

**BUILDINGSUCCESS**  
ANNUAL REPORT 2006



Khaleeji  
Commercial  
Bank

بِسْمِ اللَّهِ الرَّحْمَنِ الرَّحِيمِ



**H.H. Shaikh Khalifa Bin  
Salman Al Khalifa**

The Prime Minister



**H.M. King Hamad  
Bin Isa Al Khalifa**

The King of Bahrain



**H.H. Shaikh Salman  
Bin Hamad Al Khalifa**

The Crown Prince and  
Commander-in-Chief of the  
Bahrain Defence Force



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**Khaleeji Commercial Bank BSC (c)**

Al-Zamil Tower, Government Avenue  
PO Box 10006, Manama  
Kingdom of Bahrain  
Telephone: (+973) 17 505 050  
Facsimile: (+973) 17 500 288  
E-mail: [info@khcbonline.com](mailto:info@khcbonline.com)

[www.khcbonline.com](http://www.khcbonline.com)


## PROFILE

Established in November 2004 with a paid-up capital of BD30 million, Khaleeji Commercial Bank (KHCB) is an Islamic private bank, headquartered in the Kingdom of Bahrain, and operating under a retail Islamic banking licence granted by the Central Bank of Bahrain (CBB).

The Bank is a wholly-owned subsidiary of Gulf Finance House (GFH) and has the objective of widening the activities and enhancing the shareholder and client value of the GFH Group.

Khaleeji Commercial Bank offers a comprehensive range of innovative banking and investment products and services to high net worth individuals, corporate entities, and financial institutions. These include commercial and corporate banking, wealth management, structured investment products, and project financing facilities.

The Bank seeks to expand its network of strategic alliances with other financial institutions and business partners to source new and mutually beneficial investment and financing opportunities.



**VISION** To be a leading domestic and regional Islamic bank, providing unique, innovative and high quality Shari'a-compliant products, services and investment opportunities for our clients.

**MISSION** To participate in the economic development of Bahrain, GCC and the MENA region, maximising client and shareholder value in accordance with the principles of Shari'a, contributing towards the growth of Islamic banking, and providing a challenging environment to our employees to be innovative and realise their professional objectives.

**VALUES** The Bank will empower its clients, creating long-term relationships with them; provide the best service available; respond to clients' different needs and demands; provide superior products and services; and use market knowledge and investment prowess to achieve our clients' business objectives.

## BOARD OF DIRECTORS



Dr. Fuad Abdulla Al-Omar  
Chairman



Mr. Esam Yousif Janahi  
Vice Chairman



Mr. Buti Khalifa Al-Flasi  
Director



Mr. Yousif Mohammed  
Khayat, Director



Mr. Abdul Latif Abdulla  
Al-Meer, Director



Mr. Samir Yaqoob Al-Nafisi  
Director



Mr. Waleed A. Rahman  
Al-Rowaih, Director



## SHARI'A SUPERVISORY BOARD

Khaleeji Commercial Bank is guided by a Shari'a Supervisory Board consisting of three distinguished scholars. This Board reviews the Bank's activities to ensure that all products and investment transactions comply fully with the rules and principles of Islamic Shari'a.

**Dr. Fareed Yaqoob Al Miftah  
Chairman**

Member of the Supreme Council of Islamic Affairs, Undersecretary of the Ministry of Islamic Affairs, Kingdom of Bahrain; former Judge of the High Sharia'a Court, Lecturer, University of Bahrain; PhD from the University of Edinburgh, United Kingdom.

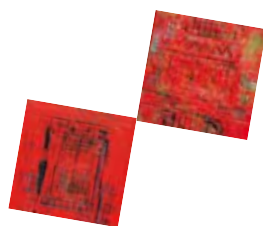
**Dr. Fareed Mohammed Hadi  
Executive Member**

Assistant Professor at the College of Arts, Department of Arabic and Islamic Studies, University of Bahrain; PhD in Ibn Hazm's Methodology of Jahala, Edinburgh University, UK; PhD in Al-Bukhari's Methodology, University of Mohammed V, Morocco; member of Shari'a Supervisory Boards of a number of Islamic banks.

