

**BOUBYAN BANK K.S.C. AND SUBSIDIARY
STATE OF KUWAIT**



**CONSOLIDATED FINANCIAL STATEMENTS
AND INDEPENDENT AUDITORS' REPORT
FOR THE YEAR ENDED 31 DECEMBER 2006**

CONSOLIDATED FINANCIAL STATEMENTS AND INDEPENDENT AUDITORS' REPORT

For the year ended 31 December 2006

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Al-Fahad & Co.
Salhia Complex
Gate 2, 4th Floor
P.O. Box 23049
Safat 13091
State of Kuwait

Tel: + (965) 2438060
Tel: + (965) 2468934
Fax: + (965) 2452080
www.deloitte.com



KPMG Safi Al-Mutawa & Partners
Rakan Tower, 18th floor
Fahad Al-Salem Street,
P.O. Box 24, Safat 13001, Kuwait
Tel : + 965 247 5090
Fax: + 965 249 2704

INDEPENDENT AUDITORS' REPORT

To the Shareholders of
Boubyan Bank K.S.C.
State of Kuwait

Report on the consolidated financial statements

We have audited the accompanying consolidated financial statements of Boubyan Bank K.S.C. ("the Bank") and subsidiary (collectively "the Group") which comprise the consolidated balance sheet as at 31 December 2006, and the consolidated income statement, consolidated statement of changes in equity and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes. The financial statements of the Bank as at and for the period from the date of incorporation on 21 September 2004 to 31 December 2005 were audited by a joint auditor other than KPMG Safi Al-Mutawa and Partners. Their report dated 21 January 2006 expressed an unqualified opinion.

Management's responsibility for the consolidated financial statements

Management of the Bank is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditors' responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as of 31 December 2006, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted for use by the State of Kuwait.

Report on other legal and regulatory requirements

Furthermore, in our opinion proper books of accounts have been kept by the Bank and the consolidated financial statements together with the contents of the report of the Bank's Board of Directors relating to these consolidated financial statements, are in accordance therewith. We further report that we obtained the information and explanations that we required for the purpose of our audit and the consolidated financial statements incorporate all the information that is required by the Kuwait Commercial Companies Law of 1960, as amended, and by the Bank's Articles of Association; that an inventory count was duly carried out; and that, to the best of our knowledge and belief, no violations of the Kuwait Commercial Companies Law of 1960, as amended, or of the Articles of Association of the bank have occurred during the year ended 31 December 2006 that might have had a material effect on the business of the Group or on its financial position.

We further report that, during the course of our audit, we have not become aware of any material violations of the provisions of Law No. 32 of 1968, as amended, concerning currency, the Central Bank of Kuwait and the organization of banking business, and its related regulations during the year ended 31 December 2006.



Jassim Ahmad Al-Fahad
License No. 53-A
Al-Fahad & Co. Deloitte & Touche



Safi A. Al-Mutawa
License No. 138-A
of KPMG Safi Al-Mutawa & Partners
Member firm of KPMG International

7 January 2007
Kuwait

**BOUBYAN BANK K.S.C. AND SUBSIDIARY
STATE OF KUWAIT**

CONSOLIDATED INCOME STATEMENT

For the year ended 31 December 2006



		31 December 2006	From date of incorporation 21 September 2004 to 31 December 2005
	Notes	KD'000	KD'000
Income			
Murabaha and other Islamic financing income, net		18,581	7,622
Investment income	5	3,361	2,734
Fees and commissions income		6,465	1,588
Share of results of associates	13	927	947
Other income		470	-
		<u>29,804</u>	<u>12,891</u>
Expenses			
Staff costs		(5,797)	(2,730)
General and administrative expenses		(2,873)	(1,368)
Depreciation		(327)	(80)
Provision for impairment - general	6	(2,080)	(1,706)
		<u>(11,077)</u>	<u>(5,884)</u>
Profit before distribution to depositors		18,727	7,007
Distribution to depositors	4	(7,936)	-
Profit for the year / period before provision for Kuwait Foundation for the Advancement of Sciences ("KFAS"), National Labour Support Tax ("NLST") and Directors' fees		10,791	7,007
Provision for contribution to KFAS		(96)	(63)
Provision for NLST		(265)	-
Directors' fees		(116)	(90)
Profit for the year / period		<u>10,314</u>	<u>6,854</u>
Attributable to:			
Equity holders of the Bank		10,259	6,854
Minority interest		55	-
Profit for the year / period		<u>10,314</u>	<u>6,854</u>
Earnings per share (fils)	7	<u>10.27</u>	<u>6.86</u>

The notes set out on pages 8 to 32 form an integral part of these consolidated financial statements.

**BOUBYAN BANK K.S.C. AND SUBSIDIARY
STATE OF KUWAIT**


CONSOLIDATED BALANCE SHEET



As at 31 December 2006

	Notes	2006 KD'000	2005 KD'000
Assets			
Cash and cash equivalents	8	22,947	27,974
Short term Murabaha	9	277,344	168,212
Receivables	10	115,539	58,192
Investments carried at fair value through profit or loss		1,020	-
Available for sale investments	11	30,710	26,237
Investment in unconsolidated subsidiary	12	1,133	-
Investments in associates	13	9,080	8,263
Trading properties		2,885	3,206
Investment properties		13,508	-
Leased assets	14	7,940	1,794
Other assets	15	18,624	32,356
Property and equipment		3,609	2,236
Total assets		504,339	328,470
Liabilities and equity			
Liabilities			
Due to banks and financial institutions	16	207,165	108,139
Depositors' accounts	17	168,592	91,233
Other liabilities	18	8,172	22,181
Total liabilities		383,929	221,553
Capital and reserves			
Share capital	19	99,941	99,941
Share premium	20	280	280
Statutory reserve	21	1,727	701
Voluntary reserve	22	1,550	701
Fair value reserve		909	-
Foreign currency translation reserve		109	(158)
Retained earnings		13,659	5,452
Equity attributable to equity holders of the parent		118,175	106,917
Minority interest		2,235	-
Total equity		120,410	106,917
Total liabilities and equity		504,339	328,470

The notes set out on pages 8 to 32 form an integral part of these consolidated financial statements.



