Kuwait Finance House 2005 Annual Report

Twenty Seventh Annual Report

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بيت التمويل الكويتي
Kuwait Finance House
الأمان والإطمئنان

بسم الله الرحمن الرحيم

In the Name of Allah the Most Gracious, the Most Merciful Ye who believe! Fear Allah and give up what remains of your demand for usury, if ye are indeed believers. If ye do it not, take notice of war from Allah and his Apostle, but if ye turn back, ye shall have your capital sums deal not unjustly and ye shall not be dealt unjustly.

Al Baqara (278 -279) Al-Qura'an

HH Sheikh Jaber
Al Ahmad Al Jaber
Al Sabah

The Late Amir of Kuwait

HH Sheikh Saad
Al Abdullah Al Salem
Al Sabah

The 14th Amir of Kuwait

HH Sheikh Sabah
Al Ahmad Al Jaber
Al Sabah

Amir of Kuwait

HH Sheikh Nawaf
Al Ahmad Al Jaber
Al Sabah

Crown Prince

HH Sheikh Naser
Mohammad Al Ahmad
Al Sabah

Prime Minister

Contents

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Telephone: 2445050, Facsimile: 2455135,
Cable: BAITMAL KT
www.kfh.com

Kuwait Finance House

With its strong Islamic values, is a financial institution whose aim is to develop and promote Islamic banking worldwide. Kuwait Finance House offers unique yet competitive products and services directed to target markets for both depositors and shareholders.

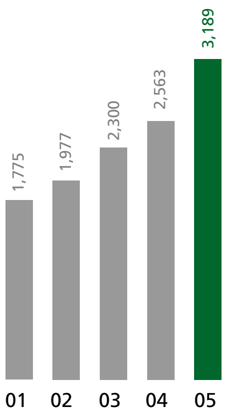
In accordance with the Islamic principles, Kuwait Finance House ensures that while working with the public professionally, the company guarantees an honourable relationship with its client base and the Islamic community as a whole.

These values are continually reinforced and adhered to in all aspects of the company's operations. Its integrity and sincerity has maintained a quality service at all times. The employees of Kuwait Finance House are constantly encouraged to be efficient, creative and above all successful. Career enhancement is actively promoted with an ever-changing financial world, creating a healthy professional environment.

Financial Highlights

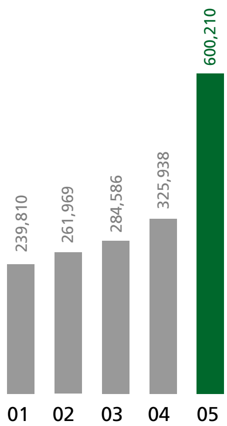
Depositors' Account Growth
(in millions of Kuwaiti Dinars)

+24.4%



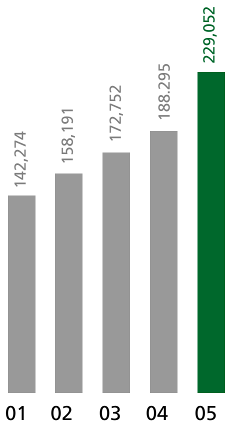
Shareholders' Funds Growth
(in thousands of Kuwaiti Dinars)

+84.1%



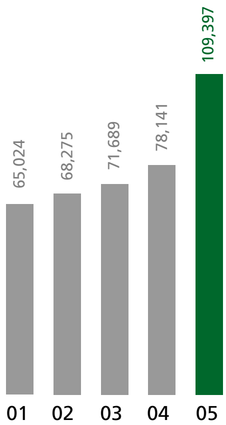
Reserves Growth
(in thousands of Kuwaiti Dinars)

+21.6%



Capital Growth
(in thousands of Kuwaiti Dinars)

+40%



Leading the way
in On-Line Banking

Board of Directors

Bader Abdul Muhsen Al-Mukhaizeem
Chairman

Sameer Yaqoub Al Nafeesi
Deputy Chairman

1. Saud Abdul Aziz Al-Babtain
   Board Member
2. Essam Saud Al-Rashed
   Board Member
3. Ali Mohammad Al-Elaimi
   Board Member
4. Dr. Mohammad A. Al-Sherif
   Board Member
5. Mohammad Ali Al-Khudairi
   Board Member
6. Meshaal Yousuf Al-Derbas
   Board Member
7. Naser Abdul Muhsen Al-Merri
   Board Member
8. Adel Abdul Muhsen Al-Subih
   Board Member

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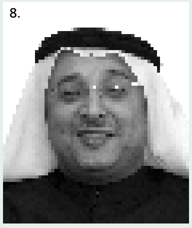

Servicing our customers better
by building closer relationships

Management

Mohammad Sulaiman Al-Omar
Deputy General Manager

1. Dr. Anwar Ahmad Al-Fuzaie
   Assistant General Manager
   Head of the Legal Department

2. Salah A. Al-Bassam
   Assistant General Manager

3. Emad A. Al-Thaqeb
   Assistant General Manager

4. Mohammad Naser Al-Fouzan
   Assistant General Manager

5. Fawaz S. Al-Othman
   Assistant General Manager

6. Dr. Waleed Essa Al-Hasawi
   Assistant General Manager

7. Abdul Aziz Al-Jaber
   Assistant General Manager

8. Anwar Mohammad Al-Bader
   Assistant General Manager

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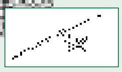
Offering our customers the
highest of standards

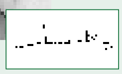
Their Eminences, Members of the Al-Fatwa and Shareea'a Supervisory Board

Report of Al-Fatwa and Shareea'a Supervisory Board

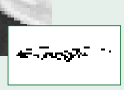
By following up the performance of Kuwait Finance House during the year ended 31 December 2005, we certify confidently that all activities were practiced in compliance with Islamic Shareea'a and no violations have occurred, to the best of our knowledge.

Sheikh Ahmad Bazie Al-Yaseen
Chairman

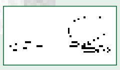



Sheikh Dr. Khalid Mathkour Al-Mathkour
Shareea'a Board member

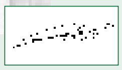



Sheikh Dr. Ajeel Jasem Al-Nashmi
Shareea'a Board member


Sheikh Dr. Mohammad Fawzi Faidullah
Shareea'a Board member

Sheikh Dr. Mohammad Abdul Razaq Al-Tabtabae
Shareea'a Board member

Sheikh Dr. Anwar Shuaib Abdulsalam
Shareea'a Board member

Delivering the highest quality products without compromising our dedication to integrity

Chairman’s Statement

A Year of Record Achievements

In the Name of Allah, the Merciful, the Compassionate.
Praise be to the Almighty God and Peace and Blessings be upon his apostle, Mohammed, his folks, companions and followers to the Day of Judgement.

Bader Abdul Muhsen Al-Mukhaizeem
Chairman

Dear Sirs,

It is my pleasure to welcome you to the 27th General Assembly Meeting. I would like to present Kuwait Finance House's (KFH) Annual Report for the year ended 31 December 2005, covering KFH's Sharia Board Report, the major achievements throughout the year, as well as the domestic, regional and global developments. The report also contains the consolidated financial statements of KFH and its subsidiaries, in addition to the Auditors' Report.

Record Achievements to Maintain KFH's Pioneering Regional Position

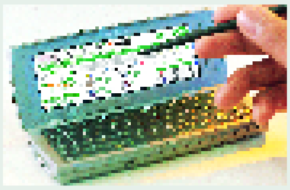
KFH continued to achieve further expansion and growth on the domestic, regional and global levels. To maintain its pioneering position as one of the world's largest Islamic banks, KFH continued to diversify its investments, fostering its achievements in quality and quantity. To do so, the Bank penetrated new markets, innovated new products and tools, and increased its financial, economic and social role, thus entering a new era of development. KFH has realized numerous achievements on all levels. These achievements reflect the sincere efforts exerted by the management team, and the loyalty of each employee, in a favorable working environment that reflects the culture of KFH and its Sharia-compliant identity. In this context, KFH represents an exemplary Islamic bank that operates within a clear strategy towards providing the customers with best services, meeting their expectations, innovating state-of-the-art products, and improving the service quality. In so doing, KFH always endeavors to upgrade the performance of its employees, maintain their stability and increase their knowledge, besides effectively communicating with the community by increasing expenditure on IT infrastructure and expanding regionally and internationally.

Highest Rating of an Islamic Bank for Excellent Management

The bold initiatives of KFH, coupled with focusing on product and service quality, as well as improvement of financial capability, had a positive impact on upgrading KFH ratings by the international rating agencies. The Bank attained high ratings, which unanimously recognize its strong assets and stability as a pioneering bank in the region. The ratings reflect the success of the development and upgrading efforts made by KFH in all its activities. The ratings also serve as a strong proof of the close link between the financial adequacy and work in accordance with the international standards, thus providing the opportunity for assessment on sound grounds. Standard and Poores rated KFH –A and A2 on the long and short terms, respectively, which are the highest ratings by a major rating agency of an Islamic bank on both regional and global levels.

KFH was awarded with the best airplane financing deal in the Middle East for 2005. The award was given by Jane's Transport Finance, an international magazine specialized in transport, for its role in financing an aviation company in Kuwait.

The Turkish government dedicated a high-level award to KFH Awqaf – Turkey, in which KFH has a stake of 65%, in appreciation of its role in Islamic financial services in the Turkish market, and its constructive contribution to fostering trade exchange between Ankara and Gulf countries. The year witnessed numerous positive reports published on KFH in the world's major economic and banking media.



Record Financial Results

Dear Sirs,

Financial results for the year ended 31 December 2005, were as follows:

Balance Sheet:

At the end of the year, assets totalled KD 4.681 billion, an increase of KD 1.223 billion over 2004, i.e. 35.3%. On the liabilities side, customers account balances amounted to KD 3.189 billion, an increase of KD 626 million, or by 24.4%, compared to the past year. Meanwhile, shareholders equity accounted for KD 600.210 million, an increase of KD 274.272 million, or by 84.1%, compared to 2004.

Revenues:

Realized revenues for the year totalled KD 383 million, an increase of KD 180 million, i.e. 88.3%. Profit before dividends, net of expenses and provisions, amounted to KD 245 million, an increase of KD 97 million, or by 65.6%, compared to 2004.

Net Profit:

Net profit for shareholders amounted to KD 119 million, an increase of KD 44 million, with a growth rate of 60%, compared to 2004.

