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Audited Financial Statements
31 December 2013

Al Ahli Bank of Kuwait K.S.C.P.

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INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF AL AHLI BANK OF KUWAIT K.S.C.P.

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of Al Ahli Bank of Kuwait K.S.C.P. (the Bank) and its subsidiary (together "the Group"), which comprise the consolidated statement of financial position as at 31 December 2013 and the consolidated income statement, consolidated statement of comprehensive income, consolidated statement of changes in shareholders' equity and consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgement, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal controls 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 at 31 December 2013, 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 account 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 the Central Bank of Kuwait ("CBK") as stipulated in CBK Circular No 2/BS/184/2005 dated 21 December 2005, as amended, the Companies Law No 25 of 2012, as amended, and by the Bank's Memorandum of Incorporation and Articles of Association, that an inventory was duly carried out and that, to the best of our knowledge and belief, no violations of the Capital Adequacy Regulations issued by the CBK as stipulated in CBK Circular No 2/BS/184/2005 dated 21 December 2005, as amended, the Companies Law No 25 of 2012, as amended, or of the Bank's Memorandum of Incorporation and Articles of Association have occurred during the year ended 31 December 2013 that might have had a material effect on the business of the Bank or on its financial position.

We further report that, during the course of our audit, we have not become aware of any violations of the provisions of Law No 32 of 1968, as amended, concerning currency, the CBK and the organisation of banking business, and its related regulations during the year ended 31 December 2013 that might have had a material effect on the business of the Bank or on its financial position.

WALEED A. AL OSAIMI
LICENCE NO. 68 A
EY
(AL-AIBAN, AL-OSAIMI & PARTNERS)

BADER A. AL-WAZZAN
LICENCE NO. 62 A
DELOITTE & TOUCHE
(AL WAZZAN & CO.)

22 January 2014
Kuwait

Consolidated Statement of Financial Position

As at 31 December 2013

	Notes	2013 (KD'000s)	2012 (KD'000s)
ASSETS			
Cash and balances with banks	3	197,921	251,477
Kuwait Government treasury bonds	4	227,673	211,775
Central Bank of Kuwait bonds	4	247,416	259,654
Loans and advances	5,20	2,189,412	1,986,869
Investment securities	22	252,168	189,545
Investment in an associate	6	13,609	10,772
Other assets	7	34,316	33,734
Premises and equipment		30,626	29,193
TOTAL ASSETS		3,193,141	2,973,019
LIABILITIES AND SHAREHOLDERS' EQUITY			
LIABILITIES			
Due to banks and other financial institutions		639,170	557,740
Customers' deposits		1,947,316	1,838,673
Other liabilities	8	65,823	59,871
TOTAL LIABILITIES		2,652,309	2,456,284
SHAREHOLDERS' EQUITY			
Share capital	9	161,917	151,324
Proposed bonus shares	9	–	10,593
Share premium	9	108,897	108,897
Treasury shares	9	(2,188)	(118)
Reserves	9	251,217	236,961
Proposed dividend	9	20,989	9,078
TOTAL SHAREHOLDERS' EQUITY		540,832	516,735
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY		3,193,141	2,973,019

Ahmed Yousuf Behbehani
Chairman

Colin Plowman
Chief General Manager and
Chief Executive Officer

The attached notes 1 to 22 form part of these consolidated financial statements.

Consolidated Income Statement
Year ended 31 December 2013

	Notes	2013 (KD'000s)	2012 (KD'000s)
Interest income	10	105,603	116,828
Interest expense	11	(21,803)	(32,510)
NET INTEREST INCOME		83,800	84,318
Net fees and commission income	12	21,984	23,420
Net foreign exchange gain		2,767	3,397
Net gain on investment securities		2,221	1,612
Dividend income		1,559	1,891
Share of results from an associate	6	1,796	667
Other income		1,495	1,144
OPERATING INCOME		115,622	116,449
Staff expenses		(19,994)	(23,291)
Other operating expenses and depreciation		(14,089)	(12,745)
OPERATING EXPENSES		(34,083)	(36,036)
OPERATING PROFIT FOR THE YEAR BEFORE PROVISIONS / IMPAIRMENT LOSSES		81,539	80,413
Provision / impairment losses	13	(43,992)	(47,361)
PROFIT FOR THE YEAR AFTER PROVISIONS / IMPAIRMENT LOSSES		37,547	33,052
Directors' fees		(360)	(280)
Taxation	14	(1,762)	(2,745)
NET PROFIT FOR THE YEAR		35,425	30,027
BASIC AND DILUTED EARNINGS PER SHARE	15	22fils	19fils

The attached notes 1 to 22 form part of these consolidated financial statements.

Consolidated Statement of Comprehensive Income

Year ended 31 December 2013

	2013 (KD'000s)	2012 (KD'000s)
NET PROFIT FOR THE YEAR	35,425	30,027
Other comprehensive income		
Items that may be reclassified subsequently to income statement:		
Effect of changes in fair values of investments available for sale	(370)	5,902
Net gain on sale / impairment losses on investments available for sale	(262)	666
Exchange difference on translation of foreign operations	(31)	62
	(663)	6,630
Items that will not to be reclassified to income statement:		
Revaluation of freehold land	483	499
	483	499
Other comprehensive (expense) income for the year	(180)	7,129
TOTAL COMPREHENSIVE INCOME FOR THE YEAR	35,245	37,156

The attached notes 1 to 22 form part of these consolidated financial statements.

Consolidated Statement of Changes in Shareholders' Equity

Year ended 31 December 2013

					Reserves									
	Share capital (KD'000s)	Proposed bonus shares (KD'000s)	Share premium (KD'000s)	Treasury shares (KD'000s)	Statutory reserve (KD'000s)	General reserve (KD'000s)	Treasury shares reserve (KD'000s)	Cumulative changes in fair value (KD'000s)	Property revaluation surplus (KD'000s)	Foreign currency translation reserve (KD'000s)	Retained earnings (KD'000s)	Total reserves (KD'000s)	Proposed dividend (KD'000s)	Total (KD'000s)
Balance as at 1 January 2012	144,118	7,206	108,897	(8,556)	53,706	53,259	6,473	18,637	5,036	(40)	80,813	217,884	21,394	490,943
Net profit for the year	–	–	–	–	–	–	–	–	–	–	30,027	30,027	–	30,027
Other comprehensive income for the year	–	–	–	–	–	–	–	6,568	499	62	–	7,129	–	7,129
Total comprehensive income for the year	–	–	–	–	–	–	–	6,568	499	62	30,027	37,156	–	37,156
Issue of bonus shares (Note 9)	7,206	(7,206)	–	–	–	–	–	–	–	–	–	–	–	–
Dividend paid (Note 9)	–	–	–	–	–	–	–	–	–	–	–	–	(21,394)	(21,394)
Treasury shares purchased	–	–	–	(104)	–	–	–	–	–	–	–	–	–	(104)
Treasury shares sold	–	–	–	8,542	–	–	1,592	–	–	–	–	1,592	–	10,134
Transfers to reserves	–	–	–	–	3,170	3,170	–	–	–	–	(6,340)	–	–	–
Proposed bonus shares (Note 9)	–	10,593	–	–	–	–	–	–	–	–	(10,593)	(10,593)	–	–
Proposed dividend (Note 9)	–	–	–	–	–	–	–	–	–	–	(9,078)	(9,078)	9,078	–
Balance as at 31 December 2012	151,324	10,593	108,897	(118)	56,876	56,429	8,065	25,205	5,535	22	84,829	236,961	9,078	516,735
Net profit for the year	–	–	–	–	–	–	–	–	–	–	35,425	35,425	–	35,425
Other comprehensive (expense) income for the year	–	–	–	–	–	–	–	(632)	483	(31)	–	(180)	–	(180)
Total comprehensive (expense) income for the year	–	–	–	–	–	–	–	(632)	483	(31)	35,425	35,245	–	35,245
Issue of bonus shares (Note 9)	10,593	(10,593)	–	–	–	–	–	–	–	–	–	–	–	–
Dividend paid (Note 9)	–	–	–	–	–	–	–	–	–	–	–	–	(9,078)	(9,078)
Treasury shares purchased	–	–	–	(2,070)	–	–	–	–	–	–	–	–	–	(2,070)
Transfers to reserves	–	–	–	–	3,743	3,743	–	–	–	–	(7,486)	–	–	–
Proposed dividend (Note 9)	–	–	–	–	–	–	–	–	–	–	(20,989)	(20,989)	20,989	–
Balance as at 31 December 2013	161,917	–	108,897	(2,188)	60,619	60,172	8,065	24,573	6,018	(9)	91,779	251,217	20,989	540,832

The attached notes 1 to 22 form part of these consolidated financial statements.

