البنك الأهلي المتحد

ahli united bank

Banking Expertise ... Modern Spirit

Annual Report 2010

His Highness
Sheikh Sabah Al-Ahmad
Al-Jaber Al-Sabah

Emir of The State of Kuwait

His Highness
Sheikh Nawaf Al-Ahmad
Al-Jaber Al-Sabah

Crown Prince of The State of Kuwait

His Highness
Sheikh Naser Al-Mohammad
Al-Ahmad Al-Sabah

Prime Minister of The State of Kuwait

CONTENTS

SPEECH OF CHAIRMAN AND MANAGING DIRECTOR

Hamad Abdul Mohsen Al-Marzouq

Chairman and Managing Director

On behalf of the Board of Directors, I'm pleased to put before you Ahli United Bank Annual Report for the year 2010. It is gratifying to inform you that that the financial statements for this year is the first as an Islamic Bank. In addition to the impediments the banking sector was exposed to in 2010, our Bank has faced an exceptional challenge to convert all its activities to become compliant with the principles of Islamic Sharia'a in execution to the wish of our shareholders. It is with Allah's grace & blessing that we have succeeded in achieving the objective and complete the conversion process with great success and have set ourselves as an example in an unprecedented paradigm at all levels.

Converting Bank's activities in be fully Sharia'a compliant at the beginning of the second quarter, introducing distinct Islamic products and excellent customer service round the clock constituted the salient features in generating a net profit of KD 27.4 million in 2010, despite the specific, general and additional precautionary provisions taken by the Bank, amounting to KD 24.5 million, demonstrating a conservative approach in calculating the provisions.

The Bank's total operating income for 2010 recorded KD77.4 million, with total assets reaching KD 2,454.3 million as of 31/12/2010, while the total equity recorded KD 265.3 million.

The regulatory capital adequacy ratio of the bank - calculated in accordance with the decisions of Basel Committee 2 – stands at a solid 18.76% exceeding the regulatory minimum requirement of 12%, which reflects a strong, distinct and solid structure of the bank's capital base and the potential to further enhance its assets.

In light of such excellent results, the Board of Directors recommends the distribution of 14% cash dividend (i.e. fourteen fils per share) and bonus shares of 5% (i.e. one share for every 20 shares) for the financial year ended on 31st December 2010 to sustain the strong position of the Bank's capital base.

Against the continuing recession in the global economy and its significant systemic impact on the economic both locally & regionally without disregarding the apparent challenges in converting the Bank to an Islamic institution. The Bank has sustained its solid financial position and further strengthened the relationship with its customers, thus delivering robust growth rates. This demonstrates the successful conversion of our Bank, the competence of its strategy, its resilience and strong fundamentals with very prudent and controlled risk environment.

Despite the ongoing repercussions of the financial crisis, the Bank successfully committed to its Islamic funding rules to thrive the size of business and finance corporate sector in excess of KD 120 million and increase its customer base.

Indubitably, the figures provided to you demonstrates the forte capital adequacy ratio, excellent solvency and high liquidity the bank possesses. The Bank continued to focus on its objectives, which include, consolidating its presence through strategic and business diversification, developing its Islamic funding rules, promoting long-term relationship with its customers by increasing the number of branches to 28 branches and introducing comprehensive financial services in accordance with the Islamic Sharia'a principles. The bank, in appreciation to its customers' confidence and trust, asserts to exert all efforts to achieve outstanding returns that transcend its peers in both the local and regional markets, which I proudly announce has been attained.

I would like to seize this opportunity to assure our shareholders and customers that – with the grace of Allah Almighty – the Bank has commenced its Islamic banking operation pursuing distinct level of professionalism in the implementation which was based on solid and strong financial position and valued customer base further asserting the pioneering role of your bank as the first bank established in Kuwait.

On your behalf and on behalf of the Board of Directors I am pleased to extend my sincere congratulations to His Highness the Amir Sheikh Sabah Al-Ahmad Al-Jaber Al-Sabah and His Highness the Crown Prince Sheikh Nawaf Al-Ahmad Al-Jaber Al-Sabah and His Highness the Prime Minister Sheikh Nasser Mohammad Al-Ahmad Al-Sabah and the entire Kuwaiti people on the occasion of commemorating 50 years since the independence and 20 years since the liberation of our beloved Kuwait, and 5 years on the assumption of His Highness the Amir Sheikh Sabah Al-Ahmad Al-Jaber Al-Sabah as the ruling Price of the State of Kuwait.

I would also like to sincerely appreciate our shareholders for their support enabling us to comply with their desire to convert the bank into a fully Islamic institution in accordance with the Islamic Sharia'a principles as well as our customers whose confidence, trust and positive cooperation were the key impetus in this process.

Allow me on your behalf and on behalf of my fellow members of the Board of Directors to extend our appreciation and gratitude to the Central Bank of Kuwait team, led by His Excellency the Governor Sheikh / Salem Abdul-Aziz al-Sabah, as well as the Ministry of Commerce and Industry team, headed by His Excellency the Minister / Ahmed Rashid Haroun for their sincere cooperation in meeting the conversion deadline smoothly and efficiently.

Also an attribution is due - on behalf of the Board of Directors and Bank employees – to extend my appreciation and gratitude to the owners of virtue, the members of the Fatwa & Sharia'a Supervisory Board for their dedicated efforts and their genuine cooperation with the Bank's management, and special and heartiest thanks to the honorable Sheikh / Ahmed Bazi Yaseen, praying for his good health and wellness.

On behalf of the Board of Directors I would like to take this opportunity to congratulate and thank our dedicated staff for their unstinting cooperation and sincere efforts enabling the Bank to successfully complete its Islamic conversion process on the due date without any delay with a success rate of 100% - by the grace of Allah Almighty.

Finally, I reiterate my congratulations and thanks to all look forward with enthusiasm and confidence for next year, which we hope to surpass by pursuing our business objectives in a prudent and focused manner, despite the difficulties and the repercussions of the financial crisis.

Sharia'a & Fatwa Supervisory Board Report

Ahli United Bank – Kuwait

To: M/s. The Shareholders ahli united bank K.S.C.

We thank Allah almighty and extend our prayers and peace to his Prophet Mohamad, all his family and friends,,

During the past period, the Bank has exerted enormous efforts to convert its operations to become compliant with the provisions of Islamic Sharia'a. The Board had comfort with regards to the contracts, forms, policies and procedures that have been provided pertaining to the steps taken to convert bank's activities to be compliant with the provisions of Islamic Sharia'a, wherein we have reviewed and examined them and incorporated the necessary amendments thereto, the Board has also confirmed their conformity to the provisions of Islamic Sharia'a and had rendered the related necessary legislative advices and decisions.

After reviewing the Report presented by the Executive Committee of the Supervisory Board stipulating the absence of any observations or legislative violations, the Board deems the following appropriate:

1- All reviewed contracts, transactions and deals performed by the Bank during the period from 1st April till 31st December 2010 have been conducted in compliance with the provisions and principles of the Islamic Sharia'a.

2- All gains realized post the Islamic conversion from Non-Sharia'a compliant resources have been warded off in preparation for disposal to charity pursuant to the legislative decision rendered in this regard.

Therefore and based on the above, The Board hereby confirms that the Bank activities post the Islamic conversion date are compliant with the provisions of Islamic Sharia'a.

We seek Allah's guidance to realize the conscious awareness and successfulness.

Allah's peace, graciousness and blessing be upon you,

Sheikh Ahmad Bazie Al Yasin
Chairman

Sheikh Dr. Khaled Mathkour Al Mathkour
Member

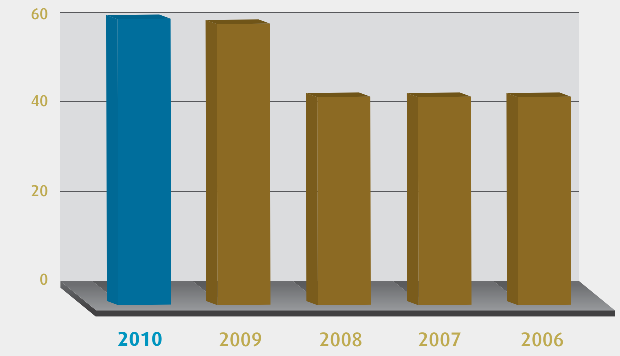
Sheikh Dr. A/Aziz Khlifa Al Qassar
Member

Sheikh Dr. Issam Khalaf Al Enezie
Member

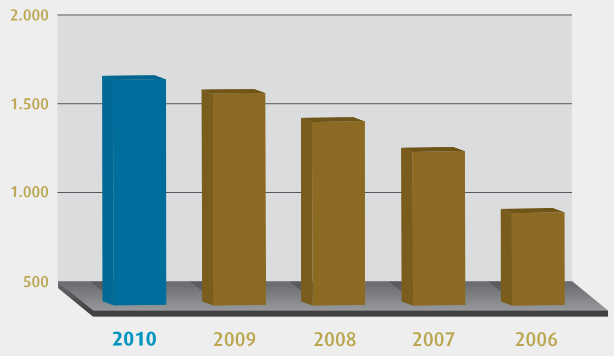
FINANCIAL PERFORMANCE

Financial Performance Summary

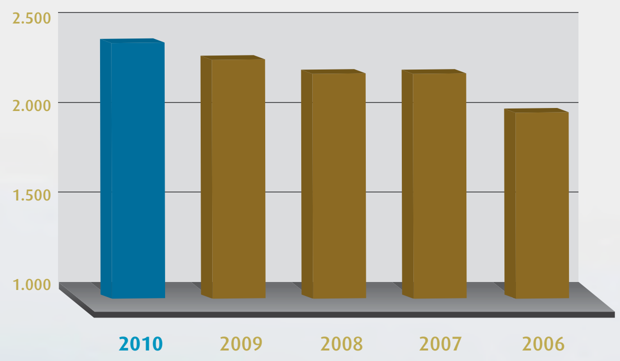
KD thousands unless otherwise stated	2010	2009	2008	2007	2006
NET PROFIT	27,444	14,262	51,365	48,179	45,111
NET FINANCING AND INTEREST INCOME	59,675	57,533	42,430	42,539	42,371
FINANCING RECEIVABLES AND LOANS	1,609,986	1,561,104	1,472,932	1,251,476	922,987
TOTAL ASSETS	2,454,337	2,260,533	2,237,018	2,238,549	1,929,406
TOTAL DEPOSITS	2,147,242	1,988,032	1,915,782	1,888,408	1,497,209
SHAREHOLDERS EQUITY	245,679	213,159	243,066	269,884	235,097
RETURN ON AVERAGE ASSETS (ROAA)	1.1%	0.6%	2.2%	2.5%	2.7%
RETURN ON AVERAGE EQUITY (ROAE)	12.2%	6.2%	20.2%	20.5%	21.5%
COST TO INCOME	38.7%	33.4%	32.0%	34.5%	34.2%
CAPITAL ADEQUACY RATIO	18.76%	16.8%	14.8%	15.6%	18.1%
EARNINGS PER SHARE (Fils)	28.4	14.8	53.1	49.9	46.7



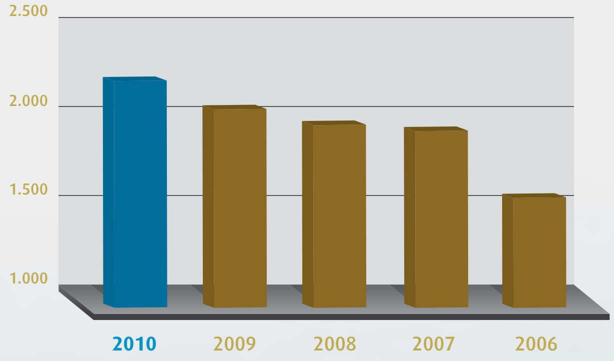
Net Financing and Interest Income KD Million



Financing Receivables and Loans KD Million



Total Assets KD Million



Total Deposits KD Million

BOARD OF DIRECTORS

Hamad A/M Al-Marzouq
Chairman and Managing Director and Chairman of the Executive Committee

Currently: Chairman, Kuwait Banking Association Kuwait; Deputy Chairman, Ahli United Bank Group Entities (A. Deputy Chairman, Ahli United Bank (B.S.C.); B. Deputy Chairman, Ahli United Bank (UK) PLC.; C. Deputy Chairman, Ahli United Bank (Egypt) S.A.E.; D. Deputy Chairman, Ahli Bank Qatar; E. Deputy Chairman, Ahli Bank Oman; F. Deputy Chairman, Commercial Bank of Iraq); Deputy Chairman, United Bank for Commerce & Industry; Board Director, Kuwait & Middle (A. Board Member, Kuwait & Middle East Financial Investment Company Kuwait; B. Board Member, Middle East Financial Investment Company Kingdom of Saudi Arabia); Board Director, Institute of Banking Studies Kuwait; Board Director, Public Authority for Higher Education & Training Kuwait; Board Director, Union of Arab Banks Lebanon.

Formerly: Director, Board of Trustees - Arab Academy for Banking & Financial Sciences; Manager Supervision Sector - Central Bank of Kuwait; Investment Officer - Kuwait Investment Company.

Sheikh Abdulla Jaber Al-Ahmad Al-Sabah
Vice Chairman and Member of the Executive Committee

Currently: Deputy Director General - Investment, Public Institute for Social Security (Kuwait); Chairman - Housing Finance Company (Kuwait); Vice Chairman Bank of London & Middle East (FSA Regulated - UK)

Formerly: Chairman - Kuwait Financing Services Co. (Kuwait); Board Member - Ahli Bank of Kuwait; Vice President - Wafra Investment Advisory Group (New York - USA); Manager Securities Department & Head of Private Equity - Public Institute for Social Security (Kuwait); Portfolio Manager specializing in U.S. & Japanese Equities - Public Institute for Social Security (Kuwait); Board Member - Global Investment House (Kuwait)

MOHAMMED SALEH BEHBEHANI
Director and Member of the Executive Committee

Currently: Partner & President, Mohammad Saleh & Reza Yousuf Behbehani Co; Partner, Mohammad Saleh Behbehani & Co. W.L.L.; Partner & President, Shereen Travels, Kuwait.; Partner, Behbehani Bros., W.L.L,Bahrain.; President, Shereen Real Estate Co.; Chairman, Maersk Kuwait Co. W.L.L.; Chairman, Kuwait Insurance Co. S.A.K.; Partner & President, Behbehani Jeep Motors Co. W.L.L.; President, Shereen Investment Co.; Chairman, Maersk Logistics Co. W.L.L.; Vice Chairman, United Beverage Co.; Director, Bank of Kuwait & the Middle East, K.S.C.; President, Shereen Motor Co.W.L.L.; Director, ahli united bank B.S.C. (Bahrain); President, Behbehani Automall Co. W.L.L.; Partner, Al Mulla & Behbehani Motor Co. W.L.L.

Formerly: Former Director, Purchase & Imports, Public Works Dept., Govt. of Kuwait; Former Deputy Chairman, Al Ahli Bank of Kuwait K.S.C.; Former Director, Swiss Kuwaiti Bank.; Former Director, UBAF (Hong Kong) Limited.

Adel A. El-Labban
Director and Member of the Executive Committee

Currently: Group Chief Executive Officer and Managing Director, Ahli United Bank BSC, Bahrain; Director, Ahli United Bank (UK) PLC; Director, Bank of Kuwait & the Middle East KSC, Kuwait; Director, Ahli Bank QSC, Qatar; Director, Ahli United Bank (Egypt) SAE, Egypt; Director, Ahli Bank SAOG, Oman; Director, Commercial Bank of Iraq, Iraq; Director, Kuwait & Middle East Financial Investment Co. (KMEFIC), Kuwait; Director Middle East Financial Investment Co. (MEFIC), Saudi Arabia; Director, United Bank for Commerce & Investment S.A.L, Libya; Board Member, Bahrain Stock Exchange, Bahrain; Director, Bahrain Association of Banks, Bahrain

Formerly: Chief Executive Officer and Director of the United Bank of Kuwait PLC, UK; Managing Director, Commercial International Bank of Egypt, (Egypt); Chairman - Commercial International Investment Company, Egypt; Vice President, Corporate Finance, Morgan Stanley, USA; Assistant Vice President, Arab Banking Corporation, Bahrain.

HERSCHEL POST
Director and Chairman of the Audit Committee

Currently: Director and Chairman of Audit Committee, ahli united bank B.S.C. (Bahrain); Director and Chairman of the Audit Committee, Ahli United Bank (UK) plc; Director and Chairman of the Audit Committee, Ahli United Bank (Egypt) SAE.; Director and Chairman of the Audit Committee, Kuwait & Middle East Financial Investment Company (KMEFIC).Director Euroclear SA/NV & Euroclear plc; Director and Chairman of the Audit Committee, Euroclear UK and Ireland Ltd; Director, Investors Capital Trust plc.; Director and Chairman of the Audit Committee, Threadneedle Asset Management Holdings S.A.R.L.; Trustee, Earthwatch Institute (Europe).

Formerly: Deputy Chairman of the London Stock Exchange; Former CEO and Deputy Chairman, Coutts & Co.; Former Chief Operating officer, Lehman Brothers International Ltd.; Former Director, Christie's International Limited

Jamal Shaker Al Kazemi
Director and Member of the Audit Committee

Currently: Deputy Chairman – Marsa Alam Holding Company K.S.C.C. (Kuwait); Director – Zain (Kuwait); Director – National Investment Company (Kuwait); Deputy General Manager – Kazema Engineering Projects WLL (Kuwait)

Formerly: Deputy Chairman – Refrigeration Industries & Storage Company S.A.K. (Kuwait)

Bassel Gamal
Director and Member of the Audit Committee

Currently: Senior Deputy Group Chief Executive Officer, Banking Group, Ahli United Bank B.S.C, Bahrain; Director, Ahli Bank QSC, Qatar; Director, Bank of Kuwait & the Middle East KSC, Kuwait; Director, Ahli United Bank (Egypt) SAE, Egypt.

Formerly: CEO, Ahli Bank QSC, Qatar; DCEO-Risk, Finance & Operations, Ahli Bank QSC, Qatar; Deputy Group Head of Risk Management, Ahli United Bank, Bahrain; Senior Manager Corporate Banking Commercial International Bank (Egypt); Board Member, Ahli United Bank Finance Company, Egypt.

Sanjeev Baijal
Director and Member of the Executive Committee

Currently: • Deputy Group CEO – Finance and Strategic Development Ahli United Bank, (Bahrain); Director – Ahli Bank S.A.O.G. (Oman); Director - AUB Investments (Cyprus Ltd.); Deputy Chairman - Legal & General Gulf BSC (c) / Legal & General Gulf Takaful BSC (c), (Bahrain).

Formerly: Director, Kuwait & the Middle East Investment Co., (Kuwait).

EXECUTIVE MANAGEMENT

Ahmed Mohamed Zulficar
Deputy Chief Executive Officer - Risk, Compliance, Finance, IT & Operations

Sherief El-Kholy
Acting Deputy Chief Executive Officer - Retail Banking

Medhat Fouad Tawfik
AGM Private Banking & Wealth Management

Waleed Sayed Abdulkarim
Acting Deputy Chief Executive Officer - Corporate Banking Commercial Banking & Treasury

Iman Wajeeh Al-Madani
Group Head of Human Resources & Development

Tanu Goel
Head of Audit

In view of the underlying role played by corporate governance in the world today, the Bank corporate governance policy is based on several pillars, the most significant of which is displayed in the precise determination of the essential role assumed by the Board of Directors, its duties and responsibilities, and to secure carrying out duties within entire transparency and disclosure parameters, safeguard shareholders' equity, protect customers, personnel and relevant parties rights, along with the active support to the internal and external audit and Risk Management functions.

As such, the Board of Directors is responsible for the overall corporate governance issues in the Bank, including strategies, directions to the senior management and ensure the availability of effective control and best international practices, along with the necessary directives to the Management performance in accordance with the stipulated standards. The Board of Directors formed three sub-committees to help it carry out these functions, as follows:

Board Committees

Executive Committee: This Committee studies the issues usually handled by the Board members. It assumes all responsibilities vested in it by the Board. It focuses on credit and market risk issues, etc.

Audit & Compliance Committee: This Committee provides support to the Board on accounting policies, internal audit, compliance procedures, financial reporting and liaison with regulators, the Kuwait Stock Exchange and external auditors.

