

Consolidated Financial Statements and Independent Auditors' Report

For the year ended 31 December 2012

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Board of Directors' Report

The Directors have pleasure in presenting their report together with the audited consolidated financial statements of National Bank of Kuwait S.A.K ("the Bank") and its subsidiaries (collectively "the Group") for the year ended 31 December 2012.

The consolidated financial statements of the Group for the year ended 31 December 2012 include the financial results of Boubyan Bank K.S.C. which became a subsidiary of the Bank in July 2012.

2012 Financial Performance

The Group reported a net profit after non-controlling interests of KD 305.1 million compared to KD 302.4 million for 2011. Operating profit at KD 466.2 million reflects a 23.3% increase from 2011 (KD 378.3 million).

Net interest income and net income from Islamic financing at KD 397.8 million reflects a 4.4% increase on 2011 (KD 381.0 million), including the contribution arising from the consolidation of Boubyan Bank K.S.C.

Investment income amounted to KD 109.8 million as compared to KD 14 million in 2011. The increase was mainly due to the unrealized gain of KD 81.5 million arising from the fair valuation of the Bank's previously held stake in Boubyan Bank K.S.C. at the time of obtaining control.

Share of results of associates amounted to KD 13.4 million as compared to KD 17.1 million in 2011. The reclassification of Boubyan Bank K.S.C. from associate to subsidiary during 2012 and the consequent change in accounting of its results was the primary reason for this decrease.

Operating expenses amounted to KD 183.7 million as compared to KD 162.0 million in 2011. The increase was largely due to the consolidation of Boubyan Bank K.S.C. and the Group's ongoing investment in its IT systems. The cost to income ratio stood at 28.3% as compared to 30.0% in 2011.

2012 Balance Sheet

Total assets of the Group grew to KD 16,424.5 million from KD 13,626.8 million at the end of 2011. The increase was partly due to the consolidation of Boubyan Bank K.S.C. for the first time during 2012. Loans, advances and Islamic financing to customers increased by KD 1,692.2 million to KD 9,874.4 million. Investment securities increased by KD 76.8 million to reach KD 1,579.8 million at the year end. Investment in associates decreased by KD 314.8 million to KD 213.2 million during the year as a result of the reclassification of the Bank's investment in Boubyan Bank K.S.C. from investment in associate to that of a subsidiary.

The Group maintained a strong liquidity position with cash, short term funds, Central Bank of Kuwait bonds and Kuwait Government treasury bonds amounting to KD 2,581.1 million at the year end. Deposits with banks amounted to KD 1,203.4 million.

The Group's general provisions in respect of on-balance sheet credit facilities amounted to KD 254.7 million at the year end compared to KD 176.6 million in 2011, whilst specific provisions increased to KD 176.8 million from KD 143.2 million in 2011. The Group operates a conservative credit policy with a balanced diversification across all business sectors and geographical areas. Loan collateral profiles and values are continually monitored to ensure that optimum protection is afforded to the Group at all times.

Customer deposits increased by KD 2,708.6 million to reach KD 9,507.8 million at the year end. The Group benefits from a loyal Kuwaiti customer base whose deposits remain a continuing source of stable funding. Due to banks and financial institutions decreased by KD 155.4 million to KD 4,155.0 million at the year end.

Cash and non-cash credit facilities provided by the Bank to members of the Board of Directors and to related parties amounted to KD 217.9 million at the year end against collateral of KD 362.3 million. Deposits of Board members and related parties were KD 22.7 million. Loans and facilities to the Bank's executive management amounted to KD 472 thousand whilst deposits of the Bank's executive management amounted to KD 1,405 thousand.

Equity Attributable to the Shareholders of the Bank

Total equity attributable to the shareholders of the Bank, after deducting the proposed cash dividend of KD 128.2 million, amounted to KD 2,298.3 million as compared to KD 2,167.5 million at the end of 2011.

The Basel II capital adequacy ratio was 17.0% at the year end as compared to the minimum 12% prescribed by the Central Bank of Kuwait.

Capital Market Authority Requirements

The necessary measures were taken to ensure compliance with the issuance of Law No (7) for the year 2010, and subsequent Executive By-Laws relating to the Establishment of the Capital Market Authority and Organization of Securities Activities.

The Bank maintains a record for reporting the Bank's shares owned, and any changes in ownership, by the members of the Board of Directors (or their spouses), Executive Management, General Managers, Deputy General Managers and Assistant General Managers to the Capital Market Authority and Stock Exchange.

The salaries and other financial benefits of the members of Executive Management, General Managers, Deputy General Managers and Assistant General Managers amounted to KD 16,057 thousand for the year 2012.

Share Based Compensation Plan

The Bank operates an equity settled share based compensation plan and granted 1,666,920 (2011: 2,291,174) share options to its senior executives in 2012 with a fair value of KD 0.914 (2011: KD 1.232) per share option. The Bank operates this plan as an incentive to retain eligible employees, enhance loyalty to the Bank and to attract experienced and skilled personnel. These options will vest if employees remain in service for a period of three years from the grant date and the employees can exercise the options within one year from the vesting date. The options will expire if the employees do not exercise them within one year from the vesting date.

The General Assembly of the Bank's shareholders on 11 March 2012 authorized the Board of Directors to designate the appropriate number of treasury shares to be used for the purpose of implementing the aforesaid plan during the term of the plan and in accordance with its provisions and the resolutions of the Bank's general assembly of 18 February 2006 and 20 February 2008 and the resolution of the Minister of Commerce and Industry No. 337 for the year 2004.

Bonus Shares, Dividends and Proposed Appropriations

The net profit for the year was principally allocated as follows:

1. KD 128.2 million to the dividend account for the distribution of a cash dividend of 30 fils per share (40 fils in 2011) subject to the approval of shareholders at the annual general meeting.
2. KD 21.8 million to the share capital account to cover the issuance of bonus shares equal to 5% of share capital at the end of 2012 (equivalent to 217,674,881 shares with a nominal value of 100 fils per share) subject to the approval of shareholders at the annual general meeting.
3. KD 19.8 million to the statutory reserve account to increase the balance to the minimum requirement of 50% of share capital.
4. KD 135.3 million to retained earnings.

Important Financial Indicators

KD million	2012	2011	2010
Total assets	16,424.5	13,626.8	12,898.9
Loans, advances and Islamic financing to customers	9,874.4	8,182.2	7,853.3
Customer deposits	9,507.8	6,799.2	6,385.2
Total operating income	649.9	540.2	498.6
Profit attributable to shareholders of the parent Bank	305.1	302.4	301.7

Consolidated Financial Statements

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Consolidated Statement of Income

For the year ended 31 December 2012

	Notes	2012 KD 000's	2011 KD 000's	2012 USD 000's	2011 USD 000's
Interest income	4	491,464	490,164	1,747,428	1,742,805
Interest expense	5	118,747	109,192	422,212	388,238
Net interest income		372,717	380,972	1,325,216	1,354,567
Murabaha and other Islamic financing income		29,757	-	105,802	-
Distribution to depositors and Murabaha costs		4,650	-	16,533	-
Net income from Islamic financing		25,107	-	89,269	-
Net interest income and net income from Islamic financing		397,824	380,972	1,414,485	1,354,567
Net fees and commissions	6	103,397	104,078	367,634	370,055
Investment income	7	109,817	13,976	390,460	49,692
Net gains from dealing in foreign currencies		24,038	22,811	85,468	81,106
Share of results of associates		13,377	17,111	47,563	60,839
Other operating income		1,477	1,290	5,252	4,587
Non-interest income		252,106	159,266	896,377	566,279
Net operating income		649,930	540,238	2,310,862	1,920,846
Staff expenses		102,169	91,347	363,268	324,789
Other administrative expenses		63,755	54,674	226,684	194,397
Depreciation of premises and equipment		13,706	11,880	48,732	42,240
Amortisation of intangible assets	14	4,053	4,081	14,411	14,510
Operating expenses		183,683	161,982	653,095	575,936
Operating profit before provision for credit losses and impairment losses		466,247	378,256	1,657,767	1,344,910
Provision charge for credit losses	11	124,283	52,393	441,895	186,286
Impairment losses for investment securities	12	14,735	4,900	52,391	17,422
Operating profit before taxation		327,229	320,963	1,163,481	1,141,202
Taxation	8	18,632	17,311	66,247	61,550
Profit for the year		308,597	303,652	1,097,234	1,079,652
Attributable to:					
Shareholders of the Bank		305,125	302,406	1,084,889	1,075,222
Non-controlling interests		3,472	1,246	12,345	4,430
		308,597	303,652	1,097,234	1,079,652
Basic and diluted earnings per share attributable to shareholders of the Bank	9	71 fils	70 fils	25 Cents	25 Cents

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

Consolidated Statement of Comprehensive Income

For the year ended 31 December 2012

	Notes	2012 KD 000's	2011 KD 000's	2012 USD 000's	2011 USD 000's
Profit for the year		308,597	303,652	1,097,234	1,079,652
Other comprehensive income					
Change in fair value of investments available for sale		16,371	(2,798)	58,208	(9,948)
Net gains on investments available for sale transferred to consolidated statement of income	7	(27,336)	(8,869)	(97,195)	(31,534)
Impairment losses on investments available for sale transferred to consolidated statement of income	12	14,735	4,900	52,391	17,422
Share of other comprehensive income (loss) of associates		966	(795)	3,435	(2,827)
Exchange differences on translation of foreign operations		(3,270)	(21,140)	(11,627)	(75,165)
Other comprehensive income (loss) for the year included in equity		1,466	(28,702)	5,212	(102,052)
Total comprehensive income for the year		310,063	274,950	1,102,446	977,600
Attributable to:					
Shareholders of the Bank		305,839	273,748	1,087,427	973,326
Non-controlling interests		4,224	1,202	15,019	4,274
		310,063	274,950	1,102,446	977,600

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

Consolidated Statement of Financial Position

As at 31 December 2012

	Notes	2012 KD 000's	2011 KD 000's	2012 USD 000's	2011 USD 000's
Assets					
Cash and short term funds	10	1,610,765	1,271,252	5,727,164	4,520,007
Central Bank of Kuwait bonds	12	614,152	454,378	2,183,651	1,615,566
Kuwait Government treasury bonds	12	356,211	396,304	1,266,528	1,409,081
Deposits with banks		1,203,418	787,517	4,278,820	2,800,060
Loans, advances and Islamic financing to customers	11	9,874,422	8,182,226	35,109,056	29,092,359
Investment securities	12	1,579,850	1,503,035	5,617,244	5,344,125
Investment in associates	13	213,175	527,978	757,956	1,877,255
Land, premises and equipment		191,485	174,201	680,836	619,381
Goodwill and other intangible assets	14	635,002	215,503	2,257,785	766,233
Other assets	15	146,007	114,454	519,136	406,948
Total assets		16,424,487	13,626,848	58,398,176	48,451,015
Liabilities					
Due to banks and other financial institutions		4,154,983	4,310,339	14,773,273	15,325,650
Customer deposits		9,507,754	6,799,192	33,805,347	24,174,905
Other liabilities	16	213,739	180,744	759,961	642,645
Total liabilities		13,876,476	11,290,275	49,338,581	40,143,200
Equity					
Share capital	17	435,349	395,772	1,547,908	1,407,189
Proposed bonus shares	18	21,768	39,577	77,397	140,718
Statutory reserve	17	217,675	197,886	773,956	703,595
Share premium account	17	699,840	699,840	2,488,320	2,488,320
Treasury shares	17	(79,171)	(33,415)	(281,497)	(118,809)
Treasury share reserve	17	17,957	20,403	63,847	72,544
General reserve	17	117,058	117,058	416,206	416,206
Retained earnings	17	864,498	729,601	3,073,771	2,594,137
Foreign currency translation reserve	17	(35,522)	(33,032)	(126,301)	(117,447)
Cumulative changes in fair values	17	26,561	23,357	94,439	83,047
Share based payment reserve	17	12,313	10,469	43,780	37,223
Total share capital and reserves		2,298,326	2,167,516	8,171,826	7,706,723
Proposed cash dividend	18	128,189	157,092	455,783	558,550
Equity attributable to shareholders of the Bank		2,426,515	2,324,608	8,627,609	8,265,273
Non-controlling interests		121,496	11,965	431,986	42,542
Total equity		2,548,011	2,336,573	9,059,595	8,307,815
Total liabilities and equity		16,424,487	13,626,848	58,398,176	48,451,015