Consolidated Statement of Cashflows

Year ended 31 December 2013

	2013 (KD'000s)	2012 (KD'000s)
OPERATING ACTIVITIES		
Net profit for the year	35,425	30,027
Adjustments for:		
Net gains on sale of investments available for sale	(2,334)	(1,993)
Dividend income	(1,559)	(1,891)
Share of results from an associate	(1,796)	(667)
Depreciation	1,621	1,595
Provisions / impairment losses	43,992	43,629
Operating profit before changes in operating assets and liabilities	75,349	70,700
Changes in operating assets and liabilities:		
Deposits with banks	40,584	16,803
Kuwait Government treasury bonds	(15,898)	25,273
Central Bank of Kuwait bonds	12,238	(59,826)
Loans and advances	(241,080)	36,567
Investments at fair value through profit or loss	(197)	777
Other assets	(1,440)	5,137
Due to banks and other financial institutions	81,430	134,749
Customers' deposits	108,643	(263,760)
Other liabilities	2,569	(1,590)
Net cash flows from (used in) operating activities	62,198	(35,170)
INVESTING ACTIVITIES		
Purchase of investments available for sale	(82,820)	(68,202)
Proceeds from sale of investments available for sale	20,882	64,763
Net movement in investment in an associate	(1,041)	–
Net purchase of premises and equipments	(2,571)	(1,428)
Dividend income received	1,559	1,891
Net cash flows used in investing activities	(63,991)	(2,976)
FINANCING ACTIVITIES		
Dividend paid	(9,078)	(21,394)
Purchase of treasury shares	(2,070)	(104)
Sale of treasury shares	–	10,134
Net cash flows used in financing activities	(11,148)	(11,364)
Foreign currency translation difference	(31)	62
Net decrease in cash and cash equivalents	(12,972)	(49,448)
Cash and cash equivalents at 1 January	167,058	216,506
Cash and cash equivalents at 31 December	154,086	167,058
Cash and cash equivalent comprise:		
Cash in hand and in current account with other banks	45,849	32,236
Balances with the Central Bank of Kuwait	62,237	73,181
Deposits with banks with original maturity of thirty days	46,000	61,641
	154,086	167,058

Interest received amounted to KD 103,493 thousand (2012: KD 121,423 thousand) and interest paid amounted to KD 24,626 thousand (2012: KD 34,458 thousand).

The attached notes 1 to 22 form part of these consolidated financial statements.

1 INCORPORATION AND REGISTRATION

Al Ahli Bank of Kuwait K.S.C.P. ("the Bank") is a public shareholding company incorporated in Kuwait on 23 May 1967 and is registered as a Bank with the Central Bank of Kuwait (CBK). Its registered office is at Al Safat Square, Ahmed Al Jaber Street, Kuwait City. It is engaged in banking, primarily in Kuwait, and in the United Arab Emirates.

The Bank has a wholly owned subsidiary, Ahli Capital Investment Company K.S.C. (Closed) ("the Subsidiary") and is engaged in investment management and advisory activities, regulated by the Capital Markets Authority, Kuwait (CMA).

These consolidated financial statements of the Bank and its Subsidiary (collectively "the Group") were approved for issue by the Bank's Board of Directors on 22 January 2014. The annual general assembly of the shareholders has the power to amend these consolidated financial statements after issuance.

The New Companies Law issued on 26 November 2012 by Decree Law no. 25 of 2012 (the "Companies Law"), cancelled the Commercial Companies Law No. 15 of 1960. The Companies Law was subsequently amended on 27 March 2013 by Decree Law no. 97 of 2013 (the Decree). The Executive Regulations of the new amended law issued on 29 September 2013 and was published in the official Gazette on 6 October 2013. As per article three of the executive regulations, the companies have one year from the date of publishing the executive regulations to comply with the new amended law.

2 SIGNIFICANT ACCOUNTING POLICIES

Basis of preparation

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

The consolidated financial statements are prepared under the historical cost basis except for "investment securities", "freehold land" and "derivative financial instruments" that have been measured at fair value.

The consolidated financial statements have been presented in Kuwaiti Dinars ("KD"), which is the Bank's functional currency, rounded to the nearest thousand except when otherwise stated.

Basis of consolidation

The consolidated financial statements comprise the financial statements of the Bank and its subsidiary. The financial statement of the Subsidiary is prepared for the same reporting year as the Bank using consistent accounting policies. Subsidiaries are entities that are controlled by the Group. Control is achieved when the Group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee.

Subsidiaries are consolidated from the date on which the Group obtains control and continues to be consolidated until the date that such control ceases.

All material intra-group balances and transactions, including material unrealised gains and losses arising on intra-group transactions are eliminated on consolidation.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Changes in accounting policies

The accounting policies adopted are consistent with those of the previous financial year, except for the following new/amendments to IFRS.

IAS 1 Financial Statement Presentation:

The amendments to IAS 1 change the grouping of items presented in other comprehensive income. Items that could be reclassified (or 'recycled') to profit or loss at a future point in time (for example, upon derecognition or settlement) would be presented separately from items that will never be reclassified. The amendment has resulted in changes in the presentation of other comprehensive income.

IFRS 10 Consolidated Financial Statements:

IFRS 10, which is effective 1 January 2013, replaces the consolidation guidance in IAS 27 Consolidated and Separate Financial Statements and SIC-12 Consolidation - Special Purpose Entities by introducing a single consolidation model for all entities based on control, irrespective of the nature of the investee. Control is achieved when the Group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. The adoption of this standard did not have any material impact on the financial performance or financial position of the Group.

IFRS 12 Disclosure of Interests in Other Entities:

IFRS 12, requires enhanced disclosures about both consolidated entities and unconsolidated entities in which an entity has involvement. The objective of IFRS 12 is to require information so that financial statement users may evaluate the basis of control, any restrictions on consolidated assets and liabilities, risk exposures arising from involvements with unconsolidated structured entities and non-controlling interest holders' involvement in the activities of consolidated entities. The adoption of this standard did not have any impact on the financial performance, financial position or disclosures in the consolidated financial statements of the Group.

IFRS 13 Fair Value Measurement:

IFRS 13, replaces the guidance on fair value measurement in existing IFRS with a single standard. IFRS 13 defines fair value, provides guidance on how to determine fair value and requires disclosures about fair value measurements. However, IFRS 13 does not change the requirements regarding which items should be measured or disclosed at fair value.

Application of IFRS 13 has not materially impacted the fair value measurements of the Bank. Additional disclosures where required, are provided in the individual notes relating to the assets and liabilities whose fair values were determined.

IAS 28 Investments in Associates and Joint Ventures (as revised in 2011):

As a consequence of the new IFRS 11 Joint Arrangements and IFRS 12 Disclosure of Interests in Other Entities, IAS 28 Investments in Associates, has been renamed IAS 28 Investments in Associates and Joint Ventures, and describes the application of the equity method to investments in joint ventures in addition to associates. The adoption of this standard did not have any impact on the financial performance, financial position or disclosures in the consolidated financial statements of the Group.

Standards issued but not yet effective

The following IASB Standards have been issued but are not yet effective and have not been early adopted by the Group.

IFRS 9 'Financial Instruments':

The standard was issued in November 2009, however at the IASB meeting in July 2013, the IASB tentatively decided to defer the mandatory effective date of IFRS 9 to be left open. The standard improves the ability of the users of the financial statement to assess the amount, timing and uncertainty of future cash flows of the entity by replacing many financial instrument classification categories, measurement and associated impairment methods.

IAS 32 Offsetting Financial Assets and Financial Liabilities:

These amendments clarify the meaning of "currently has a legally enforceable right to set-off" and the criteria for non-simultaneous settlement mechanisms of clearing houses to qualify for offsetting. These are effective for annual periods beginning on or after 1 January 2014.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Standards issued but not yet effective (continued)

IAS 39 Novation of Derivatives and Continuation of Hedge Accounting:

These amendments provide relief from discontinuing hedge accounting when novation of a derivative designated as a hedging instrument meets certain criteria. These amendments are effective for annual periods beginning on or after 1 January 2014.