 Jacob Y. Al-Muzaini
 Chairman and Managing Director

**BOUBAYAN BANK K.S.C. AND SUBSIDIARY
STATE OF KUWAIT**

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2006



	Share capital	Share premium	Statutory reserve	Voluntary reserve	Fair value reserve	Foreign currency translation reserve	Retained earnings	Attributable to equity holders of the parent	Minority interest	Total
	KD'000	KD'000	KD'000	KD'000	KD'000	KD'000	KD'000	KD'000	KD'000	KD'000
Issue of share capital (Note 19)	100,000	280	-	-	-	-	-	100,280	-	100,280
Fraction shares not issued (Note 19)	(59)	-	-	-	-	-	-	(59)	-	(59)
Total share capital	99,941	280	-	-	-	-	-	100,221	-	100,221
Profit for the period	-	-	-	-	-	-	6,854	6,854	-	6,854
Total recognized income and expense for the period	-	-	-	-	-	-	6,854	6,854	-	6,854
Foreign currency translation adjustments	-	-	-	-	-	(158)	-	(158)	-	(158)
Transfer to reserves	-	-	701	701	-	-	(1,402)	-	-	-
Balance at 31 December 2005	99,941	280	701	701	-	(158)	5,452	106,917	-	106,917
Unrealized gain on available for sale investments	-	-	-	-	909	-	-	909	-	909
Foreign currency translation adjustments	-	-	-	-	-	267	-	267	-	267
Net gain recognized directly in equity	-	-	-	-	909	267	-	1,176	-	1,176
Profit for the year	-	-	-	-	909	267	10,259	10,259	55	10,314
Total recognized income and expense for the year	-	-	-	-	909	267	10,259	11,435	55	11,490
Transfer to Zakat	-	-	1,026	(177)	-	-	-	(177)	-	(177)
Transfer to reserves	-	-	-	1,026	-	-	(2,052)	-	-	-
Net movement in Minority Interest	-	-	-	-	-	-	-	-	2,180	2,180
Balance at 31 December 2006	99,941	280	1,727	1,530	909	109	13,659	118,175	2,235	120,410

The notes set out on pages 8 to 32 form an integral part of these consolidated financial statements.

**BOUBYAN BANK K.S.C. AND SUBSIDIARY
STATE OF KUWAIT**

CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31 December 2006



		From date of incorporation 21 September 2004 to 31 December 2005
	31 December 2006	31 December 2005
Note	KD'000	KD'000
OPERATING ACTIVITIES		
Profit for the year / period before provision for contribution to KFAS, NLST and Directors' fees	10,791	7,007
Adjustments for:		
Provision for impairment - general	6 2,080	1,706
Depreciation	327	80
Gain from sale of available for sale investments	(236)	-
Share of results of associates	(927)	(947)
Dividend income	(152)	(108)
	<u>11,883</u>	<u>7,738</u>
Changes in operating assets and liabilities:		
Increase in short term Murabaha	(109,492)	(168,773)
Increase in receivables	(58,291)	(59,337)
Decrease / (increase) in trading properties	321	(3,206)
Increase in leased assets	(6,146)	(1,794)
Decrease / (increase) in other assets	13,732	(32,356)
Increase in due to banks and financial institutions	99,026	108,139
Increase in depositors' accounts	77,359	91,233
(Decrease) / increase in other liabilities	(15,439)	22,028
Dividend income received	152	108
Net cash from / (used in) operating activities	<u>13,105</u>	<u>(36,220)</u>
INVESTING ACTIVITIES		
Purchase of available for sale investments	(15,594)	(26,237)
Purchase of investments carried at fair value through profit or loss	(1,020)	-
Proceeds from sale of available for sale investments	12,096	-
Purchase of investments in associates	-	(7,474)
Dividends from associates	504	-
Purchase of investment properties	(13,508)	-
Purchase of property and equipment	(1,700)	(2,316)
Purchase of investment in unconsolidated subsidiary	(1,090)	-
Net cash used in investing activities	<u>(20,312)</u>	<u>(36,027)</u>

(Continued)

**BOUBYAN BANK K.S.C. AND SUBSIDIARY
STATE OF KUWAIT**

CONSOLIDATED CASH FLOW STATEMENT (CONTINUED)

For the year ended 31 December 2006



	31 December 2006	From date of incorporation 21 September 2004 to 31 December 2005
FINANCING ACTIVITIES		
Issue of share capital	-	100,221
Net cash from financing activities	-	100,221
Net change in minority interest	2,180	-
Net (decrease) / increase in cash and cash equivalents	(5,027)	27,974
Cash and cash equivalents at the beginning of the year / period	27,974	-
Cash and cash equivalents at the end of the year / period	8 22,947	27,974

The notes set out on pages 8 to 32 form an integral part of these consolidated financial statements.

1. INCORPORATION AND ACTIVITIES

Boubyan Bank K.S.C. ("the Bank") is a public shareholding company incorporated on 21 September 2004, in accordance with the Commercial Companies Law in the State of Kuwait, by Amiri Decree No. 88 and in accordance with the rules and regulations of the Central Bank of Kuwait ("CBK") (Law No. 30 passed in 2003). The Bank's shares were listed in Kuwait Stock Exchange on 15 May 2006.

The Bank was licensed by the Central Bank of Kuwait on 28 November 2004. The Bank is principally engaged in providing banking services, in accordance with Codes of the Islamic Sharia'a, as approved by the Bank's Sharia'a Supervisory Board.

The address of the Bank's registered office is P.O. Box 25507, Safat 13116, State of Kuwait.

The consolidated financial statements were authorised for issue by the Board of Directors on 7 January 2007.

2. SIGNIFICANT ACCOUNTING POLICIES

Basis of preparation

The financial statements have been prepared in accordance with the International Financial Reporting Standards ("IFRS") promulgated by the International Accounting Standards Board ("IASB"), and Interpretations issued by the International Financial Reporting Interpretations Committee of the IASB, as modified for use by the Government of Kuwait for financial services institutions regulated by the Central Bank of Kuwait. These regulations require adoption of all IFRS except for the IAS 39 requirement for collective impairment provision, which has been replaced by the CBK requirement for a minimum general provision as described below.

The impairment provision for finance facilities complies in all material respects with the specific provision requirements of the CBK and IFRS. In addition, in accordance with the CBK instructions, a minimum general provision of 2% on all finance facilities net of certain categories of collateral, to which CBK instructions are applicable and not subject to specific provision, is made.

The comparative amounts in the consolidated statements of income, equity, cash flows and related notes are from date of incorporation on 21 September 2004 to 31 December 2005. Actual operations of the Bank started after getting the approval of the CBK on 28 November 2004 and insignificant transactions occurred during December 2004.

IFRS 7 *Financial Instruments: Disclosures* and the Amendments to IAS 1 *Presentation to Financial Statements: Capital Disclosures* require extensive disclosures about the significance of financial instruments for entity's financial position and performance, and qualitative and quantitative disclosures on the nature and extent of risks. IFRS 7 and amended IAS 1, which become mandatory for the Group's 2007 consolidated financial statements, will require extensive additional disclosures with respect to Group's financial instruments and share capital.

Accounting convention

The consolidated financial statements are presented in Kuwaiti Dinars and are prepared under the historical cost convention, except for certain available for sale investments, investments carried at fair value through profit or loss and investment properties that are stated at fair value.

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Bank and its subsidiary Boubyan Takaful Insurance Company K.S.C. (Closed) which is controlled by the Bank (collectively "the Group"). Control is achieved where the Bank has the power to govern the financial and operating policies of a subsidiary company so as to obtain benefits from its activities.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Basis of consolidation (Continued)

Where necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with those used by the Group.

All intra-group transactions, balances, income and expenses are eliminated on consolidation. Unrealized losses are eliminated in the same way as unrealized gains, but only to the extent that there is no evidence of impairment.

Minority interests in the net assets of consolidated subsidiaries are identified separately from the Group's equity therein. Minority interests consist of the amount of those interests at the date of the original business combination and the minority's share of changes in equity since the date of the combination. Losses applicable to the minority in excess of the minority's interest in the subsidiary's equity are allocated against the interests of the Group except to the extent that the minority has a binding obligation and is able to make an additional investment to cover the losses.