Compensation Committee: This Committee assists the Board to setup rules on staff benefits and recommend remunerations to Directors which should be approved by shareholders at the Annual General Assembly.

Board of Directors

Executive Committee | **Audit Committee** | **Compensation Committee**

Integrated Package of Committees

The Bank Management monitors the performance on an ongoing basis and provides recommendations to the Board. Performance is monitored through a periodic appraisal of the performance levels compared with budgets, the preceding periods and peer banks in several market sectors. This role is enhanced by collective active committees.

Management Committee is the main forum which secures an official framework for the active recommendations and transparent decision making by the Senior Management on cross-organizational issues, such as strategies, budgets, performance, operational, personnel, and compliance. This Committee is chaired by the Chairman and Managing Director and comprises all Chief Executive Officer (CEO) deputies.

Assets and Liabilities Committee (ALCO) identifies, inspects and manages liquidity, market risk, and the Bank funding strategy. This Committee comprises the Chairman and the Managing Director, the CEO Deputies, Treasurer, Risk Department Head, heads of business departments and Head of Financial Department.

Risk Management Committee (RMC) reviews and manages the Bank overall risk management process, as well as management policies on market risks, operational, legal and compliance risks. RMC inspects the capital adequacy standard in relation to the Bank risk profile. RMC is mandated to provide clear guidance in respect of operational risk self assessment process and review the Bank Disaster Recovery and Business Continuity Plans.

Credit Committee and the **Senior Credit Committee** review and approve credit and investment applications and recommend adjustments to credit policies, including endorsement of maximum limits for sectoral and sovereign financing.

Credit Evaluation and Classification Committee. This Committee reviews and approves credit facilities for each obligor independently and evaluates them, in order to secure classification of irregular credit facilities with view of the Bank risk profiles and decides upon the standards of classification and allocation of provisions in accordance with the Central Bank of Kuwait regulations.

Comprehensive Governance Matrix

Along with the functions assumed by the Board committees and the other committees, the Board of Directors endorsed a number of policies which reached in excess of 30 policies covering all aspects concerning the Bank business. Such policies are reported to all the Bank staff to act as per their directives and to secure the entire transparency and harmony of duties carried out by the Bank departments.

To stress the Bank adherence to the Corporate Governance regulations, the Board of Directors relies upon continued revision carried out by internal and external auditors covering the internal control functions aimed at identification of the points of weakness and the remedial actions taken towards them. Such revisions help the Management set up protective plans for mitigating the impacts of crises. Worth mentioning, the Bank maintains sufficient insurance coverage and emergency plans in event of shutdown of systems. This covers the support systems and maintaining backups for records of data and information outside the Bank.

The Board of Directors and the Management are confident that these high standards of the Bank Corporate Governance shall continue to enhance the Bank performance and maximize shareholders' equity on the long run. This will result in enhancement of shareholders confidence, regulators, the world credit rating agencies as well as the Bank staff members.

The Bank vision based on "United with you" assembled with "Sharia'a & Pleasant Treatment" after converting Bank's activities to become compliant with the principles of Islamic Sharia'a reflect its sustainable methodology in expending utmost efforts to render the best quality services to customers, whereas the Bank endeavors to change the concept to banking services from a sheer routine job to building a persistent relation with customers based in essence on understanding the customer needs and lending support to achievement of his objectives, along with securing swift, active and convenient solutions to his various financial needs.

The Bank vision based on "Making Life Simple" reflects its sustainable methodology in expending utmost efforts to render the best quality services to customers, whereas the Bank endeavors to change the concept to banking services from a sheer routine job to building a persistent relation with customers based in essence on understanding the customer needs and lending support to achievement of his objectives, along with securing swift, active and convenient solutions to his various financial needs.

Private Banking and Wealth Management

Despite yet another challenging year, private banking managed to position itself positively and successfully in 2010, amidst the slowly recovering financial markets. Most notably, the department managed to sail through the crucial period of the bank's conversion from a conventional bank to a modern Islamic bank achieving all the milestones, in a timely manner. The division managed to successfully convert its accounts, deposits and facilities to be Shariah compliant, while providing its usual high standard and quality of services, ensuring our clients were not affected by the change. This smooth transition was supported by a professional and proactive approach, where continuous communication and transparency with our clientele played an integral role in the success of the conversion.

During the year, private banking has also focused on significantly increasing cross border services within the 'Ahli United Group' network, ensuring accessibility to our services for clients traveling to or residing in other countries (AUB locations such as Bahrain, Qatar, Oman, Egypt and London). Providing our unprecedented onshore and offshore service has helped capture the trust and loyalty of our customers successfully across the Group.

Further, we continue to provide through our dedicated and qualified relationship managers excellent offerings in wealth management and advisory services. On our platform is an array of services and target driven advice on investments, tax and insurance, asset protection and trust formation. Portfolio analysis and diversification are also recommended in order to minimize customers risk and maximize their returns.

In response to the competitive environment, innovative Shariah complaint investment products and services were tailor-made to meet the increasing financial appetite of our clients. Additionally, the staff at private banking has undergone intensive training on Islamic financial techniques and transactions and continues to enhance their competency by participating in various training and certification programs.

Corporate Banking

During 2010, Corporate Banking achieved continued growth despite the on-going repercussions of the market downturn given its historical strong ties with corporate clients, customized service, a larger accessible client base post our Conversion to a Sharia Compliant Institution, AUB Group's extended range of services and alliances in the many countries in which it has presence, and the diverse pool of offered Sharia Compliant Products. These products include, but are not limited to:

- Murabaha Foreign & Local
- Ijara Sale Lease Back and Lease to Own – Real Estate & Other Assets
- Istisna'a
- Tawarouq Commodities
- Wakala for Investment with the Right to Contract with Self
- Musharaka
- Wakala based Investment Deposits
- Modaraba based Investment Deposits

Moreover, Corporate Banking succeeded in maintaining a high asset corporate portfolio given the pre-emptive measures initiated early on and the timely response to market and company specific challenges; the selection of financially sound corporate clients within the commercial, industrial, and contracting industries; along with Bank's stringent review and approval policies.

Corporate Banking further continued to strengthen its staff with professionals of Islamic Banking Experience from some of the best Islamic Institutions in the Region with the end intent of offering our valued customers with the best financial solutions to their specific business requirements in line with the Principles of Islamic Sharia, be it debt or equity participation deals, whilst promoting a high level of transparency, security, and satisfaction. We are further keen on an active contribution to Islamic Banking in the Region's and the State's Banking Sector.

In line with the directives of the Central Bank of Kuwait and the State of Kuwait's Four-Year Development Plan, Corporate Banking has taken an active part in supporting a good number of deals and projects floated by the Government during 2010. Corporate Banking has further embarked on a number of real estate development projects which we are proud to add to our name.

It is our intent to continue to have a pioneering role in the active support of our clients' full banking requirements by offering financial advisory and Sharia compliant products that would ensure the growth and success of our clients in their respective industries and to have an active contribution to the State's plans to transform Kuwait into a major financial and commercial hub.

Treasury Division

Year 2010 was a turning-point for the Treasury Division and for AUB in general, where the bank has converted from a conventional bank into a bank operating in accordance with Islamic Sharia'. The Treasury Division managed to complete efficiently the conversion process within the Division professionally and smoothly. The Treasury activities have not been affected by the conversion process. On the contrary the Treasury has been able to meet all of the bank's needs in terms of financial liquidity, efficient service for the Bank's customers, as well as maintaining the distinguished solvency of the bank in the Kuwaiti market.

It is worth mentioning that the Treasury Division has been able to maintain all its customers after the conversion into the Islamic operation. The Treasury Division has further established new banking partnerships after the conversion.

Despite the ongoing global financial crisis, the Treasury was able to meet efficiently all the liquidity requirements of the bank.

Retail Banking

With the successful conversion in 2010 from a traditional bank into a bank operating in accordance with Islamic Sharia', Retail Banking played an instrumental role in the conversion process. This role does not only cover the readiness for the conversion at the front end with customers. This entails the different channels from branches, call center to electronic banking. Yet, Retail Banking took up the support roles in the back end which covers an array of activities. These activities include testing of new products and services, setting up of new polices and procedures and the execution of marketing plans.

The year 2010 success was supported by the previous years Retail Banking's efforts in strengthening the long term relationship with customers. The majority of existing customers welcomed the conversion based on the strong loyalty with the Bank. This bond has been rewarding to the customers with the competitive returns on the Mudaraba investment accounts. The announced returns or profits rates were communicated through the print media on a quarterly bases for both the Mudaraba investment saving and deposit accounts. Also, the offer of new banking products to the market post conversion have proved the Bank's ability in providing to its customers innovated products as Al Hassad Islamic draw accounts and Al Tharwa saving accounts.

Retail Banking maintained its growth strategy through the branch network and channels, by increasing the number of branches to 28 branch along with the renovation of the medium and large branches to service separately the male and female customers. The number of ATMs reached 60 machines distributed in different areas in Kuwait. This has aided the branches to be more capable to respond to the increasing traffic of customers.

To capitalize on the unique position held by the Bank post the conversion, Retail Banking setup campaigns, not only to encourage existing customers to hold more funds, but as well as to attract new customers in the Islamic Banking market. The last of such successful campaigns was the innovative offer of Qard Al Hassan (financing with out profit) to targeted customers in return for the transfer of their salaries to the Bank. This campaign was the talk of town for the last quarter of 2010.

All retail staff were trained on all of the new Shriaa compliant products and services with additional efforts and time exerted to evaluate their knowledge in a simulated branch environment through role plays. The Bank's call center working around the clock made sure that customers receive the best and highest rated service levels regardless of their whereabouts in Kuwait or abroad. Ebanking team reconstructed the Bank's website with the highest standards.

The growth plan during 2010 realized positive outcomes, despite the ongoing global financial crisis affecting the region with in all its sectors, new customer acquisitions were accomplished. On the liability side, the competitive Mudarabah accounts profit rates announced at the end of each quarter increased the market confidence in the Bank's ability to steer the customers' funds shrewdly and successfully. Retail Banki ng lead the Bank in the growth of Mudarabah balances through out 2010. This is in addition to the increasing growth of balances in the first draw account in accordance with Islamic Sharia' " Al Hassad Al Islami ".On the asset side, Retail Banking synchronized the first Islamic financing campaign through a Mousawama tool. The campaign entailed the purchase of Toyota Camry from the local agent "Al Sayer" and selling its to the customers through Mousawama financing . The campaign was successful for which other campaigns would follow as opportunities arise.

In essence, 2010 has been marked not only the year of successful conversion of Retail Banking towards Islamic Banking, but also, the ability to compete and attract new customers in a sector which is dominant by market leaders for over the past three decades.

Risk Division

1. General

In 2010 the world economy continued to reel from the aftermath of the financial crisis. Volatility remains high, especially due to concerns regarding the financial health of several sovereign and quasi-sovereign entities, some of which are in our region. In addition, we witnessed the speed and extent of the interconnectedness of such volatility.

Against this backdrop and the challenge posed by the Bank's conversion from conventional to Islamic banking, Risk Management Division endeavoured to increase the level of robustness in the assessment and management of risks.

2. Key Messages/Achievements

Credit Risk had a more proactive approach to risk assessment and management. Among the major achievements are the following:

- Conservative strategies and policies in management of key risks faced by the Bank resulted in managing the crisis without significant impact on our business in terms of employment of the cash resources and their direction to the productive economic sectors.
- Precise monitoring approach of exposures that could be more susceptible to the repercussions of the world financial crisis with the accurate study of their credit positions.
- Periodic sensitivity tests were made for measuring the economic impacts on the components and quality of the credit portfolio.
- Vulnerable and criticized accounts are handled by a specialized unit.
- Owing to the fact that availability of precise and prompt data are deemed essential for taking sound resolutions, the Bank dedicated the special unit for submission of reports and data required on credit risks and its components according to concentration by sector, credit classification, collaterals and all detailed present and comparative data that are regularly submitted either to the regulators or management for taking convenient resolutions.

Market and Operational Risk had a more proactive approach to risk assessment and management. Among the major achievements are the following:

- Continues updating of Risk Management, Internal Capital Adequacy Assessment, Stress Testing and Risk Framework policies/procedures to ensure regulatory and Sharia'a compliance and consistency with the Bank's overall risk appetite.
- Robust monitoring of exposure to market risk, measured by latest techniques including Value at Risk (VaR) on the trading portfolio and ensuring that the resulting VaR is within the limit sanctioned by the Board.
- More defined roles and responsibilities for Market Risk.
- Successful Business Continuity Testing and Disaster Recovery using the Bank's systems for Islamic banking and core operating systems.
- Successful branch off-host testing
- Successful evacuation drills
- •Closer coordination with the business units for the identification, assessment and management of operational (including fraud) risks.
- Expanding the scope of capital adequacy measurement and management through periodic stress-testing given the Islamic nature of the Bank
- Active participation from Market Risk for the implementation of OPICs Plus

3. Customer Service

The internal customers for Credit Risk are the business development units (e.g. Corporate Banking, Private Banking and Retail Credit). For Market Risk it is the Treasury Division and for Operational Risk, it is the entire bank itself, i.e., all the business units. Our level of interaction with these internal customers was raised further due to the challenges of the business environment and as we endeavor to contribute our fair share in the overall improvement of the risk governance of the Bank.

4. Team Working

Risk Management Division is customer-driven. It has always been our philosophy to add value to the business of all our internal customers. The bank emphasize the message that we are a resource at their disposal.

For credit risk, the management of such credit risk shall remain the main corner in the credit granting policies, whereas credit risks will continue to be managed with entire independence from the business development units. The same quality of independence could be said of Market and Operational Risk.

5. Staff Issues

We have always taken keen interest in improving the level of professionalism. Staff have been requested to attend relevant workshops and presentations. In addition, they are exposed to other areas via cross-training so that the knowledge stock is fairly distributed and to reduce overreliance on any single individual.

Information Technology

AUB continues to deploy modern technology as a strategic tool to gain competitive advantages and to improve both productivity and efficiency of the organization. Our investments in appropriate technologies are to create new business offerings, enhanced systems performances, which provide our customers the state-of-art systems of international standards.

In 2010, AUB evolved into an Islamic Bank, significant investments were made in new systems to effectively facilitate the transition from a conventional to an Islamic Bank. The new Islamic banking systems have been integrated with the existing ones and now provide the capability to swiftly deliver customized Islamic products. The entire conversion project was successfully completed within a record time.

The emphasis on an enterprise view of technology has led to an architecture that is highly geared towards the changing business environment. Our platforms are designed to service scalability and are capable of handling high customer and transaction volumes. We have used technology to deliver process improvements, a spectrum of innovative and value added products aligned towards meeting our customer needs effectively, through improved efficiency and service quality which is our core objective.

We have strengthened our security framework in the delivery channels, effective steps have been taken to prevent online security threats such as phishing, frauds and identity thefts. By adopting international security system standards, all card based transactions are now end-to-end secure as per recommended industry standards. AUB is the 1st bank in Kuwait to receive the international recognized PCI DSS certification.

We continue to upgrade our branch network, with the branch as an integrated sales and service point for our wide range of retail products and services. This is complemented by innovation in technology-driven channels to enhance choice and convenience for our customers.

During fiscal 2010, technology initiatives resulted in more flexible and cost-efficient solutions. Development and integration of common global AUB group wide IT solutions is on going. Given the fact that our systems are used on a 24x7 basis, we initiated a re-architecture of our Disaster Recovery and Business Continuity Centers with add-ons to reduce application multiplicity, facilitate maintenance, improve fallbacks and de-risk operations. Initiatives were also undertaken to consolidate many existing applications and virtualized the data centre technology assets.

Human Resources

Throughout 2010 AUB aimed and successfully managed to attract highly qualified and experienced Kuwaiti employees working in the Islamic Banking Sector, while increasing at the same time the ratio of Kuwaiti employees to fulfill the required percentage and Kuwaitization ratio.

Through the well established Assessment Center, the first Evaluation Centre among local banks, the bank has evaluated and selected superlative human resources and talent from the national cadres according to job requirements. These selected national cadres were and still are closely followed up and provided continuously with training.

Human Resources Division always strives to create a professional convenient work environment through practical and reality-simulating models. This matter was one of Human Resources Division's major objectives in 2010, which has been positively reflected on the enhancement of our Bank staff's performance level, raising their functional competencies and guiding them to follow the Islamic Sharia principles and behavior.

In our relentless endeavor to complete the work in a spirit of innovation and creativity, the content of our training plans is focused on banking operations and performance efficiency.

AUB policies and procedures were reviewed and updated according to Islamic Sharia and the Kuwait Private Sector Labor Law No. 6 of 2010. Also, these policies have been put into force to ensure compliance with the Ministry of Labor and Social Affairs' Law.

Striving to develop our staff skills, knowledge and expertise, and through our dedicated human resources team, we managed to complete an integrated training plan in Islamic financial operations, covering AUB's practical needs, activities, transactions and regulations, in order to consolidate the information already acquired. We have a library within a Bank's internal network folder contains all training materials as a reference for review by all staff.

Development and training of our staff, and attracting the distinguished national cadres will continue to support our current and continuous objective through year 2010, in accordance with the provisions of Islamic Sharia.

Quality Assurance Control

Focusing on being the best in Service Quality throughout 2010, QA dept. have proactively succeeded to be always prepared for changes and/or challenges that would improve Service quality. Such focus lead to exceeding all expectations and leaving AUBK customers with a positive experience when using any of AUBK's alternative channels.

QA's main objective was to seek opportunities for improvements relying on customer's feedback. QA dept., have focused on ways to gather customer feedback, as QA team believed that " feedback " and proper communication are the key factors to Service excellence. "We care"project was implemented as one of QA's strategies to gather customer's feedback in a more flexible way at the customer's convenience. "We care" project emphasized on, opening alternative gateways for customers to be heard. Customers can use branches, " Hayakom AUB" and AUBK website to submit their feedback." We care"is designed to accommodate any type of feedback where customers may submit a complaint, a suggestion and/or a comment using the "We care" forms.

Focusing on these objectives, Quality Assurance Dept. adopted an objective of strengthening the communication between customers and the Bank through the implementation of the "We Care" project, which allows customers to effectively express their opinions and brainstorm improvement ideas for the Bank interest. This in effect renders all channels open for the customer to take part in the Bank improvement process either through his physical visit to any of AUB's branches or while using any of AUB's online or telephone outlets.

"We care" feedback resulted in a number of process improvement projects resulting in improved turnaround time. Moreover, other initiatives were taken to improve communication from and to customers that really made a difference. Some of the tools used to improve Service quality were: Automation, Procedural Enhancement, and Intensive Service Quality Training.

Quality Assurance Dept. has arranged for a communicative meeting between Top Management members and Quality Assurance staff to directly communicate the Bank's main objective. This was made with the view of eliminating barriers and protocols, along with promoting the team-spirit culture which would be reflected in the achievement of the ultimate objective of each participant in the meeting. Thus, the teamwork culture and harmony is maintained.

In order to achieve even higher levels of service excellence, Quality Assurance Dept. has improved its service standards to offer AUB's customers a unique experience that promotes AUB's distinguished status. In 2010, Quality Assurance Dept. continued to make more developmental achievements with the objective to further improve services through the application of new service standards, and increasing employees' awareness of the importance of service quality. In addition, improvement workshops were held by QA dept. for the Bank's newly hired employees, and advanced courses were also conducted to increase such awareness and stimulate their positive thinking.

With the conversion of AUB to Islamic banking system, Quality Assurance Dept. being the custodian of all AUB's policies & procedures have ensured that all divisions update their respective policies& procedures to comply to the conversion before Ahli Islamic United Bank starts its first day of business.

QA Dep. perceives complains as free of charge gifts from customers, thus handles them positively. QA Dep. holds such complaints as opportunities to help AUBK improve and implement the quantum leap for the enhancement of services in general and products in particular. In support of this culture, Quality Assurance Dep. endeavored to provide positive support and disseminate the culture of availing all improvement opportunities and using creativity to find appropriate solutions to each case. Quality Assurance Dep. launched an awareness campaign to encourage all staff to deal positively with customer complaints so as to reverse path of complaint from just a negative reaction into a precious opportunity leading to further development exceeding all expectations and increasing customer satisfaction and loyalty.