The application of the above standards is not expected to have a material impact on the financial position or performance of the Group as and when they become effective, except for IFRS 9 which will result in amendments and/or additional disclosures relating to classification, measurement and associated risks of financial instruments.

Financial Instruments

Classification of financial instruments

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

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 purchase and sale of financial assets are recognised using settlement date accounting i.e. the date the Group receives or delivers the assets. Changes in fair value between the trade date and settlement date are recognised in the consolidated income statement or in other 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 regulations or conventions in the market place.

De-recognition

A financial asset (in whole or in part) is derecognised either when:

- the contractual rights to receive the cash flows from the asset have expired; or
- the Group retains the 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
- the Group has transferred its rights to receive cash flows from the asset and either

- has transferred substantially all the risks and rewards of the asset, or
- 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.

Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the bank would be required to repay.

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

Initial measurement

All financial assets or financial liabilities are initially measured at fair value. Transaction costs are added to the cost of all financial instruments 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 income statement.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Financial Instruments (continued)

Subsequent measurement

Loans and receivables
These are non-derivative financial assets having fixed or determinable payments that are not quoted in an active market. These are subsequently measured at amortised cost using the effective interest method adjusted for effective fair value hedges less any provision for impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees and costs that are an integral part of the effective interest rate. The amortisation is included in "Interest income" in the consolidated income statement. The losses arising from impairment are recognised in the consolidated income statement under "Provisions / impairment losses".

Cash and balances with banks, Kuwait Government treasury bonds, Central Bank of Kuwait bonds, loans and advances and certain other assets are classified as "loans and receivables".

Investments at fair value through profit or loss
This category has two sub-categories: investments held for trading and those designated at fair value through profit or loss at inception. An investment is classified as held for trading if it is acquired principally for the purpose of selling or repurchasing in the near term. Investments are designated at fair value through profit or loss in accordance with a documented investment strategy and reported to key management personnel on that basis. These are subsequently measured at fair value and any resultant gains or losses are recognised in the consolidated income statement. The Group has not designated any investments as 'those designated at fair value through profit or loss at inception' upon initial recognition.

Investments available for sale
These are non-derivative financial assets either designated as "available for sale" or are not classified as investments at fair value through profit or loss or loans and receivables. These are subsequently measured at fair value and any resultant gains or losses are recognised through other comprehensive income. When the asset is disposed of, or impaired, the related accumulated fair value adjustments are transferred to the consolidated income statement.

Financial liabilities other than at fair value through profit or loss
These are subsequently measured at amortised cost using the effective interest method. Amortised cost is calculated by taking into account any discount or premium on the issue and costs that are an integral part of the effective interest rate. Due to banks and other financial institutions, customers' deposits and other liabilities are classified as "financial liabilities other than at fair value through profit or loss".

Derivative financial instruments and hedging
Derivatives include interest rate swaps and forward foreign exchange contracts. Such derivative financial instruments are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at fair value. Derivatives with positive fair values (unrealised gains) are included in other assets and derivatives with negative fair values (unrealised losses) are included in other liabilities in the consolidated statement of financial position. For hedges, which do not qualify for hedge accounting and for "held for trading" derivatives, any gains or losses arising from changes in the fair value of derivatives are taken directly to the consolidated income statement.

The Group makes use of derivative financial instruments to manage exposures to interest rate and foreign currency risks. Certain derivatives embedded in other financial instruments are treated as separate derivatives when their economic characteristics and risks are not closely related to those of the host contract and the host contract is not carried at fair value through profit or loss. These embedded derivatives are measured at fair value with the changes in fair value recognised in the consolidated income statement.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Financial Instruments (continued)

Subsequent measurement (continued)

Derivative financial instruments and hedging (continued)
In order to manage particular risks, the Group applies hedge accounting for transactions, which meet the specified criteria. At inception of the hedge relationship, the Group formally documents the relationship between the hedged item and the hedging instrument, including the nature of the risk, the objective and strategy for undertaking the hedge and the method that will be used to assess the effectiveness of the hedging relationship.

Also at the inception of the hedge relationship, a formal assessment is undertaken to ensure that the hedging instrument is expected to be highly effective in offsetting the designated risk in the hedged item. Hedges are formally assessed at each reporting date. A hedge is regarded as highly effective if the changes in fair value or cash flows attributable to the hedged risk during the year for which the hedge is designated are expected to offset in a range of 80 per cent to 125 per cent.

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; and (b) cash flow hedges, which hedge exposure to variability in cash flows that is either attributable to a particular risk associated with a recognised asset or liability or a highly probable forecast transaction.

Fair value hedge
In relation to fair value hedges, which meet the conditions for hedge accounting, any unrealised gain or loss from re-measuring the hedging instrument to fair value is recognised in 'Other assets' or 'Other liabilities' and in the consolidated income statement. Any gain or loss on the hedged item attributable to the hedged risk is adjusted against the carrying value of the hedged item and recognised in the consolidated income statement.

If the hedging instrument expires or is sold, terminated or exercised, or where the hedge no longer meets the criteria for hedge accounting, the hedge relationship is terminated.

Cash flow hedge
When a derivative is designated as the hedging instrument in a hedge of the variability in cash flows attributable to a particular risk associated with a recognised asset or liability or a highly probable forecast transaction that could affect profit or loss, the effective portion of changes in the fair value of the derivative is recognised directly in the other comprehensive income. The amount recognised in the other comprehensive income is removed and included in the consolidated income statement in the same year as the hedged cash flows affect profit or loss under the same income statement line item as the hedged item. Any ineffective portion of changes in the fair value of the derivative is recognised immediately in the consolidated income statement.

If the derivative expires or is sold, terminated, or exercised, or no longer meets the criteria for cash flow hedge accounting, or the designation is revoked, then hedge accounting is prospectively discontinued and the amount recognised in the other comprehensive income remains in the other comprehensive income until the forecast transaction affects profit or loss. If the forecast transaction is no longer expected to occur, then the balance in the other comprehensive income is recognised immediately in the consolidated income statement.

Financial guarantees
In the ordinary course of business, the Group gives financial guarantees, consisting of letters of credit, guarantees and acceptances. Financial guarantees are initially recognized in the consolidated financial statements at fair value, being the premium received, in other liabilities. The premium received is amortised in the consolidated income statement in 'net fees and commission income' on a straight-line basis over the life of the guarantee. The guarantee liability is subsequently measured as a higher of the amount initially recognised less amortisation or the value of any financial obligation that may arise therefrom. Any increase in the liability relating to financial guarantees is recognised in consolidated financial statements.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Financial Instruments (continued)

Offsetting

Financial assets and liabilities are offset when the Group has a legally enforceable right to offset and intends to settle either on a net basis or to realise the asset and settle the liability simultaneously.

Assets acquired in settlement of debt

Assets acquired in settlement of debts are stated at the lower of cost or fair value. Gains or losses are recognised in the consolidated income statement.

Impairment of assets

The Group assesses at each reporting date whether there is any objective evidence that an individually significant financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets are impaired if and only if, there is objective evidence of impairment as a result of one or more loss events that has occurred after the initial recognition of the financial asset and that the loss event has an impact on the estimated future cash flows of the financial asset or the group of financial assets. For the purpose of assessing impairment, the financial assets are grouped at the lowest levels for which there are separately identifiable cash flows.

For loans and receivables, if there is objective evidence of impairment loss, the financial asset is written down to its recoverable amount. For loans and receivables with fixed interest rates, the recoverable amount is the present value of expected future cash flows discounted at the original effective interest rate and for loans and receivables with variable interest rates, the recoverable amount is discounted at the current effective interest rate as determined under the contract. Future cash flow includes amounts recoverable from guarantees and collateral. Financial guarantees are assessed and impairment loss is recorded in a similar manner as for loans and receivables. The carrying amount of the asset is reduced through the use of a provision account and the amount of impairment loss is recognised in the consolidated income statement. 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 reversed by adjusting the provision account. The amount of the increase or reversal is recognised in the consolidated income statement. Loans and receivables together with the associated provision account are written off when there is no realistic prospect of future recovery and all collateral have been realised or have been transferred to the Group. If a write off is later recovered, the recovery is recognised in the consolidated income statement.

Central Bank of Kuwait directives require the Group to maintain a minimum general provision of 1% on regular cash facilities and 0.5% on regular non cash credit facilities, net of certain categories of collateral.

