BOUBYAN BANK K.S.C. AND SUBSIDIARIES
STATE OF KUWAIT

بنك بوبيان
Boubyan Bank

CONSOLIDATED FINANCIAL STATEMENTS
AND INDEPENDENT AUDITORS' REPORT
FOR THE YEAR ENDED 31 DECEMBER 2012

INDEX

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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 its subsidiaries (collectively "the Group"), which comprise the consolidated statement of financial position as at 31 December 2012, and the consolidated statement of income, consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards as adopted for use by the State of Kuwait, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

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 about 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 auditors' judgement, 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.

Deloitte.

KPMG

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as at 31 December 2012, and their financial performance and 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 all the information and explanations that we required for the purpose of our audit and that the consolidated financial statements incorporate all information that is required by the Commercial Companies Law No. 25 of 2012, 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 Commercial Companies Law No. 25 of 2012, nor of the Articles of Association have occurred during the year ended 31 December 2012 that might have had a material effect on the business of the Group or on its consolidated 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 CBK and the organization of banking business, and its related regulations during the year ended 31 December 2012.

Bader A. Al-Wazzan	**Safi A. Al-Mutawa**
License No. 62A	**License No. 138-A**
of Deloitte & Touche	**of KPMG Safi Al-Mutawa & Partners**
Al-Fahad Al-Wazzan & Co.	**Member firm of KPMG International**

Kuwait
20 January 2013

BOUBYAN BANK K.S.C. AND SUBSIDIARIES
STATE OF KUWAIT

CONSOLIDATED STATEMENT OF INCOME
For the year ended 31 December 2012

	Notes	**2012** **KD'000**	2011 KD'000
Income			
Murabaha and other Islamic financing income		**64,670**	52,927
Distribution to depositors		**(10,176)**	(11,671)
Murabaha cost		**(2,023)**	(1,647)
Net financing income		**52,471**	39,609
Net investment loss	5	**(522)**	(2,295)
Net fees and commission income	6	**3,679**	3,991
Share of results of associates	15	**2,364**	3,611
Net foreign exchange gain		**886**	858
Other income		**1**	165
Operating income		**58,879**	45,939
Staff costs		**(17,249)**	(15,605)
General and administrative expenses		**(9,311)**	(8,181)
Depreciation and amortization		**(1,911)**	(1,594)
Operating expenses		**(28,471)**	(25,380)
Operating profit before provision for impairment		**30,408**	20,559
Provision for impairment	7	**(20,432)**	(12,226)
Operating profit before deductions		**9,976**	8,333
Contribution to Kuwait Foundation for the Advancement of Sciences ("KFAS")		**(94)**	(76)
National Labour Support Tax ("NLST")		**(209)**	(226)
Zakat		**(83)**	(90)
Board of directors' remuneration		**(54)**	-
Net profit for the year		**9,536**	7,941
Attributable to:			
Equity holders of the Bank		**10,050**	8,025
Non-controlling interests		**(514)**	(84)
Net profit for the year		**9,536**	7,941
Basic and diluted earnings per share attributable to the equity holders of the Bank (fils)	8	**5.75**	4.59

The notes from 1 to 32 form an integral part of these consolidated financial statements.

بـنـك بـوبـيـان
Boubyan Bank

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME
For the year ended 31 December 2012

	2012 **KD'000**	2011 KD'000
Net profit for the year	**9,536**	7,941
Other comprehensive income		
Change in fair value of available for sale investments	**(2,190)**	(1,802)
Net realized gains on available for sale investments	**-**	(1,730)
Impairment losses on available for sale Investments transferred to consolidated statement of income	**3,976**	3,224
Foreign currency translation adjustments	**(2,509)**	(891)
Other comprehensive loss for the year	**(723)**	(1,199)
Total comprehensive income for the year	**8,813**	6,742
Attributable to:		
Equity holders of the Bank	**9,327**	6,826
Non-controlling interests	**(514)**	(84)
Total comprehensive income for the year	**8,813**	6,742

The notes from 1 to 32 form an integral part of these consolidated financial statements.

BOUBYAN BANK K.S.C. AND SUBSIDIARIES
STATE OF KUWAIT

CONSOLIDATED STATEMENT OF FINANCIAL POSITION
As at 31 December 2012

	Notes	2012 KD'000	2011 KD'000
Assets			
Cash and cash equivalents	9	**169,530**	191,957
Due from banks	10	**251,625**	128,061
Islamic financing to customers	11	**1,270,014**	1,030,084
Financial assets at fair value through profit or loss	12	**51,293**	65,197
Available for sale investments	13	**99,929**	66,127
Investments in associates	15	**9,082**	26,449
Investment properties	16	**17,904**	25,613
Other assets	17	**7,916**	7,436
Property and equipment		**7,363**	6,179
Total assets		**1,884,656**	1,547,103
Liabilities and Equity			
Liabilities			
Due to banks		**207,133**	78,987
Depositors' accounts		**1,396,962**	1,202,428
Other liabilities	18	**24,397**	18,520
Total liabilities		**1,628,492**	1,299,935
Equity			
Share capital	19	**174,824**	174,824
Share premium	20	**62,896**	62,896
Proposed bonus shares	21	**8,741**	-
Treasury shares	22	**(1,024)**	(1,024)
Statutory reserve	23	**1,891**	842
Voluntary reserve	24	**1,813**	802
Share based payment reserve	25	**537**	253
Fair value reserve		**3,421**	1,635
Foreign currency translation reserve		**(4,873)**	(2,364)
Retained earnings		**5,424**	6,381
Equity attributable to equity holders of the Bank		**253,650**	244,245
Non-controlling interests		**2,514**	2,923
Total equity		**256,164**	247,168
Total liabilities and equity		**1,884,656**	1,547,103

Adel Abdul Wahab Al Majed
Chairman & Managing Director

The notes from 1 to 32 form an integral part of these consolidated financial statements.

BOUBYAN BANK K.S.C. AND SUBSIDIARIES
STATE OF KUWAIT

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
For the year ended 31 December 2012

	Share capital KD'000	Share premium KD'000	Proposed bonus shares KD'000	Treasury shares KD'000	Statutory reserve KD'000	Voluntary reserve KD'000	Share based payment reserve KD'000	Fair value reserve KD'000	Foreign currency translation reserve KD'000	Retained earnings KD'000	Equity attributable to equity holders of the Bank KD'000	Non-controlling interests KD'000	Total equity KD'000
Balance at 1 January 2011	174,824	87,728	-	-	3,913	3,591	-	1,943	(1,473)	(32,336)	238,190	1,920	240,110
Total comprehensive income for the year	-	-	-	-	-	-	-	(308)	(891)	8,025	6,826	(84)	6,742
Transfer to reserves	-	-	-	-	842	802	-	-	-	(1,644)	-	-	-
Write off of accumulated losses	-	(24,832)	-	-	(3,913)	(3,591)	-	-	-	32,336	-	-	-
Purchase of treasury shares	-	-	-	(1,024)	-	-	-	-	-	-	(1,024)	-	(1,024)
Share based payment (note 25)	-	-	-	-	-	-	253	-	-	-	253	-	253
Net movement in non-controlling interests	-	-	-	-	-	-	-	-	-	-	-	1,087	1,087
Balance at 31 December 2011	**174,824**	**62,896**	**-**	**(1,024)**	**842**	**802**	**253**	**1,635**	**(2,364)**	**6,381**	**244,245**	**2,923**	**247,168**
Total comprehensive income for the year	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**1,786**	**(2,509)**	**10,050**	**9,327**	**(514)**	**8,813**
Transfer to reserves	**-**	**-**	**-**	**-**	**1,049**	**1,011**	**-**	**-**	**-**	**(2,060)**	**-**	**-**	**-**
Proposed bonus shares (note 21)	**-**	**-**	**8,741**	**-**	**-**	**-**	**-**	**-**	**-**	**(8,741)**	**-**	**-**	**-**
Share based payment (note 25)	**-**	**-**	**-**	**-**	**-**	**-**	**284**	**-**	**-**	**-**	**284**	**-**	**284**
Acquisition of non-controlling interests	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**(206)**	**(206)**	**(888)**	**(1,094)**
Net movement in non-controlling interests	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**993**	**993**
Balance at 31 December 2012	**174,824**	**62,896**	**8,741**	**(1,024)**	**1,891**	**1,813**	**537**	**3,421**	**(4,873)**	**5,424**	**253,650**	**2,514**	**256,164**

The notes from 1 to 32 form an integral part of these consolidated financial statements.