Mohammed Abdul Rahman Al-Bahar
Chairman

Nasser MUSAED Abdullah Al-Sayer
Vice Chairman

Ibrahim Shucri Dabdoub
Group Chief Executive Officer

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

Consolidated Statement of Cash Flows

For the year ended 31 December 2012

Notes	2012 KD 000's	2011 KD 000's	2012 USD 000's	2011 USD 000's
Operating activities				
Profit for the year	308,597	303,652	1,097,234	1,079,652
Adjustments for :				
Investment income	(109,817)	(13,976)	(390,460)	(49,692)
Share of results of associates	(13,377)	(17,111)	(47,563)	(60,839)
Depreciation of premises and equipment	13,706	11,880	48,732	42,240
Amortisation of intangible assets	4,053	4,081	14,411	14,510
Provision charge for credit losses	124,283	52,393	441,895	186,286
Impairment losses for investment securities	14,735	4,900	52,391	17,422
Share based payment reserve	1,868	2,172	6,642	7,723
Taxation	18,632	17,311	66,247	61,550
Operating profit before changes in operating assets and liabilities	362,680	365,302	1,289,529	1,298,852
Changes in operating assets and liabilities:				
Central Bank of Kuwait bonds	(159,774)	(19,136)	(568,085)	(68,039)
Kuwait Government treasury bonds	40,093	25,833	142,553	91,851
Deposits with banks	(229,985)	(71,095)	(817,724)	(252,782)
Loans, advances and Islamic financing to customers	(633,781)	(381,238)	(2,253,444)	(1,355,513)
Other assets	11,369	(41,839)	40,423	(148,761)
Due to banks and other financial institutions	(651,161)	236,459	(2,315,239)	840,743
Customer deposits	1,748,905	413,954	6,218,329	1,471,836
Other liabilities	(3,852)	(7,601)	(13,696)	(27,026)
Tax paid	(18,824)	(21,782)	(66,930)	(77,447)
Net cash from operating activities	465,670	498,857	1,655,716	1,773,714
Investing activities				
Purchase of investment securities	(1,696,301)	(1,785,644)	(6,031,292)	(6,348,956)
Proceeds from sale/redemption of investment securities	1,739,061	1,600,418	6,183,328	5,690,375
Dividend income	3,550	4,543	12,622	16,153
Acquisition of a subsidiary, net of cash acquired	49,331	-	175,399	-
Acquisition of non-controlling interests	(733)	(4,335)	(2,606)	(15,413)
Investment in associates	-	(22,968)	-	(81,664)
Dividend from associates	10,474	7,809	37,241	27,765
Proceeds from sale of land, premises and equipment	888	310	3,157	1,102
Purchase of land, premises and equipment	(23,774)	(12,042)	(84,530)	(42,816)
Net cash from (used in) investing activities	82,496	(211,909)	293,319	(753,454)
Financing activities				
Dividends paid	(157,181)	(143,567)	(558,866)	(510,461)
Proceeds from sale of treasury shares	6,571	174	23,363	619
Purchase of treasury shares	(54,773)	(23,092)	(194,748)	(82,105)
Net cash used in financing activities	(205,383)	(166,485)	(730,251)	(591,947)
Increase in cash and short term funds				
Exchange differences on translation of foreign operations	(3,270)	(21,140)	(11,627)	(75,165)
Cash and short term funds at the beginning of the year	1,271,252	1,171,929	4,520,007	4,166,859
Cash and short term funds at the end of the year	1,610,765	1,271,252	5,727,164	4,520,007

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

Consolidated Statement of Changes in Equity

For the year ended 31 December 2012

	Equity attributable to shareholders of the Bank								Non - controlling interests	Total equity
	Proposed		Statutory reserve	Share premium account	Treasury shares	Treasury share reserve	Other reserves (Note 17)	Total		
	Share capital	bonus shares								
At 1 January 2011	359,793	35,979	179,897	699,840	(12,410)	22,316	932,220	2,217,635	12,868	2,230,503
Profit for the year	-	-	-	-	-	-	302,406	302,406	1,246	303,652
Other comprehensive loss	-	-	-	-	-	-	(28,658)	(28,658)	(44)	(28,702)
Total comprehensive income	-	-	-	-	-	-	273,748	273,748	1,202	274,950
Transfer to statutory reserve	-	-	17,989	-	-	-	(17,989)	-	-	-
Issue of bonus shares (Note 18)	35,979	(35,979)	-	-	-	-	-	-	-	-
Purchase of treasury shares	-	-	-	-	(23,092)	-	-	(23,092)	-	(23,092)
Sale of treasury shares	-	-	-	-	2,087	(1,913)	-	174	-	174
Dividends paid	-	-	-	-	-	-	(143,567)	(143,567)	-	(143,567)
Proposed bonus shares (Note 18)	-	39,577	-	-	-	-	(39,577)	-	-	-
Share based payment (Note 19)	-	-	-	-	-	-	2,172	2,172	-	2,172
Acquisition of non-controlling interests	-	-	-	-	-	-	(2,462)	(2,462)	(1,873)	(4,335)
Dividend paid by subsidiary	-	-	-	-	-	-	-	-	(232)	(232)
At 31 December 2011	395,772	39,577	197,886	699,840	(33,415)	20,403	1,004,545	2,324,608	11,965	2,336,573
Profit for the year	-	-	-	-	-	-	305,125	305,125	3,472	308,597
Other comprehensive income	-	-	-	-	-	-	714	714	752	1,466
Total comprehensive income	-	-	-	-	-	-	305,839	305,839	4,224	310,063
Transfer to statutory reserve	-	-	19,789	-	-	-	(19,789)	-	-	-
Issue of bonus shares (Note 18)	39,577	(39,577)	-	-	-	-	-	-	-	-
Purchase of treasury shares	-	-	-	-	(54,773)	-	-	(54,773)	-	(54,773)
Sale of treasury shares	-	-	-	-	9,017	(2,446)	-	6,571	-	6,571
Dividends paid	-	-	-	-	-	-	(157,181)	(157,181)	-	(157,181)
Proposed bonus shares (Note 18)	-	21,768	-	-	-	-	(21,768)	-	-	-
Share based payment (Note 19)	-	-	-	-	-	-	1,844	1,844	24	1,868
Acquisition of non-controlling interests	-	-	-	-	-	-	(393)	(393)	(340)	(733)
Dividend paid by subsidiary	-	-	-	-	-	-	-	-	(101)	(101)
Acquisition of a subsidiary (Note 26)	-	-	-	-	-	-	-	-	105,724	105,724
At 31 December 2012	435,349	21,768	217,675	699,840	(79,171)	17,957	1,113,097	2,426,515	121,496	2,548,011

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

Notes to the Consolidated Financial Statements

31 December 2012

1 INCORPORATION AND REGISTRATION

The consolidated financial statements of National Bank of Kuwait S.A.K. ("the Bank") and its subsidiaries (collectively "the Group") for the year ended 31 December 2012 were authorised for issue in accordance with a resolution of the directors on 6 January 2013. The Annual General Assembly of the Shareholders has the power to amend these consolidated financial statements after issuance. The Bank is a public shareholding company incorporated in Kuwait in 1952 and is registered as a bank with the Central Bank of Kuwait. The Bank's registered office is at Abdullah Al Ahmed Street, P.O. Box 95, Safat 13001, Kuwait. The principal activities of the Bank are described in Note 3.

2 SIGNIFICANT ACCOUNTING POLICIES

2.1 Basis of preparation

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

The consolidated financial statements are prepared under the historical cost convention except for the measurement at fair value of derivatives, investment securities other than held to maturity investments and investment properties. In addition and as more fully described below, assets and liabilities that are hedged in fair value hedging relationships are carried at fair value to the extent of the risk being hedged.

2.2 Changes in accounting policies

The accounting policies applied are consistent with those used in the previous year. The following amendments to IFRS effective for the annual periods beginning on or after 1 January 2012 did not have any impact on the accounting policies, financial position or performance of the Group.

IFRS 7 Financial Instruments: Disclosures (amendment)

IAS 12 Income Taxes (amendment) - Deferred Taxes: Recovery of Underlying Assets

Standards issued but not yet effective:

A number of new standards, amendments to standards and interpretations which are effective for annual periods beginning on or after 1 January 2013 have not been early adopted in the preparation of the Group's consolidated financial statements. None of these are expected to have a significant impact on the consolidated financial statements of the Group except the following:

IFRS 9: Financial Instruments: Classification and Measurement (effective 1 January 2015)

IFRS 9, as issued, reflects the first phase of the IASB's work on replacement of IAS 39 and applies to classification and measurement of financial assets and liabilities as defined in IAS 39. Impairment and hedge accounting will be addressed in subsequent phases.

IFRS 10: Consolidated Financial Statements (effective 1 January 2013)

IFRS 10 replaces the consolidation guidance in IAS 27 Consolidated and Separate Financial Statements and SIC-12 Consolidation - Special Purpose Entities by introducing a single consolidation model for all entities based on control, irrespective of the nature of the investee (i.e., whether an entity is controlled through voting rights of investors or through other contractual arrangements as is common in special purpose entities). Under IFRS 10, control is based on whether an investor has 1) power over the investee; 2) exposure or rights, to variable returns from its involvement with the investee and 3) the ability to use its power over the investee to affect the amount of the returns. Further in November 2012, IASB has issued an amendment to IFRS 10 Consolidated Financial Statements to provide an exception to the consolidation requirement for entities that meet the definition of an investment entity. The exception to consolidation requires investment entities to account for subsidiaries at fair value through profit or loss in accordance with IFRS 9 Financial Instruments. The amendment applies for annual periods beginning on or after 1 January 2014 with earlier application permitted. The adoption of this standard is not expected to have any material impact on the financial position or performance of the Group.

IFRS 12: Disclosure of Involvement with Other Entities (effective 1 January 2013)

IFRS 12 requires enhanced disclosures about both consolidated entities and unconsolidated entities in which an entity has involvement. The objective of IFRS 12 is to require information so that financial statement users may evaluate the basis of control, any restrictions on consolidated assets and liabilities, risk exposures arising from involvements with unconsolidated structured entities and non-controlling interest holders' involvement in the activities of consolidated entities.

IFRS 13: Fair Value Measurement (effective 1 January 2013)

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

2.3 Basis of consolidation

The consolidated financial statements comprise the financial statements of the Bank as at 31 December each year and its subsidiaries as at the same date or a date not earlier than three months from 31 December. The financial statements of subsidiaries and associates are prepared using consistent accounting policies and are adjusted, where necessary, to bring the accounting policies in line with those of the Group. All intercompany balances and transactions, including unrealised profits arising from intra-group transactions have been eliminated on consolidation.

a. Subsidiaries

Subsidiaries are all entities over which the Bank has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. Subsidiaries are fully consolidated from the date on which control is transferred to the Group and are not consolidated from the date that control ceases. Refer note 21 for the list of major subsidiaries, their principal businesses and the Group's effective holding.

b. Non-controlling interest

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

c. Associates

Associates are all entities over which the Group has significant influence but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights. Investment in an associate is initially recognised at cost and subsequently accounted for by the equity method of accounting. The Group's investment in associates includes goodwill identified on acquisition. The Group's share of its associates' post-acquisition profits or losses is recognised in the consolidated statement of income, and its share of post-acquisition movements in other comprehensive income is recognised in other comprehensive income. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment.

The Group determines at each reporting date whether there is any objective evidence that the investment in the associate is impaired. If this is the case, the Group calculates the amount of impairment as the difference between the recoverable amount of the associate and its carrying value and recognises the amount in the consolidated statement of income. Upon loss of significant influence over the associate, the Group measures and recognises any retained investment at its fair value. Gain or loss on this transaction is computed by comparing the carrying amount of the associate at the time of loss of significant influence with the aggregate of fair value of the retained investment and proceeds from disposal. This is recognised in the consolidated statement of income.

2.4 Foreign currencies

The consolidated financial statements are presented in Kuwaiti Dinars (thousands) which is also the Bank's functional currency.

Notes to the Consolidated Financial Statements

31 December 2012

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

a. Translation of foreign currency transactions

Transactions in foreign currencies are initially recorded in the functional currency rate of exchange ruling at the date of the transaction. Monetary assets and monetary liabilities in foreign currencies (other than monetary items that form part of the net investment in a foreign operation) are translated into functional currency at rates of exchange prevailing at the statement of financial position date. Any gains or losses are taken to the consolidated statement of income. Exchange differences arising on monetary items that form part of the net investment in a foreign operation are determined using closing rates and recognised in other comprehensive income and presented in the foreign currency translation reserve in equity. When a foreign operation is disposed of, the cumulative amount in foreign currency translation reserve relating to that foreign operation is recognised in the consolidated statement of income. Goodwill, intangible assets and any fair value adjustments to the carrying value of assets and liabilities are recorded at the functional currency of the foreign operation and are translated to the presentation currency at the rate of exchange prevailing at the statement of financial position date. All resulting exchange differences are recognised in equity (foreign currency translation reserve).