Short term Murabaha

Short term Murabaha are financial assets originated by the Group and represent deals with high credit quality banks and financial institutions with residual maturity of up to three months from the balance sheet date. These are stated at amortized cost.

Receivables

Murabaha

Receivables from Murabaha relate to the sale of commodities at cost plus an agreed upon profit margin, whereby the seller informs the buyer of the price at which the deal will be completed and also the amount of profit to be recognized. These receivables are stated at amortized cost.

Mudaraba

Mudaraba is a contract between the Bank and a client, whereby the Bank extends a certain amount of money to the client to be invested in a project or certain activity against a fixed share of the profit representing the total profit for the project less the client's share as a Mudarib. Balances relating to these contracts are stated net of provisions for impairment, if any.

Ijarah

Ijarah represents a contract which is executed for an asset owned by the lessor, wherein a customer requests the Bank to acquire the asset or to acquire the usufruct of an existing asset which the customer wishes to take on lease. Ijarah agreements provide a purchase option to lessees at a price equal or expected to be equal or lower than fair value of such assets at the time when such option is exercised. Ijarah assets are stated at amounts equal to the net investment outstanding in the lease.

Wakala

Wakala is an Islamic transaction involving the Muwakkil (the principle) who wishes to appoint the Wakkil (the agent) to be his agent with respect to the investment of the Muwakkil's fund in Islamically acceptable transactions. Wakala receivables are financial assets originated by the Bank stated at amortized cost net of provision for impairment.

Investments

Investments carried at fair value through profit or loss

Investments carried at fair value through profit or loss are acquired or incurred principally for the purpose of selling or repurchasing in the near term or is designated by the Group as such, upon initial recognition. Such investments are measured initially at cost, which is the fair value of the consideration given.

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Investments (Continued)

After initial recognition, the Group shall measure these investments at their fair values, without any deduction for transaction costs it may incur on sale or other disposal.

Unrealized gains and losses arising from a change in the fair value of these investments are recognized in the consolidated income statement. When the investments are sold, collected or otherwise disposed of, the realized gain or loss thereon are recognized in the consolidated income statement.

Available for sale investments

Available for sale investments are non-derivative investments that are not designated as another category of financial assets.

Investments are initially measured at cost, which is the fair value of the consideration, plus directly attributable transaction costs. Gains and losses arising from subsequent changes in fair value are recognised directly in equity, until the security is disposed of or is determined to be impaired, at which time the cumulative gain or loss previously recognised in equity is included in the consolidated income statement for the year.

Trade and settlement date accounting

All regular way purchase and sale of financial assets are recognized using settlement date accounting. Changes in the fair value between trade date and settlement date are recognized in the consolidated income statement for investments carried at fair value through profit or loss and are recognized in equity for investments available for sale. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame generally established by regulations or conventions in the market place.

Investments in associates

Associates are enterprises in which the Group exercises significant influence, and that is neither a subsidiary nor an interest in joint venture. Significant influence is the power to participate in financial and operating policy decision but not in control or joint control over those policies.

The results of associates are incorporated in the consolidated financial statements using the equity method of accounting. Under the equity method, investments in associates are carried in the consolidated balance sheet at cost as adjusted for post-acquisition changes in the Group's share of the net assets of the associate, less any impairment in the value of individual investments. Losses of an associate in excess of the Group's share of ownership in that associate (which includes any long-term share of ownership that, in substance, form part of the Group's net investment in the associate) are not recognized.

Any excess of the cost of acquisition over the Group's share of the net fair value of the identifiable assets, liabilities and contingent liabilities of the associate recognized at the date of acquisition is recognized as goodwill. The goodwill is included within the carrying amount of the investment and is assessed for impairment as part of the investment. Any excess of the Group's share of the net fair value of the identifiable assets, liabilities and contingent liabilities over the cost of acquisition, after reassessment, is recognized immediately in the consolidated income statement.

Unrealised gains arising from transactions with associates are eliminated against the investment to the extent of the Group's interest in the associate. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Leasing

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating lease.

Leased assets represent net investment in assets leased for periods which either approximate or cover a major part of the economic life of such assets. The lease agreements provide a purchase option to lessees at a price equal or expected to be equal or lower than fair value of such assets at the time when such option is exercised.

Leased assets are stated at amounts equal to the net investment outstanding in the leases.

For operating leases, lease payments (excluding costs for services such as insurance and maintenance) are recognized as an expense on a straight-line basis; whereas any initial leasing fees paid as a premium to the lessor are deferred and amortized over the life of the lease.

Impairment and uncollectability of financial assets

An assessment of financial assets is made at each balance sheet date to determine whether there is objective evidence that a specific financial asset may be impaired. If such evidence exists, an impairment loss is recognised in the consolidated income statement.

Impairment is determined as follows:

- (a) for assets carried at amortised cost, impairment is based on estimated cash flows discounted at the original effective rate of return;
- (b) for assets carried at fair value, impairment is the difference between cost and fair value; and
- (c) for assets carried at cost, impairment is the difference between cost and present value of future cash flows discounted at the current market rate of return for a similar financial asset.

In addition, in accordance with Central Bank of Kuwait instructions, a minimum general provision of 2% on all finance facilities net of certain categories of collateral, to which CBK instructions are applicable and not subject to specific provisions, is made.

Reversal of impairment losses recognised in prior years is recorded when there is an indication that the impairment losses recognised for the financial asset no longer exist or have decreased and the decrease can be related objectively to an event occurring after the impairment was recognised. Except for equity instruments classified as available for sale, reversals of impairment losses are recognised in the consolidated income statement to the extent the carrying value of the asset does not exceed its amortised cost at the reversal date. Reversals in respect of equity instruments classified as available for sale are recognised in the fair value reserve.

Impairment of tangible and intangible assets

At each balance sheet date, the Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs. Where a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual cash-generating units, or otherwise they are allocated to the smallest group of cash-generating units for which a reasonable and consistent allocation basis can be identified.

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Impairment of tangible and intangible assets (Continued)

Intangible assets with indefinite useful lives and intangible assets not yet available for use are tested for impairment annually, and whenever there is an indication that the asset may be impaired.

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

Reversal of impairment of assets

Where an impairment loss subsequently reverses, the carrying amount of the asset (cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset (cash-generating unit) in prior years. A reversal of impairment loss is recognized immediately in the consolidated income statement, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase. Impairment losses recognized in the consolidated income statement on available for sale equity instruments are not reversed through the consolidated income statement. Impairment losses recognized in profit or loss for debt instruments classified as available-for-sale are subsequently reversed if an increase in the fair value of the instrument can be objectively related to an event occurring after the recognition of the impairment loss.

Murabaha payable

Murabaha payable is an Islamic transaction involving the Group purchase of an asset from a counterparty and settlement thereof at cost plus an agreed profit on a deferred payment basis. The purchase price is payable to the counterparty on maturity. Murabaha payable is included in the balance sheet under "Due to banks and financial institutions" stated at amortized cost.

