
Chief Executive Officer

Dated: October 26, 2011
Karachi.

CONDENSED INTERIM STATEMENT OF ASSETS AND LIABILITIES AS AT SEPTEMBER 30, 2011

	Note	Un-Audited September 30, 2011 (Rupees in '000)	Un-Audited June 30, 2011 (Rupees in '000)
ASSETS			
Bank balances		93,840	79,505
Investment in government securities	4	200,852	100,250
Profit and other receivables		11,331	2,491
Preliminary expenses and floatation costs		943	993
Total assets		306,966	183,239
LIABILITIES			
Payable to Arif Habib Investments Limited - Management Company		1,673	1,599
Payable to Central Depository Company of Pakistan Limited - Trustee		49	20
Payable to Securities and Exchange Commission of Pakistan		42	4
Accrued expenses and other liabilities		14,195	59
Total liabilities		15,959	1,682
NET ASSETS			
		291,007	181,557
Unit holders' fund (as per statement attached)		291,007	181,557
(Number of units)			
NUMBER OF UNITS IN ISSUE		2,827,765	1,810,991
(Rupees)			
NET ASSET VALUE PER UNIT		102.91	100.25

The annexed notes form an integral part of these financial statements.

**For Arif Habib Investments Limited
(Management Company)**

Chief Executive

Director

CONDENSED INTERIM INCOME STATEMENT (UN-AUDITED) FOR THE QUARTER ENDED SEPTEMBER 30, 2011

	Note	September 30, 2011
		(Rupees in '000)
INCOME		
Profit on bank deposits		1,936
Capital Gain on sale of investment		597
Income from government securities		5,190
Total Income		7,723
EXPENSES		
Remuneration of Arif Habib Investment Limited - Management Company	5	830
Remuneration of Central Depository Company of Pakistan Limited - Trustee		151
Annual fee - Securities and Exchange Commission of Pakistan		42
Auditors' remuneration		57
Amortisation of preliminary expenses and floatation costs		50
Brokerage and transaction cost		10
Other expenses		111
Total expenses		1,250
Net income from operating activities		6,473
Element of income / (loss) and capital gains / (losses) included in prices of units issued less those in units redeemed		1,845
Provision for Workers' Welfare Fund	6	(73)
Net income for the period before taxation		8,245
Taxation		-
Net income for the period after taxation		8,245
Other comprehensive income for the period	7	-
Total comprehensive income for the period		8,245
Earnings per unit	8	

The annexed notes form an integral part of these financial statements.

**For Arif Habib Investments Limited
(Management Company)**

Chief Executive

Director

CONDENSED INTERIM DISTRIBUTION STATEMENT (UN-AUDITED) FOR THE QUARTER ENDED SEPTEMBER 30, 2011

	September 30, 2011
	(Rupees in '000)
Net Income brought forward	458
Final distributions for the period ended June 30, 2011:	
On July 04, 2011 at Rs 0.2532 per unit	
- Bonus distribution	(458)
Profit during the current period	8,245
Undistributed income carried forward	<u>8,245</u>

The annexed notes form an integral part of these financial statements.

**For Arif Habib Investments Limited
(Management Company)**

Chief Executive

Director

**CONDENSED INTERIM STATEMENT OF MOVEMENT IN UNIT HOLDERS' FUND (UN-AUDITED)
FOR THE QUARTER ENDED SEPTEMBER 30, 2011**

	September 30, 2011
	(Rupees in '000)
Net asset at the beginning of the period	181,557
Issue of 1,256,687 units	128,018
Issue of 4,585 bonus units	458
Redemption of 244,498 units	(24,969)
	103,508
Element of (income) / loss and capital (gains) / losses included in prices of units issued less those in units redeemed	(1,845)
Net income for the period	8,245
Final distributions for the period ended June 30, 2011:	
On July 04, 2011 at Rs 0.2532 per unit	
- Bonus distribution	(458)
Net assets as the close of the period	291,007

The annexed notes form an integral part of these financial statements.