Boubyan Bank

CONSOLIDATED STATEMENT OF CASH FLOWS
For the year ended 31 December 2012

	Notes	2012 KD'000	2011 KD'000
OPERATING ACTIVITIES			
Net profit for the year		**9,536**	7,941
Adjustments for:			
Provision for impairment	7	**20,432**	12,226
Depreciation and amortization		**1,911**	1,594
Foreign currency translation adjustments		**(2,468)**	800
Loss / (gain) on sale of investments		**373**	(1,728)
Unrealized loss from financial assets at fair value through profit or loss		**14,234**	1,202
Share of results of associates		**(2,364)**	(3,611)
Unrealised profit on interest retained subsequent to loss of significant influence		**(18,087)**	-
Realized profit from partial disposal of associate		**(5,703)**	-
Dividend income		**(872)**	(906)
Net unrealized loss from change in fair value of investment properties		**5,026**	5,402
Loss on sale of investment properties		**7,433**	-
Share based payment reserve		**284**	253
Operating profit before changes in operating assets and liabilities		**29,735**	23,173
Changes in operating assets and liabilities:			
Due from banks		**(128,384)**	18,836
Islamic financing to customers		**(256,010)**	(210,882)
Other assets		**(757)**	(2,314)
Due to banks		**128,147**	(41,543)
Depositors' accounts		**194,535**	261,400
Other liabilities		**5,877**	7,543
Dividend income received		**872**	906
Net cash (used in) / generated from operating activities		**(25,985)**	57,119
INVESTING ACTIVITIES			
Purchase of financial assets at fair value through profit or loss		**(1,990)**	(3,099)
Proceeds from sale of financial assets at fair value through profit or loss		**2,596**	13,378
Purchase of available for sale investments		**(6,754)**	(39,130)
Proceeds from sale of available for sale investments		**6,936**	29,003
Dividends received from associates	15	**290**	337
Acquisition of associates		**-**	(2,570)
Proceeds from disposals of investment in associates	15	**9,638**	-
Purchase of investment properties		**(3,961)**	(700)
Purchase of property and equipment		**(3,096)**	(3,098)
Acquisition of non-controlling interests		**(1,094)**	-
Net cash generated from / (used in) investing activities		**2,565**	(5,879)
FINANCING ACTIVITES			
Net movement in non-controlling interests		**993**	1,087
Purchase of treasury shares		**-**	(1,024)
Net cash generated from financing activities		**993**	63
Net (decrease)/ increase in cash and cash equivalents		**(22,427)**	51,303
Cash and cash equivalents at the beginning of the year		**191,957**	140,654
Cash and cash equivalents at the end of the year	9	**169,530**	191,957

The notes from 1 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 is 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 total number of employees in the Group was **807** as at 31 December 2012 (738 employees as at 31 December 2011).

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

2. BASIS OF PREPARATION

2.1 Statement of compliance

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRSs") promulgated by the International Accounting Standards Board ("IASB") and interpretations issued by the International Financial Reporting Interpretations Committee of the IASB, as adopted for use by the State of Kuwait for financial services institutions regulated by the CBK. These regulations require adoption of all IFRSs except for the IAS 39 requirements for collective impairment provision, which has been replaced by the CBK requirements for a minimum general provision as described in accounting policy 3.9.1.

The consolidated financial statements were authorised for issue by the Board of Directors on 8 January 2013 and the shareholders have the power to amend these consolidated financial statement at the annual assembly meeting.

2.2 Basis of measurement

The consolidated financial statements have been prepared under the historical cost basis except for the measurement at fair value of investment securities other than held to maturity investments and investment properties.

2.3 Functional and presentation currency

These consolidated financial statements are presented in Kuwaiti Dinars, which is the Bank's functional currency. All financial information presented in Kuwaiti Dinars ("KD") has been rounded to the nearest thousand, except when otherwise indicated.

2.4 New standards, interpretations and amendments effective from 1 January 2012

None of the new standards, interpretations and amendments, effective for the first time from 1 January 2012, have had a material effect on the consolidated financial statements.

2.5 New standards and interpretations not yet adopted

A number of new standards, amendments to standards and interpretations are effective for annual periods beginning after 1 January 2012, and have not been applied in preparing these consolidated financial statements. None of these are expected to have a significant effect on the consolidated financial statements of the Group, except for IFRS 9 "Financial Instruments", which becomes mandatory for the Group's 2015 consolidated financial statements and could change the classification and measurement of financial assets. The extent of the impact has not yet been determined.

3. SIGNIFICANT ACCOUNTING POLICIES

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements, and have been applied consistently by Group's entities.

3.1 Basis of consolidation

The consolidated financial statements comprise the Bank and its principal operating subsidiaries (collectively "the Group"), Boubyan Takaful Insurance Company K.S.C. and Boubyan Capital Investment Company K.S.C., which are controlled by the Bank as set out in note 14.

3.1.1 Business combinations

Business combinations are accounted for using the acquisition method as at the acquisition date, which is the date on which control is transferred to the Group. Control is the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, the Group takes into consideration potential voting rights that are currently exercisable.

The Group measures goodwill at the acquisition date as:

- The fair value of the consideration transferred; plus
- The recognised amount of any non-controlling interests in the acquiree; plus
- If the business combination is achieved in stages, the fair value of the pre-existing equity interest in the acquiree; less
- The net recognised amount of the identifiable assets acquired and liabilities assumed.

When the excess is negative, a bargain purchase gain is recognised immediately in consolidated statement of income.

Transactions costs, other than those associated with the issue of debt or equity securities, that the Group incurs in connection with a business combination are expensed as incurred.

3.1.2 Non-controlling interests

Interest in the equity of subsidiaries not attributable to the Group is reported as non-controlling interest in the consolidated statement of financial position. Non-controlling interest in the acquiree is measured at the proportionate share in the recognized amount of the acquiree's identifiable net assets. Losses are allocated to the non-controlling interest even if they exceed the non-controlling interest's share of equity in the subsidiary. Transactions with non-controlling interests are treated as transactions with equity owners of the Group. Gains or losses on disposals of non-controlling interests without loss of control are recorded in equity.

3.1.3 Subsidiaries

Subsidiaries are entities controlled by the Group. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. Where necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies in line with those used by the Bank.

3.1.4 Loss of control

On loss of control, the Group derecognises the assets and liabilities of the subsidiary, any non-controlling interests and the other components of equity related to the subsidiary. Any surplus or deficit arising on loss of control is recognised in the consolidated statement of income. If the Group retains any interest in the previous subsidiary, then such interest is measured at fair value at the date that control is lost. Subsequently it is accounted for as an equity-accounted investee or as a financial asset depending on the level of influence retained.

3.1.5 Investments in associates (equity-accounted investees)

Associates are those entities in which the Group has significant influence, but not control, over the financial and operating policies. Significant influence is presumed to exist when the Group holds between 20% and 50% of the voting right.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

3.1 Basis of consolidation (continued)

3.1.5 Investments in associates (equity-accounted investees) (continued)

Investments in associates are accounted for using the equity method and are recognised initially at cost. The cost of the investment includes transaction costs.

The Group recognises in the consolidated statement of income its share of the total recognised profit or loss of the associate from the date that influence effectively commences until the date that it effectively ceases. Distributions received from the associate reduce the carrying amount of the investments. Adjustments to the carrying amount may also be necessary for changes in Group's share in the associate arising from changes in the associate's equity and other comprehensive income. The Group's share of those changes is recognised directly in equity or in other comprehensive income as appropriate.

When the Group's share of losses exceeds its interest in an equity-accounted investee, the carrying amount of the investment, including any long-term interests that form part thereof, is reduced to zero, and the recognition of further losses is discontinued except to the extent that the Group has an obligation or has made payments on behalf of the investee.

Any excess of the cost of acquisition over the Group's share of the net fair value of the identifiable assets and liabilities of the associate at the date of acquisition is recognized as goodwill within the carrying amount of the associates.

Any excess of the Group's share of the net fair value of the identifiable assets and liabilities over the cost of acquisition, after reassessment, is recognized immediately in the consolidated statement of income.

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.

3.1.6 Transactions eliminated on consolidation

Intra-group balances and transactions, and any unrealised income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements.

3.2 Foreign currency

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).

Foreign currency transactions are recorded in the functional currency at the rate of exchange prevailing at the date of the transaction.

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

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 reporting date. Income and expense items are translated at the average exchange rates for the year. Exchange differences arising, if any, are classified as other comprehensive income and transferred to the Group's foreign currency translation reserve. Such translation differences are recognised in the consolidated statement of income in the year in which the foreign operation is disposed off.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

3.3 Revenue recognition

- Income from Murabaha, Wakala, and Leased assets is recognized on a pattern reflecting a constant periodic return on the outstanding net investment.
- 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.
- Rental income from investment properties is recognised on a straight line basis over the lease period.

3.4 Financial instruments

3.4.1 Financial assets

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 statement of income for financial assets at fair value through profit or loss and are recognized in other comprehensive income for available for sale investments. 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.

Recognition and derecognition of financial assets

Financial assets are recognised when the Group becomes party to contractual provisions of the instrument and are initially measured at fair value. Transaction costs are included only for those financial instruments that are not measured at fair value through profit or loss.

The Group derecognises a financial asset only when the contractual rights to the cash flows from the asset expire; or it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity. If the Group neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Group recognizes its retained interest in the asset and an associated liability for amounts it may have to pay. If the Group retains substantially all the risks and rewards of ownership of a transferred financial asset, the Group continues to recognize the financial asset and also recognizes a liability for the proceeds received.

Offsetting

Financial assets and liabilities are offset and the net amount presented in the statement of financial position when, and only when, the Group has a legal right to offset the amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

Income and expenses are presented on a net basis only if it is so permitted by the accounting standards, or for gains and losses arising from a group of similar transactions.

The Group classifies financial assets into the following categories: cash and cash equivalents, due from banks, Islamic financing to customers, financial assets at fair value through profit or loss, available for sale investments and other assets.

Cash and cash equivalents

Cash and cash equivalents consist of cash in hand, current account with other banks and placements with banks maturing within seven days.

Due from banks and Islamic financing to customers

Due from banks and Islamic financing to customers are financial assets with fixed or determinable payments that are not quoted in an active market.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

3.4 Financial instruments (continued)

3.4.1 Financial assets (continued)

Murabaha

Murabaha is an agreement relating 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. Murabaha is a financial asset originated by the Group and is stated at amortized cost net of provision for impairment.

