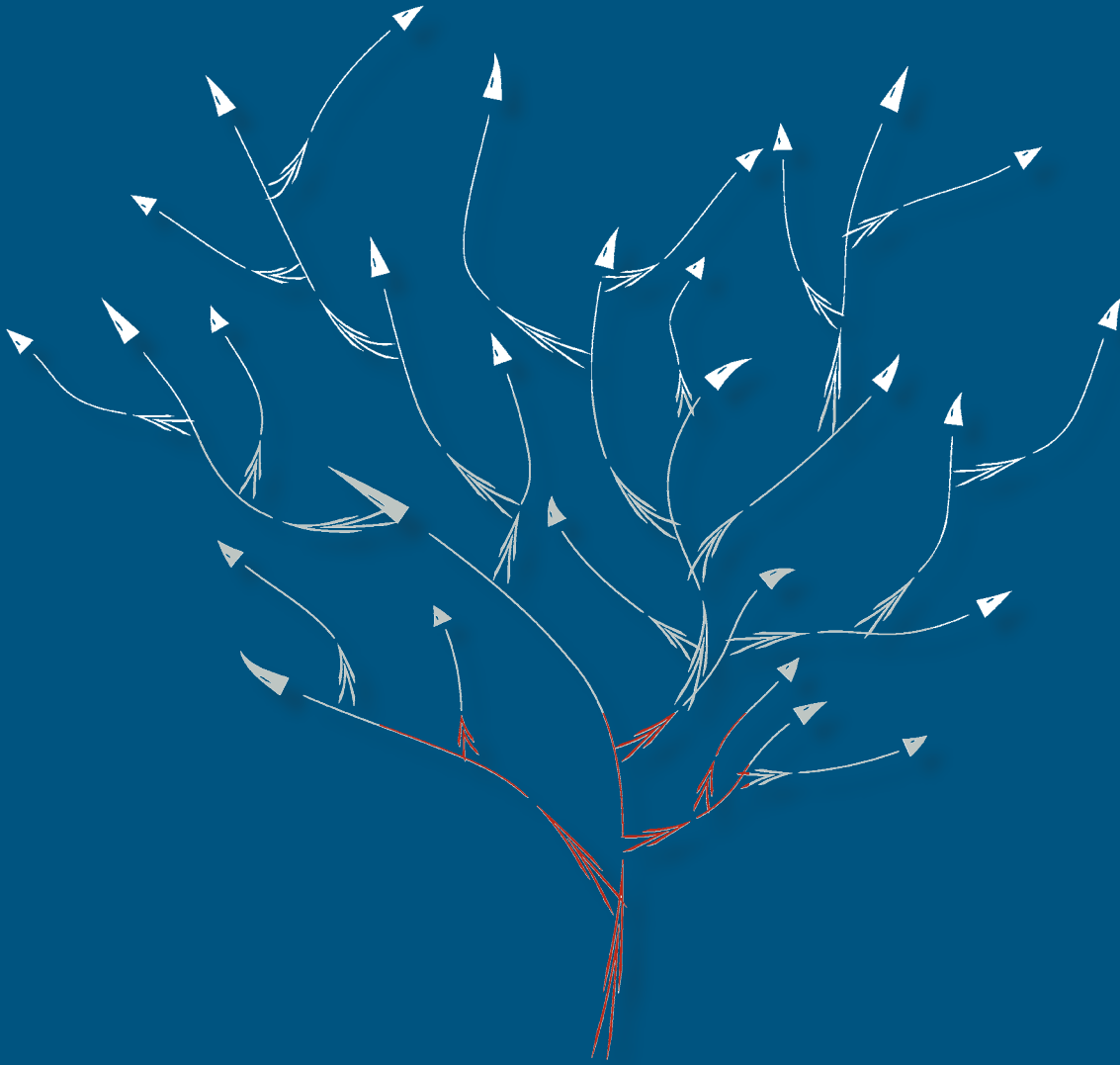


Annual Report
2006



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K M E F I C

KUWAIT AND MIDDLE EAST
FINANCIAL INVESTMENT
COMPANY k.s.c.c.

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KUWAIT AND MIDDLE EAST
FINANCIAL INVESTMENT
C O M P A N Y k . s . c . c .

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Notes to the Consolidated Financial Statement Continued

Year ended 31 December 2006

26- LIQUIDITY RISK

The maturity profile of the assets and liabilities at 31 December 2006 and 31 December 2005 are as follows:

	Kuwaiti Dinars											
	Upto 1 Month		1 to 3 Months		3 to 12 Months		Over one year		Total			
	31 December 2006	31 December 2005	31 December 2006	31 December 2005	31 December 2006	31 December 2005	31 December 2006	31 December 2005	31 December 2006	31 December 2005		
Assets												
Cash and cash equivalents	3,636,620	2,849,994	-	-	50,000	650,000	-	-	3,686,620	3,499,994		
Investments at fair value through profit or loss	6,515,939	1,493,708	15,408,179	13,912,329	-	-	-	-	21,924,118	15,406,037		
Investments available for sale	4,060,319	6,767,799	-	-	-	-	11,747,079	7,414,642	15,807,398	14,182,441		
Loans and advances	351,104	711,804	880,568	3,861,584	8,896,923	8,136,794	-	-	10,128,595	12,710,182		
Investment in an associate	-	-	-	-	-	-	-	3,136,190	-	3,136,190		
Investment in unconsolidated subsidiaries	-	-	-	-	-	-	47,920	36,546	47,920	36,546		
Other assets	6,632,309	2,488,951	9,251,628	-	-	-	-	-	15,883,937	2,488,951		
Intangible assets	-	-	-	-	-	-	12,613,766	12,613,766	12,613,766	12,613,766		
Equipment	-	-	-	-	-	-	1,013,965	992,730	1,013,965	992,730		
	<u>21,196,291</u>	<u>14,312,256</u>	<u>25,540,375</u>	<u>17,773,913</u>	<u>8,946,923</u>	<u>8,786,794</u>	<u>25,422,730</u>	<u>24,193,874</u>	<u>81,106,319</u>	<u>65,066,837</u>		
Liabilities												
Loans from banks and financial institutions	29,401,210	16,736,200	-	-	2,007,767	735,075	-	-	31,408,977	17,471,275		
Accounts payable and other liabilities	3,644,555	2,413,897	-	-	2,316,722	1,313,140	996,940	722,687	6,958,217	4,449,724		
	<u>33,045,765</u>	<u>19,150,097</u>	<u>-</u>	<u>-</u>	<u>4,324,489</u>	<u>2,048,215</u>	<u>996,940</u>	<u>722,687</u>	<u>38,367,194</u>	<u>21,920,999</u>		
Net liquidity gap	<u>(11,849,474)</u>	<u>(4,837,841)</u>	<u>25,540,375</u>	<u>17,773,913</u>	<u>4,622,434</u>	<u>6,738,579</u>	<u>24,425,790</u>	<u>23,471,187</u>	<u>42,739,125</u>	<u>43,145,838</u>		

Notes to the Consolidated Financial Statement Continued

Year ended 31 December 2006

25- INTEREST RATE RISK Continued

	Effective Interest rate %							
	31 December 2006				31 December 2005			
	KD FROM	TO	FC FROM	TO	KD FROM	TO	FC FROM	TO
Assets								
Cash and cash equivalents	1.50%	6.50%	1.44%	5.20%	1.50%	6.00%	1.44%	1.44%
Investments at fair value through profit or loss	-	-	-	-	-	-	-	-
Investments available for sale	-	-	-	-	-	-	-	-
Loans and advances	5.00%	8.75%	6.88%	10.00%	5.00%	8.50%	5.42%	9.16%
Investment in an associate								
Investment in unconsolidated subsidiaries	-	-	-	-	-	-	-	-
Other assets	-	-	-	-	-	-	-	-
Intangible assets								
Equipment	-	-	-	-	-	-	-	-
Liabilities								
Loans from banks and financial institutions	6.50%	7.00%	3.47%	6.15%	6.00%	6.00%	3.22%	5.08%
Accounts payable and other liabilities	-	-	-	-	-	-	-	-
On-balance sheet interest rate sensitivity gap								

Notes to the Consolidated Financial Statement Continued

Year ended 31 December 2006

25- INTEREST RATE RISK

	Kuwaiti Dinars											
	Upto 1 Month		1 to 3 Months		3 to 12 Months		Over one year		Non-interest sensitive		Total	
	31 December 2006	31 December 2005	31 December 2006	31 December 2005	31 December 2006	31 December 2005	31 December 2006	31 December 2005	31 December 2006	31 December 2005	31 December 2006	31 December 2005
Assets												
Cash and cash equivalents	3,636,620	2,849,994	-	-	50,000	650,000	-	-	-	-	3,686,620	3,499,994
Investments at fair value through profit or loss	6,515,939	1,493,708	-	-	-	-	-	-	15,408,179	13,912,329	21,924,118	15,406,037
Investments available for sale	-	-	-	-	-	-	-	-	15,807,398	14,182,441	15,807,398	14,182,441
Loans and advances	10,071,491	12,662,075	-	-	57,104	48,107	-	-	-	-	10,128,595	12,710,182
Investment in an associate	-	-	-	-	-	-	-	-	-	3,136,190	-	3,136,190
Investment in unconsolidated subsidiaries	-	-	-	-	-	-	-	-	47,920	36,546	47,920	36,546
Other assets	-	-	-	-	-	-	-	-	15,883,937	2,488,951	15,883,937	2,488,951
Intangible assets	-	-	-	-	-	-	-	-	12,613,766	12,613,766	12,613,766	12,613,766
Equipment	-	-	-	-	-	-	-	-	1,013,965	992,730	1,013,965	992,730
	20,224,050	17,005,777	-	-	107,104	698,107	-	-	60,775,165	47,362,953	81,106,319	65,066,837
Liabilities												
Loans from banks and financial institutions	26,408,977	17,471,275	5,000,000	-	-	-	-	-	-	-	31,408,977	17,471,275
Accounts payable and other liabilities	-	-	-	-	-	-	-	-	6,958,217	4,449,724	6,958,217	4,449,724
	26,408,977	17,471,275	5,000,000	-	-	-	-	-	6,958,217	4,449,724	38,367,194	21,920,999
On-balance sheet interest rate sensitivity gap	(6,184,927)	(465,498)	(5,000,000)	-	107,104	698,107	-	-	53,816,948	42,913,229	42,739,125	43,145,838

