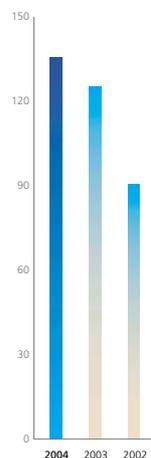




**Leaders of change** The GCC region represents one of the world's most attractive developing markets. The pace of economic reforms, the advent of full WTO membership, and the wealth and sophistication of the population are just some of the factors that underline the huge potential of the region. With its solid capital position, excellent human resource, and strong track record, GIC is well positioned to take advantage of the opportunities in its chosen sectors.

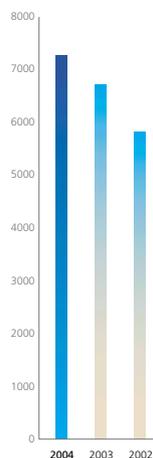
**Mission Statement** Gulf Investment Corporation is a leading regional financial institution that was established under the auspices of the Gulf Cooperation Council and is equally owned by the governments of the six member states: Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates.

We are committed to provide a comprehensive range of financial services that support the development of private enterprise and economic growth in the Gulf region.



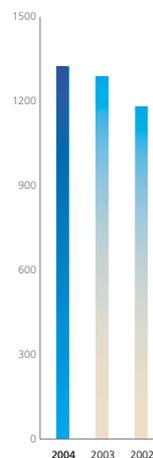
**Net Income**

US\$ Million	
2004	135.4
2003	125.0
2002	90.3



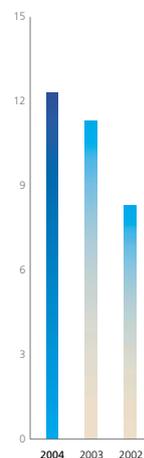
**Total Assets**

US\$ Million	
2004	7,256.6
2003	6,695.3
2002	5,804.9



**Shareholders' Equity**

US\$ Million	
2004	1,321.1
2003	1,285.9
2002	1,178.1



**Return on Adjusted Shareholders' Equity**

US\$ Million	
2004	12.3
2003	11.3
2002	8.3

(US\$ Million)	2004	2003	2002
<b>For the year</b>			
<b>Net Interest Income</b>	61.1	91.0	79.2
Other Income	117.4	87.2	43.6
Operating Expenses	36.5	30.2	28.0
<b>Net Income</b>	<b>135.4</b>	<b>125.0</b>	<b>90.3</b>
<b>At year end</b>			
<b>Total Assets</b>	<b>7,256.6</b>	<b>6,695.3</b>	<b>5,804.9</b>
Trading Securities and Managed Funds	587.6	411.9	308.7
Investment Securities	4,636.1	4,325.9	3,564.1
Loans and Credit Funds	491.5	445.8	426.8
Deposits	2,357.3	1,904.0	1,705.1
Shareholders' Equity	1,321.1	1,285.9	1,178.1
<b>Selected Ratios (%)</b>			
<b>Profitability</b>			
Return on Paid-up Capital	18.1	16.7	12.0
Return on Adjusted Shareholders' Equity	12.3	11.3	8.3
<b>Capital</b>			
BIS Ratios			
- Total	24.0	29.2	31.4
- Tier 1	22.2	27.9	30.6
Shareholders' Equity as a % of Total Assets	18.2	19.2	20.3
<b>Asset Quality</b>			
Loans & Credit Funds as a % of Total Assets	6.8	6.7	7.4
Marketable Securities as a % of Total Assets	64.3	64.7	60.1
GCC & OECD Country Risk as a % of Total Assets	99.2	99.2	99.3
<b>Liquidity</b>			
Liquid Assets Ratio	81.2	79.5	76.3
<b>Productivity</b>			
Operating Income as Multiple of Operating Expenses	4.9	5.9	4.4

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State of Qatar

**H.E. Shaikh Fahad bin Faisal Al-Thani \***  
Chairman  
Deputy Governor, Qatar Central Bank

**H.E. Dr. Hussain Al-Abdulla §**  
Deputy Secretary General for Investment Affairs  
Supreme Council for Economic Affairs and Investment

State of Kuwait

**H.E. Dr. Yousef Hamad Al-Ebraheem \*\***  
Deputy Chairman  
Advisor to the Prime Minister of the State of Kuwait

**H.E. Mr. Abdulmohsen Yousef Al-Hunaif §**  
Undersecretary, Ministry of Finance

United Arab Emirates

**H.E. Mr. Shabib Ahmed bin Rashed bin Shabib \***  
Director of Industrial Development Department  
Ministry of Finance and Industry

**H.E. Mr. Saeed Rashid Al Yateem §§**  
Director of Budget Department  
Ministry of Finance & Industry

Kingdom of Bahrain

**H.E. Dr. Zakaria Ahmed Hejres \***  
Deputy Chief Executive Officer  
Economic Development Board

**H.E. Mr. Khalid A. Al-Bassam §**

Kingdom of Saudi Arabia

**H.E. Mr. Ibrahim M. Al-Romaih \***  
Vice Chairman  
Capital Market Authority

**H.E Mr. Mohammed S. Dobaib §**  
Acting Director General  
Saudi Industrial Development Fund

Sultanate of Oman

**H.E. Darwish bin Ismail bin Ali Al-Bulushi \***  
Undersecretary of Financial Affairs  
Ministry of Finance

**H.E. Abdul Kader Askalan §**  
Chief Executive Officer  
Oman Arab Bank

Senior Management

**Mr. Hisham Abdulrazzaq Al-Razuqi**  
Chief Executive Officer & General Manager

**Mr. Rashid Bin Rasheed**  
Deputy General Manager &  
Head of Finance & Administration

\*\* Chairman of the Executive committee

\* Member of the Executive Committee

§§ Chairman of the Audit Committee

§ Member of the Audit Committee

On behalf of the Board of Directors, I have the privilege to present the Annual Report and Accounts of Gulf Investment Corporation for the year 2004.

With another successful year, GIC has entered its third decade of operations on a positive note: net income rose by 8.3% during 2004 to US\$135.4 million, driven primarily by a 34.6% surge in profits from principal investments and other non-interest income. This net income represents a return on adjusted shareholders' equity of 12.3% and a return on paid up capital of 18.1% for 2004. Balance sheet assets grew by an annual 8.4% to US\$7,256.6 million.

It is gratifying to note that this is the third consecutive year of profit growth, surpassing the record profits earned in 2003. The Corporation will continue to reap the benefits of strategic action plans initiated in 2001, targeted at diversifying and expanding revenue sources, while proactively managing risks and optimizing resource allocation.

GIC's commitment to remain focused on the GCC region proved beneficial in light of the strong growth in the regional economies. The Principal Investments team executed several new direct investment transactions within the Gulf, the major ones being in the Steel, Power and Telecom sectors. Returns from the portfolio of existing direct investments have also increased substantially, reflecting progress in their life cycles and improved operating efficiencies. The regional capital markets activity also performed well, taking advantage of the positive trends in these markets.

With the objective of achieving adequate diversification, the Corporation's exposures to the GCC region are balanced by investments in global markets spread across several asset classes and investment themes. Most of these core portfolios also performed well during 2004, contributing to overall profits.

Another achievement during the year was with regard to GIC's liability management initiatives. Liquidity and funding risk is continuously managed by securing diversified sources of funding and aligning asset and liability maturities. In this regard, during the last quarter of 2004, the Corporation successfully executed the first tranche of a US\$1 billion medium term note program, aimed at diversifying and extending our funding base. The 5 year US\$500 million note was oversubscribed by approximately 66%, reflecting the Institution's solid financial condition and good standing in the regional and international markets.

Under the guidance of and based on the recommendations of the Board of Directors, the management team at GIC continually strives to manage the various business risks and maintain a strong and healthy financial condition. This is reflected in our solid capital base and healthy capital adequacy ratios. At the end of 2004, shareholders' equity increased to US\$1,321.1 million from US\$1,285.9 million at the previous year end.

It is gratifying to note that this is the third consecutive year of profit growth, surpassing the record profits earned in 2003.

In line with our long-term corporate goals, we will continue to focus on the GCC region and are committed to provide a range of financial services that support the development of private enterprise and economic growth in the Gulf region.

With its solid capital position, excellent human resource and strong track record, GIC has established itself as a regional leader in its chosen fields of business and is well positioned to take advantage of the opportunities in its operating environments. I see a bright future for GIC. The Board will continue to play a vital role in providing strategic guidance and support to the management at GIC.

I took over as Chairman of the Board of Directors on February 11, 2004. On behalf of the Board of Directors, I wish to take this opportunity to express my gratitude to my predecessor, H.E. Darwish bin Ismail bin Ali Al-Bulusi, Undersecretary of Financial Affairs, Ministry of Finance, Sultanate of Oman. I would also like to express my appreciation to the management and staff at GIC for a commendable financial performance during 2004.

**Shaikh Fahad Bin Faisal Al-Thani**  
Chairman

Gulf Investment Corporation had another extremely successful year in 2004, with all the core businesses contributing to a boost in earnings and profitability.

During 2004, net profits reached a record US\$135.4 million, up 8.3% relative to 2003, and higher by almost 50% compared to 2002. Excluding extraordinary income earned in 2003, year-on-year growth in net income exceeded 17%. Return on adjusted shareholders' equity rose to 12.3% during 2004, compared to 11.3% in 2003. During the year under review, total balance sheet assets expanded by 8.4% to reach US\$7,256.6 million as of 31st December 2004. The strong performance in 2004 can be attributed to enhanced returns in both the key business areas – Principal Investing and Global Markets.

For the Principal Investments business, 2004 was an excellent year in terms of revenue generation and business expansion. Income from this activity increased during the year, buoyed by the positive momentum within the regional economies. More importantly, the projects team played a pivotal role in the strategic management of invested companies, enhancing operating margins and productivity.

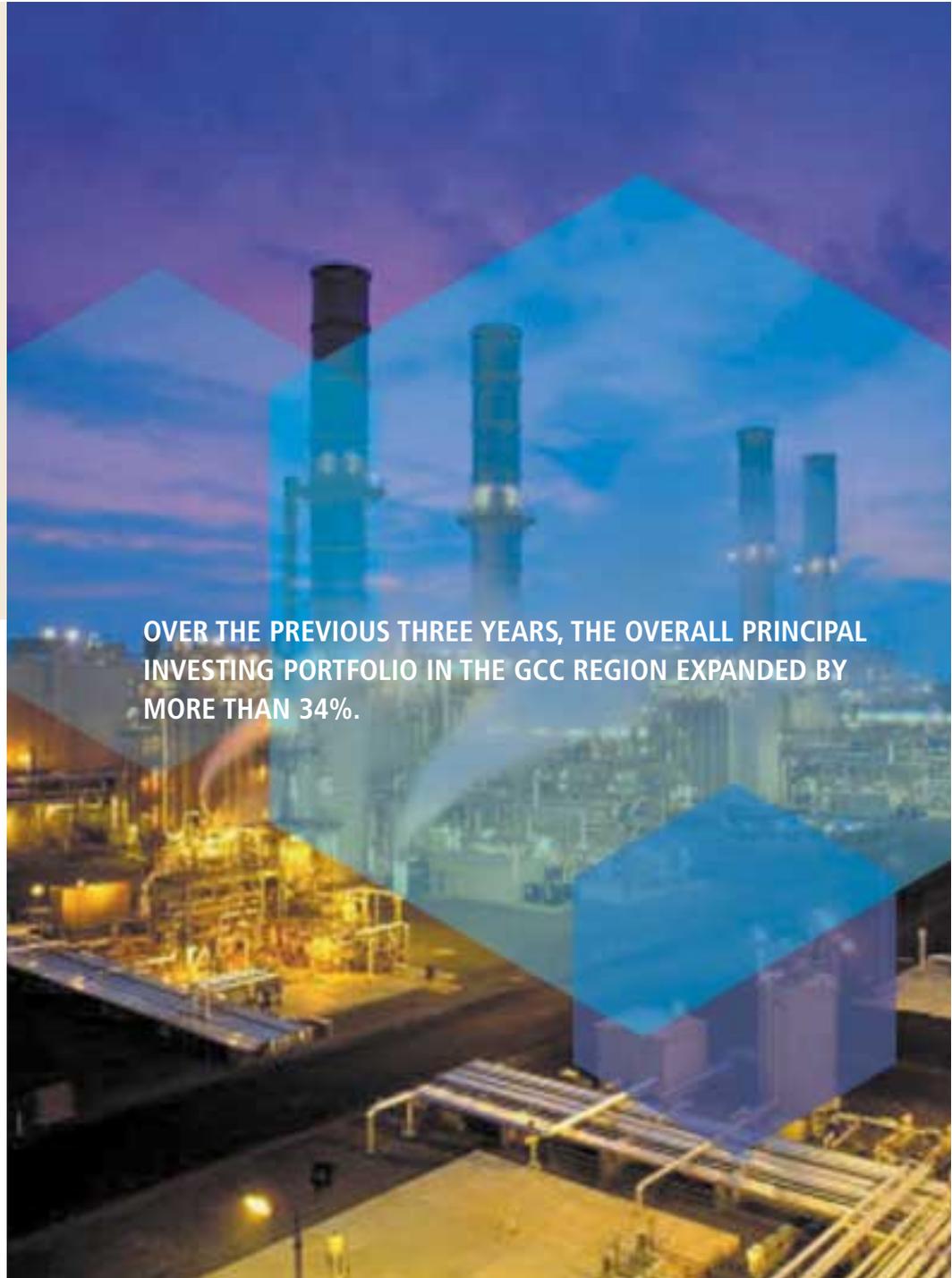
During 2004, the Principal Investments team identified several opportunities including major projects within the Power, Steel and Telecom sectors. The portfolio of direct investments grew to US\$407.0 million at the end of 2004 from US\$282.3 million the prior year. GIC, in partnership with the Belgian based Tractebel EGI, is setting up Al Ezzel Power Company, the first private power plant in Bahrain at an estimated cost of US\$500 million. This is the result of our emphasis on major value-adding projects, contributing to the economic development of the region. Within the Steel sector, United Stainless Company (USCO), a GIC led project, is being set up in Bahrain to produce approximately 90,000 tons per annum of cold rolled stainless steel. For technical know-how and project implementation, GIC has collaborated with Outokompu Stainless of Finland and Danieli S.p.A of Italy. Another focus area has been the telecom sector, where GIC has several ongoing projects. A major telecom investment in

2004 was the 20% stake taken by GIC in Wataniya Telecom Algere, a company promoted by Kuwait based National Mobile Telecom Company.