**For Arif Habib Investments Limited
(Management Company)**

Chief Executive

Director

CONDENSED INTERIM STATEMENT OF CASH FLOWS (UN-AUDITED) FOR THE QUARTER ENDED SEPTEMBER 30, 2011

	Note	September 30, 2011
		(Rupees in '000)
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income for the period before taxation		8,245
Adjustments for non-cash charges and other items:		
Capital gain on sale of investments		(597)
Amortisation of preliminary expenses and floatation costs		50
Element of (income) / losses and capital (gains) / losses included in prices of units issued less those in units redeemed		(1,845)
		5,853
(Increase) / decrease in assets		
Investments - net		(100,005)
Other receivables		(8,840)
		(108,845)
Increase / (decrease) in liabilities		
Payable to the Management Company		74
Payable to the Trustee		29
Payable to Securities and Exchange Commission of Pakistan		38
Accrued and other liabilities		14,136
		14,277
Net cashflow used in operating activities		(88,714)
CASH FLOWS FROM FINANCING ACTIVITIES		
Net receipts from issue of units		128,018
Net payments on redemption of units		(24,969)
Net cash generated from financing activities		103,050
Net increase in cash and cash equivalents during the period		14,335
Cash and cash equivalents at the beginning of the period		79,505
Cash and cash equivalents at the end of the period		93,840

The annexed notes form an integral part of these financial statements.

**For Arif Habib Investments Limited
(Management Company)**

Chief Executive

Director

NOTES TO AND FORMING PART OF THE CONDENSED INTERIM FINANCIAL STATEMENTS (UN-AUDITED) FOR THE QUARTER ENDED SEPTEMBER 30, 2011

1 LEGAL STATUS AND NATURE OF BUSINESS

MCB Islamic Income Fund (the Fund) was established under the Non-Banking Finance Companies (Establishment and Regulation) Rules, 2003 and was approved as an investment scheme by the Securities and Exchange Commission of Pakistan (SECP) on June 19, 2011. It was constituted under a Trust Deed dated March 7, 2011 between MCB Asset Management Company Limited (MCB-AMC) as the Management Company, a company incorporated under the Companies Ordinance, 1984 and Central Depository Company of Pakistan Limited as the Trustee, also incorporated under the Companies Ordinance, 1984.

Based on shareholders' resolutions of MCB-AMC and Arif Habib Investments Limited (AHI) the two companies have merged as of 27th June 2011 through operation of an order from the SECP issued under Section 282L of the Companies Ordinance 1984 (Order through letter no. SCD/NBFC-II/MCBAMCL & AHIL/271/2011 dated June 10, 2011). AHI being a listed company is the surviving entity and in compliance of SBP's approval, it is a subsidiary of MCB Bank. However subsequent to the completion of the merger, the SECP issued an order postponing the effective date of the merger to 30th July 2011 (through letter no. SCD/PR & DD/AMCW/MCB-AMCL & AHI/348/2011 dated June 27, 2011). Since the merger had already taken place and the subsequent order of the SECP could not be complied with, the Company has sought a ruling by the honourable Sindh High Court (SHC). The honourable SHC has held the SECP's subsequent order in abeyance and instructed SECP to treat the companies as merged pending a final ruling. Irrespective of the final ruling, the Fund's assets and NAV remain unaffected.

The Management Company of the Fund has been licensed to act as Asset Management Company under the NBFC Rules through a certificate of registration issued by the SECP. The registered office of the Management Company is situated at 8th Floor, Techno City Corporate Tower, Hasrat Mohani Road, Karachi.

The Fund has been categorized as an Open-End Shariah Compliant (Islamic) Scheme and offers units for public subscription on a continuous basis. The units of the Fund are transferable and can also be redeemed by surrendering to the Fund. The units are listed on the Lahore Stock Exchange.

The principal activity of the Fund is to seek to provide the investors with a rate of return consistent with a broadly diversified portfolio of long, medium and short term, high quality Shariah Compliant fixed income instruments.

The Pakistan Credit Rating Agency (PACRA) Limited has assigned an asset manager rating of 'AM2' (positive outlook) to the Management Company. Management Company will have initiated the process of obtaining the rating of the Fund which is expected to be completed in the year 2012.