Notes to the Consolidated Financial Statement Continued

Year ended 31 December 2006

24- GEOGRAPHICAL CONCENTRATION OF ASSETS AND LIABILITIES

Kuwaiti Dinars

	Kuwait		North America		Europe		Far East		Other		Total	
	31 December 2006	31 December 2005	31 December 2006	31 December 2005	31 December 2006	31 December 2005	31 December 2006	31 December 2005	31 December 2006	31 December 2005	31 December 2006	31 December 2005
Assets												
Cash and cash equivalents	1,095,274	1,153,102	-	-	9	1,920	-	-	2,591,337	2,344,972	3,686,620	3,499,994
Investments at fair value through profit or loss	14,062,203	7,668,632	6,050,008	5,500,378	1,431,167	1,184,296	-	402,299	380,740	650,432	21,924,118	15,406,037
Investments available for sale	11,817,768	12,961,780	549,774	524,708	624,275	359,843	-	-	2,815,581	336,110	15,807,398	14,182,441
Loans and advances	10,128,595	12,328,635	-	-	-	-	-	-	-	381,547	10,128,595	12,710,182
Investment in an associate	-	3,136,190	-	-	-	-	-	-	-	-	-	3,136,190
Investment in unconsolidated subsidiaries	-	-	47,920	36,546	-	-	-	-	-	-	47,920	36,546
Other assets	1,006,379	1,296,776	76,555	213,615	-	-	-	-	14,801,003	978,560	15,883,937	2,488,951
Intangible assets	12,500,000	12,500,000	-	-	-	-	-	-	113,766	113,766	12,613,766	12,613,766
Equipment	984,985	806,560	-	-	-	-	-	-	28,980	186,170	1,013,965	992,730
	51,595,204	51,851,675	6,724,257	6,275,247	2,055,451	1,546,059	-	402,299	20,731,407	4,991,557	81,106,319	65,066,837
Liabilities												
Loans from banks and financial institutions	5,785,499	16,736,200	1,222,268	735,075	-	-	-	-	24,401,210	-	31,408,977	17,471,275
Accounts payable and other liabilities	3,824,103	2,826,995	-	-	-	-	-	-	3,134,114	1,622,729	6,958,217	4,449,724
	9,609,602	19,563,195	1,222,268	735,075	-	-	-	-	27,535,324	1,622,729	38,367,194	21,920,999

Notes to the Consolidated Financial Statement *Continued*

Year ended 31 December 2006

23- ESTIMATES AND JUDGEMENT

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

Estimation uncertainty

Provision for loan losses

Considerable judgement by management is required in estimation of the amount and timing of future cash flows when determining the level of provisions required for non-performing credit facilities. Such estimates are necessarily based on assumptions about several factors involving varying degrees of judgement and uncertainty and actual results may differ resulting in future changes in such provisions.

Unquoted investment securities

The valuation techniques for unquoted investment securities make use of estimates such as future cash flows, discount factors, yield curves, current market prices adjusted for market, credit and model risks and related costs and other valuation techniques commonly used by market participants where appropriate.

Any changes in these estimates and assumptions as well as the use of different but equally reasonable estimates and assumptions may have an impact on the carrying values of the provision for investment securities and fair value of unquoted investment securities.

Judgements

Classification of financial instruments

Management has to decide on acquisition of a financial instrument whether it should be classified as carried at fair value through profit or loss, available for sale or as loans and advances. In making the judgement the Group considers the primary purpose for which it is acquired and how it intends to manage and report its performance. Such judgement determines whether it is subsequently measured at cost or at fair value and if changes in fair value of instruments are reported in the consolidated statement of income or directly in equity.

Evidence of impairment in investments

The Group treats available for sale investment securities as impaired when there has been significant or prolonged decline in the fair value below its cost or whether other objective evidence of impairment exists. The determination of what is "significant" or "prolonged" requires considerable judgement.

Notes to the Consolidated Financial Statement Continued

Year ended 31 December 2006

21- FIDUCIARY ASSETS

Fiduciary assets comprise investments and funds managed by the Company on behalf of clients. These are not assets of the Company and accordingly are not included in the consolidated financial statements. As at the balance sheet date total fiduciary assets managed by the Company amounted to KD 1,362 million equivalent to US\$ 4,709 million (2005: KD 1,196 million equivalent to US\$ 4,097 million).

22- FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

The Group in the normal course of business uses various types of financial instruments. Information on financial risks and fair value of these financial instruments is set out below.

Credit risk

The Group is exposed to credit risk if counterparties fail to perform as contracted. Financial assets which potentially subject the Group to credit risk consist principally of cash equivalents and loans and advances. The Group's maximum exposure to credit risk is equal to the carrying amount of the above assets disclosed in the consolidated balance sheet. Credit risk inherent in outstanding foreign exchange commitments disclosed in note 20, if the counterparty is unable to settle, is limited to the difference between the contracted value of the transaction and the cost of completing it with another party.

The Group seeks to manage its credit risk by monitoring credit exposures and assessing the creditworthiness of counterparties. The Group also obtains security for most of the credit portfolio. The geographical concentration of assets and liabilities is given in note 24.

Interest rate risk

Interest rate risk is the risk that the value of a financial instrument will fluctuate due to changes in market interest rates. Financial instruments, which potentially subject the Group to interest rate risk, consist principally of cash equivalents, loans and advances and loans from banks and financial institutions. The Group manages this risk by matching the reprising of related assets and liabilities. The effective interest rates of assets and liabilities are given in note 25.

Liquidity Risk

Liquidity risk is the risk that the Group will be unable to meet its net funding requirements. Liquidity risk can also be caused by market disruptions or credit downgrades which may cause certain sources of funding to become unavailable. To guard against this risk, management has diversified funding sources and assets are managed with liquidity in mind, maintaining an adequate balance of cash, cash equivalents, and readily marketable securities. The maturities of assets and liabilities are given in note 26.

Market risk

Market risk is the risk that the value of a financial instrument will fluctuate as a result of changes in market prices. Financial instruments, which potentially subject the Group to market risk, consist principally of investments at fair value through profit or loss and investments available for sale. The Group manages this risk by diversifying its investments and monitoring market movements.

Foreign exchange risk

Foreign exchange risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Group's exposure to currency risk is equal to the carrying amount of net assets denominated in foreign currencies (note 28). A significant portion of exposure to foreign currencies is in GCC currencies which are pegged to Kuwaiti Dinars.

Operational risk

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 risk relating to the investment and portfolio management activities of the Group.

The Company complies in all material respects with the Central Bank of Kuwait instructions dated 14 November 1996 regarding general guidelines for internal control systems and directives issued on 13 October 2003 regarding "Sound Practices for the Management and Control of Operational Risks".

Notes to the Consolidated Financial Statement Continued

Year ended 31 December 2006

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

Amounts due to/from related parties

	Number of directors and executive officers		Amount (KD)	
	2006	2005	2006	2005
Directors				
Loans and advances	1	2	12,230	620,935
Key Management Personnel				
Loans and advances	1	1	386,337	109,266
Other related party balances				
			2006	2005
			(KD)	(KD)
Deposits placed with parent banks			1,356,656	1,571,686
Loan from parent banks			24,401,210	15,247,000
Receivable from parent banks			101,486	20,303
Investments and funds managed in a fiduciary capacity			82,582,284	85,613,707
Commitments and contingent liabilities			7,335,133	8,200,460
Foreign exchange contracts			9,269,160	-

Transactions with related parties are as follows:

	2006	2005
	(KD)	(KD)
Directors and key management personnel:		
Directors' fees	70,000	60,000
Salaries and other short term benefits	718,917	372,619
Share based payments	205,653	-
Management fees earned	51,614	33,988
	<u>1,046,184</u>	<u>466,607</u>
Other related party transactions	2006	2005
	(KD)	(KD)
Management fees earned	544,114	460,122
Interest income	154,243	13,823
Interest expenses	1,082,285	324,531
	<u>1,780,642</u>	<u>798,476</u>

20- COMMITMENTS AND CONTINGENCIES

	2006	2005
	(KD)	(KD)
Bank guarantees	7,335,133	12,175,690
Uncalled capital contributions relating to investments	368,691	413,441
Outstanding foreign exchange commitments	20,087,345	375,585

Notes to the Consolidated Financial Statement Continued

Year ended 31 December 2006

2006 Plan:

The annual general assembly meeting of the shareholders held on 20 March 2006 approved a second share option plan for employees (2006 Plan). In accordance with the plan, the Board of Directors of the Company were authorised to grant up to 3,773,880 shares as stock options to the employees. Employees can exercise the options till June 2011. The options vest as follows:

First tranche - 50% of the grant vest immediately after the grant date;

Second tranche - 50% of the grant vest on 1 February 2007.

The first tranche option price was fixed at 287 fils per share and was determined based on the average market price for the three months from 1 March 2005 till 31 May 2005, less a discount of 30%. The second tranche was fixed at 380 fils per share and was determined based on the average market price for the three months from 1 March 2005 till 31 May 2005, less a discount of 7.32%. The option holders are eligible for any bonus shares issued by the Company after 31 May 2005.

As of 31 December 2006, 2,982,376 stock options were not exercised (31 December 2005: NIL)

The Company accounted for option expenses for stock options granted after 20 March 2006 amounting to KD 589,153. These amounts have been recognised in the consolidated statement of income with a corresponding credit to stock options reserve in equity.

The fair value of options granted to employees has been determined on the date of the respective grant using the Chicago Board of Exchange option-pricing model by applying European Option Style.