Another significant venture was Tawasul Telecom, a project initiated by GIC to setup a Telecommunications Hub in the State of Kuwait, with the objective of creating a pan-GCC network based on cutting-edge IP/MPLS technology. GIC augmented its investment in the petrochemical sector with a 20% stake in Oman Polypropylene Company, being setup in the Sohar Industrial Area of Oman, with export projections of approximately 90% of output. Other key project investments during 2004 include, a 25% equity holding in Jeddah Cables, Saudi Arabia and similar stake in Oman Fiber Optic Company, Oman.

Within the Principal Investing activity there has been a steady improvement in profitability, with contributions to the corporate bottom line increasing in each of the past three years. The revitalized strategic initiatives begun in 2001 have had a significant positive impact. Our commitment to remain focused on the GCC region has proved beneficial, given the sizable growth in the regional economies. Over the previous three years, the overall projects portfolio expanded by more than 34%. The underlying philosophy during this expansionary phase has been the same as during our earlier direct investments: detailed fundamental analysis, strict financial discipline and adequate post investment monitoring. The benefits of this rigorous approach are reflected in the enhanced performance of most of our older projects.

In the medium term, we envisage the phased expansion of the projects portfolio to continue, in line with the strengthening Gulf economies. Opportunities that promise the desired commercial return, and fit well with the existing mix of direct investments will be pursued. At the same time we will seek avenues to exit suitable investments through the capital markets, private sale or other routes.



OVER THE PREVIOUS THREE YEARS, THE OVERALL PRINCIPAL INVESTING PORTFOLIO IN THE GCC REGION EXPANDED BY MORE THAN 34%.



### Global Markets

The Corporation's Global Markets business unit manages a diversified set of portfolios in an array of different asset classes and investment themes that are primarily focused in USA, Western Europe and Japan. These comprise of investments ranging from plain vanilla bonds and equities to structured finance, private equity, market neutral, and other alternative asset classes. This unit is also responsible for asset management in the GCC capital markets – both for proprietary and client portfolios.

During 2004, spread income from the approximately US\$4.4 billion debt portfolio formed the major portion of the business unit's income. Returns from investments in international private equity funds rebounded smartly during 2004 after moderate performances in the previous two years. Higher profits from the GCC equity portfolio, improved returns from exposures to structured finance investments and enhanced performance of alternative assets also contributed to the sound performance during 2004.

The debt capital markets team actively manages a high quality bond portfolio which generates stable low-risk spread income, while being a reserve of additional liquidity. GIC had prudently scaled down exposure to the global equity markets during the volatile periods between 2000 and 2002, minimizing its adverse impact on the corporate bottom line. In the first half of 2004, investments in these markets were gradually increased yielding positive returns for this financial year. Our foray into the alternative asset management area has been rewarding with GIC's proprietary portfolio of market-neutral, managed futures and other hedge fund strategy investments providing handsome returns, while enhancing diversification vis-à-vis other conventional assets. Over the last several years our investment managers have fine-tuned the allocation to different managers / themes, achieving an optimum risk-return mix. In association with internationally reputed managers, we also provide alternative asset investment services to our client base.

GIC's regional capital markets activity has increased many-fold during the past few years. From the very beginning emphasis was placed on fundamental research and analysis, with the objective of developing expertise and a leadership role in these markets. In this regard an independent GCC research team was established a few years ago to support the GCC investments business. The substantial returns earned, in some cases multiples of invested cost, stands testimony to the success achieved through detailed research and our intimate knowledge of the region. In April 2003, the GCC equities team launched the Gulf Premier Fund with the objective of achieving long-term capital growth through investment in a diversified portfolio of GCC equities. In addition to enhancing proprietary investment income, the fund's strong performance - a 56.5% return during 2004 and a cumulative 110% since inception, has attracted third party investments augmenting fee based income as well.

Another significant achievement during 2004 was with regards to enhancement of our funding profile. In the last quarter of 2004, the Global Markets team successfully executed a US\$500 million, 5 year medium term note program. Although competitively priced, the note was oversubscribed by 66% with leading financial institutions across Europe, Asia and Middle East expressing considerable interest. Geographically, the subscription was well diversified with 47% from Europe, 29% from Asia and 24% from the Middle East. Approvals have been obtained for a similar second tranche to be issued during 2005. The issuance of these notes are in line with the Corporation's strategic objectives of achieving adequate diversity in the funding profile to enable future expansion.

GIC has always prioritized the management of expenses. Although, every effort is made to equip our staff with the cutting edge in terms of technology, systems and other resources, a sharp focus and discipline is maintained on the overall cost structure. The objective is to function as a highly efficient, productive and compact organization equipped

It is worth highlighting that even during periods of global credit deterioration we did not suffer a single credit default, thanks to prudent and proactive risk management and controls.

with all the appropriate skills and resources. Our continuous emphasis on cost management and productivity has kept us in good stead, with our relatively low expense base being a key competitive advantage, which could bring in benefits in terms of increased efficiency and improved margins.

### 2001 – 2004: accelerated growth phase

Subsequent to and as a result of the strategic reorientation initiated in early 2001, the Corporation has grown from strength to strength, enhancing profitability and financial condition along with balance sheet expansion. Profitability, in terms of return on shareholders' equity, rose from 7.3% in 2001 to 12.3% in 2004, registering steady increases in each of the interim years. In terms of stability and financial condition, GIC remains to be one of the most strongly capitalized financial institutions in the region, with total shareholders equity base reaching US\$1.32 billion as of 31st December 2004, an increase of 14.7% compared to 2001 levels. Over this same period the Corporation's overall balance sheet expanded by approximately US\$1.7 billion or 31% to US\$7.3 billion at the end of 2004. The superior quality of assets was maintained during this growth phase, as reflected in the healthy risk asset ratios.

The consistently strong performance of these years can be attributed to some key decisions taken in 2001 with regards to GIC's strategic direction, areas of focus and resource allocation. While working within clearly defined and firm strategic objectives, we have maintained adequate operational flexibility and dynamism to aggressively take advantages of appearing opportunities. Management of the US\$4 billion debt portfolio is a good example of our success with this approach. These debt portfolios were continuously restructured to take advantage of the various interest rate environments, while stringently controlling the quality, duration and diversity of holdings. During the high interest rate environments fixed

rate bonds were built up, providing substantial spread income when interest rates began declining and more recently, during the last quarter of 2003, anticipating a tightening interest rate environment, a major portion of the fixed rate debt portfolio was swapped into floating rate using interest rate swaps. It is worth highlighting that even during periods of global credit deterioration we did not suffer a single credit default, thanks to prudent and proactive risk management and controls. GIC's determination to maintain a GCC focus also played a vital role in our strong performance during the last three years. Strong regional economic growth positively impacted our direct investments portfolio as well our regional capital markets activity.

We have succeeded in our endeavors to build a strong foundation to grow our business. Going forward, I am confident that we can leverage our competitive strengths and take advantage of opportunities in the region and global markets.

2004 has been a successful year for GIC in many respects. I would like to take this opportunity to thank the Board of Directors for their un-diminishing support and guidance, which has facilitated this success. The sound performance also represents the achievement of a dedicated and committed team of professionals. I am privileged to lead such a team and am confident that we will achieve our objectives and succeed to the benefit of our shareholders and the region we serve.

**Hisham Abdulrazzaq Al-Razzuqi**  
Chief Executive Officer & General Manager

THE GROWTH IN WORLD ECONOMY WAS UNSURPASSED FOR TWO DECADES. THE GCC REGION NOT ONLY CONTRIBUTED TO THIS GROWTH BUT ALSO BENEFITED FROM IT.

GCC economies enjoyed another year of strong performance, fueled by buoyant oil prices and the best growth rate in the world economy in two decades. World capital markets have done well in 2004 after an exceptional performance in 2003. GCC equity markets were among the best emerging markets despite continued instability in Iraq and terrorist incidents in Saudi Arabia. The fly in the ointment for the GCC economies during the year was the continued weakness of the U.S. Dollar.

#### World Economy and Markets

The growth in world economy was unsurpassed for two decades. The IMF estimates world economic growth of 5%\* and the private forecasters estimate 4.8%. The major influences on world economic growth came from the US economy (representing 33% of total) with a growth rate of 3.9% and the Chinese economy which grew at an estimated 9.5% rate. Japan and Europe had slower growth as the Japanese economy grew at an estimated 0.8%, while the Euro zone, Germany and UK grew by 1.6%, 0.6% and 2.9% respectively.\*\*

This strong growth in the world economy, however, was not matched by a similar performance in world equity markets (Table 1). In the U.S. Nasdaq Composite and the S&P 500 both returned 8%-9%, while the Dow Jones

Industrial Average (DIIA) showed 3.15% gain on the year. Some of the Dow Components were hit by bad news and investors shied away from them (particularly Merck). The small cap segment of the U.S. stocks (represented by Russell 2000) performed better than other indices at 17%. Although market indices were not spectacular during the year, the IPO market in the US had its best year since 2000 with US\$132 billion of stock sold, compared with US\$52 billion in 2003, a year with remarkable stock market returns. In Europe, the UK, French and German equity indices came close to each other, up around 7.5% on the year. The disconnect between very good growth rates in the major world economies and the modest performance of their equity markets is explained in the excellent performance of the equity markets in 2003, which anticipated and discounted the high economic growth rates of 2004.

Table 1: Global Equity Indices for 2004 (in local currencies)

Index	31st Dec. 03	31st Dec. 04	% Change	High 2004	Low 2004
<b>North America</b>					
DJIA	10,453.92	10,783.01	3.15%	10,854.54 (28th Dec.)	9,749.99 (25th Oct.)
S&P 500	1,111.92	1,211.92	8.99%	1,213.55 (30th Dec.)	1,063.23 (12th Aug.)
NASDAQ Composite	2,003.37	2,175.44	8.59%	2,178.34 (30th Dec.)	1,752.49 (12th Aug.)
Russell 2000	556.91	651.57	17.00%	654.57 (28th Dec.)	517.10 (12th Aug.)
DJ Wilshire 5000	41.52	36.92	-11.08%	41.57 (30th Dec.)	35.58 (12th Aug.)
<b>Europe</b>					
FTSE 100	4,476.90	4,814.30	7.54%	4,820.10 (30th Dec.)	4,287.00 (26th Sept.)
Xetra Dax	3,965.16 <sup>Δ</sup>	4,256.08 <sup>Δ</sup>	7.34%	4,261.79 (28th Dec.)	3,646.99 (13th Aug.)
CAC 40	3,557.90	3,821.16	7.40%	3,844.14 (17th Nov.)	3,484.84 (13th Aug.)
<b>Asia</b>					
Nikkei 225	10,676.64 <sup>Δ</sup>	11,488.76 <sup>Δ</sup>	7.61%	12,163.89 (26th Apr.)	10,365.40 (10th Feb.)
Hang Seng	12,575.94	14,230.14	13.15%	14,266.38 (29th Dec.)	10,967.65 (17th May)

<sup>Δ</sup> Last day of trading was 30th Dec. for both 2003 and 2004.  
Source: Bloomberg.

\* IMF, World Economic Outlook, September 2004.

\*\* Source: Bloomberg, March 2005.

Table 2: World Equity Markets Capitalization Compared with World Economy Share (By Major Markets)

	World Market Capitalization (2004 year-end)			Gross National Income for 2002 (US\$ Bn)	
	Current (Mn US\$)	YTD (% Change)	% of World	GNI	% of World
<b>World</b>	<b>35,045,186</b>	<b>-2.24%</b>	<b>100.00%</b>	<b>31,720.0</b>	<b>100.0%</b>
United States	14,788,907	-2.27%	42.20%	10,207.0	32.2%
Canada	992,913	1.39%	2.83%	702.0	2.2%
Brazil	299,902	3.50%	0.86%	494.5	1.6%
Mexico	184,616	3.29%	0.53%	597.0	1.9%
United Kingdom	2,713,850	1.33%	7.74%	1,510.8	4.8%
France	1,619,563	-1.81%	4.62%	1,362.1	4.3%
Germany	1,205,480	2.36%	3.44%	1,876.3	5.9%
Switzerland	696,548	-2.03%	1.99%	263.7	0.8%
Italy	782,720	-1.94%	2.23%	1,100.7	3.5%
Japan	3,757,748	-1.26%	10.72%	4,323.9	13.6%
Hong Kong	786,780	-4.45%	2.25%	167.6	0.5%
Australia	616,711	-2.08%	1.76%	384.1	1.2%
China	435,950	-0.41%	1.24%	1,234.2	3.9%
Rest of the World	-	-	17.28%	7,496.1	23.6%

Source: The World Bank, World Development Indicators 2004 and Bloomberg.

There was also the impact of a rising interest rate environment on the equity markets during 2004. The US Federal Reserve raised short term interest rates during the year by 125 basis points. The impact could be seen in the US Libor rates (6-months and one-year) which moved from the beginning of the year to the end by 1.414 points and 1.622 points respectively.

An interesting phenomenon during 2004 was what happened in the US bond markets. The sell-off that has been expected by almost everyone at the end of 2003, never took place. It is significant to note that the yield on the benchmark US 10-year treasuries ended 2003 at a yield

of 4.25% and 2004 at a yield of 4.22%. This happened despite the strong upward movement during the year in the Fed Funds rate and the US dollar libor rates. It is difficult to explain this only in terms of strong buying of treasuries by Asian central banks to support the US dollar and to dampen the pressure on Asian currencies pegged to the dollar. It is also important to view the stable yield on long treasuries as a sign of investor belief that a strong Federal Reserve action on short term interest rates would fight inflation adequately, therefore protecting long term prospects. In other words, inflation expectations in the US remained subdued even though oil prices moved significantly higher during 3Q 2004.

The story in the corporate bond market was similar. Merrill Lynch Global Bond Market Corporate Index returned 5.8% in 2004 compared with 6.6% in 2003. The ECB kept short term rates on the Euro stable during 2004 and that helped the bond markets and to some degree European equity markets. The picture was different, however, in the high yield sector of the world bond markets. The Merrill Lynch Global High Yield index, which returned 28% in 2003 came only at 11.6% in 2004, reflecting the substantial narrowing of spreads that took place during the year. However, corporates sold a record of high-yield bonds in the US during the year, at US\$161 billion.