Profit Distributions:

At their meeting held on 22 January 2006, the Board of Directors of KFH recommended a cash dividend to shareholders at the rate of 55%, and 12% bonus shares. Meanwhile, dividends were distributed to investor depositors for the financial year ended 31 December 2005, as per the following percentages:

Account Type	2005	2004
Unconditional Investment Deposits	**6.807%**	4.800%
Al-Sidra Investment Deposits	**5.294%**	3.733%
Investment Saving Accounts	**4.538%**	3.200%

Diversified Activities and Major Achievements by the Group

Domestic market occupies a prominent place on the priority list of KFH's strategy, with ever-growing market share being attained. In this framework, KFH has boosted its domestic activities, either through its main structure, or its subsidiaries, which encompass a set of local and international companies. These include Al-Inmaa Real Estate Company, Al-Muthanna Investment Company, and the Kuwaiti Manager Company. AREF Group Investment Company and Palms United Real Estate Company have recently been added to the list on the local level. Furthermore, KFH has stepped up its foreign activities, either through direct investments or through its subsidiaries, such as Kuwait Finance House Awqaf – Turkey, Kuwait Finance House – Bahrain, and Kuwait Finance House – Malaysia, in addition to several participations in affiliates, all forming Kuwait Finance House Group, which are expressed collectively in the group's consolidated financial statements. The group continues its strategy that aims at upgrading its retail and corporate banking services in the areas of commercial and real estate finance, corporate finance and foundation, direct domestic, regional and international investment, so as to direct all resources towards providing the highest levels of products and services of added value to our customers. The group's achievements will be exhibited in four themes. The first highlights the development of integrated products and services to individual and corporate customers. The second tackles activation of the domestic market. The third addresses fostering KFH's presence in the Gulf and global markets. And, the fourth displays the community service.

I: Integrated Retail and Corporate Products

Throughout 2005, KFH continued its steady methodology towards upgrading its retail and corporate banking services. It was possible to realize this goal through the great efforts exerted towards serving the customers, while providing a package of programs and products that meet the requirements of the various customer segments. The ultimate goal was to attain a progressive growth in our market share, whether in terms of the number of customers or the volume of deposits, and diversification of products, all by working into five different tracks:

The first track: Expanding the Domestic Network

KFH's policy to expand the coverage of its branch network, which provide banking, financing and real estate services all over Kuwait, so as to increase coverage, market share and to provide easy access to branches, as well as a more flexible, faster and quality service to the customers. In order to achieve this goal, the year witnessed the inauguration of 3 new branches in Salwa, Hittin, and West Mishref areas, thus increasing the network to 36 branches. Moreover, 3 other branches were relocated: Hawalli, Qadisiya, and Faihaa, at the majority of which ladies branches were dedicated, thus increasing the number of ladies

“KFH's share among the major card issuers in the local market boomed as a result of launching the Taiseer Platinum Card, the first 12 month flexible installment card, designed in accordance with the Islamic Sharia rules.”

sections to 25, besides the banking branches. In addition, 18 new ATMs were installed, increasing the total to 106. Among these, 20 units are for drive-in use, distributed into 19 branches, marking the first service of its kind in Kuwait. For the first time in Kuwait, cash and cheque deposit service was introduced.

Currently, there are 1,822 Point of Sale (POS) machines, as 77 new machines were added. KFH has recently introduced POS machines using bank cards through wireless connection to enable bank cardholders to pay via these machines, wherever they are, thus surpassing the traditional place limitations and old technical requirements for use in the open areas, such as exhibitions.

Second track: Improving the Service Quality

In line with KFH's strategy to improve the service quality, new techniques were used to measure and assess customer satisfaction vis-à-vis the services provided in the branches. A Mystery Shopping program was launched early in the year in all banking sector branches. A permanent branch incentive and competition program was also launched, and outstanding performers were honored upon appraisal of their service quality.

In this context, the US Purdue University conferred KFH with Center of Excellence certificate for ALLO BAITAK service as best call center, which was launched last year to meet its customers' requirements. Having been certified by this esteemed university, KFH excelled among Middle East call centers. The assessments by the university cover more than 28 countries around the world, in addition to assessing the world's major organizations, banks and companies.

Third track: Identifying and Targeting Customer Segments

Marking the strategy of identifying and targeting the customer segments, several measures were taken to classify customers as per the latest global techniques. The aim was to meet all banking, financing, and investment requirements, achieve integration between these services at KFH, and increase customer loyalty and satisfaction. In order to realize these goals, marketing messages, together with integrated programs, were launched to suit the requirements of each segment, bearing a set of benefits and offers. Division of customer segments at KFH was built on two basic criteria: age groups and financial position.

KFH's strategy relied on dividing the customer segments according to the age groups as follows:

Children Segment (Bara'em "or Blossoms" Club)

The idea of Bara'aem Club was initiated as more than merely a bank account. A number of fully equipped rooms were provided for children at the ladies sections in the new branches, so as to set an environment of privacy for children, being the future customers.

Youth Segment (Shabab Al-Deira)

Shabab Al-Deira (Nation's Youth) account was launched in its new version, considering the characteristics of this significant segment; i.e. the youth. The account logo depicts the colors of Kuwait's flag. The account gives way to the unlimited ambitions of the youngsters thanks to its features, which indeed make it the best account for young people in Kuwait.

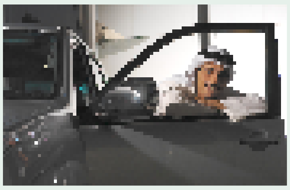
Al-Sundus and Al-Rubban Services:

According to customer segment evaluation in terms of their financial positions, a set of programs were presented to the ladies segment. Al-Sundus program was launched for ladies, and Al-Rubban program was announced for men. Al-Tamayuz segment program was designed for male and female customers with very high income. Priority segment was introduced to male and female customers with high income.

Fourth track: E-Commerce and Internet

The year was mainly characterized by the continuous growth of customer demand for direct banking services. In a parallel development, advanced techniques were adopted to train the employees, improve work environment, and reduce congestion in the branches. To this end, measures were taken to motivate customers to use KFH's remote services by focusing on the electronic channels and the call center, instead of direct service. In this context, more comprehensive banking, commercial, real estate and investment services were introduced. KFH's bi-lingual (Arabic/English) web site was entirely updated by introducing the Tamweel SMS service to communicate with customers, provide them with notes on their account and balance movements, in addition to informing them with the new services, marketing offers, and KFH's ongoing activities.

Intensive advertising, awareness and promotional campaigns were launched to encourage and guide customers to use the electronic services, with a special focus on Tamweel Online (banking service via internet) and Tamweel SMS services. Two marketing campaigns, "140 Services at your fingertips"



and "Browse and win", were introduced via electronic channels to encourage customers to use both tools. Average number of monthly transactions via Tamweel Online exceeded 300,000. KFH participated in the First Gulf Conference on E-Commerce, which was held in Abu Dhabi, to exhibit its experience, being a pioneering organization in this field. During the conference, over 140 services were introduced to customers via our web site.

Fifth track: Maintaining KFH's position as the largest Bank Card Issuer

KFH has realized an unprecedented achievement in Kuwait by launching the Islamic Sharia-compliant corporate credit card. The card was designed specifically for company employees to suit their requirements, including local or business travel expenses. The card helps companies to control expenses, while saving time and facilitating the work of their employees.

KFH's share among the major card issuers in the local market boomed as a result of launching the Taiseer Platinum Card, the first 12 month flexible installment card, designed in accordance with the Islamic Sharia rules. The card provides customers with a set of features, such as high credit line of up to three times the salary, easy repayment in convenient monthly installments, as well as combining both Visa and MasterCard. Furthermore, the cardholder is eligible to win prizes up to KD 100,000 via "Win with KFH Prizes" campaign. The distinctive card, which accounted for 20% of total KFH cards in less than a year, contributed substantially to the large increase in both numbers of issued cards and users.
In an unprecedented move, KFH used the electronic chip technology (Smart Card). It is the first Kuwaiti bank to issue all credit cards using the electronic chip. The technology is the latest in terms of securing confidentiality and safety for credit cards, as well protection against credit card forgery. Using this technology, discount offers, and personal information, such as credit card or passport number, can be stored.

II: Re-activating the Local Market:

KFH has always endeavored to intensify its expenditure in the domestic market, which exceeded KD 1 million in 2005. The spending mainly represented the purchase of miscellaneous goods from the local market, including new and used vehicles, real estate properties, construction materials and works, furniture, electrical and electronic appliances, and other goods distributed into its commercial and real estate activities. On the commercial side, its financing transactions and car sales witnessed further expansion after opening a new showroom in Ahmadi area. KFH focused on several financing tools and contributed to disseminating the concept of leasing in the Kuwaiti market, with both operating and financing elements, on both individual and corporate levels. Currently, KFH provides customers with over 20 types of vehicles for operational leasing, thus enhancing its commercial activity.

Expansive Real Estate Financing, reflecting the ongoing growth in real estate market:

The year witnessed expansion in KFH's financing of residential, investment, and commercial real estate activities in the shadow of continuous growth of real estate trading indices. KFH stepped up provision of real estate financing via its various Sharia-compliant tools. It extended consultation in the areas of valuation and real estate property. During the year, KFH issued a series of quarterly reports to the local real estate market, highlighting the major market developments, which reflected positively on increasing the customer awareness and confidence, fostering transparency, and providing accurate information on the market events. KFH is one of the major decision makers in the real estate market due to its vast expertise in this area. Contributing to solving the housing problem for Kuwaiti families, some housing land plots were offered at special prices in various locations through the exhibitions in which KFH participated during the year. Real estate services were expanded using direct channels across the branch network, or via internet and phone service. The year witnessed the launching of advertising campaigns, offering numerous features and gifts to customers.

To contribute to developing and building a number of commercial and investment complexes, several construction projects, with a value exceeding KD 100 million, are in progress, covering various areas of Kuwait, such as Al-Watiya Tower, Dasman Tower, and Al-Deira Tower.

Direct Investment: Support for National and Gulf Economies:

Continuing KFH's strategy towards supporting the national and Gulf economies, KFH established and increased the capitals of a number of subsidiaries and affiliates. The aim was to assist these companies to expand their activities and increase the business to cope with the growth in several sectors, including commercial banking, investment, leasing, real estate, IT, health care, asset management services, and other investments, in addition to

“Being one of the major Islamic banks, KFH endeavors to develop an Islamic money market, based on its expertise as market maker in the area of investing the surplus liquidity with Islamic institutions, using the latest Sharia techniques. ”

the local mega projects, and issuance of mutual funds and Islamic sukuks.

