

Annual Report 2011

Kuwait Financial Centre

المرکز
MARKAZ



H.H. SHEIKH SABAH AL-AHMAD AL-JABER AL-SABAH
The Amir of The State of Kuwait



H.H. SHEIKH NAWAF AL-AHMAD AL-JABER AL-SABAH
The Crown Prince



H.H. SHEIKH JABER AL-MUBARAK AL-HAMAD AL-SABAH
The Prime Minister

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BOARD OF DIRECTORS

Mr. Diraar Yusuf Alghanim	Chairman & Managing Director
Sheikh Humoud Sabah Al-Sabah	Vice Chairman
Mr. Faisal AbdulAziz Al-Jallal	Director
Mr. Ayman Abdulatif Alshaya	Director
Mr. Fahad Yaqoub Al-Jouan	Director
Mr. Fouzi Ebrahim Al-Mukaimi	Director
Mr. Adel M. AlGhannam	Director

BOARD STEERING COMMITTEE

Diraar Yusuf Alghanim	Chairman
Ayman Abdulatif Al-Shaya	Director
Fahad Yaqoub Al-Jouan	Director
Manaf AbdulAziz Alhajeri	Secretary

AUDIT COMMITTEE

Faisal AbdulAziz Al-Jallal	Chairman
Fouzi Ebrahim Al-Mukaimi	Director
Adel M. AlGhannam	Director
Maha I. Al-Kadi	Secretary

MANAGEMENT TEAM

Manaf AbdulAziz Alhajeri	Chief Executive Officer
Ali H. Khalil	Chief Operating Officer
Gopal Menon	Executive Vice President – International Investments
Bassam N. Al-Othman	Executive Vice President – MENA Real Estate
Amani Al-Omani	Executive Vice President – MENA Equities
Khaled A. Chowdhury	Executive Vice President – Financial Management
M.R. Raghu	Senior Vice President – Research
Ali Mustafa Abdal	Senior Vice President – Human Resources & Administration
Maha I. Al-Kadi	Senior Vice President – Private Equity & Fund Administration
Nawaf H. Marafi	Senior Vice President – Oil & Gas
Carole Six	Vice President – Institutional Sales
Leila Badine	Vice President – Markaz Lebanon Branch
Fahad G. Al-Abdul Jaleel	Vice President – Private Banking
Pradeep Rajagopalan	Vice President – Compliance & Risk Management
Johnny Al-Khoury	Vice President – Information Technology
Basma A. Ghareeb	Assistant Vice President – Media & Communications

DIRECTORS' REPORT 2011

Dear Stakeholders,

2011: A year of popular revolutions and policy evolution

Kuwait: Challenges despite sound fiscal and political positions

CMA: a problematic birth

The Financial Sector: key challenges and opportunities

In 2011, major markets around the world witnessed corrections as a result of a number economic and political turmoil, impacting both economies and societies worldwide. In the United States, fiscal policies have undergone a thorough reevaluation to assess their effectiveness in the aftermath of the 2008 subprime crisis. The Eurozone's economic stability was undermined by alarming levels of indebtedness of Greece and other member countries, which challenged the institutional, legal, and fiscal infrastructure of the common currency.

Meanwhile, several Arab countries witnessed popular revolutions on the back of flawed governance, difficult living conditions, diminishing work opportunities, and absence of fair and equal opportunities. Such extraordinary events have led to severe disruptions in their economies and harshened their investment climates.

Kuwait, with its mature constitution, democratic life, established institutions, free press, and excellent state finances was not immune to the economic upheavals. The reluctance by banks to extend credit combined with the rise in the cost of funding to the Private Sector continued to weigh heavily on the private sector, pushing down asset values.

Kuwait's Development Plan (KDP), approved by the national assembly since February 2010, had a start that lacked the critical requirements of any endeavor; namely proper well defined objectives, action plan, and relevant performance indicators. Unclear to a large degree in its parameters, the (KDP) failed so far to address in a coherent manner the four key elements of development: economic macro management and redressing structural imbalance; the structure of government organizations including financial institutions; management of human resources and job market; and enabling the public sector of reform.

In 2011, we witnessed the official launch of the long awaited regulatory body of the financial services industry, the Capital Markets Authority (CMA). This authority had a turbulent start when it came to addressing its critical priorities. Among issues pending is the stability of the commissioners' team. Many (CMA) clauses need to be amended as they were seemingly imposed without adequate study about the structure of our markets. Some of these articles threaten the business model in the non-banking financial services industry, which in turn can undermine his highness the Emir's vision of Kuwait as a regional financial centre.

Delay in solving such issues presented to the (CMA) by many market players, and despite the states excellent finances and credit ratings by all international rating agencies, played a primary role behind the severe deterioration of equities listed at Kuwait Stock Exchange (KSE). We therefore firmly believe that the key sector priority now is to change the mindset behind the (CMA) from a pure law and penalty enforcement to that of a business and economic development stimulus.

As a result of this situation, a huge pressure on daily trading and on the prices of equities of the Kuwait Stock Exchange was witnessed in 2011. The banking sector, constituting the largest segment of blue-chip companies, can be impacted by such pressures when it comes to capital increases for example, which in turn can undermine the banking sector's capital adequacy requirements. Some clauses in the (CMA) law can also result in fund managers' bias towards equities with small to medium market value, affecting the quality of mutual funds' assets.

Undoubtedly, the governance of the financial sector comes at the heart of debates related to the various economic and financial crises. However, and given the business economic model of our GCC economies, no private sector can be truly reformed without a sophisticated and strong public sector that is deep in its assessment of the critical issues, pro-knowledge and learning, and effective in its execution.

We therefore believe that the governance as a debate should now be broadened to include the public sector to help it better articulate its objectives, clarify decisions, improve its transparency, and develop high level performance measurement parameters. This is especially important when it comes to the government's role in crucial issues such as restoring Kuwait's historical image as a pro business environment; undertaking major reform in the public sector to improve its services; taking tangible action to support the private sector as a key partner to create jobs, executing major projects; and supporting small and medium enterprises.

The debate of governance is indeed profound and far reaching, extending well beyond the private sector to reach all of the state's public institutions. It is essential to implement a culture of merit, excellence, transparency and empowerment of public sector leaders to reach a world standard administration of our public institutions. Furthermore, the importance of a proper policy articulation to promote and coordinate efforts among the numerous institutions in their implementation and interaction with the private sector cannot be overemphasized.

Financial Results for the Year 2011

Markaz managed to close the most challenging year 2011 with a marginal loss of KD 230,000 or (1) fils per share as compared with a net profit of KD 8.17 million, or 17 fils per share from 2010. Shareholders' equity stood at KD 84 million, a decline of 4.3% over 2010. Markaz losses came out milder than expected as a result of strong returns from its private equity and real estate investments both regionally and in the US; which offset the decline in its investments in public equities. In addition, Markaz fees for the year reached KD 8.2 million, versus KD 8.1 million for 2010 on the back of stronger investment banking fees over 2010, though, a 20% decline in Assets Under Management (AUM) to KD 830 million as of 2011 was also witnessed.

Markaz capital structure remains healthy, with a net-debt to equity ratio of 32%. Markaz has substantially extended the maturity of its liabilities and its liquidity through the issuance of a KD 22 million unsecured bond, which matures in December 2016. The proceeds will be used to repay its US 100 million bond maturing July, 2012.

Markaz bond was rated BBB by Capital Intelligence; and has attracted strong interest from institutional investors as well as family offices and banks resulting in 45% oversubscription. The success of the placement, and the diversity of the investors, reflect the investors' confidence in Markaz's ability to prudently manage its risk and liquidity.

As Markaz has done in the past, it starts 2012 with a well-diversified asset base, a liquid balance sheet and available credit lines that gives it the flexibility and ability to alter its asset allocation to benefit from the volatile fast changing environment we are in, and properly align asset and liability maturities.

DIRECTORS' REPORT 2011 (continued)

Our Activities

Asset Management

MENA Equities

As the region struggled with extraordinary events such as the Arab spring and the EU debt crisis, the year ended with a loss of 9.2% for the S&P Pan Arab Composite Index. Qatar was the only MENA market to close the year positively with a gain of 7.5% while Saudi closed with a minor loss of 0.4%. Heavy spending by the Saudi Government in the social and infrastructure sectors led to a strong performance by the cement and retail sectors which emerged as the main out-performers for the year.

On the adverse side, the Egypt equity market witnessed one of its worst yearly performances as the country is still struggling to achieve social and economic stability. The S&P Egypt Index lost 46.8% for the year and S&P UAE Index also lost 15.2% for the year.

In Kuwait, mergers of companies and ambiguity over the Capital Markets Authority's (CMA) rules have negatively affected the investment climate in the country. Therefore, the S&P Kuwait Index lost 16.5% for the year. Banking remained the only attractive sector to investors with its earnings and dividend visibility even though trading volumes continued to remain low.

International Investments

2011 was a tough year for mutual funds as managers struggled to create alpha and were having trouble navigating through such volatile markets. U.S. Treasuries were the best performing asset class as 10-Year Treasuries rallied 16.7%. In addition, Emerging Markets, which were expected to lead the recovery, were by far the worst performing equity markets globally as a result of increased pressures from central banks' tightening policies to curb inflation, thus drying up liquidity.

The U.S. Dollar remained resilient as the reserve currency increased 1.5% for the year. Even though U.S. equity markets were flat for the year, the S&P 500 traded within a band of 300 points. In Europe, legislators have failed to reach to an effective solution to end the sovereign debt fiasco. We saw slow reforms of policymakers, lagged responses from the ECB, reluctance of core countries including Germany and France to support weaker economies for fear of "socializing debt," and Euro banks with extensive exposure to sovereign debt. The MSCI Europe Index ended the year at -13.8%.

Private Equity

Due to the volatility of debt and equity markets in 2011, there was a general slowdown of the market for private equity deals, especially exits valued at over USD 1 billion. Despite these challenges, "Markaz Private Equity Portfolio" witnessed growth in these exits and thus registered positive results.

Treasury

The Treasury Department has maintained sufficient liquidity levels yielding the proper balance of asset & liability maturities. This approach enabled Markaz to timely honor its financial obligations.

Furthermore, the Department has assisted Markaz's managed entities operating on a regional and international level in setting up their entire core banking operations and ensuring the availability of the best service facilities. The Treasury Department looks forward to continuing to expand its network with the local, regional and international banks ensuring maximum benefit for Markaz and its clients.

Banking remained the only attractive sector to investors with its earnings and dividend visibility even though trading volumes continued to remain low

U.S. Treasuries were the best performing asset class in 2011

Investment Banking

Corporate Finance

The events in the region early on in 2011 have caused governments to substantially alter their priorities, and caused investors to reassess country risk. In general, subsidies and social programs have taken priority over development programs, fueling public spending and consumer spending.

The much anticipated PPP projects in Kuwait have not come to fruition at the anticipated pace, and hence, corporate finance activities related to government projects have been stagnant. The private sectors in most of the GCC countries, except for Saudi Arabia, continue to suffer from production overcapacity, and are deleveraging. Saudi Arabia is in expansion, mainly in construction, executing government projects and fulfilling the large demand for housing.

The encouraging sign this year was the revival of the debt capital market. The appetite for Kuwaiti debt is returning, and three bond issues were successfully placed in the fourth quarter of 2011. Furthermore, Markaz witnessed a strong interest for distressed debt by regional and international investors; the Corporate Finance department executed several trades in the space, positioning Markaz as a market maker for such debt. This was encouraging as it provided the market with benchmarks to price credit default, and helped banks and creditors to agree on realistic debt restructuring plans.

Markaz continues to build strong capabilities in distressed debt and restructuring of creditors, which is helping us win asset management as well as investment banking mandates in the distressed space. In particular, we are focusing on providing advisory services related to restructuring liabilities of companies, disposing non-core assets for clients, and raising fresh capital for local corporations.

Fixed Income

In spite of the adverse economic and political events such as the Euro Debt Crisis, the downgrade of the US Debt markets by S&P, Middle East political upheaval, and the volatile oil prices, the GCC bond markets have relatively fared well in 2011. The total GCC Bonds & Sukuk issuance was USD 50.63 billion compared to USD 31.06 billion in 2010 with a total of five Bonds & Sukuk issuances from Kuwait with a total value of USD 90 million.

In January 2011, Markaz launched Fixed Income Fund "MFIF". The fund's main objective is to provide investors with stable returns by investing in highly rated Bonds and Sukuk issued by GCC governments and corporations.

In 2012, GCC fixed income market is expected to remain affected by uncertainty inflicted by global economic and regional political conditions. On the other hand, GCC sovereigns and corporations are expected to continue with the issuance trends witnessed in the past two years, driven by sovereign determination to create yield curves and develop bonds market, and actual financing needs by regional corporations.

Markaz Fixed Income team aims to increase AUMs by providing investors with customized fixed income portfolios which comply with their investment needs, in addition to revisiting investment strategy of its current fund MFIF to take advantage of the prevailing market conditions. On the advisory side, the team aims to continue to offer advisory services, utilizing its structuring and placement capabilities to assist local companies in meeting their financing and liquidity needs. The team will also continue to cooperate with the Capital Market Authority, the Gulf Association of Bonds and Sukuk (GABS) and regional asset managers in their efforts to develop a secondary market for Bonds and Sukuk in Kuwait.

The encouraging sign this year was the revival of the debt capital market

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DIRECTORS' REPORT 2011 (continued)

Structured Finance

Markaz has been the sole options market maker in the Middle East since 2005

Markaz has been the sole options market maker in the Middle East since 2005. This reflects the company's belief in the importance of having a developed options market. Markaz employs its high caliber skills, expertise, and resources to achieve this objective.