2 Statement of compliance

2.1 These condensed interim financial statements have been prepared in accordance with approved accounting standards as applicable in Pakistan. Approved accounting standards comprise of such International Financial Reporting Standards (IFRSs) issued by the International Accounting Standards Board as are notified under the Companies Ordinance, 1984, the requirements of the Trust Deed, the Non-Banking Finance Companies (Establishment and Regulation) Rules, 2003 (the NBFC Rules), the Non-Banking Finance Companies and Notified Entities Regulations, 2008 (the NBFC Regulations) and the directives issued by the Securities and Exchange Commission of Pakistan (SECP). Wherever the requirements of the Trust Deed, the NBFC Rules, the NBFC Regulations or directives issued by SECP differ with the requirements of IFRS, the requirements of the Trust Deed, the NBFC Rules, the NBFC Regulations or the directives issued by SECP prevail. The disclosures made in these condensed interim financial statements have, however, been limited based on the requirements of the International Accounting Standard 34: 'Interim Financial Reporting'.

2.2 These condensed interim financial statements are unaudited.

2.3 The comparative information of the Income Statement, Distribution Statement, Movement in Unit Holders' Fund and Cash Flow Statement have not been presented as the Fund started operations with effect from May 01, 2011.

2.4 The directors of the asset management company declare that these financial statements give a true and fair view of the Fund.

3 SIGNIFICANT ACCOUNTING POLICIES

The accounting policies adopted for the preparation of these condensed interim financial statements are the same as those applied in the preparation of the annual published financial statements of the Fund for the period ended June 30, 2011.

Note
September 30,
2011
June 30
2011
(Rupees in '000)

4 INVESTMENTS

Financial assets at fair value through profit or loss - held for trading
- Investment in government securities

4.1 200,852 100,250

4.1 Financial assets at fair value through profit or loss - held for trading - Investment in government securities

Government securities	Face Value				Balance as at September 30, 2011			Market value as a percentage of net assets	Market value as a percentage of total investment
	As at July 1, 2011	Purchased during the period	Disposed / Matured during the period	As at Sept 30, 2011	Carrying Value	Market value	Appreciation / (diminution)		
-----Rupees in '000-----								%	
Government Ijara Sukuk - 8	100,000	68,000	100,000	68,000	68,421	68,421	-	23.51	34.07
Government Ijara Sukuk - 5	-	124,000	7,500	116,500	117,403	117,403	-	40.34	58.45
Government Ijara Sukuk - 7	-	15,000	-	15,000	15,028	15,028	-	5.16	7.48
Totals - September 30, 2011					<u>200,852</u>	<u>200,852</u>	-	<u>69.01</u>	<u>100.00</u>
Totals: June 30, 2011					<u>100,250</u>	<u>100,250</u>	-	<u>55.22</u>	<u>100.00</u>

5 REMUNERATION OF MANAGEMENT COMPANY

During the period, through Sindh Sales tax on Services Act 2011, General Sales Tax on Fund Management services has been imposed @ 16%, effective from July 01, 2010. Management Fee Charged during the period includes General Sales Tax.

6 PROVISION FOR WORKERS' WELFARE FUND

The Finance Act 2008 introduced an amendment to the Workers' Welfare Fund Ordinance, 1971 (WWF Ordinance). As a result of this amendment it may be construed that all Collective Investment Schemes / mutual funds (CISs) whose income exceeds Rs 0.5 million in a tax year, have been brought within the scope of the WWF Ordinance, thus rendering them liable to pay contribution to WWF at the rate of two percent of their accounting or taxable income, whichever is higher. In this regard, a constitutional petition has been filed by certain CISs through their trustees in the Honourable High Court of Sindh (the Court), challenging the applicability of WWF to the CISs, which is pending adjudication. However, without prejudice to the above, the Management Company made a provision for WWF contribution in the annual financial statements for the year ended June 30, 2011.

Subsequent to the year ended June 30, 2010, a clarification was issued by the Ministry of Labour and Manpower (the Ministry) which stated that mutual funds are not liable to contribute to WWF on the basis of their income. However on December 14, 2010 the Ministry filed its response against the Constitutional petition requesting the court to dismiss the petition. According to the legal counsel who is handling the case, there is a contradiction between the aforementioned clarification issued by the Ministry and the response filed by the Ministry in Court.