End of service benefits

A provision is made for amounts payable to the employees for end of service benefits, which is calculated in accordance with the provisions of the Bank's regulations and in accordance with the Labour Law of the State of Kuwait.

Provisions

A provision is recognized when, and only when the Group has a present legal or constructive obligation as a result of a past event and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation.

Provisions are reviewed at each balance sheet date and adjusted to reflect the current best estimate of the expenditure required to settle the obligation at the balance sheet date, and are discounted to present value where the effect is material.

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Fair values

Investments

For investments traded in organized financial markets, fair value is determined by reference to stock exchange quoted market bid prices at the close of the business on the balance sheet date.

For investments where there is no quoted market price, a reasonable estimate of the fair value is determined by reference to an earnings multiple, or an industry specific earnings multiple or a fair value based on a similar publicly traded company, or based on the expected cash flows of the investments.

Available for sale investments with no reliable measures of their fair values or for which fair value information could not be obtained are carried at their initial cost less impairment losses, if any.

Financial assets and liabilities

For financial assets and liabilities, fair value is determined based on expected future cash flows or management's estimate of the amount at which this asset could be exchanged for cash on an arm's length basis or a liability settled to the satisfaction of creditors.

Revenue recognition

- Income from Murabaha is recognized on a weighted time apportionment basis.
- Income from Ijarah receivables is recognized on a pattern reflecting a constant periodic return on the outstanding net investment.
- Income from Wakala is recognized on a time apportionment basis over the period of the contract based on the principle amounts outstanding.
- Dividend income is recognized when the right to receive payment is established.
- Fees and commission income is recognized at the time the related services are provided.

Cash and cash equivalents

Cash includes cash in hand and cash at banks and financial institutions both in local and foreign currencies. Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash with original maturities of three months or less and that are subject to an insignificant risk of change in value.

Foreign currencies

The individual financial statements of each group entity are presented in the currency of the primary economic environment in which the entity operates (its functional currency). For the purpose of the consolidated financial statements, the results and financial position of each entity are expressed in Kuwaiti Dinars ("KD"), which is the functional currency of the Bank, and the presentation currency for the consolidated financial statements.

Foreign currency transactions are recorded in Kuwaiti Dinars at the approximate rates of exchange prevailing at the date of the transactions. Transactions between the head office, branches and the subsidiaries are recorded at annually agreed fixed rates of exchange.

Exchange differences arising on the settlement of monetary items, and on the retranslation of monetary items, are included in the consolidated income statement for the year. Exchange differences arising on the retranslation of non-monetary items carried at fair value are included in the consolidated income statement for the year except for differences arising on the retranslation of non-monetary items in respect of which gains and losses are recognised directly in equity. For such non-monetary items, any exchange component of that gain or loss is also recognised directly in equity.

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Foreign currencies (Continued)

For the purpose of presenting consolidated financial statements, the assets and liabilities of the Group's foreign operations are expressed in KD using exchange rates prevailing on the balance sheet date. Income and expense items are translated at the average exchange rates for the year. Exchange differences arising, if any, are classified as equity and transferred to the Group's translation reserve. Such translation differences are recognised in the consolidated income statement in the year in which the foreign operation is disposed of.

Offsetting

Financial assets and financial liabilities are only offset and the net amount reported in the balance sheet when there is a legally enforceable right to set off the recognized amounts and the Group intends to settle on a net basis so as to realize the assets and liabilities simultaneously.

Income and expenses are presented on a net basis only when permitted by the accounting standards, or for gains and losses arising from a group of similar transactions such as in the Group's trading activity.

Contingencies and commitments

Contingent liabilities are not recognized in the consolidated financial statements. They are disclosed unless the possibility of an outflow of resources embodying economic benefits is remote.

A contingent asset is not recognized in the consolidated financial statements but is disclosed when an inflow of economic benefits is probable.

Segment reporting

A segment is a distinguishable component of the Group that is engaged in providing products or services (business segments), which is subject to risks and rewards that are different from those of other segments.

Fiduciary assets

Assets held in trust or in a fiduciary capacity are not treated as assets of the Group and accordingly are not included in these consolidated financial statements.

Property and equipment

Property and equipment are stated at cost less accumulated depreciation and impairment losses. When assets are sold or retired, their cost and accumulated depreciation are eliminated from the accounts and any gain or loss resulting from their disposal is included in the consolidated income statement.

The initial cost of property and equipment comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use. Depreciation is computed on a straight-line basis over the estimated useful lives of items of property and equipment as follows:

<u>Asset category</u>	<u>Useful life in years</u>
Furniture	5
Leasehold improvement	5
Office equipment	3
Tools	5

The useful lives and depreciation method are reviewed periodically to ensure that the method and period of depreciation are consistent with the expected pattern of economic benefits derived from items of property and equipment.

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Investment properties

Investment properties, which are held to earn rentals and / or for capital appreciation, are stated at their fair value at the balance sheet date. Gains or losses arising from changes in the fair value of the investment properties are included in the consolidated income statement for the period in which they arise.

Trading properties

Trading properties are held for short term purposes and stated at the lower of cost and net realizable value, determined on an individual basis. Cost comprises the purchase cost and other expenses incurred to complete the underlying transaction. Net realizable value is based on the estimated selling price less any future costs to be incurred on sale. Losses arising from valuation are included in the consolidated income statement.

3. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

Critical judgements in applying the entity's accounting policies

In the process of applying the Group's accounting policies, management has made the following judgements, apart from those involving estimations, which have the most significant effect in the amounts recognised in the consolidated financial statements:

Classification of investments

Management has to decide on acquisition of an investment whether it should be classified as held to maturity, available for sale or investments carried at fair value through profit or loss account.

The Group classifies investments as carried at fair value through profit or loss if they are acquired primarily for the purpose of short term profit making. All other investments are classified as available for sale.

Impairment of investments

The Group treats available for sale equity investments as impaired when there has been a significant or prolonged decline in the fair value below its cost or where other objective evidence of impairment exists. The determination of what is "significant" or "prolonged" requires considerable judgement. In addition, the Group evaluates other factors, including normal volatility in share price for quoted equities and the future cash flows and the discount factors for unquoted equities.

Key sources of estimation uncertainty

The key assumptions concerning the future and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are discussed below.

Impairment losses on finance facilities

The Group reviews its problem finance facilities on a quarterly basis to assess whether a provision for impairment should be recorded in the consolidated income statement. In particular, considerable judgement by management is required in the estimation of the amount and timing of future cash flows when determining the level of provisions required. Such estimates are necessarily based on assumptions about several factors involving varying degrees of judgment and uncertainty, and actual results may differ resulting in future changes to such provisions.

**3. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION
UNCERTAINTY (Continued)**

Valuation of unquoted equity investments

Valuation of unquoted equity investments is based on one of the following:

- recent arm's length market transactions;
- current fair value of another instrument that is substantially the same;
- the expected cash flows discounted at current rates applicable for items with similar terms and risk characteristics; or
- other valuation models.

The determination of the cash flows and discount factors for unquoted equity investments requires significant estimation. There are a number of investments where this estimation cannot be reliably determined. As a result, these investments are carried at cost less provision for impairment.