The number of stocks covered in the Options Market at the Kuwait Stock Exchange was decreased. The removal of those stocks from the options market came as a result of adjusting the fund's strategy. The adjustment aimed to enhance the fund's performance by eliminating stocks that have failed to meet its selection criteria due to the rapid changes in the market's conditions. The list of companies traded on the options market remains dynamic depending on the latest risk and liquidity measures.

The total number of traded contracts declined by 46% from 7,227 contracts in 2010 to 3,906 contracts in 2011; the underlying value for those contracts also declined by 57% from KD 85.125 million in 2010 to an underlying value of 36.571 million in 2011.

In 2011, Markaz Structured Finance team finalized the development and testing phases of a new application "Forsa Bridge" that will integrate Forsa Options Trading System to Kuwait Stock Exchange NASDAQ OMX new trading platform.

The Structured Finance team followed up all pending proposals with Kuwait Stock Exchange which will develop the options market in Kuwait when executed. The major proposals submitted by Markaz are to allow investors to issue options contracts covered by their portfolio and to allow new market-makers in the options market to stimulate competition and liquidity.

The team also upgraded its trading infrastructure with industry standard analytics that are fast, accurate, robust, and scalable in 2011. It has also launched a dedicated options page within the company's corporate website, which provides information on the options market, pricing mechanisms and spot prices.

MENA Real Estate Investments

Fundamentals drive GCC Real Estate Markets with the residential sector on top

Kuwait's residential apartments and light industrial real estate sectors achieved growth in value by an average of 8% in 2011. The residential sector in Saudi market also preserved its positive momentum in 2011 and is expected to be the most attractive sector in the GCC. Qatari real estate was stable throughout the year with a slight improvement in occupancy levels. Across these countries, the office space continued its decline due to the continuing pressure from oversupply and weak demand. Abu Dhabi witnessed a retreat in value and prices in all real estate sectors. We expect the residential sector to preserve its positive momentum in 2012; albeit at a slower pace, the commercial and office space is expected to be stable in 2012 but we do not foresee an increase in occupancy.

Regarding MENA region, the Egyptian market is expected to provide good investment opportunities despite the current period of unrest, which is expected to have a positive effect by reducing supply of office space in the abundantly supplied market and promoting new Cairo developments over the troubled Cairo centre. Libya, Iraq, Syria, Lebanon, Tunisia, Morocco have good potential that depends on the stability of each country.

"MREF" invests in income generating properties and is unexposed to weak sectors

"Markaz Real Estate Fund", which invests in income generating properties in the Kuwaiti Market and has no exposure to the adversely affected office sector, was able to attract significant funds from new investors and acquired a number of attractive income generating properties. The fund continued to pay monthly cash distributions to investors amounting to 7% of the par value per annum.

Residential development in KSA

Markaz Real Estate Development Company (MREDco), conceived to benefit from the pent-up demand for residential units in KSA, progressed with its villas development in Al Khobar in the Eastern Province of Saudi Arabia. A first batch of villas is expected to be delivered in the first month of 2012 with buyers already expressing interest in the

Exiting investments with returns and dividends

“MREOF” an opportunistic investment tool

Opportunities and Plans

Stabilization of commercial real estate values in the U.S; fundamentals have started to improve, driven by signs of an economic recovery

project. The project is on track for completion during Q2 2012 and we expect to exit the investment by the end of 2012.

In 2011 Markaz exited Lusail Waterfront Development, an investment at Qatar managed by Masraf Al Rayan. Investors in Lusail Waterfront Development investment achieved a gross return of 20%.

“Markaz Real Estate Opportunities Fund”, which manages investments in Lebanon, KSA, Jordan, Syria, Abu Dhabi and Qatar was able to exit its investment in Qatar and distribute the proceeds to its investors. The fund also completed one of its developments in Jordan, expecting to exit the development and distribute its proceeds in Q1 2012. Efforts are in place for exiting residential developments in Jordan and land development in KSA while work continues for the remaining investments as planned.

Markaz plans to develop and retain a residential property in KSA and in Kuwait as part of its plan to benefit from the moderate return against the low risk of such investments. In addition to focusing on KSA, Markaz Real Estate team is looking into Qatar market, which is set to recover starting 2012 on the back of the large infrastructure projects being launched.

International Real Estate

Several factors in the last 18 months have contributed to the stabilization of commercial real estate values in the U.S; fundamentals have started to improve, driven by signs of an economic recovery led by Government stimulus and a stronger corporate sector, and lower yields driven by competitive bidding activity for premium assets. Notwithstanding the above, over \$1.2 trillion of commercial real estate mortgages mature in the next four years, and leveraged borrowers and lenders will continue to face challenges going forward refinancing maturing debt.

Consistent with this outlook, we have focused on the preservation of capital values for our existing funds. Towards this:

- In the second quarter, we concluded the sale of Markaz U.S. Industrial Realty Investment Unit I's portfolio of warehouse properties for approximately \$170 million. The sale generated a net IRR to end investors of approximately 9.0% and a total return on investment multiple of 1.75 times over the life of the fund.
- During the year, we successfully secured the extension / refinancing of the mortgage loans for each of the three projects of the Markaz U.S. Multifamily Realty Investment Unit – IV. In fact, two of the mortgage loans were refinanced with agency debt at attractive terms and now each of the projects have appropriate medium- to-long-term financing in place to allow organized sale efforts.

Furthermore, in order to capitalize on the prevalent distress in real estate debt markets, we are continuing to grow our U.S. distressed debt portfolio, seeking to invest in non-performing and sub-performing commercial mortgages in the U.S. During the year, we added five new transactions to our portfolio, bringing the total number of distressed debt acquisitions to twelve.

Oil and Gas

Oil prices fared well in 2011 with the Brent and the WTI advancing 13% and 8% respectively. On the other hand, abundance of natural gas supplies pushed prices lower with the Henry Hub declining 32% in 2011. The on-going uncertainty driven by the European sovereign debt crisis, the Arab Spring, and the prospects of global economic recovery continued to fuel volatility in the equities markets, which extended to the oil and gas sector equities. International energy equities traded lower with the MSCI World Energy Index and the Oil Service Sector Index (OSX) declining by 2% and 12% respectively in 2011. Regional energy equities tracked by the Bloomberg GCC Energy Index, declined by 10% during the year. Regional petrochemicals stocks declined with the Tadawul Petrochemical Industries Index losing 4.4% in 2011.

“MEF” continues to examine potential investment opportunities having considerable growth potential, in the drilling and oilfield services segments in the MENA region

Partnership of research institutions and governmental entities towards enriching knowledge base

Markaz Economic Policy Research

Markaz opens support office for research in India

Consolidation of existing partnership and development of new products

DIRECTORS' REPORT 2011 (continued)

The Oil and Gas Department manages the Markaz Energy Fund “MEF” which invests in a diversified portfolio within the oil & gas sector. “MEF” experienced a difficult year in 2011 with large losses stemming from the full impairment undertaken on money market funds in Q2. Furthermore, “MEF’s” investments in local/regional oil & gas equities had an adverse effect on the Fund’s performance.

Notwithstanding, “MEF” was able to restrict losses during the year, with a potential for upward revision as further clarity is gained on impaired assets.

For example, Kosan Crisplant, one of “MEF’s” major investments appears to be on the road to recovery in turnover and order backlog. The company has achieved major milestones during the year which includes securing key orders worth EUR 4.1 million in November alone. “MEF” continues to examine potential investment opportunities having considerable growth potential, in the drilling and oilfield services segments in the MENA region.

Kuwait First Transportation Company (KFTC), a company that leases equipment primarily to contractors in the energy sector and has both Markaz and “MEF” as investors, achieved 31% return on investment since inception. KFTC continued to implement its expansion plans in 2011. The company is growing its client base and is currently negotiating opportunities to grow inorganically through acquisitions.

Support Departments

Research

Sustainable economic growth and development can only be achieved with a strong partnership between government entities and corporate society based on a broad, objective knowledge base. Markaz is committed to aiding in increasing the depth and breadth of GCC information base in order to enhance and deepen the intellectual discussion. We believe that such an enhancement will go a long way towards increasing the efficiency of the country’s capital markets, economic development, and regulatory efforts. To that end, Markaz has also partnered with several prestigious and internationally recognized bodies to conduct high level public policy research on various aspects of the Kuwait economy and fiscal environment.

Markaz has initiated public policy research in cooperation with leading institutions. We signed an MOU for cooperation with IFRI (Paris), a leading research institution that specializes in energy studies; also, we commissioned studies with policy research scholars from the London School of Economics and from Princeton University. The areas of research revolve around topics such as sustainable economic development, overcoming labor market segmentation in Kuwait, and powering Kuwait into the 21st century.

Markaz has established Marmore MENA Intelligence Private Limited in Chennai, India with the aim of providing services of financial research and analysis of Mena economies, markets, and companies. The research team at Marmore is positioned to support Markaz in providing the very best investment ideas to its clients in addition to enriching the local/regional investment landscape with a full range of quantitative, unbiased research.

Institutional Sales

In 2011, the Institutional Sales Department worked actively to consolidate Markaz partnership with the Gulf Bank of Kuwait. The department has also initiated new collaboration with other GCC banks. Distribution of Markaz products has expanded, including equity and fixed income asset classes. New and innovative investment ideas have also been discussed and agreed upon, which should result in the launch of new products in 2012.

The Media and Communications Department enhances communications transparency at the highest standards

Corporate Social Responsibility

State Governance & Self Governance

Private Banking

The Private Banking Department (PBD) strives to meet clients' needs by venturing beyond providing conventional investment solutions and daily monitoring of clients' assets. The PBD, therefore, provides value added services that include reporting the latest developments in markets and the different sectorial and geographic classes of assets. These value added services are designed to enable our clients to make sound investment decisions based on well-researched information.

Media and Communications

The Media and Communications Department enhances communications transparency at the highest standards. The department role exceeds traditional corporate communication standards to include alliances and cooperation with local and international institutions in the fields of economic research to raise investment awareness in the current challenging environment. The department also has sustained close relationships with The Union of Investment Companies and many economic institutions that are concerned with the investment sector in order to deliver our proposals.

Within its Corporate Social Responsibility (CSR) policy, Markaz continued to support nonprofit activities related to sustainable development. Markaz focused in 2011 on issues related to human development and public health, cooperating with prominent Non-Governmental Organizations such as Lothan Youth Achievement Center (Loyac), Kuwait Association for Care of Children at Hospital (KACCH), Kuwait University and A.C. Milan Football School – Kuwait.

Compliance and Risk Management

Markaz has a comprehensive Risk Management, Compliance and Control Framework in place to ensure that the company and its related entities are appropriately governed. The Board directs the policy and process framework and is responsible for risk management and for all risk control systems that are implemented in Markaz, as well as related entities.

The Board's governance mandate is implemented through an independent Compliance and Risk Management Department. The department identifies measures, evaluates and reports on all credit risks, liquidity and market risks to which Markaz is exposed. It carries out periodic risk control and monitoring activities, and also prepares and implements new review and control policies.

The department also follows up and documents governance activities in the company including the Board's Steering Committee, which reviews and approves investment performance and investment decisions; and the Board Audit Committee which checks the effectiveness of internal controls. As part of its mandate, the Department coordinates with Regulatory Auditors, Internal Auditors, rating agencies and Internal Control Review (ICR) auditors.

During 2011, the risk management team has been working closely with the business to enlarge the concept of risk and include measures to enhance the system's robustness. In continuation of the long term strategy, Markaz risk management team has been adopting a prudent investment policy amidst heightened volatility in the local and international markets. The department was also involved in risk planning for new asset management software to upgrade the service offerings of Markaz.

As a part of Internal Compliance, the department introduced all Markaz staff to the Capital Markets Authority (CMA) law and its implications. It also played a significant role in reviewing Markaz and Markaz products in order to achieve compliance with CMA articles.

DIRECTORS' REPORT 2011 (continued)

During 2011, an internal control auditor reviewed Markaz's Internal Control Framework. The auditor was appointed pursuant to the directive of Central Bank of Kuwait (CBK) to all investment companies to be audited as part of the Internal Control Review exercise. The auditor provides an opinion on whether the internal control systems applied within Markaz were compliant to the Manual of Directives issued by CBK in all material respects. The ICR auditor does an overall assessment of the internal control system and its adequacy for each business area to address the relevant risks.

Markaz and its Kuwait based funds were also audited in 2011 by the Central Bank of Kuwait. Moreover, Markaz portfolios were audited by Kuwait stock exchange to ensure that trading activities are in line with relevant directives issued by Kuwait stock exchange.

The Department is also represented in various internal committees such as the Budget Management Committee, Investment Advisory Committee, Compliance and IT Committee, Assets and Liabilities Committee and Loan Classification Committee.

Information Technology

The Information Technology Department (IT) has been working closely with other departments and vendors to develop the new Asset Management system; a major solution that will replace several key applications with a single point customized to Markaz's vast requirements.

Moreover, the IT department plays an integral part of the Business Continuity plan by ensuring that the Disaster Recovery policies and procedures are applied at a company-wide level. These policies and procedures are designed and implemented according to the industry's standards and periodically reviewed by a top-tier consulting service. Hardware and software projects remain an integral part of the department's activities, in addition to end-user support on day-to-day basis.

Financial Management Department

Executing Markaz policy, Financial Management Department (FMD) has comprehensively implemented International Financial Reporting Standards (IFRS). Working within a strategic framework aligned with the company's annual financial budget, the department continued the application of conservative approaches to improve operational efficiency and reduce risk.

In 2011, local legislations have tightened regulatory measures for the investment sectors through three ratios: spanning liquidity, leverage, and foreign exposure. FMD, hence, has been exerting utmost endeavors to maintain full compliance. Strict adherence, as a continuous process, has been maintained adequately with regulatory bodies and more significantly with the "Capital Markets Authority" (CMA) that came into effect in March 2011.