Investment in Real Estate Companies:
In order to expand strongly in the local real estate and investment sectors, KFH participated in establishing Al-Raya International Real Estate Company, with a capital of KD 20 million. The participation was marketed in the form of KFH customer portfolio. The stake accounted for 30% of the share capital. Palms United Real Estate Company's capital was increased from KD 15 million to KD 30 million.

Stakes in Investment Companies:
In the area of domestic investment, KFH participated in the establishment of Al-Farabi Investment Company, with a capital of KD 20 million. The participation was marketed in the form of KFH customer portfolio. The stake accounted for 20% of the share capital. In another development, the share capital of Al-Muthanna Investment Company was doubled, from KD 16 million to KD 32 million. KFH's share in the increase, amounting to KD 16 million, was fully paid up.

Al-Fajer Fund:
KFH marketed Al-Fajer Fund to its customers. It is a fund investing in local, Gulf and Arab stocks. It is managed by a local investment company, and has a capital of KD 21 million. KFH's share is KD 5 million.

Direct Local Investments in Aviation Sector:
Continuing its strategy towards supporting the national economy by increasing the volume of domestic investments, the share capital of ALAFCO Aircraft Purchasing and Chartering Finance Company was increased from KD 33 million to KD 50 million, with a stake of 29%, so as to meet the increasing demand for aircraft chartering. In 2005, KFH participated in financing the purchase by a local company of 3 Airbus A320 craft. Al-Jazeera Airways is the first Kuwait privately-owned airline.

III: Enhancing KFH's Presence in the Gulf and Global Markets

Durrat Al-Bahrain Sukuks:
To enhance its presence in the Gulf market, KFH played a major role in the successful issue of Durrat Al-Bahrain sukuks of USD 152.5 million. It took over the role of Manager / Underwriter of the subscription for this issue. Durrat Al-Bahrain sukuks aim at financing the infrastructural works for Phase I of Durrat Al-Bahrain investment project, of which the total cost is estimated at USD 1 billion. It is the largest residential, entertainment project ever to be developed in the Kingdom of Bahrain.

Lease Financing for Bahrain Petroleum Company (BAPCO):
KFH acted as agent, organizer and book runner for the Islamic segment of USD 330 million of the total finance of USD 1 billion, covered by traditional and Islamic financing. The finance was used to increase the production capacity in accordance with top international product development standards, to be of added value to BAPCO. The company is fully owned by the government of the Kingdom of Bahrain, and feeds the domestic and global markets with its products.

Sharjah National Bank:
Due to the growth of the UAE market, the share capital of Sharjah National Bank (SNB) was increased from AED 385.684 million to AED 1 billion, with KFH holding a stake of AED 245.7 million.

Exporting Local Activities to the World:
On the level of expanding local activities worldwide, KFH commenced its new business activity in the Hashemite Kingdom of Jordan, by introducing the service of selling new and used cars in Kuwait, with delivery in Jordan. The step took place upon its successful expansion over the past years in 6 Arab and foreign countries: Egypt, UAE, Syria, Lebanon, USA, and Germany.

In line with the international expansion policy, KFH introduced diversified real estate services in Malaysia, thus increasing the number of countries, where international real estate financing service is provided, to 8. Currently, the service covers Mecca, Medina, Bahrain, Oman, UAE, Egypt, Lebanon, Britain, and Malaysia. KFH is currently in the process of launching this type of service in Turkey.

Short-Term Murabaha Deals in Singapore:
KFH organized short-term Murabaha deals for two global companies in Singapore, with a total value of USD 170 million. The deals revealed the high demand in Singapore market for such business, and that the government is fully prepared to support the growth of Islamic financing industry in Singapore.

Continuing Development of Murabaha Product Worldwide:
KFH participated in several commercial Murabaha deals to finance the acquisition of commodities and equipment. In this context, it participated with the Islamic Development Bank (IDB) in arranging a Murabaha deal to purchase oil for the Pakistani government, at a value of USD 100 million. Murabaha deals of up to USD 80 million were concluded with a number of Gulf and international companies.

KFH: A Pioneer in Islamic Money Market:
Being one of the major Islamic banks, KFH endeavors to develop an Islamic money market, based on its expertise as market maker in the area of investing the surplus liquidity with Islamic institutions, using the latest Sharia techniques. Treasury Department's activity increased in the international investment sector and liquidity management. Such activity took place in cooperation with new Islamic financial institutions. New information systems were developed and their application commenced in a manner compatible with the management's work mechanisms.

Al-Soor Real Estate Leasing Portfolio:
On the other hand, KFH finalized the majority of the procedures for selling the Al-Soor Real Estate Leasing portfolio. In 2001, Al-Soor Fund was established to lease real estate properties, in partnership with City Group. The fund invested its USD 115 million share capital in the acquisition of 19 residential properties located in 8 states across the United States of America, for a total purchase value of USD 378 million, using lease contracts. The portfolio was sold against USD 511 million.

IV: Serving the Community:

In light of the effective communication with the community, KFH contributed to numerous developmental projects within and outside Kuwait. A drug addiction treatment hospital was opened in the presence of HH the Prime Minister. The project is a KD 4 million donation. It occupies a total area of 50,000 m2, with a built area of up to 15,000 m2. The hospital accommodates about 300 patients. It is a 4-storey building, containing 10 wards. It is equipped to receive inpatients and outpatients. The center contains a health, sports club, playgrounds, a mosque, rehabilitation and hobbies hall, and a library. On the other hand, the treatment and rehabilitation center for convicts in the central prison was delivered. The project is constructed on an area of 12,000 m2. It accommodates about 450 prisoners to receive rehabilitative treatment programs. KFH donated about KD 900,000 to Zakat House to help poor families and support the charity activities of Zakat House. Furthermore, KFH donated KD 250,000 to the victims of Pakistan earthquake. The donation was made via Zakat House. KFH had various charity contributions to several community service projects, particularly those supporting the educational activities in Kuwait. These included the Student project of the Ministry of Education, Student Sponsorships by Zakat House, provision of educational aides and technical equipment to the various schools, and provision of treatments and medical equipment through the Patients Aide Society Fund.

KFH's sponsorships were not limited to those with special needs, but covered other segments of the society. KFH organized training courses for groups of human resources in coordination and collaboration with the Manpower Support Department, where 200 fresh graduate Kuwaiti trainees were qualified for scientific and practical aspects of the Islamic financial services industry. The training extended over 6 months. They took over vacancies at KFH's various departments and sectors, thus raising the percentage of Kuwaiti manpower to 52%, i.e. higher than the ceiling specified by the Central Bank of Kuwait. On the other hand, students of Kuwait University and Business Institute participated in the training programs tailored to their curricula, constituting KFH's opportunity to identify outstanding performers.

Economic Developments

National Economy:

During 2005 the Kuwaiti economy witnessed positive growth for the fourth consecutive year. The year-long increasing economic activity represented the momentum behind the boom. In 2005 GDP is expected to grow by 3.2%. In a nutshell, these developments are the outcome of higher demand for the various goods and services.

The growth was accelerated by a set of factors: First, the continuing economic activity in relation to Iraq, while a number of companies and investors attained a large stake of logistics contracts, improved profit of investment companies, and the arrival of foreign investors in Kuwait as a concentration area close to Iraq. Second, the continuous increases in oil prices, registering records, in addition to the Kuwaiti oil production increase, at the same time, thus reflecting positively on the public revenues, which touched the KD 9 billion (KD 8,962.4 million) edge for the fiscal year 2004-2005, an increase by 170% over the budget. As a result of the soaring public revenues, largely due to the higher oil revenues, Kuwait had attained a financial surplus for the fourth consecutive year. This positive environment reflected on increasing the expenditure, in general, and the capital expenditure, in particular.

In line with the Central Bank of Kuwait's (CBK) intention to rationalize growth and demand for goods and services to cope with the global economy developments, CBK rose the discount rate five times during the year, from 4.75% to 6%.

The Chairman's Statement continued

"In light of the effective communication with the community, KFH contributed to numerous developmental projects within and outside Kuwait. A drug addiction treatment hospital was opened in the presence of HH the Prime Minister. The project is a KD 4 million donation."

Positive performance continued at Kuwait Stock Exchange (KSE), where the price index of the market rose by 79%, gaining 1,114.4 points. During the year, the value of traded shares rose with a growth rate of 72%. During the first 3 quarters of 2005, the net profit of 133 market quoted companies amounted to nearly KD 2,260 million, an increase of KD 1,072 million, i.e. 90% over the levels registered for the same period of 2004 (KD 1,188). During the year, 116 companies were under daily trading. In terms of closing against 31/12/2004, 92 companies registered increases and 31 companies witnessed decreases, while the closing prices of 3 companies remained unchanged. The stock exchange witnessed the listing of 34 new companies during the year, with total capital of KD 958 million, representing 20% of the total capitals of quoted companies, thus increasing the number of quoted companies to 158.

Concurrently with these developments, the government continued to play an indirect role in activating the economic cycle. In November 2005, the Ministry of Planning presented the State of Kuwait Five-Year Development Plan 2006/2007-2010/2011 to a group of government and private sector economic activists, as well as a number of academia and community leaders. The plan aims at continuing the privatization policy, giving way to the private sector to play a larger role in financing the mega projects. Targeted private sector's investments were estimated at KD 4.453 billion over the proposed plan period, with a share of up to 27% of the total investments. The Ministry also issued a set of measures to activate and reform the domestic economy, including, but not limited to, the laws licensing branches of foreign banks in Kuwait, lifting guarantees on deposits with local banks, and re-activating the privatization programs.

GCC Economies:

The year 2005 was favorable to the Gulf economies, as oil revenues soared to unprecedented highs, reflecting on the private sector, which witnessed notable activity. These circumstances had a positive impact on the GCC economies in terms of growth rates and current account surpluses. It is estimated that GCC states had achieved progressive growth rates in 2005.