In line with AUBK optimal Objective to be the best in Service Quality , QA ended 2010 by promoting solution oriented employees who accept challenges positively and launched the Service Quality optimal thinker campaign where employees seeking improvements and looking for solutions are called Service Quality optimal thinkers. QA believes that SQ optimal thinker campaign would help achieving the ultimate objective of AUBK.

Corporate Social Responsibility

The Bank adopts an integrated Corporate Social Responsibility policy (CSR) which reflects its deep devotedness to provide care to all relevant parties. Such care is not confined to the Bank shareholders, its customers and personnel but it extends to local community; yet to the international community.

As such, the Bank has a strong conviction that it is a part of the community it serves. The Bank, thus pays great concern to its social programs. In the year 2009, the Bank continued encouraging summer training to Kuwaiti newly graduates and lent active contribution in support of the local community through financing a number of charity acts.

CONSOLIDATED
FINANCIAL STATEMENTS

CONSOLIDATED FINANCIAL STATEMENTS

Contents

INDEPENDENT AUDITORS' REPORT

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TO THE SHAREHOLDERS OF AHLI UNITED BANK K.S.C.

(FORMERLY THE BANK OF KUWAIT AND THE MIDDLE EAST K.S.C.)

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of Ahli United Bank K.S.C. (formerly The Bank of Kuwait and The Middle East K.S.C). (the "Bank") and its subsidiaries (collectively ''the Group'') which comprise the consolidated balance sheet as at 31 December 2010, and the related consolidated statements of income, comprehensive income, changes in equity and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as of 31 December 2010, and its financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted for use by the State of Kuwait.

Report on Other Legal and Regulatory Requirements

Furthermore, in our opinion proper books of accounts have been kept by the Bank and the consolidated financial statements, together with the contents of the report of the Bank's Board of Directors relating to these consolidated financial statements, are in accordance therewith. We further report that we obtained all the information and explanations that we required for the purpose of our audit and that the consolidated financial statements incorporate all information that is required by the Capital Adequacy Regulations issued by Central Bank of Kuwait as stipulated in CBK Circular number 2/RBA/44/ 2009 dated 15 June 2009, as amended, Commercial Companies Law of 1960, as amended, and by the Bank's Articles of Association, that an inventory was duly carried out and that, to the best of our knowledge and belief, no violations of Capital Adequacy Regulations issued by the Central Bank of Kuwait as stipulated in CBK Circular number 2/RBA/44/ 2009 dated 15 June 2009, as amended, Commercial Companies Law of 1960, as amended, nor of the Articles of Association have occurred during the year ended 31 December 2010 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 2010 and based on the Bank's Sharia'a Board report issued for the period from 1 April 2010 (date of commencement of operations as an Islamic bank) to 31 December 2010, we are not aware of any violations of the fatwas and rulings of the Bank's Sharia'a Board.

JASSIM AHMAD AL-FAHAD

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Al-Aiban, Al-Osaimi and Partners

12 January 2011
Kuwait

CONSOLIDATED STATEMENT OF INCOME

Year ended 31 December 2010

	Notes	31 December 2010 KD 000	31 December 2009 KD 000
Financing income		**72,901**	-
Interest income	3	**27,530**	109,350
Distribution to depositors	4	**(29,968)**	-
Interest expense	4	**(10,788)**	(51,817)
Net financing and interest income		**59,675**	57,533
Net fees and commission income	5	**10,291**	14,468
Foreign exchange gains		**3,432**	3,879
Net gain on sale of investments	6	**2,944**	8,062
Share of results from associate	14	**209**	(244)
Dividend income		**314**	1,303
Other income		**529**	47
Total operating income		**77,394**	85,048
Provision and impairment losses	7	**(24,493)**	(47,071)
Operating income after provision and impairment losses		**52,901**	37,977
Staff costs		**16,511**	17,087
Depreciation		**3,024**	2,336
Other operating expenses		**8,998**	8,313
Total operating expenses		**28,533**	27,736
PROFIT FROM OPERATIONS		**24,368**	10,241
Taxation & Zakat	8	**(1,324)**	(701)
Directors remuneration		**(75)**	-
PROFIT FOR THE YEAR		**22,969**	9,540
Attributable to:			
Bank's equity shareholders		**27,444**	14,262
Non-controlling interests		**(4,475)**	(4,722)
		22,969	9,540
Basic and diluted earnings per share attributable to the Bank's equity shareholders (fils)	9	**28.4**	14.8

The attached notes 1 to 29 form part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

Year ended 31 December 2010

	Notes	**31 December 2010 KD 000**	31 December 2009 KD 000
Profit for the year		**22,969**	9,540
Other comprehensive income:			
Revaluation of freehold land	16	**116**	(7,040)
Net movement in cumulative changes in fair values of investments available for sale	13	**5,099**	(12,595)
Exchange differences on translation of foreign operations		**(203)**	253
Other comprehensive income / (loss) for the year		**5,012**	(19,382)
Total comprehensive income / (loss) for the year		**27,981**	(9,842)
Total comprehensive income / (loss) attributable to:			
Bank's equity shareholders		**32,511**	(5,950)
Non-controlling interests		**(4,530)**	(3,892)
		27,981	(9,842)

31 December 2010	31 December 2009

The attached notes 1 to 29 form part of these consolidated financial statements.

CONSOLIDATED BALANCE SHEET

At 31 December 2010

	Notes	KD 000	KD 000
ASSETS			
Cash and balances with banks	10	**383,270**	140,357
Kuwait Government treasury bonds	11	**-**	207,101
Central Bank of Kuwait bonds	11	**-**	16,987
Certificates of deposit		**-**	10,038
Deposits with banks and other financial institutions		**327,117**	153,596
Financing receivables	12	**1,554,043**	-
Loans and advances	12	**55,943**	1,561,104
Investments available for sale	13	**50,754**	75,554
Investment in associate	14	**8,273**	8,231
Investment properties	15	**-**	8,541
Premises and equipment	16	**48,062**	46,176
Other assets and intangibles	17	**26,875**	32,848
TOTAL ASSETS		**2,454,337**	2,260,533
LIABILITIES AND EQUITY			
LIABILITIES			
Deposits from banks and other financial institutions		**859,715**	527,777
Deposits from customers	18	**1,287,527**	1,460,255
Other liabilities	19	**41,800**	35,165
		2,189,042	2,023,197
EQUITY			
Share capital	20	**107,323**	97,566
Reserves	20	**182,313**	159,550
		289,636	257,116
Treasury shares	21	**(43,957)**	(43,957)
Attributable to Bank's equity shareholders		**245,679**	213,159
Non-controlling interests		**19,616**	24,177
		265,295	237,336
TOTAL LIABILITIES AND EQUITY		**2,454,337**	2,260,533

Hamad Abdul Mohsen Al-Marzouq
Chairman & Managing Director

Sh. Abdullah Jaber Al-Ahmed Al-Sabah
Vice Chairman

Attributable to Bank's equity shareholders

The attached notes 1 to 29 form part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

Year ended 31 December 2010

			Reserves										
	Share capital KD 000	Share premium KD 000	Statutory reserve KD 000	General reserve KD 000	Retained earnings KD 000	Cumulative changes in fair values KD 000	Property revaluation reserve KD 000	Treasury shares reserve KD 000	Foreign currency translation reserve KD 000	Total reserves KD 000	Treasury shares KD 000	Non controlling interests KD 000	Total KD 000
Balance as at 31 December 2009	**97,566**	**12,883**	**45,844**	**22,660**	**56,163**	**9,994**	**11,041**	**974**	**(9)**	**159,550**	**(43,957)**	**24,177**	**237,336**
Profit for the year	-	-	-	-	27,444	-	-	-	-	27,444	-	(4,475)	**22,969**
Other comprehensive income / (loss) for the year	-	-	-	-	-	5,052	116	-	(101)	5,067	-	(55)	**5,012**
Total comprehensive income / (loss) for the year	-	-	-	-	27,444	5,052	116	-	(101)	32,511	-	(4,530)	**27,981**
Bonus shares issued – 2009	9,757	-	-	-	(9,757)	-	-	-	-	(9,757)	-	-	-
Other movements	-	-	-	-	9	-	-	-	-	9	-	(31)	**(22)**
Transfer to reserves (Note 20)	-	-	2,885	-	(2,885)	-	-	-	-	-	-	-	-
Balance as at 31 December 2010	**107,323**	**12,883**	**48,729**	**22,660**	**70,974**	**15,046**	**11,157**	**974**	**(110)**	**182,313**	**(43,957)**	**19,616**	**265,295**
Balance as at 31 December 2008	**88,696**	**12,883**	**44,348**	**22,660**	**76,224**	**23,293**	**18,081**	**974**	**(136)**	**198,327**	**(43,957)**	**28,826**	**271,892**
Profit for the year	-	-	-	-	14,262	-	-	-	-	14,262	-	(4,722)	**9,540**
Other comprehensive income / (loss) for the year	-	-	-	-	-	(13,299)	(7,040)	-	127	(20,212)	-	830	**(19,382)**
Total comprehensive income / (loss) for the year	-	-	-	-	14,262	(13,299)	(7,040)	-	127	(5,950)	-	(3,892)	**(9,842)**
Dividend – 2008	-	-	-	-	(23,957)	-	-	-	-	(23,957)	-	-	**(23,957)**
Bonus shares issued – 2008	8,870	-	-	-	(8,870)	-	-	-	-	(8,870)	-	-	**-**
Other movements	-	-	-	-	-	-	-	-	-	-	-	(757)	**(757)**
Transfer to reserves (Note 20)	-	-	1,496	-	(1,496)	-	-	-	-	-	-	-	**-**
Balance as at 31 December 2009	**97,566**	**12,883**	**45,844**	**22,660**	**56,163**	**9,994**	**11,041**	**974**	**(9)**	**159,550**	**(43,957)**	**24,177**	**237,336**

The attached notes 1 to 29 form part of these consolidated financial statements.

31 December 2010 31 December 2009

CONSOLIDATED STATEMENT OF CASH FLOWS

Year ended 31 December 2010

	Notes	KD 000	KD 000
OPERATING ACTIVITIES			
Profit for the year		**22,969**	9,540
Adjustments for:			
Net gain on sale of investments available for sale		**(946)**	(8,062)
Share of results from associate	14	**(209)**	244
Dividend income		**(314)**	(1,303)
Depreciation		**3,024**	2,336
Provision and impairment losses	7	**24,493**	47,071
Loss on sale of investment properties	6	**364**	-
Operating profit before changes in operating assets and liabilities		**49,381**	49,826
Changes in operating assets/ liabilities:			
Kuwait Government treasury bonds		**207,101**	49,971
Central Bank of Kuwait bonds		**16,987**	18,956
Certificates of deposit		**10,038**	3,760
Deposits with banks and other financial institutions		**(173,521)**	(110,172)
Financing receivables and loans		**(55,436)**	(116,151)
Other assets and intangibles		**2,508**	14,067
Deposits from banks and other financial institutions		**331,938**	44,506
Deposits from customers		**(172,728)**	27,744
Other liabilities		**4,123**	(15,037)
Net cash from / (used in) operating activities		**220,391**	(32,530)
INVESTING ACTIVITIES			
Purchase of investments available for sale		**(9,547)**	(5,065)
Sale and redemption of investments available for sale		**28,372**	31,708
Purchase of premises and equipment		**(4,794)**	(5,780)
Dividends received		**314**	1,303
Sale / (purchase) of investment properties		**8,177**	(8,541)
Net cash from investing activities		**22,522**	13,625
FINANCING ACTIVITIES			
Dividend paid to shareholders		**-**	(23,957)
Net cash used in financing activities		**-**	(23,957)
NET INCREASE / (DECREASE) IN CASH AND BALANCES WITH BANKS		**242,913**	(42,862)
Cash and balances with banks at 1 January		**140,357**	183,219
CASH AND BALANCES WITH BANKS AT 31 DECEMBER	10	**383,270**	140,357

The attached notes 1 to 29 form part of these consolidated financial statements.

1. INCORPORATION AND ACTIVITIES

Ahli United Bank K.S.C. (formerly The Bank of Kuwait and the Middle East K.S.C.) ("the Bank") is a public shareholding company incorporated in Kuwait in 1971 and is listed on Kuwait Stock Exchange. It is engaged in carrying out banking activities in accordance with Islamic Sharia'a and is regulated by the Central Bank of Kuwait. Its registered office is at Darwazat Al-Abdul Razzak, P.O. Box 71, Safat 13001, Kuwait.

After receiving the final approval from the Central Bank of Kuwait, shareholders and other regulatory authorities to convert its business to an Islamic bank in accordance with Islamic Sharia'a, an extraordinary general assembly meeting of the Bank held on 28 March 2010 approved the amendments of Articles of Association of the Bank to convert its business in accordance with Islamic Sharia'a and to change the name of the Bank to Ahli United Bank K.S.C. As a result the Bank has converted its conventional banking products into Islamic banking products after negotiation and agreement with its customers.

The Bank has commenced operations as an Islamic bank from 1 April 2010. From that date, all activities are conducted in accordance with Islamic Sharia'a, as approved by the Bank's Fatwa and Sharia'a Supervisory Board.

The Bank is a subsidiary of Ahli United Bank B.S.C, a Bahraini bank ("the Parent"), listed on the Bahrain and Kuwait Stock Exchanges.

The Bank's principal subsidiary is Kuwait and Middle East Financial Investment Company K.S.C. (Closed) (KMEFIC), a company incorporated in the State of Kuwait, listed on Kuwait Stock Exchange and engaged in investment and portfolio management activities for its own account and for clients. The Bank held 50.18% effective interest in KMEFIC as at 31 December 2010 (2009: 50.12%).

The consolidated financial statements comprise the financial statements of the Bank and its subsidiaries ("the Group").

The consolidated financial statements for the year ended 31 December 2010 were authorised for issue in accordance with a resolution of the Board of Directors of the Bank on 12 January 2011.

2. SIGNIFICANT ACCOUNTING POLICIES

2.1 Basis of preparation

The consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards (IFRS), as adopted for use by the State 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 International Accounting Standard (IAS) 39: Financial Instruments: Recognition and Measurement 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 Central Bank of Kuwait and the Bank's Fatwa and Sharia'a Supervisory Board have approved a three year time frame to convert all conventional investments and products to be Sharia'a compliant. All income and expenses for the period from 1 April 2010 to 31 December 2010 from such conventional investments and products including that from non-Sharia'a compliant subsidiary are included in the consolidated statement of income and surplus of conventional income over conventional expenses from 1 April 2010, if any, at each year end is transferred to a charity payable account and included under other liabilities. Utilization from the charity payable account is supervised by the Bank's Fatwa and Sharia'a Supervisory Board.

The consolidated financial statements are presented in Kuwaiti Dinars, which is also the functional currency of the Bank, rounded to the nearest thousand, except when otherwise indicated.

The consolidated financial statements are prepared under the historical cost convention except for the remeasurement at fair value of investments at fair value through profit or loss, investments available for sale, freehold land and derivative contracts.

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.1 Basis of preparation (continued)

Changes in accounting policies

The accounting policies are consistent with those used in the previous year except that during the year, the Group has adopted the following standards effective for annual periods beginning on or after 1 January 2010:

IFRS 3 (Revised) – Business Combinations and consequential amendments to IAS 27 – Consolidated and Separate Financial Statements. The main changes in the Group's accounting policies are as follows:

- Acquisition related costs are expensed in the statement of income in the periods in which the costs are incurred;
- Changes in ownership interest in a subsidiary that do not result in a loss of control are treated as transaction between equity holders and are accounted for within equity;
- Equity interest held prior to control being obtained are remeasured to fair value at the date of obtaining control, and any gain or loss is recognised in the statement of income.

2.2 New standards and interpretations issued but not yet effective

The following International Accounting Standards Board (IASB) Standards have been issued but are not yet effective:

- IFRS 7 Financial Instruments – Disclosures (revised): effective annual periods commencing 1 January 2011.
- IFRS 9 Financial Instruments - Classification and Measurement (Phase-1): effective annual periods commencing 1 January 2013.
- IAS 24 Related Party Disclosures (Revised): effective annual periods commencing 1 January 2011.
- IAS 32 Financial Instruments - Presentation (Revised): Classification of Rights Issues effective annual periods commencing 1 February 2010.

The application of the above standards is not expected to have a material impact on the consolidated financial statements as and when they become effective. IFRS 9 Phase-1 was issued in November 2009 and replaces the parts of IAS 39 relating to the classification and measurement of financial assets. In subsequent phases they will address impairment and hedge accounting.

The application of these standards will be made in the consolidated financial statements when these standards and interpretations become effective or are early adopted.

2.3 Basis of consolidation

The consolidated financial statements comprise the financial statements of the Bank and its subsidiaries as at 31 December each year. The financial statements of the subsidiaries are prepared for the same reporting year and using consistent accounting policies as followed by the Bank.

The financial statements of the subsidiaries are consolidated on a line-by-line basis by adding together like items of assets, liabilities, income and expenses. All intra-group balances and transactions, including unrealised gains and losses arising on intra-group transactions, have been eliminated on consolidation.

Subsidiaries are consolidated from the date on which control is transferred to the Group and cease to be consolidated from the date on which control is transferred out of the Group. The acquisition method of accounting is used to account for the acquisition of subsidiaries by the bank. Control is achieved where the Bank has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. Where there is a loss of control of a subsidiary, the consolidated financial statements include the results for the part of the reporting year during which the Group had control. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity.

Non-controlling interest represents the share of results and net assets in consolidated subsidiaries not attributable to the Group. Profit or losses attributable to non controlling interest is presented in the consolidated statement of income and within equity in the consolidated balance sheet, separately from Bank's shareholders' equity.

2.4 Use of judgement and estimates

The preparation of consolidated financial statements requires management to make judgements and estimates that affect the reported amounts of financial assets and liabilities and disclosure of contingent liabilities. These judgements and estimates also affect the revenues and expenses and the resultant provisions as well as the fair value changes reported in the equity.

Judgements are made in the classification of financial instruments based on management's intention at acquisition, i.e. whether it should be classified as financial assets at fair value through profit or loss, available for sale, or as loans and receivables. In making these judgements, the Group considers the primary purpose for which it is acquired and how it intends to manage and report its performance. Such judgements also determine whether the financial instruments are subsequently measured at amortised cost or at fair value and if the changes in fair value of instruments are reported in the consolidated statement of income or directly in equity. Judgements are also made in determination of the objective evidence that a financial asset is impaired.

In accordance with the accounting principles contained in the International Financial Reporting Standards, management is required to make estimates and assumptions that may affect the carrying values of financing receivables and loans, unquoted equity instruments classified as investments available for sale and intangible assets for the year.

Estimates are made regarding the amount and timing of future cash flows when measuring the level of provisions required for non-performing financing receivables and loans as well as for impairment provisions for investments available for sale and intangible assets. Estimates are also made in determining the useful lives of buildings and other premises and equipment and fair values of financial assets and derivatives that are not quoted in an active market.

Such estimates are necessarily based on assumptions about several factors involving varying degrees of uncertainty and actual results may differ resulting in future changes in such provisions.

The methodology and assumptions used for estimating future cash flows are reviewed regularly by the Group to reduce any differences between loss estimates and actual loss experience.

Any changes in these estimates and assumptions as well as the use of different, but equally reasonable estimates and assumptions may have an impact on carrying amounts of financing receivables and loans, unquoted instruments classified as investments available for sale and intangible assets for the year.

2.5 Financial instruments - classification, recognition & de-recognition, measurement, offsetting, and reclassification

Classification

The Group classifies its financial instruments as "investments at fair value through profit or loss", "loans and receivables", "investments available for sale" or "financial liability other than at fair value through profit or loss". Management determines the appropriate classification of each instrument at the time of acquisition.

(i) Investments at fair value through profit or loss

These are financial assets that are either financial assets held for trading or those designated as investments at fair value through profit or loss upon initial recognition. A financial asset is classified in this category only if they are acquired principally for the purpose of generating profit from short-term fluctuation in price or if so designated by the management in accordance with a documented risk management or investment strategy and reported to key management personnel on that basis. This includes all derivative financial instruments, other than those designated as effective hedging instruments.

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.5 Financial instruments - classification, recognition & de-recognition, measurement and offsetting, and reclassification (continued)

(ii) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Cash and balances with banks, Kuwait Government treasury bonds, Central Bank of Kuwait bonds, certificates of deposit, deposits with banks and other financial institutions, financing receivables and loans, and certain other assets are classified as "loans and receivables". The amount due is settled either by instalments or on a deferred payment basis.