4. DISTRIBUTION TO DEPOSITORS

The Bank invests all of its investment deposits and saving accounts, adjusted for reserve requirements and the Bank's liquidity requirements.

Allocation of profits between depositors and shareholders is calculated according to the Bank's standard procedures approved by the Bank's Sharia'a Supervisory Board based on the result of the financial year as follows:

	2006	From date of incorporation 21 September 2004 to 31 December 2005
	KD'000	KD'000
Investment deposits	7,614	-
Saving accounts	322	-
	<u>7,936</u>	<u>-</u>

The balance payable is included in other liabilities.

5. INVESTMENT INCOME

	2006	From date of incorporation 21 September 2004 to 31 December 2005
	KD'000	KD'000
Realized gain from sale of Sukuk real estate	-	1,839
Unrealized gain on money market funds	902	403
Realized gain on money market funds	282	-
Sukuk Coupon income	858	384
Income from investment properties	931	-
Gain from sale of available for sale investments	236	-
Dividend income	152	108
	<u>3,361</u>	<u>2,734</u>

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6. PROVISION FOR IMPAIRMENT – GENERAL

	2006 KD'000	From date of incorporation 21 September 2004 to 31 December 2005 KD'000
Provision for impairment of short term Murabaha	360	562
Provision for impairment of receivables	944	1,144
Provision for impairment of contingencies and commitments	776	-
	<u>2,080</u>	<u>1,706</u>

Movements in the provision for impairment of finance facilities are as follows:

	Specific KD'000	General KD'000	Total KD'000
Balance at 31 December 2005	-	1,706	1,706
Provided during the year	-	2,080	2,080
Balance at 31 December 2006	<u>-</u>	<u>3,786</u>	<u>3,786</u>

At 31 December 2006, non-performing finance facilities amounted to KD Nil (31 December 2005: KD Nil).

The analysis of specific and general provision stated above is based on Central Bank of Kuwait requirements. In accordance with the Central Bank of Kuwait guidelines, a general provision of 2% has been provided on all credit facilities not subject to specific provision, net of certain collaterals.

The collective impairment provision computed in accordance with IAS 39 for the year / period ended 31 December 2006 and 31 December 2005 amounted to Nil.

7. EARNINGS PER SHARE

There are no potential dilutive ordinary shares. The information necessary to calculate basic earnings per share based on weighted average number of shares outstanding during the year / period is as follows:

	31 December 2006 KD'000	From date of incorporation 21 September 2004 to 31 December 2005 KD'000
Profit for the year / period	10,259	6,854
Weighted average number of shares outstanding (shares)	999,410	999,410
Earnings per share (fils)	<u>10.27</u>	<u>6.86</u>

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8. CASH AND CASH EQUIVALENTS

	2006	2005
	KD'000	KD'000
Balances with Central Bank of Kuwait	89	9,544
Balances with banks and other financial institutions	2,155	315
Cash and balances with banks and financial institutions	2,244	9,859
Short term funds	20,703	18,115
	<u>22,947</u>	<u>27,974</u>

9. SHORT TERM MURABAHA

	2006	2005
	KD'000	KD'000
Banks	232,153	141,271
Financial institutions	46,630	27,715
Others	-	489
Less: deferred profit	(517)	(701)
Less: provision for impairment	(922)	(562)
	<u>277,344</u>	<u>168,212</u>

The Group maintains international and local short term Murabaha placements under Murabaha and Wakalah agreements of 3 months or less maturity. Placements with financial institutions (Islamic and conventional) are utilized in the purchase and sale of commodities, as trading is conducted by those financial institutions on behalf of the Group. The discretion of the conventional financial institutions over buying and selling is limited by the terms of the agreements between the Group and the conventional financial institutions.

Provision for impairment is calculated based on Central Bank of Kuwait instructions on the outstanding balance of Murabaha net of the deferred profits.

10. RECEIVABLES

Receivables principally comprise Murabaha and Tawaroq balances and are stated net of provision for impairment as follows:

	2006	2005
	KD'000	KD'000
Financial institutions	43,950	45,309
Individuals and companies	66,909	16,853
Banks	11,096	-
Less: deferred profit	(4,328)	(2,826)
Less: provision for impairment	(2,088)	(1,144)
	<u>115,539</u>	<u>58,192</u>

Provision for impairment is calculated based on Central Bank of Kuwait instructions on the outstanding balance of receivables net of the deferred profits.

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10. RECEIVABLES (Continued)

Whenever necessary, Murabaha receivables are secured by acceptable forms of collateral to mitigate the related credit risks. Receivables from banks and financial institutions comprise mainly Murabaha transactions with high credit quality institutions.

The Group's receivables are concentrated in Kuwait.

The fair values of receivables do not differ from their respective book values.

11. AVAILABLE FOR SALE INVESTMENTS

	2006	2005
	KD'000	KD'000
Investment in Sukuk	12,330	14,308
Investment in unquoted securities	10,018	9,838
Investment in unquoted funds	8,362	2,091
	<u>30,710</u>	<u>26,237</u>

It was not possible to reliably measure the fair value of certain available for sale investments of KD 14,463 thousand (31 December 2005: KD 26,237 thousand) due to lack of reliable measure to determine the fair value of such investments. Accordingly, they are stated at cost less impairment losses, if any.

12. SUBSIDIARIES

During the year, the Bank has established a wholly owned subsidiary in the United Kingdom under the name of House of London and the Middle East plc with a capital equivalent to KD 1,133 thousand whose proposed principal activities are to conduct Sharia'a compliant financial services activities. The investment has not been consolidated and is stated at cost as the subsidiary has not started its operations yet.

During the year, the Bank has acquired a 76.41% interest in Boubyan Takaful Insurance Company KSC (Closed), a Kuwaiti Shareholding Company engaged in Islamic Takaful insurance activities in accordance with Noble Islamic Sharia'a principles. The investment in the subsidiary of KD 2,820 thousand represents 56.41% of the subsidiary's paid up share capital. The remaining shares of 20% amounting to KD 1,000 thousand are classified under other assets as these shares have been committed to be subscribed by a strategic investor. On 4 January 2007, the agreement between the Bank and the strategic investor has been finalized. The Bank has signed a promise to sell agreement with one of the insurance companies in GCC ("Investor") regarding the remaining shares, which was entered into effect on 4 January 2007. The agreement stipulates that the Bank gives a committed promise to sell to the investor 20 million shares in Boubyan Takaful Insurance Company after three years as of the incorporation date of the above – mentioned company so that all the related economic risks and rewards of such shares will be transferred to the investor effective 4 January 2007.