GCC states witnessed positive growth rates. The Saudi economy realized a real growth rate of 6% in 2005, against 5.2% in 2004. Qatar's economy achieved a notable growth of 5.5% in 2005, accompanied by surplus in the state budget, compared to 9.3% in 2004. The Omani economy grew by 3.8%, against 4.5% in 2004. UAE economy registered a growth rate of 5.6% in 2005, compared to 8.5% in 2004, while the Bahraini economy witnessed a growth at the rate of 7.1% in 2005, against 5.4% in 2004.

World Economy:

During the year the world economy continued its positive track despite the risks and disasters that occurred in 2005. The ongoing positive trend was maintained due to the continuous recovery, particularly in the US, Japan and China. The substantial growth in the industrial production, world trade movement, private individual and corporate spending, in addition to the improved labor market situation, contributed to the growth of world economy by 4.3%, which is lower than last year's 30-year high level of 5%. The economic growth is expected to register 3.5% in the US, 2% in Japan, and 9% in China. The Euro region will witness a lower rate of about 1.2% as a result of the slowing recovery in both Germany and France.

In 2005 the world witnessed a continuous upward trend of interest rate on US Dollar as the Fed increased the interest on the dollar from 2.25% up to 4.25% in the form of successive amendments, the last of which took place in December 2005, for concern over the return of inflation.

The US suffered from a number of problems, mainly the scarcity of domestic savings, and the continual current account deficit, which rose to a new high of USD 753 billion by the end of September 2005, or by 6% of the GDP. Most of the deficit was financed through purchases by Asian central banks of government securities. The US policy continued to maintain its competitive edge using the exchange rate mechanism of the US Dollar, which has slipped since early 2002 against the Euro and other major currencies.

In conclusion, praise be to the Almighty God for what he bestowed on us. We pray to God to turn our efforts into success, thus achieving the objectives of KFH as well as our customers, under the leadership and directives of HH The Amir, HH The Crown Prince, and HH The Prime Minister.

I would like to extend our thanks to all concerned authorities, and our customers, who spare no effort to support this grand Islamic edifice.

Bader Abdul Muhsen Al-Mukhaizeem
Chairman and Managing Director

Consolidated Financial Statements

Auditors' Report

To the shareholders of **Kuwait Finance House K.S.C.**

We have audited the accompanying consolidated balance sheet of Kuwait Finance House K.S.C. (the parent company) and Subsidiaries (the group) as of 31 December 2005, and the related consolidated statements of income, changes in equity and cash flows for the year then ended. These consolidated financial statements are the responsibility of the parent company's management. 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 plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the group as of 31 December 2005, and the results of its operations and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted for use by the State of Kuwait.

Furthermore, in our opinion proper books of account have been kept by the company and the consolidated financial statements, together with the contents of the report of the 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 of 1960, as amended, and by the parent company's articles of association, that an inventory was duly carried out and that, to the best of our knowledge and belief, no violations of the Commercial Companies Law of 1960, as amended, nor of the articles of association have occurred during the year ended 31 December 2005 that might have had a material effect on the business of the group or on its financial position.

We further report that, during the course of our audit, we have not become aware of any material violations of the provisions of Law No. 32 of 1968, as amended, concerning currency, the Central Bank of Kuwait and the organisation of banking business, and its related regulations during the year ended 31 December 2005.

Waleed A. Al Osaimi
Licence No. 68 A
Ernst & Young
Al Aiban, Al Osaimi & Partners

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

22 January 2006
Kuwait

Consolidated Income Statement

Year ended 31 December 2005

	Note	2005 KD 000's	2004 KD 000's
Operating income			
Murabaha, Istisna'a and leasing income		189,947	133,463
Investment income	3	140,453	48,293
Fee and commission income		33,363	13,933
Net gain from dealing in foreign currencies		6,214	1,613
Other operating income		13,351	6,304
		383,328	203,606
Operating expenses			
Staff costs		43,292	27,896
General and administrative expenses		31,803	5,149
Depreciation		15,528	5,940
Provision for impairment	4	37,047	13,664
		127,670	52,649
Operating profit before distribution to depositors		255,658	150,957
Distribution to depositors	14	122,591	71,476
Profit for the year		133,067	79,481
Contribution to Kuwait Foundation for the Advancement of Sciences		1,227	766
National Labour Support Tax		2,612	1,294
Directors' fees		150	120
Net profit for the year		129,078	77,301
Attributable to:			
Equity holders of the bank		118,687	74,412
Minority interest		10,391	2,889
		129,078	77,301
Basic earnings per share	5	122 fils	87 fils

The attached notes 1 to 34 form part of these consolidated financial statements.

Consolidated Balance Sheet

At 31 December 2005

	Note	2005 KD 000's	2004 KD 000's
Assets			
Cash and balances with banks and financial institutions	6	158,293	146,161
Short-term international murabaha		663,848	380,646
Receivables	7	2,104,346	1,484,971
Leased assets	8	603,333	505,550
Available for sale investments	9	555,279	525,750
Investment in associates	10	142,734	39,288
Trading properties		93,009	127,835
Investment properties	11	184,479	105,921
Other assets		68,102	69,736
Property and equipment	12	107,695	72,208
Total assets		4,681,118	3,458,066
Liabilities, deferred revenue, fair value reserve, foreign exchange translation reserve and total equity			
Liabilities			
Due to banks and financial institutions	13	281,617	121,821
Depositors' accounts	14	3,189,344	2,563,185
Other liabilities		220,795	204,807
Total liabilities		3,691,756	2,889,813
Deferred revenue		235,239	189,002
Fair value reserve	15	62,092	31,680
Foreign exchange translation reserve	16	11,401	-
Equity attributable to the equity holders of the bank			
Share capital	17	109,397	78,141
Share premium	17	188,465	12,618
Proposed issue of bonus shares	18	13,128	7,814
Reserves	19	229,052	188,295
		540,042	286,868
Proposed cash dividend	18	60,168	39,070
Total equity attributable to the equity holders of the bank		600,210	325,938
Minority interest		80,420	21,633
Total equity		680,630	347,571
Total liabilities, deferred revenue, fair value reserve, foreign exchange translation reserve and equity		4,681,118	3,458,066

Bader Abdul Muhsen Al-Mukhaizeem
Chairman and Managing Director

Mohammed Sulaiman Al-Omar
Deputy General Manager

The attached notes 1 to 34 form part of these consolidated financial statements.

Consolidated Statement of Changes in Equity

Year ended 31 December 2005

	Attributable to equity holders of the bank										Minority interest KD 000's	Total equity KD 000's
				Reserves								
	Share capital KD 000's	Share premium KD 000's	Proposed issue of bonus shares KD 000's	Statutory reserve KD 000's	Voluntary reserve KD 000's	Treasury shares KD 000's	Sub Total KD 000's	Sub Total KD 000's	Proposed cash dividends KD 000's	Sub total KD 000's		
At 1 January 2004	71,689	7,826	4,301	137,251	28,542	(867)	164,926	248,742	35,844	284,586	20,637	305,223
Movements during the year:												
Issue of bonus shares	4,301	-	(4,301)	-	-	-	-	-	-	-	-	-
Issue of shares for cash	2,151	4,774	-	-	-	-	-	6,925	-	6,925	-	6,925
Cash received on cancellation of share options	-	18	-	-	-	-	-	18	-	18	-	18
Zakat	-	-	-	-	(4,010)	-	(4,010)	(4,010)	-	(4,010)	-	(4,010)
Cash dividends paid	-	-	-	-	-	-	-	-	(35,844)	(35,844)	-	(35,844)
Proposed issue of bonus shares	-	-	7,814	-	-	-	-	7,814	-	7,814	-	7,814
Proposed cash dividends	-	-	-	-	-	-	-	-	39,070	39,070	-	39,070
Distribution of net profit:												
Transfer to statutory reserve	-	-	-	19,868	-	-	19,868	19,868	-	19,868	-	19,868
Transfer to voluntary reserve	-	-	-	-	7,660	-	7,660	7,660	-	7,660	-	7,660
Net movement in treasury shares	-	-	-	-	-	(149)	(149)	(149)	-	(149)	-	(149)
Net change in minority interest	-	-	-	-	-	-	-	-	-	-	996	996
At 31 December 2004	78,141	12,618	7,814	157,119	32,192	(1,016)	188,295	286,868	39,070	325,938	21,633	347,571
Movements during the year:												
Issue of bonus shares	7,814	-	(7,814)	-	-	-	-	-	-	-	-	-
Issue of shares for cash	23,442	175,816	-	-	-	-	-	199,258	-	199,258	-	199,258
Cash received on cancellation of share options	-	31	-	-	-	-	-	31	-	31	-	31
Zakat	-	-	-	-	(4,372)	-	(4,372)	(4,372)	-	(4,372)	-	(4,372)
Cash dividends paid	-	-	-	-	-	-	-	-	(39,070)	(39,070)	-	(39,070)
Proposed issue of bonus shares	-	-	13,128	-	-	-	-	13,128	-	13,128	-	13,128
Distribution of net profit:												
Proposed cash dividends	-	-	-	-	-	-	-	-	60,168	60,168	-	60,168
Transfer to statutory reserve	-	-	-	12,267	-	-	12,267	12,267	-	12,267	-	12,267
Transfer to voluntary reserve	-	-	-	-	33,124	-	33,124	33,124	-	33,124	-	33,124
Net movement in treasury shares	-	-	-	-	-	(262)	(262)	(262)	-	(262)	-	(262)
Net change in minority interest	-	-	-	-	-	-	-	-	-	-	58,787	58,787
At 31 December 2005	109,397	188,465	13,128	169,386	60,944	(1,278)	229,052	540,042	60,168	600,210	80,420	680,630

The attached notes 1 to 34 form part of these consolidated financial statements.