Translation gains or losses on non-monetary items carried at fair value are included in equity as part of the fair value adjustment on investment securities available for sale, unless the non-monetary item is part of an effective hedging strategy.

b. Translation of financial statements of foreign entities

The results and financial position of all the Group entities that have a functional currency different from the presentation currency is translated to presentation currency as follows:

The assets and liabilities are translated at rates of exchange ruling at the statement of financial position date. Income and expense items are translated at average exchange rates for the year. All resulting exchange differences (including those on transactions which hedge such investments) are recognised in equity (foreign currency translation reserve) and duly recognised in the consolidated statement of income on disposal of the foreign operation.

2.5 Interest income and expenses

Interest income and expense for all interest-bearing financial instruments are recognised within 'interest income' and 'interest expense' in the consolidated statement of income using the effective interest method. The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. Fees which are considered an integral part of the effective yield of a financial asset are recognised using effective yield method. Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

2.6 Murabaha and other Islamic financing income

Income from Murabaha, Wakala and Leased assets is recognised on a pattern reflecting a constant periodic return on the outstanding net investment.

2.7 Fees and commission income

Fee income earned from services provided over a period of time is recognised over the period of service. Fees arising from providing a transaction service are recognised on completion of the underlying transaction. Portfolio and other management advisory and service fees are recognised based on the applicable service contracts, usually on a time-apportioned basis. Asset management fees related to investment funds are recognised over the period in which the service is provided. The same principle is applied for wealth management and custody services that are continuously provided over an extended period of time.

2.8 Dividend income

Dividend income is recognised when the right to receive payment is established.

2.9 Impairment of financial assets

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

a. Assets carried at amortised cost

The amount of impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the consolidated statement of income. If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognised in the consolidated statement of income. 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.

b. Assets classified as available for sale

The amount of impairment loss is measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in the consolidated statement of income. This amount is recognised in the consolidated statement of income. If, in a subsequent period, the amount of the impairment loss decreases for an equity instrument, the previously recognised losses are not reversed through the consolidated statement of income, instead, recorded as increase in the cumulative changes in fair value reserve. If, in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in consolidated statement of income, the impairment loss is reversed through the consolidated statement of income.

2.10 Impairment of non-financial assets

Goodwill and intangible assets that have an indefinite useful life are not subject to amortisation and are tested annually for impairment. Other non-financial assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. If previously recognised impairment losses have decreased, such excess impairment provision is reversed for non-financial assets other than goodwill.

2.11 Share based compensation

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

2.12 Post employment benefits

The Group is liable to make defined contributions to State Plans and lump sum payments under defined benefit plans to employees at cessation of employment, in accordance with the laws of the place they are employed. The defined benefit plan is unfunded and is computed as the amount payable to employees as a result of involuntary termination on the statement of financial position date. This basis is considered to be a reliable approximation of the present value of the final obligation.

Notes to the Consolidated Financial Statements

31 December 2012

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

2.13 Taxation

Income tax payable on taxable profit ('current tax') is recognised as an expense in the period in which the profits arise in accordance with the fiscal regulations of the respective countries in which the Group operates. Deferred tax assets are recognised for deductible temporary differences, carry forward of unused tax credits and unused tax losses, to the extent it is probable that taxable profit will be available to utilise these. Deferred tax liabilities are recognised for taxable temporary differences. Deferred tax assets and liabilities are measured using tax rates and applicable legislation enacted at the statement of financial position date.

2.14 Recognition of financial assets and financial liabilities

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

2.15 Cash and short term funds

Cash and short term funds consist of cash in hand, current account and money at call with other banks and deposits with banks maturing within seven days.

2.16 Deposits with banks

Deposits with banks are stated at amortised cost using the effective interest method less any amounts written off and provision for impairment. The carrying values of such assets which are being effectively hedged for changes in fair value are adjusted to the extent of the changes in fair value being hedged.

2.17 Loans and advances to customers

Loans and advances are financial assets with fixed or determinable payments that are not quoted in an active market.

Carrying value

Loans and advances are stated at amortised cost using the effective interest method less any amounts written off and provision for impairment. The carrying values of such assets which are being effectively hedged for changes in fair value are adjusted to the extent of the changes in fair value being hedged.

Renegotiated loans

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

2.18 Islamic financing to customers

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

a. Murabaha

Murabaha is an agreement relating to the sale of commodities at cost plus an agreed upon profit margin, whereby the seller informs the buyer of the price at which the deal will be completed and also the amount of profit to be recognized. Murabaha is a financial asset originated by the Group stated at amortized cost net of provision for impairment.

b. Wakala

Wakala is an agreement involving Al-Muwakkil (the Principal) who wishes to appoint Al-Wakil (the Agent) to be his agent with

respect to the investment of Al-Muwakkil's fund, in accordance with regulations of the Islamic Sharia'a. Wakala is a financial asset originated by the Group and stated at amortized cost net of provision for impairment.

c. Leased assets - the Group as a lessor

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating lease. Leased assets are stated at amounts equal to the net investment outstanding in the leases less provision for impairment.

2.19 Financial Investments

The Group classifies its financial investments in the following categories:

- Held to maturity
- Available for sale
- Investments carried at fair value through statement of income

All investments with the exception of investments at fair value through statement of income are initially recognised at cost, being the fair value of the consideration given including directly attributable transaction costs. Premiums and discounts on non-trading investments (excluding those carried at fair value through statement of income) are amortised using the effective yield method and taken to interest income.

Held to maturity

Held to maturity investments are investments with fixed or determinable payments and fixed maturity that the Group has the intention and ability to hold to maturity. Held to maturity investments are measured at amortised cost, less provision for impairment in value, if any. The losses arising from impairment of such investments are recognised in the consolidated statement of income. The interest income from debt securities classified as held to maturity is recorded in interest income.

Available for sale

Available for sale investments are those investments which are designated as available for sale or investments that do not qualify to be classified as fair value through statement of income, held to maturity, or loans and advances. After initial recognition, investments which are classified as "available for sale" are normally remeasured at fair value, unless fair value cannot be reliably determined in which case they are measured at cost less impairment. Fair value changes which are not part of an effective hedging relationship are recognised in other comprehensive income and presented in the cumulative changes in fair values in equity until the investment is derecognised or the investment is determined to be impaired. On derecognition or impairment the cumulative gain or loss previously reported as "cumulative changes in fair values" within equity, is included in the consolidated statement of income for the period. In case of a reversal of previously recognised impairment losses for equity investments, such changes will not be recognised in the current consolidated statement of income but will be recorded as an increase in the reserve for cumulative changes in fair values. If, in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised, the impairment loss is reversed through consolidated statement of income. The portion of any fair value changes relating to an effective hedging relationship is recognised directly in the consolidated statement of income. The interest income from debt securities classified as available for sale is recorded in interest income and the dividend income from equities are recorded in dividend income.

Investments carried at fair value through statement of income

Investments are classified as "investments carried at fair value through statement of income" if they are held for trading or, upon initial recognition, are designated as fair value through statement of income. Investments are classified as held for trading when they are acquired for the purpose of selling or repurchase in the near term with the intention of generating short-term profits, or are derivatives which are not designated as part of effective hedges. Investments are designated as fair value through statement of income if the fair value of the investment can be reliably measured and the classification as fair value through statement of income is as per the documented strategy of the Group. Investments classified as "investments carried at fair value through statement of income" are remeasured at fair value with all changes in fair value being recorded in the consolidated statement of income. Any dividend income of equities classified as 'investments carried at fair value through the statement of income' is recorded as part of 'dividend income'.

Notes to the Consolidated Financial Statements

31 December 2012

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

2.20 Fair values

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

For financial instruments where there is no active market, fair value is normally based on one of the following:

- the expected cash flows discounted at current rates applicable for items with similar terms and risk characteristics
- brokers' quotes
- recent transactions
- option pricing models

The estimated fair value of deposits with no stated maturity, including non-interest bearing deposits, is the amount payable on demand.

2.21 Repurchase and resale agreements

Assets sold with a simultaneous commitment to repurchase at a specified future date at an agreed price (repos) are not derecognised in the consolidated statement of financial position. Amounts received under these agreements are treated as interest bearing liabilities and the difference between the sale and repurchase price treated as interest expense using the effective yield method. Assets purchased with a corresponding commitment to resell at a specified future date at an agreed price (reverse repos) are not recognised in the consolidated statement of financial position. Amounts paid under these agreements are treated as interest earning assets and the difference between the purchase and resale price treated as interest income using the effective yield method.

2.22 Offsetting of financial assets and liabilities

Financial assets and financial liabilities are only offset and the net amount reported in the consolidated statement of financial position when there is a legally enforceable right to set off the recognised amounts and the Group intends to either settle on a net basis, or to realise the asset and settle the liability simultaneously.

2.23 Derecognition of financial assets and financial liabilities

Financial assets

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

- the rights to receive cash flows from the asset have expired, or
- the Group retains the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a 'pass through' arrangement, or
- the Group has transferred its rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

When the Group has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Group's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to repay.

Financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expired. Where 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.

2.24 Derivative financial instruments

The Group deals in interest rate swaps to manage its interest rate risk on interest bearing assets and liabilities and to provide interest rate risk management solutions to customers. Similarly the Group deals in forward foreign exchange contracts for customers and to manage its foreign currency positions and cash flows. All derivative financial instruments of the Group are recorded in the consolidated statement of financial position at fair value. The fair value of a derivative is the equivalent of the unrealised gain or loss from marking to market the derivative using prevailing market rates or internal pricing models. Positive and negative fair values are reported as assets and liabilities respectively and are offset when there is both an intention to settle net and a legal right to offset exists.

For the purposes of hedge accounting, hedges are classified into two categories: (a) fair value hedges which hedge the exposure to changes in the fair value of a recognised asset or liability and (b) cash flow hedges which hedge exposure to variability in cash flows that is either attributable to a particular risk associated with a recognised financial asset or liability or a highly probable forecast transaction.

In relation to fair value hedges which meet the conditions for hedge accounting, any gain or loss from remeasuring the hedging instrument is recognised immediately in the consolidated statement of income. The hedged items are adjusted for fair value changes relating to the risk being hedged and the difference is recognised in the consolidated statement of income.

In relation to cash flow hedges which meet the conditions for hedge accounting, the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised initially in equity and any ineffective portion is recognised in the consolidated statement of income. The gains or losses on cash flow hedges recognised initially in equity are transferred to the consolidated statement of income in the period in which the hedged transaction impacts the consolidated statement of income. Where the hedged transaction results in the recognition of an asset or liability, the associated gains or losses that had initially been recognised in equity are included in the initial measurement of the cost of the related asset or liability. For hedges that do not qualify for hedge accounting, any gains or losses arising from changes in fair value of the hedging instrument are taken directly to the consolidated statement of income.

Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated or exercised, no longer qualifies for hedge accounting or is revoked by the Group. For cash flow hedges, any cumulative gain or loss on the hedging instrument recognised in equity remains in equity until the forecast transaction occurs. In the case of fair value hedges of interest bearing financial instruments, any adjustment relating to the hedge is amortised over the remaining term to maturity. Where the hedged transaction is no longer expected to occur, the net cumulative gain or loss recognised in equity is transferred to the consolidated statement of income.

2.25 Trade and settlement date accounting

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

2.26 Investment properties

Investment properties are properties held either to earn rental income or for capital appreciation or for both, but not for sale in the ordinary course of business, use in the production or supply of goods or services or for administrative purposes. Investment property is measured at cost on initial recognition and subsequently at fair value with any change therein recognised in consolidated statement of income. Cost includes expenditure that is directly attributable to the acquisition of the investment property. Fair values of investment properties are determined by appraisers having an appropriate recognised professional qualification and recent experience in the location and category of the property being valued. Any gain or loss on disposal of an investment property (calculated as the difference between the net proceeds from disposal and the carrying amount of the item) is recognised in consolidated statement of income. When the use of a property changes such that it is reclassified as Land, premises and equipment, its fair value at the date of reclassification becomes its cost for subsequent accounting.

2.27 Land, premises and equipment

Land and premises comprise mainly branches and offices. All premises and equipment are stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Notes to the Consolidated Financial Statements

31 December 2012

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

Subsequent costs are included in the asset's carrying amount or are recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the consolidated statement of income during the period in which they are incurred.

Land is not depreciated. Depreciation is provided on the depreciable amount of other items of premises and equipments on a straight line basis over their estimated useful life. The depreciable amount is the gross carrying value, less the estimated residual value at the end of its useful life. The estimated useful life of premises and equipments are as follows:

Building on leasehold land	term of lease (maximum 20 years)
Building on freehold land	50 years
IT systems and equipment	3-10 years

Residual values and useful lives of assets are reviewed, and adjusted if appropriate, at each statement of financial position date. The carrying values of land, premises and equipment are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable. Gains and losses on disposals are determined by comparing proceeds with the carrying amount. These are included in the consolidated statement of income.