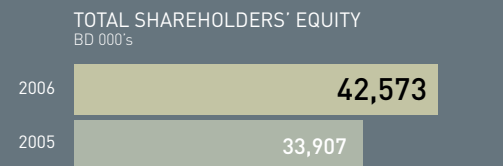
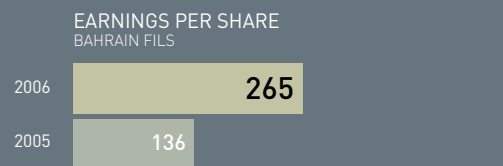
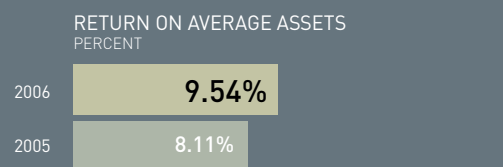
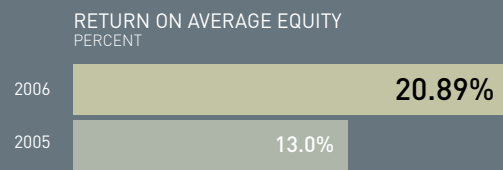
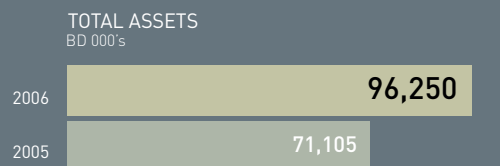
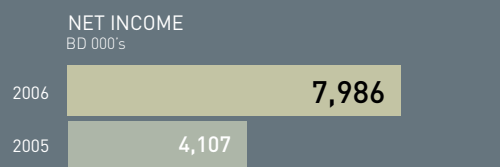
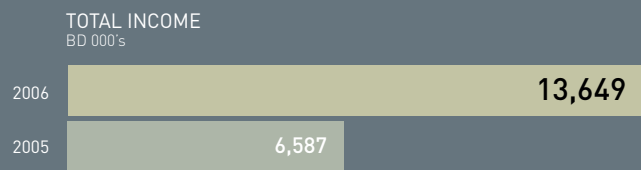
**Shaikh Nizam Mohammed Saleh  
Yaqoobi**

**Executive Member**

Executive Member of Shari'a Supervisory Board, Abu Dhabi Islamic Bank; member of Shari'a Supervisory Boards of Bahrain Islamic Bank and Shamil Bank; Board Member of Dow Jones Islamic Index; Member of Shari'a Supervisory Boards of a number of Islamic banks.



# FINANCIAL HIGHLIGHTS



## **INVESTMENT VEHICLES:**

GULF-GERMAN RESIDENCES

AMLAK II

SUROOH

AL-HARETH FRENCH PROPERTY FUND

EQARAT AL-KHALEEJ

## **PROJECT INVOLVEMENT:**

BAHRAIN FINANCIAL HARBOUR

BAHRAIN LAGOON

ORYX HILLS (AL AREEN, BAHRAIN)

ROYAL UNIVERSITY FOR WOMEN (BAHRAIN)

THE ROYAL METROPOLIS (JORDAN)

## CHAIRMAN'S STATEMENT

### **In the name of Allah, the Beneficent, the Merciful, Prayers and Peace upon the Last Apostle and Messenger, Our Prophet Muhammad.**

On behalf of the Board of Directors, it is my pleasure to present the annual report of Khaleeji Commercial Bank (KHCB) for the year ended 31 December 2006. I am delighted to report that this proved to be a most blessed second year of operations for the Bank. Strong financial results, key business achievements, and significant organisational developments underline our successful implementation of the Bank's ambitious and aggressive strategic objectives during 2006.

The Bank posted an excellent financial performance in 2006, with substantial gains over the previous year. Total income more than doubled to BD 13.6 million compared to BD 6.6 million in 2005, while net profits increased by 94.5 percent from BD 4.1 million to BD 8 million in 2006. At the year-end, total assets stood at BD 96.2 million (2005: BD 71.1 million) with shareholders' equity amounting to BD 42.6 million (2005: BD 33.9 million). Basic earnings per share grew two-fold to 265 fils compared to 136 fils the previous year. Key ratios also improved, with return on average assets at 9.54 percent (2005: 8.11 percent), return on capital at 26.5 percent (2005: 13.6 per cent) and return on average equity at 20.9 percent (2005: 13 percent).