Name of subsidiary	Country of Incorporation	2006 proportion of ownership interest and voting power %	2005 proportion of ownership interest and voting power %	Principal activity
House of London and the Middle East plc.	United Kingdom	100	-	Islamic financial services
Boubyan Takaful Insurance Co. KSC (Closed)	Kuwait	56.41	-	Islamic Takaful Insurance

13. INVESTMENTS IN ASSOCIATES

The investments in associates comprise the following:

Name of associate	Country of Incorporation	2006 proportion of ownership interest and voting power %	2005 proportion of ownership interest and voting power %	Principal activity
Bank Muamalat	Indonesia	21.28	21.28	Islamic Banking
Al Bilad Real Estate Co.	Kuwait	31.7	31.7	Real Estate

Bank Muamalat - Indonesia was established in 1991 and commenced operation on May 1992. The establishment of Bank Muamalat was initiated by the Indonesian Council of Ulama (MUI), which was supported by a group of entrepreneurs. The movement in the investment balances is as follows:

	2006 KD'000	2005 KD'000
Balance at the beginning of the year / period	8,263	-
Acquisition of associates	-	7,316
Share of results of associates	927	947
Dividends received	(504)	-
Foreign currency translation adjustment	394	-
	<u>9,080</u>	<u>8,263</u>

The Group's share of results of associates is recognised based on unaudited management financial statements. Bank Muamalat financial statements date is 31 August 2006 and Al Bilad Real Estate Company financial statements date is 30 November 2006. The Bank's balances in its associates were as follows:

Name of the associate	Assets KD'000	Liabilities KD'000	Revenues KD'000	Results KD'000
Al Bilad R/E Co.	3,934	307	559	384
Bank Muamalat	53,044	47,622	3,196	543
	<u>56,978</u>	<u>47,929</u>	<u>3,755</u>	<u>927</u>

The Bank's balances in its associates as at 31 December 2005 were as follows:

Name of the associate	Assets KD'000	Liabilities KD'000	Revenues KD'000	Results KD'000
Al Bilad R/E Co.	3,170	-	-	-
Bank Muamalat	43,947	38,807	3,954	728
	<u>47,117</u>	<u>38,807</u>	<u>3,954</u>	<u>728</u>

14. LEASED ASSETS

The net investment in leased assets comprises the following:

	2006	2005
	KD'000	KD'000
Gross investment	8,954	1,946
Unearned revenue	(1,014)	(152)
	<u>7,940</u>	<u>1,794</u>

The future minimum lease payments receivable in the aggregate are as follows:

	2006	2005
	KD'000	KD'000
Within one year	5,771	1,519
One to five years	190	275
After five years	1,979	-
	<u>7,940</u>	<u>1,794</u>

The unguaranteed residual value of the leased assets at 31 December 2006 is estimated at KD Nil (2005: KD Nil).

The fair value of the leased assets at the balance sheet date is KD 7,940 thousand (2005: KD 1,794 thousand).

15. OTHER ASSETS

	2006	2005
	KD'000	KD'000
Due from Real Estate Sukuk Fund	13,182	31,184
Income receivable on investments	2,851	342
Prepayments	1,061	230
Others	1,530	600
	<u>18,624</u>	<u>32,356</u>

16. DUE TO BANKS AND FINANCIAL INSTITUTIONS

	2006	2005
	KD'000	KD'000
Investment accounts	144,275	73,788
Murabaha payable	62,890	33,182
Non-investment accounts	-	1,169
	<u>207,165</u>	<u>108,139</u>

In accordance with Islamic Sharia'a, no profit is payable on non-investment accounts due to banks and financial institutions. The fair value of balances due to banks and financial institutions do not differ from their respective book values.

17. DEPOSITORS' ACCOUNTS

	2006	2005
	KD'000	KD'000
Non-investment accounts	90,219	60,428
Investment accounts	78,373	30,805
	<u>168,592</u>	<u>91,233</u>

Investment accounts

Investment accounts may take the form of investment deposits, which are valid for specified periods of time, and are automatically renewable on maturity for the same period unless the concerned depositors give written notice to the contrary, or take the form of investment saving accounts for unspecified periods. In all cases, investment accounts receive a proportion of the profit and bear a share of loss based on the results of the fiscal year determined by the Board of Directors of the Bank.

Non-investment accounts

Non-investment accounts represent, in accordance with Islamic Sharia'a, Qard Hasan from depositors to the Bank and take the form of current accounts. These accounts are neither entitled to profit nor do they bear any risk of loss, as the Bank guarantees to pay the related balance on demand. Investing Qard Hasan is made at the discretion of the Board of Directors of the Bank and the results of such investments are attributable to the shareholders of the Bank.

18. OTHER LIABILITIES

	2006	2005
	KD'000	KD'000
Sukuk for Real Estate Development Co.	-	21,081
Accrued expenses	218	247
Accrued staff benefits	915	355
Suppliers	56	151
Clearing accounts	1,372	-
Trade finance provision	776	-
Margin accounts	1,813	-
NLST and KFAS due	424	63
Others	2,598	284
	<u>8,172</u>	<u>22,181</u>

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19. SHARE CAPITAL

	2006		2005	
	Shares	KD'000	Shares	KD'000
Authorized ordinary shares of par value 100 fils	1,000,000,000	100,000	1,000,000,000	100,000
Fraction shares not issued	(589,670)	(59)	(589,670)	(59)
Shares issued and fully paid	999,410,330	99,941	999,410,330	99,941

20. SHARE PREMIUM

The share premium is not distributable except under specific circumstances as provided by the Kuwait Commercial Companies Law.

21. STATUTORY RESERVE

As required by the Commercial Companies Law and the Bank's Articles of Association 10% of profit for the year is transferred to statutory reserve. The Bank may resolve to discontinue such annual transfers when the reserve equals 50% of the capital. This reserve is not available for distribution except in cases stipulated by Law and the Bank's Articles of Association.

22. VOLUNTARY RESERVE

As required by the Bank's Articles of Association 10% of profit for the year is transferred to the voluntary reserve. Such annual transfers may be discontinued by a resolution of the shareholders' General Assembly upon a recommendation by the Board of Directors. Zakat is charged against the voluntary reserve and amounted to KD 177 thousand for the year ended 31 December 2005.

23. OPERATING LEASES

The Group has entered into several lease arrangements, mainly for renting buildings, offices and equipment. The total future minimum lease payments under the operating leases for each of the following periods is:

	2006	2005
	KD'000	KD'000
Not later than one year	1,303	905
After one year and not later than five years	3,234	2,308
	4,537	3,213

Such lease agreements are subject to automatic renewal unless one of the parties to that agreement notifies the other, with no purchase options or any escalation clauses.

24. RELATED PARTY TRANSACTIONS

Balances with related parties arise from commercial transactions in the normal course of business on an arm's length basis and comprise the following:

	2006	2005
	KD'000	KD'000
Due from related parties:		
Receivables and other assets	14,053	31,184
Due to related parties:		
Due to banks and financial institutions	28,414	26,003
Depositors' accounts	-	15,278

Compensation of key management personnel:

The remuneration to Directors and other members of key management during the year/period was as follows:

	31 December 2006	From date of incorporation 21 September 2004 to 31 December 2005
	KD'000	KD'000
Short-term benefits	624	496
Post-employment benefits	220	117
	<u>844</u>	<u>613</u>

During the year, the Bank sold trading properties and investment properties to related parties at book value amounting to KD 289 thousand and KD 11,688 thousand respectively (2005: Nil).