2.28 Business combinations

Business combinations are accounted for using the acquisition method of accounting. The cost of an acquisition is measured as the aggregate of the consideration transferred, measured at acquisition date fair value and the amount of any non-controlling interest in the acquiree. Non-controlling interest in the acquiree is measured at the proportionate share in the recognised amounts of the acquiree's identifiable net assets. Other acquisition related costs incurred are expensed and included in other administrative expenses.

If the business combination is achieved in stages, the acquirer's previously held equity interest in the acquiree is remeasured to fair value at the acquisition date and included in cost of acquisition. Any resulting gain or loss is recognised in consolidated statement of income. Identifiable assets acquired and liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. The excess of the cost of acquisition over the fair value of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the consolidated statement of income.

2.29 Goodwill and intangible assets

a. Goodwill

Goodwill acquired in a business combination is initially measured at cost, being the excess of the cost of the acquisition over the net fair value of the identifiable assets and liabilities acquired. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill is reviewed for impairment, annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired. Goodwill is recorded in the functional currency of the foreign operation and is translated to the presentation currency at the rate of exchange prevailing at the statement of financial position date. When subsidiaries are sold, the difference between the selling price and the net assets plus cumulative translation differences and goodwill is recognised in the consolidated statement of income.

b. Intangible assets

Intangible assets comprise separately identifiable intangible items arising from business combinations. An intangible asset is recognised only when its cost can be measured reliably and it is probable that the expected future economic benefit will flow to the Group. Intangible assets are initially measured at cost. The cost of intangible assets acquired in a business combination is their fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. The useful lives of the intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortised on a straight line basis over the useful economic life of 5 to 12 years and tested for impairment whenever there is an indication that the intangible asset may be impaired. Intangible assets with indefinite useful lives are not amortised but tested for impairment annually or whenever there is an indication that the intangible asset may be impaired. If the carrying value of the intangible asset is more than the recoverable amount, the intangible asset is considered impaired and is written down to its recoverable amount. The excess of carrying value over the recoverable amount is recognised in the consolidated statement of income. Impairment losses on intangible assets recognised in the consolidated statement of income in previous periods, are reversed when there is an increase in the recoverable amount.

2.30 Property acquired on settlement of debt

Property acquired on settlement of debt is stated at the lower of the related loans and advances and the current fair value of such assets. Gains or losses on disposal and revaluation losses are recognised in the consolidated statement of income.

2.31 Due to Banks and Financial Institutions & Customer deposits

Due to Banks and Financial Institutions & Customer Deposits are stated at amortised cost using effective interest method. The carrying values of such liabilities which are being effectively hedged for changes in fair value are adjusted to the extent of the changes in fair value being hedged.

2.32 Islamic customer deposits

Islamic customer deposits comprise of Murabaha payable, Investment accounts and Non-investment accounts.

Murabaha payable

Murabaha payable is an Islamic transaction involving the Group's purchase of an asset from a counterparty and settlement thereof at cost plus an agreed profit on a deferred payment basis. The purchase price is payable to the counterparty on maturity. Murabaha payable is stated at amortized cost.

Investment accounts

Investment accounts may take the form of investment deposits, which are valid for specified periods of time, and are automatically renewable on maturity for the same period, unless the concerned depositors give written notice to the contrary, or take the form of investment saving accounts for unspecified periods. In all cases, investment accounts receive a proportion of the profit, bear a share of loss and are carried at cost plus profit payable.

Non-investment accounts

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

2.33 Financial guarantees

In the ordinary course of business, the Group gives financial guarantees, consisting of letters of credit, guarantees and acceptances. Financial guarantees are initially recognised in the consolidated financial statements at fair value, being the premium received, in other liabilities. The premium received is recognised in the consolidated statement of income in 'net fees and commissions' on a straight line basis over the life of the guarantee. The guarantee liability is subsequently carried at initial measurement less amortisation. When a payment under the guarantee is likely to become payable, the present value of the expected net payments less the unamortised premium is charged to the consolidated statement of income.

Notes to the Consolidated Financial Statements

31 December 2012

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

2.34 Treasury shares

The Bank's holding of its own shares are accounted for as treasury shares and are stated at purchase consideration including directly attributable costs. When the treasury shares are sold, gains are credited to a separate account in equity (treasury share reserve) which is non 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 reserves. Gains realised subsequently on the sale of treasury shares are first used to offset any previously recorded losses in the order of reserves, retained earnings and the treasury share reserve amount. No cash dividends are distributed on these shares. The issue of bonus shares increases the number of shares proportionately and reduces the average cost per share without affecting the total cost of treasury shares.

2.35 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 the consolidated statement of financial position.

2.36 Significant accounting judgements and estimates

In the process of applying the Group's accounting policies, management has used judgements and made estimates in determining the amounts recognised in the consolidated financial statements. The most significant use of judgements and estimates are as follows:

Accounting Judgements

Impairment of available for sale equity investments

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

Classification of investments

Financial assets within the scope of IAS 39 are classified as financial assets at fair value through profit or loss, loans and receivables, held to maturity investments, available for sale financial assets, or as derivatives designated as hedging instruments in an effective hedge, as appropriate. The Group determines the classification of its financial assets at initial recognition.

Estimation uncertainty and assumptions

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

Impairment of goodwill

The Group determines whether goodwill is impaired at least on an annual basis. This requires an estimation of the value in use of the cash-generating units to which the goodwill is allocated. Estimating the value in use requires the Group to make an estimate of the expected future cash flows from the cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows.

Provision for credit losses

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

Fair values of assets and liabilities including intangibles

Considerable judgment by management is required in the estimation of the fair value of the assets including intangibles with definite and indefinite useful life, liabilities and contingent liabilities acquired as a result of business combination.

Share-based payments

The Group measures the cost of equity settled transactions with employees by reference to the fair value of the equity instruments at the date at which they are granted. Estimating fair value for share-based payment transactions requires determination of the most appropriate valuation model. This estimate also requires determination of the most appropriate inputs to the valuation model including the expected life of the share option, volatility and dividend yield and making assumptions about them. The assumptions and models used for estimating fair value for share-based payment transactions are disclosed in Note 19.

Valuation of unquoted financial assets

Fair value of unquoted financial assets is determined using valuation techniques including the discounted cash flow model. The inputs to these models are taken from observable markets where possible, but where this is not feasible, a degree of judgment is required in establishing fair values. The judgments include considerations of inputs such as liquidity risk, credit risk and volatility. Changes in assumptions about these factors could affect the reported fair value of financial instruments. The determination of the cash flows and discount factors requires significant estimation.

2.37 Basis of translation

The United States dollar amounts in the consolidated statement of income, consolidated statement of comprehensive income, consolidated statement of financial position and consolidated statement of cash flows represent supplementary information and have been translated at a rate of KD 0.28125 per USD which represents the mid-market rate at 31 December 2012.

3 SEGMENTAL ANALYSIS

The Group organises and manages its operations by geographic territory in the first instance, primarily Domestic and International. Within its domestic operations, the Group segments its business into Consumer and Private Banking, Corporate Banking, Investment Banking and Asset Management, Islamic Banking and Group Centre. All operations outside Kuwait are classified as International. Management treats the operations of these segments separately for the purposes of decision making, resource allocation and performance assessment.

Consumer and Private Banking

Consumer Banking provides a diversified range of products and services to individuals. The range includes consumer loans, credit cards, deposits, foreign exchange and other branch related services. Private Banking provides a comprehensive range of customised and innovative banking services to high net worth individuals and to institutional clients.

Corporate Banking

Corporate Banking provides a comprehensive product and service offering to business and corporate customers, including lending, deposits, trade finance, foreign exchange and advisory services.

Investment Banking and Asset Management

Investment Banking provides a full range of capital market advisory and execution services. The activities of Asset Management include wealth management, asset management, custody, brokerage and research.

Islamic Banking

Islamic banking represents the financial results of Boubyan Bank K.S.C, the Islamic banking subsidiary of the Group.

Group Centre

Group Centre includes treasury, investments, and other defined Group activities. Treasury provides a comprehensive range of treasury services and products to its clients, and is also responsible for the bank's liquidity and market risk management. Group Centre includes any residual in respect of transfer pricing and inter segment allocations.

International

International includes all branches, subsidiaries and associates outside Kuwait.

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3 SEGMENTAL ANALYSIS (Continued)

2012	Investment Banking and Asset Management						Total KD 000's
	Consumer and Private Banking KD 000's	Corporate Banking KD 000's	Islamic Banking KD 000's	Group Centre KD 000's	International KD 000's		
Net interest income	148,694	128,113	354	-	25,385	70,171	372,717
Net income from Islamic financing	-	-	-	25,107	-	-	25,107
Share of results of associates	-	-	-	716	-	12,661	13,377
Net operating income	195,150	165,398	25,580	24,862	112,910	126,030	649,930
Depreciation and amortisation expenses	4,732	509	143	931	8,373	3,071	17,759
Profit for the year	114,524	90,080	13,650	6,022	20,639	63,682	308,597
Total Assets	3,148,826	4,136,216	60,644	1,795,878	2,189,871	5,093,052	16,424,487
Total Liabilities	3,182,758	1,640,999	5,971	1,621,549	2,712,366	4,712,833	13,876,476

2011	Investment Banking and Asset Management						Total KD 000's
	Consumer and Private Banking KD 000's	Corporate Banking KD 000's	Islamic Banking KD 000's	Group Centre KD 000's	International KD 000's		
Net interest income	139,969	142,418	776	28,638	69,171	380,972	
Share of results of associates	-	-	-	3,832	13,279	17,111	
Net operating income	181,769	186,405	24,855	35,401	111,808	540,238	
Depreciation and amortisation expenses	4,990	354	248	8,125	2,244	15,961	
Profit for the year	112,192	134,200	13,872	(8,495)	51,883	303,652	
Total Assets	2,913,366	4,257,988	57,144	1,856,816	4,541,534	13,626,848	
Total Liabilities	2,735,164	1,198,743	5,278	3,057,177	4,293,913	11,290,275	

Geographic information:

The following table shows the geographic distribution of the Group's operating income based on the location of the operating entities.

Net operating income	2012 KD 000's	2011 KD 000's
Kuwait	523,901	431,645
Other Middle East and North Africa	95,149	84,932
Europe	18,203	14,833
Others	12,677	8,828
	649,930	540,238

4 INTEREST INCOME

	2012 KD 000's	2011 KD 000's
Deposits with banks	11,226	13,898
Loans and advances to customers	397,859	413,052
Debt investment securities	71,291	50,143
Other	11,088	13,071
	491,464	490,164

5 INTEREST EXPENSE

	2012 KD 000's	2011 KD 000's
Due to banks and other financial institutions	37,217	37,143
Customer deposits	81,530	72,049
	118,747	109,192

6 NET FEES AND COMMISSIONS

Gross fees and commission income amounted to KD 117,334 thousand (2011: KD 116,372 thousand) and related fees and commission expenses amounted to KD 13,937 thousand (2011: KD 12,294 thousand). Gross fees and commission income includes KD 26,523 thousand relating to trust and fiduciary activities (2011: KD 25,417 thousand).

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7 INVESTMENT INCOME

	2012	2011
	KD 000's	KD 000's
Net realised gains on available for sale investments	27,336	8,869
Net gains from investments carried at fair value through statement of income	3,058	564
Dividend income	3,550	4,543
Gain on fair valuation of previously held equity interest (Note 26)	81,514	-
Net loss from investment properties	(5,641)	-
	109,817	13,976

8 TAXATION

	2012	2011
	KD 000's	KD 000's
Contribution to Kuwait Foundation for the Advancement of Sciences	1,836	2,725
National labour support tax	3,809	6,207
Zakat	1,499	2,449
Taxation on overseas branches and subsidiaries	11,488	5,930
	18,632	17,311

9 EARNINGS PER SHARE

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

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

	2012	2011
	KD 000's	KD 000's
Profit for the year attributable to shareholders of the Bank	305,125	302,406
Weighted average number of shares outstanding during the year (thousands)	4,304,087	4,332,137
Basic and diluted earnings per share	71 fils	70 fils

Earnings per share calculations for 2011 have been adjusted to take account of the bonus shares issued in 2012.