Subsequent to 30 June 2011, the Honourable Lahore High Court (LHC) in a Constitutional Petition relating to the amendments brought in the WWF Ordinance, 1971 through the Finance Act, 2006, and the Finance Act, 2008, has declared the said amendments as unlawful and unconstitutional and struck them down. The Management Company is hopeful that the decision of the LHC, will lend further support to the Constitutional Petition which is pending in the Sindh High Court (SHC), on the basis of this recent positive development, the management has decided not to accure further provision against WWF. However, pending the decision of the said constitutional petition, the Management Company, as a matter of abundant caution, has not reversed the provision of Rs. 0.082 million for WWF. The aggregate unrecognised amount of WWF as at September 30, 2011 amounted to Rs. 0.094 million.

7 TAXATION

The income of the Fund is exempt from income tax under clause 99 of Part I of the Second Schedule to the Income Tax Ordinance, 2001 subject to the condition that not less than 90 percent of its accounting income for the year, as reduced by capital gains, whether realised or unrealised, is distributed amongst the unit holders. The Fund has not recorded a tax liability in respect of income relating to the current period as the management company intends to distribute more than 90 percent of the Fund's accounting income for the period as reduced by capital gains (whether realised or unrealised) to its unit holders.

8 EARNINGS / (LOSS) PER UNIT

Earnings / (Loss) per unit has not been disclosed as in the opinion of the management determination of cumulative weighted average number of outstanding units for calculating earnings / (loss) per unit is not practicable.

9 TRANSACTIONS WITH CONNECTED PERSONS / OTHER RELATED PARTIES

- 9.1** Connected persons of the Fund include the Management Company, other collective investment, schemes being managed by the Management Company, MCB Bank Limited being the parent company of the Management Company, the Trustee, directors and key management personnel, other associated undertaking and investors holding 10% or more units of the Fund.
- 9.2** The transactions with connected persons are in the normal course of business, at contracted rates and terms determined in accordance with market rates.
- 9.3** Remuneration payable to the Management Company and the fee payable to the Trustee are determined in accordance with the the provisions of the NBFC Rules 2003, the NBFC Regulations 2008 and Trust Deed respectively.
- 9.4** Details of transactions and balances at year end with related parties / connected persons, other than those which have been disclosed elsewhere in these financial statements, are as follows:

	September 30, 2011	
9.5 Transactions with connected persons during the period		
MCB Bank Limited		
Profit received on deposit accounts		556
Arif Habib Investments Limited		
Remuneration of the Management Company		830
Issue of bonus units: 2,532		253
Hamdard Laboratories (Waqf) Pakistan		
Issue of units: 193,265		20,000
Issue of bonus units: 253		25
Redemption of units: 1,540		158
Central Depository Company of Pakistan Limited-Trustee		
Fee charged during the period		151
Key Management Personnel		
Issue of units: 18,822		1,892
Issue of bonus units: 17		2
Redemption of units: 1,518		154
	September 30 2011	June 30 2011
9.6 Amount outstanding as at period end	(Rupees in '000)	
MCB Bank Limited		
Bank balance	2,003	22,843
Profit receivable on deposit accounts	41	508
Arif Habib Investments Limited		
Remuneration payable to the Management Company	270	51
Units held: 1,002,532 (June 30, 2011: 1,000,000)	103,171	100,253
Preliminary expenses and Formation Cost payable	1,000	1,000
Sale Load Payable	924	145
Others	403	403
Central Depository Company of Pakistan Limited-Trustee		
Fee payable	49	20
Hamdard Laboratories (Waqf) Pakistan		
Units held: 294,921 (June 30, 2011: 100,000)	30,350	10,025
Key Management Personnel		
Units held : 18,756 (June 30, 2011: 6,794)	1,930	681

10 DATE OF AUTHORISATION FOR ISSUE

These financial statements were authorised for issue on October 26, 2011 by the Board of Directors of the Management Company.

11 GENERAL

Figures have been rounded off to the nearest thousand rupees unless otherwise specified.

**For Arif Habib Investments Limited
(Management Company)**

Chief Executive

Director