Commodities continued to show growth in prices but not at the same level witnessed in 2003. The Bloomberg Spot Price Commodity index was up 6.6% for the year compared with 13.7% the year before. An important development during the year was the continued weakness of the US dollar against major currencies. The dollar, which peaked in 2001, has been sliding for three years and ended the year lower by 8.4% against the Euro and 7.9% against the British Pound. However, it strengthened against the Yen by 4.6%. The twin deficits in the US (a budget deficit and a current account deficit) continued to harass the dollar which in turn made dollar denominated assets less attractive.

#### The Story of Oil in 2004

Since the discovery and export of oil in the GCC countries in the 20th century, it has become a dictum that the fortune of those economies are very much linked to oil: the demand for oil, its price, and its share as an energy source worldwide. The story of oil in 2004 is basically what happened on the demand side. The high rates of economic growth in China in 2003 and 2004, and the big spurt in the growth of the US economy in 2004 (a major

user of oil and oil products) had increased demand and oil prices were demand driven and not caused by supply disruptions. To put things in perspective, let us see the quote from a respected business publication in March 1999\*:

*"The crude is gushing from the ground at the rate of 66mn b/d, half as copiously again as in OPEC's prime. The world is awash with the stuff, and it is likely to remain so."*

That was then. To get a view on the demand for oil in 2004, it is important to note that the International Energy Agency (IEA) and the Energy Information Administration (EIA) of US Department of Energy have revised their oil demand forecast for 2004 almost monthly. Demand for oil, which increased by 1.4% during the years 2000 – 2003, has increased by 3.3% in 2004, an additional 2.6 million b/d over 2003 average\*\*.

Due to the unusual spike in prices (WTI reached a high of US\$56.17 on October 22nd and Brent peaked at US\$52 per barrel on October 26th), there was strong pressure on OPEC and particularly on Saudi Arabia to produce close to full capacity. Therefore, for a period in 4Q 2004, the supply of oil surpassed demand. Another important factor affecting oil prices during the year relates to spare production capacity or rather the lack of it. During 1998 – 1999 spare production capacity was in the range of 3 – 4 million barrels, while that same capacity diminished to around 1 – 1.2 million barrels in 4Q 2004, when OPEC was producing around 30 million barrels per day. Because of dramatic increase in OPEC supply and the high prices oil enjoyed, especially in the second half of 2004\*\*\*, OPEC oil revenues for 2004 are estimated at US\$336 billion, and the GCC members (Saudi Arabia, Kuwait, the UAE and Qatar) share of that is US\$176 billion.

\* The Economist, March 1999.

\*\* EIA: Short-Term Energy Outlook, December 2004.

\*\*\* Brent average for 2004: US\$38.32 per barrel, WTI average US\$41.51 per barrel.

How does this oil picture affect the GCC economies is not, however, as straight forward as it seems. On the positive side: government finances for the oil rich countries have turned to surplus (in Saudi Arabia, it was the second year in a row that the country had a budget surplus); balance of payments in all of them were in surplus by substantial amounts (especially in Saudi Arabia and Kuwait); some governments used the extra revenues to reduce debt (Saudi Arabia) and generally GCC governments were able to meet spending demands especially on infrastructure. On the negative side, increased revenues have muted the urgency in restructuring the economies and deregulation, it enhanced further the role of the public sector and it emphasized the differential in the pay and wage structure between the public and the private sectors which reduces the chances for expanding the employment of nationals in the private sector.

**GCC Economies: Healthy But Facing Challenges**

The GCC economies did very well in 2004 as Table 3 indicates. The IMF estimates the lowest real GDP growth in the group (Oman) to be around 2.5% while the best performer (Qatar) at 9.3%. Countries like **Kuwait** which benefits from high oil production and prices proportionately more than other members, is estimated to have revenues of around US\$30 billion in its fiscal year (April 2004 – March 2005), the highest in nominal terms in three decades\*. Because Kuwait enjoys a sizeable international investment portfolio, estimated at US\$90 – US\$100 billion by end 2004, returns from these investments represent another boost to the financial position of the country.

Table 3: Real Growth Rate in the GCC Countries (%)

	2002		2003		2004 <sup>(1)</sup>		2005 <sup>(2)</sup>	
	IMF	IIF	IMF	IIF	IMF	IIF	IMF	IIF
Bahrain	5.1	5.2	5.7	6.8	5.5	6.9	5.3	8.0
Kuwait	-0.4	-0.4	10.1	9.1	2.8	4.3	2.3	3.3
Oman	1.7	1.7	1.4	3.5	2.5	4.3	3.6	4.5
Qatar	7.3	5.7	3.3	5.2	9.3	7.0	5.0	7.3
Saudi Arabia	0.1	0.1	7.2	7.2	3.6	3.2	3.9	3.5
United Arab Emirates	1.9	1.9	7.0	7.0	3.6	4.8	4.5	4.8

<sup>(1)</sup> Estimates.

<sup>(2)</sup> Forecasts.

Sources:

International Monetary Fund, World Economic Report, September 2004.

The Institute of International Finance, Country Reports, August 2004.

\* Middle East Economic Survey, 10 January 2005.

Similar boost in revenues happened in Saudi Arabia, Qatar and the UAE. All countries of the GCC have been embarking on large scale projects. In **Qatar**, the government expects its gas, oil and petrochemicals programs to cost around US\$55 billion over the next decade with a large contribution coming from the private sector. During the year, Rasgas awarded a US\$1.5 billion EPC contract to a consortium of Japanese and Italian firms for its fifth LNG train. It also ordered the construction of seven LNG tankers to transport its gas to prospective clients across Europe and the US. An Heads of Agreement was signed between ExxonMobil and Qatar Petroleum (QP) in July 2004 to set up a gas to liquids (GTL) plant in Ras Laffan with a capacity of 160,000 b/d of diesel, naphtha and lubricant oil at a projected cost of US\$7 billion.

In **Saudi Arabia**, telecoms liberalization resulted in “Etihad Ettisalat” of the UAE winning a license to build a second GSM mobile phone network. The project will result in US\$4 billion of FDI in Saudi Arabia in license fees and infrastructure cost.

In **Bahrain**, Aluminum Bahrain (Alba) has embarked on a US\$1.7 billion expansion program to boost its output to 800 thousand tons a year. Also, agreements were signed to set-up the first Independent Power Project (IPP) in Al-Ezzel with a project cost of US\$500 million. Gulf Investment Corporation together with the Belgium firm Tractabel won the bid for the BOT project and have arranged the financing with a consortium of regional and international banks.

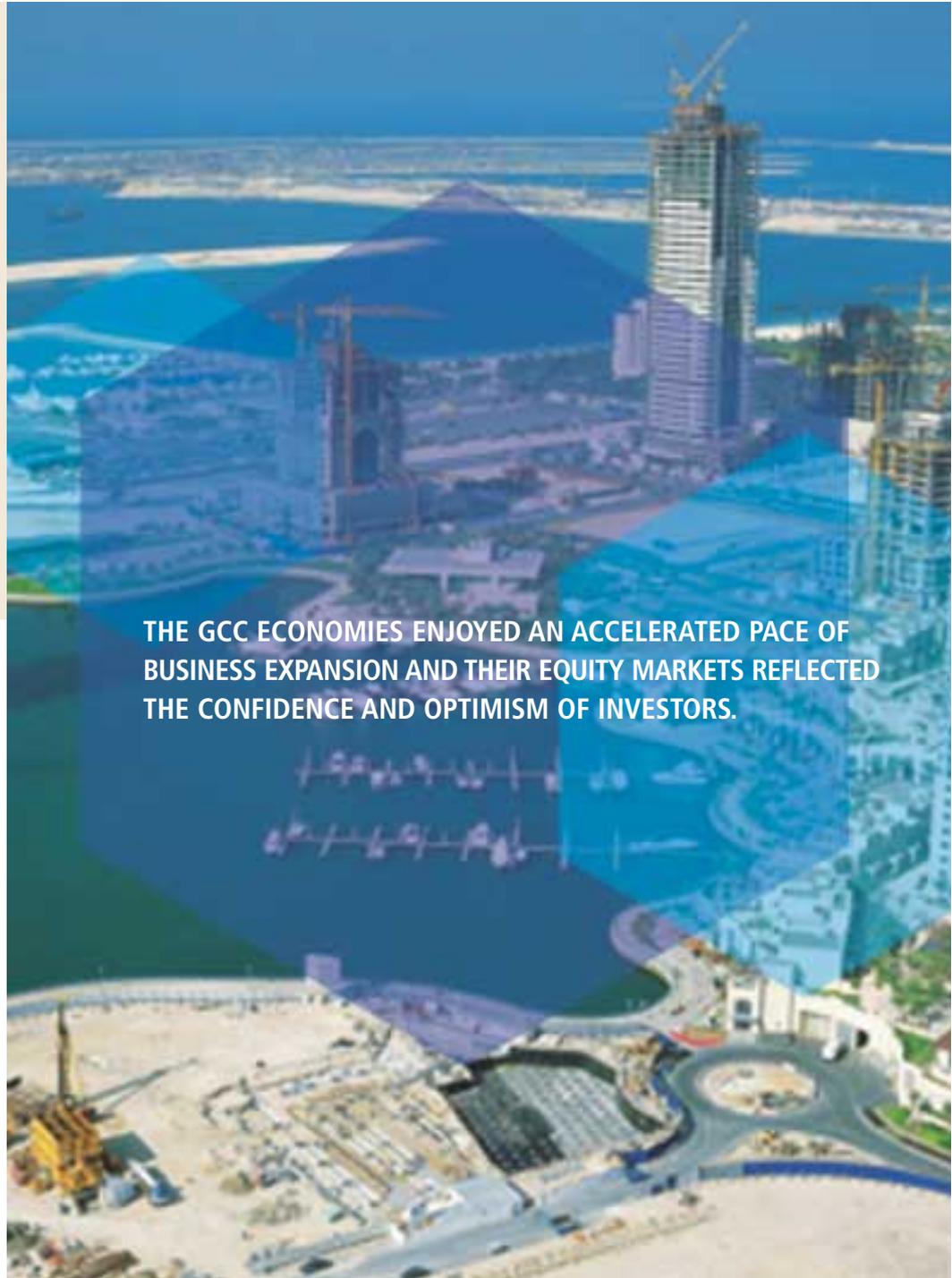
In **Oman**, a Sultani decree was issued outlining the guidelines for privatizing the electricity sector. The decree sets up a new structure for encouraging private sector investments in the sector and ensuring competition in the market while keeping prices for consumers under government supervision. In July, a Canadian firm (Alco Incorporated of Canada) signed a memorandum of understanding (MoU) to acquire 20% stake in Sohar Aluminum project with Abu Dhabi Water and Electricity Authority taking a 40% stake and Oman Oil Company the remaining 40%. The project will create the third aluminum smelter in the Gulf, joining Alba in Bahrain and Dubai in Dubai. With increasing liberalization of the world trade through WTO agreements, the GCC region will gain a competitive advantage in energy intensive projects such as Aluminum smelting. Continuing the trend towards telecom privatization, a consortium of Bank Muscat, HSBC and a Omani local Company (Fincorp) was awarded the financial advisory work for the privatization of OmanTel.

In **UAE**, a federal law was passed in 2004 to allow financial free zones to be set up in the country. The financial and administrative independence of the Dubai International Financial Center (DIFC) was accordingly established. It is intended to make Dubai a recognized hub for international financial services and the regional gateway for capital and investment. There are six primary sectors of focus within the DIFC – banking services, capital markets, asset management and fund registration, re-insurance, Islamic finance and back office operations. It offers investors zero tax on income and profits, 100% foreign ownership and no restrictions on foreign exchange or capital/profit repatriation.

The first cross-border transport agreement in the GCC was signed during the year between UAE and Oman. In Abu Dhabi, a decree was issued in December 2004, which will lead eventually to the privatization of the National Petroleum Construction Company (NPCC) – the first of privatization in Abu Dhabi's energy sector. Several important real estate mega projects took shape in Dubai. Emaar Properties, a group in which the government holds a majority stake, has signed a contract to build the world's largest retail mall (Dubai Mall Project) which is worth US\$735 million and is expected to be completed in 2007. Nakheel, a government-owned real estate company appointed Dubai Islamic Bank (DIB) as lead manager for a US\$350 million Ijara syndication to build the company's portfolio of developments. This includes the Palm Jumeirah and Jebel Ali, the world international city, Jumeirah islands and Jumeirah Lake Towers. Moreover, Dubai Holding was launched in October 2004, with an estimated value of US\$30 billion to manage a number of major projects. These projects include Dubai Internet City, Dubai Media City, Dubai Healthcare City, Jumeirah Beach Residence, Dubailand, Dubai Humanitarian City, Dubai Knowledge Village, Arab Radio Network, International Media Production Zone and other ventures.

Although GCC economies are heading in the direction of privatization, deregulation and restructuring in varying degrees, the challenges facing them are not modest. High among the list is employment creation for young nationals, especially in Saudi Arabia, Bahrain and Oman. Improving the educational system so that its contribution to the development process is enhanced is another major concern for the governments of the GCC. Supporting and furthering the role of the private sector in the economy is – in most cases – a major challenge facing economic policy makers in the region. With the impending requirement for implementing WTO agreements, the region would have to wean away local firms from a bloated subsidy structure and encourage competition and efficiency.

One should not conclude, however, that these challenges are dampening the spirits of domestic investors for the assets in the region. In almost all countries, asset prices have moved up in 2004 whether in property or the equity markets.



**THE GCC ECONOMIES ENJOYED AN ACCELERATED PACE OF BUSINESS EXPANSION AND THEIR EQUITY MARKETS REFLECTED THE CONFIDENCE AND OPTIMISM OF INVESTORS.**

**GCC Equity Markets**

GCC equity markets were markedly higher across the board during 2004. The GIC Composite Index closed the year at 4,200.70, up a remarkable 69.2% for the year. The 57.4% performance of that index in 2003 further underscores the strength of the market that has been in force for the past few years. The Composite was up 17.7% during 2002.

Saudi Arabia contributed the most to this performance, with 44.8 percentage points of the total rise in the GIC Composite Index coming from that country, with the United Arab Emirates (UAE) coming in second at 16.1 percentage points. Qatar continued to perform well, recording third place for the second consecutive year, overshadowing Kuwait, which despite its larger weight in the Composite, managed to contribute only 3 percentage points to 2004's performance.