10 CASH AND SHORT TERM FUNDS

	2012	2011
	KD 000's	KD 000's
Cash on hand and on current account with other banks	815,755	581,695
Money at call	176,486	122,490
Balances with the Central Bank of Kuwait	20,084	81,429
Deposits and Murabaha with banks maturing within seven days	598,440	485,638
	1,610,765	1,271,252

11 LOANS, ADVANCES AND ISLAMIC FINANCING TO CUSTOMERS

	Middle East and North Africa KD 000's	North America KD 000's	Europe KD 000's	Asia KD 000's	Others KD 000's	Total KD 000's
2012						
Corporate	6,695,409	113,178	291,920	81,228	131,511	7,313,246
Retail	2,991,845	197	694	-	-	2,992,736

Loans, advances and Islamic financing to customers	9,687,254	113,375	292,614	81,228	131,511	10,305,982
Provision for credit losses						(431,560)
						9,874,422

	Middle East and North Africa KD 000's	North America KD 000's	Europe KD 000's	Asia KD 000's	Others KD 000's	Total KD 000's
2011						
Corporate	5,687,514	83,983	236,828	125,384	45,534	6,179,243
Retail	2,322,065	263	345	-	134	2,322,807

Loans and advances	8,009,579	84,246	237,173	125,384	45,668	8,502,050
Provision for credit losses						(319,824)
						8,182,226

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11 LOANS, ADVANCES AND ISLAMIC FINANCING TO CUSTOMERS (Continued)

Provisions for credit losses on cash facilities are as follows:

	Specific		General		Total	
	2012 KD 000's	2011 KD 000's	2012 KD 000's	2011 KD 000's	2012 KD 000's	2011 KD 000's
Balance at beginning of the year	143,242	110,958	176,582	168,269	319,824	279,227
Amounts written off net of exchange movement	(56,423)	(11,672)	(8)	(68)	(56,431)	(11,740)
Provisions at acquired subsidiary (provisional, see Note 26)	17,923	-	27,147	-	45,070	-
Provided during the year	72,090	43,956	51,007	8,381	123,097	52,337
Balance at end of the year	176,832	143,242	254,728	176,582	431,560	319,824

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

	Corporate		Retail		Total	
	2012 KD 000's	2011 KD 000's	2012 KD 000's	2011 KD 000's	2012 KD 000's	2011 KD 000's
Balance at beginning of the year	93,161	59,653	50,081	51,305	143,242	110,958
Amounts written off net of exchange movements	(47,895)	(11,537)	(8,528)	(135)	(56,423)	(11,672)
Provisions at acquired subsidiary (provisional, see Note 26)	15,119	-	2,804	-	17,923	-
Provided (released) during the year	66,248	45,045	5,842	(1,089)	72,090	43,956
Balance at end of the year	126,633	93,161	50,199	50,081	176,832	143,242

Analysis of total provision charge for credit losses is given below:

	Specific		General		Total	
	2012 KD 000's	2011 KD 000's	2012 KD 000's	2011 KD 000's	2012 KD 000's	2011 KD 000's
Cash facilities	72,090	43,956	51,007	8,381	123,097	52,337
Non cash facilities	777	(300)	409	356	1,186	56
Provision charge for credit losses	72,867	43,656	51,416	8,737	124,283	52,393

The available provision on non-cash facilities of KD 26,077 thousand (2011: KD 23,464 thousand) is included under other liabilities (Note 16).

The impairment provision for finance facilities complies in all material respects with the specific provision requirements of the Central Bank of Kuwait and IFRS. In March 2007, the Central Bank of Kuwait issued a circular amending the basis of making general provisions on facilities changing the minimum rate from 2% to 1% for cash facilities and 0.5% for non cash facilities. The required rates were effective from 1 January 2007 on the net increase in facilities, net of certain restricted categories of collateral, during the reporting period. Pending further directive from the Central Bank of Kuwait, the general provision in excess of 1% for cash facilities and 0.5% for non-cash facilities was retained as general provision.

Non-performing loans, advances and Islamic financing to customers and related specific provisions are as follows:

	2012 KD 000's	2011 KD 000's
Loans, advances and Islamic financing to customers	283,506	131,599
Provisions	151,047	107,390

The fair value of collateral that the Group holds relating to loans, advances and Islamic financing to customers individually determined to be non-performing at 31 December 2012 amounts to KD 141,560 thousand (2011: KD 7,574 thousand). The collateral consists of cash, securities, bank guarantees and properties.

12 FINANCIAL INVESTMENTS

The table below provides the details of the categorisation of financial investments:

2012	Held to maturity KD 000's	Available for sale KD 000's	Fair value through statement of income KD 000's	Total KD 000's
Investment securities				
Debt securities - Government (Non Kuwait)	19,237	746,817	-	766,054
Debt securities - Non Government	6,433	430,831	-	437,264
Equities	-	102,950	33,961	136,911
Other investments	-	158,361	81,260	239,621
	25,670	1,438,959	115,221	1,579,850
Central Bank of Kuwait bonds	614,152	-	-	614,152
Kuwait Government treasury bonds	356,211	-	-	356,211
	996,033	1,438,959	115,221	2,550,213

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12 FINANCIAL INVESTMENTS (Continued)

2011	Held to maturity KD 000's	Available for sale KD 000's	Fair value through statement of income KD 000's	Total KD 000's
Investment Securities				
Debt securities - Government (Non Kuwait)	29,272	844,654	-	873,926
Debt securities - Non Government	10,500	393,989	-	404,489
Equities	-	73,303	-	73,303
Other investments	-	90,531	60,786	151,317
	39,772	1,402,477	60,786	1,503,035
Central Bank of Kuwait bonds	454,378	-	-	454,378
Kuwait Government treasury bonds	396,304	-	-	396,304
	890,454	1,402,477	60,786	2,353,717

All unquoted available for sale equities are recorded at fair value except for investments with a carrying value of KD 4,908 thousand (2011: KD 5,729 thousand), which are recorded at cost since fair value cannot be reliably estimated.

Debt securities include KD 57,917 thousand (2011: KD 133,679 thousand) at variable rates of interest and KD 1,145,401 thousand (2011: KD 1,144,736 thousand) at fixed rates of interest.

An impairment loss of KD 14,735 thousand (2011: KD 4,900 thousand) has been made against investments classified as available for sale on which there has been a significant or prolonged decline in value.

13 INVESTMENT IN ASSOCIATES

Associates of the Group:

	Carrying value	
	2012 KD 000's	2011 KD 000's
Boubyan Bank K.S.C.	-	370,597
International Bank of Qatar Q.S.C.	132,016	128,832
Turkish Bank A.S.	31,022	28,403
Bank Syariah Muamalat Indonesia T.B.K.	40,946	-
United Capital Bank	5,294	-
Others	3,897	146
	213,175	527,978

The Group obtained control over Boubyan Bank K.S.C. during the year (Note 26) and reclassified the investment from associate to subsidiary.

Name of major associates	Country of incorporation	% Effective ownership	
		2012	2011
International Bank of Qatar Q.S.C.	Qatar	30.0	30.0
Turkish Bank A.S.	Turkey	38.1	40.0
Bank Syariah Muamalat Indonesia T.B.K.	Indonesia	25.0	-
United Capital Bank	Sudan	21.7	-

Summarised financial information of all the associates is as follows:

	2012 KD 000's	2011 KD 000's
Assets	3,878,940	3,744,757
Liabilities	3,417,564	3,156,721
Contingent liabilities	916,795	639,860
Net operating income	146,609	121,549
Results for the year	54,208	52,182

14 GOODWILL AND OTHER INTANGIBLE ASSETS

	Goodwill KD 000's	Intangible assets KD 000's	Total KD 000's
Cost			
At 1 January 2012	165,873	65,877	231,750
Acquisition of a subsidiary (Note 26)	429,930	-	429,930
Exchange adjustments	(5,427)	(1,626)	(7,053)
At 31 December 2012	590,376	64,251	654,627
Accumulated amortisation			
At 1 January 2012	-	16,247	16,247
Charge for the year	-	4,053	4,053
Exchange adjustments	-	(675)	(675)
At 31 December 2012	-	19,625	19,625
Net book value			
At 31 December 2012	590,376	44,626	635,002

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14 GOODWILL AND OTHER INTANGIBLE ASSETS (Continued)

	Goodwill KD 000's	Intangible assets KD 000's	Total KD 000's
Cost			
At 1 January 2011	173,651	67,703	241,354
Additions	-	464	464
Exchange adjustments	(7,778)	(2,290)	(10,068)
At 31 December 2011	165,873	65,877	231,750
Accumulated amortisation			
At 1 January 2011	-	12,768	12,768
Charge for the year	-	4,081	4,081
Exchange adjustments	-	(602)	(602)
At 31 December 2011	-	16,247	16,247
Net book value			
At 31 December 2011	165,873	49,630	215,503

Net book value of goodwill as at 31 December 2012 includes KD 429,930 thousand in respect of Boubyan Bank K.S.C, the newly acquired subsidiary in Kuwait, KD 157,678 thousand (2011: KD 163,131 thousand) in respect of Al Watany Bank of Egypt S.A.E. (AWB), a subsidiary in Egypt and KD 2,768 thousand (2011: KD 2,742 thousand) in respect of Credit Bank of Iraq S.A, a subsidiary in Iraq.

Net book value of intangible assets as at 31 December 2012 includes Brokerage licenses amounting to KD 18,001 thousand (2011: KD 18,016 thousand) and are considered as intangible assets with indefinite useful life. Other intangible assets amounting to KD 26,625 thousand are in respect of AWB (2011: KD 31,614 thousand) and are amortised over a period of 5 to 12 years.

Impairment testing for goodwill and intangible assets with indefinite useful life

The carrying value of goodwill and intangible assets with indefinite useful life are tested for impairment on an annual basis (or more frequently if evidence exists that goodwill or intangible assets might be impaired) by estimating the recoverable amount of the cash generating unit (CGU) to which these items are allocated using value-in-use calculations unless fair value based on an active market price is higher than the carrying value of the CGU. The value in use calculations use pre-tax cash flow projections based on financial budgets approved by management over a five years period and a relevant terminal growth rate. These cash flows were then discounted to derive a net present value which is compared to the carrying value. The discount rate used is pre-tax and reflects specific risks relating to the relevant cash generating unit.

A discount rate of 9% (2011: 8.25%) is used to estimate the recoverable amount of the Brokerage license in Kuwait. The goodwill in respect of AWB is allocated to a single CGU which consists of identifiable net assets including intangible assets of AWB. A discount rate of 14.2% (2011: 13.3%) is used to estimate the recoverable amount of this cash generating unit. A terminal growth rate of 5% (2011: 5%) is applied in all cases. The Group has also performed a sensitivity analysis by varying these input factors by a reasonable possible margin.

Based on such analysis, there are no indications that goodwill or intangible assets are impaired.

15 OTHER ASSETS

	2012 KD 000's	2011 KD 000's
Interest receivable	36,589	37,499
Sundry debtors and prepayments	39,412	33,683
Investment properties	17,904	-
Property acquired on settlement of debts	21,898	4,121
Others	30,204	39,151
	146,007	114,454

16 OTHER LIABILITIES

	2012 KD 000's	2011 KD 000's
Interest payable	29,214	27,377
Income received in advance	17,223	19,809
Taxation	14,379	14,059
Provision on non-cash facilities (Note 11)	26,077	23,464
Accrued expenses	26,344	16,855
Staff payables	23,628	20,399
Others	76,874	58,781
	213,739	180,744

17 SHARE CAPITAL AND RESERVES

a) Share capital

	2012 KD 000's	2011 KD 000's
Authorised, issued and fully paid:		
4,353,497,625 (2011 : 3,957,725,114) shares of KD 0.100 each	435,349	395,772

The movement in ordinary shares in issue during the year was as follows:

	2012	2011
Number of shares in issue as at 1 January	3,957,725,114	3,597,931,922
Bonus issue	395,772,511	359,793,192
Number of shares in issue as at 31 December	4,353,497,625	3,957,725,114

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17 SHARE CAPITAL AND RESERVES (Continued)

b) Statutory reserve

The Board of Directors recommended a transfer of KD 19,789 thousand (2011: KD 17,989 thousand) to the statutory reserve. This is in compliance with the Bank's Articles of Association and the Law of Commercial Companies which require a minimum of 10% of profit for the year attributable to the shareholders of the Bank before KFAS, NLST and Zakat to be transferred to a non distributable statutory reserve until such time as this reserve equals 50% of the Bank's issued capital. Accordingly the transfer to statutory reserve, which is less than 10% of the profit for the year, is that amount required to make the statutory reserve 50% of the Bank's issued capital.