The Board of Directors are authorised to allocate unvested share options relating to employees who resign or are terminated from services, to new employees of the Company, based on the same terms.

	Options Outstanding (Number)	Weighted Exercise Price (KD)	Weighted Average share price (KD)
Balance as at 31 December 2005	601,557		
Options Exercised for the 2001 plan	(234,135)	0.301	0.855
Bonus shares for the 2001 plan	73,484		
Issued options for the 2006 Plan	3,773,880		
Options exercised for the 2006 plan	(791,504)	0.239	0.683
Outstanding Options as at 31 December 2006	<u>3,423,282</u>		

18- PROPOSED DIVIDEND AND BONUS SHARES

The Board of Directors have proposed a cash dividend of 10% amounting to 10 fils per share (2005: 30% amounting to 30 fils per share).

The Board of Directors have also proposed an issue of 20 bonus shares for every 100 shares held (2005: 20 bonus shares for every 100 shares held). The consolidated financial statements have not been adjusted to reflect the dividend or the issue of bonus shares as they are subject to the approval of the shareholders in the Annual General Assembly meeting.

19- RELATED PARTY TRANSACTIONS

Related parties primarily comprise subsidiaries, associates, significant shareholders, directors and key management personnel of the Group, their families and entities of which they are principal owners. All related party transactions are carried at terms approved by the Group's management.

Notes to the Consolidated Financial Statement *Continued*

Year ended 31 December 2006

e- Treasury shares

	2006	2005
Number of own shares	8,338,438	3,200,365
Percentages of issued shares	4.72%	2.19%
Market value (KD)	5,503,369	2,528,288

f- Treasury share reserves are non-distributable.

15- INTEREST INCOME AND INTEREST EXPENSE

	2006 (KD)	2005 (KD)
Interest income:		
Term deposits	183,215	58,648
Loans and advances	1,654,097	793,373
Others	13,878	4,830
Total interest income	1,851,190	856,851
Interest expenses:		
Bank borrowings	1,418,597	518,756
Others	359,044	72,344
Total interest expense	1,777,641	591,100

16- EARNINGS PER SHARE

	2006 (KD)	2005 (KD)
Net income for the year (KD)	8,610,202	10,168,490
Weighted average number of issued shares	146,439,563	146,439,563
Issue of Bonus shares for the year	29,287,913	29,287,913
Weighted average number of Company's treasury shares	(6,664,205)	(1,480,575)
Weighted average number of shares issued – employee share option plan	465,221	-
Adjusted weighted average number of shares	169,528,492	174,246,901
Earnings per share (Fils)	50.79	58.36
Diluted earnings per share (Fils)	50.32	58.36

17- EMPLOYEE SHARE OPTION PLAN

2001 Plan:

The annual general assembly meeting of the shareholders held on 12 March 2001 approved a share option plan for employees (2001 Plan). In accordance with the plan, the Board of Directors of the Company were authorised to grant up to 6,037,500 shares as stock options to the employees. The period over which the employees could exercise the options were extended up to March 2011. The options vest as follows:

First tranche - 40% vest after expiry of one year from the grant date;

Second tranche - 40% vest after expiry of two years from the grant date; and

Third tranche - 20% vest after expiry of three years from the grant date.

As of 31 December 2006, 440,906 stock options were not exercised (31 December 2005: 601,557 stock options).

Notes to the Consolidated Financial Statement Continued

Year ended 31 December 2006

13- LOANS FROM BANKS AND FINANCIAL INSTITUTIONS

	2006 (KD)	2005 (KD)
Unsecured bank loans	29,401,210	16,736,200
Secured bank loans	2,007,767	735,075
	<u>31,408,977</u>	<u>17,471,275</u>

Secured loans amounting to KD 2.008 million (US\$ 6.84 million) (2005: KD 0.735 million (US\$ 2.52 million)) represents margin loan from a foreign bank by mortgaging Company's investment in shares. These loans have been taken at existing LIBOR rates and have indefinite maturity period. Unsecured loans represent money market loans and revolving loans taken from local and foreign banks. Effective interest rates of loans from banks are stated in Note 25.

14- EQUITY

a- Share capital

In the annual general meeting held on 20 March 2006, the shareholders approved the increase of share capital from 146,439,563 shares of 100 fils each to 179,501,356 shares of 100 fils each. The Ministry of Commerce and Industry's approval for the increase in share capital was obtained on 12 April 2006.

Accordingly the authorised, issued and paid capital of the Company are as follows:

	2006 (KD)	2005 (KD)
Authorised: 179,501,356 shares of 100 fils each (31 December 2005: 146,439,563 shares of 100 fils each)	17,950,136	14,643,956
Issued and fully paid up: 176,518,980 shares of 100 fils each (31 December 2005: 146,439,563 shares of 100 fils each)	17,651,898	14,643,956

The issued and fully paid up capital includes 9,811,380 shares (2005: 6,037,500 shares) on account of share option plan for employees (see note 17).

b- Share premium

The share premium represents premiums collected upon issuing new shares to employees under Employee Stock Option Plan. These amounts are not available for distribution.

c- Statutory reserve

In accordance with the Kuwait Commercial Company Law and the Company's Articles of Association, 10% of the net profit for the year is required to be transferred to the statutory reserve until the reserve reaches a minimum of 50% of share capital. Distribution of the statutory reserve is limited to the amount required to enable the payment of a dividend of up to 5% of share capital in years when retained earnings are not sufficient for payment of dividend.

d- General reserve

In accordance with the Company's Articles of Association, 10% of the net profit for the year is required to be transferred to the general reserve. The transfer to this reserve can be discontinued by a resolution adopted by the Board of Directors. The general reserve includes dividends received on the treasury shares prior to Central Bank of Kuwait circular no. 2/RS/75/99 dated 14 December 1999, amounting to KD 36,500 (2005: KD 36,500) which is not distributable.

Notes to the Consolidated Financial Statement Continued

Year ended 31 December 2006

9- INVESTMENT IN UNCONSOLIDATED SUBSIDIARIES

	Country of incorporation	Percentage of holding	Year of incorporation	2006 (KD)	2005 (KD)
Safat Limited	Antigua & Barbuda	100%	1986	30,116	15,937
KME Fund Managers Limited	Guernsey	100%	1988	10,576	13,309
KME Cayman Limited	Cayman Islands	100%	2005	7,228	7,300
				<u>47,920</u>	<u>36,546</u>

10- OTHER ASSETS

	2006 (KD)	2005 (KD)
Application money for investments	9,869,172	-
Due from unsettled trades	3,847,868	1,032,045
Accrued management fee	560,863	507,263
Prepaid Expenses	526,675	395,143
Others	1,079,359	554,500
	<u>15,883,937</u>	<u>2,488,951</u>

Application money of KD 9,869,172 consist of KD 9,251,628 paid for acquiring 30% stake in a Saudi Company, KD 601,660 paid for acquiring 100% stakes in three companies in Egypt and KD 15,884 paid for acquiring 100% stake in a Qatari Company. These amounts are not classified as investments, as the companies are under incorporation as on 31 December 2006.

11- INTANGIBLE ASSETS

Intangible assets represent broking licences acquired from Kuwait Stock Exchange for KD 12,500,000 and Muscat Securities Market for KD 113,766 (Omani Riyals 150,000). The management believes that these licences have indefinite useful lives.

12- EQUIPMENT

	Furniture and Equipment KD	Computers KD	Software KD	Total KD
Cost				
At 1 January 2006	759,595	672,420	586,433	2,018,448
Additions	106,549	170,553	49,748	326,850
Disposals	(5,204)	(21,200)	-	(26,404)
At 31 December 2006	<u>860,940</u>	<u>821,773</u>	<u>636,181</u>	<u>2,318,894</u>
Accumulated depreciation				
At 1 January 2006	544,794	292,971	187,953	1,025,718
Depreciation	82,168	135,366	87,348	304,882
Disposals	(4,560)	(21,111)	-	(25,671)
At 31 December 2006	<u>622,402</u>	<u>407,226</u>	<u>275,301</u>	<u>1,304,929</u>
Net book value				
At 31 December 2006	<u>238,538</u>	<u>414,547</u>	<u>360,880</u>	<u>1,013,965</u>
At 31 December 2005	<u>214,801</u>	<u>379,449</u>	<u>398,480</u>	<u>992,730</u>
Depreciation rates	20%-25%	25%	14.34%	

Notes to the Consolidated Financial Statement Continued

Year ended 31 December 2006

5- INVESTMENTS AVAILABLE FOR SALE

	2006 (KD)	2005 (KD)
Quoted equities	4,060,319	6,767,799
Unquoted equity and fund investments	11,884,945	7,537,544
Less: impairment	(137,866)	(122,902)
	<u>15,807,398</u>	<u>14,182,441</u>

Investments available for sale include unquoted equity investments with original cost of KD 2,820,473 (2005: KD 153,968) carried at cost less impairment losses. The fair value of these investments cannot be reliably determined as there is no active market for these investments and there have not been any recent transactions that provide evidence of the current fair value.

6- LOANS AND ADVANCES

	2006 (KD)	2005 (KD)
Loans to customers	10,277,032	12,920,484
Loans to staff	58,269	49,089
	<u>10,335,301</u>	<u>12,969,573</u>
General provision (see note 2 (d))	(206,706)	(259,391)
	<u>10,128,595</u>	<u>12,710,182</u>

The effective interest rates on loans and advances are stated in Note 25.

7- INVESTMENT IN AN ASSOCIATE

During the year ended 31 December 2006, the Company sold 2% of its investments (3,000,000 shares) in its associate, Strategia Investment Company K.S.C. (Closed) reducing its percentage of holding from 21.6% to 19.6%. With effect from the date of sale the Company discontinued equity accounting for the above investment and its carrying value was classified as available for sale investment. Proportionate share in the losses of the Strategia Investment Company K.S.C. (Closed) till the date of this sale is accounted as loss from associate in the consolidated statement of income.