During the year, the Bank also sold available for sale investments to its associate, Al Bilad Real Estate Co. for KD 2,939 thousand, which resulted in a realized gain of KD 157 thousand after eliminating the Bank's share (31.7%) of KD 72 thousand in the associate (Note 13).

25. CONTINGENCIES AND COMMITMENTS

At the balance sheet date there were outstanding contingencies and commitments entered in the ordinary course of business in respect of the following:

	2006	2005
	KD'000	KD'000
Guarantees	27,453	-
Acceptances and letters of credit	13,030	-
Investment commitments	31,303	5,259
Capital commitments (projects under construction)	670	1,839
	<u>72,456</u>	<u>7,098</u>

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26. SEGMENT REPORTING

For management purposes, the Bank is organized into the following four major business segments:

Retail banking: Principally handling the deposits of individual customers and small businesses, and providing consumer and commercial type Murabaha, Ijara and Islamic covered cards facilities.

Corporate banking: Principally handling Murabaha and Ijarah facilities for corporate and institutional customers.

Investment: Principally handling direct investments, Sukuk, and local and international real estate investment.

Treasury: Principally handling local and international Murabaha and Wakala, primarily with financial institutions, as well as the management of the Bank's funding operations.

For the year ended 31 December 2006

	<u>Retail banking</u>	<u>Corporate banking</u>	<u>Investment</u>	<u>Treasury</u>	<u>Unallocated items</u>	<u>Total</u>
	KD'000	KD'000	KD'000	KD'000	KD'000	KD'000
Segment revenues	553	2,903	6,381	19,495	472	29,804
Segment expenses	(3,088)	(1,733)	(769)	(8,974)	(4,926)	(19,490)
Segment results	<u>(2,535)</u>	<u>1,170</u>	<u>5,612</u>	<u>10,521</u>	<u>(4,454)</u>	<u>10,314</u>
	<u>Retail banking</u>	<u>Corporate banking</u>	<u>Investment</u>	<u>Treasury</u>	<u>Unallocated items</u>	<u>Total</u>
	KD'000	KD'000	KD'000	KD'000	KD'000	KD'000
Assets						
Cash and cash equivalents	1,811	-	4,110	17,026	-	22,947
Short term Murabaha	-	-	-	277,344	-	277,344
Receivables	-	78,737	-	36,802	-	115,539
Investments carried at fair value through profit or loss	-	-	1,020	-	-	1,020
Available for sale investments	-	-	18,379	12,331	-	30,710
Investment in unconsolidated subsidiary	-	-	1,133	-	-	1,133
Investments in associates	-	-	9,080	-	-	9,080
Trading properties	-	-	2,885	-	-	2,885
Investment properties	-	-	13,508	-	-	13,508
Leased assets	-	7,940	-	-	-	7,940
Other assets	132	-	16,541	51	1,900	18,624
Property and equipment	524	44	51	37	2,953	3,609
Total assets	<u>2,467</u>	<u>86,721</u>	<u>66,707</u>	<u>343,591</u>	<u>4,853</u>	<u>504,339</u>
Liabilities and equity						
Due to banks and financial institutions	-	-	-	207,165	-	207,165
Depositors' accounts	128,833	-	-	39,759	-	168,592
Other liabilities	1,937	596	2,262	177	3,200	8,172
Equity	-	-	-	-	120,410	120,410
Total Liabilities and equity	<u>130,770</u>	<u>596</u>	<u>2,262</u>	<u>247,101</u>	<u>123,610</u>	<u>504,339</u>

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26. SEGMENT REPORTING (CONTINUED)

From date of incorporation 21 September 2004 to 31 December 2005

	<u>Retail banking</u>	<u>Corporate banking</u>	<u>Investment</u>	<u>Treasury</u>	<u>Unallocated items</u>	<u>Total</u>
	KD'000	KD'000	KD'000	KD'000	KD'000	KD'000
Segment revenues	-	390	3,527	8,974	-	12,891
Segment expenses	(482)	(638)	(338)	(2,110)	(2,469)	(6,037)
Segment results	<u>(482)</u>	<u>(248)</u>	<u>3,189</u>	<u>6,864</u>	<u>(2,469)</u>	<u>6,854</u>
	<u>Retail banking</u>	<u>Corporate banking</u>	<u>Investment</u>	<u>Treasury</u>	<u>Unallocated items</u>	<u>Total</u>
	KD'000	KD'000	KD'000	KD'000	KD'000	KD'000
Assets						
Cash and cash equivalents	-	-	-	27,974	-	27,974
Short term Murabaha	-	473	-	167,739	-	168,212
Receivables	-	15,410	-	42,782	-	58,192
Available for sale investments	-	-	11,929	14,308	-	26,237
Investments in associates	-	-	8,263	-	-	8,263
Trading properties	-	-	3,206	-	-	3,206
Leased assets	-	1,794	-	-	-	1,794
Other assets	-	-	31,184	342	830	32,356
Property and equipment	-	-	-	-	2,236	2,236
Total assets	<u>-</u>	<u>17,677</u>	<u>54,582</u>	<u>253,145</u>	<u>3,066</u>	<u>328,470</u>
Liabilities and equity						
Due to banks and financial institutions	1,169	-	-	106,970	-	108,139
Depositors' accounts	60,428	-	-	30,805	-	91,233
Other liabilities	-	-	21,081	-	1,100	22,181
Equity	-	-	-	-	106,917	106,917
Total liabilities and equity	<u>61,597</u>	<u>-</u>	<u>21,081</u>	<u>137,775</u>	<u>108,017</u>	<u>328,470</u>

26. SEGMENT REPORTING (CONTINUED)

Secondary segment information

The Bank operates in various geographical sectors. The geographical analysis is as follows:

For the year ended 31 December 2006

	<u>Assets</u>	<u>Liabilities & equity</u>	<u>Commitments & contingencies</u>
	2006	2006	2006
	KD'000	KD'000	KD'000
Geographical area:			
Kuwait and the Middle East	461,616	491,725	51,635
North America	6,589	-	-
Western Europe	26,061	2,035	14,835
Others	10,073	10,579	5,986
	<u>504,339</u>	<u>504,339</u>	<u>72,456</u>
		<u>Operating income</u>	<u>Operating profit before distribution to depositors</u>
		2006	2006
		KD'000	KD'000
Kuwait and the Middle East		23,895	12,872
North America		490	488
Western Europe		3,890	3,886
Others		1,529	1,481
		<u>29,804</u>	<u>18,727</u>

From date of incorporation 21 September 2004 to 31 December 2005

	<u>Assets</u>	<u>Liabilities & equity</u>	<u>Commitments & contingencies</u>
	2005	2005	2005
	KD'000	KD'000	KD'000
Geographical area:			
Kuwait and the Middle East	312,123	327,346	6,610
North America	3,811	24	488
Western Europe	40	-	-
Others	12,496	1,100	-
	<u>328,470</u>	<u>328,470</u>	<u>7,098</u>
		<u>Operating income</u>	<u>Operating profit before distribution to depositors</u>
		2005	2005
		KD'000	KD'000
Kuwait and the Middle East		10,449	4,765
Others		2,442	2,242
		<u>12,891</u>	<u>7,007</u>

26. SEGMENT REPORTING (CONTINUED)

Concentration of assets

Concentrations arise when a number of counterparties are engaged in similar business activities, or activities in the same geographic region or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations indicate the relative sensitivity of the Group's performance to developments affecting a particular industry or geographic location.