Wakala

Wakala is an agreement involving Al-Muwakkil (the Principal) who wishes to appoint Al-Wakil (the Agent) to be his agent with respect to the investment of Al-Muwakkil's fund, in accordance with regulations of the Islamic Sharia'a. Wakala is a financial asset originated by the Group and is stated at amortized cost net of provision for impairment.

Leased assets - the Group as a lessor

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 are stated at amounts equal to the net investment outstanding in the leases less provision for impairment.

Renegotiated finance facilities

In the event of a default, the Group seeks to restructure facilities rather than take possession of collateral. This may involve extending the payment arrangements and the agreement of new facility conditions. When the terms and conditions of these finance facilities are renegotiated, the terms and conditions of the new contractual arrangement apply in determining whether these facilities remain past due. Management continually reviews renegotiated facilities to ensure that all criteria are met and that future payments are likely to occur. The facility continues to be subject to an individual or collective impairment assessment.

Financial assets at fair value through profit or loss

A financial asset is classified as at fair value through profit or loss if it is classified as held for trading or is designated as such on initial recognition. Financial assets are designated as at fair value through profit or loss if the Group manages such investments and makes purchase and sale decisions based on their fair value in accordance with the Group's strategy or such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise.

Attributable transaction costs are recognised in consolidated statement of income as incurred. Financial assets at fair value through profit or loss are measured at fair value and changes therein, which takes into account any dividend income, are recognised in consolidated statement of income.

Available-for-sale investment

Available-for-sale investment is non-derivative financial assets that are not classified in any of the above categories of financial assets.

Available-for-sale investment is recognised initially at fair value plus any directly attributable transaction costs.

Subsequent to initial recognition, they are measured at fair value and changes therein, other than impairment losses (see note 3.9.1) and foreign currency differences on available-for-sale debt instruments, are recognised in other comprehensive income and presented in the fair value reserve in equity. When an investment is derecognised or is determined to be impaired, the gain or loss accumulated in equity is reclassified to consolidated statement of income.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

3.4 Financial instruments (continued)

3.4.2 Financial liabilities

All financial liabilities are recognised initially on the settlement date at fair value less any directly attributable transaction costs. Subsequent to initial recognition, these financial liabilities are measured at amortised cost.

The Group derecognises a financial liability when its contractual obligations are discharged, cancelled or expire.

Financial liabilities comprise due to banks, depositors' accounts and other liabilities.

Due to banks and depositors' accounts

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 profit, bear a share of loss and are carried at cost plus profit payable.

Non-investment accounts

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

Murabaha payable

Murabaha payable is an Islamic transaction involving the Group's 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 stated at amortized cost.

3.5 Fair values

For investments traded in organized financial markets, fair value is determined by reference to stock exchange quoted market bid prices on the reporting 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 are carried at their initial cost less impairment losses, if any.

3.6 Investment properties

Investment properties are properties held either to earn rental income or for capital appreciation or for both, but not for sale in the ordinary course of business, use in the production or supply of goods or services or for administrative purposes. Investment property is measured at cost on initial recognition and subsequently at fair value with any change therein recognised in consolidated statement of income. Cost includes expenditure that is directly attributable to the acquisition of the investment property.

Fair values of investment properties are determined by appraisers having an appropriate recognised professional qualification and recent experience in the location and category of the property being valued.

Any gain or loss on disposal of an investment property (calculated as the difference between the net proceeds from disposal and the carrying amount of the item) is recognised in consolidated statement of income.

When the use of a property changes such that it is reclassified as property and equipment, its fair value at the date of reclassification becomes its cost for subsequent accounting.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

3.7 Property and equipment

Items of property and equipment are measured at cost less accumulated depreciation and accumulated impairment losses. 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.

Subsequent expenditure is capitalised only when it is probable that the future economic benefits associated with the expenditure will flow to the Group. On-going repairs and maintenance is expensed as incurred.

Items of property and equipment are depreciated on a straight-line basis in consolidated statement of income over the estimated useful lives of each component

The estimated useful lives for the current and comparative years of significant items of property and equipment are as follows:

- Furniture and leasehold improvement 5 years
- Office equipment 3 years
- Building on leasehold land 20 years

Depreciation methods, useful lives and residual values are reviewed periodically and adjusted, if appropriate.

3.8 Intangible assets

Intangible assets acquired separately, which consist of software that have finite useful lives, are reported at cost less accumulated amortization and accumulated impairment losses. Software amortization is charged on a straight-line basis over its estimated useful life of 10 years. The estimated useful life and amortization method are reviewed at the end of each annual reporting period, with the effect of any changes in estimates being accounted for on a prospective basis.

3.9 Impairment

3.9.1 Financial assets

The Group assesses at each reporting date whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred loss event) and that loss event has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. If such evidence exists, any impairment loss is recognised in the consolidated statement of income.

Financial assets measured at amortised cost

The amount of impairment loss in respect of a financial asset measured at amortised cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the asset's original effective yield. Losses are recognised in the consolidated statement of income and reflected in an allowance account against Islamic financing to customers. When an event occurring after the impairment was recognised causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through the consolidated statement of income.

In addition, in accordance with CBK instructions, a minimum general provision of 1% for the cash facilities and 0.5% for the non-cash facilities, net of certain categories of collateral, to which CBK instructions are applicable and not subject to specific provisions is made. In March 2007, CBK issued a circular amending the basis of calculating general provisions on facilities changing the rate from 2% to 1% for cash facilities and from 1% to 0.5% for non-cash facilities. The required rates were to be applied effective from 1 January 2007 on the net increase in facilities, net of certain categories of collateral, during the reporting period. The general provision in excess of the present 1% for cash facilities and 0.5% for non-cash facilities as of 31 December 2006 would be retained as a general provision until a further directive from the CBK is issued.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

3.9 Impairment (continued)

3.9.1 Financial assets (continued)

Available for sale investment

Impairment losses on available for sale investment are recognised by reclassifying the losses accumulated in the fair value reserve in equity to consolidated statement of income. The cumulative loss that is reclassified from equity to consolidated statement of income is the difference between the acquisition cost, net of any principal repayment and amortisation, and the current fair value, less any impairment loss recognised previously in consolidated statement of income. If, in a subsequent period, the fair value of an impaired available-for-sale debt security increases and the increase can be related objectively to an event occurring after the impairment loss was recognised, then the impairment loss is reversed, with the amount of the reversal recognised in consolidated statement of income. However, any subsequent recovery in the fair value of an impaired available-for-sale equity security is recognised in other comprehensive income.

3.9.2 Non-financial assets

At each reporting date, the Group reviews the carrying amounts of its non-financial 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.

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 rates 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 consolidated statement of income, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

For non-financial assets excluding goodwill, an assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. Where an impairment loss is subsequently reversed, the carrying amount of the asset (cash-generating unit) is increased to the revised estimate of its recoverable amount and is limited to 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 statement of income, 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.

3.10 Provisions

A provision is recognised if, as a result of a past event, the Group has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are reviewed at each financial reporting date and adjusted to reflect the current best estimate of the expenditure required to settle the obligation at the financial reporting date and are discounted to present value where the effect is material.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

3.11 Contingent liabilities and contingent assets

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

Contingent assets are not recognized in the consolidated financial statements but are disclosed when an inflow of economic benefits is probable

3.12 Share based payment

The Bank operates an equity settled share based compensation plan. The fair value of the employee services received in exchange for the grant of options or shares is recognized as an expense, together with a corresponding increase in equity. The total amount to be expensed over the vesting period is determined by reference to the fair value of the options or shares on the date of grant using the Black Scholes model. At each reporting date, the Group revises its estimates of the number of options that are expected to become exercisable. It recognises the impact of the revision of original estimates, if any, in the consolidated statement of income, with a corresponding adjustment to equity.

3.13 Segment reporting

Operating segments are identified on the basis of internal reports that are regularly reviewed by the decision makers in order to allocate resources to the segments and to assess their performance. Such operating segments are classified as either business segments or geographical segments.

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

A geographic segment is a distinguishable component of the Group that is engaged in providing products or services within a particular economic environment which is subject to risks and returns different from those of segments operating in other economic environments.

3.14 Treasury shares

Treasury shares consist of the Bank's own shares that have been issued, subsequently reacquired by the Bank and not yet reissued or cancelled. The treasury shares are accounted for using the cost method.Under the cost method, the weighted average cost of the shares reacquired is charged to a contra equity account. When the treasury shares are reissued, gains are credited to a separate account in equity (treasury shares reserve) which is not distributable. Any realised losses are charged to the same account to the extent of the credit balance on that account. Any excess losses are charged to retained earnings then reserves. Gains realised subsequently on the sale of treasury shares are first used to offset any previously recorded losses in the order of reserves, retained earnings and the gain on sale of treasury shares account.

No cash dividends are paid on these shares. The issue of bonus shares increases the number of treasury shares proportionately and reduces the average cost per share without affecting the total cost of treasury shares.

4. CRITICAL ACCOUNTING JUDGMENTS AND KEY SOURCES OF ESTIMATION

4.1 Critical judgments in applying the Group's accounting policies

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

Classification of investments

Management decides on acquisition of an investment whether to classify it as held to maturity, available for sale or financial asset at fair value through profit or loss.

In designating financial assets at fair value through profit or loss, the Group determines if it meets one of the criteria for this designation set out in the significant accounting policies (note 3).

4. CRITICAL ACCOUNTING JUDGMENTS AND KEY SOURCES OF ESTIMATION (CONTINUED)

4.1 Critical judgments in applying the Group's accounting policies (continued)

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.