Transaction Processing & Reporting Department

In line with regulatory requirements to strengthen internal controls and enhance operational efficiency, Markaz had undergone an internal restructuring of the back office functions by consolidating various teams into one Transaction Processing and Reporting Department (TPR). The Department has been a vital factor in enhancing Markaz's control and commitment towards best international practices.

TPR's main goal is to ensure that convergence and streamlining of the Company's back-office functions (Primarily Settlement, Reconciliation, and Reporting) are carried out as effectively and efficiently as possible to minimize operational risk. To achieve this objective, processes were streamlined and cross training was done amongst the newly constituted TPR team on the existing portfolio management systems and revised processes.

Financial Management Department (FMD) has comprehensively implemented International Financial Reporting Standards (IFRS)

Developing and measuring the performance of human capital

The department's primary system was upgraded to a new version enhancing its capability to handle multi-currency portfolios and reports. An implementation of a new system is planned to strengthen the Company's capabilities in handling diverse asset classes on one platform.

Human Resources and Administration

The Human Resources and Administration Department continued in 2011 its constant endeavor to upgrade the skills of Markaz employees and strengthen the organization. The department is working on developing a "Performance Management Scheme" that will integrate corporate goals and objectives to performance planning/appraisal; talent management; compensation, reward, and recognition. In addition, the Department continues to upgrade and update its policies, procedures, and systems as part of its constant improvement process. The department also extended its efforts to recruit the appropriate candidates for all Markaz staffing requirements.

Outlook

Looking ahead, the few companies that survived the crisis in 2008 can aim to have a different business model that focuses on alternative assets like debt, distressed assets, private equity and real estate. They can also progressively work on achieving their goals in the region. Traditional benchmark oriented fund management is currently not favorable with investors as they are favoring products focusing on wealth preservation and volatility management. This can be achieved through enhancing the quality of professionals working in the sector and renewing the focus on customer service.

We also foresee signs of positive activities in Kuwait's bond market as several companies issued bonds in the fourth quarter of 2011. We expect these activities to continue in 2012. We also anticipate promising opportunities in the residential part of the real estate sector, which showed steadiness during economic turbulence.

We believe in the importance of developing the primary and secondary debt capital markets in Kuwait due to the favorable impact it would have on the cost and success of the Kuwait Development Plan. In addition, such markets would provide Kuwaiti investors with low risk and regulated investment instruments and decrease long term debt. Despite the benefits of debt capital markets and the fundamental role they could play in financing the country's development plan, the next stage should include developing the regulations required by capital market institutions in Kuwait and increasing coordination among them.

We would like to seize this opportunity to thank our Shareholders and Clients for their continued support and to our staff for their dedication and relentless efforts which helped the company stand firmly with strong prowess. We also extend our gratitude to the regulatory authorities, specifically, the Central Bank of Kuwait, the Capital Markets Authority (CMA), the Kuwait Stock Exchange and the Ministry of Commerce and Industry, for their cooperation.

The Board of Directors

13 March 2012

INDEPENDENT AUDITORS' REPORT

To the Shareholders of

Kuwait Financial Centre – SAK (Closed)

Kuwait

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of Kuwait Financial Centre – SAK (Closed) (“parent company”) and its subsidiaries, (“the group”) which comprise the consolidated statement of financial position as at 31 December 2011, and the consolidated statement of income, statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, as adopted for use in 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' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditors' consider 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 Kuwait Financial Centre – SAK (Closed) and its subsidiaries as at 31 December 2011, and their financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards, as adopted for use in the State of Kuwait.

Report on Other Legal and Regulatory Matters

In our opinion, proper books of account have been kept by the parent company and the consolidated financial statements, together with the contents of the report of the parent company's board of directors relating to these consolidated financial statements, are in accordance therewith. We further report that we obtained all the information and explanations that we required for the purpose of our audit and that the consolidated financial statements incorporate all information that is required by the Commercial Companies Law of 1960 and by the company's articles of association, as amended, that an inventory was duly carried out and that, to the best of our knowledge and belief, no violations of the Commercial Companies Law of 1960 nor of the parent company's articles of association, as amended, have occurred during the year that might have had a material effect on the business or financial position of the parent company.

We further report that, during the course of our audit, we have not become aware of any material violations, during the year, 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.

Abdullatif M. Al-Aiban (CPA)
(Licence No. 94-A)
of Grant Thornton – Al-Qatami, Al-Aiban & Partners

Jassim Ahmad Al-Fahad
(Licence No. 53-A)
of Al-Fahad, Al-Wazzan & Co. – Deloitte & Touche

Kuwait

17 January 2012

CONSOLIDATED STATEMENT OF INCOME

	Notes	Year ended 31 December 2011 KD '000	Year ended 31 December 2010 KD '000
Revenue			
Interest income	8	1,271	1,566
Dividend income		187	54
Management fees and commission	9	8,189	8,088
Loss on sale of investments at fair value through statement of income		(131)	(75)
Change in fair value of investments at fair value through statement of income	11	(5,449)	4,668
Gain on redemption/sale of available for sale investments		3,555	1,991
Gain on sale of investment properties		-	44
Foreign exchange (loss)/gain		(308)	12
Loss on liquidation of subsidiaries	7	(17)	(36)
Other income		1	42
		7,298	16,354
Expenses and other charges			
General and administrative expenses	12	(5,472)	(5,698)
Impairment of available for sale investments	20	(1,265)	(839)
Reversal of provision for credit losses		2	30
Reversal/(charge) of impairment of investments properties	21	143	(274)
Finance costs	13	(936)	(874)
		(7,528)	(7,655)
(Loss)/profit before contribution to Kuwait Foundation for the Advancement of Sciences (KFAS), National Labour Support Tax (NLST), Zakat and directors' remuneration		(230)	8,699
Provision for contribution to KFAS		-	(78)
Provision for NLST		-	(249)
Provision for Zakat		-	(99)
Directors' remuneration		-	(105)
(Loss)/profit for the year		(230)	8,168
Attributable to:			
Owners of the parent company		(356)	8,123
Non-controlling interests		126	45
(Loss)/profit for the year		(230)	8,168
Basic and diluted (loss)/earnings per share attributable to the owners of the parent company	14	(1) Fils	17 Fils

The notes set out on pages 22 to 50 form an integral part of these consolidated financial statements.

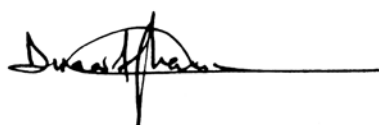
CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

	Year ended 31 December 2011 KD '000	Year ended 31 December 2010 KD '000
(Loss)/profit for the year	(230)	8,168
Other comprehensive income:		
Available for sale investments:		
- Net change arising during the year	(1,782)	3,785
- Transferred to consolidated statement of income on sale	(3,555)	(1,991)
- Transferred to consolidated statement of income on impairment	1,265	839
Cash flow hedges		
- Net change arising during the year	314	3
Foreign currency translation		
- Exchange differences arising on translation of foreign operations	(31)	(17)
Total other comprehensive (loss)/income for the year	(3,789)	2,619
Total comprehensive (loss)/income for the year	(4,019)	10,787
Total comprehensive (loss)/income attributable to:		
Owners of the parent company	(4,149)	10,751
Non-controlling interests	130	36
	(4,019)	10,787

The notes set out on pages 22 to 50 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

	Notes	31 December 2011 KD '000	31 December 2010 KD '000
Assets			
Cash and bank balances	15	3,750	2,177
Time deposits	15	19,107	3,500
Investments at fair value through statement of income	16	41,863	52,097
Accounts receivable and other assets	17	3,362	6,164
Short-term financing	18	878	-
Loans to customers	19	11,884	12,893
Available for sale investments	20	52,645	56,823
Investment properties	21	7,538	2,340
Property and equipment		394	426
Total assets		141,421	136,420
Liabilities and equity			
Liabilities			
Due to banks and other financial institutions	15	-	3,753
Accounts payable and other liabilities		3,976	5,215
Short-term borrowings		-	5,500
Bonds	22	49,896	28,060
Total liabilities		53,872	42,528
Equity			
Share capital	23	53,130	50,600
Share premium	24	7,902	7,902
Legal reserve	25	13,005	13,005
Voluntary reserve	26	12,951	12,951
Treasury shares	27	(16,342)	(16,342)
Treasury shares reserve		7,973	7,973
Other components of equity	28	3,522	7,315
Retained earnings		2,031	9,521
Equity attributable to the owners of the parent company		84,172	92,925
Non-controlling interests		3,377	967
Total equity		87,549	93,892
Total liabilities and equity		141,421	136,420



Diraar Yusuf Alghanim
Chairman & Managing Director



Manaf AbdulAziz Alhajeri
Chief Executive Officer

The notes set out on pages 22 to 50 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	Attributable to the owners of the parent company							Non-controlling interests	Total		
	Share capital	Share premium	Legal reserve	Voluntary reserve	Treasury shares	Treasury shares reserve	Other components of equity			Retained earnings	
	KD '000	KD '000	KD '000	KD '000	KD '000	KD '000	KD '000	KD '000	KD '000		
Balance at 1 January 2011	50,600	7,902	13,005	12,951	(16,342)	7,973	7,315	9,521	92,925	967	93,892
(Loss)/profit for the year	-	-	-	-	-	-	-	(356)	(356)	126	(230)
Other comprehensive (loss)/income (note 28)	-	-	-	-	-	-	(3,793)	-	(3,793)	4	(3,789)
Total comprehensive (loss)/income for the year	-	-	-	-	-	-	(3,793)	(356)	(4,149)	130	(4,019)
Issue of bonus shares (note 29)	2,530	-	-	-	-	-	-	(2,530)	-	-	-
Dividends (note 29)	-	-	-	-	-	-	-	(4,579)	(4,579)	-	(4,579)
Arising on part disposal of subsidiary (note 7)	-	-	-	-	-	-	-	(25)	(25)	25	-
Capital contribution by non-controlling interests	-	-	-	-	-	-	-	-	-	2,255	2,255
Transactions with owners	2,530	-	-	-	-	-	-	(7,134)	(4,604)	2,280	(2,324)
Balance at 31 December 2011	53,130	7,902	13,005	12,951	(16,342)	7,973	3,522	2,031	84,172	3,377	87,549

The notes set out on pages 22 to 50 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY (CONTINUED)

	Attributable to the owners of the parent company							Non-controlling interests	Total		
	Share capital	Share premium	Legal reserve	Voluntary reserve	Treasury shares	Treasury shares reserve	Other components of equity			Retained earnings	Sub Total
	KD '000	KD '000	KD '000	KD '000	KD '000	KD '000	KD '000	KD '000	KD '000	KD '000	
Balance at 1 January 2010	50,600	7,902	12,140	12,086	(16,342)	7,973	4,687	3,125	82,171	47	82,218
Profit for the year	-	-	-	-	-	-	-	8,123	8,123	45	8,168
Other comprehensive income/(loss) (note 28)	-	-	-	-	-	-	2,628	-	2,628	(9)	2,619
Total comprehensive income for the year	-	-	-	-	-	-	2,628	8,123	10,751	36	10,787
Arising on sale of subsidiaries	-	-	-	-	-	-	-	-	-	(43)	(43)
Arising on part disposal of subsidiaries	-	-	-	-	-	-	-	3	3	196	199
Capital contribution by non-controlling interests	-	-	-	-	-	-	-	-	-	731	731
Transactions with owners	-	-	-	-	-	-	-	3	3	884	887
Transfer to reserves	-	-	865	865	-	-	-	(1,730)	-	-	-
Balance at 31 December 2010	50,600	7,902	13,005	12,951	(16,342)	7,973	7,315	9,521	92,925	967	93,892

The notes set out on pages 22 to 50 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

Notes	Year ended 31 December 2011 KD '000	Year ended 31 December 2010 KD '000
OPERATING ACTIVITIES		
(Loss)/profit for the year	(230)	8,168
Adjustments for:		
Depreciation	128	139
Gain on redemption/sale of available for sale investments	(3,555)	(1,991)
Gain on sale of investment properties	-	(44)
Loss on liquidation/disposal of subsidiaries	17	36
Impairment of available for sale investments	1,265	839
(Reversal)/charge of impairment of investments properties	(143)	274
Reversal of provision for credit losses	(2)	(30)
Foreign exchange gain on bonds	(164)	(620)
Finance costs	936	874
Dividend income	(187)	(54)
Interest income	(1,271)	(1,566)
	(3,206)	6,025
Changes in operating assets and liabilities:		
Investments at fair value through statement of income	10,234	(10,932)
Accounts receivable and other assets	3,058	(1,374)
Short term financing	(878)	54
Loans to customers	1,011	(990)
Accounts payable and other liabilities	(1,013)	664
Net cash from/(used in) operating activities	9,206	(6,553)
INVESTING ACTIVITIES		
Term deposit maturing after three months	(4,003)	-
Purchase of property and equipment	(96)	(64)
Proceeds from redemption/sale of available for sale investments	10,732	6,459
Purchase of available for sale investments	(10,680)	(12,310)
Purchase of investment properties	(2,712)	(975)
Proceeds from disposal of investment properties	-	336
Proceeds from liquidation/disposal of subsidiaries	39	263
Dividend income received	187	54
Interest income received	959	1,343
Net cash used in investing activities	(5,574)	(4,894)

The notes set out on pages 22 to 50 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS (CONTINUED)

	Notes	Year ended 31 December 2011 KD '000	Year ended 31 December 2010 KD '000
FINANCING ACTIVITIES			
Net (repayment)/receipt of short term borrowings		(5,500)	1,488
Proceeds from issue of bonds		22,000	-
Dividends paid		(4,491)	(24)
Finance costs paid		(936)	(874)
Capital contribution by non-controlling interest		2,255	731
Net cash from financing activities		13,328	1,321
Foreign currency adjustments		(30)	(8)
Increase/(decrease) in cash and cash equivalents		16,930	(10,134)
Cash and cash equivalents at the beginning of the year		1,924	12,058
Cash and cash equivalents at the end of the year	15	18,854	1,924
Non-cash transactions			
Available for sale investments		2,343	-
Purchase of investment properties		(2,343)	-

The notes set out on pages 22 to 50 form an integral part of these consolidated financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

31 December 2011

1. Incorporation and activities

Kuwait Financial Centre – SAK (Closed) (“the parent company”) was incorporated in 1974 in accordance with the Commercial Companies Law in the State of Kuwait. The parent company is listed on the Kuwait Stock Exchange and is governed under the directives of the Central Bank of Kuwait and Capital Market Authority of Kuwait.