The distribution of assets by industry sector was as follows:

	2006	2005
	KD'000	KD'000
Trading and manufacturing	25,056	-
Banks and financial institutions	362,708	293,747
Construction and real estate	46,569	15,862
Others	70,006	18,861
	<u>504,339</u>	<u>328,470</u>

27. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

In the normal course of business, the Group uses primary financial instruments such as cash and short term funds, investments, bank borrowings, accounts receivable and accounts payable and as a result, is exposed to the risks indicated below. The Group currently does not use derivative financial instruments to manage its exposure to these risks.

Credit risk

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation causing the other party to incur a financial loss. To limit this risk, the Group deals exclusively with high credit rating financial institutions and has policies and procedures in place to limit the amount of credit exposure to any counter party. These policies include the non-concentration of credit risk. The Bank minimizes other concentrations of credit risk by undertaking transactions with a large number of consumers.

Market risk

Market risk is the risk that the value of an asset will fluctuate as a result of changes in market prices.

Market risk is managed on the basis of pre-determined asset allocations across various asset categories, a continuous appraisal of market conditions and trends and management's estimate of long and short term changes in fair value.

The Group is not exposed to any risk in terms of the repricing of its liabilities since in accordance with Islamic Sharia'a the Group does not provide contractual rates of return to its depositors.

Operational risk

The Bank has a set of policies and procedures, which is applied to identify, assess and supervise operational risk in addition to other types of risks relating to the banking and financial activities of the Bank. Operational risk is managed by the operational risk function, which ensures compliance with policies and procedures and monitors operational risk as part of overall global risk management.

The operational risk function of the Bank is in line with the Central Bank of Kuwait instructions concerning the general guidelines for internal controls and best practice for managing and supervising operational risks in banks.

27. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (CONTINUED)

Foreign currency risk

The Group is exposed to foreign currency risk on transactions that are denominated in a currency other than the Kuwaiti Dinar. The Bank ensures that the net exposure is kept to an acceptable level by dealing in currencies that do not fluctuate significantly against the Kuwaiti Dinar.

The Group has the following significant net exposures of assets denominated in Kuwaiti Dinar equivalents:

	2006	2005
	KD'000	KD'000
US Dollar	(7,948)	6,649
Sterling Pound	370	-
Euros	376	-
GCC Currencies	27	-
Other currencies	5,612	65

Liquidity risk

Liquidity risk is the risk that the Group will be unable to meet its net funding requirements. Liquidity risk can be caused by market disruptions or credit downgrades which may cause certain sources of funding to dry up immediately. To guard against this risk, management have diversified funding sources and assets are managed with liquidity in mind, maintaining a healthy balance of cash, cash equivalents and readily marketable securities. Further, the Group periodically assesses the financial viability of customers.

The table below summarizes the maturity profile of the Group's assets and liabilities. The contractual maturities of assets and liabilities have been determined on the basis of the remaining period at the balance sheet date to the contractual maturity date and do not take into account the effective maturities as indicated by the availability of liquid funds. The maturity profile is monitored by management to ensure that adequate liquidity is maintained. The maturity profile of the assets and liabilities at period end is based on contractual repayment arrangements.

27. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (CONTINUED)

The maturity profile of the assets and liabilities is as follows:

31 December 2006

	Within three months	From 3 months to 6 months	From 6 months to 1 year	More than 1 year	Total
	KD'000	KD'000	KD'000	KD'000	KD'000
Assets					
Cash and cash equivalent	22,947	-	-	-	22,947
Short term Murabaha	277,344	-	-	-	277,344
Receivables	37,259	50,192	16,132	11,956	115,539
Investments carried at fair value through profit or loss	-	-	1,020	-	1,020
Available for sale investments	-	-	-	30,710	30,710
Investments in unconsolidated subsidiary	-	-	-	1,133	1,133
Investments in associates	-	-	-	9,080	9,080
Trading properties	-	-	2,885	-	2,885
Investment properties	-	-	-	13,508	13,508
Leased assets	-	-	5,771	2,169	7,940
Other assets	-	18,624	-	-	18,624
Property and equipment	-	-	-	3,609	3,609
Total assets	<u>337,550</u>	<u>68,816</u>	<u>25,808</u>	<u>72,165</u>	<u>504,339</u>
Liabilities and equity					
Due to banks and financial institutions	185,325	8,054	13,786	-	207,165
Depositors' accounts	166,938	1,654	-	-	168,592
Other liabilities	6,137	-	2,035	-	8,172
Equity	-	-	-	120,410	120,410
Total liabilities and equity	<u>358,400</u>	<u>9,708</u>	<u>15,821</u>	<u>120,410</u>	<u>504,339</u>

27. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (CONTINUED)

31 December 2005

	Within three months	From 3 months to 6 months	From 6 months to 1 year	More than 1 year	Total
	KD'000	KD'000	KD'000	KD'000	KD'000
Assets					
Cash and cash equivalents	27,974	-	-	-	27,974
Short term Murabaha	168,212	-	-	-	168,212
Receivables	-	37,598	9,989	10,605	58,192
Available for sale investments	-	14,308	-	11,929	26,237
Investments in associates	-	-	-	8,263	8,263
Trading properties	-	-	-	3,206	3,206
Leased assets	-	-	1,520	274	1,794
Other assets	31,184	-	1,172	-	32,356
Property and equipment	-	-	-	2,236	2,236
Total assets	227,370	51,906	12,681	36,513	328,470
Liabilities and equity					
Due to banks and financial institutions	104,106	4,033	-	-	108,139
Depositors' accounts	91,233	-	-	-	91,233
Other liabilities	21,081	1,100	-	-	22,181
Equity	-	-	-	106,917	106,917
Total liabilities and equity	216,420	5,133	-	106,917	328,470

Fair value of financial instruments

Fair value is defined as the amount at which the instrument could be exchanged in a current transaction between knowledgeable willing parties in an arm's length transaction, other than in a forced or liquidation sale. Fair values are obtained from quoted market prices, discounted cash flow models and other models as appropriate. The carrying values of financial instruments approximate their fair values at 31 December due to the relatively short-term maturity of the instruments except that it was not possible to reliably measure the fair value of unquoted securities.

28. FIDUCIARY ASSETS

The aggregate value of assets held in a trust or fiduciary capacity by the Bank amounted to KD 118,511 thousand (31 December 2005: KD 26,868 thousand).

29. PROPOSED DIVIDEND

The board of directors recommended distribution of bonus shares dividend of 6% on outstanding shares as at 31 December 2006. The proposed dividend, if approved, shall be payable to the shareholders registered in the Bank's records as of the date of the general assembly meeting.

**BOUBYAN BANK K.S.C. AND SUBSIDIARY
STATE OF KUWAIT**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006



30. COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform with the current year's presentation. Prior period figures are not comparable with current year since it covers a period of 15 months.