8- CONSOLIDATED SUBSIDIARIES

The following are the consolidated subsidiaries of the Company.

Name of the Subsidiaries	Country of incorporation	Activity	Capital	Percentage of holding
Online Soft Computer Systems Company (K.S.C.C.)	Kuwait	Online brokerage	500,000 KD	100%
Al Awsat First Holding Company (K.S.C.C.)	Kuwait	Holding company	1,000,000 KD	100%
Middle East Financial Brokerage Company L.L.C.	U.A.E.	Brokerage	10,000,000 AED	100%
Middle East Brokerage Company L.L.C.	Oman	Brokerage	1,000,000 OMR	100%
Future E-Trade Company (K.S.C.C.)	Kuwait	Electronic trade	150,000 KD	60%
Middle East Financial Brokerage Company (K.S.C.)	Kuwait	Brokerage	17,500,000 KD	90%

During the year ended 31 December 2006, the Company established Middle East Financial Brokerage Company K.S.C. to carry out brokerage activities in Kuwait and the Company's brokerage division net assets were transferred at carrying value.

Notes to the Consolidated Financial Statement Continued

Year ended 31 December 2006

l- Foreign currency translation

Foreign currency transactions are recorded at rates of exchange ruling at the date of transactions. Monetary assets and liabilities denominated in foreign currencies, outstanding at the year end are translated into Kuwaiti Dinars at rates of exchange ruling at the balance sheet date. Any resultant gains or losses are taken to the consolidated statement of income. Translation difference on non-monetary assets classified as 'fair value through profit or loss' are reported as part of the fair value gain or loss in the consolidated statement of income and 'available for sale' assets are included in the cumulative changes in fair value, in equity.

Foreign subsidiaries are treated as independent foreign units. The balance sheets of foreign subsidiaries are translated at the year end exchange rate and their profit and loss accounts are translated at the rates of exchange prevailing at the date of transaction. The exchange differences are recognised in foreign currency translation reserve in equity. When the foreign subsidiary is disposed off, in part or in full, the relevant amount in the foreign currency translation reserve is transferred to the consolidated statement of income.

m- Fiduciary assets

Third party assets managed by the Group and assets held in trust or in a fiduciary capacity are not treated as assets of the Group and accordingly are not included in these consolidated financial statements.

n- Share-based payments

The share option programme allows employees to acquire shares of the Company. The fair value of options granted is recognised as an employee expense with corresponding increase in equity. The fair value is measured at grant date and spread over the period during which the employees become unconditionally entitled to the options. The amount recognised as an expense is adjusted to reflect the actual number of share options that vest during the period.

o- Segment reporting

A segment is a distinguishable component of the Group that is engaged in providing services (business segment), or in providing services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments. The Group's primary format for segment reporting is based on business segments. Segment results include revenue and expenses directly attributable to a segment and an allocation of cost of funds to segments based on the daily weighted average balance of segment assets. Segment revenue and segment expenses do not include adjustment for inter segment transfers.

3- CASH AND CASH EQUIVALENTS

	2006 (KD)	2005 (KD)
Cash and bank balances	1,330,881	2,562,772
Fixed deposits	2,355,739	937,222
	<u>3,686,620</u>	<u>3,499,994</u>
Less: Fixed deposits maturing after 3 months	(50,000)	(650,000)
Cash and cash equivalent in cash flow	<u>3,636,620</u>	<u>2,849,994</u>

4- INVESTMENTS AT FAIR VALUE THROUGH PROFIT OR LOSS

	2006 (KD)	2005 (KD)
Quoted equities	888,963	2,884,022
Quoted funds	21,035,155	12,522,015
	<u>21,924,118</u>	<u>15,406,037</u>

Notes to the Consolidated Financial Statement Continued

Year ended 31 December 2006

Loans and advances are subject to credit risk provision for loan impairment if there is objective evidence that the Group will not be able to collect all amounts due. The amount of the provision is difference between the carrying amount and the recoverable amount, being the present value of expected future cash flows, including amount recoverable from guarantee and collateral, discounted based on the contractual interest rate. The amount of loss arising from impairment is taken to the consolidated statement of income.

In addition, in accordance with Central Bank of Kuwait instructions, a minimum general provision of 2% is made on all loans and advances (net of certain restricted categories of collateral) that are not provided for specifically.

e- Investments in associates

Associated companies are those entities in which the Group has significant influence but not control, generally accompanying a shareholding between 20% and 50% of the voting rights. Investment in associates is accounted for by equity method of accounting. Any impairment in value is recognised in consolidated statement of income.

f- Intangible assets

Intangible assets acquired separately are measured on initial recognition at cost. The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortised over their useful economic lives, assessed and adjusted for impairment whenever there is an indication that an intangible asset may be impaired. Intangible assets with indefinite useful lives are not amortised but are tested annually for impairment. For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows.

g- Equipment

Equipment are stated at cost less accumulated depreciation and impairment losses, if any. Equipment are impaired if the carrying amount of the asset or its cash generating unit exceeds its recoverable amount. The impairment losses are recognised in the consolidated statement of income.

Depreciation is calculated based on the estimated useful lives of the applicable assets using the straight-line method. The estimated useful lives of equipment are 4 to 7 years.

h- Provisions

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

i- Employees' end of service indemnity

Provision is made for employees' end of service indemnity in accordance with the Kuwait Labour Law based on employees' salaries and accumulated periods of service or on the basis of employment contracts, where such contracts provide extra benefits. The provision, which is unfunded, is determined as the liability that would arise as a result of involuntary termination of staff at the balance sheet date. This basis is considered to be an approximation of the present value of final obligation.

j- Treasury shares

The cost of the Company's own shares purchased, including directly attributable costs is recognised in equity. Gains or losses arising on sale are separately disclosed under equity and in accordance with the instructions of Central Bank of Kuwait, these amounts are not available for distribution. No cash dividend is paid on treasury shares held by the Company. The issue of bonus shares increases the number of treasury shares proportionately and reduces the average cost per share without affecting the total cost of treasury shares.

k- Revenue recognition

Management fees and placement fees are accounted on an accrual basis as soon as the fees are earned. Commission incomes and performance fees are recognised when earned. Interest income and expenses are recognised using the effective interest method taking into account the principal outstanding and the rate applicable. Dividend incomes are recognised when the right to receive payment is established. Share of income from an associate is the Company's share of the post acquisition total recognized gains and losses of an associate. Realised gains or losses from dealing in securities represent differences between sale proceeds and cost of securities on a weighted average basis.

Notes to the Consolidated Financial Statement Continued

Year ended 31 December 2006

Loans and advances

Loans and advances are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. These are carried at amortized cost using effective interest method, less any provision for impairment.

Available for sale

These are non derivative financial assets not included in any of the above classifications and are principally those acquired to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rate or equity prices. These are subsequently measured and carried at fair value and any resultant unrealised gains or losses are recognised as a separate component in equity. When the "available for sale" asset is disposed off or impaired, the related accumulated fair value adjustments in equity are transferred to the consolidated statement of income as realised gains or losses.

Financial liabilities

Financial liabilities are subsequently measured at amortised cost using the effective yield method.

Trade and settlement date accounting

All regular way purchases and sales of financial assets are recognized using settlement date accounting. Changes in fair value between the trade date and settlement date are recognised in the consolidated statement of income. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame generally established by regulations or conventions in the market place.

Fair values

For financial instruments traded in organised financial markets, 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.

The fair value of interest bearing financial instruments that are not quoted in an active market is estimated based on discounted cash flows using interest rates for items with similar terms and risk characteristics. The estimated fair value of deposits with no stated maturity, which includes non-interest bearing deposits, is the amount payable on demand.

The fair value of forward exchange contract is calculated by reference to forward exchange rates with similar maturities.

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

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

Impairment of financial assets

A financial asset is impaired if its carrying amount is greater than its estimated recoverable amount. An assessment is made at each balance sheet date to determine whether there is objective evidence that a specific financial asset, or a group of financial assets, may be impaired. In the case of financial asset classified as available for sale, a significant or prolonged decline in the fair value of assets below its cost is considered in determining whether the assets are impaired. If any such evidence exists for available for sale financial assets, the cumulative loss 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, is removed from equity and recognised in the consolidated statement of income. Impairment losses on equities available for sale recognised in the consolidated statement of income are not reversed through the consolidated statement of income.

Notes to the Consolidated Financial Statement Continued

Year ended 31 December 2006

b- Consolidation

Subsidiaries are those entities controlled by the Group. Control exists when the Group has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The financial statements of subsidiaries, other than those which are held with a view to disposal within twelve months are consolidated from the date control effectively commences until the date control effectively ceases.

The financial statements of subsidiaries are prepared for the same reporting year as the Company, using consistent accounting policies. Adjustments are made to subsidiaries' financial statements in the consolidation to align the accounting policies for any dissimilarities that may exist.

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

Minority interest represents the share of results and net assets in consolidated subsidiaries not held by the Group. Minority interest is presented separately in the consolidated statement of income and within equity in the consolidated balance sheet.

c- Cash and cash equivalents

Cash and cash equivalents comprise cash and bank balances, short-term deposits and investments in money market instruments with original maturities of three months or less.

d- Financial instruments – recognition and de-recognition, classification and measurement

Recognition and de-recognition

A financial asset or a financial liability is recognised when the Group becomes a party to the contractual provisions of the instrument. A financial asset is derecognised when the contractual rights to the cash flows from the financial asset expire or when the Group has transferred substantially all the risks and rewards of the ownership or when it has neither transferred nor retained substantially all risks and rewards and when it no longer has control over the asset or portion of the asset. If the Group has retained control, it shall continue to recognise the financial asset to the extent of its continuing involvement in the financial asset.

Classification and measurement

The Group classifies its financial assets as “investments at fair value through profit or loss”, “loans and advances”, or “available for sale” and its financial liabilities as financial liabilities other than at fair value through profit or loss”. Management determines the appropriate classification of each instrument at the time of acquisition.