Key business achievements by the Bank during the year include providing project finance and corporate financing facilities; launching a

number of new investment products, and completing our first investment exit of Amlak. In addition, the real estate investment products launched by the Bank in 2005 (Al Hareth French Property Fund and Eqarat Al Khaleej) continued to perform well. Furthermore, the Bank continued during 2006 its active participation in prestigious regional Sukuk issues, with a total commitment of US\$ 20 million.

The Bank's strategic developments included the opening of the new branch at Al-Zamil Tower, the implementation of a new dedicated core banking system and the issue of ATM cards. In addition, plans were finalised for the introduction in 2007 of new retail products and the launch of Internet and SMS banking services. The Bank will also lease a number of floors at Bahrain Financial Harbour where the offices of Management and staff will be relocated. Furthermore, the Bank will retain its existing branch at Al Zamil building and open a new branch in the Financial Mall at Bahrain Financial Harbour.

A most significant strategic development during the year was our decision to introduce a new name and corporate identity for the Bank. The re-branding is designed to differentiate the Bank in the increasingly competitive banking sector by emphasising our focus on the region and our commitment to provide innovative Shari'a-compliant commercial banking products and services for our clients. As a more autonomous commercial banking subsidiary of Gulf Finance House, we will be better able to carve out a distinctive niche in our particular

market segments, while continuing to widen the overall activities of the Group and enhance shareholder and client value.

In line with the re-branding and strategic market repositioning of the Bank, we took a number of important steps during 2006 to strengthen our organisational structure and enhance our institutional capability. These include the successful recruitment of well qualified and experienced professionals to fill key management and specialist positions, and the development of the Bank's corporate governance, risk management and compliance framework, and corporate policies and procedures.

As a result of these significant achievements during 2006, KHCB is better positioned and equipped to achieve its vision of being a leading domestic and regional Islamic commercial bank, providing unique, innovative and high quality Shari'a-compliant products, services and investment opportunities for our clients.

To support our strategic repositioning, during 2006 we obtained approval to increase the Bank's capital and widen our shareholding base. We also entered into discussions with the Central Bank of Bahrain to expand our existing licence, in order to be able to offer additional retail banking products and services, thereby widening our offering to clients and also diversifying our risk. At the same time, we reviewed our investment strategy with the aim of broadening our geographic and industry focus to build upon our traditional strengths in the GCC real estate and property development sector.

At the same time, we take very seriously our corporate social responsibility to contribute to the social and economic well-being of Bahrain and its citizens, and to support the growth and development of the Islamic banking and finance industry.

These excellent results were achieved against a very positive regional economic and business environment. The Kingdom of Bahrain witnessed strong growth in 2006 accompanied by a healthy rise in per capita gross domestic product and a significant fall in inflation.

The entry of many new conventional and Islamic financial institutions during the year, together with initiatives by the Central Bank of Bahrain such as the modified banking licensing framework, will provide a more competitive banking environment and will reinforce the status of Bahrain as the pre-eminent financial centre and Islamic hub of the Middle East. The real estate development sector also continued to flourish, with excellent progress being made by existing landmark projects such as Bahrain Financial Harbour, while new groundbreaking projects such as Bahrain Investment Wharf, were announced.

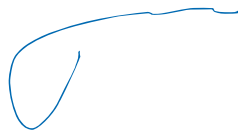
Such ongoing enhancement of Bahrain's reputation, coupled with the robust economic and business outlook for the GCC region, will unveil additional business opportunities to support the growth and development of Khaleeji Commercial Bank. The Board has every confidence in the Management's ability to build upon

these in order to sustain profitability and growth in 2007 and beyond, and to maximise returns for our shareholders and clients.

On behalf of the Board of Directors, I would like to express my gratitude to His Majesty the King, His Highness the Prime Minister, and His Highness the Crown Prince and Commander-in-Chief of the Bahrain Defence Force, for their wise and inspired leadership of the Kingdom of Bahrain, and for their encouragement for the growth of the private sector and the development of the banking and finance industry. I also extend my thanks to all Government ministries and the Central Bank of Bahrain for their continued guidance and support.

Special appreciation is due to our shareholders, clients and business partners for their ongoing confidence and loyalty; and to the Bank's management and staff for their hard work and dedication.