Fair value hierarchy

As disclosed in note 29, the Group is required to determine and disclose the level in the fair value hierarchy into which the fair value measurements are categorized in their entirety, segregating fair value measurements in accordance with the levels defined in IFRS. Differentiating between Level 2 and Level 3 fair value measurements, i.e., assessing whether inputs are observable and whether the unobservable inputs are significant, may require judgement and a careful analysis of the inputs used to measure fair value, including consideration of factors specific to the asset or liability.

4.2 Key sources of estimation uncertainly

The key assumptions concerning the future and other key sources of estimation uncertainty at the reporting 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 irregular finance facilities on a quarterly basis to assess whether a provision for impairment should be recorded in the consolidated statement of income. 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.

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 has substantially the same characteristics; or
- Other valuation models.

The determination of the cash flows and discount factors for unquoted equity investments requires significant estimation.

5. NET INVESTMENT LOSS

	2012	2011
	KD'000	KD'000
Unrealized profit on interest retained subsequent to loss of significant influence (note 15)	**18,087**	-
Realized profit from partial disposal of associate (note 15)	**5,703**	-
Sukuk coupon income	**1,687**	1,571
Dividend income	**872**	906
Net rental income from investment properties	**195**	104
Unrealized loss from financial assets at fair value through profit or loss	**(14,234)**	(1,202)
Loss on sale of investment properties	**(7,433)**	-
Unrealized loss from changes in fair value of investment properties	**(5,026)**	(5,402)
(Loss)/gain on sale of financial assets at fair value through profit or loss	**(276)**	133
(Loss)/gain on sale of available for sale investment	**(97)**	1,595
	(522)	(2,295)

6. NET FEES AND COMMISSION INCOME

	2012	2011
	KD'000	KD'000
Gross fees and commission income	**4,825**	4,873
Fees and commission expenses	**(1,146)**	(882)
	3,679	3,991

7. PROVISION FOR IMPAIRMENT

	2012	2011
	KD'000	KD'000
Provision for impairment of finance facilities	**16,175**	6,494
Provision for impairment of available for sale investment	**3,976**	3,224
Provision for impairment of other assets	**281**	2,508
	20,432	12,226

The analysis of provision for impairment of finance facilities based on specific and general provision is as follows:

	Specific	General	Total
	KD'000	KD'000	KD'000
Balance at 1 January 2011	1,711	23,497	25,208
(Released) / provided during the year	(3,377)	9,871	6,494
Recovery of written off balances	4,535	-	4,535
Written off balances during the year	(196)	-	(196)
Balance at 31 December 2011	2,673	33,368	36,041
Provided/(released) during the year	**20,858**	**(4,683)**	**16,175**
Recovery of written off balances	**240**	**-**	**240**
Written off balances during the year	**(19,532)**	**-**	**(19,532)**
Foreign currency movement	**22**	**-**	**22**
Balance at 31 December 2012	**4,261**	**28,685**	**32,946**

Further analysis of provision for impairment of finance facilities by category is as follows:

	Due from banks	Islamic finance to customers	Non-cash facilities	Total
	KD'000	KD'000	KD'000	KD'000
Balance at 1 January 2011	-	24,194	1,014	25,208
(Released)/ provided during the year	(4,350)	10,620	224	6,494
Recovery of written off balances	4,350	185	-	4,535
Written off balances during the year	-	(196)	-	(196)
Balance at 31 December 2011	-	34,803	1,238	36,041
Provided during the year	**5,616**	**10,402**	**157**	**16,175**
Recovery of written off balances	**-**	**240**	**-**	**240**
Written off balances during the year	**(5,638)**	**(13,894)**	**-**	**(19,532)**
Foreign currency movement	**22**	**-**	**-**	**22**
Balance at 31 December 2012	**-**	**31,551**	**1,395**	**32,946**

At 31 December 2012, non-performing finance facilities amounted to **KD 20,566 thousand**, net of provision of **KD 4,261 thousand** (31 December 2011: 5,476 thousand net of provision of KD 2,673 thousand). The analysis of specific and general provision stated above is based on CBK instructions.

8. BASIC AND DILUTED EARNING PER SHARE

Basic earnings per share are calculated by dividing the profit for the year by the weighted average number of shares outstanding during the year.

Diluted earnings per share is calculated by dividing the profit for the year by the weighted average number of shares outstanding during the year plus the weighted average number of share that would be issued on the conversion of all the dilutive potential shares into shares. The diluted earnings per share arising from the issue of employee share option does not result in any change from the reported basic earnings per share.

	2012	2011
Net profit for the year attributable to the equity holders of the Bank (KD'000)	**10,050**	8,025
Weighted average number of shares outstanding during the year (thousands of shares)	**1,746,520**	1,747,228
Basic and diluted earnings per share attributable to the equity holders of the Bank (fils)	**5.75**	4.59

9. CASH AND CASH EQUIVALENTS

	2012	2011
	KD'000	KD'000
Cash on hand	**14,020**	9,225
Balances with CBK – current account	**840**	177
Balances with banks – current accounts	**3,675**	11,477
Placement with banks maturing within seven days	**150,995**	171,078
	169,530	191,957

The fair values of cash and cash equivalents do not differ from their respective carrying values.

10. DUE FROM BANKS

The geographical distribution of balances due from banks is as follows:

	2012	2011
	KD'000	KD'000
Kuwait & Middle East	**240,911**	126,443
Europe	**11,090**	1,800
Less: deferred profit	**(376)**	(182)
	251,625	128,061

11. ISLAMIC FINANCING TO CUSTOMERS

The geographical distribution of Islamic financing to customers is as follows:

	Kuwait & Middle East	Europe	Asia	**Total**
	KD'000	KD'000	KD'000	**KD'000**
2012				
Corporate banking	**889,242**	**4,125**	**3,520**	**896,887**
Consumer banking	**540,791**	**-**	**-**	**540,791**
Less: deferred profit	**(136,052)**	**(61)**	**-**	**(136,113)**
	1,293,981	**4,064**	**3,520**	**1,301,565**
Less: provision for impairment	**(31,475)**	**(41)**	**(35)**	**(31,551)**
	1,262,506	**4,023**	**3,485**	**1,270,014**
2011				
Corporate banking	821,349	4,476	3,802	829,627
Consumer banking	325,670	-	-	325,670
Less: deferred profit	(90,118)	(292)	-	(90,410)
	1,056,901	4,184	3,802	1,064,887
Less: provision for impairment	(34,723)	(42)	(38)	(34,803)
	1,022,178	4,142	3,764	1,030,084

11. ISLAMIC FINANCING TO CUSTOMERS (CONTINUED)

Provision for impairment of Islamic financing to customers is calculated and analysed based on CBK instructions on the outstanding balance net of deferred profits (if any) as follows:

	Specific		General		Total	
	2012	2011	**2012**	2011	**2012**	2011
	KD'000	**KD'000**	**KD'000**	**KD'000**	**KD'000**	**KD'000**
Balance at beginning of the year	**2,673**	1,711	**32,130**	22,483	**34,803**	24,194
Provided/(release) during the year	**15,242**	973	**(4,840)**	9,647	**10,402**	10,620
Recovery of written off balances	**240**	185	**-**	-	**240**	185
Written off balances	**(13,894)**	(196)	**-**	-	**(13,894)**	(196)
Balance at end of the year	**4,261**	2,673	**27,290**	32,130	**31,551**	34,803

Further analysis of specific provision based on class of financial assets is given below:

	Corporate banking		Consumer banking		Total	
	2012	2011	**2012**	2011	**2012**	2011
	KD'000	**KD'000**	**KD'000**	**KD'000**	**KD'000**	**KD'000**
Balance at beginning of the year	**349**	266	**2,324**	1,445	**2,673**	1,711
Provided/(released) during the year	**15,766**	89	**(524)**	884	**15,242**	973
Recovery of written off balances	**240**	185	**-**	-	**240**	185
Written off balances	**(13,894)**	(191)	**-**	(5)	**(13,894)**	(196)
Balance at end of the year	**2,461**	349	**1,800**	2,324	**4,261**	2,673

Whenever necessary, Islamic financing to customers is secured by acceptable forms of collateral to mitigate the related credit risks.

Non performing Islamic financing to customers and related specific provisions are as follows:

	2012	2011
	KD'000	**KD'000**
Islamic financing to customers	**24,827**	8,149
Specific provision for impairment	**(4,261)**	(2,673)
	20,566	5,476

At 31 December 2012 management estimates the fair value of collaterals held against individually impaired Islamic finance facilities to **KD 17,594 thousand** (31 December 2011: KD 6,025 thousand).

12. FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

	2012	2011
	KD'000	KD'000
Investment in unquoted securities	**32,781**	30,461
Investment in quoted securities	**1,181**	3,849
Investment in unquoted funds	**17,331**	30,887
	51,293	65,197

13. AVAILABLE FOR SALE INVESTMENTS

	2012	2011
	KD'000	KD'000
Investment in Sukuk	**33,685**	35,164
Investment in unquoted funds	**17,711**	17,690
Investment in unquoted securities	**44,968**	10,640
Investment in quoted securities	**3,565**	2,633
	99,929	66,127

14. SUBSIDIARIES

Principal operating subsidiaries are as follows:

Name of subsidiary	Country of incorporation	**2012 proportion of ownership interest and voting power %**	2011 proportion of ownership interest and voting power %	Principal activity
Boubyan Takaful Insurance Company KSC (Closed)	Kuwait	**67.63**	57.63	Takaful insurance
Boubyan Capital Investment Company KSC (Closed)	Kuwait	**100.00**	100.00	Islamic investments

15. INVESTMENTS IN ASSOCIATES

Name of associate	Country of incorporation	**2012 proportion of ownership interest and voting power %**	2011 proportion of ownership interest and voting power %	Principal activity
United Capital Bank	Republic of Sudan	**21.67**	21.67	Islamic commercial banking
Bank Syariah Muamalat Indonesia Tbk	Indonesia	**-**	25.03	Islamic commercial banking
Ijarah Indonesia Finance Company	Indonesia	**33.33**	33.33	Islamic financing services
Saudi Projects Holding Group	Kuwait	**20.00**	20.00	Real Estate

In the prior year, the Group held a 25.03% interest in Bank Syariah Muamalat Indonesia Tbk and accounted for the investment as an associate. On 25 April 2012, the Group disposed off a 6% interest in Bank Syariah Muamalat Indonesia Tbk for a sale of consideration of **KD 9,638 thousand**. The Group has retained the remaining 19.03% interest as an available for sale investment whose fair value at the date of disposal was **KD 30,568 thousand**. This transaction has resulted in the recognition of a gain in the consolidated statement of income, calculated as follows.

	KD'000
Proceeds from the interest disposed off	9,638
Fair value of investment retained (19.03%)	30,568
Amount reclassified from other comprehensive income	(476)
Carrying amount of investment on the date of loss of significant influence	(15,940)
Gain recognized	23,790

The gain recognised in the current period comprises a realised profit of **KD 5,703 thousand** (being the proceeds of **KD 9,638 thousand** less carrying amount of the interest disposed of **KD 3,935 thousand**) and an unrealised profit of **KD 18,087 thousand** (being the fair value less the carrying amount of the 19.03% interest retained).

The movement in the investments in associates' balances is as follows:

	2012 KD'000	2011 KD'000
Balance at the beginning of the year	**26,449**	21,080
Transfer to available for sale investment	**(12,481)**	-
Partial (disposal)/acquisition of associates	**(3,935)**	2,570
Share of results of associates	**2,364**	3,611
Dividends received	**(290)**	(337)
Fair value reserve of associates	**(508)**	445
Foreign currency translation adjustments	**(2,517)**	(920)
	9,082	26,449

15. INVESTMENTS IN ASSOCIATES (CONTINUED)

Summarized financial information in respect of the Group's associates is set out below:

	2012	2011
	KD'000	KD'000
Total assets	**127,870**	973,588
Total liabilities	**(90,436)**	(866,583)
Net assets	**37,434**	107,005
Group's share of net assets	**9,082**	26,449
Group's share of contingent liabilities	**16,078**	14,107

	2012	2011
	KD'000	KD'000
Total revenue	**11,831**	72,906
Net profit	**1,744**	11,540
Group's share of results	**2,364**	3,611

There were no published price quotations for any associates of the Group.

16. INVESTMENT PROPERTIES

The movement in the investment properties is as follows:

	2012	2011
	KD'000	KD'000
Balance at the beginning of the year	**25,613**	30,788
Additions during the year	**3,961**	700
Disposals during the year	**(7,390)**	-
Net unrealized loss from change in fair value of investment properties	**(5,026)**	(5,402)
Foreign currency translation adjustments	**746**	(473)
Balance at the ending of the year	**17,904**	25,613

17. OTHER ASSETS

	2012	2011
	KD'000	KD'000
Accrued income	**887**	1,001
Prepayments	**3,092**	1,707
Software	**1,837**	1,655
Trading properties	**-**	279
Others	**2,100**	2,794
	7,916	7,436

18. OTHER LIABILITIES

	2012	2011
	KD'000	KD'000
Creditors and accruals	**5,146**	4,591
Accrued staff benefits	**5,147**	4,530
Clearing accounts	**7,974**	6,478
General provision on non-cash facilities	**1,395**	1,238
Margin accounts	**2,421**	1,025
Others	**2,314**	658
	24,397	18,520

19. SHARE CAPITAL

	2012		2011	
	Shares	**KD'000**	Shares	KD'000
Shares issued and fully paid of 100 fils each	**1,748,235,315**	**174,824**	1,748,235,315	174,824

20. SHARE PREMIUM

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

21. PROPOSED DIVIDEND

The board of directors recommended distribution of bonus share of 5% on outstanding shares as at 31 December 2012 (2011: Nil). The proposed dividends, if approved by the shareholders' general assembly shall be payable to the shareholders registered in the bank's records as of the date of the general assembly meeting.

22. TREASURY SHARES

The bank held the following treasury shares as at 31 December:

	2012	2011
Number of treasury shares	**1,715,000**	1,715,000
Treasury shares as a percentage of total issued shares - %	**0.0981%**	0.0981%
Cost of treasury shares – KD thousand	**1,024**	1,024
Market value of treasury shares – KD thousand	**1,098**	1,012

23. STATUTORY RESERVE

As required by the Commercial Companies Law and the Bank's Articles of Association 10% of profit for the year attributable to the shareholders of the Bank before KFAS, NLST, Zakat and Board of directors' remuneration 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.

24. VOLUNTARY RESERVE

As required by the Bank's Articles of Association 10% of profit for the year attributable to the shareholders of the Bank 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.

25. SHARED BASED PAYMENT RESERVE

The Bank operates an equity settled share based compensation plan and granted share options to its senior executives. These options will vest if the employees remain in service for a period of three years from the grant date and the employees can exercise the options within one year from the vesting date. If the exercise price is not paid within one year from date of vesting, the options vested will be cancelled. The exercise price of the granted options is equal to 100 fils per share.

The fair value of options granted during the year as determined using the Black-Scholes valuation model was **497 fils** (2011:538 fils). The significant inputs into the model were a share price of **590 fils** (2011:630 fils) at the grant date, an exercise price of 100 fils as shown above, a standard deviation of expected share price returns of **42%** (2011:47%), option life disclosed above and annual risk free rate of 2.5%. The volatility measured at the standard deviation of expected share price returns is based on statistical analysis of daily share prices over the last three years.

The following table shows the movement in number of share options during the year:

	2012 Number of share options	2011 Number of share options
Outstanding at 1 January	**1,409,630**	-
Granted during the year	**810,280**	1,409,630
Cancelled during the year	**(319,694)**	-
Outstanding at 31 December	**1,900,216**	1,409,630

The expense accrued on account of share based compensation plans for the year amounts to **KD 284 thousand** (31 December 2011: KD 253 thousand) and is included under staff cost.

26. RELATED PARTY TRANSACTIONS

As of 31 July 2012 the majority of the Bank's shares were acquired by the National Bank of Kuwait S.A.K.As a result, the ultimate controlling party of the Group is the National Bank of Kuwait S.A.K ("the Parent Company").

Related parties comprise the major shareholders, board of directors, entities controlled by them or under their joint control, associates, key management personnel and their close family members and the parent company including their board members, key management personnel, branches, associates and subsidiaries. Balances with related parties arise from commercial transactions in the normal course of business on an arm's length basis and are included within the following financial information captions:

	Number of board member or executive officers		Number of related parties			
	2012	2011	**2012**	2011	**2012**	2011
					KD'000	KD'000
Islamic financing to customers	**6**	8	**2**	2	**8,956**	13,653
Depositors' accounts	**12**	11	**7**	7	**33,711**	14,584
Letters of guarantee and letters of credit	**1**	-	**-**	3	**62**	460
Revenues					**194**	510
Expenses					**(335)**	(123)
Proceed from disposal of an Investment					**9,638**	-
Parent Company						
Due from banks					**80,028**	23,003
Due to banks					**53,254**	25,215
Revenues					**98**	396
Expenses					**(145)**	(277)

The Group holds collaterals against Islamic finance facilities to related parties in the form of shares and real estate. An estimate of the fair value of collaterals held against Islamic finance facilities to related parties amounted to **KD 1,236 thousand** as at 31 December 2012 (31 December 2011: KD 44,170 thousand).

Compensation of key management personnel:

Details of compensation for key management comprise the following:

	2012	2011
	KD'000	KD'000
Short-term benefits	**1,716**	1,692
Post-employment benefits	**257**	185
Share based compensation	**167**	98
	2,140	1,975

Senior executive officers also participate in the Group's share based payment programme (see note 25)

27. CONTINGENCIES AND COMMITMENTS

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

	2012	2011
	KD'000	KD'000
Guarantees	**137,909**	111,142
Acceptances and letters of credit	**47,749**	39,592
Capital commitments (projects under construction)	**1,307**	856
Credit commitments	**8,437**	20,158
	195,402	171,748

28. SEGMENT REPORTING

Operating segments are identified on the basis of internal reports that are regularly reviewed by the decision makers in order to allocate resources to the segments and to assess their performance. The operating segments are divided as either business segments or geographical segments.

Business Segments

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

Consumer banking: Provides a diversified range of products and services to individuals and institutional clients. The range includes consumer finance, credit cards, deposits and other branch related services.

Corporate banking: Provides Murabaha, Ijarah, trade service and other related services to business and corporate customers.

Investment banking: Principally handling direct investments, local and international real estate investment and asset management.

Treasury: Principally handling local and international Murabaha and other Islamic financing, primarily with banks, as well as the management of the Bank's funding operations.

Group centre: Includes other group activities and residual in respect of transfer pricing and inter segment allocation.