**Table 4: Return Contribution Analysis**

GIC Composite Index Closing Value	4,200.70
Value Traded (US\$ Mn)	408,764
Value Traded Previous Year (US\$ Mn)	148,386
Change During Year	69.2%
Change During Previous Year	57.4%
Market Cap (US\$ Mn)	184,607

**Country Contribution**

Bahrain	1.3%
Emirates	16.1%
Kuwait	3.0%
Oman	0.6%
Qatar	3.4%
Saudi Arabia	44.8%

**Sector Contribution**

Banking	30.9%
Telecom	7.9%
Other	30.3%

Source: GIC Equity Research Department.

With world markets only managing a late-year rally, regional markets outperformed dramatically. Compared to the GIC Composite Index, the 2004 gains of Morgan Stanley Capital International's (MSCI) World Index and Emerging Markets Index were markedly less spectacular at 15.2% and 26.0%, respectively.

As trading activity continued to pick up in all six countries with no exception, volumes increased remarkably. Value traded during the year was more than 2.7 times the levels seen in the previous year, coming in at US\$408.8 billion, following a 3.7 fold increase in 2003 over 2002.

The surge in trading activity was most evident in Saudi Arabia. Historically the most liquid market in the region, Saudi Arabia boosted its status further, accounting for fully 90% of all trading liquidity in the region versus 81% the previous year and 66% in 2002. Kuwait continued to occupy second place, albeit with a diminished share of only 7% of overall liquidity versus 13% in 2003 and 30% in 2002.

The year opened with the 102 constituents in the GIC Composite Index representing a private-sector market capitalization of US\$117.3 billion. Four quarterly index reviews later, involving a number of additions and deletions that took into consideration the increased prominence of small cap stocks, especially in Saudi Arabia, the number of companies in the Composite was 114 at the end of the year. Driven mainly by the strong performance of most constituents, market capitalization at the end of the year rose to US\$184.6 billion.

Bahrain, Kuwait and Oman saw their volatility drop in 2004 compared to the three preceding years, as measured by the annualized standard deviation of daily returns over the 2 periods. Volatility in Qatar, Saudi Arabia and the UAE rose markedly during the year, with the latter more than doubling from the level seen between 2001 and 2003. This is a somewhat expected side effect of strong performance.

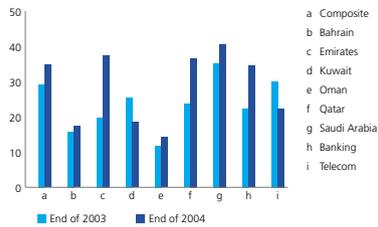
Despite higher volatility, returns outstripped the increased risk by a good margin in all markets except Kuwait and Qatar. This is clearly shown by looking at Sharpe Ratios.

**Table 5: Risk/Return Analysis**

	Annualized Return	Annualized Standard Deviation of Daily Returns (12 months of Data)	Sharpe Ratio
<b>2004</b>			
Composite	69.2%	12.7%	5.3
Bahrain	46.8%	7.8%	5.8
Emirates	114.1%	14.3%	7.9
Kuwait	13.5%	13.1%	0.9
Oman	36.3%	9.5%	3.7
Qatar	49.0%	16.5%	2.9
Saudi Arabia	94.8%	22.8%	4.1
Banking	70.3%	10.3%	6.7
Telecom	41.7%	14.2%	2.8
MSCI World	15.2%	9.7%	1.4
MSCI EMF	26.0%	15.4%	1.6
<b>2001 – 2003</b>			
Composite	32.0%	9.5%	3.2
Bahrain	16.0%	10.1%	1.4
Emirates	29.6%	7.0%	4.0
Kuwait	44.0%	15.6%	2.7
Oman	16.4%	14.7%	1.0
Qatar	56.6%	13.4%	4.1
Saudi Arabia	25.0%	14.5%	1.6
Banking	24.4%	9.4%	2.4
Telecom	47.0%	10.1%	4.5
MSCI World	-3.5%	17.4%	NM
MSCI EMF	12.8%	15.9%	0.7

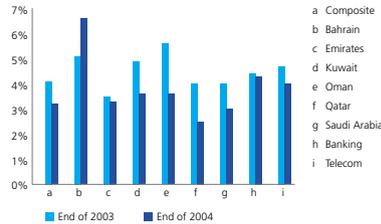
Source: GIC Equity Research Department, Morgan Stanley Capital International.  
NM: Not Meaningful.

Figure 1: Trailing PE Changes During 2003



Source: GIC Equity Research Department, regional exchanges.

Figure 2: Dividend Yield Changes During 2003



Source: GIC Equity Research Department, regional exchanges.

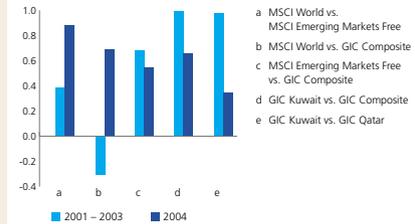
While part of the rise in stock prices during 2004 was surely linked to higher levels of reported profits and dividend distributions, a sizeable portion of the appreciation resulted in expansions of earnings multiples (PEs) and reductions in yield; clear signs of higher future growth expectations and lower perceptions of risk.

**Correlation with World Markets**

Unlike the trend prevailing historically, where the region's markets were highly negatively correlated with the rest of the world, 2004 saw a continuation of the convergence of markets seen during 2003, albeit at a lower level. Correlation between the MSCI World Index and the GIC Composite Index went from -0.92 in the period 2000 – 2002 to +0.96 during 2003 and +0.69 in 2004. Similarly, correlation between the MSCI EMF Index and the GIC Composite moved from -0.69 during 2000 – 2002 to +0.96 in 2003 and +0.55 in 2004.



Figure 3: Correlations Among Stock Indices



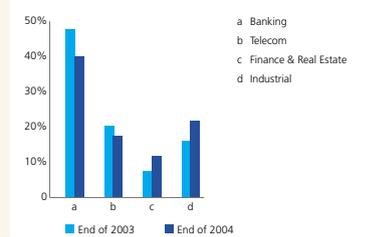
Source: GIC Equity Research Department, Morgan Stanley Capital International.

Within the region, the Kuwaiti market, which spent the first half of the year trading sideways, saw its correlation with the rest of the region drop to +0.66 in 2004 from +0.99 in the period 2001 – 2003. Comparing Kuwait to individual regional markets shows the same trend, which is underscored most clearly in the correlation between the GIC Kuwait Index and the GIC Qatar Index as shown in figure 3.

**Decline in Weight of Banking & Telecom Stocks**

As companies from a wider variety of sectors are opening up to private sector investments across the region, and are therefore listed on regional exchanges, the traditional make-up of markets continued to change in 2004. The preceding year had witnessed the beginning of a trend, whereby every quarterly review of the GIC Indices brought with it a precipitous decline in the weight of banking stocks.

Figure 4: Changes in Sector Weights



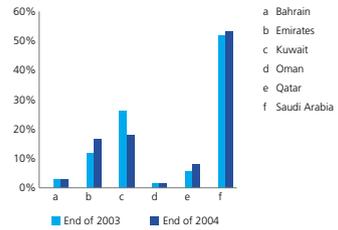
Source: GIC Equity Research Department.

Ending 2002 at a weight of 60.3% of the GIC Composite Index, the banking sector represented 47.9% of that index by the end of 2003 and declined further to 40.1% in 2004.

The absence of new listings during the year caused the telecom sector to shrink its share of the region's total market cap, as represented by the GIC Composite Index, to 17.5% in 2004 from 20.5% in 2003.

Picking up the extra weight were the industrial, finance and real estate sectors.

Figure 5: Changes in Country Weights



Source: GIC Equity Research Department.

#### Shifting in Country Weights

The inclusion of a number of new Saudi companies continued to push that country's share in the GIC Composite Index higher. With the impressive performance of the UAE in 2004, its share rose during the year, mainly at the expense of Kuwait, which lagged behind other regional markets. This is in contrast to 2003 performance, which saw Kuwait maintain its share as the UAE lost ground.

Good performance of Qatari stocks continued to help increase that country's weight in the GIC Composite Index during 2004, while a general lag in both performance and new listings in Bahrain continued to see that market decline in weight.

**To conclude the economic review**, one must say that 2004 was an excellent year for the region's economies. What is more important, in our view, is that the factors that spawned the remarkable performance of the GCC economies during the year are there to stay: strong oil prices, diminished external threats, strong growth in the world economy and continuing efforts by the GCC governments to restructure and deregulate their economies. The weakening dollar has a slight negative impact, however, one should still conclude, that the bright picture has only a single cloud.

WHAT IS MORE IMPORTANT, IN OUR VIEW, IS THAT THE FACTORS THAT SPAWNED THE REMARKABLE PERFORMANCE OF THE GCC ECONOMIES DURING THE YEAR ARE THERE TO STAY: STRONG OIL PRICES, DIMINISHED EXTERNAL THREATS, STRONG GROWTH IN THE WORLD ECONOMY AND CONTINUING EFFORTS BY THE GCC GOVERNMENTS TO RESTRUCTURE AND DEREGULATE THEIR ECONOMIES.

## GULF INVESTMENT CORPORATION'S NET INCOME FOR 2004 AT US\$135.4 MILLION WAS UP 17% FROM THE PREVIOUS YEAR.

**Our Financial Goal:** To maximize long-term shareholder value through consistently superior financial performance while maintaining strong financial condition .

**Our Financial Performance Objective:** To consistently achieve target earnings growth and return on equity, with an appropriate dividend payout.

**Our Financial Condition Objective:** To efficiently manage the various forms of risks associated with our business and maintain strong asset quality, capital based and liquidity, while achieving target balance sheet growth.

### Net Income Analysis

Gulf Investment Corporation's net income for 2004 at US\$135.4 million was up 17% from the previous year (excluding extraordinary item). This represents a return on adjusted average equity of 12.3% compared to 11.3% in 2003, and a return on paid up capital of 18.1% compared to 16.7% in the previous year.

2004 was a challenging year for the spread based investment, due to the increasing interest rate environment that GIC experienced during 2004. However, the dynamics of GIC's asset mix, the strength of its core investments and the diversified blend of its investment activities provided GIC with a resilience to sustain its level of profitability.

Net interest income was down by 32.8% compared to the previous year, but the fact that other operating income reported an increase of 34.6% compared to 2003 confirms the strength of GIC's investment philosophy.

### Net Interest and similar Income

Interest income is generated from debt securities portfolio, credit funds and loans, returns on the outstanding receivable from shareholders and proceeds from the money book.

Spread income from debt securities portfolio continued to be the major significant contributor to interest income.

Gross interest and similar income grew 13.2% to US\$272.5 million during 2004. The 41.1% increase in interest expense due to increase in interest rates, resulted in a net interest income of US\$61.1 million.

The negative impact of the upward movement of interest rates has been mitigated through the hedge against the risk of possible increase in interest rates. A major portion of the long duration fixed rate debt securities was hedged against this risk. This also enabled us to lock-in future earnings at the most opportune time.

The outstanding balance of "due from shareholders", arising from the sale of GIB in 2001, earned a competitive return of approximately 3.6% during 2004. Income from this receivable decreased to US\$8.0 million from US\$18.7million in 2003 due to the reduction in the outstanding balance. (Details of this transaction are provided in Note 7 of the Financial Statements).

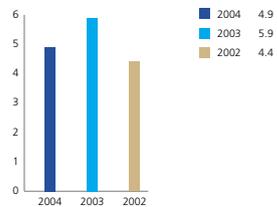
Investments in credit funds have been made as loan replacement vehicles, with credit funds offering superior risk adjusted returns. As a result, income from these credit funds, constituting over 90% of aggregate income from the loans and the credit funds category, registered a year-on-year increase of 23.0%. Income from declining loan book was US\$1.5 million in 2004 compared to US\$2.0 million in 2003.

The Corporation's interest rate sensitivity gap is set out in Note 22 to the Financial Statements. Exposure to interest rate risk is restricted due to the limited mismatch between the repricing of a majority of the Corporation's assets and liabilities.

### Other Operating Income

Other operating income for the year has increased to US\$117.4 million, boosted by strong growth in earning form proprietary asset management (both internally and externally managed) and available for sale investments.

Operating Income as a Multiple of Operating Expenses

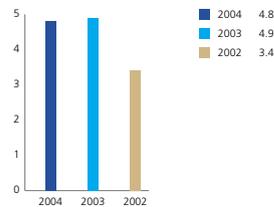


In 2004, "other operating income" constituted almost 65.8% of total gross operating income, compared to 48.9% in 2003, reflecting a more balanced revenue stream and improved risk profile. A detailed breakdown of other operating income is available in Note 16 to the financial statements. The key constituents of other operating income are discussed below.

The net gain on trading securities and managed funds rose to US\$34.3 million in 2004 from US\$28.6 million in 2003.

At US\$22.3 million, earnings from hedge fund and managed future investments, formed the major component of this category. Such investments cover a broad range of strategies including relative value, event driven, long-short, global macro, and are managed by a well diversified pool of external managers. Gains from GCC equity trading amounted to US\$9.3 million for the year, buoyed by strong performance of the regional markets. The balance of income in this category represents gains from the trading bond and managed fund portfolios.

Net Revenue as a Multiple of Operating Expenses



A net gain of US\$6.0 million was recorded from investment securities portfolio. The gain on disposal of available for sale investments, totaling US\$14.4 million, represents realizations transferred out of shareholders' equity on sale of such assets. US\$10.0 million of this is related to investment securities and the balance of US\$4.4 million pertains to equity funds.

Income from investments in international private equity funds increased to US\$11.4 million in 2004 from US\$5.1 million in the previous year. Management believe that the gradual recovery witnessed by the global private equity sector during 2004 is likely to continue in the future.

Earnings from projects and equity participations activities registered US\$26.2 million, representing GIC's share of profits from unconsolidated subsidiary and associated companies. Additionally, dividend income of approximately US\$4.7 million was earned in 2004 and is included within the "Dividend income" category. The excellent performance during the year can be primarily attributed to enhanced

operating margins for several of the Companies within GIC's portfolio of project investment. With representation on the Board of Directors of most of the ventures, the principal investing team plays an active role in the strategic management of these companies and continuously monitors performance. GIC adheres to a policy of strict financial discipline while evaluating and managing project investments, seeking ventures that will provide a commercial rate of return. Several of the project participations are green field in nature and still in start-up mode. Earnings from such participations are expected to grow with the maturing of these projects.

Dividend income of US\$10.4 million comprises receipts from equity funds, equity portfolios, managed funds and project investments.