For available for sale equity investments, the Group assess on each statement of financial position date whether there is objective evidence that an investment or a group of investments is impaired. When there is evidence of impairment, the cumulative loss, measured as the difference between the acquisition cost and the current fair value less any impairment loss on that investment previously recognised in the consolidated income statement, is transferred from other comprehensive income and recognised in the consolidated income statement. Impairment losses on equity investments are not reversed through the consolidated income statement. Any increase in their fair value after impairment is taken directly to other comprehensive income.

For available for sale debt instruments, the Group assess the instruments at an individual level to determine whether any objective evidence for impairment exists. When there is objective evidence of impairment, the amount of loss is measured as the difference between the instrument's carrying value and the present value of the future cash flows. If in a subsequent year, the fair value of a debt instruments increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in the consolidated income statement, the impairment loss is reversed through the consolidated income statement.

Certain other assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Impairment loss is recognised for the amount by which the carrying amount of the asset exceeds its recoverable amount. The recoverable amount is the higher of the asset's fair value less cost of sale and value in use.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Financial Instruments (continued)

Renegotiated loans

In the event of a default, the Group seeks to restructure loans rather than take possession of collateral. This may involve extending the payment arrangements and the agreement of new loan conditions. When the terms and conditions of these loans are renegotiated, the terms and conditions of the new contractual arrangement apply in determining whether these loans remain past due. Management continually reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur.

Investment in an associate

An associate is an entity over which the Group has significant influence. Significant influence is the power to participate in the financial and operating policy decisions of the investee, but is not control or joint control over those policies.

The Group's investment in its associate is accounted for using the equity method. Under the equity method, the investment in the associate is carried in the consolidated statement of financial position at cost plus post acquisition changes in the Group's share of net assets of the associate. Unrealised gains and losses resulting from transactions between the Group and the associate are eliminated to the extent of the interest in the associate.

The Group's share of its associate's post-acquisition profits or losses is recognised in the consolidated income statement and its share of post-acquisition movements in other comprehensive income of associate is recognised in consolidated statement of changes in equity. Goodwill relating to the associate is included in the carrying amount of the investment and is neither amortized nor individually tested for impairment.

Where applicable, adjustments are made to bring the accounting policies of the associate in line with those of the Group. The difference in reporting date of the associate and the Group is not more than three months. Adjustments are made for the effects of significant transactions or events that occur between that date and the date of the Group's consolidated financial statements.

At each reporting date, the Group determines if there is any objective evidence that the investment in the associate is impaired, in which case the Group calculates the amount of impairment loss as the difference between the recoverable amount of the associate and its carrying value and recognises the amount in the consolidated income statement.

Upon loss of significant influence over the associate, the Group measures and recognises any retaining investment at its fair value. Any difference between the carrying amount of the associate upon loss of significant influence and the fair value of the retained investment and proceeds from disposal is recognised in the consolidated income statement.

Cash and cash equivalents

Cash and cash equivalents consists of cash on hand, balances and deposits with banks with original maturity not exceeding thirty days.

Premises and equipment

Premises and equipments other than freehold land are stated at cost less accumulated depreciation and impairment losses. Depreciation is provided on all premises and equipments, other than freehold land, at rates calculated to write off the cost of each asset on a straight line basis over its estimated useful life.

Freehold land is initially recognised at cost. After initial recognition freehold land is carried at its revalued amount which is the fair value at the date of revaluation based on valuations by external independent valuers. The resultant revaluation surplus or deficit is recognised, as a separate component under other 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 surplus is recognised in the consolidated income statement. To the extent that a revaluation surplus reverses a revaluation loss previously recognised in the consolidated income statement, the increase is recognised in the consolidated income statement. Upon disposal the revaluation surplus relating to the freehold land sold is transferred directly to retained earnings.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Premises and equipment (continued)

The assets residual values, useful lives and methods of depreciation are reviewed, and adjusted if appropriate, at each financial year end. The estimated useful lives of the assets for the calculation of depreciation are as follows:

Buildings	20 years
Furniture and equipment	3 to 5 years

The carrying amounts of premises and equipments are reviewed at each statement of financial position date to determine whether there is any indication of impairment. If any such indication exists, the assets are written down to their recoverable amounts and the impairment loss is recognised in the consolidated income statement.

End of service benefits

Provision is made for amounts payable to employees under the Kuwait Labour Law, employee contracts and respective applicable laws in the countries where the branches operate.

Treasury shares

Treasury shares consist of the Bank's own issued shares that have been reacquired by the Bank 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 the "treasury shares reserve", which is not distributable. Any realised losses are charged to the same account to the extent of the credit balance in that account. Any excess losses are charged to retained earnings then to the reserves. No cash dividends are paid on these shares. The issue of bonus shares increases the number of treasury shares proportionately and reduces the average cost per share without affecting the total cost of treasury shares.

Fair value measurement

For those assets and liabilities carried at fair value, the Group measures fair value at each statement of financial position date. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The fair value measurement of financial instruments is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- In the principal market for the asset or liability, or
- In the absence of a principal market, in the most advantageous market for the asset or liability

The principal or the most advantageous market must be accessible to the Group. The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

A fair value measurement of non-financial instruments (instruments other than financial instruments) takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Fair value measurement (continued)

The Group uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

Fair value measurement

Fair values for financial instruments traded in active markets are based on closing bid prices. For all other financial instruments including instruments for which the market has become inactive, the fair value is determined by using appropriate valuation techniques. Valuation techniques include the fair value derived from recent arm's length transaction, comparison to similar instruments for which market observable prices exist, discounted cash flow method or other relevant valuation techniques commonly used by market participants. For investments in equity instruments where a reasonable estimate of fair value cannot be determined, the investment is carried at cost.

The fair value of financial instruments carried at amortised cost, other than short-term in nature is estimated by discounting the future contractual cash flows at the current market interest rates for similar financial instruments.

Fair values of non financial instruments are measured based on valuation provided by independent valuators

The fair value of a derivative financial instrument is the equivalent of the unrealised gain or loss from marking to market the derivative financial instrument, using relevant market rates or internal pricing models.

All assets and liabilities for which fair value is measured are categorised and disclosed in the financial statements as follows

- Level 1 - Traded in the active market based on closing bid price
- Level 2 - Valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable. Valuation is derived from recent arm's length transaction, comparison to similar instruments for which market observable prices exists
- Level 3 - Valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable. Valuation techniques includes discounted cash flow method, book value method or other relevant valuation techniques commonly used by market participants.

For assets and liabilities that are recognised in the financial statements on a recurring basis, the Group determines whether transfers have occurred between Levels in the hierarchy by re-assessing categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

Revenue recognition

Interest income and expenses are recognised on an effective interest basis. Once a financial instrument categorised as loans and receivables is impaired, interest income is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. Interest income and expenses for all interest bearing financial instruments including those classified as investments at fair value through profit or loss and investments available for sale, are recognised within interest income in the consolidated income statement.

Fees and commission that are an integral part of the effective interest rate of a financial instrument are treated as an adjustment to the effective interest rate. Other fees and commission are recognized over the period of service. Dividend income is recognised when the right to receive the payment is established.

Taxation

Taxation is provided for in accordance with the fiscal regulations in Kuwait and the United Arab Emirates where the foreign branches operate.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Foreign currencies

Foreign currency transactions are recorded at rates of exchange ruling at value date of the transaction. Monetary assets and liabilities in foreign currencies outstanding at the year end are translated into Kuwaiti Dinars at rates of exchange ruling at the statement of financial position date.

Non-monetary assets and liabilities 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. Non-monetary assets and liabilities in foreign currencies that are stated at fair value are translated to Kuwaiti Dinars at the foreign exchange rates ruling at the dates that the values were determined. In case of non-monetary assets whose changes in fair values are recognised directly in other comprehensive income, related foreign exchange differences are also recognised directly in other comprehensive income. For other non-monetary assets foreign exchange differences are recognised directly in the consolidated income statement.

Assets and liabilities, both monetary and non-monetary, of foreign operations are translated at the exchange rates prevailing at the statement of financial position date. Operating results of such operations are translated at average exchange rates for the year. The resulting exchange differences are accumulated in other comprehensive income until the disposal of the foreign operation.

Segment information

A segment is a distinguishable component of the Group that engages in business activities from which it earns revenues and incurs costs. The operating segments are used by the management of the Bank to allocate resources and assess performance. Operating segments exhibiting similar economic characteristics, product and services, class of customers where appropriate are aggregated and reported as reportable segments.