2012	Consumer banking KD'000	Corporate banking KD'000	Investment banking KD'000	Treasury KD'000	Group centre KD'000	**Total KD'000**
Murabaha and other Islamic financing income	**20,388**	**42,337**	**-**	**1,842**	**103**	**64,670**
Distribution to depositors & murabaha cost	**(3,526)**	**(517)**	**(144)**	**(8,250)**	**238**	**(12,199)**
Net financing income	**16,862**	**41,820**	**(144)**	**(6,408)**	**341**	**52,471**
Net investment (loss)/income	**(1)**	**1,687**	**(2,208)**	**-**	**-**	**(522)**
Net fees and commission income	**847**	**2,422**	**2,543**	**-**	**(2,133)**	**3,679**
Share of results of associates	**-**	**-**	**2,364**	**-**	**-**	**2,364**
Net foreign exchange gain	**-**	**-**	**-**	**886**	**-**	**886**
Other income	**-**	**-**	**95**	**-**	**(94)**	**1**
Segment revenues	**17,708**	**45,929**	**2,650**	**(5,522)**	**(1,886)**	**58,879**
Segment expenses	**(7,041)**	**(34,223)**	**(11,799)**	**14,180**	**(10,460)**	**(49,343)**
Segment results	**10,667**	**11,706**	**(9,149)**	**8,658**	**(12,346)**	**9,536**

2012	Consumer banking KD'000	Corporate banking KD'000	Investment banking KD'000	Treasury KD'000	Group centre KD'000	**Total KD'000**
Assets						
Cash and cash equivalents	**11,520**	**-**	**1,530**	**154,603**	**1,877**	**169,530**
Due from banks	**-**	**3,761**	**6,014**	**247,864**	**(6,014)**	**251,625**
Islamic financing to customers	**407,396**	**879,900**	**-**	**-**	**(17,282)**	**1,270,014**
Financial assets at fair value through profit or loss	**-**	**-**	**51,293**	**-**	**-**	**51,293**
Available for sale investments	**-**	**34,187**	**65,742**	**-**	**-**	**99,929**
Investments in associates	**-**	**-**	**9,082**	**-**	**-**	**9,082**
Investment properties	**-**	**-**	**17,904**	**-**	**-**	**17,904**
Other assets	**-**	**-**	**-**	**-**	**7,916**	**7,916**
Property and equipment	**-**	**-**	**-**	**-**	**7,363**	**7,363**
Total assets	**418,916**	**917,848**	**151,565**	**402,467**	**(6,140)**	**1,884,656**
Liabilities and Equity						
Due to banks	**-**	**-**	**4,264**	**207,133**	**(4,264)**	**207,133**
Depositors' accounts	**543,912**	**156,591**	**-**	**703,920**	**(7,461)**	**1,396,962**
Other liabilities	**-**	**-**	**-**	**-**	**24,397**	**24,397**
Equity	**-**	**-**	**-**	**-**	**256,164**	**256,164**
Total liabilities and equity	**543,912**	**156,591**	**4,264**	**911,053**	**268,836**	**1,884,656**

28. SEGMENT REPORTING (CONTINUED)

2011	Consumer banking KD'000	Corporate banking KD'000	Investment banking KD'000	Treasury KD'000	Group centre KD'000	Total KD'000
Murabaha and other Islamic financing income	11,417	39,838	-	1,757	(85)	52,927
Distribution to depositors & murabaha cost	(3,383)	(436)	(342)	(9,567)	410	(13,318)
Net financing income	8,034	39,402	(342)	(7,810)	325	39,609
Net investment income/(loss)	38	1,571	(3,904)	-	-	(2,295)
Net fees and commission income	1,013	2,482	1,905	(28)	(1,381)	3,991
Share of results of associates	-	-	3,611	-	-	3,611
Net foreign exchange gain	-	-	-	858	-	858
Other income	35	-	69	-	61	165
Segment revenues	9,120	43,455	1,339	(6,980)	(995)	45,939
Segment expenses	(4,548)	(20,748)	(12,542)	13,598	(13,758)	(37,998)
Segment results	4,572	22,707	(11,203)	6,618	(14,753)	7,941

2011	Consumer banking KD'000	Corporate banking KD'000	Investment banking KD'000	Treasury KD'000	Group centre KD'000	Total KD'000
Assets						
Cash and cash equivalents	6,644	-	7,884	182,726	(5,297)	191,957
Due from banks	-	6,525	5,131	121,536	(5,131)	128,061
Islamic financing to customers	242,151	813,125	-	-	(25,192)	1,030,084
Financial assets at fair value through profit or loss	-	-	65,197	-	-	65,197
Available for sale investments	-	35,841	30,286	-	-	66,127
Investments in associates	-	-	26,449	-	-	26,449
Investment properties	-	-	25,613	-	-	25,613
Other assets	-	-	-	-	7,436	7,436
Property and equipment	-	-	-	-	6,179	6,179
Total assets	248,795	855,491	160,560	304,262	(22,005)	1,547,103
Liabilities and Equity						
Due to banks	-	-	4,105	78,987	(4,105)	78,987
Depositors' accounts	453,546	118,381	-	638,380	(7,879)	1,202,428
Other liabilities	-	-	-	-	18,520	18,520
Equity	-	-	-	-	247,168	247,168
Total liabilities and equity	453,546	118,381	4,105	717,367	253,704	1,547,103

Geographical segment

In presenting information on the basis of geographical areas, revenue is based on the geographical location of customers and assets are based on the geographical location of assets.

2012	Middle East & North Africa KD'000	North America KD'000	Europe KD'000	Asia KD'000	Other KD'000	**Total KD'000**
Assets	**1,775,037**	**476**	**69,582**	**35,198**	**4,363**	**1,884,656**
Non-current assets (excluding financial instruments)	**21,598**	**-**	**11,585**	**-**	**-**	**33,183**
Liabilities and equity	**1,875,899**	**2,558**	**4,557**	**-**	**1,642**	**1,884,656**
Segment income/(expenses)	**43,874**	**(816)**	**(8,913)**	**25,071**	**(337)**	**58,879**

2011	Middle East & North Africa KD'000	North America KD'000	Europe KD'000	Asia KD'000	Other KD'000	Total KD'000
Assets	1,446,680	2,950	73,297	21,171	3,005	1,547,103
Non-current assets (excluding financial instruments)	9,738	657	22,436	616	-	33,447
Liabilities and equity	1,538,712	-	8,254	6	131	1,547,103
Segment income/(expenses)	48,509	(1,283)	(3,694)	2,253	154	45,939

29. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

29.1 Introduction and overview

Risk is inherent in the Group's activities but is managed in a structured, systematic manner through a Group risk policy that embeds comprehensive risk management into organisational structure, risk measurement and monitoring processes. The overall risk management direction and oversight is provided by the Board of Directors and Board Risk Committee with the support of the Management Executive Committee and the Group's Risk Management functions.

The Group is exposed to credit risk, market risk, liquidity risk and operational risk.

In accordance with the Central Bank of Kuwait's directives, the Group has implemented a comprehensive system for the measurement and management of risk. This methodology helps in reflecting both the expected loss likely to arise in normal circumstances and unexpected losses, which are an estimate of the ultimate actual loss based on statistical models. Information compiled from all internal business groups are closely examined and analysed to identify, manage and control risks.

Transactions and outstanding risk exposures are quantified and compared against authorised limits, whereas non- quantifiable risks are monitored against policy guidelines and key risk and control indicators. Any discrepancies, excesses or deviations are escalated to management for appropriate action.

As part of its overall risk management, the Group uses financial instruments to manage exposures resulting from changes in foreign exchange and equity risks. Collateral is used to reduce the Group's credit risk.

The Group's comprehensive risk management framework has specific guidelines that focus on maintaining a diversified portfolio to avoid excessive concentration of risks.

29.2 Credit risk

Credit risk is the risk that counterparty will cause a financial loss to the Group by failing to discharge an obligation. Credit risk arises in the Group's normal course of business.

All policies relating to credit are reviewed and approved by the Board of Directors.

Credit limits are established for all customers after a careful assessment of their creditworthiness. Standing procedures, outlined in the Group's Credit Policy Manual, require that all credit proposals be subjected to detailed screening by the respective credit risk functions. Whenever necessary, Islamic facilities are secured by acceptable forms of collateral to mitigate the related credit risks.

In accordance with the instructions of the Central Bank of Kuwait, setting out the rules and regulations regarding the classification of credit facilities, the Group has formed an internal committee comprising competent professional staff and having as its purpose the study and evaluation of the existing credit facilities of each customer of the Group. This committee, which meets regularly throughout the year, is required to identify any abnormal situations and difficulties associated with a customer's position which might cause the debt to be classified as irregular, and to determine an appropriate provisioning level.

The Group further limits risk through diversification of its assets by industry sector. In addition, all credit facilities are continually monitored based on a periodical review of the credit performance and account rating.

29.2.1 Maximum exposure to credit risk

An analysis of Islamic financing to customers and contingent liabilities before and after taking account of collateral held or other credit enhancements is as follows:

	2012		2011	
	Gross exposure	**Net exposure**	Gross exposure	Net exposure
	KD'000	KD'000	KD'000	KD'000
Islamic financing to customers	**1,270,014**	**839,241**	1,030,084	710,623
Contingent liabilities	**195,402**	**169,415**	171,748	158,343

29. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (CONTINUED)

29.2 Credit risk (continued)

29.2.1 Maximum exposure to credit risk (continued)

Collateral and other credit enhancements

The amount, type and valuation of collateral are based on guidelines specified in the risk management framework. The main types of collateral accepted includes real estate, shares, cash collateral and bank guarantees. The revaluation and custody of collaterals are performed independent of the business units. The Group may also obtain guarantees from parent companies for financing provided to their subsidiaries.