**Allah the Almighty is the Purveyor of All Success.**



**Dr. Fuad Abdulla Al-Omar**  
Chairman



Dr. Fuad Abdulla Al-Omar



THE BANK INTRODUCED A  
NEW NAME AND CORPORATE  
IDENTITY TO EMPHASISE OUR  
COMMITMENT TO PROVIDE  
INNOVATIVE SHARI'A-  
COMPLIANT SERVICES

# MANAGEMENT REVIEW

I am delighted to report that during 2006, the Bank continued to grow and expand its business operations and strengthen its institutional capability. During this period, we enhanced the range of commercial banking and investment products and services offered to high net worth individuals, financial institutions and corporate clients, and also further developed our organisational structure.

## Organisational developments

During 2006 we took a number of important steps which included the launch of our new identity and change of name from Gulf Finance House Commercial Bank to Khaleeji Commercial Bank. In addition, we relocated to new premises, and successfully recruited well qualified and experienced professionals to fill key management and specialist positions. Furthermore, the Bank implemented a new dedicated core banking system and made good progress in developing the Bank's corporate governance, risk management and compliance framework, and corporate policies, processes and procedures.

## Commercial banking

The Bank built upon its strong performance in 2005, successfully expanding its commercial banking client base by 80 percent, growing deposits by 65 percent, and increasing financing facilities by 468 percent.

Key developments include the opening of the new branch office at Al-Zamil Tower and the issue of ATM cards. In addition, plans were finalised for the introduction in 2007 of new retail products, the launch of Internet and SMS banking services, and the opening of a new branch in the Financial Mall at Bahrain Financial Harbour.

A major achievement during the year was the Bank's involvement in arranging financing for the US\$ 120 million Lagoon project in the Kingdom of Bahrain. The project is the first of its type in the Gulf, with commercial space previously only being offered on a rental basis. The Bank has also been appointed to provide mortgage facilities for end users.

## Investments

During 2006, the Bank launched three new investment companies, completed its first investment exit, provided structured finance and project financing facilities, and participated in a combined total of six regional Sukuk issues and financing syndications. In addition, the real estate investment funds that were launched by KHCB in 2005 continued to perform well.

## New investment companies

**Gulf-German Residences:** This Euro 154 million Investment Company was launched in February 2006 and closed in March 2006 in collaboration with Abu Dhabi Investment House, with the purpose of investing in a diversified portfolio of 100 income-producing residential properties in Germany. The anticipated annual cash yield is 10 percent being distributed quarterly, with an overall targeted internal rate of return (IRR) in excess of 14 percent over an expected tenor of five years.

**Amlak II:** This US\$ 39.35 million Investment Company was launched in November 2006. Amlak II offers investors the opportunity to invest in plots of land in the Kingdom of Bahrain. The targeted return on investment (ROI) is 13 percent per annum over an expected two-year investment tenor.

**Surooh:** Launched in November 2006, this BD 14.2 million Investment Company has the purpose of investing solely in the Oryx Hills residential project and Bahrain Investment Wharf industrial development project in the Kingdom of Bahrain. The targeted internal rate of return (IRR) is 17 percent over an expected three-year investment period.

## MANAGEMENT REVIEW

The Oryx Hills gated residential community forms part of the broader US\$ 1.2 billion Al Areen development project. Covering an area of approximately 140,000 square metres, the prestigious Oryx Hills master-planned development comprises luxury villas set amidst breathtaking natural surroundings.

### Investment exit

In November 2006, the Bank successfully completed its exit from the Amlak Al-Bahrain Fund. Amlak Fund was one of the first real estate-focused investment companies to be launched by KHCB during 2005. The US\$ 41 million Amlak Al-Bahrain Fund offered investors the opportunity to invest in a variety of plots of land in the Kingdom of Bahrain, providing investors with a total return of approximately 20 percent over an 18-month holding period, thus exceeding the expected investment return of 13 percent per annum.

### Structured finance and project financing facilities

The Bank participated in a US\$ 330 million five-year dual-tranche Murabaha financing facility for Dubai Financial, the 99 percent-owned subsidiary of Dubai Investment Group. The Bank also supported the Government's new public-private-

partnership (PPP) initiative, which is designed to encourage greater participation by the private sector in addressing the Kingdom's social and affordable housing needs.