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

Investments at fair value through profit or loss

These are financial assets that are either held for trading or are designated as investments at fair value through profit or loss upon initial recognition. A financial asset is classified in this category only if they are acquired principally for the purpose of generating profit from short-term fluctuations in price or if so designated by the management upon initial recognition if they are managed and their performance is evaluated and reported internally on a fair value basis in accordance with a documented risk management or investment strategy. Financial assets classified as investments at fair value through profit or loss are subsequently measured and carried at fair value. Resultant unrealised gains and losses arising from changes in fair value are included in the consolidated statement of income. This includes all derivative financial instruments, other than those designated as effective hedging instruments.

Notes to the Consolidated Financial Statement

Year ended 31 December 2006

1- INCORPORATION AND PRINCIPAL ACTIVITIES

Kuwait and Middle East Financial Investment Company K.S.C. (Closed) (the 'Company') is a Kuwaiti Shareholding Company incorporated on 1 January 1984. The Company is engaged in carrying out investment and portfolio management activities for its own account and for clients.

The Company's registered office is at 13th floor, Kuwait Real Estate Bank Building, Joint Banking Center, Kuwait city, Kuwait.

The Company's shares are listed on the Kuwait Stock Exchange. The Company is a subsidiary of The Bank of Kuwait and the Middle East (the 'parent bank'), which is listed on the Kuwait Stock Exchange. The Bank of Kuwait and the Middle East is a subsidiary of Ahli United Bank B.S.C., a Bahraini bank (the 'ultimate parent bank'), listed on Bahrain and Kuwait Stock Exchanges.

The consolidated financial statements of the Company for the year ended 31 December 2006 comprise of the Company and its subsidiaries (together referred to as the "Group"). For details on the Group's subsidiaries, refer Notes 8 and 9.

Number of employees of the Group as of 31 December 2006 was 197 (31 December 2005: 159)

These consolidated financial statements were approved for issue by the Board of Directors on 31 January 2007 and will be submitted to the shareholders of the Company for approval at the forthcoming Annual General Assembly.

2- BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES

a- Basis of preparation

The consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted for use by Government of Kuwait for financial services institutions regulated by the Central Bank of Kuwait. These regulations require adoption of all International Financial Reporting Standards (IFRS) except for the International Accounting Standard (IAS) 39: Financial Instruments: Recognition and Measurement requirement for collective provision, which has been replaced by the Central Bank of Kuwait's requirement for a minimum general provision as described under the accounting policy for impairment of financial assets. (Refer Note 2 (d)).

These consolidated financial statements are prepared under the historical cost convention as modified by revaluation of financial assets classified as 'at fair value through profit or loss' and 'available for sale'.

The preparation of financial statements requires management to make judgements and estimates that affect the reported amounts of financial assets and liabilities and disclosure of contingent liabilities. These judgements and estimates also affect the revenues and expenses and the resultant provisions as well as the fair value changes reported in the equity. The areas involving a high degree of judgment or complexity or areas where assumptions and estimates are significant to the financial statements are disclosed in the Note 23.

The accounting policies are consistent with those of the previous financial year.

The application of IFRS 7, which will be effective for the year ending 31 December 2007 will result in amended and additional disclosures relating to financial instruments and associated risks. The application of IFRIC 8, which is also effective for 2007 is not expected to have a material impact on the consolidated financial statements of the Group.

These consolidated financial statements are presented in Kuwaiti Dinars (KD), which is the Company's functional currency.

Consolidated Statement of Cash Flows

1 January 2006 to 31 December 2006

	2006	2005
Note	(KD)	(KD)
CASH FLOWS FROM OPERATING ACTIVITIES		
Profit for the year attributable to Company's equity shareholders	8,610,202	10,168,490
Adjustments:		
Interest income	(1,851,190)	(856,851)
Unrealised gains on investments at fair value through profit or loss	(1,147,385)	(2,748,398)
Gains on disposal of investments available for sale	(4,403,038)	(762,270)
Dividends	(426,113)	(341,461)
Share of loss/(gain) from an associate	20,339	(526,165)
Income from unconsolidated subsidiaries	(5,059)	(336)
Equity share option expenses	589,153	7,810
Depreciation	304,882	264,370
Interest expense	1,777,641	591,100
Impairment loss of loans and advances and other assets	16,946	170,385
Impairment loss of investments available for sale	14,964	122,902
Operating income before changes in operating assets and liabilities	3,501,342	6,089,576
Investments at fair value through profit or loss	(5,370,696)	(3,100,942)
Loans and advances	2,634,272	(8,519,242)
Interest income received	1,851,190	856,851
Other assets	(3,595,445)	(863,147)
Accounts payable and other liabilities	2,508,493	2,954,970
Net cash from/(used in) operating activities	1,529,156	(2,581,934)
CASH FLOWS FROM INVESTING ACTIVITIES		
Acquisition of investments available for sale	(9,815,279)	(2,677,944)
Proceeds from disposal of investments available for sale	11,055,416	2,862,873
Proceeds from sale of interest in associate	291,000	-
Capital (contribution)/distribution from unconsolidated subsidiaries	(8,091)	74,157
Fixed Deposit matured/(deposited)	600,000	(650,000)
Application money for acquisition of investments	10 (9,869,172)	-
Acquisition of intangible assets	-	(113,766)
Acquisition of equipment net of proceeds from sale of equipment	(326,117)	(659,075)
Dividends received	426,113	341,461
Net cash used in investing activities	(7,646,130)	(822,294)
CASH FLOWS FROM FINANCING ACTIVITIES		
Loans from banks and financial institutions	13,937,702	8,610,889
Interest expense paid	(1,777,641)	(591,100)
Purchase of treasury shares	(3,164,443)	(1,742,224)
Sale of treasury shares	6,038	-
Proceeds from employee share option plan	236,231	31,256
Dividends paid	(4,224,955)	(1,378,359)
Net cash from financing activities	5,012,932	4,930,462
Change in minority interest	1,890,668	56,180
Increase in cash and cash equivalents	786,626	1,582,414
Cash and cash equivalents at beginning of the year	2,849,994	1,267,580
Cash and cash equivalents at end of the year	3 (3,636,620)	2,849,994

The notes set out on pages 15 to 33 form an integral part of these consolidated financial statements.

Consolidated Statement of Changes in Equity Continued

1 January 2006 to 31 December 2006

	Kuwaiti Dinars											
	Attributable to the equity shareholders of the company											
	Share capital	Treasury shares	Share premium	Statutory reserve	General reserve	Retained earnings	Fair valuation reserve	Foreign currency translation reserve	Treasury shares reserve	Share options reserve	Minority interest	Total
Balance at 31 December 2005	14,643,956	(1,925,212)	237,841	4,003,979	3,571,873	14,552,803	6,250,171	11,754	1,734,683	7,810	56,180	43,145,838
Changes in equity for the year ended 31 December 2006												
Available for sale investments:												
Valuation gain taken to equity	-	-	-	-	-	-	68,365	-	453	-	-	68,818
Transferred to consolidated statement of income on sale	-	-	-	-	-	-	(4,403,038)	-	-	-	-	(4,403,038)
Exchange differences on translating foreign operations	-	-	-	-	-	-	-	(14,934)	-	-	-	(14,934)
Net income recognised directly in equity	-	-	-	-	-	-	(4,334,673)	(14,934)	453	-	-	(4,349,154)
Profit for the year	-	-	-	-	-	8,610,202	-	-	-	-	140,668	8,750,870
Total recognised income and expenses for the year	-	-	-	-	-	8,610,202	(4,334,673)	(14,934)	453	-	140,668	4,401,716
Dividends	-	-	-	-	-	(4,224,955)	-	-	-	-	-	(4,224,955)
Bonus shares	2,928,791	-	-	-	-	(2,928,791)	-	-	-	-	-	-
Transfer to reserves	-	-	-	-	-	-	-	-	-	-	-	-
Equity share options issued	79,151	-	157,080	-	-	-	-	-	-	589,153	-	825,384
Purchase of treasury shares	-	(3,158,858)	-	-	-	-	-	-	-	-	-	(3,158,858)
Balance at 31 December 2006	17,651,898	(5,084,070)	394,921	4,003,979	3,571,873	16,009,259	1,915,498	(3,180)	1,735,136	596,963	196,848	40,989,125
Minority interest	-	-	-	-	-	-	-	-	-	-	1,750,000	1,750,000
Balance at 31 December 2006	17,651,898	(5,084,070)	394,921	4,003,979	3,571,873	16,009,259	1,915,498	(3,180)	1,735,136	596,963	1,946,848	42,739,125

The notes set out on pages 15 to 33 form an integral part of these consolidated financial statements.