On conversion to an Islamic bank, the Bank offers Sharia'a compliant products and services such as Murabaha, Wakala, Istisna'a, and Ijara.

Murabaha is the sale of commodities, real estate and certain other assets at cost plus an agreed profit mark up whereby the seller informs the purchaser of the cost of the product purchased and the amount of profit to be recognized.

Wakala is an agreement whereby the Group provides a sum of money to a customer under an agency arrangement, who invests it according to specific conditions in return for a fee. The agent is obliged to return the amount in case of default, negligence or violation of any terms and conditions of the Wakala.

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.

Ijara is an agreement whereby the Bank (lessor) purchases or constructs an asset for lease according to the customer's request (lessee), based on his promise to lease the asset for a specific period and against certain rent instalments. Ijara could end by transferring the ownership of the asset to the lessee.

(iii) Investments available for sale

These are financial assets either designated as "available for sale" or are not classified as fair value through profit or loss, loans and receivables, and held to maturity.

(iv) Financial liabilities other than at fair value through profit or loss

Financial liabilities which are not held for trading are classified as "other than at fair value through profit or loss". Deposits from banks and other financial institutions, deposits from customers and other liabilities are classified as "financial liabilities other than at fair value through profit or loss".

On conversion to an Islamic bank, financial liabilities include depositors' accounts created by Murabaha, Mudaraba and Wakala contracts.

Recognition and de-recognition

A financial asset or a financial liability is recognised when the Group becomes a party to the contractual provisions of the instrument. All "regular way" purchases and sales of financial assets are recognised on the settlement date, i.e. the date that the Group receives or delivers the asset. Changes in fair value between the trade date and settlement date are recognised in the consolidated statement of income or in the consolidated statement of comprehensive income in accordance with the policy applicable to the related instrument. 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.

A financial asset (in whole or in part) is derecognised either when: (i) the contractual rights to receive the cash flows from the asset have expired or (ii) the Group has retained its right to receive cash flows from the assets but has assumed an obligation to pay them in full without material delay to a third party under a ''pass through'' arrangement; or (iii) the Group has transferred its rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset. Where the Group has transferred its right to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Group's continuing involvement in the asset.

A financial liability is derecognised when the obligation specified in the contract is discharged, cancelled or expired.

Measurement

All financial assets and liabilities are initially measured at fair value of the consideration given plus transaction costs except for financial assets classified as investments at fair value through profit or loss. Transaction costs on financial assets classified as investments at fair value through profit or loss are recognised in the consolidated statement of income.

On subsequent re-measurement financial assets classified as "investments at fair value through profit or loss" are measured and carried at fair value. Realised and unrealised gains/ losses arising from changes in fair value are included in the consolidated statement of income. "loans and receivables" are carried at amortised cost using effective yield method, less any provision for impairment. Those classified as "investments available for sale" are subsequently measured at fair value until the investment is sold or otherwise disposed of, or the investment is determined to be impaired, at which time the cumulative gain or loss previously reported in equity is included in the consolidated statement of income for the year.

"Financial liabilities other than at fair value through profit or loss" are subsequently measured at amortised cost.

Fair values

For financial instruments quoted in an active market, fair value is determined by reference to quoted market prices. Bid prices are used for assets and offer prices are used for liabilities. The fair value of investments in mutual funds, unit trusts or similar investment vehicles are based on the last published net assets value.

For unquoted financial instruments fair value is determined, by reference to the market value of a similar investment, discounted cash flows, other appropriate valuation models or brokers' quotes.

For financial instruments carried at amortised cost, the fair value is estimated by discounting future cash flows at the current market rate of return for similar financial instruments.

For investments in equity instruments, where a reasonable estimate of fair value cannot be determined, the investment is carried at cost.

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.

2.6 Hedge accounting

The Group makes use of derivative instruments to manage exposures to profit rate, foreign currency and credit risks, including exposures arising from forecast transactions. In order to manage particular risks, the Group applies hedge accounting for transactions which meet the specified criteria. On conversion to an Islamic bank, the bank no longer deals in new derivative transactions.

For the purposes of hedge accounting, hedges are classified into two categories (a) fair value hedges which hedge the exposure to changes in the fair value of a recognised asset or liability or firm commitments and (b) cash flows hedges which hedge exposure to variability in cash flows of a recognised asset or liability or forecast transaction.

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.6 Hedge accounting (continued)

In case of fair value hedges, which meet the conditions for hedge accounting, any gain or loss from re-measuring the hedging instruments to fair value are recorded in the consolidated statement of income, along with the corresponding change in fair value of the hedged asset or liability that is attributable to that specific hedged risk.

In relation to cash flow hedges, which meet the conditions for hedge accounting, the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised in the consolidated comprehensive statement of income and the ineffective portion is recognised in the consolidated statement of income. For cash flow hedges affecting future transactions that subsequently results in the recognition of a financial asset or a financial liability, the associated gains or losses which are recognised in shareholders' equity are re-classified into the consolidated statement of income in the same period or periods during which the financial asset or financial liability affects the consolidated statement of income.

For hedges, which do not qualify for hedge accounting are classified as "held for trading" derivatives and any gains or losses arising from changes in the fair value of the hedging instrument are taken directly to the consolidated statement of income.

Hedge accounting is discontinued prospectively when the hedging instrument expires or is sold, terminated or exercised, or no longer qualifies for hedge accounting or the forecast transaction is no longer expected to occur or the designation is revoked. For fair value hedges of financial instruments with fixed maturities any adjustment arising from hedge accounting is amortised over the remaining term to maturity. For cash flow hedges, any cumulative gain or loss on the hedging instrument recognised in equity remains in equity until the hedged transaction occurs. If the hedged transaction is no longer expected to occur, the net cumulative gain or loss recognised in equity is transferred to the consolidated statement of income.

Derivatives with positive market values are included in the other assets and derivatives with negative market values are included in other liabilities in the consolidated balance sheet.

2.7 Financial guarantees

In the ordinary course of business, the Group provides financial guarantees, consisting of letter of credit, guarantees and acceptances.

Financial guarantees are initially recognised in the consolidated financial statements at fair value, being the premium received, in other liabilities. The premium received is recognised in the consolidated statement of income on a straight line basis over the life of the guarantee. Subsequent to initial recognition, the Group's liability under each guarantee is measured at the higher of the amortised premium received and the best estimate of net cash flow required to settle any financial obligation arising as a result of the guarantee.

2.8 Impairment of financial assets

At each balance sheet date the Group assesses whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is impaired, if and only if, there is objective evidence of impairment as a result of one or more events that have occurred after the initial recognition of the asset and that loss event has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated. If such evidence exists the asset or group of financial assets is written down to its recoverable amount. The recoverable amount of a profit-bearing instrument is estimated based on the net present value of future cash flows discounted at original profit rates, and of equity instrument is determined with reference to market rates or appropriate valuation models. For variable profit rate bearing instruments, the net present value of future cash flows is discounted at the current effective profit rate determined under the contract.

The carrying amount of the asset is reduced through the use of an allowance account and the amount of impairment loss is recognised in the consolidated statement of income.

The Group assesses whether objective evidence of impairment exists on an individual basis for each individual significant financing and collectively for others. The main criteria that the Group uses to determine that there is objective evidence of impairment include whether any payment of principal or profit are overdue by more than 90 days or there are any known difficulties in the cash flows including the sustainability of the counterparty's business plan, credit rating downgrades, breach of original terms of the contract, its ability to improve performance once a financial difficulty has arisen, deterioration in the value of collateral, bankruptcy, other financial reorganization, and economical or legal reasons. The impairment losses are evaluated at each reporting date, unless unforeseen circumstances require more careful attention.

Financial guarantees and letter of credit are assessed and provisions are made in a similar manner as for financing receivables.

Financing receivables and loans together with the associated allowance are written off when there is no realistic prospect of future recovery and all collateral has been realised or has been transferred to the Group. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognised, the previously recognised impairment loss is increased or reduced by adjusting the allowance account. If a write-off is later recovered, the recovery is credited to the "Provision for impairment" in the consolidated statement of income.

For equity instruments classified as investments available for sale, impairment losses are not reversed through the consolidated statement of income; any increase in the fair value subsequent to the recognition of impairment loss, is recognised in the consolidated statement of comprehensive income. For Sukuk classified as investments available for sale, if in a subsequent year, the fair value of the Sukuk increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in the consolidated statement of income; the impairment loss is reversed through the consolidated statement of income.

General provision

In accordance with CBK instructions, a minimum general provision is made on all applicable credit facilities (net of certain categories of collateral) that are not provided for specifically. In March 2007, the CBK issued a circular amending the basis of making minimum general provisions on facilities changing the rate from 2% to 1% for cash facilities and 0.5% for non cash facilities. The required rates were to be applied effective from 1 January 2007 on the net increase in facilities, net of certain categories of collateral during the reporting period.

The minimum general provision in excess of the present 1% for cash facilities and 0.5% for non cash facilities is retained as a general provision until further directive from the CBK.

2.9 Renegotiated financing receivables

Where considered appropriate, the Group seeks to restructure past due financing receivables. This may involve extending the payment arrangements and the agreement of new financing conditions including enhancing collateral position. Management continuously reviews renegotiated financing receivables to ensure that all criteria are met and that future payments are likely to occur. Once the terms have been renegotiated, the facility is neither considered past due nor impaired.

2.10 Investment in associate

Associates are entities in which the Group exerts significant influence represented by an interest of between 20% and 50% of the voting rights and is neither a subsidiary nor a joint venture. Investments in associates are accounted for under the equity method of accounting.

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.11 Investment properties

Land and buildings held for the purpose of capital appreciation or for long term rental yields and not occupied by the Group is classified as investment properties.

Investment properties are measured at cost less accumulated depreciation (based on an estimated useful life of twenty five years using the straight line method) and accumulated impairment.

Any gains or losses on the retirement or disposal of an investment property are recognised in the consolidated statement of income in the period of retirement or when sale is completed.

2.12 Premises and equipment

Freehold land is initially recognised at cost and not depreciated. After initial recognition freehold land is carried at the revalued amount, which is the fair value at the date of revaluation. The revaluation is carried out periodically by professional property evaluators. The resultant revaluation surplus or deficit is recognised in the consolidated statement of comprehensive income to the extent the deficit does not exceed the previously recognised surplus. The portion of the revaluation deficit that exceeds a previously recognised revaluation surplus is recognised in the consolidated statement of income. To the extent that a revaluation surplus reverses a revaluation decrease previously recognised in the consolidated statement of income, the increase is recognised in the consolidated statement of income. Upon disposal the revaluation reserve relating to the freehold land sold is transferred to retained earnings.

Buildings, other premises and equipment are stated at cost, less accumulated depreciation and impairment losses if any. Depreciation of buildings and other premises and equipment is provided on a straight-line basis over their estimated useful lives.

The estimated useful lives of the assets for the calculation of depreciation are as follows:

Buildings	20 to 30 years
Other premises and equipment	2 to 5 years

2.13 Treasury shares

Treasury shares consist of the Bank’s own issued shares that have been reacquired by the Group and not yet reissued or cancelled. The treasury shares are accounted for using the cost method. Under this method, the weighted average cost of the shares reacquired is charged to a contra account in equity. When the treasury shares are reissued, gains are credited to a separate account in equity, (the “treasury shares reserve”), which is not distributable. Any realised losses are charged to the same account to the extent of the credit balance on that account. Any excess losses are charged to retained earnings then to the general reserve and statutory reserve. Gains realised subsequently on the sale of treasury shares are first used to offset any previously recorded losses in the order of reserves, retained earnings and the treasury shares reserve account. No cash dividends are paid on these shares. The issue of stock dividend shares increases the number of treasury shares proportionately and reduces the average cost per share without affecting the total cost of treasury shares.

2.14 Cash and cash equivalents

Cash and cash equivalents include cash and balances with Central Bank of Kuwait, deposits with banks and other financial institutions maturing within seven days.

2.15 Recognition of income

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised.

(i) Financing and interest income

For all financial instruments measured at amortised cost, profit/interest bearing financial assets classified as available for sale, financing and interest income is recorded using the effective profit rate, which is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or financial liability. The calculation takes into account all contractual terms of the financial instrument (for example, prepayment options) and includes any fees or incremental costs that are directly attributable to the instrument and are an integral part of the effective profit rate, but not future credit losses.

Once a financial instrument categorised as "loans and receivables" is written down to its estimated recoverable amount, related income is thereafter recognised on the unimpaired portion based on the original effective profit rate that was used to discount the future cash flows for the purpose of measuring the recoverable amount.

(ii) Fee and commission income

The Group earns fee and commission income from a diverse range of services it provides to its customers.

Fee income can be divided into the following two categories:

Fee income earned from services that are provided over a certain period of time

Fees earned for services over a period of time are accrued over that period.

Fee income from providing transaction services

Fees arising from negotiating or participating in the negotiation of a transaction for a third party, are recognised on completion of the underlying transaction. Fees or components of fees that are linked to a certain performance are recognised after fulfilling the corresponding criteria.

(iii) Dividend income is recognised when right to receive payment is established.

(iv) Rental income is recognized on accrual basis.

2.16 Provisions

Provisions are recognised when, as a result of past events, it is probable that an outflow of economic resources will be required to settle a present, legal or constructive obligation and the amount can be reliably estimated.

2.17 Foreign currency

Foreign currency transactions are recorded at the rate of exchange prevailing at the date of transactions. Monetary assets and liabilities denominated in foreign currencies outstanding at the year-end are translated into Kuwaiti Dinars at the rates of exchange prevailing at the balance sheet date. Any resultant gains or losses are taken to the consolidated statement of income.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Translation difference on non-monetary investments at fair value through profit or loss are reported as part of the fair value gain or loss in the consolidated statement of income, whilst those for available for sale non-monetary assets are included in the consolidated statement of comprehensive income, unless it is part of an effective hedging strategy, using exchange rates when the fair value was determined.

Translation differences arising on consolidation of the subsidiaries are taken to the consolidated statement of comprehensive income.

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.18 Segment information

Operating segments are reported in a manner consistent with the internal reporting provided to the Chief operating decision maker.

2.19 Contingencies

Contingent assets are not recognised in the financial statements, but are disclosed when an inflow of economic benefit is probable.

Contingent liabilities are not recognised in the financial statements, but are disclosed unless the possibility of an outflow of resources embodying economic benefit is remote. Provisions for contingent liabilities are recognized when the outflow of resources is probable.

2.20 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.

3. INTEREST INCOME

Interest income represents interest earned on the conventional loan portfolio mainly before conversion.

4. DISTRIBUTION TO DEPOSITORS AND INTEREST EXPENSE

Interest expense represents interest on deposits before conversion.

The Board of Directors of the Bank determines the depositors' share of profit based on the Bank's results for the nine months from 1 April to 31 December 2010.

5. NET FEES AND COMMISSION INCOME

	2010	2009
	KD 000	KD 000
Investment management fees	**2,304**	3,094
Credit related fees and commission	**6,887**	8,801
Brokerage fees	**1,903**	3,382
Total fees and commission income	**11,094**	15,277
Fees and commission expense	**(803)**	(809)
Net fees and commission income	**10,291**	14,468

6. NET GAIN ON SALE OF INVESTMENTS

	2010 KD 000	2009 KD 000
Gain on sale of Kuwait Government treasury bonds	**2,362**	-
Net gain on sale of investments available for sale	**946**	8,062
Loss on sale of investment properties	**(364)**	-
	2,944	8,062

7. PROVISION AND IMPAIRMENT LOSSES

	2010 KD 000	2009 KD 000
Financing receivables and loans (net) (Note 12)	**6,554**	27,979
Non-cash credit facilities (Note 12)	**107**	(687)
Investments available for sale	**12,107**	16,230
Others	**5,725**	3,549
	24,493	47,071

8. TAXATION & ZAKAT

	2010 KD 000	2009 KD 000
Contribution to Kuwait Foundation for the Advancement of Sciences (KFAS)	**304**	182
National Labour Support Tax (NLST)	**730**	373
Zakat	**290**	146
	1,324	701

9. BASIC AND DILUTED EARNINGS PER SHARE

	2010	2009
Profit for the year attributable to the Bank's equity shareholders (KD 000)	**27,444**	14,262
Weighted average number of shares outstanding during the year	**966,274,717**	966,274,717
Basic and diluted earnings per share (fils)	**28.4**	14.8

The weighted average number of shares outstanding during the year is calculated after adjusting for treasury shares as follows:

	2010	2009
Weighted average number of Bank's issued and paid up shares	**1,073,225,408**	1,073,225,408
Less: Weighted average number of treasury shares	**(106,950,691)**	(106,950,691)
	966,274,717	966,274,717

Earnings per share was 16.2 fils for the year ended 31 December 2009 before retroactive adjustment to the number of shares following the bonus issue (Note 20).

10. CASH AND BALANCES WITH BANKS

	2010 KD 000	2009 KD 000
Balances with the Central Bank of Kuwait	**10,921**	2,409
Cash in hand and current account balances with other banks	**32,149**	23,573
Short-term Murabaha and placements (maturing within seven days)	**340,200**	114,375
	383,270	140,357

11. KUWAIT GOVERNMENT TREASURY BONDS AND CENTRAL BANK OF KUWAIT BONDS

These financial instruments are issued by the Central Bank of Kuwait either on behalf of the Ministry of Finance or its own behalf, acquired from the primary market by the Group.

12. FINANCING RECEIVABLES AND LOANS

Financing receivables comprise Islamic Sharia'a compliant facilities extended to the customers by the Bank in the form of financing contracts. Wherever necessary, financing receivables are secured by acceptable forms of collateral to mitigate the related credit risk.

Loans represent facilities to the Bank's customers which are in accordance with conventional banking contracts that remain outstanding after the conversion to an Islamic Bank. The Bank is in the process of converting these facilities to comply with Islamic Sharia'a.

The movement in provision for impairment of financing receivables and loans by class of financial assets is as follows:

	Retail financing KD 000	Commercial financing KD 000	Total KD 000
At 1 January 2010	**31,536**	**55,607**	**87,143**
Charge for the year (Note 7)	**2,206**	**4,348**	**6,554**
Amounts written off	**(21,073)**	**(17,748)**	**(38,821)**
At 31 December 2010	**12,669**	**42,207**	**54,876**
At 1 January 2009	26,502	32,921	59,423
Charge for the year (Note 7)	5,293	22,686	27,979
Amounts written off	(259)	-	(259)
At 31 December 2009	31,536	55,607	87,143

As at 31 December 2010, non-performing financing receivables and loans on which income has been suspended from recognition amounted to KD 48,469 thousand (2009: KD 81,134 thousand).

The split of non-performing facilities granted and related provision for impairment are as follows:

	2010 KD 000	2009 KD 000
Financing receivables and loans	**48,469**	81,134
Specific provision for impairment	**17,204**	50,206
Total provision for financing receivables and loans	**54,876**	87,143

The provision charge / (release) for the year on non-cash facilities is KD 107 thousand (2009: KD (687) thousand). The available provision on non-cash facilities of KD 3,252 thousand (2009: KD 3,145 thousand) is included in other liabilities (Note 19).

The policy of the Group for calculation of the impairment provision for financing receivables and loans complies in all material respects with the provision requirements of Central Bank of Kuwait. According to the Central Bank of Kuwait instructions, a minimum general provision of 1% for cash facilities and 0.5% for non cash facilities has been made on all applicable credit facilities (net of certain categories of collateral), that are not provided for specifically.

The Central Bank of Kuwait in accordance with Decree No. 32/1992 and Law No. 41/ 93, as amended, has funded provisions in respect of pre-invasion loans. Any recoveries made against these provisions are ceded to the Central Bank of Kuwait in accordance with the prevalent law, and are not included in the consolidated statement of income. During the year pre-invasion loans and advances along with related provision were transferred to off-balance sheet memorandum account with approval of the Central Bank of Kuwait.

13. INVESTMENTS AVAILABLE FOR SALE

	2010 KD 000	2009 KD 000
Sukuk	**6,898**	-
Equity securities and funds		
- Quoted	**20,746**	54,567
- Unquoted	**23,110**	20,987
	50,754	75,554

Investments available for sale include unquoted equity instruments carried at cost of KD 2,237 thousand (2009: KD 500 thousand).