The principal activities of the parent company and its subsidiaries (“the group”) are investment management, corporate financing, investment and financial advisory services, private equity funds, mutual funds and real estate funds and real estate funds management, real estate investments, money market and foreign exchange.

The address of the parent company’s registered office is PO Box 23444, Safat 13095, State of Kuwait.

These consolidated financial statements of the group for the year ended 31 December 2011 were authorised for issue by the parent company’s board of directors on 17 January 2012 and are subject to the approval of the General Assembly of the shareholders.

2. Basis of preparation

The consolidated financial statements of the group have been prepared under historical cost convention except for financial assets at fair value through statement of income, financial assets available for sale and derivatives financial instruments that have been measured at fair value.

The consolidated financial statements have been presented in Kuwaiti Dinars (“KD”) which is the functional and presentation currency of the parent company rounded off to the nearest thousand.

The group has elected to present the “statement of comprehensive income” in two statements: the “statement of income” and a “statement of comprehensive income”.

3. Statement of compliance

The consolidated financial statements of the group have been prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB) and applicable requirements of Ministerial Order No. 18 of 1990, as modified by the State of Kuwait for financial services institutions regulated by Central Bank of Kuwait.

These regulations require adoption of all IFRS except for the IAS 39 requirement for collective impairment provision, which has been replaced by the Central Bank of Kuwait requirement for a minimum general provision as described under the accounting policy for impairment of financial assets.

4. Changes in accounting policies

The accounting policies adopted in the preparation of the consolidated financial statements are consistent with those used in previous year except as below:

The group has adopted the following new and amended IFRS and International Financial Reporting Interpretations Committee (IFRIC) interpretations during the year:

4.1 Adoption of Improvements to IFRSs 2010

The Improvements to IFRSs 2010 made several minor amendments to a number of IFRSs. The only amendment relevant to the group relates to IAS 1 Presentation of Financial Statements. The group previously presented the reconciliations of each component of other comprehensive income in the statement of changes in equity. The group now presents these reconciliations in the notes to the financial statements, as permitted by the amendment (see note 28). This reduces duplicated disclosures and presents more clearly the overall changes in equity. Prior period comparatives have been restated accordingly.

4.2 IASB Standards issued but not yet effective

At the date of authorisation of these consolidated financial statements, certain new standards, amendments and interpretations to existing standards have been published by the IASB but are not yet effective, and have not been adopted early by the group.

Management anticipates that all of the relevant pronouncements will be adopted in the group’s accounting policies for the first period beginning after the effective date of the pronouncements. Information on new standards, amendments and interpretations that are expected to be relevant to the group’s financial statements is provided below. Certain other new standards and interpretations have been issued but are not expected to have a material impact on the group’s financial statements.

Standard or Interpretation	Effective for annual periods beginning
IAS 1 Presentation of Financial Statements – amendment	1 July 2012
IAS 27 Consolidated and Separate Financial Statements - Revised as IAS 27 Separate Financial Statements	1 January 2013
IFRS 7 Financial Instruments: Disclosures – amendment	1 July 2011
IFRS 9 Financial Instruments: Classification and Measurement	1 January 2015
IFRS 10 Consolidated Financial Statements	1 January 2013
IFRS 13 Fair Value Measurement	1 January 2013

4.2.1 IAS 1 Presentation of Financial Statements

The amendment to IAS 1 requires entities to group other comprehensive income items presented in the consolidated statement of comprehensive income based on those:

- a) Potentially reclassifiable to consolidated statement of income in a subsequent period, and
- b) That will not be reclassified to consolidated statement of income subsequently.

The group will change the current presentation of the consolidated statement of comprehensive income when the amendment becomes effective.

4.2.2 IAS 27 Consolidated and Separate Financial statements – Revised as IAS 27 Separate Financial Statements

As a result of the consequential amendments, IAS 27 now deals with separate financial statements.

4.2.3 IFRS 7 Financial Instruments: Disclosures

The amendments to IFRS 7 Financial Instruments: Disclosures resulted as a part of comprehensive review of off financial position activities. The amendments will allow users of financial statements to improve their understanding of transfer transactions of financial assets (for example, securitisations), including understanding the possible effects of any risks that may remain with the entity that transferred the assets. The amendments also require additional disclosures if a disproportionate amount of transfer transactions are undertaken around the end of a reporting period. The adoption of this amendment is not expected to have any significant impact on the financial position or performance of the group.

4.2.4 IFRS 9 Financial Instruments – Classification and measurement

The IASB aims to replace IAS 39 Financial Instruments: Recognition and Measurement in its entirety by the end of 2010, with the replacement standard to be effective for annual periods beginning 1 January 2015. IFRS 9 is being issued in phases and to date phase 1 has been issued. The main phases are:

- Phase 1: Classification and Measurement
- Phase 2: Impairment methodology
- Phase 3: Hedge accounting

In addition, a separate project is dealing with derecognition.

Although earlier application of this standard is permitted, the Technical Committee of the Ministry of Commerce and Industry of Kuwait decided on 30 December 2009, to postpone this early application till further notice, due to the non-completion of the remaining stages of the standard.

4.2.5 IFRS 10 Consolidated Financial Statements

IFRS 10 supersedes IAS 27 Consolidated and Separate Financial Statements. It revised the definition of control together with accompanying guidance to identify an interest in subsidiary. However, the requirements and procedures of consolidation and the accounting for any non-controlling interests and changes in control remain the same.

4.2.6 IFRS 13 Fair Value Measurement

IFRS 13 does not affect which items to be fair valued, but clarifies the definition of fair value and provides related guidance and enhanced disclosures about fair value measurements. The adoption of this standard is not expected to have a significant impact on the financial position and performance of the group.

5. Significant accounting policies

The significant accounting policies adopted in the preparation of the consolidated financial statements are set out below:

5.1 Basis of consolidation

The group financial statements consolidate those of the parent company and all of its subsidiaries (see note 7).

Subsidiaries are all entities over which the group has the power to control the financial and operating policies. The group obtains and exercises control through more than half of the voting rights. The financial statements of the subsidiaries are prepared for reporting dates which are typically not more than three months from that of the parent company, using consistent accounting policies. Adjustments are made for the effect of any significant transactions or events that occur between that date and the reporting date of the parent company's financial statements.

All transactions and balances between group companies are eliminated on consolidation, including unrealised gains and losses on transactions between group companies. Where unrealised losses on intra-group asset sales are reversed on consolidation, the underlying asset is also tested for impairment from a group perspective. Amounts reported in the financial statements of subsidiaries have been adjusted where necessary to ensure consistency with the accounting policies adopted by the group.

Profit or loss and other comprehensive income of subsidiaries acquired or disposed of during the year are recognised from the effective date of acquisition, or up to the effective date of disposal, as applicable.

Non-controlling interests, presented as part of equity, represent the portion of a subsidiary's profit or loss and net assets that is not held by the group. The group attributes total comprehensive income or loss of subsidiaries between the owners of the parent and the non-controlling interests based on their respective ownership interests.

5.1 Basis of consolidation (continued)

When a controlling interest in the subsidiaries is disposed off, the difference between the selling price and the net asset value plus cumulative translation difference and goodwill is recognised in the consolidated statement of income.

Changes in the group's ownership interests in subsidiaries that do not result in the group losing control over the subsidiaries are accounted for as equity transactions. The carrying amounts of the group's interests and the non-controlling interests are adjusted to reflect the changes in their relative interests in the subsidiaries. Any difference between the amount by which the non-controlling interests are adjusted and the fair value of the consideration paid or received is recognised directly in equity and attributed to the owners of the parent company.

5.2 Revenue

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, regardless of when payment is made.

Revenue arises from rendering of services and is measured by reference to the fair value of consideration received or receivable.

The group applies the revenue recognition criteria set out below to each separately identifiable component of revenue.

5.2.1 Rendering of services

The group earns fees and commission income from diverse range of asset management, investment banking, custody and brokerage services provided 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 the provision of services over a period of time are accrued over that period. These fees include commission income and asset management, custody and other management fees.

Fee income from providing transaction services

Fees arising for rendering specific advisory services, brokerage services, equity and debt placement transactions for a third party or arising from negotiating or participating in the negotiation of a transaction for a third party are recognised on completion of the underlying transaction.

5.2.2 Interest income

Interest income are reported on an accrual basis using the effective interest method.

5.2.3 Dividend income

Dividend income are recognised at the time the right to receive payment is established.

5.3 Operating expenses

Operating expenses are recognised in consolidated statement of income upon utilisation of the service or at the date of their origin.

5.4 Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset are capitalised during the period of time that is necessary to complete and prepare the asset for its intended use or sale. Other borrowing costs are expensed in the period in which they are incurred and reported in finance costs.

5.5 Taxation

5.5.1 Kuwait Foundation for the Advancement of Sciences (KFAS)

The contribution to KFAS is calculated at 1% of taxable profit of the group in accordance with the modified calculation based on the Foundation's Board of Directors' resolution, which states that income from associates and subsidiaries, Board of Directors' remuneration, transfer to statutory reserve should be excluded from profit for the year when determining the contribution.

5.5.2 National Labour Support Tax (NLST)

NLST is calculated in accordance with Law No. 19 of 2000 and the Minister of Finance Resolutions No. 24 of 2006 at 2.5% of taxable profit of the group after deducting directors' fees for the year. As per law, income from associates and subsidiaries, cash dividends from listed companies which are subjected to NLST have to be deducted from the profit for the year.

5.5.3 Zakat

Contribution to Zakat is calculated at 1% of the profit of the group in accordance with the Ministry of Finance resolution No. 58/2007 effective from 10 December 2007.

For the year ended 31 December 2011, the parent company has no liability towards NLST, KFAS and Zakat due to losses incurred. Under the NLST, KFAS and Zakat regulations no carry forward of losses to the future years nor any carry back to prior years is permitted.

5.5.4 Taxation on overseas subsidiaries

Taxation on overseas subsidiaries is calculated on the basis of the tax rates applicable and prescribed according to the prevailing laws, regulations and instructions of the countries where these subsidiaries operate.

5.6 Segment reporting

The group has two operating segments: the asset management and investment banking. In identifying these operating segments, management generally follows the group's service lines representing its main services. Each of these operating segments is managed separately as each requires different approaches and other resources. All inter-segment transfers are carried out at arm's length prices.

For management purposes, the group uses the same measurement policies as those used in its financial statements. In addition, assets or liabilities which are not directly attributable to the business activities of any operating segment are not allocated to a segment.

5.7 Business combinations

The group applies the acquisition method in accounting for business combinations. The consideration transferred by the group to obtain control of a subsidiary is calculated as the sum of the acquisition-date fair values of assets transferred, liabilities incurred and the equity interests issued by the group, which includes the fair value of any asset or liability arising from a contingent consideration arrangement. Acquisition costs are expensed as incurred. For each business combination, the acquirer measures the non-controlling interests in the acquiree either at fair value or at the proportionate share of the acquiree's identifiable net assets.

If the business combination is achieved in stages, the acquisition date fair value of the acquirer's previously held equity interest in the acquiree is remeasured to fair value at the acquisition date through consolidated statement of income.

The group recognises identifiable assets acquired and liabilities assumed in a business combination regardless of whether they have been previously recognised in the acquiree's financial statements prior to the acquisition. Assets acquired and liabilities assumed are generally measured at their acquisition-date fair values.

5. Significant accounting policies (continued)

5.7 Business combinations (continued)

When the group acquires a business, it assesses the financial assets and liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic circumstances and pertinent conditions as at the acquisition date. This includes the separation of embedded derivatives in host contracts by the acquiree.

Goodwill is stated after separate recognition of identifiable intangible assets. It is calculated as the excess of the sum of a) fair value of consideration transferred, b) the recognised amount of any non controlling interest in the acquiree and c) acquisition-date fair value of any existing equity interest in the acquiree, over the acquisition-date fair values of identifiable net assets. If the fair values of identifiable net assets exceed the sum calculated above, the excess amount (ie gain on a bargain purchase) is recognised in consolidated statement of income immediately.

5.8 Investment property

Investment properties are properties held to earn rentals and/or for capital appreciation and are initially measured at cost, including transaction costs. Subsequently, investment properties are accounted for using the cost model whereby these investments are stated at cost less accumulated depreciation and impairment losses, if any. The group depreciates its investment property except land on the straight-line method over their expected useful lives.

When investment property is sold, its cost and accumulated depreciation are eliminated from the accounts and any gain or loss resulting from the disposal is recognised in the consolidated statement of income.

Transfers are made to or from investment property only when there is a change in use. For a transfer from investment property to owner-occupied property, the deemed cost for subsequent accounting is the fair value at the date of change in use. If owner-occupied property becomes an investment property, the group accounts for such property in accordance with the policy stated under property, plant and equipment up to the date of change in use.

5.9 Property and equipment

Property and other equipment (comprising fittings, furniture, vehicles and decoration) are initially recognised at acquisition cost or manufacturing cost, including any costs directly attributable to bringing the assets to the location and condition necessary for it to be capable of operating in the manner intended by the group's management.