Fees, commissions and sundry income earned totaled US\$14.1 million. Fee income was generated by the financial advisory, underwriting service and management of funds. The marketing team aims to deliver a range of financial products available in the international markets, to a regional clientele, in addition to the sale of internally developed GCC investment products to clients in and outside the region. Emphasis will continue to be on expansion of fee based revenues to help diversify revenue sources into lower risk assets with lower capital utilisation.

#### Operating Expenses

Management of expenses remains a priority for the Corporation. We continue to maintain a sharp focus and discipline in our cost structure by managing recurring costs while improving efficiency through investment in technology, systems and training.

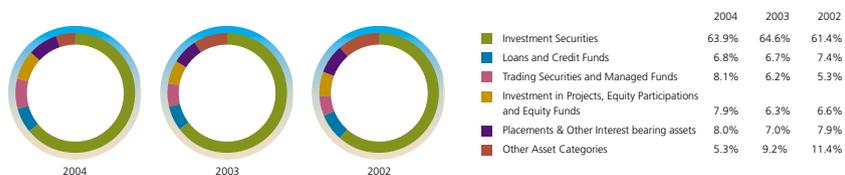
Productivity, expressed in terms of total operating income as a multiple of related operating expenses at 4.9, was broadly in line with previous years. Net revenue, after reducing loss provisions for the year as a multiple of operating expenses was 4.8 in 2004 compared to 4.9 in 2003. The amortization of goodwill, excluded from the operating expenses aggregate in computing the ratios mentioned above, was marginal. Inclusion of these expenses will not have a material impact on the above ratios.

Operating expenses are made up of employee compensation and benefits, occupancy, information technology, and other expenses. Staff costs, the major compensation, which varies in accordance with individuals as well as Corporate performance. Information technology costs include expenditure relating to ongoing enhancement of computer systems.

#### Provisions for Credit Losses

We maintain provisions to absorb losses inherent in our traditional extensions of credit that we believe are probable and that can be reasonably estimated. Given the varied nature of businesses, these may arise from our lending, treasury and investment activities. Estimating losses is inherently uncertain and depends on many factors, including general, macroeconomic and political conditions, rating migration, risk concentration, structural changes within industries, and other external factors such as legal and regulatory requirements. The Corporation periodically reviews such factors and reassesses the adequacy of the provisions.

Asset Mix by Category



As a result of our conservative provisioning policy, the net charge for the year in provisions was US\$5.1 million in 2004, less by US\$25.9 million charged in 2003. Provisions for the current year included US\$0.7 million relating to projects and equity participations, US\$5.8 million for a decline in the value of equity funds. US\$1.1 million of provisions made against certain debt securities during previous years were reversed in 2004 due to an improvement in market value. Also, US\$0.3 million relating to loans and guarantees was reversed in 2004. A detailed break down is provided in Note 17 to the Financial Statements.

**Balance Sheet Analysis**

In line with our aim of optimizing capital utilization through the growth of total assets and an emphasis on risk adjusted return criterion in asset allocation decisions, total assets during the year reached US\$7,256.6 million, up 8.4% over the previous year end. 2004 witnessed a more balanced expansion in assets with the principal investing activity,

trading securities, equity fund portfolios and credit funds registering double-digit growth. Investment securities also registered an increase. Diversification in sources of revenue was further enhanced during 2004 with investments being made in products with superior risk-return characteristics. The outstanding receivable balance "due from shareholders" was further reduced by US\$205.5 million during 2004.

The Corporation's strategic focus continues to be on the GCC states and their major trading partners in the industrialized world. Note 25 to the Financial Statements sets out the geographic distribution of the Corporation's assets. The following sections provide details on the key asset categories.

**Investment Securities**

As at 31 December 2004, the investment securities portfolio made up 63.9% of GIC's total balance sheet assets. This portfolio was established to provide stable coupon/spread income and as a reserve of additional liquidity. With almost

78% of the portfolio allocated to securities within North America and Europe, and covering a wide range of sectors, geographic and industry risk diversification is also achieved vis-a-vis GIC's other GCC based investments. The investment securities portfolio is composed mostly of investment grade marketable debt securities. Investments in equities and funds, at US\$272.6 million, form less than 5.9% of this portfolio. Investment securities totaled US\$4,636.1 million at 31 December 2004 as against US\$4,325.9 million at end of 2003. The investment securities portfolio includes securities available for sale of US\$4,205.2 million and securities held to maturity of US\$430.9 million. Approximately 90% of the debt portion of the investment portfolio is made up of plain floating rate notes or fixed rate notes swapped into floating rate using interest rate swaps. The balance comprises fixed rate securities of a shorter duration.

The high quality of the portfolio is reflected in the unrealized gains associated with the portfolio, approximately US\$93.7 million in unrealized gains relating to investment securities available for sale were included within shareholders' equity as at year end 2004. Within the held to maturity portion, the fair value of holdings exceeds book value by approximately US\$7.4 million. These significant increases in market value are indicative of the superior quality holdings within the portfolio. Within the held to maturity portion, US\$1.1 million of provisions were reversed during the year as a result of improvement in quality. A credit risk analysis of the investment securities portfolio is provided in the risk management section on page 34, and other details, including rating profile, are contained in Note 5 to the Financial Statements.

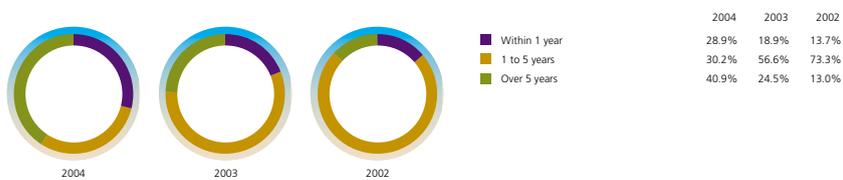
**Loans and Credit Funds**

This category includes loans and advances of US\$41.5 million and investments in credit funds of US\$450.0 million. Outstanding loans declined by 51.6% year-on-year, in line with the strategic decision to discontinue this business and allow loans to run-off. A further 32.3% of currently outstanding loans are due to mature by the end of 2005. As a replacement asset, investment in credit funds increased 25% compared to 2003 levels. Credit funds, yielding higher spreads than GIC's loan portfolio, are managed by experienced external international fund managers and offer enhanced risk adjusted returns. As of 31 December 2004, loans and advances were entirely to customers within the GCC countries. There were no significant concentrations by industrial sector at the year end. Investments in credit funds were distributed among several managers within North America and Europe.

Based on contractual maturities at the balance sheet date, approximately 59% of the outstanding loans and investments in credit funds were due to mature within five years, with 29% due to mature within one year. Details of the maturity profile are given in Note 21 to the Financial Statements and other details including loss provision made are contained in Note 6.

Total loan loss provisions including loan guarantees amounted to US\$6.9 million at 31 December 2004. Counterparty specific provisions amounted to US\$5.0 million while general provisions were US\$1.9 million. The US\$5.0 million specific provisions were made against loans, guarantees and related exposures to project investments. Specific provisions for loans are made to the full extent of the estimated potential loss while general provisions are

Loans and Credit funds Maturity Profile



maintained to cover possible future losses which as yet have not been specifically identified. It is the Corporation's policy to write off loans after all reasonable restructuring and collection activities have taken place and the possibility of further recovery is considered to be remote.

As of 31 December 2004, there were no non-performing loans within GIC's loan book.

#### Trading Securities and Managed Funds

Trading securities and managed funds grew 42.7% during 2004 to reach US\$587.6 million. The bulk of the portfolio comprises of investments in a range of alternative asset strategies, managed by a diverse pool of external managers. The portfolio of alternative asset investments is continuously monitored and restructured to fit GIC's risk-return profile, while gradually expanded in line with growth targets. Fresh investments of US\$158.8 million were made during the year,

bringing the overall exposure to alternative strategies and other funds to approximately US\$527.4 million at 31 December 2004. The Alternative strategies fund (ASF), managed by GIC in association with internationally reputed managers, had another successful year.

The proprietary trading portfolios within this category are managed by the Corporation's asset management team and cover the GCC bond and equity markets. This portfolio of US\$54.6 million is made up of a trading bond portfolio of US\$26.8 million and an exposure to GCC equity markets of approximately US\$27.8 million. GIC is committed to the gradual expansion of the GCC debt and equity portfolios, taking advantage of its unique knowledge of the region. Details of the Corporation's trading portfolio are given in Note 4 to the Financial Statements. Trading securities and managed funds are accounted for at market value.

#### Placement and Other Interest Bearing Assets

Placements and money market funds totaled US\$568.0 million at the 2004 year end. Reciprocity is a key feature of our placement policy. Notes 21 and 25 to the Financial Statements provide the maturity profile and geographic distribution of placements, respectively. Almost US\$559.3 million or 98.5% of total exposure mature within twelve months. Of this, US\$549.4 million had a maturity within three months. Only 3.6% of total placements were with non-bank financial institutions. Other liquid assets at the balance sheet date included US\$10.7 million cash and bank balances.

#### Equity Funds

Equity funds amounted to US\$167.0 million at December 31, 2004, up to 18.4% compared to the prior year. The portfolio is principally invested in equity investments of a structured finance nature with a wide range of externally managed private equity funds. These funds invest in leveraged and un-leveraged acquisitions, privatizations, recapitalisation, rapidly growing companies, expansion financings, turnaround situations, and other special equity situations.

With the exception of listed equity investments, where fair value is reliably discernable, investments in equity funds are carried at cost. Provisions for other than temporary decline in value, determined on an individual basis, amounted to US\$27.8 million at the reporting year end. During 2004, additional provisions of US\$5.8 million were made against expected value diminution in certain investments. Details on equity funds are provided in Note 8 to the financial statements.

#### Investment in Projects and Equity Participations

Investments in projects and equity participations amounted to US\$407.0 million at the end of 2004, compared to US\$282.3 million at the end of 2003. This category includes a mix of investments in unconsolidated GCC and other subsidiaries and equity stakes in GCC companies.

During 2004, the principal investing team made investments in six new projects, and conducted exhaustive appraisals for several others. GIC was proactive in the establishment of a new telecommunication project Wataniya Telecom, in Algeria, in collaboration with Wataniya Telecom Kuwait. GIC made an initial investment of US\$42.4 million for 20% equity stake in this project. Other new additions included investments in diversified projects comprising of fiber optic, power generation, petrochemical, medicare and information technology.

Net provisions during the year decreased by US\$1.6 million. The decrease resulted from a utilization of provision amounted to US\$2.3 million, and net charge for the year amounted to US\$0.7 million. Detailed analysis of the portfolio, including a breakdown of unconsolidated subsidiaries and associated companies, is contained in Note 9 to the Financial Statements. A list of the Corporation's direct investments is also given on page 70.

#### Receivable from Shareholders

The receivable from shareholders amounted to US\$194.2 million at the end of 2004. Subsequent to the sale of Gulf International Bank (GIB) in 2001, US\$577.1 million relating to proceeds from the sale was outstanding from the

shareholders at 31 December 2001. The outstanding balance earned a competitive rate of return. During 2002, 2003 and 2004 US\$382.9 million was repaid by the shareholders towards principal and interest, resulting in a balance of US\$194.2 million at 31 December 2004. As demonstrated in the past three years, the shareholders intend to repay this outstanding over the next two years through dividends received from GIB and the Corporation. Note 7 to the financial statements provide additional details.

#### Property and Other Assets

Including property and fixed assets, total other assets amounted to US\$194.5 million at 31 December 2004. Of this US\$24.0 million related to property and other fixed assets. The remaining US\$170.5 million comprised of accrued interest and fees receivable, goodwill arising on acquisitions, derivative assets used for hedging, employees' end of service benefit assets, accounts receivable, prepaid expenses and other miscellaneous assets. Details are set out in Notes 10 and 11 to the Financial Statements.

A more detailed discussion on liquidity and funding, the various risks associated with our business activities, and capital strength is included in the risk management section that follows.



INVESTMENTS IN PROJECTS AND EQUITY PARTICIPATIONS AMOUNTED TO US\$407.0 MILLION AT THE END OF 2004, COMPARED TO US\$282.3 MILLION AT THE END OF 2003.

The financial goal of the Corporation is to consistently earn competitive returns, while maintaining risks within acceptable levels. Recognizing the relationship between returns and risk, the management of risk forms an integral part of the Corporation's strategic objective. The continuous and rapidly changing business environment has increased the complexity and diversity of risks. The goal of risk management is not to avoid risks, but to understand and manage them.

The various business activities of the Corporation generate a wide spectrum of risks. The four primary risks assessed are credit, market, liquidity and operational. Management of these risks through investment in knowledge and systems has been a priority at GIC. A combination of competent and experienced staff, quantitatively based analytical tools, and ongoing investment in technology are the key resources used to manage our risks effectively. The qualitative and quantitative techniques utilized to optimize the risk return profile incorporate information from the past, trends in the present business environment, and expectations of the future.

Risk management begins with management defining its risk appetite. This is followed by a three step process: identifying and measuring the various risks generated, monitoring and controlling them, and finally optimizing in relation to return.

The primary function of the independent Risk Management Division is to develop and maintain a common risk management framework that serves as a basis for setting policies and limits and for enhancing GIC's ability to manage risks, evaluate performance and allocate capital. This unit acts as a critical link between management and the risk taking divisions – assisting management in defining / quantifying its risk appetite and then effectively communicating this to the risk takers and ensuring that the risk taking activity is within management's acceptable levels. Within the Corporation, responsibility for management of

risks is not restricted to a single division. The philosophy adopted has been to encourage a culture of prudent risk management across all business and support areas.

From the perspective of control, the process of risk management is facilitated through a set of independent functions in addition to the Risk Management Division. These units, which report directly to senior management, include Financial Control, Internal Audit, Compliance and Credit. This multi faceted approach aids the effective management of risks by identifying and monitoring risks from a variety of perspectives.

The process of managing the four risk categories identified above are discussed in more detail in the following sections.

**Credit Risk**

Credit risk is the possibility of loss arising from the failure of an obligor to completely fulfill its contractual obligations. In its various on and off-balance sheet business activities, the Corporation seeks opportunities to take credit risk prudently and manage it effectively to achieve competitive returns. Credit risk is managed concurrently at the transaction, obligor and portfolio levels.

An activity-wise break down of the principal sources of credit risk is illustrated in the graph on page 36. The proportions reflect Credit Risk Weighted Exposure, computed based on BIS capital adequacy guidelines.