The Bank is also involved in two major regional development projects, which were launched in 2005: the Royal University for Women (RUW) in the Kingdom of Bahrain, and the Royal Metropolis project in the Hashemite Kingdom of Jordan. RUW is the first private, purpose-built international university in the Gulf dedicated solely to educating women. The Bank is a strategic partner with Emirates Islamic bank, Amlak Finance and the Islamic Corporation for the Development of the Private Sector, to provide Musharaka financing for the construction of the university campus. The Bank was appointed lead financier for the US\$ 1.25 billion Royal Metropolis project, which comprises Jordan Gate and Royal Village in Amman.

### Sukuk issues

During 2006, the Bank continued its active participation in prestigious regional Sukuk issues, with a total commitment of US\$ 14.5 million. The Sukuks which the Bank participated in financed the following companies/projects: Qatar Real Estate Investment Company (Qatar), National Industries Company for Building Materials (Kuwait), Sharjah Islamic Bank (Sharjah), Kuwait Commercial Markets Complex Company (Kuwait), and the Lagoon City Project Development (Kuwait).

### Existing investment funds

#### Al Hareth French Property Fund:

Launched in 2005, this Euro 25 million income-producing fund focuses on commercial and industrial real estate in the Isle de France, Paris and other region of France. The Fund is performing to expectations, in line with the targeted cash yield of 9 percent with quarterly distributions, and an expected annual internal rate of return (IRR) in excess of 10 percent over a five-year tenor.

**Eqarat Al Khaleej:** This private equity investment company was established with the purpose of investing in income-generating properties across the GCC region. The private placement issue in 2005 received an enthusiastic response, closing with investor subscriptions exceeding US\$ 51 million. Eqarat Al Khaleej is performing to expectations, in line with the targeted cash yield of 9 percent with quarterly distributions, and an expected annual internal rate of return (IRR) of over 13 percent.

### Social responsibility

The Bank takes very seriously its corporate social responsibility to contribute to the well-being of the local community, and to support the growth and development of the Islamic banking and finance industry. Throughout 2006, we continued to provide financial assistance, in association with our parent company, GFH, for a number of charitable, medical, educational and cultural



organisations and other deserving causes, and encouraged the active participation of its staff in community activities in the Kingdom of Bahrain. In partnership with Gulf Finance House, the Bank provided major sponsorship for national motor racing icon, Hamad Al Fardan, who heads the Bahrain team in the Toyota Racing Series. This is designed to maximize the winning potential of the national racing champion whilst promoting Bahrain as the emerging hub of motor sport in the Middle East. The Bank also supported the development of Islamic banking through the Bahrain Institute of Banking and Finance (BIBF), and the Auditing & Accounting Organisation for Islamic Financial Institutions (AAOIFI).

#### Looking ahead

As a result of these significant achievements by the Bank during 2006, we are now strongly placed to achieve our ambitious and challenging plans for the future. These include expanding our regional presence, introducing new retail banking products, enhancing our investment activities, and forging new relationships with other financial institutions and business partners.



**Ebrahim Hussain Ebrahim**  
General Manager



Ebrahim Hussain Ebrahim

## CORPORATE GOVERNANCE

**As a subsidiary of Gulf Finance House (GFH), Khaleeji Commercial Bank (KHCB) is currently governed by the Group's corporate governance framework which seeks to balance entrepreneurship, control and transparency, while creating value for all stakeholders.**

Corporate governance – the way the Board and Management is organized and how they operate in practice – ultimately aims at leading the Bank towards successfully meeting its strategic objectives.

The Board of Directors is accountable to the Bank's shareholders for the creation and delivery of strong sustainable financial performance and long-term shareholder value. To achieve this, the Board approves and monitors the Bank's strategy and financial performance, within a framework of sound corporate governance and effective risk management.

Currently the Board of Directors consists of 7 members. The Chairman is responsible for leading the Board, ensuring its effectiveness, monitoring the performance of the GM, and maintaining a dialogue with the Bank's stakeholders. The Internal Audit function reports to the Audit Committee and also have access to the Chairman.

The Board currently has two committees and is in the process of setting up a third committee as detailed below.