Fiduciary assets

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

Use of estimates and judgements

The Group bases its estimates and judgements on parameters available when the consolidated financial statements were prepared. Existing circumstances and judgements about future developments, however, may change due to market changes or circumstances arising beyond the control of the Group.

The basis used by management in determining the carrying values of certain class of assets and the underlying risks therein are discussed below:

Impairment losses on loans and receivables

The Group reviews its loans and receivables on a regular basis to assess whether an impairment loss should be recorded in the consolidated income statement. In particular, considerable judgement by management is required in the estimation of the amount and timing of future cash flows when determining the level of provisions required. Such estimates are necessarily based on assumptions about several factors involving varying degrees of judgment and uncertainty.

Fair value measurement

Where the fair values recorded in the statement of financial position is measured using valuation techniques or pricing models, the inputs to these models are taken from either observable or unobservable data. The unobservable inputs include assumptions regarding the future financial performance of the investee, its risk profile and economic assumptions regarding the industry and geographical jurisdiction in which the investee operates.

Any changes in these estimates as well as the use of different, but equally reasonable estimates may have an impact on their carrying amounts.

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

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Use of estimates and judgements (continued)

Classification of financial assets

On acquisition of financial assets, management decides whether it should be classified as investments at fair value through profit or loss or investments available for sale or loans and receivables. Further, determining whether or not the market for a quoted financial instrument is active requires judgement based on assessment of the volume/market conditions and availability of ready and regular quotes.

Impairment of investments available for sale

The Group treats investments available for sale as impaired when there has been a significant or prolonged decline in the fair value below its cost or where other objective evidence of impairment exists. The determination of what is "significant" or "prolonged" requires considerable judgement and involves evaluating factors including industry and market conditions, future cash flows and discount factors.

3 CASH AND BALANCES WITH BANKS

	2013 (KD'000s)	2012 (KD'000s)
Cash in hand and in current account with other banks	45,849	32,236
Balances and deposits with the Central Bank of Kuwait	62,237	73,181
Deposits with banks	89,835	146,060
	197,921	251,477

4 KUWAIT GOVERNMENT TREASURY BONDS AND CENTRAL BANK OF KUWAIT BONDS

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

5 LOANS AND ADVANCES

A reconciliation of the provision for credit losses for loans and advances to customers is as follows:

	2013 (KD'000s)	2012 (KD'000s)
At 1 January	148,043	121,982
Exchange difference	53	49
Amounts written off during the year	(44,876)	(18,301)
Recoveries	1,167	1,370
Charge for the year (Note 13)	38,537	42,943
At 31 December	142,924	148,043
General Provision	119,707	122,418
Specific Provision	23,217	25,625

5 LOANS AND ADVANCES (CONTINUED)

As at 31 December 2013, loans and advances to customers individually determined to be impaired amounted to KD 60,358 thousand (31 December 2012: KD 112,106 thousand) with a specific provision of KD 23,217 thousand (2012: KD 25,625 thousand). The fair value of collateral that the Group held for impaired loans and advances to customers, as at 31 December 2013 was KD 39,317 thousand (31 December 2012: KD 99,774 thousand).

The available provision on non-cash facilities is KD 15,462 thousand (2012: KD 13,078 thousand) and is included in other liabilities (Note 8).

For disclosures relating to credit risk management, credit concentration, credit quality by class and credit risk mitigants for loans and advances, refer to note 20A.

6 INVESTMENT IN AN ASSOCIATE

During the previous year, the Bank has acquired 35% equity interest in Credit One Kuwait Holding Company K.S.C. ("Credit One"), an unquoted holding company incorporated in Kuwait engaged in providing credit facilities to customers on instalment sale of goods and services. Subsequently during the year, the Bank acquired additional 5% equity interest. Accordingly, the total equity interest in Credit one has increased to 40%.

Summarised financial information for the period ended 30 November is as follows:

	2013 (KD'000s)	2012 (KD'000s)
Assets	74,520	67,289
Liabilities	39,739	35,522
Equity	34,781	31,767
Revenue	8,976	8,312
Net profit	4,534	4,037

7 OTHER ASSETS

	2013 (KD'000s)	2012 (KD'000s)
Interest receivable	20,839	18,736
Others	13,477	14,998
	34,316	33,734

Others include KD 8,779 thousand (2012: KD 8,585 thousand) which represents assets acquired in settlement of a debt.

8 OTHER LIABILITIES

	2013 (KD'000s)	2012 (KD'000s)
Interest payable	6,800	9,695
Staff related accruals	10,154	9,507
Provisions on non cash facilities (Note 5)	15,462	13,078
Others	33,407	27,591
	65,823	59,871

9 SHARE CAPITAL AND RESERVES

a) The authorised, issued and fully paid share capital comprises 1,619,166,234 shares (2012: 1,513,239,471 shares) of 100 fils each.

The shareholders at the Annual General Meeting held on 16 March 2013 approved the distribution of cash dividend of 6 per cent amounting to KD 9,078 thousand and bonus shares of 7 per cent for the year ended 31 December 2012 (cash dividend of 15 per cent amounting to KD 21,394 thousand and bonus shares of 5 per cent for the year ended 31 December 2011). The issue of bonus shares resulted in an increase in the number of authorised and issued shares by 105,926,763 shares (2012: 72,059,022 shares) and share capital by KD 10,593 thousand (2012: KD 7,206 thousand). Treasury shares are not entitled to any cash dividends.

b) The balance in the share premium account is not available for distribution.

c) As required by the Companies Law, 10 per cent of the profit for the year before directors' fees, contribution to Kuwait Foundation for the Advancement of Sciences, National Labour Support tax and Zakat has been transferred to statutory reserve. The Bank may resolve to discontinue such annual transfers when the reserve totals 50 per cent of paid up share capital.

Distribution of this reserve is limited to the amount required to enable the payment of a dividend of 5 per cent of share capital in years when accumulated profits are not sufficient for the payment of a dividend of that amount.

d) The articles of association of the Bank require that an amount of not less than 10 per cent of the profit for the year be transferred annually to a general reserve. The transfer is before directors' fees, contribution to Kuwait Foundation for the Advancement of Sciences, National Labour Support tax and Zakat. There is no restriction on distribution of this reserve.

e) As at 31 December 2013, the Bank held 4,590,449 (2012: 202,743) of its own shares equivalent to 0.28 per cent (2012: 0.01 per cent) of the total issued share capital at the reporting date. The market value of these shares at 31 December 2013 amounted to KD 2,020 thousand (31 December 2012: KD 114 thousand).

f) The directors have proposed a cash dividend of 13 per cent for the year ended 31 December 2013, (2012: 6 per cent cash dividend and bonus shares of 7 per cent) subject to the approval of the shareholders at the annual general meeting.

10 INTEREST INCOME

	2013 (KD'000s)	2012 (KD'000s)
Balances with banks	605	2,379
Bonds and debt securities	10,967	10,934
Loans and advances	94,031	103,515
	105,603	116,828

During the year, CBK has issued Circular No. 2/RB,RBA,RS/306/2013 to all local banks and investment companies regarding formation of the Family Support Fund (the "Fund") under Law No. 104/2013. The Fund has been established to purchase outstanding balance of instalment and consumer loans from the Bank as on 12 June 2013 for loans granted before 30 March 2008. The Bank has identified these loans and is suspending interest on these loans where applications are filed by customers.

11 INTEREST EXPENSE

	2013 (KD'000s)	2012 (KD'000s)
Due to banks and other financial institutions	4,379	5,603
Customers' deposits:		
- Sight deposits	1,413	2,259
- Time deposits	16,011	24,648
	21,803	32,510

12 NET FEES AND COMMISSION INCOME

	2013 (KD'000s)	2012 (KD'000s)
Fees and commission income	23,785	24,567
Fees and commission expense	(1,801)	(1,147)
	21,984	23,420

Fees and commission income includes KD 1,190 thousand (2012: KD 932 thousand) from fiduciary activities.

13 PROVISIONS / IMPAIRMENT LOSSES

	2013 (KD'000s)	2012 (KD'000s)
Cash facilities – general	16,870	17,976
Cash facilities – specific	21,667	24,967
Charge / (release) on non cash facilities	2,383	(1,973)
Investments available for sale	2,072	2,659
Others	1,000	3,732
	43,992	47,361

14 TAXATION

	2013 (KD'000s)	2012 (KD'000s)
Kuwait Foundation for the Advancement of Sciences	337	285
National Labour Support Tax	936	793
Zakat	374	317
Tax on overseas branches	115	1,350
	1,762	2,745

15 BASIC AND DILUTED EARNINGS PER SHARE

Basic and diluted earnings per share are computed by dividing the net profit for the year by the weighted average number of shares outstanding during the year.