MANAGEMENT OF THESE RISKS THROUGH INVESTMENT IN KNOWLEDGE AND SYSTEMS HAS BEEN A PRIORITY AT GIC.

Sources of Credit Risk (Weighted Credit Risk Exposure)



Principal Investing (Projects) by Industry



Rating Profile – Investment Securities Portfolio



Market Risk Constituents – Overall



The primary tool used in the management of credit risk is a set of well defined credit policies and procedures. In addition to communicating management's risk appetite in the form of limits for country, product, industry and obligor, these policies detail the process of measurement, monitoring and reporting. The stringent credit approval framework mandates a rigorous and thorough evaluation of creditworthiness of each obligor, after which limits are approved by management. A country risk review system is utilized to set country limits. Additionally, limits for product and industry are also defined to ensure broad diversification of credit risk. Credit policies and procedures are designed to identify, at an early stage, exposures which require more detailed monitoring and review. The credit risk management process utilizes statistical methods as well, to estimate expected and unexpected loss amounts for the various business activities.

Although, business units are responsible for maintaining exposures within limits, actual exposures are continuously monitored by independent control functions including Risk Management, Financial Control, Compliance and Internal Audit. Technology is a key element in the monitoring

process and in this regard, cutting edge systems, capable of close to real time monitoring and control of risk taking activities, are being effectively utilized.

As of end 2004, the key components of the Corporation's total credit risk exposure were investment securities; principal equity investments and equity funds; and credit funds and loans. The approximately US\$4.4 billion investment securities portfolio is predominantly made up of high grade debt securities, with 91.8% constituting issuers rated investment grade or better. The superior quality of the portfolio is highlighted in the rating profile on page 37. Independent compliance and control units continuously monitor the portfolio for adherence to stringent portfolio guidelines.

The principal investments activity focuses on the GCC countries, a region whose dynamics we comprehend well and where we have a better understanding of the inherent risks. Investments are made after rigorous qualitative and quantitative analysis, and where the desired risk-return objectives are met. As is highlighted in the above graph, a healthy diversification across industry sectors is maintained

within this portfolio. Credit funds, managed by a range of experienced and highly rated fund managers, are invested in superior quality structured finance transactions. The Corporation's lending activity is being gradually phased out, with the residual balance in the loan book amounting to just US\$41.5 million as of 31st December 2004.

**Off-balance sheet Financial Instruments**

In the normal course of its business, the Corporation utilizes derivative and foreign exchange instruments to meet the financial needs of its customers, to generate trading revenues and to manage its exposure to market risk.

For derivative and foreign exchange transactions, procedures similar to on balance sheet products are used for measuring and monitoring credit risk. Credit risk weighted exposure to off balance sheet products amounted to about 2.2% of total credit risk weighted exposure. This amount represents the mark-to-market or replacement cost of these transactions. In terms of maturity, all trading foreign exchange and interest rate contracts were short term with maturities within one year. Credit risk amounts arising from these transactions relate to major banks. Off balance sheet transactions also include

credit-related contingent items designed to meet the financial requirement of the Corporation's customers. A detailed credit risk analysis of credit-related contingent items, derivatives and foreign exchange products is set in Notes 23 and 24 to the Financial Statements.

Although, detailed and thorough analysis is conducted prior to taking on credit risk, unforeseen events could trigger a decline in the creditworthiness associated with a transaction, resulting in loss. Adequate levels of provisions are set aside to cover such losses. The Corporation's provisioning philosophy, including numerical analysis, is discussed in the financial review section on page 25.

**Market Risk**

Market risk is the possibility of loss in value of financial instruments, resulting from an adverse change in market factors. Within the Corporation, market risk is made up of three key risk constituents – interest rate risk, equity risk and foreign exchange risk. A breakdown, based on risk constituents, is provided above for the combined mark-to-market and investment activities. The percentages reflect average VaR amounts, considered independently, and ignore the effects of diversification across risk classes.

Market risk is measured, monitored and managed, both on a notional basis, and using a Value at Risk (VaR) concept. Quantitative statistical methods combined with judgment and experience are used to effectively manage market risk. A system of limits and guidelines restrain the risk taking activity with regard to individual transactions, net positions, volumes, maturities, concentrations, maximum allowable losses, and ensure that risks are within the acceptable levels in terms of notional amounts. The VaR based system provides a more dynamic measure of market risk, capturing in a timely manner, the impact of changes in the business environment on the value of the portfolio of financial instruments.

VaR is calculated and reported to senior management on a daily basis at various levels of consolidation including portfolio, business unit and Corporation. The average, minimum and maximum value at risk amounts for the combined mark-to-market and investment activities are tabulated below. These VaR measures are based on a 95% confidence level, 25 day holding period, and using exponentially weighted historical market data. A profile of daily VaR is charted on page 39.

2004 Value at Risk – 25 day holding period, 95% confidence level

US\$ 000's	Average	Minimum	Maximum	31 Dec 2004
Interest rate	2,317	1,028	4,303	1,201
Equity	22,221	14,360	27,625	23,985
Foreign Exchange	1,313	291	2,576	2,087
<b>Total</b>	<b>22,605</b>	<b>15,357</b>	<b>27,691</b>	<b>24,412</b>

The average overall VaR of US\$22.6 million was 27.9% higher than the average overall level for 2003. The increase in VaR during 2004 can be primarily attributed to the higher equity VaR, resulting from increased exposures to the global equity markets. Interest rate VaR continued to decrease during 2004 as a result substituting fixed rate bonds with floating rate. The value at risk associated with exposures to alternative investment strategies is also quantified and aggregated with risk components of GIC's more conventional on and off balance sheet asset classes. A profile of daily VaR is provided on page 39. At year end 2004, the overall VaR was US\$24.4 million.

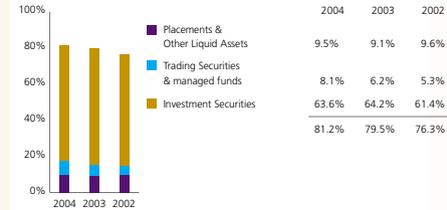
Scenario analysis is an essential component of the market risk management framework. The assumption of normality on which the statistical models are based may become invalid due to the occurrence of certain events. Future scenarios, which result in a breakdown of the historical behavior and relationships between risk constituents, are projected, and potential loss amounts are determined. Most of these scenarios are derived from macroeconomic events of the past, modified with the expectations for the future.



Profile of daily VaR – 25 day holding period, 95% confidence level (US\$ 000's)



Liquid Assets Ratio



Liquidity Risk

Liquidity risk is the risk of being unable to meet financial obligations at reasonable prices. Liquidity risk arises due to

- (1) **Cash flow illiquidity**, arising from the potential inability to procure funds at reasonable rates and required maturities.
- (2) **Asset illiquidity**, relating to the possibility of having to sell assets on a forced basis.

The Corporation adopts a conservative approach to liquidity management with an objective of maintaining sufficient levels of funds and funding capacity to meet our commitments, both on and off balance sheet. In addition to historical data and current information, a vital element in our liquidity measurement methodology is to forecast future scenarios of a tightening in liquidity due to adverse events which may affect both the Corporation and the wider financial system. Extreme event scenarios are evaluated both on the assets and liability side.

GIC considers that a strong capital position is integral to its ability to manage liquidity by ensuring its secure and continuous access to deposits from both, customers and banks. Liquidity controls are in place to closely monitor the profile of future cash flows from maturing assets and liabilities to ensure that the resultant liquidity requirements are within prudently established limits.

A measure of the Corporation's liquidity coverage is highlighted in the following paragraphs.

Liquid Assets Ratio

The Corporation maintains a high proportion of liquid assets, the majority of which include marketable securities. The liquid asset ratio as of 31st December 2004 was 81.2%, marginally higher than the end 2003 level of 79.5%. The ratio is computed by determining the proportion of total assets that can be readily converted into cash, without incurring undue capital losses. Liquid assets include bank balances, money market instruments, placements and securities. Investment securities, constituting over 78.3% of the liquid assets, are primarily made up of superior grade debt securities which are readily realizable.

**Diversified sources of funding**

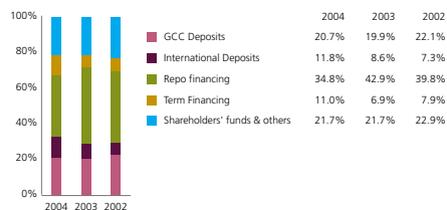
In line with the Corporation's liability management initiatives, the treasury team successfully executed a US\$500 million 5-year medium term note program during the last quarter of 2004. With this latest issuance, GIC's total term finance funding has reached US\$800 million. Although, competitively priced, the note was oversubscribed by 66% with leading financial institutions across Europe, Asia and Middle East expressing considerable interest. Approvals are in place for a second tranche of similar size to be issued during 2005. Liquidity and funding risk is continuously managed by securing diversified sources of funding and aligning asset and liability maturities, enabling future balance sheet expansion.

The Corporation's solid financial condition, augmented by its good standing in the regional and international markets, contributed towards achieving the objective of extending and diversifying its funding base.

As the chart above illustrates, we are continuously trying to achieve an optimal mix of sources of funding.

Another key funding source for GIC is its deposit base. GCC deposits, amounting to 63.7% of total deposits, forms stable funding source. Compared to the previous year this core GCC deposit base increased by US\$172.7 million or 13%. International deposits on the other hand increased by an annual 48.9%. At 31st December 2004, deposits from various sources totaled US\$2,357.3 million, compared to US\$1,904 million at 31st December 2003. Over the years,

Diversified Sources of funding



the Corporation has applied its marketing skills to develop a reliable source of deposits, both regionally and in international markets.

**Maturity profile of assets and liabilities**

A detailed breakdown of the maturity profile by individual asset and liability category is provided in Note 21 to financial statements. At December 31st 2004, roughly 24.4% of total assets were due to mature within 12 months. Approximately to 80.1% of assets with longer maturities were readily realizable securities. The maturity profile is based on contractual repayment arrangements and as such does not take account of effective maturities of deposits. The Corporation's GCC retention record shows that short maturity deposits from GCC governments, central banks and other regional financial institutions have been regularly renewed over the past several years.

**Credit Rating**

During 2004, both Standard & Poors and Moodys reaffirmed GIC's investment grade ratings. We believe that the Corporation's enhanced rating is indicative of a sound business operation and future business potential.

	Moodys	Standard & Poor's
Long-term Deposits	Baa1	BBB+
Short-term Deposits	P2	A2
Bank Financial Strength (BFSR)	C-	-

These ratings reflect the Corporation's strong capital position, its ownership structure and position in the Gulf region, good profitability, asset quality, loan loss experience, the high level of professionalism of our staff and effective management.

**Capital Strength**

Capital represents the shareholder's investment and is a key strategic resource which supports the Corporation's risk taking business activities. In line with the Corporation's financial objective, management strives to deploy this resource in an efficient and disciplined manner to earn competitive returns. Capital also reflects financial strength and security to the Corporation's creditors and depositors. Capital management is fundamental to GIC's risk management philosophy, and takes into account economic and regulatory requirements.

**Regulatory Capital**

At the end of the year under review, the Total and Tier 1 capital ratios were 24.0% and 22.2% respectively. In 2004, amendments were made in the capital adequacy computation methodology pertaining to Available For Sale assets – unlike in the previous years when such assets were considered part of trading book, in 2004 they were considered as part of the banking book. The prior year figures in the table below have been re-computed to conform to changes in presentation in the current year. The ratios are computed based on the Capital Adequacy guidelines of the Basle Committee on Banking Supervision, incorporating the capital charge in respect of market risk as well.

**BIS Capital Ratio Computations**

US\$ Million	2004	2003	2002
Tier 1 Capital (A)	1,103.8	1,149.3	1,099.0
Total capital Base (B)	1,190.8	1,203.0	1,127.1
Risk Weighted Exposure (C)	4,967.4	4,119.0	3,593.5

**BIS Capital ratios (%)**

Tier 1 capital ratio (A/C*100)	22.2	27.9	30.6
Total capital ratio (B/C*100)	24.0	29.2	31.4

With the objective of optimizing capital allocation, GIC has developed a program of phased and gradual growth to be executed over the next few years. This build up will be governed predominantly on risk-return objectives.

**Economic Capital**

In addition to maintaining capital reserves based on regulatory requirements, economic capital sufficiency based on internal models is also determined. The economic capital computation process has three fundamental objectives: determine economic capital sufficiency, in addition to regulatory capital adequacy; assist in equitable / standardized performance measurement of businesses, on a 'real' (risk adjusted) basis; and assist in optimizing resource allocation to achieve target risk adjusted ROE for the Corporation. Economic capital computations are based on extreme scenarios, and cover all types of risks.

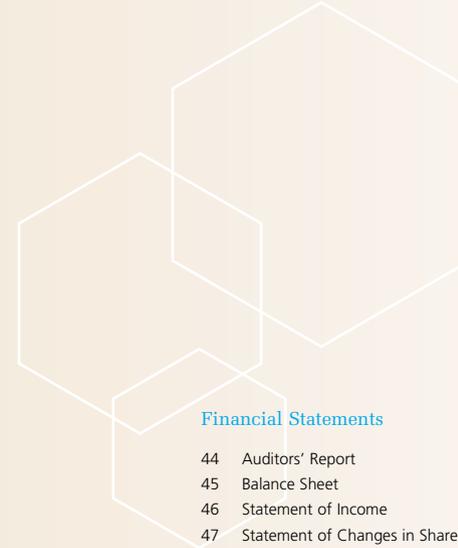
**Operational Risk**

Operational risk is the potential for financial and reputational loss arising from a breakdown in internal controls, operational processes or the various systems that support them. It also includes human errors, criminal acts and natural disasters. Operational risk factors can be categorized into internal and external. Internal risk factors are managed through the establishment of effective segregation of responsibilities, infrastructure and controls within the Corporation. External risk factors are managed by anticipating the occurrence of adverse events, preparing contingency plans and implementing sound back-up systems.

**Internal Audit & Control**

The Internal Audit division plays an important role in the risk management process, particularly in managing operational risk. Operational risk is managed through an effective infrastructure of internal controls including systems and procedures to monitor transactions, positions, confirmations and documentation. The Internal Audit division ensures that these control mechanisms, which cover the front and back office functions, are adhered to and adequately functioning and reports directly to the Audit Committee of the Board of Directors. In addition to internal audits, the Corporation's system of internal controls is regularly examined and evaluated by external auditors, as required by the local regulatory body.