Consolidated Statement of Changes in Equity

1 January 2006 to 31 December 2006

Kuwaiti Dinars

	Attributable to the equity shareholders of the company										Total	
	Share capital	Treasury shares	Share premium	Statutory reserve	General reserve	Retained earnings	Fair valuation reserve	Foreign currency translation reserve	Treasury shares reserve	Share options reserve		Minority interest
Balance at 31 December 2004	13,946,625	(182,988)	206,585	2,948,792	2,516,686	8,570,377	1,888,889	14,078	1,734,683	-	-	- 31,643,727
Changes in equity for the year ended 31 December 2005												
Available for sale investments: Valuation gains taken to equity	-	-	-	-	-	-	4,773,987	-	-	-	-	4,773,987
Transferred to consolidated statement of income on sale	-	-	-	-	-	-	(535,607)	-	-	-	-	(535,607)
Transferred to consolidated statement of income on impairment	-	-	-	-	-	-	122,902	-	-	-	-	122,902
Exchange differences on translating foreign operations	-	-	-	-	-	-	-	(2,324)	-	-	-	(2,324)
Net income recognised directly in equity	-	-	-	-	-	-	4,361,282	(2,324)	-	-	-	4,358,958
Profit for the year	-	-	-	-	-	10,168,490	-	-	-	-	(3,820)	10,164,670
Total recognised income and expenses for the year	-	-	-	-	-	10,168,490	4,361,282	(2,324)	-	-	(3,820)	14,523,628
Dividends	-	-	-	-	-	(1,378,359)	-	-	-	-	-	(1,378,359)
Bonus shares	697,331	-	-	-	-	(697,331)	-	-	-	-	-	-
Transfer to reserve	-	-	-	1,055,187	1,055,187	(2,110,374)	-	-	-	-	-	-
Equity share options issued	-	-	31,256	-	-	-	-	-	-	7,810	-	39,066
Sale of treasury shares	-	(1,742,224)	-	-	-	-	-	-	-	-	-	(1,742,224)
Balance at 31 December 2005	14,643,956	(1,925,212)	237,841	4,003,979	3,571,873	14,552,803	6,250,171	11,754	1,734,683	7,810	(3,820)	43,085,838
Minority Interest	-	-	-	-	-	-	-	-	-	-	60,000	60,000
Balance at 31 December 2005	14,643,956	(1,925,212)	237,841	4,003,979	3,571,873	14,552,803	6,250,171	11,754	1,734,683	7,810	56,180	43,145,838

Consolidated Statement of Income

1 January 2006 to 31 December 2006

	Note	2006 (KD)	2005 (KD)
INCOME			
Management fees		4,341,202	3,700,820
Performance fees		74,307	1,724,665
Interest income	15	1,851,190	856,851
Commission income		6,145,257	5,963,018
Placement fees		160,868	111,204
Gains on investments at fair value through profit or loss		752,278	3,011,683
Gains on disposal of investments available for sale		4,403,038	762,270
Dividends		426,113	341,461
Share of (loss)/income from an associate		(20,339)	526,165
Income from unconsolidated subsidiaries		5,059	336
Foreign exchange gains		129,748	118,905
Other income		41,720	9,590
TOTAL INCOME		18,310,441	17,126,968
OPERATING EXPENSES AND OTHER CHARGES			
Staff expenses		3,968,336	3,190,611
Stock option expenses	17	589,153	7,810
Other operating expenses		2,516,879	2,231,741
Depreciation		304,882	264,370
Interest expense	15	1,777,641	591,100
Provision for impairment of loans and advances and other assets		16,946	170,385
Impairment loss on investments available for sale		14,964	122,902
TOTAL OPERATING EXPENSES AND OTHER CHARGES		9,188,801	6,578,919
PROFIT FROM OPERATIONS		9,121,640	10,548,049
Contribution to Kuwait Foundation for the Advancement of Sciences (KFAS)		(82,095)	(89,705)
National Labour Support Tax (NLST)		(218,675)	(233,674)
Directors' fees		(70,000)	(60,000)
PROFIT FOR THE YEAR		8,750,870	10,164,670
Attributable to:			
Company's equity shareholders		8,610,202	10,168,490
Minority interest		140,668	(3,820)
		8,750,870	10,164,670
EARNINGS PER SHARE (Fils)	16	50.79	58.36
DILUTED EARNINGS PER SHARE (Fils)	16	50.32	58.36

The notes set out on pages 15 to 33 form an integral part of these consolidated financial statements.

Consolidated Balance Sheet

As at 31 December 2006

	Note	2006 (KD)	2005 (KD)
ASSETS			
Cash and cash equivalents	3	3,686,620	3,499,994
Investments at fair value through profit or loss	4	21,924,118	15,406,037
Investments available for sale	5	15,807,398	14,182,441
Loans and advances	6	10,128,595	12,710,182
Investment in an associate	7	-	3,136,190
Investment in unconsolidated subsidiaries	9	47,920	36,546
Other assets	10	15,883,937	2,488,951
Intangible assets	11	12,613,766	12,613,766
Equipment	12	1,013,965	992,730
TOTAL ASSETS		81,106,319	65,066,837
LIABILITIES AND EQUITY			
LIABILITIES			
Loans from banks and financial institutions	13	31,408,977	17,471,275
Accounts payable and other liabilities		6,958,217	4,449,724
TOTAL LIABILITIES		38,367,194	21,920,999
EQUITY			
Share capital	14	17,651,898	14,643,956
Treasury shares		(5,084,070)	(1,925,212)
Share premium		394,921	237,841
Statutory reserve		4,902,076	4,003,979
General reserve		4,469,970	3,571,873
Retained earnings		14,213,065	14,552,803
Fair valuation reserve		1,915,498	6,250,171
Foreign currency translation reserve		(3,180)	11,754
Treasury shares reserve		1,735,136	1,734,683
Share options reserve		596,963	7,810
Equity attributable to equity share holders of the Company		40,792,277	43,089,658
Minority interest		1,946,848	56,180
TOTAL EQUITY		42,739,125	43,145,838
TOTAL LIABILITIES AND EQUITY		81,106,319	65,066,837

The notes set out on pages 15 to 33 form an integral part of these consolidated financial statements.



Hamed Saleh Al-Saif
Chairman & Managing Director



Nasser Barak Al Mutair
Vice Chairman

Auditors' Report

Independent to the Shareholders of Kuwait & Middle East Financial Investment Company K.S.C.C.

We have audited the accompanying consolidated financial statements of Kuwait and Middle East Financial Investment Company K.S.C.C. ('the Company') and its subsidiaries (together referred to as 'the Group') which comprise the consolidated balance sheet as at 31 December 2006 and the consolidated statement of income, consolidated statement of changes in equity and consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes. The consolidated financial statement of the Group as at and for the year ended 31 December 2005 were audited by Bader & Co. PricewaterhouseCoopers jointly with another auditor. Their report dated 5 February 2006 expressed an unqualified opinion.

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. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

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

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as of 31 December 2006 and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted for use by the State of Kuwait.


Report on other Legal and Regulatory Requirements

Furthermore, in our opinion proper books of accounts have been kept by the Company and the consolidated financial statements, together with the contents of the report of the Board of Directors relating to these consolidated financial statements, are in accordance therewith. We further report that we obtained all the information and explanations that we required for the purpose of our audit and that the consolidated financial statements incorporate the information that is required by the Kuwait Commercial Companies Law of 1960, as amended, and by the Company's Articles of Association; that an inventory was duly carried out; and that, to the best of our knowledge and belief, no violation of the Kuwait Commercial Companies Law of 1960, as amended, or of the Articles of Association have occurred during the year ended 31 December 2006 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 examination, we have not become aware of any material violations of the provisions of Law No. 32 of 1968, as amended, concerning currency, the Central Bank of Kuwait and the organisation of banking business, and its related regulations, during the year ended 31 December 2006.



Bader A. Al Wazzan
License No.62-A
Pricewaterhouse Coopers



Safi Al-Mutawa
License No. 138-A
of KPMG Safi Al-Mutawa & Partners
Member firm of KPMG International

31 January 2007
Kuwait

Consolidated Financial Statements
& Independent Auditors' Report
for the year ended 31 December 2006

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all of KMEFIC's subsidiaries in the region, and subsequently the Treasury team has expanded in 2006.

In 2006, KMEFIC launched Al-Awsat USD Money Market Fund, and Amwal Money Market Fund (Shari'a compliant). In addition to Al-Awsat KD Money Market Fund, all three Money Market Funds took the lead amongst all similar funds in the local market returning the highest yields.

Corporate Finance

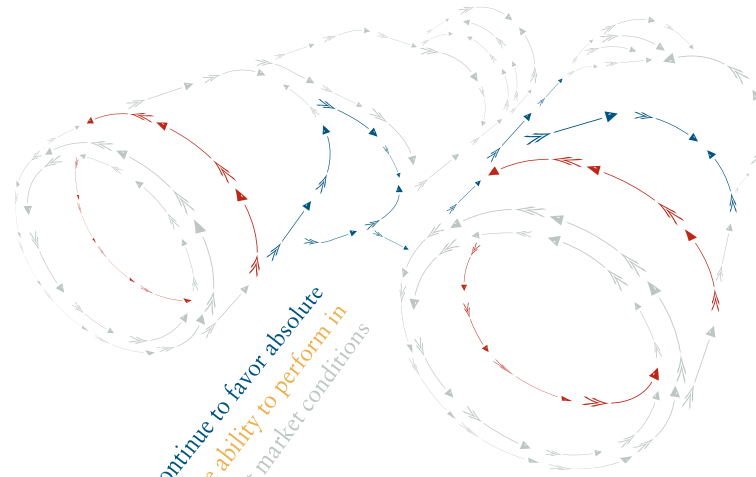
KMEFIC has re-established its Corporate Finance & Advisory Division (CFD) during the year to provide a wide range of value added services to our clients across the Region. The division is staffed by highly qualified, experienced and skilled professionals. The focus areas of Corporate Finance Division initially would be:

- Fund raising & management of debt and equity issues through public and private placement.
- Mergers and acquisitions advisory and due diligence
- Advisory on privatization and divestment
- Advisory on infrastructure projects
- Corporate Advisory & Business valuation
- Fund raising through structured finance transactions

With the robust economic growth being witnessed in the Region we expect the Corporate Finance Division to contribute substantially to the fee based revenue in the future in addition to providing strategic inputs to other divisions of the Company. Within a short span of time, the Division was successful in securing select mandates for Advisory and fundraising assignments including one from a multi-national corporation and prospecting several more mandates, the results of which are expected to materialize in the coming financial year(s).

Research

In line with our expansion of the brokerage operations and enhancing value added client services, the research team was strengthened during the year to focus on the sell-side, generate superior investment ideas and initiate company and sector coverage in other GCC countries. The sell-side reports published during the year have been widely appreciated by the market participants for their timeliness, common sense analysis and brevity. Moving ahead, the strategy is to differentiate and carve a niche for research in a crowded market place by (1) resisting the institutional imperatives (2) relentlessly focusing on the process rather than the outcome and (3) delivering uncompromising quality. Also, we plan to further expand the team so as to bring breadth and depth to the research function.