Vehicles and other equipment are subsequently measured using the cost model, cost less subsequent depreciation and impairment losses. Depreciation is recognised on a straight-line basis to write down the cost less estimated residual value of vehicles and other equipment. The useful life and depreciation method are reviewed periodically to ensure that the method and period of depreciation are consistent with the expected pattern of economic benefits arising from items of property and equipment. The following useful lives are applied:

Office equipment and soft ware	3 - 5 years
Motor vehicles	3 - 4 years
Furniture and fixtures	7 - 10 years
Decorations	7 years
Licence fee	2 - 3 years

When assets are sold or retired, their cost and accumulated depreciation are eliminated from the accounts and any gain or loss resulting from their disposal is recognised in the consolidated statement of income.

5.10 Impairment testing of non financial assets

An impairment loss is recognised for the amount by which the asset's or cash-generating unit's carrying amount exceeds its recoverable amount, which is the higher of fair value less costs to sell and value-in-use. To determine the value-in-use, management estimates expected future cash flows from each cash-generating unit and determines a suitable interest rate in order to calculate the present value of those cash flows. The data used for impairment testing procedures are directly linked to the group's latest approved budget, adjusted as necessary to exclude the effects of future reorganisations and asset enhancements. Discount factors are determined individually for each cash-generating unit and reflect management's assessment of respective risk profiles, such as market and asset-specific risks factors.

Impairment losses for cash-generating units reduce first the carrying amount of any goodwill allocated to that cash-generating unit. Any remaining impairment loss is charged pro rata to the other assets in the cash-generating unit. With the exception of goodwill, all assets are subsequently reassessed for indications that an impairment loss previously recognised may no longer exist. An impairment charge is reversed if the cash-generating unit's recoverable amount exceeds its carrying amount.

5.11 Financial instruments

5.11.1 Recognition, initial measurement and derecognition

Financial assets and financial liabilities are recognised when the group becomes a party to the contractual provisions of the financial instrument and are measured initially at fair value adjusted by transactions costs, except for those carried at fair value through statement of income which are measured initially at fair value.

A financial asset (or, where applicable a part of financial asset or part of group of similar financial assets) is derecognised when:

- rights to receive cash flows from the assets have expired;
- the group has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass through' arrangement and either

(a) the group has transferred substantially all the risks and rewards of the asset or

(b) the group has neither transferred nor retained substantially all risks and rewards of the asset but has transferred control of the asset.

Where the group has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, a new asset is recognised to the extent of the group's continuing involvement in the asset.

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires. When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognised in consolidated statement of income.

5.11.2 Classification and subsequent measurement of financial assets

For the purpose of subsequent measurement, financial assets other than those designated and effective as hedging instruments are classified into the following categories upon initial recognition:

- Loans and receivables
- Financial assets at fair value through statement of income (FVTSI)
- Available-for-sale (AFS) financial assets.

All financial assets except for those at FVTSI are subject to review for impairment at least at each reporting date to identify whether there is any objective evidence that a financial asset or a group of financial assets is impaired. Different criteria to determine impairment are applied for each category of financial assets, which are described below.

• Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial recognition, these are measured at amortised cost using the effective interest rate method, less provision for impairment. Discounting is omitted where the effect of discounting is immaterial.

Individually significant receivables are considered for impairment when they are past due or when other objective evidence is received that a specific counterparty will default. Receivables that are not considered to be individually impaired are reviewed for impairment in groups, which are determined by reference to the industry and region of a counterparty and other shared credit risk characteristics. The impairment loss estimate is then based on recent historical counterparty default rates for each identified group.

In addition, in accordance with Central Bank of Kuwait instructions, a minimum general provision is made on all applicable credit facilities (net of certain categories of collateral) that are not provided for specifically.

The group categorises loans and receivables into following categories:

- Loans and advances

Loans and advances are financial assets originated by the group by providing money directly to the borrower that have fixed or determinable payments and are not quoted in an active market. The group loans and advances comprises loan to customers and short term financing.

- Cash and cash equivalents

Cash and cash equivalents comprise cash on hand, bank balances and term deposits, that are readily convertible into known amounts of cash within 90 days and which are subject to an insignificant risk of changes in value net of due to banks and other financial institutions.

5. Significant accounting policies (continued)

5.11 Financial instruments (continued)

5.11.2 Classification and subsequent measurement of financial assets (continued)

- **Financial assets at FVTSI**

Classification of investments as financial assets at FVTSI depends on how management monitor the performance of these investments. When they are not classified as held for trading but have readily available reliable fair values and the changes in fair values are reported as part of consolidated statement of income in the management accounts, they are as designated at FVTSI upon initial recognition. All derivative financial instruments fall into this category, except for those designated and effective as hedging instruments, for which the hedge accounting requirements apply (see note 5.11.4).

Assets in this category are measured at fair value with gains or losses recognised in consolidated statement of income. The fair values of financial assets in this category are determined by reference to active market transactions or using a valuation technique where no active market exists.

- **AFS financial assets**

AFS financial assets are non-derivative financial assets that are either designated to this category or do not qualify for inclusion in any of the other categories of financial assets.

Financial assets whose fair value cannot be reliably measured are carried at cost less impairment losses, if any. Impairment charges are recognised in consolidated statement of income. All other AFS financial assets are measured at fair value. Gains and losses are recognised in other comprehensive income and reported within the fair value reserve within equity, except for impairment losses, and foreign exchange differences on monetary assets, which are recognised in consolidated statement of income. When the asset is disposed of or is determined to be impaired, the cumulative gain or loss recognised in other comprehensive income is reclassified from the equity reserve to consolidated statement of income and presented as a reclassification adjustment within other comprehensive income.

The group assesses at each reporting date whether there is objective evidence that a financial asset available for sale or a group of financial assets available for sale is impaired. In the case of equity investments classified as financial assets available for sale, objective evidence would include a significant or prolonged decline in the fair value of the equity investment below its cost. 'Significant' is evaluated against the original cost of the investment and 'prolonged' against the period in which the fair value has been below its original cost. Where there is evidence of impairment, the cumulative loss is removed from other comprehensive income and recognised in the consolidated statement of income.

Reversals of impairment losses are recognised in other comprehensive income, except for financial assets that are debt securities which are recognised in consolidated statement of income only if the reversal can be objectively related to an event occurring after the impairment loss was recognised.

5.11.3 Classification and subsequent measurement of financial liabilities

The group's financial liabilities include borrowings (short term loan and due to banks and other financial institutions), accounts payables and other liabilities, bonds and derivative financial instruments.

The subsequent measurement of financial liabilities depends on their classification as follows:

- **Financial liabilities other than at fair value through statement of income**

These are stated using effective interest rate method. Short term borrowing, due to banks and other financial institutions and bonds are classified as financial liabilities other than at fair value through statement of income.

- **Trade payables**

Liabilities are recognised for amounts to be paid in the future for goods or services received, whether billed or not.

- **Borrowings**

All borrowings are subsequently measured at amortised cost using the effective interest rate method. Gains and losses are recognised in the consolidated statement of income when the liabilities are derecognised as well as through the effective interest rate method (EIR) amortisation process.

- **Bonds**

Bonds are carried on the consolidated statement of financial position at their principal amount, net of directly related costs of issuing the bonds to the extent that such costs have not been amortised. These costs are amortised through the consolidated statement of income over the life of the bonds using the effective interest rate method.

All derivative financial instruments that are not designated and effective as hedging instruments are accounted for at FVTSI.

All interest-related charges and, if applicable, changes in an instrument's fair value that are reported in consolidated statement of income, are included within finance costs or finance income.

5.11.4 Derivative financial instruments and hedge accounting

Derivative financial instruments are accounted for at FVTSI except for derivatives designated as hedging instruments in cash flow hedge relationships or fair value hedge relationship, which requires a specific accounting treatment. To qualify for hedge accounting, the hedging relationship must meet several strict conditions with respect to documentation, probability of occurrence of the hedged transaction and hedge effectiveness.

All derivative financial instruments used for hedge accounting are recognised initially at fair value and reported subsequently at fair value in the consolidated statement of financial position. To the extent that the hedge is effective, changes in the fair value of derivatives designated as hedging instruments in cash flow hedges are recognised in other comprehensive income and included within the cash flow hedge reserve in equity. Any ineffectiveness in the hedge relationship is recognised immediately in consolidated statement of income.

At the time the hedged item affects consolidated statement of income, any gain or loss previously recognised in other comprehensive income is reclassified from equity to consolidated statement of income and presented as a reclassification adjustment within other comprehensive income. However, if a non-financial asset or liability is recognised as a result of the hedged transaction, the gains and losses previously recognised in other comprehensive income are included in the initial measurement of the hedged item.

All derivative financial instruments are recognised in the consolidated statement of financial position as either assets (positive fair values) or liabilities (negative fair values).

Derivative financial instruments used by the group include foreign exchange forwards contracts and interest rate swaps.

- Hedge accounting

The group has designated its interest rate swaps as hedging instruments for cash flow hedges in order to mitigate interest rate risk arising from its bonds.

At the inception of the hedge relationship, the group documents the relationship between the hedging instrument and the hedged item, along with its risk management objectives and its strategy for undertaking various hedge transactions. Furthermore, at the inception of the hedge and on an ongoing basis, the group documents whether the hedging instrument is highly effective in offsetting changes in fair values or cash flows of the hedged item.

Note 36 sets out details of the fair values of the derivative instruments used for hedging purposes.

- Cash flow hedges

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in other comprehensive income. The gain or loss relating to the ineffective portion is recognised immediately in the consolidated statement of income.

Amounts previously recognised in other comprehensive income and accumulated in equity are reclassified to the consolidated statement of income in the periods when the hedged item is recognised in the consolidated statement of income. However, when the forecast transaction that is hedged results in the recognition of a non-financial asset or a non-financial liability, the gains and losses previously accumulated in equity are transferred from equity and included in the initial cost of the non-financial asset or non-financial liability.

Hedge accounting is discontinued when the group revokes the hedging relationship, when the hedging instrument expires or is sold, terminated, or exercised, or when it no longer qualifies for hedge accounting. When a forecast transaction is expected to occur, any gain or loss accumulated in equity at that time remains separately in equity and is recognised in the consolidated statement of income when the forecast transaction is ultimately recognised in the consolidated statement of income. When a forecast transaction is no longer expected to occur, the gain or loss accumulated in equity is recognised immediately in the consolidated statement of income.

5.11.5 Amortised cost of financial instruments

This is computed using the effective interest method less any allowance for impairment. The calculation takes into account any premium or discount on acquisition and includes transaction costs and fees that are an integral part of the effective interest rate.

5.11.6 Trade and settlement date accounting

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

5. Significant accounting policies (continued)

5.11 Financial instruments (continued)

5.11.7 Offsetting of financial instruments

Financial assets and financial liabilities are offset and the net amount reported in the consolidated statement of financial position if, and only if, there is a currently enforceable legal right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the assets and settle the liabilities simultaneously.

5.11.8 Fair value of financial instruments

The fair value of financial instruments that are traded in active markets at each reporting date is determined by reference to quoted market prices or dealer price quotations (bid price for long positions and ask price for short positions), without any deduction for transaction costs.

For financial instruments not traded in an active market, the fair value is determined using appropriate valuation techniques. Such techniques may include using recent arm's length market transactions; reference to the current fair value of another instrument that is substantially the same; a discounted cash flow analysis or other valuation models.

An analysis of fair values of financial instruments and further details as to how they are measured are provided in Note 35.

5.12 Equity, reserves and dividend payments

Share capital represents the nominal value of shares that have been issued and paid up.

Share premium includes any premiums received on issue of share capital. Any transaction costs associated with the issuing of shares are deducted from share premium.

Legal and voluntary reserves comprise appropriations of current and prior period profits in accordance with the requirements of the Commercial Companies' Law and the parent company's articles of association.

Other components of equity include the following:

- Foreign currency translation reserve – comprises foreign currency translation differences arising from the translation of financial statements of the group's foreign entities into Kuwaiti Dinars
- Fair value reserve – comprises gains and losses relating to available for sale financial assets
- Cash flow hedging reserve – comprises gain and losses relating to cash flow hedging.
- Treasury shares reserve – comprises gain and losses resulting from sale of treasury shares

Retained earnings includes all current and prior period retained profits and losses. All transactions with owners of the parent are recorded separately within equity.

Dividend distributions payable to equity shareholders are included in other liabilities when the dividends have been approved in a general meeting.

5.13 Treasury shares

Treasury shares consist of the parent company'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 voluntary reserve and statutory reserve. 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.

5.14 Provisions, contingent assets and contingent liabilities

Provisions are recognised when the group has a present legal or constructive obligation as a result of a past event, it is probable that an outflow of economic resources will be required from the group and amounts can be estimated reliably. Timing or amount of the outflow may still be uncertain.

Provisions are measured at the estimated expenditure required to settle the present obligation, based on the most reliable evidence available at the reporting date, including the risks and uncertainties associated with the present obligation. Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. Provisions are discounted to their present values, where the time value of money is material.

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

Contingent liabilities are not recognised in the consolidated statement of financial position, but are disclosed unless the possibility of an outflow of resources embodying economic benefits is remote.

5.15 Foreign currency translation

5.15.1 Functional and presentation currency

The consolidated financial statements are presented in currency Kuwait Dinar (KD), which is also the functional currency of the parent company. Each entity in the group determines its own functional currency and items included in the financial statements of each entity are measured using that functional currency.

5.15.2 Foreign currency transactions and balances

Foreign currency transactions are translated into the functional currency of the respective group entity, using the exchange rates prevailing at the dates of the transactions (spot exchange rate). Foreign exchange gains and losses resulting from the settlement of such transactions and from the remeasurement of monetary items denominated in foreign currency at year-end exchange rates are recognised in consolidated statement of income. Non-monetary items are not retranslated at year-end and are measured at historical cost (translated using the exchange rates at the transaction date), except for non-monetary items measured at fair value which are translated using the exchange rates at the date when fair value was determined.