	2013	2012
Net profit for the year (KD '000s)	35,425	30,027
Weighted average number of the Bank's issued and paid-up shares	1,619,166,234	1,619,166,234
Less: Weighted average number of treasury shares	(1,651,873)	(9,060,155)
Weighted average number of shares outstanding during the year	1,617,514,361	1,610,106,079
Basic and diluted earnings per share (fils)	22	19

The prior year comparative has been restated for the effect of bonus shares issued during the current year.

16 RELATED PARTY TRANSACTIONS

These represent transactions with certain related parties (major shareholders, directors and senior management of the Group, close members of their families and entities of which they are principal owners or over which they are able to exercise significant influence, managed funds and an associate entity) who were customers of the Group during the period. The terms of these transactions are approved by the Group's management.

In the normal course of business, these related parties have deposits with the Bank and credit facilities granted to them by the Bank. The balances included in the consolidated financial statements are as follows:

	Number		Number of parties related to directors		Amount	
	2013	2012	**2013**	2012	**2013 (KD'000s)**	2012 (KD'000s)
Directors						
Loans and advances	4	4	2	1	12,991	2,643
Deposits	8	7	7	7	17,151	23,358
Commitments and contingent liabilities	–	–	3	2	2,958	346

Loans and advances are fully collateralised.

	Number		Amount	
	2013	2012	**2013 (KD'000s)**	2012 (KD'000s)
Key management				
Loans and advances	10	8	159	92
Deposits	10	10	669	945
Commitments and contingent liabilities	1	1	1	1
Major Shareholders				
Loans and advances	1	1	9,370	9,331
Deposits	5	5	5,362	1,735
Commitments and contingent liabilities	1	–	547	–
Associate				
Loans and advances			–	12,500
Deposits			905	754

Interest income and interest expense includes KD 1,020 thousand (2012: KD 1,632 thousand) and KD 283 thousand (2012: KD 222 thousand) respectively, on transactions with related parties.

16 RELATED PARTY TRANSACTIONS (CONTINUED)

Key management compensation

Compensation for key management is as follows:

	2013 (KD'000s)	2012 (KD'000s)
Salaries and other benefits	2,118	3,228
Post employment benefits	962	1,026
	3,080	4,254

17 COMMITMENTS AND CONTINGENT LIABILITIES

	2013 (KD'000s)	2012 (KD'000s)
Acceptances	28,661	61,965
Letters of credit	214,243	198,768
Guarantees	646,916	660,575
	889,820	921,308

The above balances represent the irrevocable contractual amounts of the Group's off balance sheet financial instruments that commit the Bank to make payments on behalf of the customers in the event of a specific act. The contractual amounts represent the credit risk, assuming that the amounts are fully advanced and that any collateral or other security is of no value. The total contractual amount of commitments to extend credit does not necessarily represent future cash requirements, since many of these commitments may expire or terminate without being funded. Total commitments to extend credit at the statement of financial position date amounted to KD 194,736 thousand (2012: KD 210,071 thousand).

18 DERIVATIVE FINANCIAL INSTRUMENTS

In the normal course of its business the Group utilises derivative financial instruments to manage its exposure to fluctuations in interest and foreign exchange rates. Derivative transactions result, to varying degrees, in credit as well as market risks.

The Group's measure of derivative related credit risk is the cost of replacing contracts at current market rates should the counter party default on or prior to the settlement date and is limited to the positive fair value of instruments that are favourable to the Group.

Market risk arises as interest and foreign exchange rates fluctuate affecting the value of a contract. For risk management purposes and to control these activities, the Group has established appropriate procedures and limits approved by the Board of Directors.

The table below shows the fair values of derivative financial instruments, recorded as assets or liabilities, together with their contractual amounts. The contractual amount, recorded gross, is the amount of a derivative's underlying asset, reference rate or index and is the basis upon which changes in the value of derivatives are measured. The contractual amounts represent the volume of transactions outstanding at the year end and are not indicative of the credit or market risk.

18 DERIVATIVE FINANCIAL INSTRUMENTS (CONTINUED)

	2013			2012		
	Assets (KD'000s)	Liabilities (KD'000s)	Contractual amounts (KD'000s)	Assets (KD'000s)	Liabilities (KD'000s)	Contractual amounts (KD'000s)
Held for hedging:						
Fair value hedges						
Interest rate swaps	212	528	54,879	–	683	16,875
Held for trading:						
Forward foreign exchange contracts	667	137	139,500	4,054	1,171	189,007
Interest rate swaps	209	249	88,883	–	439	88,883
	1,088	914	283,262	4,054	2,293	294,765

All derivative contracts are fair valued based on observable market inputs and are classified as level 2.

Forward foreign exchange contracts are contractual agreements to buy, sell or exchange a specified financial instrument at a specific price and date in the future. Forwards are customized contracts transacted on the over the counter market and are settled on a gross basis.

Interest rate swaps are contractual agreements between two parties and may involve exchange of interest or exchange of both principal and interest for a fixed period of time based on contractual terms.

19 SEGMENTAL INFORMATION

The Group is organised into segments that engage in business activities which earns revenue and incurs expenses. These segments are regularly reviewed by the chief operating decision maker for resource allocation and performance assessment. For the purposes of segment reporting the management has grouped the products and services into the following operating segments:

Commercial Banking - Comprising a full range of credit, deposit and related banking services provided to its commercial customers.

Treasury and Investment - Comprising money market, foreign exchange, treasury bonds, asset and surplus fund management, investment securities and investment in an associate.

Operating income includes operating revenue directly attributable to a segment. Segment results include revenue and expenses directly attributable to a segment. Segment assets comprise those operating assets that are directly attributable to the segment.

19 SEGMENTAL INFORMATION (CONTINUED)

Segmental information for the year ended 31 December is as follows:

	Commercial banking		Treasury and Investment		Total	
	2013 (KD'000s)	2012 (KD'000s)	**2013 (KD'000s)**	2012 (KD'000s)	**2013 (KD'000s)**	2012 (KD'000s)
Operating income	**97,139**	102,029	**18,483**	14,420	**115,622**	116,449
Segment result	**36,748**	38,750	**14,375**	10,999	**51,123**	49,749
Unallocated expense					**(13,576)**	(16,697)
Profit before tax and directors' fees					**37,547**	33,052
Segment assets	**2,271,578**	2,091,814	**856,621**	818,278	**3,128,199**	2,910,092
Unallocated assets					**64,942**	62,927
Total assets					**3,193,141**	2,973,019
Segment liabilities	**1,799,473**	1,739,506	**787,013**	656,907	**2,586,486**	2,396,413
Unallocated liabilities					**65,823**	59,871
Total Liabilities					**2,652,309**	2,456,284

The commercial banking segment includes operating income of KD 8,277 thousand (2012: KD 10,147 thousand) and segment assets of KD 195,251 thousand (2012: KD 248,463 thousand) relating to overseas branches.

20 RISK MANAGEMENT

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 financial instruments exposed to these risks, the objectives, policies and procedures for managing and measuring these risks is explained in the Risk Management section of the annual report.

The maximum exposure to credit risk as at the statement of financial position date is represented by the carrying amount of each financial asset in the consolidated statement of financial position.

Concentrations of credit risk arise when a number of counter parties are engaged in similar business activities or activities in the same geographic region, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations of credit risk indicate the relative sensitivity of the Group's performance to developments affecting a particular industry or geographic location. Maximum concentration of credit risk to a single or group of related counterparties is limited to 15 per cent of the Group's comprehensive capital as determined by the regulatory guidelines.

In accordance with the instructions of the Central Bank of Kuwait dated 18 December 1996, setting out the rules and regulations regarding the classification of credit facilities, the Group has formed an internal committee which is composed of competent professional staff and which has as its purpose the study and evaluation of the existing credit facilities of each customer of the Group. This Committee is required to identify any abnormal situations and difficulties associated with a customer's position, which might cause the debt to be classified as irregular, and to determine an appropriate provisioning level.

20 RISK MANAGEMENT (CONTINUED)

A. CREDIT RISK (continued)

Derivative financial instruments

Credit risk arising from derivative financial instruments is limited to those with positive fair values, as recorded in the consolidated statement of financial position.