Consolidated Statement of Cash Flows

Year Ended 31 December 2005

	Note	2005 KD 000's	2004 KD 000's
Operating activities			
Net profit for the year		129,078	77,301
Adjustment for:			
Depreciation		15,528	5,940
Provision for impairment		37,047	13,664
Share of the accumulated retained earnings of the newly consolidated subsidiaries as of 1 January 2005		(11,957)	-
Share of results of associates		(14,376)	-
Operating profit before changes in operating assets and liabilities		155,320	96,905
(Increase) decrease in operating assets:			
Exchange of deposits		(4,727)	-
Receivables		(289,610)	32,476
Leased assets		(53,124)	(217,437)
Trading properties		34,826	11,790
Other assets		20,285	29,914
Increase (decrease) in operating liabilities:			
Due to banks and financial institutions		24,769	58,144
Depositors' accounts		313,244	263,023
Other liabilities		(13,147)	33,051
Deferred revenue		46,237	6,592
Net cash from operating activities		234,073	314,458
Investing activities			
Net sale (purchase) of available for investments		65,777	(120,590)
Purchase of investment properties		(108)	(5,557)
Purchase of property and equipment		(31,669)	(55,057)
(Purchase) sale of investment in associates		(61,391)	695
Net cash used in investing activities		(27,391)	(180,509)
Financing activities			
Issue of shares		199,258	6,925
Cash dividends paid		(39,070)	(35,844)
Cash received on cancellation of share options		31	18
Payment of Zakat		(4,372)	(4,010)
Net movement in treasury shares		(262)	(149)
Net cash from (used in) financing activities		155,585	(33,060)
Increase in cash and cash equivalents		362,267	100,889
Cash and cash equivalents at 1 January		339,315	238,426
Cash and cash equivalents at 31 December	6	701,582	339,315

The attached notes 1 to 34 form part of these consolidated financial statements.

Notes to the Consolidated Financial Statements

At 31 December 2005

1 Activities

The consolidated financial statements of the group for the year ended 31 December 2005 were authorised for issue in accordance with a resolution of the parent company's board of directors on 22 January 2006.

The group comprises Kuwait Finance House K.S.C. and its consolidated subsidiaries as noted in Note 20. The parent company is a public shareholding company incorporated in Kuwait on 23 March 1977 and is registered as an Islamic Parent company with the Central Bank of Kuwait on 24 May 2004. It is engaged principally in providing banking services, the purchase and sale of properties, leasing, project construction for its own account as well as for third parties and other trading activities without practising usury. Trading activities are conducted on the basis of purchasing various goods and selling them on Murabaha at negotiated profit margins which can be settled in cash or on instalment credit basis. The parent company's registered head office is at Abdulla Al-Mubarak Street, Murqab, Kuwait.

All activities are conducted in accordance with Islamic Shareea'a, as approved by the parent company's Fatwa and Shareea'a Supervisory Board.

The parent company operates through 36 local branches (2004: 33) and employed 1,750 employees as of 31 December 2005 (2004: 1,594) of which 920 (2004: 742) are Kuwaiti nationals representing 53% (2004: 47%) of the total work force.

2 Significant Accounting Policies

Basis of preparation

The consolidated financial statements have been prepared in accordance with the regulations of the Government of Kuwait for financial services institutions regulated by the Central Bank of Kuwait. These regulations require adoption of all International Financial Reporting Standards (IFRS) except for the IAS 39 requirement for collective provision, which has been replaced by the Central Bank of Kuwait's requirement for a minimum general provision as described under the accounting policy for impairment of financial assets.

The consolidated financial statements have been presented in Kuwaiti Dinars.

Accounting convention

The consolidated financial statements are prepared under the historical cost convention modified to include the measurement at fair value of available for sale investments.

The accounting policies, except for the adoption of the applicable revised and new accounting standards, are consistent with those used in the previous year.

The adoption of the revised accounting standards that formed part of the International Accounting Standards Board's improvements project and are applicable from 1 January 2005, has had no material impact on the consolidated financial statements during the year ended 31 December 2005.

The adoption of IAS 1 revised "Presentation of Financial Statements" during the year has resulted in amendments to the presentation of minority interest. Minority interest is now presented within equity.

During the year, the parent company consolidated five previously unconsolidated subsidiaries – Al Nakheel United Real Estate Company K.S.C. (Closed), Kuwait Finance House (Bahrain) B.S.C., Kuwait Finance House (Malaysia) Berhard, Kuwait Turkish Evkaf Finance House, AREF Investment Group K.S.C. (Closed) and equity accounted for associates namely, First Takaful Insurance Company K.S.C. (Closed), Liquidity Management Centre Company B.S.C. (Closed), Gulf Investment House K.S.C. (Closed), A'ayan Leasing and Investment Company K.S.C. (Closed) and National Bank of Sharjah PSJC. Previously, these associates and unconsolidated subsidiaries were carried at cost.

On consolidation, the group's share of the accumulated retained earnings of the subsidiaries as of 1 January 2005 amounting to KD 11,957 thousand along with results of the year ended 31 December 2005 amounting to KD 19,674 thousand have been included in the consolidated income statement for the year ended 31 December 2005. On equity accounting, the group's share of the post acquisition results of the associates upto 1 January 2005 amounting to KD 7,755 thousand along with share of results of the year ended 31 December 2005 amounting to KD 6,621 thousand have been included in the consolidated income statement for the year ended 31 December 2005.

Notes to the Consolidated Financial Statements

At 31 December 2005

2 Significant Accounting Policies (continued)

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the parent company for the year ended 31 December 2005, Al Enma'a Real Estate Company K.S.C. (Closed) for the year ended 31 October 2005, The Kuwaiti Manager Company for Managing Real Estate Projects K.S.C. (Closed) for the year ended 31 October 2005, Al Muthana Investment Company K.S.C. (Closed) for the year ended 30 September 2005, Kuwait Turkish Evkaf Finance House for the period ended 30 September 2005, Aref Investment Group K.S.C. (Closed) for the period ended 30 June 2005, Kuwait Finance House (Bahrain) B.S.C. for the period ended 30 November 2005, Kuwait Finance House (Malaysia) Berhad for the period ended 30 November 2005 and Al-Nakheel United Real Estate Company K.S.C. (Closed) for the year ended 31 October 2005. All significant intra-group balances, transactions and unrealised profits are eliminated upon consolidation.

The financial statements used in the consolidation are drawn up to different reporting dates, hence adjustments were made for the effects of significant transactions or other events that occurred between the reporting date of the subsidiaries and 31 December 2005, the reporting date of the parent company.

Some of the consolidated subsidiaries use accounting policies other than that adopted in the consolidated financial statements for certain assets. Hence, appropriate adjustments are made to their financial statements when used in preparing the consolidated financial statements to bring these in line with group accounting policies.

Short-term international murabaha

Short-term international murabaha are financial assets originated by the group and represent deals with high credit quality international banks and financial institutions with a residual maturity of upto three months from the balance sheet date. These are stated at amortised cost.

Receivables

Receivables are financial assets originated by the group and principally comprise Murabaha and Istisna'a receivables. These are stated at amortised cost.

Murabaha is the sale of commodities and real estate at cost plus an agreed profit mark up whereby the seller informs the purchaser of the price at which he purchases the product and also stipulates an amount of profit.

Istisna'a is a sale contract between a contract owner and a contractor whereby the contractor based on an order from the contract owner undertakes to manufacture or otherwise acquire the subject matter of the contract according to specifications, and sells it to the contract owner for an agreed upon price and method of settlement whether that be in advance, by instalments or deferred to a specific future time.

Impairment of financial assets

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

Impairment is determined as follows:

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

For available for sale equity investments, reversal of previously recognised impairment losses, which are no longer recognised in statement of income, are recorded as increases in the fair value reserve.

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

Notes to the Consolidated Financial Statements

At 31 December 2005

2 Significant Accounting Policies (continued)

Leased assets

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

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

Available for sale

Investments are initially recognised at cost and are subsequently remeasured to fair value unless fair value cannot be reliably determined. Changes in fair value are reported in the fair value reserve until the investment is sold, collected or otherwise disposed off, or the investment is determined to be impaired, at which time the cumulative gain or loss previously included within the fair value reserve is included within investment income in the consolidated income statement.

Investments in associates

An associate is a company over which the group exerts significant influence or holding of 20% to 50% of the voting power of the investee company. The consolidated financial statements include the group's share of the associated company's results using the equity method of accounting based on the latest audited financial statements available. Certain financial statements used for the purposes of equity accounting are drawn up to different reporting dates, hence adjustments were made for the effects of significant transactions or other events that occurred between the reporting date of the associates and the reporting date of the parent company where it was practicable to do so.

Under the equity method of accounting, the initial investment is recorded at cost and the carrying amount is increased or decreased to recognise the group's share of profit or loss and other changes in the equity of the associated company. Distributions received from the associated company reduce the carrying amount of the investment.

An assessment of the investment in associated company is performed when there is an indication that the asset has been impaired or the impairment losses recognised in prior years no longer exist.

Trading properties

Trading properties are carried at the lower of cost or market value determined on an individual basis.

Investment properties

Investment properties are initially recorded at cost. Depreciation is provided on a straight-line basis over the estimated useful lives of all rental properties other than freehold land which is deemed to have an indefinite life. The carrying amounts are reviewed at each balance sheet date on an individual basis by reference to their fair value to assess whether they are recorded in excess of their recoverable amount. The recoverable amount of an asset is the higher of an asset's net selling price and value in use. Net selling price is the amount obtainable from the sale of an asset in an arm's length transaction. Value in use is the present value of estimated future cash flows expected to arise from the continuing use of an asset and from its disposal at the end of its useful life. Impairment losses, if any, are recognised in the consolidated income statement where carrying values exceed the recoverable amount.

Fair values

Available for sale investments

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

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

Investments with no reliable measures of their fair values and for which no fair value information could be obtained are carried at cost less impairment in value.

Notes to the Consolidated Financial Statements

At 31 December 2005

2 Significant Accounting Policies (continued)

Investment properties

For local investment properties, fair value is determined by the group's specialist resources which have recent experience in the local property market. For overseas investment properties, fair value is determined based on external valuations by independent, registered real estate valuers.

Financial assets and liabilities

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

Revenue recognition

i) Income from Murabaha and Istisna'a is recognised on a weighted time apportionment basis.
ii) Income from leased assets is recognised on a pattern reflecting a constant periodic return on the net investment outstanding.
iii) Rental income from investment properties is recognised on an accruals basis.
iv) Dividend income, including dividend income on own shares (held on behalf of depositors), is recognised when the right to receive payment is established.
v) Fee and commission income is recognised at the time the related services are provided.

Zakat

Zakat is calculated at 2.577% on the opening reserves of the parent company (excluding proposed distributions) which have remained for one complete fiscal year and is paid under the direction of the parent company's Al-Fatwa and Shareea'a Supervisory Board. Zakat is charged to voluntary reserve.

Foreign currencies

Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the rate of exchange ruling at the balance sheet date. All differences are taken to the consolidated income statement.