5.15.3 Foreign operations

In the group's financial statements, all assets, liabilities and transactions of group entities with a functional currency other than the KD are translated into KD upon consolidation. The functional currency of the entities in the group has remained unchanged during the reporting period.

On consolidation, assets and liabilities have been translated into KD at the closing rate at the reporting date. Income and expenses have been translated into KD at the average rate over the reporting period. Exchange differences are charged/credited to other comprehensive income and recognised in the foreign currency translation reserve in equity. On disposal of a foreign operation, the related cumulative translation differences recognised in equity are reclassified to consolidated statement of income and are recognised as part of the gain or loss on disposal.

5.16 Related party transactions

Related parties consist of directors, executive officers, their close family members and companies of which they are principal owners. All related party transactions are approved by management.

5.17 End of service indemnity

The group provides end of service benefits to its employees. The entitlement to these benefits is based upon the employees' final salary and length of service, subject to the completion of a minimum service period in accordance with relevant labour law and the employees' contracts. The expected costs of these benefits are accrued over the period of employment. This liability, which is unfunded, represents the amount payable to each employee as a result of termination on the reporting date.

With respect to its Kuwaiti national employees, the group makes contributions to the Public Institution for Social Security calculated as a percentage of the employees' salaries. The group's obligations are limited to these contributions, which are expensed when due.

5.18 Fiduciary assets

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

6. Significant management judgments and estimation uncertainty

The preparation of the group's consolidated financial statements requires management to make judgments, estimates and assumptions that affect the reported amount of revenues, expenses, assets and liabilities and the disclosure of contingent liabilities, at the end of the reporting period. However uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of the asset or liability affected in future periods.

6.1 Significant management judgments

In the process of applying the group's accounting policies, management has made the following significant judgments, which have the most significant effect on the amounts recognised in the consolidated financial statements:

6. Significant management judgments and estimation uncertainty (continued)

6.1 Significant management judgments (continued)

6.1.1 Classification of financial instruments

Judgements are made in the classification of financial instruments based on management's intention at acquisition.

The group classifies financial assets as held for trading if they are acquired primarily for the purpose of short term profit making.

Classification of financial assets as fair value through statement of income depends on how management monitors the performance of these financial assets. When they are not classified as held for trading but have readily available fair values and the changes in fair values are reported as part of consolidated statement of income in the management accounts, they are classified as fair value through statement of income.

Classification of assets as loans and receivables depends on the nature of the asset. If the Group is unable to trade these financial assets due to inactive market and the intention is to receive fixed or determinable payments the financial asset is classified as loans and receivables.

All other financial assets are classified as available for sale.

6.1.2 Classification of real estate

Management decides on acquisition of a real estate whether it should be classified as trading, property held for development or investment property.

The group classifies property as trading property if it is acquired principally for sale in the ordinary course of business.

The group classifies property as investment property under development if it is acquired with the intention of development.

The group classifies property as investment property if it is acquired to generate rental income or for capital appreciation, or for undetermined future use.

6.2 Estimates uncertainty

Information about estimates and assumptions that have the most significant effect on recognition and measurement of assets, liabilities, income and expenses is provided below. Actual results may be substantially different.

6.2.1 Impairment of available for sale equity investments

The group treats available for sale equity investments as impaired when there has been a significant or prolonged decline in the fair value below its cost or where other objective evidence of impairment exists. The determination of what is "significant" or "prolonged" requires considerable judgment.

6.2.2 Useful lives of depreciable assets

Management reviews its estimate of the useful lives of depreciable assets at each reporting date, based on the expected utility of the assets. Uncertainties in these estimates relate to technical obsolescence that may change the utility of certain software and equipment.

6.2.3 Impairment of loans to customers

An estimate of the collectible amount of loans to customers is made when collection of the full amount is no longer probable. For individually significant amounts, this estimation is performed on an individual basis. Amounts which are not individually significant, but which are past due, are assessed collectively and a provision applied according to the length of time past due, based on historical recovery rates.

At the financial position date, gross receivable from loans to customers were KD12,482 thousand (2010: KD13,502 thousand), and the provision for credit losses was KD598 thousand (2010: KD609 thousand). Any difference between the amounts actually collected in future periods and the amounts expected will be recognised in the consolidated statement of income.

6.2.4 Fair value of financial instruments

Management apply valuation techniques to determine the fair value of financial instruments where active market quotes are not available. This requires management to develop estimates and assumptions based on market inputs, using observable data that market participants would use in pricing the instrument. Where such data is not observable, management uses its best estimate. Estimated fair values of financial instruments may vary from the actual prices that would be achieved in an arm's length transaction at the reporting date (see note 35).

7. Subsidiaries

Name	Country of incorporation	Voting capital held		Purpose
		31 December 2011	31 December 2010	
Margulf Management Inc.	USA	100%	100%	Assets management
KFC Lone Star 1, Inc.	USA	-	100%	Assets management
First Management and Economic Consultancy Company – KSC (Closed)	Kuwait	60%	100%	Economic consultancy
MDI Holding Limited	Cayman Islands	66.66%	66.66%	Property management
MDI Management Limited	Cayman Islands	66.66%	66.66%	Property management
MDI Ventures Ltd	Cayman Islands	50%	-	Property management
Markaz Offshore Ltd.	Cayman Islands	100%	100%	Investment in fixed income securities
Marmore Mena Intelligence Private Limited	India	90%	-	Consultancy

During the year, the parent company disposed of 40% ownership interest in First Management Economic Consultancy Company – KSCC resulting in a loss of KD25 thousand on the partial disposal. Since, the parent company continues to control the subsidiary before and after the disposal, the loss on the partial disposal of this subsidiary has been recognised directly in retained earnings.

During the year, the parent company liquidated 100% owned subsidiary KFC Lone Star 1, Inc. and realised a loss of KD17 thousand on liquidation.

During the year, the parent company incorporated a 90% owned subsidiary in India namely Marmore Mena Intelligence Private Limited and a 50% owned subsidiary in Cayman Islands namely MDI Ventures Ltd.

8. Interest income

	Year ended 31 December 2011	Year ended 31 December 2010
	KD '000	KD '000
Time deposits	27	103
Investments at fair value through statement of income	376	831
Short-term financing	155	49
Loans to customers	713	583
	1,271	1,566

9. Management fees and commission

Management fees and commission relate to income arising from the group's management of portfolios, funds, custody and similar trust and fiduciary activities.

10. Net (loss) / gain on financial assets

Net (loss)/gain on financial assets analysed by category is as follows:

	Year ended 31 December 2011	Year ended 31 December 2010
	KD '000	KD '000
Time deposits	27	103
Investments at fair value through statement of income	(5,159)	5,448
Available for sale investments	2,432	1,182
Loans to customers	715	613
Short term financing	155	49
Net realised (loss)/gain	(1,830)	7,395
Net unrealised (loss)/gain recognised in equity	(1,782)	3,785
	(3,612)	11,180

11. Change in fair value of investments at fair value through statement of income

	Year ended 31 December 2011	Year ended 31 December 2010
	KD '000	KD '000
Change in fair value of trading securities	(142)	266
Change in fair value of investments designated as investments at fair value through statement of income	(5,307)	4,402
	(5,449)	4,668

12. General and administrative expense

General and administrative expenses include the following:

	Year ended 31 December 2011	Year ended 31 December 2010
	KD '000	KD '000
Staff costs	3,245	3,747
Depreciation	128	139

13. Finance costs

	Year ended 31 December 2011	Year ended 31 December 2010
	KD '000	KD '000
Bonds	432	419
Short term borrowings	141	79
Due to banks and other financial institutions	363	376
	936	874

14. Basic and diluted (loss)/earning per share attributable to the owners of the parent company

Basic and diluted (loss)/earnings per share is calculated by dividing the (loss)/profit for the year attributable to the owners of the parent company by the weighted average number of shares in issue excluding treasury shares.

	Year ended 31 December 2011	Year ended 31 December 2010
	KD '000	KD '000
(Loss)/profit for the year attributable to the owners of the parent company (KD '000)	(356)	8,123
Weighted average number of shares in issue during the year (excluding treasury shares) (000's)	480,802	480,802
Basic and diluted (loss)/earnings per share attributable to the owners of the parent company	(1) Fils	17 Fils

The comparative weighted average number of shares for the calculation of basic and diluted (loss)/earnings per share has been adjusted to reflect the bonus issue in March 2011 (note 29).

15. Cash and cash equivalents

Cash and cash equivalents included in the consolidated statement of cash flows comprise of the following consolidated statement of financial position accounts:

	31 December 2011	31 December 2010
	KD '000	KD '000
Cash and bank balances	3,750	2,177
Time deposits	19,107	3,500
Total cash and cash equivalents	22,857	5,677
Less: Time deposits maturing after three months	(4,003)	-
Less: Due to banks and other financial institutions	-	(3,753)
Cash and cash equivalent for statement of cash flow	18,854	1,924

The group's time deposits yield interest at an average interest rate of 1.75% (31 December 2010: 1.29%) per annum.

16. Investments at fair value through statement of income

	31 December 2011	31 December 2010
	KD '000	KD '000
Trading:		
Local quoted securities	770	710
Foreign quoted securities	642	1,910
	1,412	2,620
Designated on initial recognition:		
Local quoted securities	650	530
Local managed funds	28,078	32,875
Foreign unquoted securities	1,821	802
Foreign managed funds	3,534	3,901
Fixed income securities	6,368	11,369
	40,451	49,477
	41,863	52,097

The investments in managed fund investments are carried at net asset value provided by the respective Fund Managers due to the nature of those investments. Management believes the net asset value provided by the Fund Managers represents the best estimate of fair value available for these investments.

Total investments amounting to KD31,612 thousand (2010: KD36,776 thousand) are managed by the parent company.

The interest rates on fixed income securities range from 1.20% to 10.75% (2010: 1.19% to 8.75%) per annum.

17. Accounts receivable and other assets

	31 December 2011	31 December 2010
	KD '000	KD '000
Management fees and commission receivable	1,416	2,158
Interest receivable	312	223
Receivable from sale of available for sale investments	528	80
Prepayments	279	256
Others	827	3,447
	3,362	6,164

18. Short term financing

	31 December 2011	31 December 2010
	KD '000	KD '000
Balance at 1 January	-	54
Granted during the year	878	766
Settled during the year	-	(820)
Balance at 31 December	878	-

Short term financing represented short term advances at an interest rate of 11% per annum (2010: 12% per annum). The advance is due within 6 months of the financial position date.

19. Loans to customers

	31 December 2011	31 December 2010
	KD '000	KD '000
Commercial loans	5,270	5,300
Margin loans	51	5,485
Personal loans	7,161	2,717
	12,482	13,502
Provision for credit losses	(598)	(609)
	11,884	12,893

The maturity profile of loans to customers is as follows:

	31 December 2011	31 December 2010
	KD '000	KD '000
Up to one month	739	1,584
Between one month and six months	48	1,259
Between six months and one year	10,563	10,181
Over one year	654	-
Non-performing loans (fully impaired)	478	478
	12,482	13,502

Provision for credit losses is made in accordance with Central Bank of Kuwait requirements including general provision (see Note 5.1.1.2) on the balance of regular facilities for which no specific provisions are made.

The total non-performing loans which have been fully provided amounts to KD478 thousand (2010: KD478 thousand).

The interest rate on loans to customers ranges between 5.00% to 5.50% (2010: 5.00% to 5.50%) per annum for commercial and margin loans and between 4.00% to 5.50% (2010: 3.00% to 5.50%) per annum for personal loans.

All loans are denominated in KD or US Dollars. Commercial loans are fully secured by charges over property and investments in the funds and securities held in fiduciary portfolios on behalf of the borrowers.

20. Available for sale investments

	31 December 2011	31 December 2010
	KD '000	KD '000
Foreign quoted securities	13,521	16,672
Unquoted securities	184	1,381
Managed funds	11,599	12,599
Equity participation	22,561	23,322
Debt instruments	4,780	2,849
	52,645	56,823

Investments amounting to KD5,578 thousand (2010: KD3,648 thousand) are carried at cost due to unpredictable nature of future cash flows and the unavailability of financial information to arrive at a reliable measure of fair value.

Investments in equity participations include investments amounting to KD22,561 thousand (2010: KD23,322 thousand) whose fair values are determined using valuation techniques frequently used by Fund Managers that are not based on observable market prices or rates. Management believes the net asset value provided by the Fund Managers represents the best estimate of fair value available for these investments.

During the year, the group recognised an impairment loss of KD1,265 thousand (2010: KD839 thousand) in respect of certain available for sale investments. Management has preformed an analysis of the underlying investments which indicate that there is no further impairment.

Total investments amounting to KD17,183 thousand (2010: KD18,583 thousand) are managed by the parent company

Investments in debt instrument amounting to KD4,780 thousand (2010 KD2,849 thousand) are fully secured by charges over real estate properties.

21. Investment properties

	31 December 2011	31 December 2010
	KD '000	KD '000
Carrying value at 1 January	2,340	1,931
Additions	2,712	975
Transfer from available for sale investments (see below)	2,343	-
Disposals	-	(292)
Reversal/(charge) for impairment	143	(274)
Carrying amount at 31 December	7,538	2,340

Investment properties are located outside Kuwait. In the opinion of management the carrying value of the investment properties approximates their fair value.

During the year the parent company acquired two properties in Kingdom of Saudi Arabia for total consideration of KD2,712 thousand.

During the year, the group foreclosed on certain debt instruments resulting into acquisition of the real estate properties underlying those debt instruments. Those debt instruments were previously classified as available for sale investments.

22. Bonds

On 19 December 2011, the parent company issued unsecured bonds in the principle amount of KD22,000 thousand as follows:

- KD12,200 thousand with a fixed rate of 5.00% payable half yearly in arrears maturing on 19 December 2016.
- KD9,800 thousand with variable rate of 2.50%, above Central Bank of Kuwait payable half yearly in arrears maturing on 19 December 2016.