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

c) Share premium account

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

d) Treasury shares and Treasury share reserve

The Bank held the following treasury shares at the year end:

	2012	2011
Number of treasury shares	80,527,958	30,423,135
Treasury shares as a percentage of total shares in issue	1.8%	0.8%
Cost of treasury shares (KD thousand)	79,171	33,415
Market value of treasury shares (KD thousand)	77,307	34,074

Movement in treasury shares was as follows:

	No. of shares	
	2012	2011
Balance as at 1 January	30,423,135	10,294,498
Purchases	56,186,226	21,000,000
Bonus issue	2,819,167	875,107
Sales	(8,900,570)	(1,746,470)
Balance as at 31 December	80,527,958	30,423,135

The balance in the treasury share reserve account is not available for distribution.

e) Other reserves

KD 000's

	General reserve	Retained earnings	Foreign currency translation reserve	Cumulative changes in fair values	Share based payment reserve	Proposed cash dividend	Total other reserves
At 1 January 2011	117,058	644,377	(11,578)	30,561	8,297	143,505	932,220
Profit for the year	-	302,406	-	-	-	-	302,406
Other comprehensive loss	-	-	(21,454)	(7,204)	-	-	(28,658)
Total comprehensive income (loss)	-	302,406	(21,454)	(7,204)	-	-	273,748
Transfer to statutory reserve (Note 17b)	-	(17,989)	-	-	-	-	(17,989)
Dividends paid	-	-	-	-	-	(143,567)	(143,567)
Dividends on treasury shares sold	-	(62)	-	-	-	62	-
Proposed bonus shares (Note 18)	-	(39,577)	-	-	-	-	(39,577)
Proposed cash dividend 40fils per share (Note 18)	-	(157,092)	-	-	-	157,092	-
Share based payment (Note 19)	-	-	-	-	2,172	-	2,172
Acquisition of non-controlling interests	-	(2,462)	-	-	-	-	(2,462)
At 31 December 2011	117,058	729,601	(33,032)	23,357	10,469	157,092	1,004,545
Profit for the year	-	305,125	-	-	-	-	305,125
Other comprehensive (loss) income	-	-	(2,490)	3,204	-	-	714
Total comprehensive income (loss)	-	305,125	(2,490)	3,204	-	-	305,839
Transfer to statutory reserve (Note 17b)	-	(19,789)	-	-	-	-	(19,789)
Dividends paid	-	-	-	-	-	(157,181)	(157,181)
Dividends on treasury shares sold	-	(89)	-	-	-	89	-
Proposed bonus shares (Note 18)	-	(21,768)	-	-	-	-	(21,768)
Proposed cash dividend 30fils per share (Note 18)	-	(128,189)	-	-	-	128,189	-
Share based payment (Note 19)	-	-	-	-	1,844	-	1,844
Acquisition of non-controlling interests (Note 21)	-	(393)	-	-	-	-	(393)
At 31 December 2012	117,058	864,498	(35,522)	26,561	12,313	128,189	1,113,097

The general reserve was created in accordance with Bank's Articles of Association and is freely distributable.

The foreign currency translation reserve includes the exchange differences on conversion of results and financial position of all group entities including goodwill, intangible assets and any fair value adjustments to the carrying value of assets and liabilities from their functional currency to the presentation currency.

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18 PROPOSED DIVIDEND

The Board of Directors recommended distribution of a cash dividend of 30 fils per share (2011: 40 fils per share) and bonus shares of 5% (2011: 10%) on outstanding shares as at 31 December 2012. The proposed dividend, if approved, shall be payable to the shareholders registered in the Bank's records as of the date of the annual general assembly meeting.

19 SHARE BASED PAYMENT

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

The fair value of options granted during the year as determined using the Black-Scholes valuation model was KD 0.914 (2011: KD 1.232). The significant inputs into the model were a share price of KD 1.120 (2011: KD 1.440) at the grant date, an exercise price of 100 fils as shown above, a standard deviation of expected share price returns of 45.6 % (2011: 50.8%), option life disclosed above and annual risk free interest rate of 2.50% (2011: 2.50%). The volatility measured at the standard deviation of expected share price returns is based on statistical analysis of daily share prices over the last three years.

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

	2012	2011
	No. of share options	No. of share options
Outstanding at 1 January	7,132,651	7,226,062
Granted during the year	1,666,920	2,291,174
Exercised during the year	(2,510,570)	(1,746,470)
Lapsed during the year	(597,811)	(638,115)
Outstanding at 31 December	5,691,190	7,132,651

The expense accrued on account of share based compensation plans for the year amounts to KD 1,868 thousand (2011: KD 2,172 thousand) and is included under staff expenses.

20 FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

The fair value of investment securities, quoted in an active market (stock exchanges and actively traded funds) amounts to KD 590,987 thousand (2011: KD 701,565 thousand) for debt securities and KD 187,442 thousand (2011: KD 146,479 thousand) for equities and other investments. Investment securities, which are tradable over the counter and / or are valued by using a significant input of observable market data amounts to KD 541,131 thousand (2011: KD 481,602 thousand) for debt securities and KD 88,680 thousand (2011: KD 9,495 thousand) for equities and other investments. Debt securities under this category mainly include sovereign debt instruments and corporate bonds in the MENA region.

Investment securities, for which a significant input of the valuation is not based on observable market data amounts to KD 45,530 thousand (2011: KD 55,476 thousand) for debt securities and KD 95,502 thousand (2011: KD 62,917 thousand) for equities and other investments. The table below analyses the movement in these investment securities and the income (interest, dividend and realised gain) generated during the year.

	At 1 January 2012 KD 000's	Change in fair value KD 000's	Additions KD 000's	Sale/ redemption KD 000's	Exchange rate movements KD 000's	At 31 December 2012 KD 000's	Net gains in the consolidated statement of income KD 000's
Debt securities	55,476	-	30,406	(40,852)	500	45,530	1,455
Equities and other investments	62,917	5,358	31,118	(4,012)	121	95,502	3,791
	118,393	5,358	61,524	(44,864)	621	141,032	5,246

	At 1 January 2011 KD 000's	Change in fair value KD 000's	Additions KD 000's	Sale/ redemption KD 000's	Exchange rate movements KD 000's	At 31 December 2011 KD 000's	Net gains in the consolidated statement of income KD 000's
Debt securities	45,787	-	15,576	(5,190)	(697)	55,476	783
Equities and other investments	66,194	100	3,918	(6,994)	(301)	62,917	6,148
	111,981	100	19,494	(12,184)	(998)	118,393	6,931

The positive and negative fair values of interest rate swaps and forward foreign exchange contracts, which are valued using significant inputs of observable market data, amount to KD 12,529 thousand (2011: KD 9,150 thousand) and KD 17,430 thousand (2011: KD 16,802 thousand) respectively (refer note 23 for details).

Other financial assets and liabilities are carried at amortized cost and the carrying values are not materially different from their fair values as most of these assets and liabilities are of short term maturities or are repriced immediately based on market movement in interest rates.

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21 SUBSIDIARIES

Principal operating subsidiaries:

Name of entities	Country of incorporation	Principal business	% Effective ownership	
			2012	2011
National Bank of Kuwait (International) plc	United Kingdom	Banking	100.0	100.0
NBK Banque Privée (Suisse) S.A.	Switzerland	Investment management	100.0	100.0
National Bank of Kuwait (Lebanon) S.A.L.	Lebanon	Banking	85.5	85.5
National Investors Group Holdings Limited	Cayman Islands	Investment management	100.0	100.0
Credit Bank of Iraq S.A.	Iraq	Banking	81.0	80.1
Watani Investment Company K.S.C.(Closed)	Kuwait	Investment Company	99.9	99.9
Watani Financial Brokerage Company K.S.C. (Closed)	Kuwait	Brokerage	86.7	86.7
Al Watany Bank of Egypt S.A.E.	Egypt	Banking	98.5	98.5
Boubyan Bank K.S.C.	Kuwait	Islamic Banking	58.4	47.3

At 31 December 2012, 38.1 % (2011: 38.1%) of the Group's interest in National Bank of Kuwait (Lebanon) S.A.L. was held by an intermediate holding company, NBK Holding (Liban) S.A.L.

Boubyan Bank K.S.C. became subsidiary of the Group during the year (Note 26).

The Group acquired an additional 0.9% equity interest in Credit Bank of Iraq S.A. during the year for KD 733 thousand. The difference between the cost of acquisition and share of net assets acquired amounting to KD 393 thousand is charged to retained earnings.

The Bank also holds voting capital in certain special purpose entities which have been established to manage funds and fiduciary assets on behalf of the Bank's customers. The Bank does not have a beneficial interest in the underlying assets of these companies. Information about the Group's fund management activities is set out in note 29.

22 COMMITMENTS AND CONTINGENT LIABILITIES

	2012	2011
	KD 000's	KD 000's
Commitments on behalf of customers for which there are corresponding liabilities by the customers concerned:		
Acceptances	85,689	99,555
Letters of credit	307,416	281,398
Guarantees	2,067,690	1,685,644
	2,460,795	2,066,597

Irrevocable commitments to extend credit amount to KD 318,110 thousand (31 December 2011: KD 184,196 thousand). This represents commitments to extend credit which is irrevocable over the life of the facility or is revocable only in response to a material adverse change.

In the normal course of business the Group has exposure to various indirect credit commitments which, though not reflected in the consolidated statement of financial position, are subject to normal credit standards, financial controls and monitoring procedures.

These credit commitments do not necessarily represent future cash requirements, since many of these commitments will expire or terminate without being funded. Credit losses, if any, which may result from exposure to such commitments are not expected to be significant.

23 INTEREST RATE SWAPS AND FORWARD FOREIGN EXCHANGE CONTRACTS

Interest rate swaps and forward foreign exchange contracts are financial instruments that derive their value by referring to interest rates and foreign exchange rates respectively. 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.

Interest rate swaps and forward foreign exchange contracts are carried at fair value in the consolidated statement of financial position. 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 statement of financial position date. Credit risk in respect of interest rate swaps and forward foreign exchange contracts are limited to the positive fair value of the instruments. Negative fair value represents the cost to the Group's counter parties of replacing all their transactions with the Group.

The Group deals in interest rate swaps to manage its interest rate risk on interest bearing asset and liabilities and to provide interest rate risk management solutions to customers. Similarly the Group deals in forward foreign exchange contracts for customers and to manage its foreign currency positions and cash flows.

Interest rate swaps used to hedge the change in fair value of the Group's financial assets and liabilities and which qualify as effective hedging instruments are shown as interest rate swaps held as fair value hedges. Other interest rate swaps and forward foreign exchange contracts are carried out for customers or used for hedging purpose but do not meet the qualifying criteria for hedge accounting. The risk exposures on account of interest rate swaps and forward foreign exchange contracts for customers are covered by entering into similar transactions with counter parties or by other risk mitigating transactions.

Interest rate swaps

Interest rate swaps are contractual agreements between two counter-parties to exchange interest payments on a defined principal amount for a fixed period of time.

Forward foreign exchange

Forward foreign exchange contracts are agreements to buy or sell currencies at a specified rate and at a future date.

The fair value of interest rate swaps and forward foreign exchange contracts included in the financial records, together with their notional amounts is summarised as follows:

	2012			2011		
	Positive fair value KD 000's	Negative fair value KD 000's	Notional KD 000's	Positive fair value KD 000's	Negative fair value KD 000's	Notional KD 000's
Interest rate swaps (held as fair value hedges)	21	14,348	136,480	73	14,254	156,684
Interest rate swaps (others)	-	-	-	1,678	123	58,506
Forward foreign exchange	12,508	3,082	895,735	7,399	2,425	1,039,998
	12,529	17,430	1,032,215	9,150	16,802	1,255,188

The net fair value of interest rate swaps held as fair value hedges as at 31 December 2012 is negative KD 14,327 thousand (2011: negative KD 14,181 thousand). Gain on the hedged fixed income financial assets amounted to KD 15,131 thousand (2011: KD 12,248 thousand).

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24 RELATED PARTY TRANSACTIONS

Certain related parties (major shareholders, directors and officers of the Bank, companies which they control or over which they exert significant influence, and entities associated with the Group) were customers of the Bank and its subsidiaries in the ordinary course of business. Such transactions were made on substantially the same terms, including interest rates and collateral, as those prevailing at the same time for comparable transactions with unrelated parties and did not involve more than a normal amount of risk.

In accordance with Central Bank of Kuwait regulations regarding lending to Board Members and their related parties such lending is secured by tangible collateral.

Details of the interests of Board Members, Executive Officers and balances with associates are as follows:

	Number of Board Members or Executive Officers		Number of related parties		2012 KD 000's	2011 KD 000's
	2012	2011	2012	2011		
Board Members						
Loans (secured)	4	5	12	14	204,469	235,723
Contingent liabilities	1	2	12	13	13,446	14,787
Credit cards	8	7	2	2	28	89
Deposits	9	9	14	15	22,726	70,166
Collateral against credit facilities	4	5	15	17	362,293	390,751
Interest and fee income					7,607	7,612
Interest expense					360	1,012
Executive Officers						
Loans	9	8	-	-	460	792
Contingent liabilities	2	1	-	-	6	6
Credit cards	5	5	-	-	6	30
Deposits	16	16	-	-	1,405	1,854
Interest and fee income					2	6
Interest expense					17	15
Associates						
Placements					195,268	220,721
Acceptances					544	38,834

25 KEY MANAGEMENT COMPENSATION

Details of compensation for key management, including Executive Officers, comprise the following:

	2012 KD 000's	2011 KD 000's
Salaries and other short term benefits	13,631	12,591
Post-employment benefits	1,288	957
Share based compensation	1,138	1,307
	16,057	14,855

The Board of Directors does not receive any emoluments in the form of fees, salaries or bonuses for their services rendered to the Bank.