On consolidation, assets and liabilities of foreign entities are translated into Kuwaiti dinars at the period end rates of exchange and the results of these entities are translated into Kuwaiti dinars at the average rates of exchange for the period, except for entities operating in hyper-inflationary economies. The results of entities operating in hyper inflationary economics are translated into Kuwaiti Dinars at the period end exchange rates. On equity accounting, the carrying value of the associates is translated into Kuwaiti dinars at the period end rates of exchange and the results of the associates are translated into Kuwaiti dinars at the average rates of exchange for the year. All foreign exchange translation adjustments are taken to the foreign exchange translation reserve until disposal at which time they are recognised in the consolidated income statement.

Trade and settlement date accounting

All "regular way" purchases and sales of financial assets are recognised on the trade date, i.e. the date that the group commits to purchase or sell the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame generally established by regulation or convention in the market place.

Offsetting

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

Cash and cash equivalents

Cash and cash equivalents comprise cash, tawarruq balances with the Central Bank of Kuwait, balances with banks and financial institutions and international murabaha contracts and exchange of deposits maturing within three months of contract date.

Notes to the Consolidated Financial Statements

At 31 December 2005

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

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

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

The group classified all of its investments as available for sale.

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

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

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

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

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

The determination of the cash flows and discount factors for unquoted equity investments requires significant estimation. There are a number of investments where this estimation cannot be reliably determined, and as a result investments with a carrying amount of KD 62,838 (2004: KD 9,934) are carried at cost.

Notes to the Consolidated Financial Statements

At 31 December 2005

3 Investment Income

	2005 KD 000's	2004 KD 000's
Income from sale of trading properties	26,878	9,042
Rental income	11,690	8,812
Dividend income	20,156	18,045
Gain from sale of investments	55,396	12,394
Group's share of the accumulated retained earnings of the newly consolidated subsidiaries as of 1 January 2005	11,957	-
Post acquisition results of associates as of 1 January 2005	7,755	-
Share of results of associates for the current year	6,621	-
	140,453	48,293

4 Provision for impairment

	2005 KD 000's	2004 KD 000's
Provision for impairment of receivables and other assets	28,783	12,615
Provision for impairment of investments	8,264	1,049
	37,047	13,664

5 Basic Earnings per Share

Basic earnings per share are based on the net profit for the year attributable to equity holders of the parent company of KD 118,687 thousand (2004: KD 74,412 thousand) and the weighted average number of ordinary shares outstanding during the year of 975,543 thousand (2004: 858,645 thousand) after adjusting by average treasury shares held by the group.

The basic earnings per share of the previous year has been restated for bonus shares issued in 2005.

6 Cash and Cash Equivalents

	2005 KD 000's	2004 KD 000's
Cash	42,328	18,919
Balances with Central Banks	46,875	69,960
Balances with banks and financial institutions - current accounts	67,977	45,880
Balances with banks and financial institutions - exchange of deposits	1,113	11,402
Cash and balances with banks and financial institutions	158,293	146,161
Short-term international murabaha – maturing within 3 months of contract date	447,646	192,154
Tawarruq balances with Central Bank of Kuwait	100,370	1,000
Exchange of deposits – maturing after 3 months of contract date	(4,727)	-
Cash and cash equivalents	701,582	339,315

Notes to the Consolidated Financial Statements

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6 Cash and Cash Equivalents (continued)

The parent company exchanges deposits with high credit quality banks and financial institutions in local and foreign currencies with the legal right reserved to set off such deposits exchanged in the event that a counter party bank or financial institution becomes insolvent. The gross balances of deposits exchanged were as follows:

	2005 KD 000's	2004 KD 000's
Due from banks and financial institutions	251,231	341,273
Due to banks and financial institutions	(304,447)	(378,140)
	(53,216)	(36,867)

Included in the consolidated balance sheet as net balances:

	2005 KD 000's	2004 KD 000's
In assets:		
Cash and balances with banks and financial institutions – exchange of deposits	1,113	11,402
In liabilities:		
Due to banks and financial institutions – exchange of deposits (Note 13)	(54,329)	(48,269)
	(53,216)	(36,867)

The fair value of cash and balances with banks and financial institutions do not differ from their respective book values.

7 Receivables

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

	2005 KD 000's	2004 KD 000's
International murabahas	116,786	131,601
Local murabahas	1,617,166	1,362,911
Istisna'a and other receivables	507,151	113,144
	2,241,103	1,607,656
Less: provision for impairment	(136,757)	(122,685)
	2,104,346	1,484,971

The industry concentration of receivables is as follows:

	2005 KD 000's	2004 KD 000's
Trading and manufacturing	1,325,779	953,966
Banks and financial institutions	396,563	306,616
Construction and real estate	379,352	335,116
Other	139,409	11,958
	2,241,103	1,607,656
Less: provision for impairment	(136,757)	(122,685)
	2,104,346	1,484,971

Notes to the Consolidated Financial Statements

At 31 December 2005

7 Receivables (continued)

Provisions for losses on receivables from customers for finance facilities are as follows:

	Specific		General		Total	
	2005 KD 000's	2004 KD 000's	**2005 KD 000's**	2004 KD 000's	**2005 KD 000's**	2004 KD 000's
Balance at beginning of year	**87,276**	80,375	**35,409**	29,695	**122,685**	110,070
Provided during the year,net	**3,511**	6,901	**10,561**	5,714	**14,072**	12,615
Balance at end of year	**90,787**	87,276	**45,970**	35,409	**136,757**	122,685

At 31 December 2005, non-performing finance facilities amounted to KD 98,926 thousand (2004: KD 98,316 thousand) and are split between facilities granted pre-invasion and post liberation as follows:

	Pre-invasion KD 000's	Post liberation KD 000's	Total KD 000's
2005			
Finance facilities	**31,737**	**67,189**	**98,926**
Provisions	**31,737**	**59,050**	**90,787**
2004			
Finance facilities	31,790	66,526	98,316
Provisions	31,790	55,486	87,276

The provision charge for the year on unfunded facilities is KD 1,467 thousand (2004: KD 569 thousand). The available provision on unfunded facilities of KD 5,188 thousand (2004: KD 3,721 thousand) is included under other liabilities.

The analysis of specific and general provisions set out above is based on the requirements of the Central Bank of Kuwait. According to the Central Bank of Kuwait instructions, a general provision of 2% on all credit facilities net of certain categories of collateral, to which Central Bank of Kuwait instructions are applicable and not subject to specific provision, is made.

Provisions include certain amounts purchased by the Central Bank of Kuwait. Such provisions must be ceded to the Central Bank of Kuwait when they are no longer required.

Whenever necessary, murabaha receivables are secured by acceptable forms of collateral to mitigate the related credit risks. Real estate murabaha receivables are secured by mortgage on the underlying property.

Receivables from banks and financial institutions comprise mainly murabaha transactions with high credit quality institutions.

The group's receivables are principally concentrated in Kuwait.

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

Notes to the Consolidated Financial Statements

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8 Leased Assets

The net investment comprises the following:

	2005 KD 000's	2004 KD 000's
Gross investment	629,607	525,598
Unearned revenue	(16,153)	(19,157)
Provision for impairment	(10,121)	(891)
	603,333	505,550

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

	2005 KD 000's	2004 KD 000's
Within one year	494,733	423,491
One to five years	107,030	65,386
Later than five years	27,844	36,721
	629,607	525,598

The unguaranteed residual value of the leased assets at 31 December 2005 is estimated at KD Nil (2004: KD Nil).

9 Available for Sale Investments

	2005 KD 000's	2004 KD 000's
Investments comprise:		
Quoted equity investments	55,395	48,841
Unquoted equity investments	62,838	9,934
Managed portfolios	66,988	34,411
Funds	198,978	187,874
Sukook	87,569	64,089
Unconsolidated subsidiaries	83,511	180,601
	555,279	525,750
Investments carried at fair value	384,199	281,060
Investments carried at cost less impairment	171,080	244,690
	555,279	525,750

Included in managed portfolios is an amount of KD 18,594 thousand (2004: KD 9,643 thousand) which represents the group's investment in 7,559 thousand (2004: 5,953 thousand) of its own shares on behalf of depositors, equivalent to 0.69% of the total issued share capital at 31 December 2005 (2004: 0.76%). The results from activities relating to dealing in these shares are attributed only to the depositors and hence these shares are classified under investments.

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At 31 December 2005

9 Available for Sale Investments (continued)

The parent company's unconsolidated subsidiaries primarily consist of the following:

	Interest in equity %	Country of registration	Principal activities
Development Enterprises Holding Co.	100	Kuwait	Holding Company
Gulf International Automobile Trading Company K.S.C. (Closed)	100	Kuwait	Trading in motor vehicles
ALAFCO - Aviation Lease and Finance Company K.S.C. (Closed)	85	Kuwait	Leasing and financing of aircraft
International Turnkey Systems Company K.S.C. (Closed)	85	Kuwait	Development of computer software and hardware
Public Services Company K.S.C. (Closed)	80	Kuwait	Administrative services
Al Salaam Hospital Company K.S.C. (Closed)	52	Kuwait	Health care

10 Investment in Associates

The parent company's associates comprise the following companies:

	Interest in equity %	Country of registration	Principal activities
First Takaful Insurance Company K.S.C. (Closed)	27	Kuwait	Islamic Takaful insurance
Gulf Investment House K.S.C. (Closed)	26	Kuwait	Islamic investments
Liquidity Management Centre Company B.S.C. (Closed)	25	Bahrain	Islamic banking and financial services
National Bank of Sharjah PJSC	20	United Arab Emirates	Islamic banking services
A'ayan Leasing & Investment Company K.S.C. (Closed)	16	Kuwait	Leasing and Islamic investments

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At 31 December 2005

10 Investment in Associates (continued)

Carrying amount of investments in associates:

	2005 KD 000's	2004 KD 000's
At 1 January	39,288	39,983
Post acquisition results as of 1 January 2005	7,755	-
Investments in associates arising on consolidation	91,716	-
Share of results for the year	6,621	-
Dividends received	(2,646)	(695)
At 31 December	142,734	39,288
Share of associates' assets and liabilities:		
Assets	247,498	121,310
Liabilities	(104,764)	(82,022)
Net assets	142,734	39,288
Share of associates' revenue and results:		
Revenue	13,003	8,587
Results	6,621	-

Investments in associates with a carrying amount of KD 103,497 thousand have a fair value of KD 185,898 thousand. The remaining associates with a carrying value of KD 39,237 thousand are unquoted companies and do not have a reliable measure of fair value.