14. INVESTMENT IN ASSOCIATE

The Group has a 30% (2009: 30%) interest in Middle East Financial Investment Company, an unquoted company incorporated in Kingdom of Saudi Arabia engaged in investment activities.

The share in assets, liabilities, and results of the associate for the year ended is as follows:

	2010 KD 000	2009 KD 000
Share of associate's balance sheet:		
Current assets	**1,051**	240
Non-current assets	**7,305**	8,077
Current liabilities	**(64)**	(36)
Non-current liabilities	**(19)**	(50)
Net assets	**8,273**	8,231
Share of associate's results:		
Operating income	**816**	387
Profit / (loss) for the year	**209**	(244)

15. INVESTMENT PROPERTIES

These represent properties acquired by KMEFIC and have been sold during the year.

16. PREMISES AND EQUIPMENT

Premises and equipment includes a revaluation increase of KD 116 thousand (2009: decrease of KD 7,040 thousand) in the value of freehold land based on valuations determined by independent valuation experts.

17. OTHER ASSETS AND INTANGIBLES

	2010 KD 000	2009 KD 000
Income / interest receivable	**4,303**	4,789
Stock exchange brokerage licences	**12,736**	12,692
Positive fair value of derivatives (Note 24)	**-**	1,693
Others	**9,836**	13,674
	26,875	32,848

Stock exchange brokerage licenses are classified as intangible assets with an indefinite life.

18. DEPOSITS FROM CUSTOMERS

Depositors' accounts are deposits received from customers under current account, saving investment accounts, and fixed term investments accounts. 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 Hassan from depositors to the Bank under Islamic Sharia'a. Investing such Qard Hassan is made at the discretion of the Board of Directors of the Bank, the results of which are attributable to the equity shareholders of the Bank.

ii) Investment deposit accounts include savings accounts, fixed term deposit accounts, and open term deposit accounts.

Saving Investment Accounts
These are open-term deposits and the client is entitled to withdraw the balances of these accounts or portions thereof at any time.
Fixed-Term Deposit Investment Accounts
These are fixed-term deposits based on the deposit contract executed between the Bank and the depositor. These deposits are matured monthly, quarterly, semi-annually, or annually.
Open –Term Deposit Investment Accounts
These are open-term deposits and are treated as annual deposits renewed automatically for a similar period, unless the depositor notifies the Bank in writing of his/her desire not to renew the deposit.

Funds utilized in investments for each investment deposit are computed using ratios identified in the contracts for opening of these accounts with clients. The Bank guarantees to pay the remaining un-invested portion of these investment deposits. Accordingly, this portion is considered Qard Hassan from depositors to the Bank, on the grounds of Islamic Sharia'a.

The fair values of depositors' accounts do not differ from their carrying book values.

19. OTHER LIABILITIES

	2010	2009
	KD 000	KD 000
Expenses / interest payable	**9,977**	10,906
Provision for staff indemnity	**3,401**	2,954
Provision for non-cash credit facilities (Note 12)	**3,252**	3,145
Negative fair value of derivatives (Note 24)	**-**	292
Others	**25,170**	17,868
	41,800	35,165

20. EQUITY

i) The authorised, issued and fully paid share capital as at 31 December 2010 comprises 1,073,225,408 ordinary shares (31 December 2009: 975,659,462 shares) of 100 fils each. The Extraordinary General Assembly Meeting held on the 28 March 2010 approved increase in the share capital from 975,659,462 ordinary shares to 1,073,225,408 ordinary shares of 100 fils each, which was fully utilised by issuance of bonus shares for the year ended 31 December 2009.

20. EQUITY (CONTINUED)

ii) The Board of Directors of the Bank has proposed bonus shares of 5% (2009: bonus shares of 10%) and cash dividend of 14% amounting to 14 fils per share (2009: Nil). The proposed bonus shares are subject to the approval of the shareholders at the Bank's Annual General Assembly. The bonus shares for the year ended 31 December 2009 were approved by the Bank's Annual General Assembly held on 28 March 2010.

iii) The Bank is required by the Commercial Companies' Law and the Bank's Articles of Association to transfer 10% of the profit for the year attributable to the Bank's equity shareholders before KFAS, NLST, Zakat and Board of Directors' remuneration to the statutory reserve. The Bank may resolve to discontinue such annual transfers when the statutory reserve equals 50% of the paid up share capital. The Bank has transferred KD 2,885 thousand (2009: KD 1,496 thousand) to statutory reserve. Distribution of the statutory reserve is limited to the amount required to enable the payment of a dividend of up to 5% of share capital in years when retained earnings are not sufficient for the payment of such dividend.

iv) The Articles of Association of the Bank requires that an amount of not less than 10% of the profit for the year attributable to the Bank's equity shareholders before KFAS, NLST, Zakat and Board of Directors' fees should be transferred annually to a general reserve account. The Board of Directors have resolved to discontinue such transfer from the year ended 31 December 2007 onwards, which was approved by the shareholders at the Bank's Annual General Assembly on 6 March 2008.There is no restriction on distribution of this reserve.

v) The balances of share premium and treasury shares reserve are not available for distribution. The balance in the property revaluation reserve is not available for distribution unless the relevant assets are derecognised.

vi) The cost of the Bank's own shares purchased, including directly attributable costs, is recognised in equity. In accordance with the instructions of the Central Bank of Kuwait and Annual General Assembly the Bank may purchase treasury shares up to 10% of it's paid up share capital.

21. TREASURY SHARES

There was no purchase or sale of treasury shares during the current year.

	2010	2009
Number of treasury shares	**106,950,691**	97,227,901
Treasury shares as a percentage of total shares issued	**9.97%**	9.97%
Cost of treasury shares (KD 000)	**43,957**	43,957
Market value of treasury shares (KD 000)	**70,587**	48,614

22. RELATED PARTY TRANSACTIONS

The Group enters into transactions with the parent, associates, major shareholders, directors and key management, close members of their families and entities controlled, jointly controlled or significantly influenced by such parties in the ordinary course of business. The terms of these transactions are approved by the Group's management.

The year-end balances included in the consolidated financial statements are as follows:

	Number of directors and executive officers		Number of parties related to directors and executive officers		Amount	
	2010	2009	**2010**	2009	**2010 KD 000**	2009 KD 000
Directors						
Financing receivables and loans	**2**	1	**5**	5	**14,557**	15,834
Deposits taken	**5**	5	**6**	7	**2,426**	2,591
Commitments and contingent liabilities	**-**	-	**2**	2	**783**	805
Key management						
Deposits taken	**2**	2	**1**	1	**344**	391

	2010 KD 000		2009 KD 000	
	Parent	**Other related parties**	Parent	Other related parties
Deposits placed	**103,375**	**-**	8,669	-
Deposits taken	**10,375**	**671,804**	14,557	442,960
Commitments and contingent liabilities	**7,593**	**-**	1,998	-
Foreign exchange contracts	**-**	**-**	17,962	-

The related financing income and the estimated distribution to depositors on the above balances are included in the consolidated statement of income.

Further, during the year the Bank has disposed off investments available for sale to a related party for a total consideration of KD 18,787 thousand and realised a net gain on sale of KD 611 thousand.

The transactions included in the consolidated statement of income are as follows:

	2010 KD 000	2009 KD 000
Directors:		
Board of Directors remuneration	**75**	-
Key management compensation:		
Salaries and other short term benefits	**1,470**	1,528
Post employment benefits	**63**	88
	1,608	1,616

Board of Directors remuneration is subject to approval of shareholders in Annual General Assembly.

23. COMMITMENTS AND CONTINGENT LIABILITIES

a) Credit- related commitments

Credit-related commitments include commitments to extend credit, standby letters of credit, guarantees and acceptances, which are designed to meet the requirements of the Group's customers.

Letters of credit (including standby letters of credit), guarantees and acceptances commit the Group to make payments on behalf of customer's upon failure of the customers to perform under the terms of the contract.

Commitment to extend credit represents contractual commitments to financing and revolving credits. Commitments generally have fixed expiration dates, or other termination clauses. Since commitments may expire without being drawn upon, the total contract amounts do not necessarily represent future cash requirements. The Group has the following credit related commitments:

	2010 KD 000	2009 KD 000
Acceptances	**7,530**	8,023
Letters of credit	**44,999**	36,470
Guarantees	**208,249**	173,928
	260,778	218,421

Irrevocable credit commitments to extend credit at the balance sheet date amounted to KD 28,248 thousand (2009: KD 5,330 thousand).

b) Capital commitment

The capital commitment for purchase of assets as at 31 December 2010 is KD 3,104 thousand (2009: KD 2,446 thousand).

24. DERIVATIVES

In the ordinary course of business until conversion to Islamic bank , the bank had entered into various types of transactions that involve derivative financial instruments to mitigate foreign currency, credit risk and profit rate risk. A derivative financial instrument is a financial contract between two parties where payments are dependent upon movements in price of one or more underlying financial instruments, reference rate or index. In accordance with Islamic Sharia'a the Bank no longer deals in new derivative products from 1 April 2010.

The notional amount, disclosed gross, is the amount of a derivative's underlying asset and is the basis upon which changes in the value of derivatives are measured. The notional amounts indicate the volume of transactions outstanding at the year-end and are neither indicative of the market risk nor credit risk.

The table below shows the fair value of derivative financial instruments and their notional amounts:

	2010			2009		
	Assets (Positive) KD 000	Liabilities (Negative) KD 000	Notional amounts KD 000	Assets (Positive) KD 000	Liabilities (Negative) KD 000	Notional amounts KD 000
Derivatives held for trading:						
Forward foreign exchange contracts	-	-	-	1,691	290	46,154
Interest rate swaps	-	-	-	2	2	452
	-	-	-	1,693	292	46,606

Most of the Group's derivative trading activities relate to deals with customers, which are normally matched by entering into reciprocal deals with counterparties.

25. FAIR VALUES OF FINANCIAL INSTRUMENTS

Fair value is the amount at which a financial instrument could be exchanged or settled between knowledgeable willing parties in an arm's length transaction. Underlying the definition of fair value is the presumption that the Group is a going concern without any intention, or need, to liquidate, curtail materially the scale of its operations or undertake a transaction on adverse terms.

The Group uses the following hierarchy for determining and disclosing the fair values of financial instruments that are carried at fair value:

Level 1: Quoted prices in active market for the identical instrument;

Level 2: Quoted prices in active market for similar instruments or other valuation techniques for which all significant inputs are based on observable market data either directly or indirectly; and

Level 3: Valuation techniques for which any significant input is not based on observable market data.

The following table shows an analysis of financial instruments recorded at fair value by level of the fair value hierarchy:

31 December 2010	**Level: 1 KD 000**	**Level: 2 KD 000**	**Total KD 000**
Financial assets			
Investments available for sale (Note 13)	27,643	20,874	48,517

31 December 2009	Level: 1 KD 000	Level: 2 KD 000	Total KD 000
Financial assets			
Investments available for sale (Note 13)	54,567	20,487	75,054

Derivative financial instruments are classified at level 2. There is no financial instrument classified at Level 3 fair value as of 31 December 2010 (2009: Nil).

26. MATURITY ANALYSIS OF ASSETS AND LIABILITIES

The table below summaries the maturity profile of the Group's assets and liabilities based on contractual remaining maturity:

At 31 December 2010:	Up to 3 months KD 000	3 to 12 months KD 000	Over 1 year KD 000	Total KD 000
ASSETS				
Cash and balances with banks	383,270	-	-	383,270
Kuwait Government treasury bonds	-	-	-	-
Central Bank of Kuwait bonds	-	-	-	-
Certificates of deposit	-	-	-	-
Deposits with banks and other financial institutions	216,423	110,694	-	327,117
Financing receivables and loans	664,559	263,558	681,869	1,609,986
Investments available for sale	16,044	1,926	32,784	50,754
Investment in associate	-	-	8,273	8,273
Premises and equipment	-	-	48,062	48,062
Other assets and intangibles	9,112	1,190	16,573	26,875
Total assets	1,289,408	377,368	787,561	2,454,337
LIABILITIES				
Deposits from banks and other financial Institutions	369,984	489,731	-	859,715
Deposits from customers	994,370	289,610	3,547	1,287,527
Other liabilities	34,275	3,991	3,534	41,800
Total liabilities	1,398,629	783,332	7,081	2,189,042
Net liquidity gap	(109,221)	(405,964)	780,480	265,295

At 31 December 2009:	Up to 3 months KD 000	3 to 12 months KD 000	Over 1 year KD 000	Total KD 000
ASSETS				
Cash and balances with banks	140,357	-	-	140,357
Kuwait Government treasury bonds	51,158	119,165	36,778	207,101
Central Bank of Kuwait bonds	16,987	-	-	16,987
Certificates of deposit	10,038	-	-	10,038
Deposits with banks and other financial institutions	153,596	-	-	153,596
Financing receivables and loans	695,298	192,154	673,652	1,561,104
Investments available for sale	40,144	-	35,410	75,554
Investment in associate	-	-	8,231	8,231
Investment properties	-	-	8,541	8,541
Premises and equipment	-	-	46,176	46,176
Other assets and intangibles	13,113	4,350	15,385	32,848
Total assets	1,120,691	315,669	824,173	2,260,533
LIABILITIES				
Deposits from banks and other financial Institutions	235,780	291,997	-	527,777
Deposits from customers	1,159,970	294,261	6,024	1,460,255
Other liabilities	27,170	4,042	3,953	35,165
Total liabilities	1,422,920	590,300	9,977	2,023,197
Net liquidity gap	(302,229)	(274,631)	814,196	237,336

27. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Strategy in using financial instruments

As an Islamic commercial bank, the Bank's activities are principally related to the sourcing of funds through Sharia'a compliant financial instruments, within the guidelines prescribed by Central Bank of Kuwait (CBK) and deploying these funds in Sharia'a compliant financing and investment activities, to earn a profit. The profit is shared between the shareholders and profit sharing deposit account holders, as per the Bank's policies approved by the Board of Directors and Fatwa and Sharia'a Supervisory Board. The funds raised vary in maturity between short and longer tenors and are mainly in Kuwaiti Dinars, apart from major foreign currencies and GCC currencies. While deploying the funds, the Bank focuses on the safety of the funds and maintaining sufficient liquidity to meet all claims that may fall due. Safety of shareholder and depositor funds is further enhanced by diversification of financing activities across economic and geographic sectors, and types of financed parties.

RISK MANAGEMENT

The use of financial instruments also brings with it associated inherent risks. The Group recognises the relationship between returns and risks associated with the use of financial instruments and the management of risks forms an integral part of the Group's strategic objectives.

27. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (CONTINUED)

RISK MANAGEMENT (continued)

The strategy of the Group is to maintain a strong risk management culture and manage the risk/reward relationship within and across each of the Group's major risk-based lines of business. The Group continuously reviews its risk management policies and practices to ensure that it is not subject to large asset valuation and earnings volatility.

Group's objectives, policies and process for managing its risk are explained in detail in the Pillar 3 disclosures of the Annual Report. The following sections describe the several risks inherent in the banking process, their nature, techniques used to minimise the risks, their significance and impact on profit and loss and equity due to future expected changes in market conditions.

A. 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. The Group attempts to control risk by monitoring credit exposures, limiting transactions with reputable counterparties, and continually assessing the creditworthiness of counterparties.

Concentration of credit risk 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.

Concentration of credit risk indicates the relative sensitivity of the Group's performance to developments, affecting a particular industry or geographic location.

The Group seeks to manage its credit risk exposure through diversification of financing activities to avoid undue concentrations of risks with individuals or groups of customers in specific locations or businesses. It also obtains collateral, when appropriate. The amount and type of collateral required depends on an assessment of the credit risk of the counterparty. Guidelines are implemented regarding the acceptability of types of collateral and valuation parameters.

The main types of collateral obtained include charges over bank deposits and balances, listed securities acceptable to the Group, real estate, plant and equipment, inventory and trade receivables

Management monitors the market value of collateral on a daily basis for quoted shares and periodically for others, requests additional collateral in accordance with the underlying agreement, and monitors the market value of collateral obtained during its review of the adequacy of the allowance for impairment losses.

Geographical and industry-wise concentration of assets and off balance sheet items:

At 31 December 2010

	Assets representing credit risk KD 000	Contingencies & commitments representing credit risk KD 000
Geographic region:		
Kuwait	**2,162,448**	**222,158**
Other GCC	**156,686**	**64,284**
Europe	**49,217**	**1,302**
North America	**5,140**	**449**
Other countries	**6,398**	**833**
	2,379,889	**289,026**
Industry sector:		
Trading and manufacturing	**299,843**	**110,963**
Banks and financial institutions	**761,233**	**69,418**
Construction and real estate	**722,702**	**85,260**
Other	**596,111**	**23,385**
	2,379,889	**289,026**

At 31 December 2009

	Assets representing credit risk KD 000	Contingencies & commitments representing credit risk KD 000
Geographic region:		
Kuwait	1,928,041	175,225
Other GCC	173,052	46,000
Europe	58,011	1,091
North America	3,879	338
Other countries	12,208	1,097
	2,175,191	223,751
Industry sector:		
Trading and manufacturing	322,445	100,762
Banks and financial institutions	578,749	51,890
Construction and real estate	557,726	49,420
Other	716,271	21,679
	2,175,191	223,751

27. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (CONTINUED)

A. CREDIT RISK (continued)

The table below shows the maximum exposure to credit risk for the components of the balance sheet and off-balance sheet items without taking account of any collateral and other credit enhancements.

	Gross maximum exposure 2010 KD 000	Gross maximum exposure 2009 KD 000
Credit risk exposures relating to balance sheet items:		
Balances with banks	**373,459**	129,658
Kuwait Government treasury bonds	**-**	207,101
Central Bank of Kuwait bonds	**-**	16,987
Certificates of deposits	**-**	10,038
Deposits with banks and other financial institutions	**327,117**	153,596
Financing receivables and loans	**1,664,862**	1,648,247
Investments available for sale	**6,898**	-
Other assets	**7,553**	9,564
	2,379,889	2,175,191
Credit risk exposures relating to off - balance sheet items: (Note 23a)		
Acceptances, letters of credit, and guarantees	**260,778**	218,421
Irrevocable credit commitments	**28,248**	5,330
	289,026	223,751

The gross maximum credit exposure to a single client or counterparty as of 31 December 2010 was KD 33,271 thousand (2009: KD 33,451 thousand) and credit exposure net of eligible collateral to the same counterparty was KD Nil (2009: Nil).

Credit quality of the financial assets is managed by the Group with a combination of external and internal ratings mechanism. It is the Group's policy to maintain accurate and consistent risk ratings across the credit portfolio. This facilitates focused management of the applicable risks and the comparison of credit exposures across all lines of business, geographic regions and products. The rating system is supported by a variety of financial analytics, combined with processed market information to provide the main inputs for the measurement of counterparty risk. All internal risk ratings are tailored to the various categories and are derived in accordance with the Group's rating policy. The credit quality of class of assets with underlying credit risks are as follows:

Neither past due nor impaired
At 31 December 2010

				KD 000
	High grade	Standard grade	Closely monitored	Total
Balances with banks	373,459	-	-	373,459
Kuwait Government treasury bonds	-	-	-	-
Central Bank of Kuwait bonds	-	-	-	-
Certificates of deposits	-	-	-	-
Deposits with banks and other financial institutions	327,117	-	-	327,117
Financing receivables and loans	1,468,855	129,255	10,380	1,608,490
Investments available for sale	6,898	-	-	6,898
Other assets	7,553	-	-	7,553
	2,183,882	129,255	10,380	2,323,517

At 31 December 2009	High grade	Standard grade	Closely monitored	Total
				KD 000
Balances with banks	129,658	-	-	129,658
Kuwait Government treasury bonds	207,101	-	-	207,101
Central Bank of Kuwait bonds	16,987	-	-	16,987
Certificates of deposits	10,038	-	-	10,038
Deposits with banks and other financial institutions	153,596	-	-	153,596
Loans and advances	1,427,929	124,830	6,764	1,559,523
Other assets	9,564	-	-	9,564
	1,954,873	124,830	6,764	2,086,467

Financial assets by class that are past due but not impaired:

At 31 December 2010	**Past due upto 60 days KD 000**	**Past due 61 to 90 days KD 000**	**Total KD 000**
Financing receivables and loans			
-Retail financing	**5,241**	**1,797**	**7,038**
-Commercial financing	**486**	**379**	**865**
	5,727	**2,176**	**7,903**
Fair value of collateral			**1,048**

At 31 December 2009	Past due upto 60 days KD 000	Past due 61 to 90 days KD 000	Total KD 000
Loans and advances			
-Retail loans	3,802	1,983	5,785
-Commercial loans	1,330	475	1,805
	5,132	2,458	7,590
Fair value of collateral			4,104

Financial assets by class that are impaired:

At 31 December 2010	**Gross exposure KD 000**	**Impairment provision KD 000**	**Fair value of collateral KD 000**
Financing receivables and loans			
-Retail financing	**12,368**	**6,662**	**-**
-Commercial financing	**36,101**	**10,542**	**27,846**
	48,469	**17,204**	**27,846**

At 31 December 2009	Gross exposure KD 000	Impairment provision KD 000	Fair value of collateral KD 000
Loans and advances			
-Retail loans	32,717	25,979	-
-Commercial loans	48,417	24,227	23,293
	81,134	50,206	23,293

The factors the Group considered in determining impairment are disclosed in Note 2 - Significant accounting policies.

27. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (CONTINUED)

A. CREDIT RISK (continued)

Renegotiated financing receivables and loans:

The Group has not renegotiated any financial asset in 2010 (2009: Nil) that would otherwise be past due or impaired.

B. LIQUIDITY RISK

Liquidity risk is the risk that the Group will be unable to meet its net funding requirements. Liquidity risk can also 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 has diversified funding sources and assets are managed with liquidity in mind, maintaining an adequate balance of cash, cash equivalents, and readily marketable securities.

Analysis of financial liabilities by remaining contractual maturities

The table below summarises the maturity profile of the Group's financial liabilities based on contractual undiscounted repayment obligations. Repayments which are subject to notice are treated as if notice were to be given immediately. However, the Group expects that many customers will not request repayment earlier than the contractual date and the table does not reflect the expected cash flows indicated by the Group's deposit retention history.

	Less than 1 month KD 000	1 to 3 months KD 000	3 to 12 months KD 000	1 to 5 years KD 000	Over 5 years KD 000	Total KD 000
At 31 December 2010						
Deposits from banks and other financial institutions	**220,695**	**149,901**	**494,346**	**-**	**-**	**864,942**
Deposits from customers	**651,044**	**345,389**	**291,986**	**3,902**	**146**	**1,292,467**
Other liabilities	**29,209**	**5,066**	**3,991**	**2,280**	**1,254**	**41,800**
	900,948	**500,356**	**790,323**	**6,182**	**1,400**	**2,199,209**
At 31 December 2009						
Deposits from banks and other financial institutions	110,066	126,667	296,454	-	-	533,187
Deposits from customers	765,367	396,627	298,328	6,745	45	1,467,112
Other liabilities	22,386	4,784	4,042	3,953	-	35,165
	897,819	528,078	598,824	10,698	45	2,035,464

Refer to Note 26 'Maturity analysis of assets and liabilities' for maturities of the financial liabilities shown above. The financial liabilities shown in Note 26 exclude future distribution to depositors.

The table below shows the contractual expiry by maturity of the Group's credit related contingent liabilities and commitments as disclosed in Note 23:

	Less than 1 month KD 000	1 to 3 months KD 000	3 to 12 months KD 000	1 to 5 years KD 000	Over 5 years KD 000	Total KD 000
At 31 December 2010						
Credit related contingent liabilities	**7,694**	**36,298**	**84,207**	**130,690**	**1,889**	**260,778**
Irrevocable loan commitments	**-**	**-**	**3,616**	**22,862**	**1,770**	**28,248**
	7,694	**36,298**	**87,823**	**153,552**	**3,659**	**289,026**
At 31 December 2009						
Credit related contingent liabilities	8,387	26,432	102,588	78,080	2,934	218,421
Irrevocable loan commitments	-	-	-	5,330	-	5,330
	8,387	26,432	102,588	83,410	2,934	223,751

Derivative cash flows

The table below analysis the Group's derivative financial instruments that will be settled on a gross basis into relevant maturity groupings based on the remaining period at the balance sheet date to the contractual maturity date:

	Less than 1 month KD 000	1 to 3 months KD 000	3 to 12 months KD 000	Total KD 000
At 31 December 2010				
Gross settled derivatives:				
Forward foreign exchange contracts	-	-	-	-
At 31 December 2009				
Gross settled derivatives:				
Forward foreign exchange contracts	6,451	30,673	9,030	46,154

C. MARKET RISK

The Group defines market risk as the uncertainty in future earnings on the Group's on and off balance sheet positions resulting from changes in market conditions.

C.1 INTEREST RATE RISK

Interest rate risk arises from the possibility that changes in interest rates will affect the value of the underlying financial instruments. The Group is not exposed to interest rate risk since in accordance with Islamic Sharia'a the Bank does not charge interest except on non-converted loans and advances. The sensitivity of net interest income for one year on these loans is not considered to be significant.

Sensitivity to interest rate movements will be on a symmetric basis, as financial instruments giving rise to non-symmetric movements are not significant.

C.2 CURRENCY RISK

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate due to changes in foreign exchange rates. Positions are monitored on a daily basis and hedging strategies are used to ensure positions are maintained within established limits.

The Group had the following net exposures denominated in foreign currencies.

	2010 KD 000 Equivalent Long (Short)	2009 KD 000 Equivalent Long (Short)
US Dollars	**623**	(2,727)
GCC Currencies	**13,516**	12,156
Egyptian Pounds	**119**	17,989
Others	**2,022**	1,237

The effect on profit before tax, as a result of change in currency rate, with all other variables held constant is shown below:

		Effect on profit before tax	
Currency	Change in currency rate in %	2010 KD 000	2009 KD 000
US Dollars	+5%	**(422)**	(284)

Sensitivity to currency rate movements will be on a symmetric basis, as financial instruments giving rise to non-symmetric movements are not significant

27. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (CONTINUED)

C. MARKET RISK (continued)

C.3 EQUITY PRICE RISK

Equity price risk is the risk that the fair values of equity investments decrease as a result of the changes in the level of equity indices and the value of the individual stocks. The non-trading equity price risk exposure arises from the Group's investment portfolio.

The effect on equity as a result of a change in the fair value of the equity instruments at 31 December 2010 due to a reasonable possible change in the equity indices, with all other variables held as constant is as follows:

		2010	2009
Market indices	Changes in equity price %	**Effect on equity KD 000**	Effect on equity KD 000
Kuwait Index	+10%	**697**	464
Doha, Qatar Index	+10%	**-**	174
MSCI Index	+10%	**254**	134

Sensitivity to equity price movements will be on a symmetric basis, as financial instruments giving rise to non-symmetric movements are not significant.

C.4 PREPAYMENT RISK

Prepayment risk is the risk that the Group will incur a financial loss because its customers and counterparties repay or request repayment earlier than expected, such as fixed rate mortgages when profit /interest rates fall. Due to the contractual terms of its Islamic products, the Bank is not significantly exposed to prepayment risk.

D. OPERATIONAL RISK

The Group has a set of policies and procedures approved by the Board of Directors and are applied to identify, assess and supervise operational risk in addition to other types of risk relating to the banking and financial activities of the Group.

Operational risk is managed by the Risk Management Division. This Division ensures compliance with policies and procedures to identify, assess, supervise and monitor operational risk as part of overall Global Risk Management.

The Group manages operational risks in line with the Central Bank of Kuwait instructions dated 14 November 1996 regarding general guidelines for internal control systems and directives issued on 13 October 2003 regarding "Sound Practices for the Management and Control of Operational Risks".

28. SEGMENT REPORTING

The Group's operating segments are determined based on the reports reviewed by the Chief Operating decision maker that are used for strategic decisions. These segments are strategic business units having similar economic characteristics that offer different products and services. These operating segments are monitored separately by the Group for the purpose of making decisions about resource allocation and performance assessment.

These operating segments meet the criteria for reportable segments and are as follows:

• **Retail and Commercial Banking** – comprising a full range of banking operations covering credit and deposit services provided to customers. The Bank uses a common marketing and distribution strategy for its commercial banking operations.

• **Treasury and Investment Management** – comprising correspondent banking, clearing, money market, foreign exchange, government bills and bonds, other treasury and miscellaneous operations, proprietary investment, securities trading activities and fiduciary fund management activities.

Segment results include revenue and expenses directly attributable to a segment and an allocation of cost of funds to segments based on the daily weighted average balance of segment assets.

The Group measures the performance of operating segments through measure of segment profit or loss net of taxes in management and reporting systems

Segment assets and liabilities comprise those operating assets and liabilities that are directly attributable to the segment.

	Retail and Commercial Banking		Treasury and Investment Management		Total	
	2010 KD 000	2009 KD 000	**2010 KD 000**	2009 KD 000	**2010 KD 000**	2009 KD 000
Segment revenue	**61,146**	63,739	**16,248**	21,309	**77,394**	85,048
Segment result	**30,450**	13,043	**(7,481)**	(3,503)	**22,969**	9,540
Add loss attributable to non-controlling interests					**4,475**	4,722
Profit attributable to Bank's equity shareholders					**27,444**	14,262
Segment assets	**1,829,122**	1,715,970	**574,009**	492,887	**2,403,131**	2,208,857
Unallocated Group assets					**51,206**	51,676
Total assets					**2,454,337**	2,260,533
Segment liabilities	**1,689,605**	1,300,136	**460,293**	687,896	**2,149,898**	1,988,032
Unallocated Group liabilities					**39,144**	35,165
Total liabilities					**2,189,042**	2,023,197

The group primarily operates in Kuwait

29. CAPITAL ADEQUACY

The disclosures relating to the Capital Adequacy Regulations issued by Central Bank of Kuwait (CBK) as stipulated in CBK circular number 2/RBA/44/2009 dated 15 June 2009 and the disclosures required by the amendments of IAS 1- Capital disclosures are included under the section 'Pillar III' of the Annual Report.

Capital management

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

The Group manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of its activities. In order to maintain or adjust the capital structure, the Group may adjust the amount of dividend payment to shareholders, return capital to shareholders or issue capital securities.

Information on Subsidiaries and Significant Investments

The public disclosures under this section have been prepared in accordance with the Central Bank of Kuwait (CBK) Rules and Regulations concerning Capital Adequacy Standard (Basel II) vide circular reference 2/RBA/44/2009 dated June 15, 2009, which apply to Ahli United Bank, Kuwait (formerly Bank of Kuwait & Middle East) ("the Bank" or "AUBK"). The disclosures under this section consist of disclosures of the Bank and its subsidiary together known as "the Group".

The Bank's principal subsidiary is Kuwait and Middle East Financial Investment Company K.S.C. (closed) {subsidiary}, a company incorporated in the State of Kuwait and engaged in investment management activities and regulated by the CBK.

Subsidiaries are fully consolidated on a line by line basis for both accounting and regulatory reporting purposes. Minority interest arising on consolidation is reported as a part of equity for accounting purposes and recognized as part of Tier 1 Capital for regulatory reporting purposes.

Fund transfer transactions within the Group are in accordance with the CBK instructions BS/101/1995 on Maximum Credit Concentration Limits and subsequent amendments / updates. Investments by the Bank in the Group are in accordance with the CBK instruction No.2/BS/79/2000 on Organization of Local Bank's Investment Policy and subsequent amendments / updates.

Information Related to the Capital Structure of the Licensed Bank

The authorized, issued and fully paid share capital as at 31 December 2010 comprises 1,073,225,408 ordinary shares of 100 fils each. Cost of treasury shares acquired by the Bank is reduced from the Tier 1 capital. In accordance with the CBK instruction vide circular 2/BS/75/1999 and subsequent amendments / updates, the Group may purchase treasury shares equal to 10% of the issued shares. No cash dividend is paid on treasury shares held by the Group.

Table 1 – Capital Structure

KD 000

	Funded
Tier 1 Capital	
Paid up share capital	107,323
Reserves	142,690
Minority interest in the equity of consolidated company	19,616
Less:	
Treasury shares	(43,957)
Goodwill	(1,273)
Significant minority equity investment	(4,137)
Total - Tier 1 capital	**220,262**
Tier 2 and Tier 3 capital	**27,320**
Less:	
Significant minority equity investment	(4,136)
Total	**243,446**

Information on Licensed Bank's Capital Adequacy

The process of assessing the capital requirements of the Group commences with the compilation of the annual business plan by individual business units which are then consolidated into the annual budget plan of the Group. The annual budget plan provides an estimate of the overall growth in assets, its impact on capital and targeted profitability.

Annual dividend payout, is prudently determined and proposed by the Board of Directors (the Board), endeavoring to meet shareholder expectations while ensuring adequate retention of capital to support budgeted growth.

The Group ensures that capital adequacy ratios are maintained above the regulatory minimum.

The Group assesses the adequacy of its capital to support its current and future activities on an ongoing basis. Risk weighted assets and capital are monitored periodically to assess the quantum of capital available to support assets growth and optimally deploy capital to achieve targeted returns.

The Group regularly monitors its credit and market risks exposures, limits transactions with specific counterparties, and continually assesses the creditworthiness of counterparties to avoid any unexpected capital charge.

The Bank's credit rating continues to be rated "A-" by Capital Intelligence and "A-" by Fitch. Given the favorable ratings, the Bank is confident of meeting any additional capital requirements by resorting to eligible subordinated debt at competitive pricing to support any need for regulatory capital requirement and maintaining it at optimal levels.

Currently the Group's measurement of capital requirement is based on the CBK guidelines on capital adequacy. However the Group ultimately, aims to achieve a convergence of the regulatory capital with economic capital as it adopts advanced risk measurements for performance evaluation and capital adequacy.

Table 2 – Capital requirement for Credit, Market and Operational Risks

KD 000

Standard Portfolio		
Claims on Banks		**12,190**
Claims on Corporate		**76,128**
Regulatory retail exposures		**33,800**
Past due exposures		**851**
Inventory & commodity other than real estate		**15**
Share & commercial real estate financing		**7,658**
Other exposures		**12,850**
Total Credit Risk Capital Charge		**143,492**
Total Market Risk Capital Charge		**1,296**
Total Operational Risk Capital Charge		**10,964**
Total		**155,752**
Total Capital Adequacy Ratio	**18.76**	
Tier 1 Capital Adequacy Ratio	**16.97**	

Information Related to a Licensed Bank's Internal Capital Adequacy Assessment Process (ICAAP)

The Board and Senior Management take active interest in the overall capital adequacy assessment process. The Bank takes reasonable care in organizing and controlling its affairs responsibly and effectively. This is supported by adopting risk management systems in line with industry best practices and maintaining adequate financial resources.

Internal Capital Adequacy Assessment Process (ICAAP) provides the foundation as to how the Bank internally assesses the capital requirements of the Bank and its subsidiary. It is intended to:

- Review the Bank's exposure to risk areas under Pillar 1 (Minimum Capital Requirements) and those under Pillar 2 (Supervisory Review Process);
- Assess the risk mitigation techniques;
- Determine the level of capital required to support the risk profile of the Bank over and above the minimum capital adequacy required by the Central Bank of Kuwait;
- Provide the appropriate capital and liquidity planning to support current and future capital and funding requirements vis-à-vis business growth targets;
- Provide robust management information system regarding coverage, scenarios and key assumptions used, segregation of roles, independent review, reporting the outcome and periodicity of such reporting; and
- Provide sound guidance in the business decision-making process.

The Bank's ICAAP comprises a comprehensive analysis of the Bank's key risks. Below are the key risks that form part of the Bank's ICAAP under Pillar 1 and Pillar 2:

Risks covered under Pillar 1

- Credit Risk
- Operational Risk
- Market Risk

Risks Covered Under Pillar 2

- Credit Concentration Risk
- Residual Risk
- Fraud Risk
- Profit Rate Risk
- Liquidity Risk
- Legal Risk
- Reputational Risk
- Strategic Risk

The Bank's ICAAP Policy also employs stress testing, which is an evaluation of the Bank's financial position under severe but plausible scenarios. Stress testing also provides an indication of the appropriate level of capital necessary to ensure the economic viability of the Bank in the face of deteriorating business conditions. ICAAP is an ongoing process and reviewed by management on a semi annual basis.

Stress Testing

Stress testing and scenario analysis are essential tools that the Bank employs for its capital management and planning as well as risk management process.

Stress testing is an evaluation of the Bank's financial position under severe scenarios that try to capture potentially adverse conditions. It covers a range of risks and business areas, including at the bank-wide level and the wider environment within which the tests are developed, evaluated and used within the decision making process. Consequently it alerts the Bank's management to adverse unexpected outcomes related to a variety of risks and provides an indication of how much capital might be needed to absorb losses, should economic shocks occur.

In consultation with the Board of Directors and Senior Management, the process takes into account the following major considerations, which are then communicated across all the business units. These include the following:

- Risks that the Bank is and may be exposed to as well as assessment of adequacy of compensating control processes
- Assessment of business conditions obtaining in the markets, including marketing practices, level of competition and consumer preferences
- Assessment of the legal and regulatory environments pertaining to the business activities and sources of financing
- Short-term and medium-term business plans and strategies to achieve such plans
- Assessment of the level of capital required to protect the Bank against anticipated as well as unanticipated business risks
- Sources of capital
- Profit distribution
- Supplementary funding
- Allocation of bank capital and financing to the business units and subsidiary

While stress tests provide an indication of the appropriate level of capital necessary to endure deteriorating economic conditions, the Bank alternatively employs other actions in order to help mitigate increasing levels of risk. In this connection, stress testing is a supplementary tool to other risk management approaches and measures.

Information Related to a Licensed Bank's Risk Management

The Bank maintains a strong risk management culture and manages the risk / reward relationship within and across each of the major risk-based lines of business. The Bank continuously reviews its risk management policies and practices to ensure that it is not subject to large asset valuation and earnings volatility. Stress testing is also conducted on a periodical basis to sensitize the secured exposures with Real Estate and Shares, along with a comprehensive sensitization of the portfolio in relation to stress scenarios. The Board, senior management, risk officers, and line managers contribute to effective bank wide risk management. The Board defines its expectations, and through its oversight determines its accomplishment. The Board also has ultimate responsibility for risk management as they set the tone and other components of an enterprise-wide risk management framework. Risk officers have the responsibility for monitoring progress and for assisting line managers in reporting relevant risk information. The line managers are directly responsible for all business booked in their respective domains. The effective relationship between these parties significantly contributes to the improvement in the Bank risk management practices as this leads to the timely identification of risk and facilitation of appropriate response.

Information Related to a Licensed Bank's Risk Management (continued)

The Risk Management Division (RMD) structure has a distinct identity and independence from business units. The division is comprised of units to address the pertinent risk exposure of the Bank. Its main responsibilities are to:

1) Evaluate and analyze the Bank wide risk profile by developing risk monitoring techniques;

2) Set up and develop criteria for defining the Bank's risk threshold in terms of various risk;

3) Develop and establish tools for the measurement of the Bank's various risk types; and

4) Recommend appropriate strategies / actions for mitigating risk and ensuring a sound risk asset structure for the Bank.

The following committees have the overall responsibility and authorities vested in them for the day-to-day risk management activities of the Bank. Authorities vested in the committees are exercised within the objectives and policies approved by the Board, and subject to the rules and regulations laid down by the CBK.

1) Executive Committee (EC) to assist the Board in discharging its responsibilities in two capacities, deputizing between Board meetings on matters normally reserved to the Board's own decision and discharging responsibilities delegated by the Board including credit, investment, liquidity and market risks, in excess of limits assigned to other committees.
2) Sharia'a Supervisory Board (SSB) supervises and controls the validity of the Bank's activities to ensure that they comply with principles and rulings of the Islamic Sharia'a, and provides its recommendations. It has the right to submit written objections to the Board of Directors with respect to any of the Bank's activities which it considers non-compliant with any of the principles and rulings of the Islamic Sharia'a.
3) Senior Credit Committee (SCC) approves credit, liquidity and market risks in excess of limits assigned to individual executives or other committees, within the set parameters by the Board. The committee likewise reviews bank and country exposures and makes appropriate recommendations to the Board, where needed.
4) Credit Committee (CC) reviews and approves credit proposals which exceed individual credit authority limits, within the set parameters by the Board, provided the proposal meets the Bank's credit criteria requirements.
5) Credit Classification and Evaluation Committee (CCEC) studies and evaluates classified accounts and bank's over-all financing portfolio and determines an appropriate provisioning level.
6) Assets and Liabilities Committee (ALCO) meets periodically to review and approve strategies relating to the management of assets and liabilities including liquidity, profit rate, foreign exchange, cost of funds, cost allocation, deposit pricing matrix and strategic trading positions.
7) Risk Management Committee (RMC) reviews effectiveness of the Bank's overall risk management processes and procedures, amendments to the credit risk, market risk, operational risk and treasury polices. It monitors compliance with financial regulatory ratios, corporate legislations and recommends to the Board, changes in the Bank's policies and methodologies needed to identify, measure, manage and monitor the multiple dimensions of risks inherent in the Bank's business activities.