26 BUSINESS COMBINATION

During the year the Bank acquired an additional equity interest of 11.1% in Boubyan Bank K.S.C. (previously classified as 'investment in associate') increasing the effective equity interest to 58.4%. Having obtained control, the Bank reclassified the investment in Boubyan Bank K.S.C. from associate to subsidiary and consolidated the financial statements of Boubyan Bank K.S.C. from 31 July 2012 (acquisition date). Boubyan Bank K.S.C. is incorporated in the State of Kuwait and is engaged in providing Islamic banking services.

As the business combination was achieved in stages, in accordance with IFRS 3: Business Combinations, the Bank re-measured its previously held equity interest in Boubyan Bank K.S.C. at the acquisition date fair value and recognised the resulting gain in the consolidated statement of income. The acquisition date fair value amounted to KD 453,023 thousand and the gain on remeasurement amounted to KD 81,514 thousand which is included under 'investment income' in the consolidated statement of income (Note 7).

The acquisition of Boubyan Bank K.S.C. has been accounted based on provisional fair values of identifiable assets and liabilities on the date of acquisition and the management is in the process of determining the fair values of assets and liabilities acquired. The consideration paid, the provisional fair values of the assets and liabilities recognised at the date of acquisition and the non-controlling interest's proportionate share in the recognised amounts of the acquiree's identifiable net assets are summarised as follows:

	KD 000's
Assets	
Cash and short term funds	170,985
Deposits with banks	185,916
Islamic financing to customers	1,181,480
Investment securities	145,812
Investment properties	21,124
Investment in associates	8,789
Land, premises and equipment	8,104
Other assets	21,798
	1,744,008
Liabilities	
Due to banks and other financial institutions	495,805
Depositors accounts	959,657
Other liabilities	38,075
	1,493,537

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26 BUSINESS COMBINATION (Continued)

Net assets	250,471
Non-controlling interests	(2,572)
Provisional fair value of net assets acquired by the Group	247,899
Consideration transferred	121,654
Non-controlling interest in the acquiree	103,152
Fair value of acquirer's previously held equity interest	453,023
	677,829
Less: net assets acquired by the Group	247,899
Provisional goodwill	429,930
Cash and cash equivalents in subsidiary acquired	170,985
Consideration settled in cash	(121,654)
Cash inflow on acquisition	49,331

The consolidated statement of income of the Group for the year includes operating income of KD 24,758 thousand and profit attributable to the equity holders of the Bank amounting to KD 2,879 thousand of Boubyan Bank K.S.C.

Had the acquisition of Boubyan Bank K.S.C. taken place at the beginning of the year, the operating income of the Group for the year would have been higher by KD 32,518 thousand amounting to a total of KD 682,448 thousand and the profit attributable to the equity holders of the Bank would have been higher by KD 25 thousand amounting to a total of KD 305,150 thousand.

27 RISK MANAGEMENT

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

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

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

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

As part of its overall risk management, the Group uses interest rate swaps, forward foreign exchange contracts and other instruments to manage exposures resulting from changes in interest rates, foreign exchange, equity risks, credit risks and exposures arising from forecast transactions. Collaterals are used to reduce the Group's credit risks.

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

27.1 CREDIT RISK

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

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

Credit limits are established for all customers after a careful assessment of their creditworthiness. Standing procedures, outlined in the Group's Credit Policy Manual, require that all credit proposals be subjected to detailed screening by the domestic or international credit control divisions pending submission to the appropriate credit committee. Whenever necessary, all loans are secured by acceptable forms of collateral to mitigate the related credit risks.

In accordance with the instructions of the Central Bank of Kuwait dated 18 December 1996, setting out the rules and regulations regarding the classification of credit facilities, the Group has formed an internal committee comprising competent professional staff and having as its purpose the study and evaluation of the existing credit facilities of each customer of the Group. This committee is required to identify any abnormal situations and difficulties associated with a customer's position which might cause the debt to be classified as irregular, and to determine an appropriate provisioning level. The committee, which meets regularly throughout the year, also studies the positions of those customers whose irregular balances exceed 25% of their total debt, in order to determine whether further provisions are required.

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

27.1. 1 MAXIMUM EXPOSURE TO CREDIT RISK

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

	2012		2011	
	Gross exposure KD 000's	Net exposure KD 000's	Gross exposure KD 000's	Net exposure KD 000's
Loans, advances and Islamic financing to customers	9,874,422	6,496,281	8,182,226	5,416,971
Contingent liabilities	2,460,795	2,356,279	2,066,597	1,978,798

Collateral and other credit enhancements

The amount, type and valuation of collateral are based on guidelines specified in the risk management framework. The main types of collateral accepted includes real estate, quoted shares, cash collateral and bank guarantees. The revaluation and custody of collaterals are performed independent of the business units.

27.1. 2 RISK CONCENTRATION OF THE MAXIMUM EXPOSURE TO CREDIT RISK

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

Credit risk can also arise due to a significant concentration of Group's assets to any single counterparty. This risk is managed by diversification of the portfolio. The 20 largest loans, advances and Islamic financing to customers outstanding as a percentage of gross loans, advances and Islamic financing to customers as at 31 December 2012 is 19% (2011: 22%).

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27 RISK MANAGEMENT (Continued)

27.1 CREDIT RISK (Continued)

27.1. 2 RISK CONCENTRATION OF THE MAXIMUM EXPOSURE TO CREDIT RISK (Continued)

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

Geographic region	2012					Total KD 000's
	Middle East and North Africa KD 000's	North America KD 000's	Europe KD 000's	Asia KD 000's	Others KD 000's	
Cash and deposits with banks	1,932,651	545,488	288,612	47,432	-	2,814,183
Central Bank of Kuwait bonds	614,152	-	-	-	-	614,152
Kuwait Government treasury bonds	356,211	-	-	-	-	356,211
Loans, advances and Islamic financing to customers	9,261,917	111,924	289,388	80,720	130,473	9,874,422
Held to maturity investments	16,922	-	-	8,748	-	25,670
Available for sale investments	1,003,684	19,312	92,771	61,881	-	1,177,648
Other assets	99,392	1,271	4,692	850	-	106,205
	13,284,929	677,995	675,463	199,631	130,473	14,968,491
Commitments and contingent liabilities (Note 22)	1,699,403	180,859	391,990	504,553	2,100	2,778,905
	14,984,332	858,854	1,067,453	704,184	132,573	17,747,396

Geographic region	2011					Total KD 000's
	Middle East and North Africa KD 000's	North America KD 000's	Europe KD 000's	Asia KD 000's	Others KD 000's	
Cash and deposits with banks	1,509,495	331,016	193,558	24,700	-	2,058,769
Central Bank of Kuwait bonds	454,378	-	-	-	-	454,378
Kuwait Government treasury bonds	396,304	-	-	-	-	396,304
Loans and advances to customers	7,696,805	83,070	234,326	122,763	45,262	8,182,226
Held to maturity investments	25,018	-	1,914	12,840	-	39,772
Available for sale investments	867,333	174,435	105,247	91,628	-	1,238,643
Other assets	101,252	606	7,755	1,232	3,609	114,454
	11,050,585	589,127	542,800	253,163	48,871	12,484,546
Commitments and contingent liabilities (Note 22)	1,368,089	161,397	257,015	438,216	26,076	2,250,793
	12,418,674	750,524	799,815	691,379	74,947	14,735,339

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

Industry sector	2012	2011
	KD 000's	KD 000's
Trading	1,689,277	1,385,730
Manufacturing	1,068,342	898,548
Banks and other financial institutions	5,223,629	4,027,996
Construction	990,787	813,124
Real Estate	1,974,608	1,407,465
Retail	2,906,121	2,243,103
Government	1,292,891	1,400,200
Others	2,601,741	2,559,173
	17,747,396	14,735,339

27.1. 3 CREDIT QUALITY PER CLASS OF FINANCIAL ASSETS

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

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

2012	Neither past due nor impaired		Past due or impaired KD 000's	Total KD 000's
	High KD 000's	Standard KD 000's		
Deposits and Murabaha with banks maturing within seven days	598,440	-	-	598,440
Central Bank of Kuwait bonds	614,152	-	-	614,152
Kuwait Government treasury bonds	356,211	-	-	356,211
Deposits with banks	1,141,648	61,770	-	1,203,418
Loans, advances and Islamic financing to customers	8,228,225	1,738,183	339,574	10,305,982
Held to maturity investments	8,748	16,922	-	25,670
Available for sale investments	743,117	434,531	-	1,177,648
	11,690,541	2,251,406	339,574	14,281,521

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27 RISK MANAGEMENT (Continued)

27.1 CREDIT RISK (Continued)

27.1.3 CREDIT QUALITY PER CLASS OF FINANCIAL ASSETS (Continued)

	Neither past due nor impaired		Past due or impaired KD 000's	Total KD 000's
	High KD 000's	Standard KD 000's		
2011				
Deposits with banks maturing within seven days	485,638	-	-	485,638
Central Bank of Kuwait bonds	454,378	-	-	454,378
Kuwait Government treasury bonds	396,304	-	-	396,304
Deposits with banks	574,920	212,597	-	787,517
Loans and advances to customers	6,856,202	1,322,056	323,792	8,502,050
Held to maturity investments	14,754	25,018	-	39,772
Available for sale investments	847,561	391,082	-	1,238,643
	9,629,757	1,950,753	323,792	11,904,302

27.1.4 AGEING ANALYSIS OF PAST DUE OR IMPAIRED LOANS, ADVANCES AND ISLAMIC FINANCING TO CUSTOMERS

	Corporate		Retail		Total	
	Past due and not impaired KD 000's	Past due and impaired KD 000's	Past due and not impaired KD 000's	Past due and impaired KD 000's	Past due and not impaired KD 000's	Past due and impaired KD 000's
2012						
Up to 30 days	12,789	-	21,467	-	34,256	-
31 - 60 days	2,049	-	9,655	-	11,704	-
61 - 90 days	8,766	-	1,342	-	10,108	-
91-180 days	-	16,842	-	11,375	-	28,217
More than 180 days	-	206,230	-	49,059	-	255,289
	23,604	223,072	32,464	60,434	56,068	283,506

2011						
Up to 30 days	3,686	-	15,827	-	19,513	-
31 - 60 days	194	-	7,024	-	7,218	-
61 - 90 days	165,139	-	323	-	165,462	-
91-180 days	-	50	-	10,670	-	10,720
More than 180 days	-	72,426	-	48,453	-	120,879
	169,019	72,476	23,174	59,123	192,193	131,599

Of the aggregate amount of gross past due or impaired credit facilities to customers, the fair value of collateral that the Group held as at 31 December 2012 was KD 154,869 thousand (2011: KD 158,979 thousand).