11 Investment Properties

	2005 KD 000's	2004 KD 000's
At 1 January	105,921	102,447
Arising on consolidation	30,687	-
Purchases	55,729	6,625
Disposals	(5,216)	(1,068)
Depreciation charged for the year	(2,743)	(2,075)
Impairment losses released (charged)	101	(8)
At 31 December	184,479	105,921
Cost	214,342	133,143
Accumulated depreciation	(23,274)	(20,532)
Impairment	(6,589)	(6,690)
	184,479	105,921

Included in investment properties is an investment in Al-Muthana Complex in Kuwait which is constructed on land leased from the Government of Kuwait. The ownership of the building, as well as any results from the activities relating to the investment, are attributed only to the equity holders of the bank.

The fair value of the investment properties at the balance sheet date is KD 208,520 thousand (2004: KD 122,982 thousand).

Notes to the Consolidated Financial Statements

At 31 December 2005

12 Property and Equipment

Included in property and equipment are the head office building and all branches of the parent company constructed on land leased from the Government of Kuwait. The ownership of the buildings as well as the net rental income from these buildings are attributable only to the equity holders of the parent company.

13 Due to Banks and Financial Institutions

	2005 KD 000's	2004 KD 000's
Current accounts	70,865	4,624
Murabaha payable	156,423	68,928
Exchange of deposits (Note 6)	54,329	48,269
	281,617	121,821

The fair values of balances due to banks and financial institutions do not differ from their respective book values.

14 Depositors' Accounts

a) The depositors' accounts of the bank comprise the following:

i) Non-investment deposits in the form of current accounts. These deposits are not entitled to any profits nor do they bear any risk of loss as the bank guarantees to pay the related balances on demand. Accordingly, these deposits are considered Qard Hasan from depositors to the parent company on the grounds of Islamic Shareea'a.

ii) Investment deposits comprise deposits for unlimited periods and savings accounts. Unlimited investment deposits are initially valid for one year and are automatically renewable for the same period unless notified to the contrary in writing by the depositor. Investment savings accounts are valid for an unlimited period.

In all cases the investment deposits receive a proportion of the profit as the board of directors of the bank determines, or bear a share of loss based on the results of the financial year.

The parent company generally invests approximately 90% of investment deposits for an unlimited period ("Mustamera"), 70% of investment deposits for an unlimited period ("Al-Sedra") and 60% of investment savings accounts ("Tawfeer"). The parent company guarantees to pay the remaining uninvested portion of these investment deposits. Accordingly, this portion is considered Qard Hasan from depositors to the parent company, on the grounds of Islamic Shareea'a. Investing such Qard Hasan is made at the discretion of the board of directors of the parent company, the results of which are attributable to the equity holders of the parent company.

b) On the basis of the results for the year the board of directors of the parent company determined the depositors' share of profit at the following rates:

	2005 % per annum	2004 % per annum
Investment deposits for an unlimited period ("Mustamera")	6.807	4.800
Investment deposits for an unlimited period ("Al-Sedra")	5.294	3.733
Investment savings accounts ("Tawfeer")	4.538	3.200

c) The fair values of depositors' accounts do not differ from their respective book values.

Notes to the Consolidated Financial Statements

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15 Fair Value Reserve

Changes in fair value of available for sale investments are reported in the fair value reserve. Management of the parent company is of the opinion that this reserve is attributable to both the depositors and equity holders. As a result, the reporting of this reserve as a separate item on the consolidated balance sheet enables a fairer presentation than its inclusion under equity.

The movement on the fair value reserve is analysed as follows:

	2005 KD 000's	2004 KD 000's
Balance at 1 January	31,680	19,776
Change in fair value during the year	49,480	15,314
Gain realised during the year	(19,068)	(3,410)
Balance at 31 December	62,092	31,680

16 Foreign Exchange Translation Reserve

The foreign exchange translation reserve arises on the consolidation of foreign subsidiaries and equity accounting of foreign associates.

Management of the parent company is of the opinion that this reserve is attributable to both the depositors and equity holders. As a result, the reporting of this reserve as a separate item on the consolidated balance sheet enables a fairer presentation than its inclusion under equity.

17 Share Capital

The ordinary and extraordinary general assembly meeting of the equity holders of the parent company held on 14 March 2005 approved an increase in the authorised share capital from KD 78,141 thousand to KD 85,955 thousand (by way of an issuance of 10% bonus shares amounting to KD 7,814 thousand) and by 234,422 thousand shares with a nominal value of 100 fils per share amounting to KD 23,442 thousand plus premium of 750 fils per share amounting to KD 175,816 thousand. Accordingly, the authorised, issued and fully paid-up share capital at 31 December 2005 comprises 1,093,968 thousand (31 December 2004: 781,406 thousand) shares of 100 fils each.

18 Proposed Cash Dividend and Issue of Bonus Shares

The board of directors of the parent company have proposed a cash dividend of 55% for the year ended 31 December 2005 (2004: 50%) and an issue of bonus shares of 12% (2004: 10%) of paid up share capital. This proposal is subject to the approval of the Ordinary General Assembly of the equity holders of the parent company and completion of legal formalities. Proposed dividends are shown separately within equity.

The parent company increased its share capital at end of June 2005 which has impacted the distributable earnings per share. The distributable earnings per share calculated by the management based on the total number of shares as at 31 December 2005 (excluding treasury shares) of 1,092,754 thousand is 109 fils per share, distributed as above, after deduction of transfers to reserves.

19 Reserves

The Extraordinary General Assembly of the parent company held on 18 March 1996 approved an amendment to article 58 of its articles of association, in which the Ordinary General Assembly can approve an increase in the transfer of 10% each of the net profit for the year to statutory and voluntary reserves, as appropriate, if proposed by the board of directors of the parent company. As of this year, the Ordinary General Assembly has resolved to suspend transfers to statutory reserve in excess of 10%. As a result, an amount of KD 12,267 thousand equivalent to approximately 10% (2004: KD 19,868 thousand equivalent to approximately 27%), of the profit for the year before contribution to Kuwait Foundation for the Advancement of Sciences, Directors' fees and National Labour Support tax has been transferred to statutory reserve.

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19 Reserves (continued)

Only that part of the statutory reserve in excess of 50% of paid-up share capital is freely distributable and useable at the discretion of the Ordinary General Assembly in ways that may be deemed beneficial to the parent company. Distribution of the balance of the statutory reserve is limited to the amount required to enable the payment of a dividend of 5% of paid-up share capital to be made in years when accumulated profits are not sufficient for the payment of a dividend of that amount.

27% of the profit for the year before contribution to Kuwait Foundation for the Advancement of Sciences, Directors' fees and National Labour Support tax has been transferred to voluntary reserve.

The share premium account is not available for distribution.

20 Consolidated Subsidiaries

Details of material consolidated subsidiaries are set out below:

Name	Country of registration	Interest in equity %	Principal activities
Kuwait Finance House B.S.C.	Bahrain	100	Islamic banking services
The Kuwaiti Manager Company for Managing Real Estate Projects K.S.C. (Closed)	Kuwait	100	Contracting, trading and project management
Al Muthana Investment Company K.S.C. (Closed)	Kuwait	100	Islamic investments
Al-Nakheel United Real Estate Company K.S.C. (Closed)	Kuwait	100	Real estate investment and trading
Kuwait Finance House (Malaysia) Berhad	Malaysia	100	Islamic banking services
Kuwait Turkish Evkaf Finance House	Turkey	62	Islamic banking services
Aref Investment Group K.S.C. (Closed)	Kuwait	52	Islamic investments
Al Enma'a Real Estate Company K.S.C. (Closed)	Kuwait	51	Real estate, investment, trading and management

21 Contingencies and Commitments

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

	2005 KD 000's	2004 KD 000's
Acceptances and letters of credit	43,002	36,846
Guarantees	197,760	160,842
	240,762	197,688
Capital commitments	103,865	244,460

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22 Related Party Transactions

Certain related parties (directors and executive employees, officers of the group, their families and companies of which they are principal owners) were depositors and financing facilities customers of the parent company, in the ordinary course of business. Such transactions were made on substantially the same terms, including profit rates and collateral, as those prevailing at the same time for comparable transactions with unrelated parties and did not involve more than a normal amount of risk. These transactions are approved by the Ordinary General Assembly of the equity holders of the parent company.

Details of the interests of Board Members and Executive Officers are as follows:

	The number of Board Members or Executive Officers		The number of related parties			
	2005	2004	**2005**	2004	**2005 KD 000's**	2004 KD 000's
Board Members						
Finance facilities	**6**	6	**4**	2	**137**	111
Contingent liabilities	-	1	-	-	-	15
Credit cards	**13**	9	**18**	6	**17**	10
Deposits	**16**	11	**475**	57	**3,762**	2,546
Collateral against financing facilities	-	-	-	-	-	-
Executive Officers						
Finance facilities	**21**	25	**40**	11	**479**	955
Contingent liabilities	-	-	-	-	-	-
Credit cards	**30**	19	**43**	27	**37**	13
Deposits	**34**	29	**123**	72	**617**	1,363
Collateral against financing facilities	**7**	7	**17**	-	**754**	1,645

Compensation of key management personnel is as follows:

	2005 KD 000's	2004 KD 000's
Short-term employee benefits	2,982	2,009
Termination benefits	3,883	3,149
	6,865	5,158

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23 Currency Risk

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

Currency risk is managed on the basis of limits determined by the parent company's board of directors and a continuous assessment of the group's open positions and current and expected exchange rate movements. The group where necessary matches currency exposures inherent in certain assets with liabilities in the same or a correlated currency.

The group had the following significant net exposures denominated in foreign currencies as of 31 December:

	2005 KD 000's equivalent	2004 KD 000's equivalent
U.S. Dollars	(7,850)	83,994
Sterling Pounds	664	1,197
Japanese Yen	(4)	645
Euros	(9,109)	1,346
Gulf Cooperation Council currencies	(6,101)	(10,557)
Others	299	1,530

24 Segmental Analysis

Primary segment information

For management purposes the parent company is organised into three major business segments. The principal activities and services under these segments are as follows:

Treasury: Liquidity management, international murabaha investments, exchange of deposits with banks and financial institutions and international banking relationships.