The risk management function of the subsidiary is managed by its independent Board of Directors and Senior Management. The Bank's nominee directors on the Board of Directors of the subsidiary through its oversight manage and monitor the risk management activities of the subsidiary.

The following sections below, detail the risks inherent in the activities undertaken by the Bank, their nature and approach adopted towards management / mitigation of these risks.

Financing Risk

Financing risk is the risk that one party to a financial instrument will fail to discharge an obligation on time and in full as contracted and cause the other party to incur a financial loss. Financing risk includes the major risks mentioned below:

Direct Financing Risk

The risk that actual customer obligations will not be repaid on time. Direct financing risk occurs in various Islamic products offered by the bank, both secured and unsecured. It exists for the entire life of the transactions.

Contingent Financing Risk

The risk that potential contingent obligations will become actual obligations and will not be repaid on time. Contingent financing risk occurs in products offered by the bank ranging from letters of credit and guarantees to unused financing commitments. It exists for the entire life of the transaction.

Issuer Risk

The risk that the market value of a security or other financing instrument may change when the perceived or actual financing standing of the issuer changes thereby exposing the Bank to a financial loss. It is interrelated to price risk.

Pre-Settlement Risk

The risk that a counter-party with which the Bank trades may default on a contractual obligation before settlement of the contract.

Settlement Risk

The risk occurs when the counter-party fails to settle the transaction on settlement date.

The Bank's Financing Policy aims to promote a strong financing risk management architecture that includes financing policies, procedures and processes. The policy defines the areas and scope of financing activities undertaken by the Bank and its main goal is not simply to avoid losses, but to ensure achievement of targeted financial results with a high degree of reliability in an efficient manner. The Bank's financing risk management focuses on the dynamic and interactive relationship between three financing extension process.

Portfolio Strategy and Planning

The portfolio strategy and planning phase defines desired financial results (in each Business Unit and for the Bank) and the credit standards required to achieve them. Business strategies integrate risks and meet defined hurdles for risk-adjusted return on capital. Facility structure translates this risk-conscious business strategy into terms and conditions that mitigate risk. Portfolio management establishes composition targets, monitors the results of these diverse business strategies on a continual basis, and allows the Bank to manage concentrations that can result from seemingly unrelated activities. Specifically, portfolio management involves setting concentration limits by standard dimensions so that no one category of assets or dimension of risk can materially harm the overall performance of the Bank.

The Risk Management and Senior Management, on monthly basis reviews portfolio concentrations in terms of geographical concentrations, individual economic sectors and credit risk rating to ensure that there are no undue concentrations in one sector or risk rating, and that the limits are within those set out by the Bank. These reports are submitted to the Board on quarterly basis.

Information Related to a Licensed Bank's Risk Management (continued)

The Approving bodies (EC, SCC and CC) approve bank-wide portfolio credit concentration limits to corporate or individual counterparties based on the Bank's overall risk capacity, capital considerations, and assessment of the internal and external environments. The Bank's credit exposure to individuals or group of counterparties is in accordance with the CBK instructions BS/101/1995 on Maximum Credit Concentration Limits and subsequent amendments / updates.

The process of periodic review and approval of country and bank limits is centralized at Ahli United Bank B.S.C. (AUB) Head Office, the parent. Allocation of limits for each is advised to all group entities, including AUBK, upon annual review of such limits. These limits are further segregated in terms of Commercial Banking, Treasury and Investments.

A summary of bank wide risk exposure incorporating all the above concentration limits plus discussion on past due, non performing financings (NPFs), collateral concentration, funding profile, capital adequacy and other risk management initiatives are reviewed by the Senior Management and Group Risk on monthly basis and reported to the Board on quarterly basis.

Financing Origination and Maintenance

In the Financing origination and maintenance phase, each Business Unit solicits, evaluates and manages credit according to the strategies and portfolio parameters established in the portfolio strategy and planning phase. Transactions are generated within well-defined target market criteria, product structure and are approved on risk-adjusted basis through the use of risk rating models.

The Bank uses a Credit Risk Rating ("CRR") model to assess the credit worthiness of borrowers. The Financing risk measurement methodology is geared towards measuring Financing risk for corporate and private banking portfolio in a scale of 1 to 10 which meets the requirements of Bank for International Settlements (BIS). Risk ratings 1 to 6 for performing assets; and risk rating 7 to watch list accounts while ratings from 8 to 10 for classified accounts.

Financing maintenance involves processes to control documentation and disbursement, monitor timely repayment, value collateral and review the status of exposures. Within this phase, origination and underwriting for distribution to investors take place. A Post Fact Approval Unit independently reviews Financing approvals to ensure that the approvals are consistent with policy and that all covenants of the approvals are met prior to disbursement of proceeds and throughout the tenure of the Financing facilities.

Financing maintenance also includes early problem identification and remedial management of troubled exposures. The Special Asset Management Unit established within Risk Management Division provides a more focused attention to irregular and delinquent accounts. The primary objective of the unit is to develop effective strategies in order to either rehabilitate or restructure impaired financing .

In view of the current financial crisis, the Bank has constantly been reviewing the entire Financing portfolio and conducting stress tests in order to provide senior management with clear indication of the composition, maximum exposure at risk, overall Financing quality as well as identifying potential signs of weaknesses. As a result, the Bank is able to take timely and appropriate courses of action.

For secured Financing exposure, the collateral valuation is updated in robust manner. Quoted securities are independently valued on a daily basis while the most recent independent valuation for other securities, including real estate, is obtained. Whenever a gap in minimum-security coverage is identified, the concerned counterparty is asked to provide collateral top-up and/or reduce the outstanding exposure to comply with the minimum-security requirement. For unsecured exposure, selected counterparties are requested to provide acceptable collateral. While structuring Financing facilities, the Bank ensures that Financing exposure will be repaid from clearly identifiable and unencumbered sources of repayment.

Performance Assessment and Reporting

The performance assessment and reporting phase allows both the Senior Management and Business Units to monitor results and improve performance continually. Both portfolio and process trends are monitored in order to make appropriate and timely adjustments to business strategies, portfolio parameters, financing policies and credit origination and maintenance practices. This phase of the credit process draws on information within the Bank and external benchmarks to help evaluate performance.

Credit performance is assessed through analysis of:

1) Portfolio concentrations by obligor, industry, risk rating, tenor, product, collateral and other dimensions
2) Credit quality indicators
3) Exceptions to risk acceptance criteria
4) Other policy exceptions

The Bank has adopted an internal account profitability model (APM) to determine the profitability of corporate and private banking accounts. The methodology is based on the risk-adjusted return on capital (RAROC).

In addition, periodic review of both portfolio and process are performed by the Business Units as well as by Risk Management and Audit Division.

In accordance with the instructions of the CBK dated 18 December 1996, setting out the rules and regulations regarding the classification of financing facilities, the Bank has a Credit Classification and Evaluation Committee which is composed of senior management. The committee studies and evaluates existing financing facilities of each customer of the Bank, and identifies any abnormal situations and difficulties associated with a customer's position which might cause the debt to be classified as irregular and to determine an appropriate provisioning level.

Market Risk

The Bank defines 'Market risk' as the uncertainty in future earnings, of the Bank's on and off Balance Sheet positions, resulting from changes in market conditions i.e. changes in prices of assets and profit rates. Market risk pertains to the profit, equity, foreign exchange and commodity risks in the Bank's trading and banking books.

Market Risk management addresses the following areas:

- Quantitative parameters that define the acceptable level of market risk;
- Authorized instruments and hedging policies for managing risk exposures; and
- Exposure limits.

Risk Exposure Reporting

Risk Management Division submits on monthly basis the risk exposure report to senior management.

Information Related to a Licensed Bank's Risk Management (continued)

The Market Risk Management policy covers the following broad areas:

Profit rate risk management in the trading book and banking book;

The Bank is exposed to profit rate risk as a result of mismatches or gaps in the amounts of assets and liabilities and off balance sheet instruments that mature or re-price in a given period. The Bank manages this risk by matching the re-pricing profile of assets and liabilities through risk management strategies.

The Bank assesses its profit rate risk in the balance sheet through gapping analysis based on the re-pricing mismatches of assets and liabilities. This report is complemented by an EaR (Earnings-at-Risk) analysis, which measures the profit income volatility given a 1% parallel instantaneous change in profit rate over a one-year horizon. The main strength of the applied EaR approach is its simplicity in providing senior management a general picture of profit rate risk on the Bank's balance sheet.

Given the Islamic nature of Bank's Assets and Liabilities there is no significant exposure to profit rate risk in the Banking Book.

Foreign exchange risk management in the trading and banking book;

Foreign exchange risk in the banking book arises from a currency mismatch between the Bank's assets and liabilities. The Bank views itself as a Kuwaiti entity with Kuwaiti Dinars as its functional currency. Hedging transactions are used to manage any significant risk in other currencies. Non-monetary assets carried at fair values that are not denominated in Bank's functional currency are hedged using non-derivative Islamic financial liabilities for foreign currency risk.

Risk Management Division monitors the various foreign exchange limits (overnight, forward gap, stop loss, etc.) on daily basis and the report summarizing all these are presented to ALCO on regular basis.

Equity risk management in the trading book and banking book;

Equity price risk arises from the changes in fair values of equity investments. Values of individual securities can fluctuate in response to a variety of factors, other than movements in the profit or exchange rates. For example market valuations of equity securities may respond to factors such as operating results of the company, rights issues, key corporate decisions, changes in credit ratings of the securities and other market changes.

The Bank manages the equity risk in its trading book by setting up position limits and closely monitoring breaches. Equity risks in the banking book are mitigated through diversification of Sharia'a compliant investments in terms of risk rating, quality of issuer, marketability, transferable currencies and maturity profile.

Liquidity risk

The Bank defines liquidity risk as its ability to meet all present and future financial obligations in a timely manner and without undue effort and cost.

The following key factors are taken into consideration while assessing and managing the liquidity risk of the bank:

- The bank keeps a well diversified base for funding sources comprising a portfolio of retail customers, large corporate and institutions, small and medium enterprises, high net worth individuals without significant correlation or concentrations thereby diversifying the funding base and mitigating concentration risks.
- The past behavioral pattern analysis of our main liabilities, management expects large portion of our customers deposits to be rolled over at contractual maturity.

- As per Central Bank of Kuwait rules and regulation the bank keeps at least 18% of its deposits in qualifying short term liquid assets.
- Commitments for financing are approved after taking into account the bank's overall liquidity position.
- Criteria for the allocation of transactions into the trading book have been set by Treasury Division. Treasury Operations reviews the compliance to the established criteria for allocation of financial instruments to the trading book. Internal Audit conducts an independent review to ensure compliance on an annual basis. Any exceptions are brought to the attention of the ALCO.

In application of the general guidelines highlighted above, the bank maintains, reviews and reports the following:

A periodic Liquid Asset Ratio (LAR) report is prepared to measure the level of liquid assets available to fund short-term contractual liability obligations including unused standby commitments. Under normal circumstances, the LAR report assumes various changes in deposits in line with the historical movements Assumptions are modified depending on the change on the characteristics of deposit liabilities. The LAR is further stress tested and results are reviewed by senior management and appropriate actions are taken when needed.

A weekly liquidity gapping report is likewise prepared following the CBK guidelines which show periodic and cumulative net outflows between asset and liability run-off profiled in terms of their contractual maturities.

A daily liquidity report is submitted to senior management. This report summarizes the 8-week liquidity forecast taking into account the behavioral adjustments, duly approved by ALCO, and presents different scenarios for efficient management of liquidity risk.

A daily monitoring of the Bank's exposure to bank counterparties against approved limits and tenor is presented to senior management. The Bank, in coordination with the AUB Group, periodically reviews the latest available quantitative and qualitative information on the counterparties and based on the findings, limits and tenor are adjusted accordingly.

A weekly independent valuation report of the Bank's investment portfolio is submitted to senior management. This report presents the constitution of the portfolio and compares the latest independent valuation with that of the previous week, both at the individual investment asset and portfolio level.

In order to supplement the existing liquidity risk monitoring reports, a set of liquidity ratios, collectively known as "Management Action Triggers" (MAT), are monitored on a regular basis to manage the day-to-day liquidity funding profile of the Bank. A guiding range for each ratio has been set by ALCO and appropriate actions are taken, whenever the ratios are breached.

A liquidity contingency plan to address systemic and localized liquidity emergencies is reviewed periodically to ensure that it is kept up to date and in line with the business continuity plan.

Operational Risk

The Bank defines operational risk as the risk of direct and indirect loss resulting from inadequate or failed internal processes, people or systems or from external events. This definition clearly includes disaster recovery planning as a function of operational risk management. It is for this reason that the Bank finds it prudent to include the same consideration, namely, unexpected significant and unusual one-time events, such as disaster events in its framework for operational risk management.

The Bank's conversion to Islamic financial institution has brought with it the added risk of non compliance with Sharia'a principles. To address this risk, the Bank went through an enterprise wide assessment of potential risks, came up with robust control processes, updated the policy and procedures documents and educated the staff on the Islamic products, processes and systems. These were complemented by the establishment of the Sharia'a Board to ensure that the Bank's activities comply with the principles and rulings of the Islamic Sharia'a.

The operational risk management framework provides the Bank with the foundation for a comprehensive and an effective operational risk management program with the following major objectives:

1) Provide a clear understanding throughout the Bank of what constitutes an operational risk event;
2) Promote communication among senior management and risk taking units on various elements that impact operational risk, thereby clarifying accountability; and

Information Related to a Licensed Bank's Risk Management (continued)

3) Systematically track relevant operational risks by business lines across the Bank and build up an operational loss database.

The framework likewise outlines the quantitative approach the Bank adopts in measuring operational risk unique to the Bank's own risk profile as well as the allocation of economic capital. As an application of the quantitative approach, operational risks self assessment (ORSA) exercises, which also cover risk of non-Sharia'a compliance, are conducted on regular basis. The primary objective of the exercises is two-pronged: first, to promote greater understanding of inherent operational risks associated with business undertaken; and second, strengthen the discipline of consciously monitoring operational risks on an ongoing basis. The Bank's ORSA approach is in line with the BIS requirements and recommendations.

The Bank defines "contingency planning", Disaster Recovery Plan (DRP) and Business Continuity Plan (BCP) as the process of identifying critical information systems and business functions and developing plans to enable those systems and functions to be resumed in the event of a disruption. This process includes regular testing to ensure that contingency plans are effective. During the testing process, management verifies that the business unit plans complement the information systems plans that are in effect for mainframe functions.

The Bank's DRP, in its entirety, constitute four critical factors, namely (a) Technical DRP, (b) Business Continuity Plans, (c) logistical requirements in the event of a disaster and (d) procedures to be followed to activate during the implementation of the DRP. Integral to the DRP is the assignment of key individuals who will be tasked to trigger and oversee the DRP until the Bank regains normal operations.

The Technical DRP is the foundation on which the remaining three factors have been built up e.g. the business continuity plan or recovery process is developed, reviewed and updated based on the progress in the technical disaster recovery front. In case of disaster at Head Office, all the data is replicated at DR site on real-time basis.

The Bank has been conducting periodic DRP tests, including "data integrity" and branch "off-host" systems and procedures. The "off host" tests are conducted for all branches on regular basis. All "off host" transactions posted by the branches are accepted as soon as the system is shifted back to "on-host" mode. The data integrity test is also conducted at the Disaster Recovery Site at regular intervals. The results of both "off-host" and "data integrity" tests have been found to be satisfactory.

BCP procedures are updated regularly in line with any technical changes implemented by IT. The exercise also requires the end users to accomplish a "business impact analysis" to assess and support business continuity in the end-users' respective areas.

The above operational risk initiatives comply in all material respects with the CBK instructions dated 14 November 1996 regarding general guidelines for internal control systems and directives issued on 13 October 2003 regarding "Sound Practices for the Management and Control of Operational Risks".

Moreover, the Bank conducted fire drills intended to meet any contingency. The results of these tests were very satisfactory.

Data Security Management

Data Security is a fundamental element in a Bank's overall posture; breaches in security often pose an immediate threat. Lapses in data security could result in breaches of privacy, theft or corruption of information, contamination of programs and theft of resources or assets. An unsecured network may allow access to sensitive information (e.g., personnel, loan, or payroll records, customer information).In order to safeguard the Bank from the various security threats; a robust information security program has been established. A few of the core elements are discussed below.

- The Bank has deployed a well defined security manual which forms the basis for protecting critical information. The policy has been circulated to employees, customers, partners and others to demonstrate that the Bank takes the security of data seriously. The Bank's main statement of policy is to implement a secure information system by identifying the responsibilities at every level of information handling i.e. from data ownership (encoding) to data access.

The comprehensive security policy covers not only the technical aspects of security, but also defines how Bank employees should treat sensitive information this is to ensure:

- Data privacy
- Availability of resources
- Data integrity

- Well defined baselines are in place to handle core infrastructure including but not limited to firewalls, network devices, servers. These baselines identify the minimal configurations required to ensure security.
- To ensure the integrity of critical systems the Bank maintains change management procedures in addition to audit logs.
- Periodic vulnerability, penetration testing and configuration assessments both internally and externally on infrastructure components are carried out to ensure that the Bank maintains a good security posture.
- The Bank analyzes network traffic to important critical servers on a daily basis and proactively blocks any suspicious activity to ensure that any unseen security risks are controlled.
- The Bank also provides security guidelines on banking projects to establish an equitable and standard approach.
- Periodic audits are conducted to ensure compliance with the policies and standards set by the Bank.
- In the area of Payment Cards security, the bank has attained and maintains PCI-DSS compliance.
- The Bank is also in the process of finalizing ISO27001 certification with all the required controls in place.

Legal and Compliance

Legal risks represent the possibility of incurring a monetary loss as a result of inability to enforce contracts / agreements signed by the Bank due to faulty documentation / improper drafting. As a general rule, the Bank ensures that the counterparties and customers have legal and necessary authorities to engage in contracts and transactions with the Bank and that obligations arising from these transactions are enforceable.

Legal Division ensures that the Bank is compliant with all legislation applicable to the Bank's business activities. Meanwhile, the Compliance Officer ensures that the Bank is compliant with all the requirements of the CBK. Part of the Compliance Officer's main responsibilities is to comply with the CBK's instruction regarding combating money laundering and terrorist financing. Policy and procedures manual related to anti-money laundering are implemented.

The Bank, whenever required, follows international standards and adopts best market practices when it comes to risk management activities. RMD stays aware of developments both within the organization as well as in the marketplace to ensure that the Bank may quickly adapt its risk management policies for any significant changes. The risk control programs are periodically benchmarked against regulatory standards and industry best practices.

Whilst the Bank adheres to the regulatory standards and best market practices, it also recognizes the fact that the myriad of risks, affecting different parts of the Bank's risk-taking activities is continuously evolving. The biggest challenge, therefore, is keeping the information updated and relevant to facilitate better understanding of risk and effective response. To this end, RMD periodically performs a re-evaluation of significant risk management policies and procedures and develops action plans to correct any weaknesses. This also ensures that the Bank moves further along the continuum in terms of sophistication and analytical tools with respect to each of the risk dimensions.

Information Related to a Licensed Bank's Investment & Finance Exposures

Finance facilities with overdue amounts of over 90 days are identified as past due and in line with regulatory guidelines; facilities with overdue amounts are classified as either sub-standard, doubtful or bad depending on the number of days which the amounts are overdue. Other credit exposures are considered as impaired if its carrying amount is greater than its estimated recoverable amount. An assessment is made at each balance sheet date to determine whether there is objective evidence that a specific finance exposure, or a group of similar exposures, are impaired.