Our asset allocation will continue to favor absolute return investments that have the ability to perform in most market conditions

Closing thoughts and outlook

Given the underlying strength in the Kuwaiti economy, attractive market valuations and post the corrections in most GCC markets, we believe the worst is behind us. Moving away from the regional markets, we believe that international equity markets have the ability to perform well during 2007. This outlook also has an element of caution built in to it, as our assessment of global equities includes a degree of volatility that could be high at certain times. As such, our asset allocation will continue to favor absolute return investments that have the ability to perform in most market conditions. We will also focus on economies and sectors that have a compelling risk/reward profile such as the high growth economies of Asia & the sectors that are natural beneficiaries of high global liquidity and consumption. Furthermore, our strategy to grow our assets under management and enhance our product offerings also takes these assumptions in to account.

Finally, I would like to express my deepest gratitude and appreciation to KMEFIC's management and staff for their continued commitment and dedication that enabled the company to achieve its goals and objectives and to maintain its status as one of the leading Investment companies in Kuwait.

Hamed Saleh Al-Saif
Chairman & Managing Director

Due to their efficiency in decreasing market impact risk, the Futures transactions volume increased significantly since the establishment of the Waad's Futures Trading in June 2004. Recently, the Kuwait Stock Exchange increased the margin payment on forward contracts to 40%, and also increased the interest rates on forward contracts to 13%.

In our quest to introduce new products and services in the Kuwait Stock Exchange that aim to diversify and reduce risk for investors, we have introduced Shari'a compliant Forward / Futures products advised by an external Sharia Board.

International Investments

Global stock markets performed remarkably well in 2006 driven by global liquidity, robust growth in corporate earnings, a boom in mergers and acquisitions, weakening energy prices (in the second half of the year) and a relatively healthy global economy. This strong showing was noteworthy given a backdrop of concerns that included heightened geopolitical tensions in the Middle East and claims of successful nuclear weapon tests in North Korea and a sharp mid year market correction. None of these concerns were able to dampen investor sentiment as stock markets trended higher to record sizeable gains for the year. Moreover, liquidity was abundant despite the fact that the world's leading central banks were in a tightening mode. The US Federal Reserve continued to increase interest rates four times before pausing at 5.25 percent in August. Additionally, the European Central Bank also increased interest rates four times, and even Japan ended its zero interest rate policy. Collectively, the MSCI World Index gained 13.5 percent (in local currency terms) for the year.

Despite a shift in leadership in the US congress (where the Republicans lost their majority in the midterm elections), a weakening dollar and severe set-backs in the auto and home-building industries, US equities were driven higher. This was a result of strong domestic consumer spending, global growth (which helped US multinationals) and the ability of buyout firms to raise billions of dollars to take a significant number of companies private. European stock markets also ended the year with noteworthy gains as the region enjoyed sustained recovery and investor sentiment was high. Elsewhere in Asia, Japan's stock market performance was disappointing for the year as it lagged both the developed as well as emerging markets. Despite a healthy rate of unemployment and modest wage gains, Japanese consumers appeared to have been reluctant participants in the Japanese economic recovery. As for the emerging stock markets, they continued to attract sizeable inflows from foreign investors. Emerging giants such as China and India accelerated their economies

with a combination of domestic demand and overseas trade, while commodity dependant countries like Russia, Brazil and Venezuela, benefited from higher commodity prices, which resulted into significant stock-market gains.

Our International Investments portfolio was well placed to react to the year's events and outcomes. Our cautiously optimistic stance that carried over from the previous year combined with an overlay of tactical asset allocation was quite rewarding as it afforded our portfolio significant upside participation with negligible draw-downs. We were also able to reap the benefits of our continued bullish stance towards the emerging markets (particularly the Indian equity markets). These markets delivered impressive gains outpacing the returns offered by more mature markets. Our conviction towards these markets remains intact for the year to come, and we intend to take further advantage of these high growth economies.

Information Technology & Online trading

In the midst of weak and falling regional markets, KMEFIC's Online Trading with its flagship product alawsat.com generated considerable profits during 2006. We completed the white labeling for Ahlibank Qatar and successfully tested the FIX Hub using Reuters ROR. Moreover during 2006, the division successfully embarked on the project to implement IVR for customer service. Apart from these projects, major updates were carried out on the existing Hardware and Software. During the year, the division was able to establish a trading route for large banks and institutional clients in the regional markets.

We continue to pursue our vision of translating technological innovations into profitable ventures and strive to attain profitability by harnessing the current potential of technology for new and diversified services and products for tomorrow.

Going forward we aim to establish connectivity with Egypt, Jordan, Qatar, and Bahrain Stock exchanges in 2007 as well as to launch trading on ARABEX in Egypt. Plans are in place to establish an algorithm trading engine to supplement the existing trading platform to service institutional clients. We foresee a huge potential in targeting Institutional clients from outside the region and are working towards the same to achieve our objectives.

Treasury

Focused Treasury operations helped maximize the interest income and reduce KMEFIC'S over all cost of funds during the year. Furthermore, the Treasury business expanded to cover

Though the total income grew by 7%, operating expenses rose much faster by 39.7% during the year to KD 9.18 million over the previous year mainly on account of higher staff expenses and other operating expenses. These expenses need to be viewed in line with our completed expansions during the year and the benefits of which will ensue in the coming years. A combination of the above factors helped the company achieve a net profit of KD 8.75 million lower by 13.9% compared to KD 10.16 million in 2005. This translated into diluted earnings per share of 50.32 Fils in 2006 compared to 58.36 Fils in 2005.

The annual general assembly of the shareholders held on 12 March 2001 approved a stock option plan for employees (2001 Plan). In accordance with the plan, the Board of Directors of the company is authorized to grant up to 6,037,500 shares as stock options to the employees. The period over which the employees could exercise the stock options were extended up to March 2011. As of 31 December 2006, the number of stock options outstanding stood at 440,906.

The annual general assembly of the shareholders held on 20 March 2006 approved a second stock option plan for employees (2006 Plan). In accordance with the plan, the Board of Directors of the company is authorized to grant up to 3,773,880 shares as stock options to the employees. Employees could exercise the stock options till June 2011. As of 31 December 2006, the number of stock options outstanding stood at 2,982,376.

The Company accounted for the stock option expenses granted (after 20 March 2006) amounting to KD 589,153. These amounts have been charged to consolidated statement of income with a corresponding credit to the stock options reserve in the shareholders equity.

Brokerage Operations

In 2006, the commission income remained the highest contributor to KMEFIC's total income, driven mainly by online trading (alawsat.com) and the brokerage operations in Kuwait, UAE and Oman represented by our subsidiaries: Middle East Financial Brokerage Company (MEFBC) and Middle East Brokerage Company (MEBC) respectively. These two companies that were set up during 2005 are now wholly owned subsidiaries, and have well complemented our online trading business and further helped KMEFIC to diversify its income stream.

In this respect, this year saw the addition of new subsidiaries in Bahrain, Jordan, Egypt (all fully owned), and Saudi Arabia (30% stake), where the brokerage operations are expected to commence in 2007. At the closing of 2006, KMEFIC's brokerage operations in Kuwait occupied the first position with around 16% market share measured by three key parameters : number of trades, volume and value traded.

Local and Arabian Investments

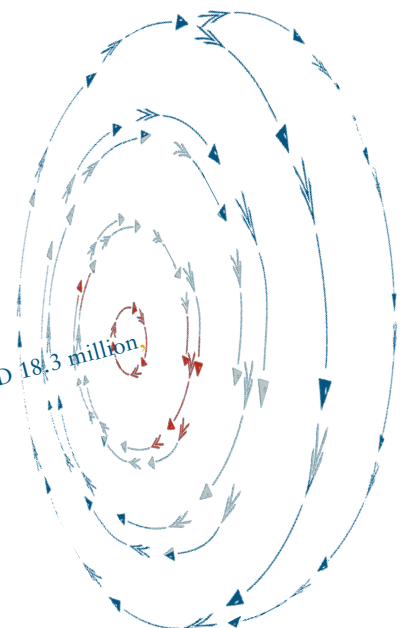
Our discretionary portfolios returned (4.86%) (weighted average returns) during 2006, outperforming the KSE weighted index that achieved (5.43%) returns during the same period. Moreover, the total assets managed by the division stood at KD 846 million (USD 2,926 million) higher by 13.6% compared to KD 744 million (USD 2,575 million) in 2005. KMEFIC's local equity fund (Al-Rouyah Fund), achieved a return of (0.4%) during 2006 and a 178.2% return since inception.

Furthermore, in August 2006, we introduced KMEFIC's G.C.C equity fund (Gulf Gate Fund), 30% of which will invest in the Kuwait Stock Exchange and 70% in various Gulf markets. The division has succeeded in marketing the fund locally and regionally, and consequently the fund has started trading in November 2006.

Local Financial Derivatives

The Local Financial Derivatives portfolio "Waad" recently completed its ninth year of operations. "Waad" being a service which allows investors to trade select Kuwait Stock Exchange listed securities on a forward basis of three, six, nine or twelve month maturity dates. The "Waad" portfolio includes companies representing the majority of the Kuwaiti economy sectors such as the banking, investment, real estate, industry, food and services.

Despite a tough and challenging year the company achieved a total income of KD 18.3 million a 7% increase compared to KD 17.1 million in the previous year.



Chairman's Message

Dear Shareholders,

The Kuwait Stock Exchange after witnessing an unprecedented five year bull-run since 2001 came to a pause in the beginning of 2006. During the period 2001-2005, the KSE Price Index registered a compounded annual growth of 61% while the KSE Weighted Index grew by 44%. As of the end of 2006, the KSE Price Index stood at 10,067 down by 1,378 points and lower by 12% compared to the previous year, while the Weighted Index closed at 532 down by 30 points and lower by 5.4% over the same period. Negative returns during the year were largely attributed to oil prices retracing from their historic highs, lag effect of higher interest rates, higher inflation driven by excessive liquidity, slow down in corporate sector earnings growth, geo-political tensions in the region and most importantly the negative sentiment held by the investment community as a result of the selling pressure seen in the neighboring GCC markets.