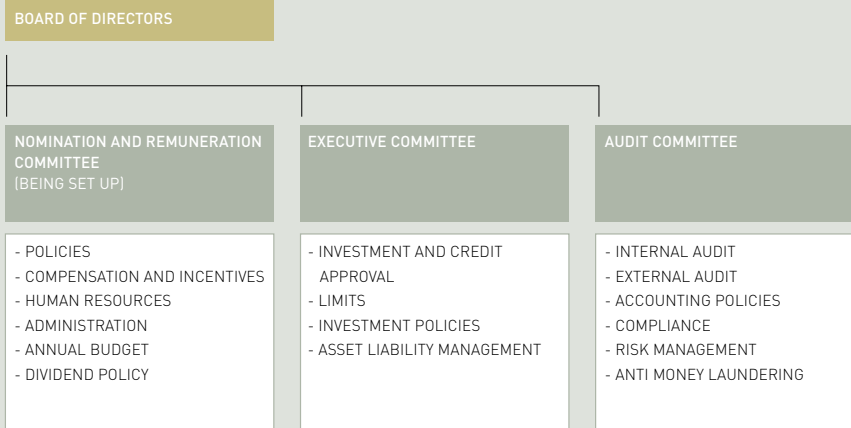
1. **Audit Committee**, which is responsible for internal and external audit, compliance, risk management and anti money laundering.
2. **Executive Committee**, which is responsible for investment and credit approval, setting limits and investment policies, asset liability management and maintaining banking relationships.
3. **Nominations & Remunerations Committee** ( being set up), which will be responsible for setting policies for compensation and incentives, human resources and administration. It will also be responsible for approval of annual budget, dividend policy and the capital expenditure of the Bank.

During 2006, the Board of Directors held 6 meetings, the Executive Committee held 3 meetings, and the Audit Committee held 2 meetings. The Board of Directors as well as its committees receives regular reports on various aspects of the Bank's business from senior management as well as internal audit, risk management, operations and finance.

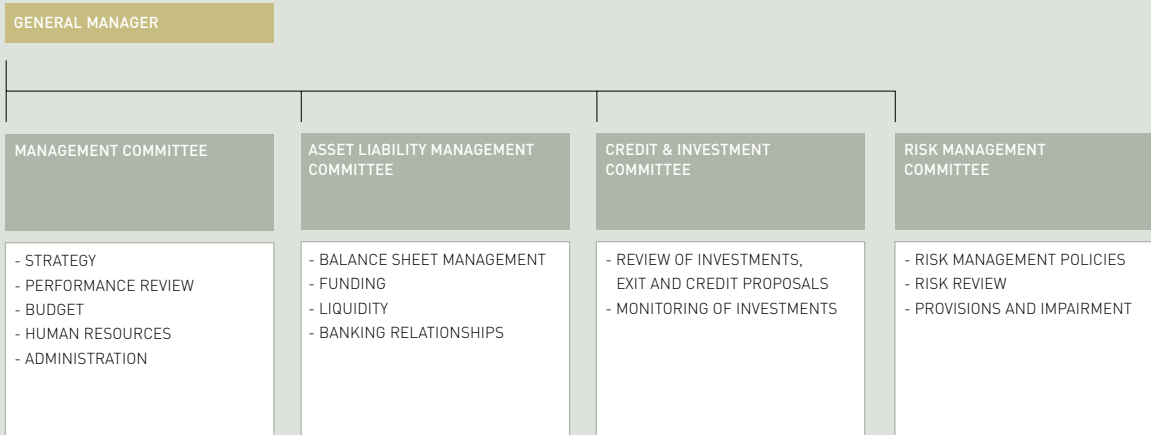
The Board of Directors delegates the authority for management of the business to the General Manager who uses a highly consultative approach through several general and specific cross functional committees.

KHCB is committed to continuously reviewing and developing its corporate governance standards to ensure compliance with the requirements of the revised corporate governance framework being implemented by the Central Bank of Bahrain, and also to keep abreast with international best practice.

BOARD COMMITTEES



MANAGEMENT COMMITTEES





KHCB Executive Management:  
 (from right to left)  
 Fuad Ali Taqi, Assistant General  
 Manager, Commercial Banking;  
 Dimitry Blasi, Executive Senior  
 Manager, Investment;  
 Mahdi A. Nabi, Executive Senior  
 Manager, Support Group (seated).