29.2.2 Risk Concentration of the maximum exposure to credit risk

Concentrations of credit risk arise from exposure to customers having similar characteristics in terms of the geographic location in which they operate or the industry sector in which they are engaged, such that their ability to discharge contractual obligations may be similarly affected by changes in political, economic or other conditions.

Credit risk can also arise due to a significant concentration of Group's assets to any single counterparty. This risk is managed by diversification of the portfolio. The 20 largest facilities outstanding as a percentage of gross facilities as at 31 December 2012 are **27.3%** (2011: 31.1%).

The Group's financial assets and off-balance sheet items, before taking into account any collateral held or credit enhancements can be analysed by the following geographic regions:

	Middle East & North Africa	North America	Europe	Asia	Other	**Total**
2012	KD'000	KD'000	KD'000	KD'000	KD'000	**KD'000**
Cash and cash equivalents (excluding cash on hand)	**146,601**	**476**	**8,286**	**143**	**4**	**155,510**
Due from banks	**240,562**	**-**	**11,063**	**-**	**-**	**251,625**
Islamic financing to customers	**1,262,506**	**-**	**4,023**	**3,485**	**-**	**1,270,014**
Available for sale investments (Sukuk)	**29,319**	**-**	**4,366**	**-**	**-**	**33,685**
Other assets (excluding software)	**6,079**	**-**	**-**	**-**	**-**	**6,079**
	1,685,067	**476**	**27,738**	**3,628**	**4**	**1,716,913**
Contingent liabilities	**177,175**	**-**	**457**	**8,026**	**-**	**185,658**
Commitments	**8,153**	**-**	**-**	**-**	**1,591**	**9,744**
Total credit risk exposure	**1,870,395**	**476**	**28,195**	**11,654**	**1,595**	**1,912,315**

	Middle East & North Africa	North America	Europe	Asia	Other	Total
2011	KD'000	KD'000	KD'000	KD'000	KD'000	KD'000
Cash and cash equivalents (excluding cash on hand)	166,490	1,985	14,126	126	5	182,732
Due from banks	126,261	-	1,800	-	-	128,061
Islamic financing to customers	1,022,178	-	4,142	3,764	-	1,030,084
Available for sale investments (Sukuk)	31,010	-	4,154	-	-	35,164
Other assets (excluding software)	5,502	-	-	-	-	5,502
	1,351,441	1,985	24,222	3,890	5	1,381,543
Contingent liabilities	142,406	-	303	8,025	-	150,734
Commitments	18,950	-	1,507	557	-	21,014
Total credit risk exposure	1,512,797	1,985	26,032	12,472	5	1,553,291

29. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (CONTINUED)

29.2 Credit risk (continued)

29.2.2 Risk Concentration of the maximum exposure to credit risk (continued)

The Group's financial assets before taking into account any collateral held or credit enhancements, can be analysed by the following industry sectors:

	2012	2011
	KD'000	KD'000
Trading	**126,359**	108,009
Manufacturing	**92,370**	89,312
Banking and other financial institutions	**415,736**	373,272
Construction	**37,390**	40,121
Real Estate	**322,045**	227,142
Retail	**410,064**	245,578
Government	**176,911**	163,732
Others	**136,038**	134,377
	1,716,913	1,381,543

In managing its portfolio, the Group utilises ratings and other measures and techniques which seek to take account of relevant aspects of perceived risk. Credit exposures classified as 'High' quality are those where the ultimate risk of financial loss from the obligor's failure to discharge its obligation is assessed to be low. These include facilities to corporate entities with financial condition, risk indicators and capacity to repay which are considered to be good to excellent. Credit exposures classified as 'Standard' quality comprise all other facilities whose payment performance is fully compliant with contractual conditions and which are not impaired. The ultimate risk of possible financial loss on 'Standard' quality is assessed to be higher than that for the exposures classified within the 'High' quality range.

The table below shows the credit quality by class of asset for statement of financial position lines, based on the Group's credit rating system.

	Neither past due nor impaired		Past due or impaired	**Total**
	High	Standard		
	KD'000	KD'000	KD'000	**KD'000**
2012				
Cash and cash equivalents (excluding cash on hand)	**155,510**	**-**	**-**	**155,510**
Due from banks	**246,523**	**5,102**	**-**	**251,625**
Islamic financing to customers	**1,072,837**	**189,027**	**39,701**	**1,301,565**
Available for sale investments (Sukuk)	**33,685**	**-**	**-**	**33,685**
Other assets (excluding software)	**6,079**	**-**	**-**	**6,079**
	1,514,634	**194,129**	**39,701**	**1,748,464**
2011				
Cash and cash equivalents (excluding cash on hand)	182,732	-	-	182,732
Due from banks	119,736	6,525	1,800	128,061
Islamic financing to customers	789,900	240,469	34,519	1,064,888
Available for sale investments (Sukuk)	33,298	1,866	-	35,164
Other assets (excluding software)	5,502	-	-	5,502
	1,131,168	248,860	36,319	1,416,347

29. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (CONTINUED)

29.2 Credit risk (continued)

29.2.2 Risk Concentration of the maximum exposure to credit risk (continued)

Ageing analysis of past due or impaired financial assets:

	Corporate banking		Consumer banking		**Total**	
	Past due and not impaired	Past due and impaired	Past due and not impaired	Past due and impaired	**Past due and not impaired**	**Past due and impaired**
	KD'000	KD'000	KD'000	KD'000	**KD'000**	**KD'000**
2012						
Up to 30 days	**4,643**	**-**	**5,293**	**-**	**9,936**	**-**
31 – 60 days	**2,001**	**-**	**1,916**	**-**	**3,917**	**-**
61 – 90 days	**27**	**-**	**994**	**-**	**1,021**	**-**
91 – 180 days	**-**	**-**	**-**	**804**	**-**	**804**
More than 180 days	**-**	**22,210**	**-**	**1,813**	**-**	**24,023**
	6,671	**22,210**	**8,203**	**2,617**	**14,874**	**24,827**
2011						
Up to 30 days	1,162	-	5,856	-	7,018	-
31 – 60 days	5,705	-	1,688	-	7,393	-
61 – 90 days	12,944	-	815	-	13,759	-
91 – 180 days	-	-	-	708	-	708
More than 180 days	-	6,015	-	1,426	-	7,441
	19,811	6,015	8,359	2,134	28,170	8,149

At 31 December 2012 management estimates the fair value of collaterals held against individually past due or impaired Islamic finance facilities to reasonably **KD 18,455 thousand** (31 December 2011: KD 13,458 thousand).

29.3 Market risk

Market risk is the risk that the fair value of financial instruments will fluctuate due to changes in market prices. Market risks arise from open positions in currency and equity products, all of which are exposed to general and specific market movements and changes in the level of volatility of prices such as foreign exchange rates and equity prices.

The Group is not exposed to material risk in terms of the re-pricing of its liabilities since, in accordance with Islamic Sharia'a, the Group does not provide a guaranteed contractual rate of return to its depositors.

Foreign currency risk

Foreign currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign currency exchange rates.

Foreign exchange risks are controlled through limits pre-established by the Board of Directors on currency position exposures. Assets are typically funded in the same currency as that of the business being transacted to eliminate exchange exposures. Appropriate segregation of duties exists between the treasury front and back office functions, while compliance with position limits is independently monitored on an ongoing basis by an independent middle office function.

29. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (CONTINUED)

29.3 Market risk (continued)

The table below analyses the effect on profit and equity of an assumed 5% strengthening in value of the currency rate against the Kuwaiti Dinar from levels applicable at the year end, with all other variables held constant. A negative amount in the table reflects a potential net reduction in profit or equity, whereas a positive amount reflects a net potential increase.

		2012		2011	
		Effect on profit KD'000	**Effect on equity KD'000**	Effect on profit KD'000	Effect on equity KD'000
US Dollar	+5	**(8)**	**-**	79	-
Sterling Pound	+5	**(45)**	**-**	(10)	-
Euro	+5	**-**	**-**	(53)	-
Indonesian Rupiah	+5	**1,519**	**60**	-	847
Sudanese Pound	+5	**13**	**265**	-	347
Japanese Yen	+5	**2**	**-**	4	-
Others	+5	**9**	**-**	(48)	-

A 5 percent decrease of the above currencies against the Kuwaiti Dinar would have had equal, but opposite, effect of the amounts shown above, on the basis that all other variables remain constant.

Equity price risk

Equity price risk arises from the change in fair values of equity investments. The Group manages this risk through diversification of investments in terms of geographical distribution and industry concentration.

For such investments classified as available for sale, a five percent increase in stock prices as at 31 December 2012 would have increased equity by **KD 2,427 thousand** (31 December 2011: an increase of KD 664 thousand). For such investments classified as at fair value through profit or loss, the impact on profit or loss would have been an increase of **KD 1,698 thousand** (31 December 2011: an increase of KD 1,715 thousand). An equal change in the opposite direction would have had equal, but opposite effect to the amounts shown above, on the basis that all other variables remain constant.

29.4 Liquidity risk

Liquidity risk is the risk that the Group will be unable to meet its financial liabilities when they fall due. To limit this risk, management has arranged diversified funding sources, manages assets with liquidity in mind and monitors liquidity on a daily basis.