Credit-related commitments risks

The Group makes available to its customers, financial guarantees which may require that the Group makes payments on their behalf. Such payments are collected from customers based on the terms of the financial guarantees. They expose the Group to similar risks to loans and advances and these are mitigated by the same control processes and policies.

Credit concentration risks

Geographical and industry sector concentrations of financial assets and contingent liabilities with credit risk are as follows:

	2013		2012	
	Assets (KD'000s)	Credit related contingent liabilities (KD'000s)	Assets (KD'000s)	Credit related contingent liabilities (KD'000s)
Geographic region:				
Domestic (Kuwait)	2,526,922	359,906	2,355,268	422,385
Other Middle East	344,468	135,307	360,816	135,940
Europe	136,643	94,202	86,954	96,381
United States of America	5,908	475	2,949	375
Rest of the world	37,706	299,930	46,075	266,227
	3,051,647	889,820	2,852,062	921,308
Industry sector:				
Trading and manufacturing	320,614	194,709	292,139	185,903
Banks and other financial institutions	586,834	414,680	559,877	377,979
Construction and real estate	703,860	198,385	729,011	246,003
Personal	756,233	5,115	658,644	15,919
Government	475,089	–	471,429	–
Others	209,017	76,931	140,962	95,504
	3,051,647	889,820	2,852,062	921,308

20 RISK MANAGEMENT (CONTINUED)

A. CREDIT RISK (continued)

Gross maximum exposures and credit quality of financial instruments

The table below shows the maximum exposure to credit risk for the components of the consolidated statement of financial position, without taking account of any collateral and other credit enhancements. The maximum exposure is shown gross, before the effect of mitigation through the use of master netting and collateral agreements.

The table also shows the credit risk exposure by credit quality of financial assets by class, grade and status:

	Neither Past due nor Impaired			Past due including individually impaired (KD'000s)	Gross Maximum exposures (KD'000s)
	High Grade (KD'000s)	Standard grade (KD'000s)	Acceptable grade (KD'000s)		
31 December 2013					
Balances with banks	182,882	6	–	–	182,888
Kuwait Government treasury bonds	227,673	–	–	–	227,673
Central Bank of Kuwait bonds	247,416	–	–	–	247,416
Loans and advances					
- Loans to customers	1,594,958	166,304	176,098	101,785	2,039,145
- Loans to banks	150,267	–	–	–	150,267
Debt securities available for sale (Note 22)	176,595	3,500	–	–	180,095
Other assets	21,302	1,183	1,227	451	24,163
Total	2,601,093	170,993	177,325	102,236	3,051,647
31 December 2012					
Balances with banks	242,792	12	–	–	242,804
Kuwait Government treasury bonds	211,775	–	–	–	211,775
Central Bank of Kuwait bonds	259,654	–	–	–	259,654
Loans and advances					
- Loans to customers	1,423,674	235,959	136,467	108,960	1,905,060
- Loans to banks	81,809	–	–	–	81,809
Debt securities available for sale (Note 22)	122,049	5,000	–	–	127,049
Other assets	21,171	1,646	932	162	23,911
Total	2,362,924	242,617	137,399	109,122	2,852,062

The gross maximum credit risk exposure relating to contingencies amounts to KD 889,820 thousand (2012: KD 921,308 thousand).

20 RISK MANAGEMENT (CONTINUED)

A. CREDIT RISK (continued)

Gross maximum exposures and credit quality of financial instruments (continued)

The high, standard and acceptable grades of classification of loans to customers above is based on inherent credit quality of the counterparties, the assessed risk profile, acceptability and availability of collateral in accordance with Group's internal rating model. Grading of balances with banks, loans to banks and debt investments available for sale are based on the external rating of the counterparties.

Past due including individually impaired loans and advances above include KD 64,828 thousand (2012: KD 23,697 thousand) which are past due for less than 90 days and are not considered as impaired.

The fair value of collateral that the Group held for past due including individually impaired loans and advances to customers, as at 31 December 2013 was KD 65,035 thousand (31 December 2012: KD 139,631 thousand). The Group has taken adequate legal measures to secure recovery of collateral when needed. Impairment losses on loans and advances are disclosed in Note 5.

Where financial instruments are recorded at fair value the amounts shown above represent the current credit risk exposure but not the maximum risk exposure that could arise in the future as a result of changes in values.

Collateral and other credit enhancements

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 are cash, securities, and charges over real estate properties and counter-guarantees.

Management monitors the market value of collateral on an ongoing basis and requests additional collateral, if required, in accordance with the underlying agreement. At 31 December 2013, the Group held collateral with a fair value of KD 1,925,076 thousand (31 December 2012: KD 1,834,563 thousand).

It is the Group's policy to repossess collaterals mortgaged and reduce or repay the outstanding claims. The repossessed assets are disposed depending upon the market conditions and regulatory directives. In general, the Group does not use repossessed assets for business.

At 31 December 2013, 50.67 per cent (31 December 2012: 52.40 per cent) of the total outstanding loans to customers were secured with a collateral coverage of 1.51 times (2012: 1.52 times) the underlying loans.

B. LIQUIDITY RISK

Liquidity is the ongoing ability to accommodate maturing liabilities and deposit withdrawals; fund asset growth and business operations; and meet contractual obligations through unconstrained access to funding at reasonable market rates.

Liquidity risk is the risk that the Group will encounter difficulty in raising funds to meet commitments associated with financial instruments. Liquidity risk may also result from an inability to sell a financial asset quickly at close to its fair value. The financial instruments exposed to these risks, the objectives, policies and procedures for managing and measuring these risks are explained in the Risk Management section of the annual report.

20 RISK MANAGEMENT (CONTINUED)

B. LIQUIDITY RISK (continued)

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.

Financial liabilities	Less than one month (KD'000s)	One month to one year (KD'000s)	One year to five years (KD'000s)	Total (KD'000s)
31 December 2013				
Due to banks and other financial institutions	155,512	487,877	–	643,389
Customers' deposits	1,184,843	641,450	136,423	1,962,716
Other liabilities	–	59,023	–	59,023
	1,340,355	1,188,350	136,423	2,665,128
31 December 2012				
Due to banks and other financial institutions	162,998	343,928	55,907	562,833
Customers' deposits	1,004,846	717,366	139,177	1,861,389
Other liabilities	–	50,176	–	50,176
	1,167,844	1,111,470	195,084	2,474,398

Contractual amounts for gross settled derivative positions total to KD 228,383 thousand (2012: KD 277,890 thousand), of which KD 96,597 thousand (2012: KD 118,779 thousand) expires within three months.

Substantially all acceptances and letters of credit commitments expire within a year, while 60 per cent (2012: 63 per cent) of the guarantees expire within one year, while the remaining portion expires within a period not exceeding five years.

The table below summarises the maturity profile of the Group's assets and liabilities. The maturities of assets and liabilities have been determined on the basis of the remaining period at the statement of financial position date to the contractual maturity date, except for equity investments classified at fair value through profit or loss, equity investments available for sale, investment in an associate and premises and equipment. The maturity profile for investments at fair value through profit or loss, equity investments available for sale, investment in an associate and premises and equipment is determined based on management's estimate of liquidation of those investments.

The actual maturities may differ from the maturities shown below since the borrower may have the right to prepay obligations with or without prepayment penalties, and customers' deposits might have to be repaid on demand.