KHCB Investment Placement Team  
 members:  
 (from right to left)  
 Abdullah Buallay, Executive Senior  
 Manager, Investment Placement;  
 Mohammed Abdulrahman, Senior  
 Manager;  
 Khalil Al Za'abi, Senior Manager;  
 Abdulrahman Murad, Officer.

# RISK MANAGEMENT

**Risk is inherent in the Bank's business and effective management of that risk is seen as a core requirement to create shareholder value. The Board of Directors of the Bank has overall responsibility for establishing the Bank's risk culture and ensuring that an effective risk management framework is in place. The Board approves and periodically reviews the risk management policies and strategies of the Bank.**

The assumption of risks by the Bank is guided by the certain fundamental principles such as protection of investor and shareholder funds by adoption of sound credit and investment culture and prudent practices, adoption of effective 'risk reward' strategy to optimize stakeholders' returns, and adherence to prudent levels of total risk exposure and concentration, while focusing on the target market segments such as high net worth individuals, corporate and public sector clients and products which generate high profitability and growth.

The Risk Management Committee (RMC) consisting of the GM and Head of Risk Management, Head of Financial Control, Head of Business Services, Head of Commercial Banking and Head of Investment Banking is responsible

for implementing risk management policies, guidelines and limits, and for ensuring that monitoring processes are in place. The Risk Management department, together with the Internal Audit and Compliance departments, provides independent assurance that all types of risk are being measured and managed in accordance with the policies and guidelines set by the Board.

## **Risk policies**

The Bank's risk policies identify approval authorities, reporting requirements, and the procedures for referring risk related issues to executive management, RMC and the Board, as appropriate. Policies are in place to address the categories of reputation, liquidity, investment and credit, currency, operational, legal and regulatory risk, together with capital adequacy requirements.

## **Reputation risk**

Reputational risk is the risk that negative perception regarding the Bank's business practices or internal controls, whether true or not, will cause a decline in the Bank's investor base, lead to costly litigation and that could have an adverse impact on liquidity or capital of the Bank. The senior management through the relevant committees examines issues that are considered to have reputational repercussions for the Bank and issues guidelines to address these.

## **Liquidity risk and Capital Adequacy**

Liquidity Risk is defined as the risk that funds will not be available to meet liabilities as they fall due. The Asset and Liability Management Committee (ALCO), which is chaired by the GM and comprises senior executives of the Bank, has overall responsibility for managing the balance sheet and liquidity of KHCB. ALCO provides broad guidelines with regard to minimum liquid assets to be maintained and uses a maturity ladder approach for managing and monitoring the liquidity risk. It is the Bank's policy to keep a significant part of its assets in highly liquid assets such as short term murabahas and sukuks.

The Bank's capital adequacy ratio is calculated in accordance with the guidelines issued by the CBB and has policies in place for calculation, maintenance and monitoring of regulatory capital.

# RISK MANAGEMENT



## Investment and credit risk

The Bank has well defined policies for managing credit and investment risks. These include delegated approval authority limits, concentration limits, maximum exposure limits, and counter-party limits. Credit and Investment limits are approved after thorough assessment of credit and investment risks.

KHCB controls and manages credit risk by monitoring credit exposures, limiting transactions with specific counter-parties, and continually assessing the creditworthiness of counter-parties as well as through diversification of financing and investment activities. In addition, every investment and credit application is reviewed and discussed by the Management and Investment and Credit Committee and forwarded to the appropriate authority for approval.

Fair valuation of the investments take place every quarter with inputs from investment and risk management departments followed by a review by the external auditors. It is the Bank's policy to ensure that adequate provisions are made for expected credit or investment losses.

## Currency risk

The Bank's currency risk is managed on the basis of limits on net open position set by the Board of Directors and a continuous assessment of current and expected exchange rate movements. The Bank does not engage in foreign exchange trading and, where necessary, matches currency exposures inherent in certain assets with liabilities in the same or correlated currency.

## Operational risk

Operational risk is the exposure to loss resulting from inadequate or failed internal processes, people and systems or external events. The Bank seeks to minimize this risk through a framework of policies and procedures to identify, control and manage these risks.

## Legal and Regulatory risk

Legal risk includes the risk of unexpected loss from transactions and/or contracts not being enforceable under applicable law or from unsound documentation. The Bank manages the legal risk through effective use of internal and external legal advisers.