Finance facilities identified and classified as past due are subject to specific provision for impairment, the amount of provision is the difference between the carrying amount and the recoverable amount, being the present value of expected future cash flows, including amounts recoverable from guarantee and collateral, discounted based on contractual profit rate.

The provision for impairment of credit facilities covers losses where there is objective evidence that losses may be present in components of the finance facilities portfolio at the balance sheet date. These have been estimated based on historical patterns of losses in each component, the credit ratings allotted to the borrowers and reflecting the current economic climate in which the borrowers operate. Besides, as per the CBK's requirements, a minimum general provision of 1% for cash facilities and 0.5% for non cash facilities is made on all asset based & proxy based facilities not subject to specific provision.

Where available, the Group uses External Credit Assessment Institutions (ECAI) ratings for categorizing riskiness of credit assets.

ECAI's have been used for the following standard portfolios

Standard portfolio	ECAI
Claims on banks	Fitch, Moody's and Standard & Poor's

Table 3 – Gross Credit Risk Exposures Before CRM

KD 000

Standard Portfolio	Funded	Unfunded	Total Gross Credit Exposures before CRM
Claims on cash Items	9,814	-	**9,814**
Claims on sovereigns	431,090	-	**431,090**
Claims on multilateral development banks	-	-	**-**
Claims on banks	276,379	33,339	**309,718**
Claims on Corporates	1,189,144	99,307	**1,288,451**
Claims on regulatory retail	301,691	2,213	**303,904**
Past due exposures	23,766	15	**23,781**
Inventory & commodities other than real estate	103	-	**103**
Share & commercial real estate financing	136,833	3,409	**140,242**
Other exposures	105,034	2,599	**107,633**
Total	**2,473,854**	**140,882**	**2,614,736**

Table 3 - Gross Credit Risk Exposures Before CRM (continued)

KD 000

Standard Portfolio	Year end balances Funded	Year end balances Unfunded	Year end balances Total	Monthly average balances Funded	Monthly average balances Unfunded	Monthly average balances Total
Claims on cash items	9,814	-	**9,814**	8,997	-	**8,997**
Claims on Sovereigns	431,090	-	**431,090**	404,670	15	**404,685**
Claims on multilateral development banks	-	-	-	73	-	**73**
Claims on Banks	276,379	33,339	**309,718**	258,807	28,198	**287,005**
Claims on Corporates	1,189,144	99,307	**1,288,451**	1,214,775	109,368	**1,324,143**
Regulatory retail exposures	301,691	2,213	**303,904**	320,730	2,837	**323,567**
Past due exposures	23,766	15	**23,781**	24,387	19	**24,406**
Inventory & commodities other than real estate	103	-	**103**	273	-	**273**
Share & commercial real estate financing	136,833	3,409	**140,242**	150,632	4,119	**154,751**
Other exposures	105,034	2,599	**107,633**	116,902	1,965	**118,867**
Total	**2,473,854**	**140,882**	**2,614,736**	**2,500,246**	**146,521**	**2,646,767**

Average balances are calculated by averaging month-end balances of capital adequacy returns which is the most frequent reporting interval for Management reporting purpose.

Table 4 – Geographic Distribution of Exposures

KD 000

Standard Portfolio	Kuwait	Other Middle East	Europe	North America	Other Countries	Total
Claims on cash items	9,814	-	-	-	-	**9,814**
Claims on Sovereigns	431,090	-	-	-	-	**431,090**
Claims on multilateral development banks	-	-	-	-	-	**-**
Claims on Banks	77,668	173,393	48,707	5,356	4,594	**309,718**
Claims on Corporates	1,271,498	16,448	53	58	394	**1,288,451**
Regulatory retail exposures	303,904	-	-	-	-	**303,904**
Past due exposures	23,781	-	-	-	-	**23,781**
Inventory & commodities other than real estate	103	-	-	-	-	**103**
Share & commercial real estate financing	140,242	-	-	-	-	**140,242**
Other exposures	96,171	6,986	1,892	457	2,127	**107,633**
Total	**2,354,271**	**196,827**	**50,652**	**5,871**	**7,115**	**2,614,736**

Information Related to a Licensed Bank's Investment & Finance Exposures (continued)

Table 5 - Distribution of Gross Exposures by Industry

KD 000

Standard Portfolio	Funded	Unfunded	Total
Trading & Manufacturing	313,109	50,611	**363,720**
Banks & Financial Institutions	795,601	34,840	**830,441**
Construction & Real Estate	723,795	42,211	**766,006**
Others	641,349	13,220	**654,569**
Total banking book assets	**2,473,854**	**140,882**	**2,614,736**

Table 6 - Distribution of Gross Exposures by Residual Contractual Maturity

KD 000

Standard Portfolio	Upto 1 Month	1 to 3 Months	3 to 12 Months	Over 1 Year	Total
Claims on cash items	9,814	-	-	-	**9,814**
Claims on Sovereigns	230,255	90,141	110,694	-	**431,090**
Claims on Banks	232,674	36,568	24,834	15,642	**309,718**
Claims on Corporates	298,011	270,647	190,086	529,707	**1,288,451**
Regulatory retail exposures	5,000	2,449	7,682	288,773	**303,904**
Past due exposures	23,781	-	-	-	**23,781**
Inventory & commodities other than real estate	103	-	-	-	**103**
Share & commercial real estate financing	32,198	46,785	21,499	39,760	**140,242**
Other exposures	17,977	546	7,446	81,664	**107,633**
Total	**849,813**	**447,136**	**362,241**	**955,546**	**2,614,736**

Table 7 - Impaired Financings and Provision

KD 000

Standard Portfolio	Impaired Financings	Past Due Financings	Specific Provisions	Charge for the Period	Write Off	General Provisions
Trading & Manufacturing	2,517	482	1,259	1,530	2,737	7,258
Banks & Financial Institutions	13,742	154	1,437	-1,196	574	1,530
Construction & Real Estate	6,803	341	959	503	4,056	15,394
Others	33,473	6,926	13,549	4,984	31,454	13,490
Total	**56,535**	**7,903**	**17,204**	**5,821**	**38,821**	**37,672**

There are no impaired financings outside Kuwait.

As at 31 December 2010, the Group carries a total provision of KD 54,876 thousand including the above mentioned specific provision and general provision of minimum 1% on all claims on corporate and regulatory retail exposure (net of certain categories of collateral), that are not provided for specifically in line with CBK instructions. The above balances of impaired financings and past due financings include profit suspended amounting to KD 8,066 thousand.

The amount of impaired financings and past due financings outside Kuwait is not material.

Renegotiated Financing:

The Group has not renegotiated any financial asset that would otherwise be past due or impaired.

Related Party transactions

Refer note 22 to the consolidated financial statements of the Group for the year ended 31 December 2010.

Table 8 - Exposure Post Risk Mitigation and Credit Conversion

KD 000

Standard Portfolio	Rated	Unrated	Total
Claims on banks	104,484	41	**104,525**
Claims on corporates	-	668,490	**668,490**
Regulatory retail exposures	-	298,109	**298,109**
Past due exposures	-	7,317	**7,317**
Inventory & commodity other than real estate	-	129	**129**
Share & commercial real estate financing	-	67,516	**67,516**
Other exposures	-	107,633	**107,633**
Total	**104,484**	**1,149,235**	**1,253,719**

Information Related to Financing Risk Mitigation

Collateral is obtained from clients pursuant to the Bank's appraisal of the financial position, solvency, reputation and past experience of the client and the Bank's estimation of the degree of financing risks. Adequate collateral coverage ratios are maintained by the Bank in line with CBK guidelines and bank policies. In the event of a decline in value of collateral, additional coverage is sought by the Bank. A significant portion of the Bank's financing portfolio is adequately covered either by tangible collateral that adhere to the Islamic Sharia'a principles or assignment of revenues and third party receivables or other kind of support such as personal/corporate guarantees.

In order to mitigate the financing risk the Bank is exposed to, it accepts collateral in the form of cash (e.g., fixed deposits, deposit certificates and/or other savings instruments); shares / portfolio of shares traded on recognized exchanges that are compliant with the Islamic Sharia'a principles and unconditional Stand-by letters of credit or Bank guarantees by financial institutions having pre-approved limits covering principal amount plus profit.

In addition to the above, the Bank accepts lien on sponsored funds, mortgages on real estate properties and chattel, legal assignment of contracting works or supply contracts as well as legal assignment of rentals or leases.

With respect to counter-party guarantors, the Bank accepts only those that are considered investment grade risks.

Where applicable, on and off-balance sheet netting are used to the extent allowed as per the provisions of the contracted documentation, legal right to set-off and there being no maturity mismatches.

The Bank has a system of periodic collateral valuation, monitoring, and follow-up for inadequate coverage. This ensures that the Bank has an effective collateral management process, wherein:

1) The collateral are appraised periodically, following the CBK guidelines as the minimum time interval, e.g. real estate properties are appraised regularly while shares / portfolio of shares traded on recognized stock exchanges are monitored daily;
2) The minimum Financing to Value (LTV) of 50% is required upon granting share/real estate financing bearing in mind, that LTV for individual obligor maybe lower than that set parameters depending on the financing circumstances, structure of facility, and creditworthiness of the obligor;
3) the Bank execute documentation with borrowers empowering the bank, the right to liquidate or take legal possession of the collateral; and
4) The obligor and the value of the collateral do not have a material positive correlation.

Financing exposure is reviewed monthly by the RMC to ensure that there is no undue concentration. In the event that there is heavy concentration towards specific economic sector or counter-party, the Bank sells down the related assets and / or requires the client to put up sufficient liquid security.

Table 9 – Eligible Financial Collateral and Guarantees

KD 000

Standard Portfolio	Gross Exposure	Eligible CRM
Claims on Banks	309,718	21,452
Claims on Corporates	1,288,451	619,961
Regulatory retail exposures	303,904	5,246
Past due exposures	23,781	12,075
Real Estate & Shares Trading	140,242	95,231
Total	**2,066,096**	**753,965**

Information Related to Market Risk for Trading Portfolio, Foreign Exchange and Commodities Exposure

The Group currently follows the standardized approach in determining capital requirement for market risk on the trading book.

For measuring the market risk in the trading book, all positions are marked to market daily, including recognition of accrued profit, dividends or other benefits as appropriate. Foreign exchange positions are marked to market using a close-out valuation based on a mid-market price for spot positions. Financial instruments that impact profit rate risk positions, are valued based on industry accepted valuation models. Equities and commodities are marked to market, using bid prices

Table 10 - Capital Requirement For Components of Market Risk

KD 000

Standard Portfolio	Capital Charge
Commodity risk	18
Equity Position risk	6
Foreign Exchange Risk	1,272
Total	**1,296**

Information Related to Operational Risk

Operational risk is defined by Group as the risk of direct and indirect loss resulting from inadequate or failed internal processes, people or systems or from external events. The operational risk capital charge is calculated using the Basic Indicator approach. As required under this approach, the Bank has computed its capital as a percentage of the positive average annual gross income of the previous three years. Gross income for this purpose is defined as net profit income plus net non-profit income.

The Basel II accord requires banks to hold capital against operational risk. The accord offers a continuum of approaches from the simplest basic indicator approach to the more advanced measurement approaches. The Group realizes that the current spectrum of possible quantitative approaches to operational risk is broad.

In its endeavor to adopting a risk sensitive approach to assess the operational loss, the Group views operational risk management as a progression involving three layers of activity. These could be summarized as follows:

Level 1 - Risk Self Assessment deals with words more than numbers. It involves:

- Qualitative review of inherent risks
- Review of controls and procedures
- Specification of corrective actions if necessary and follow-up on implementation of such actions

The self-assessment process involves both line management (business risk officer) and external facilitator (ORSA facilitators are officers from both Risk Management and Internal Audit Divisions) to encourage frank and open discussions of issues and remedial actions. This activity is seen to generate significant amounts of descriptive and subjective rating information.

Level 2 - Key Risk Indicators (KRI) is the process of collecting and reporting on an eclectic set of quantitative measures that correlate with the likelihood of potential failures in a process. These indicators are not readily combined into a single aggregate, rather, they are useful on a comparative basis across similar processes and over time. They allow effective benchmarking of processes. When tracked overtime, they can give valuable early warning of possible problems and can facilitate timely corrective action.

Level 3 - Loss Data Collection. The Bank's collection of historical operational risk losses as well as "near misses" is an ongoing exercise. Internal loss data are not the only, or necessarily the most important, indicators of operational risk. But such losses do represent the ultimate negative consequences of process failures. Combined with external loss data (where available), they are central to scaling the magnitude of an aggregate risk capital allocation.

The Bank is resolute in reducing and controlling operational risk, and to this end, has adopted a disciplined approach to all layers of operational risk identified above. This qualitative to quantitative approach to operational risk is in line with the recommendations of the BIS.

The Bank has also documented the policy for business continuity in case of outbreak of contagious diseases. The document has been circulated to all officers and staff for their information and proper action.

Table 11 – Capital Charge For Operational Risk

KD 000

Business Line	Capital Charge
Net income from financing activities	7,975
Net income from investing activities	600
Fees and service income	2,389
Total	**10,964**

Information Related to Equity Position

Investments in the banking book are made in Sharia'a compliant instruments and are classified at the time of acquisition into those acquired for capital gains and strategic investments. The Bank also has in its books, non-Sharia'a investments that existed prior to conversion and are carried over after conversion to Islamic Bank. The Bank has three year time frame to liquidate these investments from its books as approved by Sharia'a Board. Investments acquired with a view of generating income and profits from capital appreciation are reviewed periodically and disposed off at opportune instances. The Bank reviews its strategic investment portfolio based on the industry, market and economic developments and then either liquidates or further consolidates holdings in these investments.

In accordance with International Financial Reporting Standard, equity positions in the banking book are classified as available for sale securities. These investments are fair valued periodically and revaluation gains / losses are accounted as cumulative changes in fair value in equity. For equity investments quoted in organized financial markets, fair value is determined by reference to quoted bid prices. Fair values of unquoted equity investments are determined by reference to the market value of a similar investment, on the expected discounted cash flows, or other appropriate valuation models. Equity investments whose fair value cannot be estimated accurately are carried at cost less impairment if any.

Table 12 – Equity Position in Banking Book

KD 000

Investment Type	Carrying Value	Capital Charge
Publicly Traded	8	1
Privately held	43,849	4,293
Total	**43,857**	**4,294**

Publicly traded investments represent quoted equities traded on local and international stock exchanges. Privately held investments represent investments in unquoted entities and venture funds. The total value of investments in the banking book in the balance sheet is KD 50,754 thousand, which includes KD 43,857 thousand of equity positions and KD 6,897 thousand of Sukuk investments. Cumulative realized gain from sale of available for sale securities is KD 946 thousand. The total unrealized gain recognized in the equity is KD 15,046 thousand of which KD 6,723 is included in Tier 2 Capital.

Investment Accounts

Ahli United Bank receives deposits from customers as part of several unrestricted investment accounts. These deposits are fixed-term, open-term, or renewable automatically with different investment rates.

These funds are used by the bank in all finance activities that will achieve targeted return. Investment returns are distributed among the bank as a Mudarib and investment account holders on proportionate basis for each type of these accounts and the elapsed period of these funds.

The bank also receives deposits from customers that are restricted. The bank is investing these deposits as an investment agent (Wakeel).

Customers' deposits are received and invested according to certain regulations that are mentioned in the procedures manual and instructions guide to ascertain that these funds, whether in Kuwaiti Dinar or foreign currency, are invested according to Islamic Sharia'a principles.

Ratio for the invested amount from the Investment Accounts are as per the terms and conditions agreed with the Customers.

Following are the Investment percentage for major Mudaraba based deposits used for the Profit distribution:

Deposit category	Investment Percentage
Savings	60%
1 Month	60%
3 Months	60% - 62%
6 Months	65%
9 Months	70%
1 Year	70% - 90%

Sharia'a Regulations

Sharia'ah Controller and the executive committee of Fatwa and Sharia'a Supervisory Board of the Bank monitor and execute Sharia'ah decisions issued by Fatwa and Sharia'a Supervisory Board. The Board supervises the implementation of such regulations on daily operations and answers all inquiries concerning issued Sharia'a decisions.

Certain funds are realized from Non-Sharia'a compliant transactions. These funds are identified through certain procedures designed to review entries, agreements and transactions by Sharia'a Controller during the year.

Such funds are deposited in certain charity accounts and donated as per the directions of the Bank's Fatwa and Sharia'a Supervisory Board.

Sharia'a executive committee of Fatwa and Sharia'a Supervisory Board conduct audits on the Bank's activities and presents its report to the general assembly in its annual general assembly meeting.

Zakat is calculated annually in cooperation with Zakat House and other internal control departments.

Head Office

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Commercial Area No.9
Joint Banking Complex - East Tower
Tel.: 22312535 - Fax: 22462974

Fahad Al-Salem Br.

Fahad Al-Salem St.
Al-Abrar Comercial Complex - Opp. Al-Ghanim Travel.
Tel.: 22432826 - Fax: 22405830

Ahmadi

Block 5 - Ahmadi Market - Beside Post Office.
Tel.: 23987902 - Fax: 23981289

Salmiyah

Salem Al-Mubarak St. - Salmiyah Northern Building.
Tel.: 25751960 - Fax: 25751960

Fahahil

Dabous St. - Block 8
Naief Hamad Al-Dabous Bldg.
Tel.: 23926216 - Fax: 23926215

Hawally

Tunis St. - Block 183
Heris Yousef Rashed Brously Bldg.
Tel.: 22625725 - Fax: 22625726

Jahra

Marzouq Al-moteb St. - Block 28 - Bldg.15
Tel.: 24555820 - Fax: 24555830

Ghazali

Shuwaikh - Ghazali Street
Tel.: 24848537 - Fax: 24836968

Jabriya

Block 4 - Beside Mubarak Al-Kabir Hospital.
Tel.: 25329274 - Fax: 25319904

Yarmouk

Block 2 - Street 2 - Bldg. 7
Tel.: 25337769 - Fax: 25329275

Sabah Al-Salem

Block 12
Beside Sabah Al-Salem South Clinic
Tel.: 25516357 - Fax: 25525945

Salwa

Block 5 - Behind Salwa Co-operative Society
Tel.: 25657987 - Fax: 25632275

Airport

South Farwaniya – Dajeej Area
Kuwait Airways Corp.Adm. Bldg.
Tel.: 24735295 - Fax: 24735294

Farwaniya

Habib Munawer St. – Block B
Tel.: 24740050 - Fax: 24733866

Demna

Salem Al-Mubarak St. - Ominiya center
Tel.: 25728877 - Fax: 25725680

Gharnata

Gharnata – Block (1) - Shamiya &
Shuwaikh Co-operative Society Building
Tel.: 24860357 - Fax: 24860376

Kaifan

Kaifan – Al-Jahra St.
Adjacent To Kuwait Sport Club Building
Tel.: 24837556 - Fax: 24838264

Mishref

Khalid bin AbdilAziz street, block 4
beside AlBisher Mosque
Tel.: 22312514 - Fax: 22312513

Rayya

Sharq - Al–Raya Complex
Tel.: 22997606 - Fax: 22997609

South Surra

Al-Zahra area – Ministries st.
Tel.: 22312501 - Fax: 22312504

Ministers Of Complex

Murqab – Ministers Of Complex - Ground Floor
Tel.: 22494033 - Fax: 22494031

Al-Shamiya

Al-Shamiya - Block (10)
Al-Shamiya Co-operative Society
Tel.: 24927174 - Fax: 24927176

Kout

Al-Fahaheel – Al- Kout Complex
Tel.: 23930960 - Fax: 23930961

Al Sour

Kuwait city - Al Sour st. – Al Shamiya tower
Tel.: 22331571 - Fax: 22331572

Al-Rifai

Hawally – Iben Khaldoun Street – Al Rifai Complex
Tel.: 22312559 - Fax: 22312558

360 Mall

South Al Soura – Al Zahra Area – 360 Mall
Tel: 25309604 - Fax: 22312510

Al Reqqa
block 5, street 50, next to the police station Al Reqqa
Tel: 23967190 - Fax:23167191

Al Andalus
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Tel: 24846214 - Fax:24895971

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