27.2 LIQUIDITY RISK

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

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

	Up to 3 months KD 000's	3 to 12 months KD 000's	Over 1 year KD 000's	Total KD 000's
2012				
Assets				
Cash and deposits with banks	2,730,473	79,491	4,219	2,814,183
Central Bank of Kuwait bonds	444,626	169,526	-	614,152
Kuwait Government treasury bonds	93,184	162,454	100,573	356,211
Loans, advances and Islamic financing to customers	3,924,764	2,059,483	3,890,175	9,874,422
Held to maturity investments	19,237	-	6,433	25,670
Available for sale investments	175,377	280,722	982,860	1,438,959
Investments carried at fair value through statement of income	115,221	-	-	115,221
Investment in associates	-	-	213,175	213,175
Land, premises and equipment	-	-	191,485	191,485
Goodwill and other intangible assets	-	-	635,002	635,002
Other assets	84,166	22,039	39,802	146,007
	7,587,048	2,773,715	6,063,724	16,424,487
Liabilities and equity				
Due to banks and other financial institutions	3,330,196	732,124	92,663	4,154,983
Customer deposits	7,954,248	1,259,383	294,123	9,507,754
Other liabilities	164,035	-	49,704	213,739
Share capital and reserves	-	-	2,298,326	2,298,326
Proposed cash dividend	128,189	-	-	128,189
Non-controlling interests	-	-	121,496	121,496
	11,576,668	1,991,507	2,856,312	16,424,487

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27 RISK MANAGEMENT (Continued)

27.2 LIQUIDITY RISK (Continued)

	Up to 3 months KD 000's	3 to 12 months KD 000's	Over 1 year KD 000's	Total KD 000's
2011				
Assets				
Cash and deposits with banks	1,996,409	1,625	60,735	2,058,769
Central Bank of Kuwait bonds	404,619	49,759	-	454,378
Kuwait Government treasury bonds	100,664	275,600	20,040	396,304
Loans and advances to customers	2,898,086	1,813,781	3,470,359	8,182,226
Held to maturity investments	33,350	4,508	1,914	39,772
Available for sale investments	364,648	263,318	774,511	1,402,477
Investments carried at fair value through statement of income	60,786	-	-	60,786
Investment in associates	-	-	527,978	527,978
Land, premises and equipment	-	-	174,201	174,201
Goodwill and other intangible assets	-	-	215,503	215,503
Other assets	92,158	18,175	4,121	114,454
	5,950,720	2,426,766	5,249,362	13,626,848
Liabilities and equity				
Due to banks and other financial institutions	3,110,628	768,255	431,456	4,310,339
Customer deposits	6,152,002	449,559	197,631	6,799,192
Other liabilities	136,881	-	43,863	180,744
Share capital and reserves	-	-	2,167,516	2,167,516
Proposed cash dividend	157,092	-	-	157,092
Non-controlling interests	-	-	11,965	11,965
	9,556,603	1,217,814	2,852,431	13,626,848

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

	Up to 3 months KD 000's	3 to 12 months KD 000's	Over 1 year KD 000's	Total KD 000's
2012				
Financial Liabilities				
Due to banks and other financial institutions	3,333,216	737,174	96,564	4,166,954
Customer deposits	7,977,762	1,276,632	325,485	9,579,879
	11,310,978	2,013,806	422,049	13,746,833
Contingent liabilities and commitments				
Contingent liabilities	758,184	757,310	945,301	2,460,795
Irrevocable commitments	25,947	190,189	101,974	318,110
	784,131	947,499	1,047,275	2,778,905
Forward foreign exchange contracts settled on a gross basis				
Contractual amounts payable	747,882	141,532	3,758	893,172
Contractual amounts receivable	739,415	139,394	3,758	882,567

	Up to 3 months KD 000's	3 to 12 months KD 000's	Over 1 year KD 000's	Total KD 000's
2011				
Financial Liabilities				
Due to banks and other financial institutions	3,112,506	775,248	438,542	4,326,296
Customer deposits	6,155,684	453,831	222,362	6,831,877
	9,268,190	1,229,079	660,904	11,158,173
Contingent liabilities and commitments				
Contingent liabilities	617,074	696,232	753,291	2,066,597
Irrevocable commitments	25,329	84,049	74,818	184,196
	642,403	780,281	828,109	2,250,793
Forward foreign exchange contracts settled on a gross basis				
Contractual amounts payable	913,696	117,898	4,392	1,035,986
Contractual amounts receivable	914,285	116,421	4,391	1,035,097

27.3 MARKET RISK

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

27.3.1 INTEREST RATE RISK

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

The Group is not excessively exposed to interest rate risk as its assets and liabilities are repriced regularly and most exposures arising on medium term fixed rate lending or fixed rate borrowing are covered by interest rate swaps. Furthermore, the reverse cumulative interest rate gap is carefully monitored on a daily basis and adjusted where necessary to reflect changing market conditions.

Interest rate sensitivity

Interest rate sensitivity of profit measures the effect of the assumed changes in interest rates on the net interest income for one year, based on the interest bearing financial assets and financial liabilities held at the year end. This includes the effect of hedging instruments but excludes loan commitments. The sensitivity of equity is the impact arising from changes in interest rate on fair value of available for sale investments. Sensitivity to interest rate movements will be on a symmetric basis as financial instruments giving rise to non-symmetric movements are not significant.

Based on the Group's financial assets and financial liabilities held at the year end, an assumed 25 basis points increase in interest rate, with all other variables held constant, would impact the Group's profit and equity as follows:

Currency	Movement in Basis points	2012		2011	
		Effect on profit KD 000's	Effect on equity KD 000's	Effect on profit KD 000's	Effect on equity KD 000's
KWD	+25	4,624	-	5,337	-
USD	+25	(1,041)	(2,867)	153	(2,272)
EUR	+25	(186)	(19)	152	(106)
GBP	+25	(51)	-	(74)	-
EGP	+25	97	(325)	71	(339)

Notes to the Consolidated Financial Statements

31 December 2012

27 RISK MANAGEMENT (Continued)

27.3 MARKET RISK (Continued)

27.3.2 FOREIGN EXCHANGE RISK

Foreign exchange risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates.

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

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

Currency	% Change in currency rate	2012		2011	
		Effect on profit KD 000's	Effect on equity KD 000's	Effect on profit KD 000's	Effect on equity KD 000's
USD	+5	1,586	1,003	2,160	793
GBP	+5	(711)	-	103	-
EUR	+5	(454)	-	(1,978)	-
EGP	+5	228	11,846	-	12,460
QAR	+5	-	5,538	-	5,479
TRY	+5	-	1,521	-	1,402
IDR	+5	-	2,043	-	-
Other	+5	119	3,120	499	2,543

27.3.3 EQUITY PRICE RISK

Equity price risk is the risk that the fair values of equities will fluctuate as a result of changes in the level of equity indices or the value of individual share prices. Equity price risk arises from the change in fair values of equity investments. The Group manages the risk through diversification of investments in terms of geographic distribution and industry concentration. The table below analyses the effect of equity price risk on profit (as a result of change in the fair value of equity investments held as fair value through statement of income) and on equity (as a result of change in the fair value of equity investments held as available for sale) at the year end due to an assumed 5% change in market indices, with all other variables held constant.

Market indices	% Change in equity price	2012		2011	
		Effect on profit KD 000's	Effect on equity KD 000's	Effect on profit KD 000's	Effect on equity KD 000's
Kuwait stock exchange	+5	51	767	-	840
Doha securities market	+5	-	424	-	928
Saudi stock exchange	+5	-	-	-	193

27.4 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 in addition to other types of risks relating to the banking and financial activities of the Group. Operational risk is managed by the operational risk function, which ensures compliance with policies and procedures and monitors operational risk as part of overall global risk management.

The Operational Risk function of the Group is in line with the Central Bank of Kuwait instructions dated 14 November 1996, concerning the general guidelines for internal controls and the instructions dated 13 October 2003, regarding the sound practices for managing and supervising operational risks in banks.

28 CAPITAL

A key Group objective is to maximise shareholder value with optimal levels of risk and to maintain a strong capital base to support the development of its business.

Capital adequacy and the use of regulatory capital are monitored regularly by the Group's management and are governed by guidelines of Basel Committee on Banking Supervision as adopted by the Central Bank of Kuwait. The Group's regulatory capital and capital adequacy ratios are shown below:

	2012 KD 000's	2011 KD 000's
Risk Weighted Assets	10,112,938	8,585,566
Capital required	1,213,553	1,030,268
Capital available		
Tier 1 capital	1,657,408	1,570,414
Tier 2 capital	60,185	-
Total capital	1,717,593	1,570,414
Tier 1 capital adequacy ratio	16.4%	18.3%
Total capital adequacy ratio	17.0%	18.3%

The disclosures relating to the capital adequacy regulations issued by Central Bank of Kuwait as stipulated in Central Bank of Kuwait circular number 2/BS/184/2005 dated 21 December 2005 are included under the 'Risk Management' section of the annual report.

The calculations for 31 December 2012 include Boubyan Bank K.S.C., an Islamic Banking subsidiary acquired during the year (note 26). For purposes of determining risk-weighted assets and capital required, exposures and assets at Boubyan Bank K.S.C. are risk weighted, and capital charge calculated, in accordance with Central Bank of Kuwait regulations applicable to banks providing banking services compliant with Codes of Islamic Sharia'a. Those figures are then added to corresponding figures pertaining to all the rest of the Group, identical with the treatment in relevant reports submitted to the Central Bank of Kuwait.

29 FUNDS UNDER MANAGEMENT

The Group manages a number of funds, some of which are managed in association with other professional fund managers. The funds have no recourse to the general assets of the Group and the Group has no recourse to the assets of the funds. Accordingly, the assets of these funds are not included in the consolidated statement of financial position. As at 31 December 2012, funds under management were KD 2,817 million (2011: KD 2,530 million).

Independent Auditors' report to the Shareholders of National Bank of Kuwait S.A.K.

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of National Bank of Kuwait S.A.K. (the "Bank") and its subsidiaries (collectively the "Group"), which comprise the consolidated statement of financial position as at 31 December 2012, and the consolidated statement of income, consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgement, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Group'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 the management, as well as evaluating the overall presentation of the consolidated financial statements.

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as at 31 December 2012, and its financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted for use by the State of Kuwait.

Report on Other Legal and Regulatory Requirements

Furthermore, in our opinion proper books of account have been kept by the Bank and the consolidated financial statements, together with the contents of the report of the Bank's Board of Directors relating to these consolidated financial statements, are in accordance therewith. We further report that we obtained all the information and explanations that we required for the purpose of our audit and that the consolidated financial statements incorporate all information that is required by the Capital Adequacy Regulations issued by the Central Bank of Kuwait ("CBK") as stipulated in CBK Circular No. 2/BS/184/2005 dated 21 December 2005, as amended, the Commercial Companies Law No. 25 of 2012, and by the Bank's Articles of Association, that an inventory was duly carried out and that, to the best of our knowledge and belief, no violations of the Capital Adequacy Regulations issued by the CBK as stipulated in CBK Circular No. 2/BS/184/2005 dated 21 December 2005, as amended, the Commercial Companies Law No. 25 of 2012, nor of the Articles of Association have occurred during the year ended 31 December 2012 that might have had a material effect on the business of the Group or on its consolidated financial position.

We further report that, during the course of our audit, we have not become aware of any material violations of the provisions of Law No. 32 of 1968, as amended, concerning currency, the CBK and the organisation of banking business, and its related regulations during the year ended 31 December 2012.

Waleed A. Al Osaimi

Licence No. 68 A
Of Ernst & Young

8 January 2013

Kuwait

Jassim Ahmad Al-Fahad

Licence No. 53 A
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Fax: 2246 7929

Alternative Channels
Ext: 3217
Fax: 2259 5811

Direct Sales
Ext: 5000
Fax: 2259 5522

Consumer Lending
Ext: 3112
Fax: 2224 6865

Marketing
Ext: 3036
Fax: 2259 5679

Consumer Credit Collection
Ext: 2181
Fax: 2259 5671

Private Banking Group
Ext: 2226
Fax: 2241 8415 or
2224 6619

Corporate Banking Group

Domestic Corporate Banking
Ext: 2411
Fax: 2259 5640

Foreign Corporate, Oil and Trade Finance Group
Ext: 2307
Fax: 2242 6813

Treasury Group
Ext: 2889
Fax: 2246 7627

Credit Risk Management Group
Ext: 2417
Fax: 2246 4162

Economic Research Group
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Fax: 2224 6973

Legal Affairs Group
Ext: 3091
Fax: 2244 5098

Human Resources
Ext: 5162
Fax: 2244 3250

International Banking Group

Regional Institutional Banking
Ext: 5328
Fax: 2224 6977

Please refer to international network for a complete listing

Operations Group
Ext: 3060
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Information Technology Group
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Fax: 2245 9233

Group Financial Control
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Fax: 2242 2730

International Legal Affairs
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Fax: 2243 6208

Executive Office
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Fax: 2246 2469

Public Relations
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Fax: 2259 5804

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Fax: 2571 1785

Advertising
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Local Branches

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Ahmadi

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Ahmed Al-Jaber

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Fax: 2241 9442

Ali Sabah Al-Salem

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Fax: 2328 7153

Al Rihab

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Fax: 2259 3715

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Fax: 2476 1290

Andalus

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Fax: 2499 1802

Ardiya

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Fax: 2488 3927

Arraya 2

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Avenues

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Bayan

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Fahaheel

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Fahaheel Al Sahely

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Faiha

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Fax: 2254 6741

Farwaniya

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Fax: 2474 0013

Fintas

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Fax: 2390 3552

Ghazali

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Fax: 2483 4752

Hadiya

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Fax: 2259 3974

Hawalli

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Fax: 2261 2407

Kheitan

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Jabriya

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Fax: 2533 1944

Jahra

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Fax: 2455 3121

Jahra Commercial Branch

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Nuzha

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Othman

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Fax: 2265 6425

Qadisiya

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Fax: 2254 6738

Qurain

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Fax: 2544 0772

Qurtuba

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Fax: 2534 4780

Ras Al-Salmiya

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Rawdha

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Riqqa

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Rumaithiya

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Sabhan

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Salmiya

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Fax: 2574 3681

Salwa

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Shamiah

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Sharq

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Shuwaikh

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