Regulatory risk includes the risk of non-compliance with regulatory and legal requirements. The Bank has established a compliance function, to act as the coordinating department in respect of matters relating to the regulator i.e. CBB. The compliance department is also responsible for the Bank's anti money laundering initiatives.

## REPORT OF THE SHARI'A SUPERVISORY BOARD

**In the name of Allah, the Beneficent, the Merciful, Prayers and Peace upon the Last Apostle and Messenger, Our Prophet Mohammed, His Comrades and Relatives.**

The Shari'a Supervisory Board of Khaleeji Commercial Bank BSC (c) has reviewed the Bank's activities and compared them with the previously issued fatwas and rulings during the financial year ended 31 December 2006 and found them compatible with the already issued fatwas and rulings.

The Board believes that it has expressed its opinion in respect of the activities carried out by the Bank and it is the responsibility of the management to ensure the implementation of such decisions. It is the duty of the Board to express an independent opinion on the basis of its control and review of the Bank's operations and to prepare a report about them.

A representative of the Bank's management explained and clarified the contents of the Balance Sheet, attached notes and Income Statement for the financial year ended 31 December 2006 to our satisfaction. The report of the Board has been prepared based on the contents provided by the Bank.

The Board is further satisfied that any income which is not in compliance with the Glorious Islamic Shari'a has been dispersed to charitable organisations and that the responsibility of the payment of the Zakat lies with the shareholders in their shares.

The Board is satisfied that the activities and services of the Bank are in compliance with the Glorious Islamic Shari'a.

**Peace be to Allah, Lord of the Worlds.**

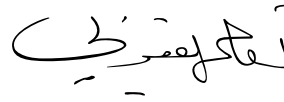
**Prayers be upon Prophet Mohammed (Peace Be Upon Him), all His Family and Companions.**



Dr. Fareed Yaqoob Al Miftah  
Chairman



Dr. Fareed Mohammed Hadi  
Executive Member



Shaikh Nizam Mohammed Saleh  
Yaquby  
Executive Member

# AUDITORS' REPORT

REPORT OF THE AUDITORS TO THE SHAREHOLDERS

**KHALEEJI COMMERCIAL BANK BSC (c)**

28 JANUARY 2007

MANAMA, KINGDOM OF BAHRAIN

**We have audited the accompanying financial statements of Khaleeji Commercial Bank B.S.C. (c) ("the Bank"), which comprise the balance sheet as at 31 December 2006, and the income statement, statement of changes in equity, cash flow statement, and statement of changes in restricted investment accounts for the year then ended, and a summary of significant accounting policies and other explanatory notes.**

## Responsibility of the directors for the financial statements

The directors of the Bank are responsible for the preparation and fair presentation of these financial statements in accordance with Financial Accounting Standards issued by the Accounting and Auditing Organisation for Islamic Financial Institutions and International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatements, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances. In addition the Directors of the Bank are responsible for the Bank's undertaking to operate in accordance with Islamic Sharia'a rules and principles.

## Auditors' responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with both the Auditing Standards for Islamic Financial Institutions

and International Standards on Auditing. Those standards require that we comply with relevant ethical requirements and plan and perform the audit to obtain reasonable assurance 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 financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the 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 principles used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the 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 financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2006, and of its financial performance, its cash flows, the changes in its equity, and changes in restricted investment accounts for the year then ended in accordance with Financial Accounting Standards

issued by the Accounting and Auditing Organisation for Islamic Financial Institutions and the Sharia'a rules and principles as determined by the Sharia'a Supervisory Board of the Bank.

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

## Report on other legal and regulatory requirements

In addition, in our opinion, the Bank has maintained proper accounting records and the financial statements are in agreement therewith. We have reviewed the accompanying report of the chairman and confirm that the information contained therein is consistent with the financial statements. We are not aware of any violations of the Bahrain Commercial Companies Law 2001, the Central Bank of Bahrain and Financial Institutions Law 2006, terms of the Bank's license or its memorandum and articles of association having occurred during the year ended 31 December 2006 that might have had a material effect on the business of the Bank or on its financial position. Satisfactory explanations and information have been provided to us by the management in response to all our requests.

KPMG  
28 January 2007