The Group has established an Asset and Liabilities Management Committee to manage the assets and liabilities of the Group comprehensively and strategically. The committee meets regularly to determine and review policies for managing liquidity risk, as well as to set risk limits.

29. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (CONTINUED)

29.4 Liquidity risk (continued)

The table below summarises the maturity profile of Group's assets, liabilities and equity based on contractual cash flows and maturity dates. This does not necessarily take account of the effective maturities.

	Up to three months	3 to 6 months	6 to 12 months	Over 1 year	**Total**
	KD'000	KD'000	KD'000	KD'000	**KD'000**
2012					
Assets					
Cash and cash equivalents	**169,530**	**-**	**-**	**-**	**169,530**
Due from banks	**171,271**	**72,348**	**8,006**	**-**	**251,625**
Islamic financing to customers	**548,906**	**213,996**	**96,296**	**410,816**	**1,270,014**
Financial assets at fair value through profit or loss	**1,181**	**-**	**-**	**50,112**	**51,293**
Available for sale investments	**-**	**-**	**2,111**	**97,818**	**99,929**
Investments in associates	**-**	**-**	**-**	**9,082**	**9,082**
Investment properties	**-**	**-**	**-**	**17,904**	**17,904**
Other assets	**2,100**	**-**	**3,979**	**1,837**	**7,916**
Property and equipment	**-**	**-**	**-**	**7,363**	**7,363**
Total assets	**892,988**	**286,344**	**110,392**	**594,932**	**1,884,656**
Liabilities and Equity					
Due to banks	**158,594**	**7,772**	**2,117**	**38,650**	**207,133**
Depositors' accounts	**935,043**	**196,004**	**263,423**	**2,492**	**1,396,962**
Other liabilities	**10,289**	**-**	**7,568**	**6,540**	**24,397**
Equity	**-**	**-**	**-**	**256,164**	**256,164**
Total liabilities and equity	**1,103,926**	**203,776**	**273,108**	**303,846**	**1,884,656**

	Up to three months	3 to 6 months	6 to 12 months	Over 1 year	Total
	KD'000	KD'000	KD'000	KD'000	KD'000
2011					
Assets					
Cash and cash equivalents	191,957	-	-	-	191,957
Due from banks	96,658	31,403	-	-	128,061
Islamic financing to customers	494,101	213,485	65,475	257,023	1,030,084
Financial assets at fair value through profit or loss	3,849	-	-	61,348	65,197
Available for sale investments	26,085	-	4,178	35,864	66,127
Investments in associates	-	-	-	26,449	26,449
Investment properties	-	-	-	25,613	25,613
Other assets	2,793	-	2,988	1,655	7,436
Property and equipment	-	-	-	6,179	6,179
Total assets	815,443	244,888	72,641	414,131	1,547,103
Liabilities and Equity					
Due to banks	40,294	-	-	38,693	78,987
Depositors' accounts	711,966	246,627	237,503	6,332	1,202,428
Other liabilities	7,138	-	5,616	5,766	18,520
Equity	-	-	-	247,168	247,168
Total liabilities and equity	759,398	246,627	243,119	297,959	1,547,103

29. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (CONTINUED)

29.4 Liquidity risk (continued)

The liquidity profile of financial liabilities of the Group summarised below reflects the projected cash flows including future profit payments over the life of these financial liabilities based on contractual repayment arrangements.

2012	Up to three months KD'000	3 to 6 months KD'000	6 to 12 months KD'000	Over 1 year KD'000	**Total** **KD'000**
Financial Liabilities					
Due to banks	**158,636**	**7,798**	**2,135**	**40,844**	**209,413**
Depositors' accounts	**935,592**	**196,760**	**265,533**	**2,569**	**1,400,454**
	1,094,228	**204,558**	**267,668**	**43,413**	**1,609,867**
2011					
Financial Liabilities					
Due to banks	40,284	-	-	41,426	81,710
Depositors' accounts	712,568	247,951	240,074	6,536	1,207,129
	752,852	247,951	240,074	47,962	1,288,839

29.5 Operational risk

Operational risk is the risk of loss arising from inadequate or failed internal processes, systems failure, human error, or from external events. When controls fail to perform, it can lead to legal or regulatory implications, or financial /reputational loss.

The Group has established policies and procedures, which are applied to identify, assess, monitor, control and mitigate operational risk in addition to other types of risks relating to the banking and financial activities of the Group as part of overall risk management activities.

The operational risk of the Group is managed in line with the CBK instructions concerning the general guidelines for internal controls and best practice for managing and supervising operational risks in banks.

29.6 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 are approximate to their fair values at 31 December due to the relatively short-term maturity of the instruments.

Fair value hierarchy

The table below analyses financial instruments carried at fair value by valuation method. The different levels have been defined as follows:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2: inputs other than quoted prices included within level 1 that are observable, either directly (i.e. as prices) or indirectly (i.e. derived from prices);
- Level 3: inputs that are not based on observable market data (unobservable inputs).

2012	**Level 1** **KD'000**	**Level 2** **KD'000**	**Total** **KD'000**
Financial assets held for trading	**155**	**-**	**155**
Financial assets at fair value through profit or loss	**1,026**	**50,112**	**51,138**
Available for sale investments	**489**	**99,440**	**99,929**
	1,670	**149,552**	**151,222**

2011	Level 1 KD'000	Level 2 KD'000	Total KD'000
Financial assets held for trading	167	-	167
Financial assets at fair value through profit or loss	3,682	61,348	65,030
Available for sale investments	-	66,127	66,127
	3,849	127,475	131,324

29. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (CONTINUED)

29.7 Capital management

The primary objectives of the Group's capital management are to ensure that the Group complies with externally imposed capital requirements and that the Group maintains strong and healthy capital ratios in order to support its business and to maximize shareholders' value.

The Group actively manages its capital base in order to cover risks inherent in the business. The adequacy of the Group's capital is monitored using, among other measures, the rules and ratios established by the Basel Committee on Banking Supervision (BIS rules/ratios) and adopted by the Central Bank of Kuwait in supervising the Group.

During the year, the Group has complied in full with all its externally imposed capital requirements.

The Group's regulatory capital and capital adequacy ratios are shown below:

	2012	2011
	KD'000	KD'000
Tier 1 capital		
Share capital	**174,824**	174,824
Share premium	**62,896**	62,895
Proposed bonus shares	**8,741**	-
Treasury shares	**(1,024)**	(1,024)
Statutory reserve	**1,891**	842
Voluntary reserve	**1,813**	802
Share based payment reserve	**537**	253
Retained earnings	**5,424**	6,381
Non-controlling interests	**2,514**	2,923
Deductions from tier 1 capital	**(3,246)**	(13,040)
	254,370	234,856
Tier 2 capital		
Fair value and foreign currency translation reserves	**(3,334)**	(1,628)
General provision	**12,380**	10,928
Deductions from tier 2 capital	**(3,246)**	(13,040)
	5,800	(3,740)
Total regulatory capital	**260,170**	231,116
Risk-weighted assets	**1,066,494**	922,151
Capital ratios		
Total regulatory capital expressed as a percentage of total risk-weighted assets	**24.39%**	25.06%
Total tier 1 capital expressed as a percentage of risk - weighted assets	**23.85%**	25.47%

30. FINANCIAL ASSETS AND LIABILITIES

The table below sets out the Group's classification of each class of financial assets and liabilities

	Designated as at fair value KD'000	Held for trading KD'000	Loans & receivables KD'000	Available for sale KD'000	Other amortized cost KD'000	**Total carrying amount KD'000**
2012						
Cash and cash equivalents	**-**	**-**	**150,996**	**-**	**18,534**	**169,530**
Due from banks	**-**	**-**	**251,625**	**-**	**-**	**251,625**
Islamic financing to customers	**-**	**-**	**1,270,014**	**-**	**-**	**1,270,014**
Financial assets at fair value through profit or loss	**51,138**	**155**	**-**	**-**	**-**	**51,293**
Available for sale investments	**-**	**-**	**-**	**99,929**	**-**	**99,929**
	51,138	**155**	**1,672,635**	**99,929**	**18,534**	**1,842,391**
Due to banks	**-**	**-**	**-**	**-**	**207,133**	**207,133**
Depositors' accounts	**-**	**-**	**-**	**-**	**1,396,962**	**1,396,962**
	-	**-**	**-**	**-**	**1,604,095**	**1,604,095**

	Designated as at fair value KD'000	Held for trading KD'000	Loans & receivables KD'000	Available for sale KD'000	Other amortized cost KD'000	Total carrying amount KD'000
2011						
Cash and cash equivalents	-	-	171,078	-	20,879	191,957
Due from banks	-	-	128,061	-	-	128,061
Islamic financing to customers	-	-	1,030,084	-	-	1,030,084
Financial assets at fair value through profit or loss	65,030	167	-	-	-	65,197
Available for sale investments	-	-	-	66,127	-	66,127
	65,030	167	1,329,223	66,127	20,879	1,481,426
Due to banks	-	-	-	-	78,987	78,987
Depositors' accounts	-	-	-	-	1,202,428	1,202,428
	-	-	-	-	1,281,415	1,281,415

31. FIDUCIARY ASSETS

The aggregate value of assets held in a trust or fiduciary capacity by the Bank amounted to **KD 70,246 thousand** (31 December 2011: KD 59,241 thousand).

32. COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform to the current year's presentation. Such reclassifications did not affect previously reported profit or loss, equity or opening balances of the earliest comparative period presented; accordingly a third statement of financial position is not presented.