The influence of technology has increased substantially over the recent past and this trend is likely to accelerate in future. Keeping this in perspective, considerable resources have been allocated to managing the system side of operational risk. An EDP audit function within the Internal Audit Division works in close conjunction with the Risk Management division to oversee system risk issues.



**Financial Statements**

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**The Shareholders, Gulf Investment Corporation G.S.C., State of Kuwait**

We have audited the accompanying balance sheet of Gulf Investment Corporation G.S.C. ("the Corporation") as at December 31, 2004 and the related statements of income, changes in shareholders' equity and cash flows for the year then ended.

**Respective responsibilities of management and auditors**

These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audit.

**Basis of opinion**

We conducted our audit in accordance with the International Standards on Auditing as promulgated by the International Federation of Accountants. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

**Opinion**

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Corporation as at December 31, 2004 and of the results of its operations and its cash flows for the year then ended, in accordance with International Financial Reporting Standards promulgated by the International Accounting Standards Board.

**Other regulatory matters**

We further report that we have obtained all the information and explanations that we required for the purpose of our audit and the financial statements include the information required by the Kuwait Commercial Companies Law of 1960, as amended, and the Corporation's articles and memorandum of association. In our opinion, proper books of account have been kept by the Corporation and the accounting information given in the report of the Chairman agrees with the books of account. We have not become aware of any contravention, during the year ended December 31, 2004, of the Kuwait Commercial Companies Law of 1960, as amended, or of the Corporation's articles and memorandum of association, or of Law No. 32 of 1968, as amended, concerning currency, the Central Bank of Kuwait and the organization of banking business and its related regulations, that would materially affect the Corporation's activities or its financial position.



KPMG  
Public Accountants  
Kuwait  
January 13, 2005

(US\$ million)	Note	2004	2003
<b>Assets</b>			
Cash and bank balances		10.7	11.5
Placements and money market funds	3	568.0	412.8
Securities purchased under resale agreements		-	46.5
Trading securities and managed funds	4	587.6	411.9
Investment securities	5	4,636.1	4,325.9
Loans and credit funds	6	491.5	445.8
Receivable from shareholders	7	194.2	399.7
Equity funds	8	167.0	141.0
Investment in projects and equity participations	9	407.0	282.3
Property and other fixed assets	10	24.0	26.2
Other assets	11	170.5	191.7
<b>Total assets</b>		<b>7,256.6</b>	<b>6,695.3</b>
<b>Liabilities and shareholders' equity</b>			
<b>Liabilities</b>			
Securities sold under repurchase agreements		2,527.7	2,873.1
Deposits	12	2,357.3	1,904.0
Term finance	13	800.0	460.0
Other liabilities	14	250.5	172.3
<b>Total liabilities</b>		<b>5,935.5</b>	<b>5,409.4</b>
<b>Shareholders' equity</b>			
Share capital		750.0	750.0
Reserves		386.8	421.5
Unrealised gain on available-for-sale assets		184.3	114.4
<b>Total shareholders' equity</b>	15	<b>1,321.1</b>	<b>1,285.9</b>
<b>Total liabilities and shareholders' equity</b>		<b>7,256.6</b>	<b>6,695.3</b>

The accompanying notes form an integral part of these financial statements.

Shaikh Fahad bin Faisal Al-Thani  
Chairman

Hisham Abdulrazzaq Al-Razuqi  
Chief Executive Officer & General Manager

## Statement of Income

For the year ended December 31, 2004

(US\$ million)	Note	2004	2003
Interest and similar income		272.5	240.8
Interest expense and similar charges		(211.4)	(149.8)
<b>Net interest income</b>		<b>61.1</b>	91.0
Other operating income	16	117.4	87.2
<b>Gross operating income</b>		<b>178.5</b>	178.2
Provision for impairment losses	17	(5.1)	(31.0)
Staff cost		(21.0)	(19.4)
Premises		(2.5)	(2.6)
Amortization of goodwill		(1.5)	(1.3)
Other operating expenses		(13.0)	(8.2)
<b>Net income from ordinary activities</b>		<b>135.4</b>	115.7
Extraordinary item	18	-	9.3
<b>Net income for the year</b>		<b>135.4</b>	125.0

The accompanying notes form an integral part of these financial statements.

## Statement of Changes in Shareholders' Equity

For the year ended December 31, 2004

(US\$ million)	Capital	Reserves			Subtotal reserves	Unrealised gain on available-for-sale assets	Total
		Compulsory reserve	Voluntary reserve	Retained earnings			
Balance as at January 1, 2003	750.0	153.3	135.8	82.4	371.5	56.6	1,178.1
Dividend for 2002	-	-	-	(75.0)	(75.0)	-	(75.0)
Net gains on disposal of available-for-sale assets transferred to income statement	-	-	-	-	-	(3.6)	(3.6)
Change in fair value of available-for-sale assets	-	-	-	-	-	61.4	61.4
Net income for the year	-	-	-	125.0	125.0	-	125.0
Transfer to compulsory reserve	-	12.5	-	(12.5)	-	-	-
<b>Balance as at December 31, 2003</b>	<b>750.0</b>	<b>165.8</b>	<b>135.8</b>	<b>119.9</b>	<b>421.5</b>	<b>114.4</b>	<b>1,285.9</b>
Balance as at January 1, 2004	750.0	165.8	135.8	119.9	421.5	114.4	1,285.9
Dividend for 2003	-	-	(100.0)	(75.0)	(175.0)	-	(175.0)
Net gains on disposal of available-for-sale assets transferred to income statement	-	-	-	-	-	(23.0)	(23.0)
Share of pre acquisition profits for associates acquired in stages and share of revaluation reserves of associated companies (See Note 9a)	-	-	-	4.9	4.9	-	4.9
Change in fair value of available-for-sale assets	-	-	-	-	-	92.9	92.9
Net income for the year	-	-	-	135.4	135.4	-	135.4
Transfer to compulsory reserve	-	13.5	-	(13.5)	-	-	-
Transfer to voluntary reserve	-	-	13.5	(13.5)	-	-	-
<b>Balance as at December 31, 2004</b>	<b>750.0</b>	<b>179.3</b>	<b>49.3</b>	<b>158.2</b>	<b>386.8</b>	<b>184.3</b>	<b>1,321.1</b>

The accompanying notes form an integral part of these financial statements.

# Statement of Cash Flows

For the year ended December 31, 2004

# Notes to the Financial Statements

For the year ended December 31, 2004

(US\$ million)	2004	2003
<b>Cash flows from operating activities:</b>		
Net income for the year before extraordinary item	135.4	115.7
Extraordinary item	-	9.3
Adjustments to reconcile net income to net cash outflow from operating activities:		
Income receivable from the shareholders (see note 7)	(8.0)	(18.7)
Provision for impairment losses	5.1	31.0
Amortisation of goodwill	1.5	1.3
Gain on sale of investment securities	(15.0)	(0.8)
Gain on sale of investment in projects	(0.3)	-
Income from projects and equity participations	(26.2)	(26.0)
Amortisation of net premium/discount on investment securities	14.1	7.7
Depreciation	2.7	2.8
Decrease/(increase) in fair value of available-for-sale investments	38.9	(16.3)
Increase in trading securities and managed funds	(175.6)	(103.2)
Decrease/(increase) in other assets and other liabilities (net)	20.3	(43.6)
<b>Net cash outflow from operating activities</b>	<b>(7.1)</b>	<b>(40.8)</b>
<b>Cash flows from investing activities:</b>		
(Increase)/decrease in placements and money market funds	(155.6)	30.2
Decrease/(increase) in securities purchased under resale agreements	46.5	(36.3)
Increase in loans and credit funds	(45.5)	(18.7)
Sale and maturity of investment securities	893.4	700.4
Purchase of investment securities	(1,158.5)	(1,395.7)
Increase in investment in equity funds	(21.7)	(32.3)
Sale of investment in projects	0.6	-
(Increase)/decrease in investment in projects and equity participations	(38.7)	9.4
Purchase of property and other fixed assets	(0.5)	(0.3)
Received from shareholders	213.4	105.9
<b>Net cash outflow from investing activities</b>	<b>(266.6)</b>	<b>(637.4)</b>
<b>Cash flows from financing activities:</b>		
Increase in deposits and repurchase agreements	107.9	761.2
Term finance	340.0	-
Dividend paid	(175.0)	(75.0)
<b>Net cash inflow from financing activities</b>	<b>272.9</b>	<b>686.2</b>
(Decrease)/increase in cash and cash equivalents	(0.8)	8.0
Cash and cash equivalents at beginning of year	11.5	3.5
<b>Cash and cash equivalents at end of year</b>	<b>10.7</b>	<b>11.5</b>

The accompanying notes form an integral part of these financial statements.

Cash and cash equivalents comprise of cash and bank balances.

## 1 Incorporation and Activity

The Gulf Investment Corporation G.S.C. ("the Corporation") is an investment company incorporated in the State of Kuwait on November 15, 1983 as a Gulf Shareholding Company. It is equally owned by the governments of the six member states of the Gulf Co-operation Council ("GCC") – Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates. The Corporation is engaged in all aspects of investment banking activities.

The Corporation is domiciled in Kuwait and its registered office is at Jaber Al Mubarak Street, Al Sharq, Kuwait. The total number of staff employed by the Corporation as at December 31, 2004 was 147 (2003: 139).

The financial statements were approved and authorised for issue by the Board of Directors on January 13, 2005.

## 2 Significant Accounting Policies

### 2.1 Statement of compliance

The financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRSs") as promulgated by the International Accounting Standards Board ("IASB"), interpretations issued by the International Financial Reporting Interpretations Committee of the IASB and the requirements of the Kuwait Commercial Companies Law of 1960, as amended, Ministerial Order No.18 of 1990, Law No. 32 of 1968 concerning currency, the Central Bank of Kuwait and the Organisation of Banking Business and subsequent amendments thereto and the Corporation's memorandum and articles of association.

### 2.2 Basis of presentation

The Corporation's functional currency is US Dollars and the figures presented in the financial statements are rounded to the nearest million.

The financial statements are prepared on a fair value basis for derivative financial instruments, financial assets and liabilities held for trading, and available for-sale assets, except those for which a reliable measure of fair value is not available. Other financial assets and liabilities and non-financial assets and liabilities are stated at amortised cost or historical cost.

The accounting policies have been consistently applied by the Corporation and are consistent with those used in the previous year.

### 2.3 Subsidiaries

Subsidiaries are those enterprises controlled by the Corporation. Control exists when the Corporation has the power, directly or indirectly, to govern the financial and operating policies of an enterprise so as to obtain benefits from its activities.

The investments in Bitumat Company Limited, GIC Technology Partnership Co. and Gulf Paramount Electric Services WLL, subsidiary companies, are not material to the financial statements of the Corporation. Accordingly, these subsidiaries are included under 'Investment in Projects and Equity Participations' and are accounted for using the equity method.

# Notes to the Financial Statements (continued)

For the year ended December 31, 2004

## 2 Significant Accounting Policies (continued)

### 2.4 Financial instruments

#### (i) Classification

**Trading instruments** are those that the Corporation principally holds for the purpose of short-term profit taking. These include trading securities and managed funds, derivative contracts that are not designated as effective hedging instruments, and liabilities from short sales of financial instruments. All trading derivatives in a net receivable position (positive fair value), as well as options purchased, are reported as part of other assets. All trading derivatives in a net payable position (negative fair value), as well as options written, are reported as part of other liabilities.

**Originated loans and receivables** are loans and receivables created by the Corporation providing money to a debtor other than those created with the intention of short-term profit taking. Originated loans and receivables comprise deposits with banks and financial institutions, securities purchased under resale agreements, loans and advances to customers (other than purchased loans), receivables from shareholders and debt instruments purchased at original issuance.

**Held-to-maturity assets** are financial assets with fixed or determinable payments and fixed maturity that the Corporation has the intent and ability to hold to maturity. These include credit funds and certain debt instruments.

**Available-for-sale assets** are financial assets that are not held for trading purposes, originated by the Corporation, or held-to-maturity. Available-for-sale instruments include money market funds, certain investment securities, equity funds and certain investments in projects.

#### (ii) Recognition

The Corporation recognizes financial assets held to maturity, held for trading and available-for-sale assets on the trade date, i.e. the date it commits to purchase the assets. From this date any gains and losses arising from changes in fair value of the assets are recognized.

Originated loans and receivables are recognized on the settlement date.

#### (iii) Measurement

Financial instruments are measured initially at cost, including transaction costs.

Subsequent to initial recognition all trading instruments and all available-for-sale assets are measured at fair value, except that any instrument that does not have a quoted market price in an active market and whose fair value cannot be reliably measured is stated at cost, including transaction costs, less impairment losses (see note 2.9).

All non-trading financial liabilities, originated loans and receivables and held-to-maturity assets are measured at amortised cost less impairment losses (see note 2.9). Amortised cost is calculated on the effective interest rate method. Premiums and discounts, including initial transaction costs, are included in the carrying amount of the related instrument and amortised based on the effective interest rate of the instrument.

#### (iv) Fair value measurement principles

The fair value of financial instruments is based on their quoted market price (bid price for assets and offer price for liabilities) at the balance sheet date without any deduction for transaction costs. If a quoted market price is not available then the fair value of the instrument is estimated using pricing models or discounted cash flow techniques or market price of similar financial instruments.

Where discounted cash flow techniques are used, estimated future cash flows are based on management's best estimates and the discount rate is a market related rate at the balance sheet date for an instrument with similar terms and conditions. Where pricing models are used, inputs are based on market related measures at the balance sheet date.

The fair value of derivatives that are not exchange-traded is estimated at the amount that the Corporation would receive or pay to terminate the contract at the balance sheet date taking into account current market conditions and the current credit worthiness of the counterparties.

#### (v) Gains and losses on subsequent measurement

Gains and losses arising from a change in the fair value of available-for-sale assets are recognized directly in shareholders' equity. When the financial assets are sold, collected or otherwise disposed off the cumulative gain or loss recognized in shareholders' equity is transferred to the income statement.

Gains and losses arising from a change in the fair value of trading instruments are recognized in the statement of income.

#### (vi) Derecognition

A financial asset is derecognized when the Corporation no longer has control over the contractual rights that comprise the asset. This occurs when the rights are realized, expired or are surrendered. A financial liability is derecognized when it is extinguished.

Held-to-maturity, available-for-sale assets and assets held for trading are derecognized using trade date accounting. The Corporation uses the weighted average method to determine the gain or loss on derecognition.

Originated loans and receivables are derecognized on the day they are transferred by the Corporation.