Amongst the GCC markets, the worst performing markets during the year 2006 were Saudi Arabia (down 52.5%), Dubai (down 44.4%), Abu Dhabi (down 42.3%) and Qatar (down 35.5%). These markets witnessed a sharp correction from their peaks as the valuations were overstretched in relation to the underlying fundamentals and the earnings power of the corporate sector. Though the KSE also closed in the red; the underperformance was modest compared to the other GCC markets. Oman was the best performing market and closed higher by 14.5% compared to the previous year while Bahrain was marginally up by 1%.

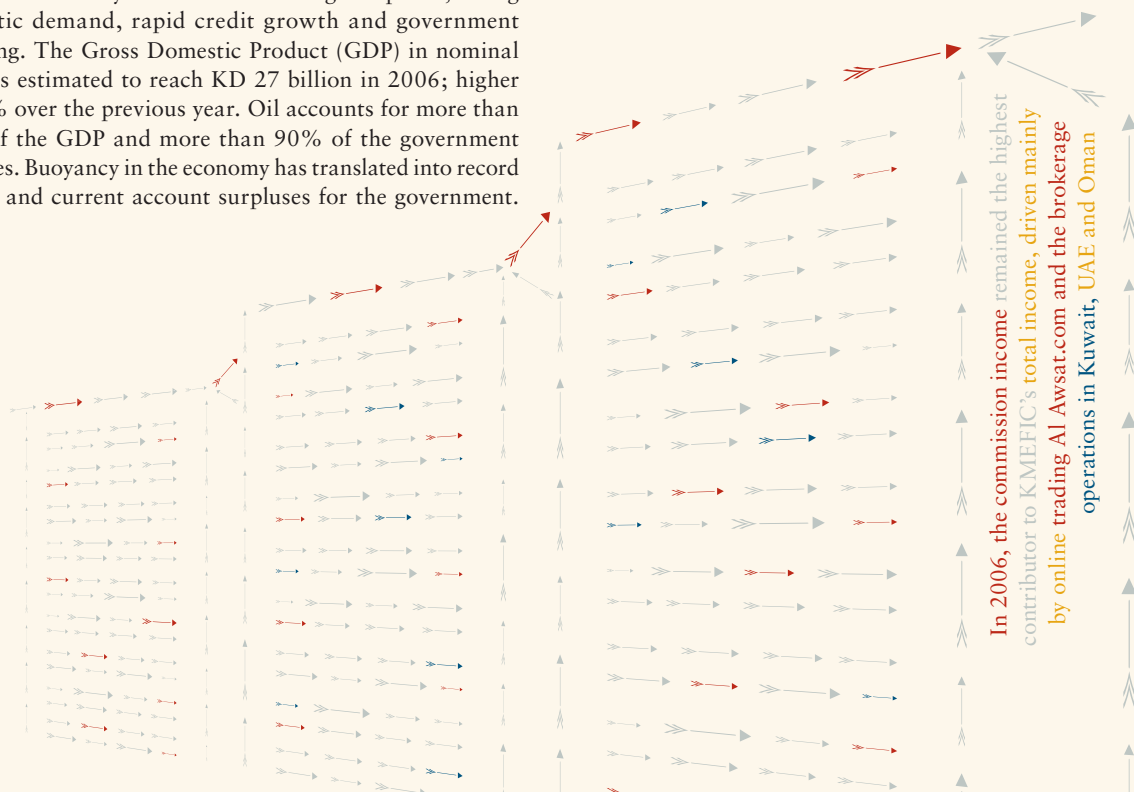
The macro-economic fundamentals of the Kuwaiti economy continue to be buoyant on the back of high oil prices, strong domestic demand, rapid credit growth and government spending. The Gross Domestic Product (GDP) in nominal terms is estimated to reach KD 27 billion in 2006; higher by 15% over the previous year. Oil accounts for more than 50% of the GDP and more than 90% of the government revenues. Buoyancy in the economy has translated into record budget and current account surpluses for the government.

The Central Bank of Kuwait (CBK) increased the discount rate by 25 basis points to 6.25% during the year.

Company's performance

Despite a tough and challenging year for the Kuwaiti capital markets, KMEFIC's performance has been satisfactory. In 2006, the company achieved a total income of KD 18.3 million higher by 7% compared to KD 17.1 million in the previous year. During the year, the key drivers for the growth in income were attributed to the commission income at KD 6.14 million (higher by 3% compared to KD 5.96 million in the previous year) constituted around 34% of the total income. This is followed by the management fees at KD 4.34 million (higher by 17.3% compared to KD 3.7 million in the previous year) constituted around 24% of the total income. Gains on disposal of Available For Sale (AFS) investments at KD 4.4 million (higher by 478% compared to KD 0.76 million in the previous year) constituted 24% of the total income while the interest income at KD 1.85 million (higher by 116% compared to KD 0.85 million in the previous year) constituted 10% of the total income.

Growth in management fees was mainly attributed to the increase in the assets under management in 2006 which was higher by KD 166 million or 14% to reach KD 1,362 million (USD 4,709 million) compared to KD 1,196 million (USD 4,097 million) in 2005. Though the margin loans to customers were lower at KD 10.2 million in 2006 compared to KD 12.9 million in the previous year, higher spreads on the margin loans and higher interest rates on term deposits translated into a sharp growth in interest income during the year.



General Management



Hamed H. Al-Sanee
Chief Executive Officer



Osama R. Al-Armaly
General Manager
Local & Arabian Investments



Adel F. Al-Humaidhi
General Manager
Local Financial Derivatives



Abdulmohsen A. Qarooni
General Manager
IT & Online Trading



Mohammed A. Al-Marzook
General Manager
International Investments



Hisham K. Hayat
General Manager
Brokerage



Rana Y. Al-Tharban
Assistant General Manager
Marketing / Client Relations



Christy I. Kulathrooran
Assistant General Manager
Finance and Operations



Mohammed S. Al-Saleh
Assistant General Manager
Treasury



Maha Mansour
Senior Manager - Human
Resources & Administration



Vijay Rabindranath
Senior Manager
Research



S. Kasiraman
Manager
Corporate Finance

Board of Directors



Hamed S. Al-Saif
Chairman & Managing Director



Nasser B. Al-Mutair
Vice Chairman



Michael Collis
Board Member



Hamad A. Al-Marzouk
Board Member



Hasan Y. Behbahani
Board Member



Adel Ellabban
Board Member



Tareq Z. Zuaiter
Board Member



H.H. Sheikh Nawaf Al-Ahmad Al-Jaber Al-Sabah
Crown Prince of the State of Kuwait



H.H. Sheikh Sabah Al-Ahmad Al-Jaber Al-Sabah
Amir of the State of Kuwait



H.H. Sheikh Nasser Al-Mohammed Al-Ahmed Al-Sabah
Prime Minister of the State of Kuwait

Notes to the Consolidated Financial Statement Continued

Year ended 31 December 2006

27- SEGMENT REPORTING

Business segments

The Group operates in the following distinguishable business segments. These business segments form the basis on which the Company reports its primary segmental information.

- International Investments, which is engaged in carrying out investment activities for own account and for clients, in international markets;
- GCC Market Investments, which is engaged in carrying out investment activities for own account and for clients, in the Kuwaiti and GCC markets; and
- Broking, which is engaged in broking and on-line trading for own account and for clients in international and local markets.

Financial information about business segments for the year ended 31 December 2006 and 31 December 2005 are set out below:

	Kuwaiti Dinars							
	International Investments		GCC Markets		Broking		Total	
	2006	2005	2006	2005	2006	2005	2006	2005
Segment revenue	1,239,811	1,147,428	8,698,923	8,802,670	5,941,661	6,227,074	15,880,395	16,177,172
Segment expenses	778,408	835,157	1,891,510	1,617,228	4,285,534	3,214,720	6,955,452	5,667,105
Segment result	461,403	312,271	6,807,413	7,185,442	1,656,127	3,012,354	8,924,943	10,510,067
Unallocated Revenues							2,430,046	949,796
Unallocated Expenses							2,744,787	1,291,373
Profit for the year							8,610,202	10,168,490
Segment assets	15,185,586	9,157,956	30,812,790	24,115,958	16,342,700	16,626,652	62,341,076	49,900,566
Unallocated assets							18,765,243	15,166,271
Total assets							81,106,319	65,066,837
Segment liabilities						1,469,493		1,469,493
Unallocated liabilities							38,367,194	20,451,506
Total liabilities							38,367,194	21,920,999
Capital expenditure					8,905	548,443	8,905	548,443
Unallocated capital expenditure							317,212	224,398
Total capital expenditure					8,905	548,443	326,117	772,841
Depreciation							130,035	141,358
Unallocated depreciation							(130,035)	123,012
Total depreciation							-	264,370
Impairment loss recognised in statement of income	14,964	122,902					14,964	122,902
Income from unconsolidated subsidiaries	5,059	336					5,059	336

Geographical segments

Apart from its main operations in Kuwait, the Group also operates through its foreign subsidiaries in UAE and Oman. The Group's assets relate to different geographical areas of the world. The carrying amount of the Group's assets and liabilities by geographical area are presented in note 24 to the consolidated financial statements.

Notes to the Consolidated Financial Statement Continued

Year ended 31 December 2006

28- ASSETS DENOMINATED IN FOREIGN CURRENCIES

As at the balance sheet date the Group had the following significant net asset exposures denominated in foreign currencies:

	2006 (KD)	2005 (KD)
US Dollars	76,620	11,470,870
GCC Currencies	5,545,843	2,711,297
Other	143,091	184,459
	<u>5,765,554</u>	<u>14,366,626</u>

29- COMPARATIVES

Certain comparative figures have been regrouped to conform to current year classification. Such re-classification has not affected the previously reported profit or equity.