On 5 July 2007, the parent company issued unsecured bonds in the principal amount of US Dollars 100,000 thousand with an interest rate of LIBOR plus 1.10% payable quarterly in arrears. The bonds are listed on the Dubai International Financial Exchange and mature on 5 July 2012. Interest rate risk relating to these bonds risk have been hedged by the parent company by the interest rate swap contracts (see note 34 and 36).

23. Share capital

The authorised, issued and fully paid up share capital consists of 531,300 thousand shares of 100 fils each (2010: 506,000 thousand shares of 100 fils each).

The shareholders' Annual General Assembly held on 17 March 2011 approved to increase the authorised, issued and paid up share capital of the Parent Company by way of bonus shares of 25,300 thousand.

24. Share premium

Share premium is not available for distribution.

25. Legal reserve

As required by the Kuwait Commercial Companies Law and the parent company's Articles of Association, 10% of profit for the year attributable to owners of the parent company before KFAS, NLST, Zakat and Directors' remuneration is to be transferred to the legal reserve until the reserve reaches a minimum of 50% of the paid up share capital. This reserve is not available for distribution except for payment of a dividend of 5% of paid up share capital in years when retained earnings are not sufficient for the payment of such dividends. No transfer is required in the year of loss or where cumulative losses exist.

26. Voluntary reserve

In accordance with the parent company's Articles of Association, 10% of profit for the year attributable to owners of the Parent Company before KFAS, NLST, Zakat and Directors' remuneration is required to be transferred to the voluntary reserve until the shareholders decide to discontinue the transfer. No transfer is required in the year of loss or where cumulative losses exist.

27. Treasury shares

	31 December 2011	31 December 2010
	KD '000	KD '000
Number of shares (000's)	50,498	48,094
Percentage of issued shares	9.5%	9.5%
Cost (KD '000)	16,342	16,342
Market value (KD '000)	5,757	6,829

28. Other components of equity

	Fair value reserve	Foreign currency translation reserve	Cash flow hedging reserve	Total
	KD '000	KD '000	KD '000	KD '000
Balance at 1 January 2011	7,880	(8)	(557)	7,315
Available for sale investments				
- Net change arising during the year	(1,782)	-	-	(1,782)
- Transferred to consolidated statement of income on sale	(3,555)	-	-	(3,555)
- Transferred to consolidated statement of income on impairment	1,265	-	-	1,265
Exchange differences on translating foreign operations	-	(35)	-	(35)
Cash flow hedging				
- Net change in fair value during the year	-	-	314	314
Other comprehensive (loss)/income	(4,072)	(35)	314	(3,793)
Balance at 31 December 2011	3,808	(43)	(243)	3,522

	Fair value reserve KD '000	Foreign currency translation reserve KD '000	Cash flow hedging reserve KD '000	Total KD '000
Balance at 1 January 2010	5,247	-	(560)	4,687
Available for sale investments				
- Net change arising during the year	3,785	-	-	3,785
- Transferred to consolidated statement of income on sale	(1,991)	-	-	(1,991)
- Transferred to consolidated statement of income on impairment	839	-	-	839
Exchange differences on translating foreign operations	-	(8)	-	(8)
Cash flow hedging				
- Net change arising during the year	-	-	3	3
Other comprehensive income/(loss)	2,633	(8)	3	2,628
Balance at 31 December 2010	7,880	(8)	(557)	7,315

29. Proposed dividend

The Directors did not propose dividend for the year ended 31 December 2011.

The shareholders' annual general assembly held on 17 March 2011 approved the audited consolidated financial statements of the group for the year ended 31 December 2010 and declared a cash dividend of 10 Fils per share amounting to KD4,579 thousand (31 December 2009: Nil) and bonus shares of 5% (5 shares for every 100 shares) of paid up share capital for the year ended 31 December 2010 (31 December 2009: Nil) and was paid following that approval.

30. Related party transactions

Related parties represent associated companies, major shareholders, directors and key management personnel of the group, and entities controlled, jointly controlled or significantly influenced by such parties. Pricing policies and terms of these transactions are approved by the group's management. Transactions between the parent company and its subsidiaries which are related parties of the parent company have been eliminated on consolidation and are not disclosed in this note. Details of transactions between the group and other related parties are disclosed below.

During the year, the group entities entered into the following transactions with related parties that are not members of the group:

	31 December 2011 KD '000	31 December 2010 KD '000
Transactions included in the consolidated statement of income:		
Interest income on loans and short term financing	507	525
Management fees and commission	6,420	5,804
Key management compensation:		
Salaries and other short-term benefits	629	519
Terminal benefits	62	52
Directors remuneration	-	105
	691	676
Balances included in the consolidated statement of financial position:		
Short-term financing (see note 18)	878	-
Loans to directors and senior management	3,469	4,203
Loans to other related parties	5,217	5,327
Available for sale investment (see note 20)	17,183	18,583
Investment at fair value through statement of income (see note 16)	31,612	36,726
Management fees and commission receivable	1,078	604
	59,437	65,443

31. Segmental analysis

Operating segments are identified based on internal management reporting information that is regularly reviewed by the chief operating decision maker in order to allocate resources to the segment and to assess its performance, and is reconciled to group profit or loss.

The revenues and profits generated by the group from business segments are summarised as follows:

Asset management

- GCC and MENA investments
- International investments
- Private equity

Investment banking

- Corporate finance & advisory
- Real estate
- Oil and gas
- Treasury
- Loans
- Structured finance and derivatives

	Asset Management		Investment Banking		Total	
	31 December 2011	31 December 2010	31 December 2011	31 December 2010	31 December 2011	31 December 2010
	KD '000	KD '000	KD '000	KD '000	KD '000	KD '000
Segment income	2,112	12,444	5,186	3,910	7,298	16,354
Segment (loss)/profit	(1,292)	8,240	1,062	459	(230)	8,699
KFAS, NLST, Zakat and directors remuneration	-	(480)	-	(51)	-	(531)
(Loss)/profit for the year	(1,292)	7,760	1,062	408	(230)	8,168
Total segment assets	64,911	66,345	76,510	70,075	141,421	136,420
Total segment liabilities	27	1,327	53,845	41,201	53,872	42,528
Interest income	-	-	1,271	1,566	1,271	1,566
Finance costs	-	-	(936)	(874)	(936)	(874)
Depreciation	(34)	(39)	(94)	(100)	(128)	(139)
Impairment of available for sale investments	(754)	(533)	(511)	(306)	(1,265)	(839)
Purchase of property and equipment	(18)	(6)	(78)	(58)	(96)	(64)
Purchase of investment properties	-	-	(5,055)	(975)	(5,055)	(975)
Provision for staff indemnity	(45)	(32)	(246)	(191)	(291)	(223)

Segment income above represents income generated from external customers. There was no inter-segment income in the year (2010: Nil).

For the purposes of monitoring segment performance and allocating resources between segments:

- There are no assets used jointly by any reportable segment.
- There are no liabilities for which any segment is jointly liable

32. Fiduciary accounts

The group manages portfolios on behalf of others, mutual funds and maintains cash balances and securities in fiduciary accounts, which are not reflected in the consolidated statement of financial position. Assets under management as at 31 December 2011 amounted to KD829,961 thousand (2010: KD1,029,743 thousand). The group earned management fee of KD6,159 thousand (2010: KD7,063 thousand) from these activities.

33. Contingent liabilities and commitments

	31 December 2011	31 December 2010
	KD '000	KD '000
Commitments for purchase of investments	6,832	9,362

34. Financial risk management objectives

The group's activities expose it to the variety of financial risks: Market risk (including foreign currency, equity price and investment rate risks), credit risk and equity risk.

The board of directors of the parent company are ultimately responsible for setting out risk management objectives. The group's risk management function provides services to the business, co-ordinates access to domestic and international financial markets, monitors and manages the financial risks relating to the operations of the group through internal risk reports which analyse exposures by degree and magnitude of risks.

The group does not enter into or trade in financial investment, including derivative financial instruments, for speculative purpose.

The most significant financial risks to which the group is exposed to are described below.

34.1 Market risk

Market risk is the risk that changes in market prices, such as equity prices, foreign exchange rates and interest rates will affect the group's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return.

The group's activities expose it primarily to the financial risks of changes in foreign currency exchange rates, interest rates and equity prices.

a) Equity price risk

The group is exposed to the equity price risk with respect to its equity investments. Equity investments are classified either as investments at fair value through statement of income or available for sale investments.

To manage its price risk arising from investments in equity securities, the group diversifies its portfolio in accordance with the limits set by the group.

The equity price risk sensitivity analysis shown below has been determined based on the quoted market price of investments at fair value through statement of income and available for sale investments that are listed on the Kuwait Stock Exchange at the reporting date.

If equity price had been 2% (2010: 2%) higher/lower, the effect on the (loss)/profit and equity for the year ended 31 December would have been as follows:

A positive number below indicates an increase in (loss)/profit and equity where the equity price increases by 2% (2010: 2%). A 2% (2010: 2%) decrease in the equity price would have the opposite effect. All other variables are held constant. There has been no change in the methods and the assumptions used in the preparation of the sensitivity analysis.

	31 December 2011			31 December 2010		
	change in price	Effect on profit	Effect on equity	change in price	Effect on profit	Effect on equity
	%	KD'000	KD'000	%	KD'000	KD'000
Market indices:						
Kuwait Stock Exchange	2%	41	-	2%	43	7

The group is not significantly exposed to any single stock exchange other than the Kuwait Stock Exchange.

34. Financial risk management objectives (continued)

34.1 Market risk (continued)

b) Foreign currency risk

The group undertakes certain transactions denominated in foreign currencies. Hence, exposures to exchange rate fluctuations arise. Exchange rate exposures are managed within approved policy parameters.

The carrying amounts of the group's foreign currency denominated monetary assets and monetary liabilities at the reporting date are as follows:

	Financial liabilities		Financial assets	
	31 December 2011	31 December 2010	31 December 2011	31 December 2010
	KD'000	KD'000	KD'000	KD'000
US Dollars	32,086	33,440	60,937	66,154
Euros	3	3	4,615	5,331
Sterling Pounds	1	1	492	581
Bahraini Dinars	-	-	168	194
UAE Dirhams	-	-	1,286	1,352
Qatari Riyals	-	-	245	382
Others	8	6	3,059	1,311

The group is maintaining exposure mainly to the US Dollars, Euros and UAE Dirhams.

The following table details the group's sensitivity to a 2% (2010: 2%) increase and decrease in the KD against US Dollars, Euros and UAE Dirhams. The sensitivity analysis includes only outstanding US Dollars, Euros and UAE Dirhams denominated monetary assets and liabilities and adjusts their translation at the year end for a 2% change in foreign currency rates. All other variables are held constant. There has been no change in the methods and the assumptions used in the preparation of the sensitivity analysis.

	+2 % Impact 31 December 2011 KD'000	+2 % Impact 31 December 2010 KD'000	-2 % Impact 31 December 2011 KD'000	-2 % Impact 31 December 2010 KD'000
(Loss)/profit for the year	(127)	38	127	(38)
Equity (i)	(796)	(723)	796	723

i) This is as a result of the changes in fair value of available for sale investments.

c) Interest rate risk

The group is exposed to interest rate risk as it borrows funds at both fixed and floating interest rates. The risk is managed by the group by maintaining an appropriate mix between fixed and floating rate borrowings and by the use of interest rate swap contracts. Hedging activities are evaluated regularly to align with interest rates views and defined risk appetite, ensuring the most cost effective hedging strategies were applied.

The group's exposures to interest rates on assets and liabilities are detailed in the liquidity risk management section of this note.

The following table illustrates the sensitivity of the (loss)/profit for the year to a reasonably possible change in interest rates of +1% and -1% (2010: +1% and -1%) with effect from the beginning of the year. These changes are considered to be reasonably possible based on observation of current market conditions. The calculations are based on the group's financial instruments held at each financial position date. All other variables are held constant. There has been no change in the methods and the assumptions used in the preparation of the sensitivity analysis other than the fact that the floating interest rate on bonds with a total value of US Dollars 50,000 thousand have now been converted in to a fixed interest rate through the use of interest rate swaps (see note 36).

A positive number below indicates an increase in (loss)/profit and negative number indicates decrease in (loss)/profit

	31 December 2011		31 December 2010	
	+1%	-1%	+1%	-1%
	KD'000	KD'000	KD'000	KD'000
(Loss)/profit for the year	(97)	97	(193)	193

34.2 Credit risk management

Credit risk refers to the risk that the counterparty will default on its contractual obligations resulting in financial loss to the group. The group has adopted a policy of only dealing with creditworthy counterparties and obtaining sufficient collateral, where appropriate, as a means of mitigating the risk of financial loss from defaults. The group uses publicly available financial information and its own trading records to rate its major customers. The group's exposure and the credit ratings of its counterparties are continuously monitored and the aggregate value of transactions concluded is spread amongst approved counterparties. Credit exposure is controlled by counterparty limits that are reviewed and approved by the management annually. Ongoing credit evaluation is performed on the financial condition of accounts receivable.

The group does not have any significant credit risk exposure to any single counterparty or any group of counterparties having similar characteristics. The group defines counterparties as having similar characteristics if they are related entities. Concentration of credit risk did not exceed 5 % of gross monetary assets at any time during the year.