20 RISK MANAGEMENT (CONTINUED)

B. LIQUIDITY RISK (continued)

The maturity profile as at 31 December 2013 was as follows:

	Less than one month (KD'000s)	One month to one year (KD'000s)	One year to five years (KD'000s)	Over five years (KD'000s)	Total (KD'000s)
ASSETS					
Cash and balances with banks	183,818	14,103	–	–	197,921
Kuwait Government treasury bonds	6,337	126,652	84,684	10,000	227,673
Central Bank of Kuwait bonds	61,485	185,931	–	–	247,416
Loans and advances	577,786	1,028,709	373,683	209,234	2,189,412
Investment securities	–	82,999	151,100	18,069	252,168
Investment in an associate	–	–	13,609	–	13,609
Other assets	–	25,537	8,779	–	34,316
Premises and equipment	–	–	–	30,626	30,626
Total assets	829,426	1,463,930	631,855	267,929	3,193,141
LIABILITIES					
Due to banks and other financial institutions	155,015	484,155	–	–	639,170
Customers' deposits	1,183,409	636,702	127,205	–	1,947,316
Other liabilities	–	65,823	–	–	65,823
Total liabilities	1,338,424	1,186,680	127,205	–	2,652,309

20 RISK MANAGEMENT (CONTINUED)

B. LIQUIDITY RISK (continued)

The maturity profile as at 31 December 2012 was as follows:

	Less than one month (KD'000s)	One month to one year (KD'000s)	One year to five years (KD'000s)	Over five years (KD'000s)	Total (KD'000s)
ASSETS					
Cash and balances with banks	223,950	27,527	–	–	251,477
Kuwait Government treasury bonds	10,762	121,419	74,594	5,000	211,775
Central Bank of Kuwait bonds	94,969	164,685	–	–	259,654
Loans and advances	426,321	1,002,172	385,273	173,103	1,986,869
Investment securities	–	68,941	107,786	12,818	189,545
Investment in an associate	–	–	10,772	–	10,772
Other assets	–	25,149	8,585	–	33,734
Premises and equipment	–	–	–	29,193	29,193
Total assets	756,002	1,409,893	587,010	220,114	2,973,019
LIABILITIES					
Due to banks and other financial institutions	162,903	339,619	55,218	–	557,740
Customers' deposits	1,002,610	709,219	126,844	–	1,838,673
Other liabilities	–	59,871	–	–	59,871
Total liabilities	1,165,513	1,108,709	182,062	–	2,456,284

C. MARKET RISK

C.1 INTEREST RATE RISK

Interest rate risk arises from the possibility that changes in interest rates will affect future cash flows or the fair values of financial instruments. The Board has established limits on the interest rate gaps for stipulated years. Positions are monitored on a daily basis and hedging strategies are used to ensure positions are maintained within the established limits. The financial instruments exposed to these risks, the objectives, policies and procedures for managing and measuring these risks are explained in the Risk Management section of the annual report.

The sensitivity of interest rate variability on the Group's consolidated income statement is the effect of the assumed changes in interest rates on the net interest income for one year, based on the floating rate financial assets and financial liabilities held at 31 December 2013 including the effect of hedging instruments. The sensitivity of interest rate variability on the Equity is calculated by revaluing fixed rate investments available for sale, including the effect of any associated hedges as at 31 December 2013 for the effects of the assumed changes in interest rates and is analysed by maturity of the asset or swap.

20 RISK MANAGEMENT (CONTINUED)

C. MARKET RISK (continued)

C.1 INTEREST RATE RISK (continued)

The following table reflects the effect of 25 basis points change in interest rates, with all other variables held constant.

	Effect			
	2013		2012	
	Net profit (KD'000s)	Equity (KD'000s)	Net profit (KD'000s)	Equity (KD'000s)
Kuwaiti Dinar	1,347	24	1,666	–
US Dollars	131	584	103	764

C.2 CURRENCY RISK

Currency risk is the risk that the value of financial instruments will fluctuate due to changes in foreign exchange rates. The Board of Directors has set limits on positions by currency. Positions are monitored on a daily basis and hedging strategies are used to ensure positions are maintained within established limits. The financial instruments exposed to these risks. The objectives, policies and procedures for managing and measuring these risks are explained in the Risk Management section of the annual report.

The effect on net profit for the year, as a result of 5 per cent change in currency rate due to the changes in fair value of monetary assets and liabilities, with all other variables held constant is shown below:

	Effect	
	2013 (KD'000s)	2012 (KD'000s)
Currency		
US Dollars	38	18
Euro	2	1
Others	48	22

C.3 EQUITY PRICE RISK

Equity price risk is the risk that the fair values of equities decrease as the result of changes in the levels of equity indices and the value of individual stocks. The equity price risk exposure arises from the Bank's investment portfolio. The financial instruments exposed to these risks, the objectives, policies and procedures for managing and measuring these risks are explained in the Risk Management section of the annual report.

The effect on consolidated income statement (as a result of equity price risk on investments at fair value through profit and loss and further impairment on impaired available for sale equity investments) and on Equity (as a result of a change in the fair value of available for sale equity investments), as at 31 December, due to a 5 per cent change in equity indices, with all other variables held constant is as follows:

	Effect			
	2013		2012	
	Net profit (KD'000s)	Equity (KD'000s)	Net profit (KD'000s)	Equity (KD'000s)
GCC Stock Exchanges	188	875	272	782

20 RISK MANAGEMENT (CONTINUED)

C. MARKET RISK (continued)

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 or later than expected, such as fixed rate loans and advances when interest rates fall. Majority of the Group's interests bearing financial assets are at floating rates. Also, majority of the interest bearing financial liabilities have a maturity of less than 1 year and accordingly, the Group is not exposed to significant prepayment risk. The financial instruments exposed to these risks, the objectives, policies and procedures for managing and measuring these risks are explained in the Risk Management section of the annual report.

D OPERATIONAL RISK

Operational risk is the risk of loss arising from systems failure, human error, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to financial loss. The Group cannot expect to eliminate all operational risks, but through a control framework and by monitoring and responding to potential risks, the Group is able to manage the risks. Controls include effective segregation of duties, access, authorisation and reconciliation procedures, staff education and assessment processes, including the use of internal audit. The financial instruments exposed to these risks, the objectives, policies and procedures for managing and measuring these risks are explained in the Risk Management section of the annual report.

The Risk Management Division manages operational risks in line with the Central Bank of Kuwait instructions dated 14 November 1996, concerning the general guidelines for internal controls and the instructions dated 13 December 2003, regarding the sound practices for managing and supervising operational risks in banks.

21 CAPITAL MANAGEMENT

The Group's regulatory capital and capital adequacy ratios are as follows:

	2013 (KD'000s)	2012 (KD'000s)
Risk weighted exposure	**1,903,911**	1,816,694
Capital required	**228,469**	218,003
Capital available :		
Tier 1 capital	**482,448**	471,530
Tier 2 capital	**30,344**	30,820
Total Capital	**512,792**	502,350
Tier 1 capital adequacy ratio	**25.34%**	25.96%
Total capital adequacy ratio	**26.93%**	27.65%

The disclosures relating to the Capital Adequacy Regulations issued by Central Bank of Kuwait as stipulated in CBK Circular number 2/BS/184/2005 dated 21 December 2005, as amended, are included under the Risk Management section of the annual report.

22 FAIR VALUE MEASUREMENT

Financial Instruments

Financial Instruments comprise of financial assets and financial liabilities.

Financial assets consist of cash and balances with banks, Kuwait Government treasury bonds, Central Bank of Kuwait Bonds, loans and advances, investment securities and certain other assets. Financial liabilities consist of due to banks and other financial institutions, customer deposits and certain other liabilities.

The fair value of financial instruments are categorised as under:

Investment securities

	Investments at fair value through profit or loss		Investments available for sale	
	2013 (KD'000s)	2012 (KD'000s)	**2013 (KD'000s)**	2012 (KD'000s)
Level 1:				
Equity	985	788	11,383	11,660
Debt securities	–	–	164,843	115,349
Level 2:				
Equity	–	–	25,841	23,881
Debt securities	–	–	11,752	6,700
Managed funds	–	–	11,482	4,182
Level 3:				
Equity	–	–	19,331	21,985
Debt securities	–	–	3,500	5,000
Managed funds	–	–	3,051	–
	985	788	251,183	188,757

The fair value of the above investment securities is categorised as per the policy on fair value measurement in Note 2. Movement in level 3 is mainly on account of purchases and change in fair value. During the year, a decrease of KD 2,315 thousand (2012: increase of KD 1,480 thousand) was recorded in the other comprehensive income representing change in fair value. There were no material transfers between levels during the year.

Fair values of all other financial instruments are not materially different from their carrying value.

The impact on the consolidated statement of financial position or the consolidated statement of shareholders' equity would be immaterial if the relevant risk variables used to fair value the unquoted securities were altered by 5 per cent.

Non Financial Instruments

Instruments carried at fair value, other than financial instruments, include assets acquired in settlement of debt and freehold land (classified as premises and equipments) were fair valued using significant valuation inputs based on unobservable market data and is classified under level 3 fair value hierarchy.

If the freehold land was measured using the cost model, the net carrying amount as at 31 December 2013 would be KD 16,600 thousand (2012: KD 16,599 thousand).

Al Ahli Bank of Kuwait K.S.C.P.

Established in the State of Kuwait
By Amiri Decree on 23 May 1967
Paid Up Capital as at 31 Dec 2013: KD 161,916,623.404
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Telex: 22067, 23256, 23257
Reuters: AHLK
SWIFT: ABKK-KW-KW
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