Investment: Managing direct investments, investments in subsidiaries, associated companies and international leasing.

Retail and corporate banking: Providing a range of banking services and investment products to corporate and individual customers, providing commodity and real estate murabaha finance, local leasing, wakala and Istisna'a facilities.

31 December 2005	Treasury KD 000's	Investment KD 000's	Retail and Corporate banking KD 000's	Other groups KD 000's	Total KD 000's
Assets					
Cash and balances with banks and financial institutions	158,293	-	-	-	158,293
Short-term international murabaha	658,153	5,695	-	-	663,848
Receivables	116,786	11,301	1,957,493	18,766	2,104,346
Leased assets	-	79,423	523,910	-	603,333
Available for sale investments	-	555,279	-	-	555,279
Investment in associates	-	142,734	-	-	142,734
Trading properties	-	93,009	-	-	93,009
Investment properties	-	184,479	-	-	184,479
Other assets	1,921	10,347	52,170	3,664	68,102
Property and equipment	1,043	2,246	82,466	21,940	107,695
	936,196	1,084,513	2,616,039	44,370	4,681,118

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24 Segmental Analysis (continued)

Liabilities, deferred revenue, fair value reserve, foreign exchange translation reserve and total equity

31 December 2005	Treasury KD 000's	Investment KD 000's	Retail and Corporate banking KD 000's	Other groups KD 000's	Total KD 000's
Due to banks and financial institutions	281,617	-	-	-	281,617
Depositors' accounts	-	50,352	3,138,992	-	3,189,344
Other liabilities	66	6,620	132,391	81,718	220,795
Deferred revenue	-	-	235,239	-	235,239
Fair value reserve	-	62,092	-	-	62,092
Foreign exchange translation reserve	-	11,401	-	-	11,401
Total equity	-	-	-	680,630	680,630
	281,683	130,465	3,506,622	762,348	4,681,118
Year ended 31 December 2005					
Operating income	6,214	140,453	223,309	13,352	383,328
Profit before distribution to depositors	4,144	93,674	148,935	8,905	255,658

31 December 2004	Treasury KD 000's	Investment KD 000's	Retail and Corporate banking KD 000's	Other groups KD 000's	Total KD 000's
Assets					
Cash and balances with banks and financial institutions	146,161	-	-	-	146,161
Short-term international murabaha	380,381	265	-	-	380,646
Receivables	94,885	12,862	1,356,020	21,204	1,484,971
Leased assets	-	73,029	432,521	-	505,550
Available for sale investments	-	525,750	-	-	525,750
Investment in associates	-	39,288	-	-	39,288
Trading properties	-	127,835	-	-	127,835
Investment properties	-	105,921	-	-	105,921
Other assets	-	14,996	51,127	3,613	69,736
Property and equipment	304	153	36,356	35,395	72,208
	621,731	900,099	1,876,024	60,212	3,458,066
Liabilities, deferred revenue, fair value reserve, foreign exchange translation reserve and total equity					
Due to banks and financial institutions	121,821	-	-	-	121,821
Depositors' accounts	168	87,621	2,181,292	294,104	2,563,185
Other liabilities	75	4,865	122,663	77,204	204,807
Deferred revenue	9,764	-	179,238	-	189,002
Fair value reserve	-	31,680	-	-	31,680
Foreign exchange translation reserve	-	-	-	-	-
Total equity	-	-	-	347,571	347,571
	131,828	124,166	2,483,193	718,879	3,458,066
Year ended 31 December 2004					
Operating income	17,720	51,104	127,018	7,764	203,606
Profit before distribution to depositors	9,367	47,428	88,473	5,689	150,957

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24 Segmental Analysis (continued)

Secondary segment information

The group operates in different geographical areas. A geographical analysis is as follows:

	Assets		Liabilities, deferred revenue, fair value reserve, foreign exchange translation reserve and total equity		Contingencies and commitments under letters of credit and guarantees	
	2005 KD 000's	2004 KD 000's	**2005 KD 000's**	2004 KD 000's	**2005 KD 000's**	2004 Total
Geographical areas:						
Kuwait and the rest of the Middle East	**3,868,116**	2,985,770	**4,263,022**	3,414,246	**171,413**	140,940
North America	**111,041**	135,036	**11,933**	22,722	**2,312**	1,892
Western Europe	**186,946**	237,887	**12,363**	20,889	**11,558**	9,458
Other	**515,015**	99,373	**393,800**	209	**55,479**	45,398
	4,681,118	3,458,066	**4,681,118**	3,458,066	**240,762**	197,688

	Local		International		Total	
	2005 KD 000's	2004 KD 000's	**2005 KD 000's**	2004 KD 000's	**2005 KD 000's**	2004 Total
Operating income	**297,656**	173,778	**85,672**	29,828	**383,328**	203,606
Profit before distribution to depositors	**198,520**	128,842	**57,138**	22,115	**255,658**	150,957

25 Concentration of Assets and Deposit Liabilities

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

(a) The distribution of assets by industry sector was as follows:

	2005 KD 000's	2004 KD 000's
Trading and manufacturing	**1,425,500**	310,018
Banks and financial institutions	**1,363,962**	1,260,765
Construction and real estate	**1,296,547**	1,148,230
Other	**595,109**	739,053
	4,681,118	3,458,066

See Note 24 for distribution of assets by geographical areas.

Notes to the Consolidated Financial Statements

At 31 December 2005

25 Concentrations of Assets and Deposit Liabilities (continued)

(b) The distribution of deposit liabilities was as follows:

	2005 KD 000's	2004 KD 000's
Geographic region		
Kuwait and the rest of the Middle East	3,124,753	2,643,897
North America	40	22,103
Western Europe	5,079	18,957
Other	341,089	49
	3,470,961	2,685,006
Industry sector		
Trading and manufacturing	568,010	461,392
Banks and financial institutions	281,617	121,884
Construction and real estate	22,172	13,344
Other	2,599,162	2,088,386
	3,470,961	2,685,006

26 Credit Risk

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss.

All policies relating to credit including the determination of approval limits are approved by the parent company's board of directors.

The group manages credit risk on both an individual counterparty and portfolio or product line basis together with geographical and business diversification to avoid undue concentration of risk. Credit limits or individual transactions resulting in credit risk are approved in accordance with appropriately defined procedures for the assessment of creditworthiness, collateral requirements and approval limits by the group's management and executive credit committees. Security is obtained when considered appropriate and is considered by management in the determination of provisions. The group's credit granting process including the subsequent monitoring, timely identification of defaults and determination of provisions are subject to periodic independent internal reviews.

The credit risk concentrations within receivables, which form a significant portion of assets subject to credit risk, are given in Note 7.

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27 Liquidity Risk

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

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

The maturity profile of assets and liabilities at 31 December 2005 is as follows:

	Within 3 months KD 000's	3 to 6 months KD 000's	6 to 12 months KD 000's	After one year KD 000's	Total KD 000's
Assets					
Cash and balances with banks and financial institutions	158,293	-	-	-	**158,293**
Short-term international murabaha	663,848	-	-	-	**663,848**
Receivables	462,956	315,652	441,913	883,825	**2,104,346**
Leased assets	168,933	126,700	199,100	108,600	**603,333**
Available for sale investments	-	-	-	555,279	**555,279**
Investment in associates	-	-	-	142,734	**142,734**
Trading properties	-	93,009	-	-	**93,009**
Investment properties	-	-	-	184,479	**184,479**
Other assets	45,968	4,488	-	17,646	**68,102**
Property and equipment	-	-	-	107,695	**107,695**
	1,499,998	**539,849**	**641,013**	**2,000,258**	**4,681,118**
Liabilities					
Due to banks and financial institutions	281,617	-	-	-	**281,617**
Depositors' accounts	1,945,073	11,120	33,663	1,199,488	**3,189,344**
Other Liabilities	29,028	45,454	45,770	100,543	**220,795**
	2,255,718	**56,574**	**79,433**	**1,300,031**	**3,691,756**

Notes to the Consolidated Financial Statements

At 31 December 2005

27 Liquidity Risk (continued)

The maturity profile of assets and liabilities at 31 December 2004 is as follows:

	Within 3 months KD 000's	3 to 6 months KD 000's	6 to 12 months KD 000's	After one year KD 000's	Total KD 000's
Assets					
Cash and balances with banks and financial institutions	146,161	-	-	-	146,161
Short-term international murabaha	380,646	-	-	-	380,646
Receivables	315,967	199,317	226,901	742,786	1,484,971
Leased assets	194,578	125,018	86,938	99,016	505,550
Available for sale investments	-	-	-	525,750	525,750
Investment in associates	-	-	-	39,288	39,288
Trading properties	-	127,835	-	-	127,835
Investment properties	-	-	-	105,921	105,921
Other assets	37,008	32,001	562	165	69,736
Property and equipment	-	-	-	72,208	72,208
	1,074,360	484,171	314,401	1,585,134	3,458,066
Liabilities					
Due to banks and financial institutions	121,821	-	-	-	121,821
Depositors' accounts	1,532,055	6,181	6,181	1,018,768	2,563,185
Other liabilities	130,796	17,958	56,053	-	204,807
	1,784,672	24,139	62,234	1,018,768	2,889,813

28 Market Risk

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

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

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

Notes to the Consolidated Financial Statements

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29 Equity Price Risk

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

30 Operational Risk

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

The operational risk function of the parent company is in line with the CBK instructions concerning the general guidelines for internal controls and the sound practices for managing and supervising operational risks in banks.

31 Management of Purchased Debts

In accordance with Decree 32/92 and Law 41/93 in respect of the financial and banking sector, the group is required to manage the purchased debts without remuneration in conformity with the terms of the debt purchase agreement.

32 Financial Instruments

In the ordinary course of business, the group uses primary financial instruments such as cash and balances with or due to banks and other financial institutions, investments, receivables and payables. The group does not make use of derivative financial instruments. Information about fair values of financial assets and liabilities are disclosed in the related notes to the consolidated financial statements.

33 Fiduciary Assets

The aggregate value of assets held in a trust or fiduciary capacity by the parent company at 31 December 2005 amounted to KD 274,239 thousand (2004: KD 155,266 thousand).

34 Comparative Figures

Certain of the comparative figures have been restated to conform with the presentation in the current year. Such reclassifications do not affect previously reported net profit or equity.