Exposure to credit risk

The carrying amount of financial assets which is net of impairment losses, recorded in the consolidated statement of financial position represents the group's maximum credit exposure without taking account of the value of any collateral obtained. The maximum exposure to credit risk at the reporting date was:

	Carrying amount	
	31 December 2011	31 December 2010
	KD '000	KD '000
Bank balances	3,749	2,175
Time deposits	19,107	3,500
Accounts receivable and other assets	3,081	5,906
Short term financing	878	-
Loans to customers	11,884	12,893
Available for sale investments	52,645	56,823
	91,344	81,297

The maximum exposure to credit risk at the reporting date by geographic region was:

	Carrying amount	
	31 December 2011	31 December 2010
	KD '000	KD '000
Kuwait	48,051	42,215
North America	25,200	20,896
GCC	981	634
Europe	9,359	9,315
MENA	5,306	6,031
Emerging Markets	2,175	2,042
Japan	22	22
Others	250	142
	91,344	81,297

34.3 Credit quality of financial assets

The credit quality of financial assets that are neither past due nor impaired can be assessed by reference to historical information about counterparty default rates. The group assesses the credit quality of financial assets using internal records and customer profiles.

34. Financial risk management objectives (continued)

34.4 Liquidity risk

Liquidity risk is the risk that the group will not be able to meet its financial obligations as they fall due. The group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the group's reputation.

Ultimate responsibility for liquidity risk management rests with the board of directors, which has built an appropriate liquidity risk management framework for the management of the group's short, medium and long-term funding and liquidity management requirements. The group manages liquidity risk by maintaining adequate reserves, banking facilities and reserve borrowing facilities, by continuously monitoring forecast and actual cash flows and matching the maturity profiles of financial assets and liabilities.

Liquidity and interest risk tables

The table below analyses the group's financial liabilities based on the remaining period at the financial position date to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows. Balances due within 12 months equal their carrying balances as the impact of discounting is not significant.

	Upto 1 month	Upto 1-3 months	3-12 months	1 to 5 years	Total	Weighted average effective interest rate
	KD '000	KD '000	KD '000	KD '000	KD '000	%
31 December 2011						
Financial liabilities						
Accounts payable and other liabilities	311	44	262	1,818	2,435	-
Dividends payable	432	-	-	-	432	-
Bonds	-	181	29,177	26,400	55,758	1.406
	743	225	29,439	28,218	58,625	
Commitments	-	-	-	6,832	6,832	
31 December 2010						
Financial liabilities						
Due to banks and other financial institutions	3,753	-	-	-	3,753	4.833
Accounts payable and other liabilities	576	426	19	1,904	2,925	-
Dividends payable	344	-	-	-	344	-
Short term borrowings	5,500	-	-	-	5,500	4.125
Bonds	-	181	543	28,422	29,146	1.441
	10,173	607	562	30,326	41,668	
Commitments	-	-	-	9,362	9,362	

The maturity profile of the group's asset and liabilities is as follows:

	Upto one year KD'000	More than one year KD'000	Total KD'000
31 December 2011			
Assets:			
Cash and bank balances	3,750	-	3,750
Time deposits	19,107	-	19,107
Investments at fair value through statement of income	41,863	-	41,863
Accounts receivable and other assets	3,309	53	3,362
Short term finance	878	-	878
Loans to customers	11,237	647	11,884
Available for sale investments	-	52,645	52,645
Investment properties	-	7,538	7,538
Property and equipment	-	394	394
	80,144	61,277	141,421
Liabilities			
Accounts payable and other liabilities	1,726	1,818	3,544
Dividends payable	432	-	432
Bonds	27,896	22,000	49,896
	30,054	23,818	53,872
31 December 2010			
Assets:			
Cash and bank balances	2,177	-	2,177
Time deposits	3,500	-	3,500
Investments at fair value through statement of income	42,106	9,991	52,097
Accounts receivable and other assets	6,144	20	6,164
Loans to customers	12,893	-	12,893
Available for sale investments	-	56,823	56,823
Investment properties	-	2,340	2,340
Property and equipment	-	426	426
	66,820	69,600	136,420
Liabilities			
Due to banks and other financial institutions	3,753	-	3,753
Accounts payable and other liabilities	2,967	1,904	4,871
Dividends payable	344	-	344
Short term borrowings	5,500	-	5,500
Bonds	-	28,060	28,060
	12,564	29,964	42,528

35. Summary of financial assets and liabilities by category

The carrying amounts of the group's financial assets and liabilities as stated in the consolidated statement of financial position may also be categorized as follows:

	31 December 2011	31 December 2010
	KD '000	KD '000
Financial assets:		
Cash and bank balances	3,750	2,177
Time deposits	19,107	3,500
Investments at fair value through statement of income	41,863	52,097
Accounts receivable and other assets	3,081	5,906
Short term financing	878	-
Loans to customers	11,884	12,893
Available for sale investments	52,645	56,823
	133,208	133,396
Financial liabilities:		
Due to banks and other financial institutions	-	3,753
Accounts payable and other liabilities	2,435	2,925
Dividends payable	432	344
Short term borrowings	-	5,500
Bonds	49,896	28,060
	52,763	40,582

Fair value represents amounts at which an asset could be exchanged or a liability settled on an arm's length basis. In the opinion of the group's management, except for certain available for sale investments which are carried at cost for reasons specified in Note 20 to these consolidated financial statements, the carrying amounts of financial assets and liabilities as at 31 December 2011 and 2010 approximate their fair values.

The carrying amounts of the group's financial assets and liabilities as stated in the consolidated statement of financial position may also be categorized as follows:

	31 December 2011		31 December 2010	
	Fair value	Carrying amount	Fair value	Carrying amount
	KD '000	KD '000	KD '000	KD '000
Financial assets:				
Cash and bank balances	-	3,750	-	2,177
Time deposits	-	19,107	-	3,500
Investments at fair value through statement of income	41,863	-	52,097	-
Accounts receivable and other assets	-	3,081	-	5,906
Short term financing	-	878	-	-
Loans to customers	-	11,884	-	12,893
Available for sale investments	47,067	5,578	53,175	3,648
	88,930	44,278	105,272	28,124
Financial liabilities:				
Due to banks and other financial institutions	-	-	-	3,753
Accounts payable and other liabilities	243	2,192	557	2,368
Short term borrowings	-	-	-	5,500
Bonds	-	49,896	-	28,060
	243	52,088	557	39,681

Financial instruments measured at fair value

The following table presents financial assets and liabilities measured at fair value in the consolidated statement of financial position in accordance with the fair value hierarchy.

The following table provides an analysis of financial instruments that are measured subsequent to initial recognition at fair value, grouped into Levels 1 to 3 based on the degree to which the fair value is observable:

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The level within which the financial asset or liability is classified is determined based on the lowest level of significant input to the fair value measurement.

The financial assets and liabilities measured at fair value in the statement of consolidated financial position are grouped into the fair value hierarchy as follows:

31 December 2011

		Level 1 KD '000	Level 2 KD '000	Level 3 KD '000	Total KD '000
Investments at fair value through statement of income					
Investments held for trading	a	1,412	-	-	1,412
Financial assets designated at fair value through statement of income	a	3,773	33,432	3,246	40,451
Available for sale investments					
Managed funds					
- local	b	-	4,523	-	4,523
- foreign	c	-	16,217	-	16,217
Equity participations and other investments	d	-	-	26,327	26,327
Derivative financial instruments:					
Negative fair value					
-cash flow hedges		-	(243)	-	(243)
		5,185	53,929	29,573	88,687

35. Summary of financial assets and liabilities by category (continued)**Financial instruments measured at fair value (continued)****31 December 2010**

		Level 1	Level 2	Level 3	Total
		KD '000	KD '000	KD '000	KD '000
Investments at fair value through statement of income					
Investments held for trading	a	1,040	1,580	-	2,620
Financial assets designated at fair value through statement of income	a	8,635	33,368	7,474	49,477
Available for sale investments					
Quoted securities	a	277	-	-	277
Managed funds					
- local	b	-	5,436	-	5,436
- foreign	c	-	19,339	1,381	20,720
Equity participations and other investments	d	-	-	26,742	26,742
Derivative financial instruments:					
Negative fair value					
-cash flow hedges		-	(557)	-	(557)
		9,952	59,166	35,597	104,715

There have been no significant transfers between levels 1 and 2 during the reporting period.

Measurement at fair value

The methods and valuation techniques used for the purpose of measuring fair value are unchanged compared to the previous reporting period.

a) Quoted Securities

All the listed equity securities are publicly traded on a recognized stock exchange. Fair value has been determined by referring to their quoted bid prices at the reporting date.

b) Local managed funds

The underlying investments in local managed funds primarily comprise of local quoted securities whose fair values has been determined by reference to their quoted bid prices at the reporting date.

c) Foreign managed funds

The underlying investments of foreign managed funds primarily comprise of foreign quoted and unquoted securities. The fair value of the quoted underlying securities has been determined by reference to their quoted bid prices at the reporting date. The fair value of the unquoted underlying securities has been determined using valuation techniques that are normally used by Fund Managers. All significant inputs into the model are based on observable market prices

d) Unquoted securities

Unlisted securities are measured at fair value estimated using various models like discounted cash flow model, which includes some assumptions that are not supportable by observable market prices or rates.

Level 3 fair value measurements

The group's financial assets and liabilities classified in Level 3 uses valuation techniques based on significant inputs that are not based on observable market data. The financial instruments within this level can be reconciled from beginning to ending balances as follows:

31 December 2011

	Investments at fair value through statement of income	Available for sale investments	Total
	KD '000	KD '000	KD '000
Opening balance	7,474	28,123	35,597
Purchases	-	2,782	2,782
Reclassification to level 2	(4,228)	-	(4,228)
Sales	-	(5,762)	(5,762)
Gains or losses recognised in:			
- Consolidated statement of income	-	2,244	2,244
- Other comprehensive income	-	(1,060)	(1,060)
Closing balance	3,246	26,327	29,573

31 December 2010

	Investments at fair value through statement of income	Available for sale investments	Total
	KD '000	KD '000	KD '000
Opening balance	3,693	26,579	30,272
Purchases	4,209	2,331	6,540
Sales	(428)	(2,730)	(3,158)
Gains or losses recognised in:			
- Consolidated statement of income	-	1,419	1,419
- Other comprehensive income	-	524	524
Closing balance	7,474	28,123	35,597

Gains or losses recognized in the consolidated statement of income for the year are included in Loss on sale of investments at fair value through statement of income, Change in fair value of investments at fair value through statement of income and Gain on sale of available for sale investments.

Changing inputs to the level 3 valuations to reasonably possible alternative assumptions would not change significantly amounts recognized in the consolidated statement of income, total assets, total liabilities or total equity.

36. Derivative financial instruments

Derivatives are financial instruments that derive their value by referring to interest rate, foreign exchange rate or other indices. Notional principal amounts merely represent amounts to which a rate or price is applied to determine the amounts of cash flows to be exchanged and do not represent the potential gain or loss associated with the market or credit risk of such instruments.

Derivatives are carried at fair value and shown in the consolidated statement of financial position net of any internal arbitrage deals. Positive fair value represents the cost of replacing all transactions with a fair value in the group's favour had the rights and obligations arising from that instrument been closed in an orderly market transaction at the consolidated statement of financial position date. Credit risk in respect of derivative financial instruments is limited to the positive fair value of instruments. Negative fair value represents the cost to the group in favour of the counter parties.

The group deals in interest rate swaps to manage its interest rate risk on interest bearing bonds. Similarly the group deals in forward foreign exchange contracts to manage its foreign currency positions and cash flows.

a) Cash flow hedges (Interest rate swap contracts)

Under interest rate swap contracts, the group agreed to exchange the difference between fixed and floating rate interest amounts on bonds calculated on agreed notional principal amounts. Such contracts enable the group to mitigate the risk of changing interest rates on the cash flow exposures on the bonds issued at variable interest of 3 months LIBOR plus 1.1%. The fair value of interest rate swaps at the end of the reporting period is determined by discounting the future cash flows using the curves at the end of the reporting period and the credit risk inherent in the contract, and is disclosed below. The average interest rate is based on the outstanding balances at the end of the reporting period.

36. Derivative financial instruments (continued)

The following table details the notional principal amounts and remaining terms of interest rate swap contracts outstanding at the end of the reporting period.

	Average contracted fixed		Notional principal value		Fair value Negative	
	interest rate					
	31 December 2011	31 December 2010	31 December 2011	31 December 2010	31 December 2011	31 December 2010
	%	%	KD '000	KD '000	KD '000	KD '000
5 July 2012	+2.38	+2.38	6,974	7,015	(99)	(221)
5 July 2012	+3.27	+3.27	6,974	7,015	(144)	(336)

The interest rate swaps settle on a quarterly basis. The floating rate on the interest rate swaps is the 3 months LIBOR. The group settles the difference between the fixed and floating interest rate on a net basis.

All interest rate swap contracts exchanging floating rate interest amounts for fixed rate interest amounts are designated as cash flow hedges in order to reduce the group's cash flow exposure resulting from variable interest rates on bonds. The net cash inflow or outflow on the interest rate swaps and the interest payments on the bonds occur simultaneously.

37. Operational risk

Operational risk is the risk of loss arising from inadequate or failed internal processes, human error, systems failure or from external events. The group has a set of policies and procedures, which are approved by the Board of Directors and are applied to identify, assess and supervise operational risk. The management ensures compliance with policies and procedures and monitors operational risk as part of overall risk management.

38. Capital management objectives

The group manages its capital to ensure that it will be able to continue as a going concern while maximising the return to shareholders through the optimisation of the debt and equity balance. The group's overall strategy remains unchanged from previous year.

The capital structure of the group consists of equity attributable to Owners of the parent company, comprising issued share capital, share premium and reserves as disclosed in notes 23, 24, 25 and 26 respectively, treasury shares as disclosed in note 27 and retained earnings. Debt consists of short term borrowings and bonds disclosed in note 22.

Gearing ratio

The gearing ratio at year end was as follows:

	31 December 2011	31 December 2010
	KD '000	KD '000
Debt	49,896	33,560
Less: Cash and cash equivalents (see note 15)	(22,857)	(1,924)
Net debt	27,039	31,636
Equity	84,172	92,925
Net debt to equity ratio	32.12%	34.04%

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