#### (vii) Offsetting

Financial assets and liabilities are offset and the net amount is reported in the balance sheet when the Corporation has a legally enforceable right to set off the recognized amounts and the transactions are intended to be settled on a net basis.

# Notes to the Financial Statements (continued)

For the year ended December 31, 2004

## 2 Significant Accounting Policies (continued)

### 2.5 Repurchase and resale arrangements

The Corporation enters into purchases (sales) of investments under agreements to resell (repurchase) substantially identical investments at a certain date in the future at a fixed price. The amounts paid are recognized as securities purchased under resale agreements. Investments sold under repurchase agreements continue to be recognized in the balance sheet and are measured in accordance with the accounting policy for either assets held for trading or held-to-maturity or available-for-sale, as appropriate. The proceeds from the sale of the investments are reported as part of liabilities as securities sold under repurchase agreements.

The difference between the sale and repurchase considerations is recognized on an accrual basis over the period of the transaction and is included in interest.

### 2.6 Investment in projects and equity participations

Investment in enterprises in which the Corporation holds 20% or more of the voting capital and/or exercises significant control or influence over the financial and operating policies ("associates") are accounted for using the equity method. Provision is made for any impairment losses and recognized in the income statement.

Other investments in projects and equity participations are classified as available-for-sale assets. Provision is made for any impairment losses (see note 2.9) on an individual investment basis and is recognized as set out in note 2.9.

### 2.7 Property and other fixed assets

Property and other fixed assets are carried at cost less accumulated depreciation and impairment losses (see note 2.9). Depreciation is computed on a straight-line basis over the estimated useful life of each asset category as follows:

Buildings	20 years
Installations	5 – 10 years
Office equipment	3 – 4 years
Furniture	4 – 6 years
Motor vehicles	3 years

### 2.8 Amortisation of goodwill

Goodwill arising on acquisition of an associate, jointly controlled entity or subsidiary company represents the excess of the cost of the acquisition over the fair value of the net identifiable assets acquired. Goodwill is stated at cost less accumulated amortisation and impairment losses (see note 2.9). Goodwill will be annually reviewed for impairment.

### 2.9 Impairment

Property, other fixed assets, goodwill and financial assets are reviewed at each balance sheet date to determine whether there is an indication of impairment. If any such indication exists, the asset's recoverable amount is estimated.

#### Property, other fixed assets and goodwill

An impairment loss is recognized whenever the carrying amount of an asset exceeds its recoverable amount. The recoverable amount of assets is the greater of their net selling price and value in use. The impairment losses are recognized in the statement of income.

#### Originated loans and advances, receivables and held-to-maturity assets

The recoverable amount of originated loans and advances, receivables and purchased loans that are classified as held-to-maturity, is calculated as the present value of the expected future cash flows, discounted at the instrument's original effective interest rate. Short-term balances are not discounted.

Loans and advances and receivables are carried at amortised cost less specific and general allowances for uncollectibility. Specific provision for impairment is established if there is an objective evidence that the Corporation will not be able to collect all amounts due. The amount of specific provision is determined as the difference between the carrying amount and the recoverable amount of the asset. General provision for impairment is made in accordance with the instructions of the Central Bank of Kuwait dated December 18, 1996, as amended.

If in a subsequent period the amount of an impairment loss decreases and the decrease can be linked objectively to an event occurring after the write-down, the write-down or allowance is reversed through the income statement.

#### Financial assets remeasured to fair value directly through shareholders' equity

The recoverable amount of an equity instrument is its fair value. The recoverable amount of debt instruments and purchased loans remeasured to fair value is calculated as the present value of expected future cash flows discounted at the current market rate of interest. Where an asset remeasured to fair value directly through shareholders' equity is impaired, and a write-down of the asset was previously recognized directly in shareholders' equity, the write down is transferred to the income statement and recognized as part of the impairment loss. Where an asset measured to fair value directly through shareholders' equity is impaired, and an increase in the fair value of the asset was previously recognized in shareholders' equity, the increase in fair value of the asset recognized in shareholders' equity is reversed to the extent the asset is impaired. Any additional impairment loss is recognized in the income statement.

If in a subsequent period the amount of an impairment loss decreases and the decrease can be linked objectively to an event occurring after the write-down, the write-down is reversed through the income statement.

## Notes to the Financial Statements (continued)

For the year ended December 31, 2004

### 2 Significant Accounting Policies (continued)

#### 2.10 Other provisions

Other provisions are recognised in the balance sheet when the Corporation has a legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation.

#### 2.11 Fiduciary activities

Assets managed for third parties or held in trust or in a fiduciary capacity are not treated as assets of the Corporation and accordingly are not included in these financial statements.

#### 2.12 Hedge accounting

A hedging relationship exists where:

- at the inception of the hedge there is formal documentation of the hedge;
- the hedge is expected to be highly effective;
- the effectiveness of the hedge can be reliably measured;
- the hedge is highly effective throughout the reporting period; and
- for hedges of a forecasted transaction, the transaction is highly probable and presents an exposure to variations in cash flows that could ultimately affect net profit or loss.

Where there is a hedging relationship between a derivative instrument and a related item being hedged, the hedging instrument is measured at fair value. The treatment of any resultant gains and losses is set out below.

The fair value of derivative hedging instruments is calculated in the same way as the fair value of trading instruments (refer accounting policy 2.4 (iv)).

Where a derivative financial instrument hedges the exposure to changes in the fair value of a recognized asset or liability, the hedged item is stated at fair value in respect of the risk being hedged. Gains or losses on remeasurement of both the hedging instrument and the hedged item are recognized in the income statement.

Where a derivative financial instrument hedges the exposure to variability in the cash flows of recognized assets or liabilities (or homogeneous groups/portfolios thereof) or anticipated transactions or firm commitments, the effective part of any gain or loss on remeasurement of the hedging instrument is recognized directly in shareholders' equity. The ineffective part of any gain or loss is recognized in the income statement.

When a hedged anticipated transaction or firm commitment results in the recognition of an asset or liability, the cumulative gain or loss on the hedging instrument recognized in shareholders' equity is removed from shareholders' equity and included in the initial measurement of the asset or liability. Otherwise the cumulative gain or loss recognized in shareholders' equity is transferred to the income statement at the same time that the hedged transaction affects net profit or loss and included in the same line item as the hedged transaction.

When a hedging instrument or hedge relationship is terminated but the hedged transaction is still expected to occur, the cumulative gain or loss recognized in shareholders' equity remains in shareholders' equity and is recognized in accordance with the above policy. If the hedged transaction is no longer expected to occur, the cumulative gain or loss recognized in shareholders' equity is recognized in the income statement immediately.

#### 2.13 Interest, fee income and dividend income

Interest income and expense is recognized on an accrual basis taking into account the effective yield of the asset or an applicable floating rate. Interest income includes the amortisation of any discount or premium or other difference between the initial carrying amount of an interest bearing instrument and its amount at maturity calculated on an effective interest rate basis. Fee income is recognized when earned. Dividend income is recognized when the right to receive payment is established.

#### 2.14 Foreign currency

The reporting currency of the Corporation is the US Dollar. The share capital of the Corporation is also denominated in US Dollars. Transactions in foreign currencies are converted to US Dollars at the rate of exchange prevailing at the date of the transaction. Foreign currency monetary assets and liabilities are converted into US Dollars at market rates of exchange prevailing on the balance sheet date. Realised and unrealised foreign exchange gains and losses are included in the statement of income. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated to US Dollars at foreign exchange rates ruling at the dates the values were determined. Non-monetary assets and liabilities denominated in foreign currency that are stated at historical cost or amortised cost, are recorded at the exchange rate ruling at the date of transaction.

### 3 Placements and Money Market Funds

Placements and money market funds at December 31, 2004 included placements with non-bank financial institutions amounting to US\$ 20.2 million (2003: US\$ 68.3 million) and money market funds amounting to US\$ 8.7 million (2003: US\$ 59.1 million).

### 4 Trading Securities and Managed Funds

(US\$ million)	2004	2003
Managed funds	587.6	408.6
Listed debt securities	-	3.3
	<b>587.6</b>	<b>411.9</b>

## Notes to the Financial Statements (continued)

For the year ended December 31, 2004

### 5 Investment Securities

(US\$ million)	2004	2003
<b>Debt and other interest bearing instruments available-for-sale</b>		
AAA/Aaa rated debt securities	213.4	608.0
GCC Government securities	166.5	302.0
Debt securities of other investment grade issuers	3,452.8	2,671.0
Other debt securities	99.9	96.8
	<b>3,932.6</b>	<b>3,677.8</b>
<b>Debt and other interest bearing instruments held-to-maturity</b>		
AAA/Aaa rated debt securities	36.3	45.2
GCC Government securities	106.6	172.6
Debt securities of other investment grade issuers	282.5	298.5
Other debt securities	5.5	11.8
	<b>430.9</b>	<b>528.1</b>
<b>Equity investments available-for-sale</b>		
Listed equity investments	97.3	48.0
Unlisted equity investments	175.3	72.0
	<b>272.6</b>	<b>120.0</b>
<b>Total</b>	<b>4,636.1</b>	<b>4,325.9</b>

Investment securities amounting to US\$ 2,527.7 million (2003: US\$ 2,826.6 million) are pledged as security in respect of borrowings under securities sold under repurchase agreements.

During the year, a provision of, US\$ 1.1 million was released (2003: US\$ 3.0 million). The investments shown above are net of any provision.

### 6 Loans and Credit Funds

(US\$ million)	2004	2003
Loans and advances to customers	41.5	85.8
Credit funds	450.0	360.0
	<b>491.5</b>	<b>445.8</b>

Loans and advances to customers at December 31, 2004 did not include any amount to a GCC Country Government Agency (2003: US\$ 32.3 million).

There were no significant concentrations by industrial sector at December 31, 2004 or at December 31, 2003.

#### a) Provision for loan losses

The movements in the provision for loan losses were as follows:

(US\$ million)	2004	2003
Balance at beginning of the year	3.6	4.0
Net write back for the year	(0.2)	(0.4)
<b>Balance at end of the year</b>	<b>3.4</b>	<b>3.6</b>

#### b) Provision for loan guarantees

(US\$ million)	2004	2003
Balance at beginning of the year	3.6	3.4
Net (write back)/charge for the year	(0.1)	0.2
<b>Balance at end of the year</b>	<b>3.5</b>	<b>3.6</b>

### 7 Receivable from Shareholders

This primarily represents the unpaid balance from the sale of Gulf International Bank ("GIB") to its shareholders on April 7, 2001. Repayment of this outstanding balance will be from any future dividends received by the shareholders from GIB and from the Corporation. The outstanding balance carries a rate of return to be computed annually. The rate for 2004 was 3.64% (2003: 4.49%).

## Notes to the Financial Statements (continued)

For the year ended December 31, 2004

### 8 Equity Funds

(US\$ million)	2004	2003
Listed equity investments	26.9	17.8
Unlisted equity investments	167.9	145.2
	194.8	163.0
Provision for impairment	(27.8)	(22.0)
	167.0	141.0

Unlisted equity securities held by the equity funds are carried by the Corporation at cost less any impairment losses, since the fair value of these investments cannot be reliably determined. There is no active market for these investments and there have not been any recent transactions that provide evidence of the current fair value.

The following is a summary of movements in the balance of provisions for impairment of equity funds.

(US\$ million)	2004	2003
Balance at beginning of the year	22.0	30.7
Amounts utilised	-	(14.4)
Charge for the year	5.8	5.7
<b>Balance at end of the year</b>	<b>27.8</b>	<b>22.0</b>

### 9 Investment in Projects and Equity Participations

(US\$ million)	2004	2003
Project investments equity accounted	195.3	127.2
Other project investments and equity participations	265.7	210.7
	461.0	337.9
Provision for impairment	(54.0)	(55.6)
	407.0	282.3

#### a) Investments equity accounted

Details of investment in projects which are equity accounted are as follows:

	Share of capital held %	Carrying Value	
		(US\$ million) 2004	(US\$ million) 2003
Bitumat Company Ltd.	100.0	18.1	18.7
Gulf Paramount for Electric Services WLL	92.5	3.7	3.0
GIC Technology Partnership Co.	80.0	4.1	-
Gulf Industrial Investment Co.	50.0	42.1	39.7
Delta Gulf Services FZ LLC	50.0	0.3	0.5
Al Ezzel Power Co.	45.0	0.3	-
Bahrain Industrial Pharmaceutical Co.	40.0	0.7	0.7
The National Titanium Dioxide Co, Ltd.	33.0	36.6	31.7
A'Saffa Poultry Farms SAOG	30.9	3.2	4.2
Al Manar Plastic Products Co.	30.0	0.6	0.6
Kuwait International Advanced Industries Co.	25.0	2.5	0.7
Oman Fibre Optic Co. SAOG	25.0	3.3	-
Technical Supplies and Services Co.	25.0	3.9	-
Interplast Co. Ltd.	23.5	14.3	13.1
Celtex Weaving Mills E.C.	23.0	1.2	1.2
Rawabi Emirates (PJSC)	22.5	14.1	13.1
Wataniya Telecom Algeria	20.0	34.4	-
Gulf Stone Co.	20.0	0.5	-
Advanced Electronics Co.	20.0	11.4	-
		195.3	127.2

All the above entities except Wataniya Telecom Algeria (registered in Algeria) are incorporated within GCC.

Gulf Stone Company and Advanced Electronics Company were included within equity participations in the previous year.

#### b) Other project investments and equity participations

(US\$ million)	2004	2003
Listed investments	148.6	71.2
Unlisted investments	117.1	139.5
	265.7	210.7

Unlisted investments are carried at cost less any impairment losses, since the fair value of these investments cannot be reliably determined. There is no active market for these investments and there have not been any recent transactions that provide evidence of the current fair value.

## Notes to the Financial Statements (continued)

For the year ended December 31, 2004

### 9 Investment in Projects and Equity Participations (continued)

#### c) Provision for impairment in investment in projects and equity participations

The movement in the provisions was as follows:

(US\$ million)	2004	2003
Balance at beginning of the year	55.6	30.1
Amounts utilized	(2.3)	-
Net charge for the year	0.7	25.5
<b>Balance at end of the year</b>	<b>54.0</b>	<b>55.6</b>

### 10 Property and Other Fixed Assets

(US\$ million)	Cost	Accumulated depreciation	2004 Net book value	2003 Net book value
Building and installations	28.8	6.7	22.1	23.7
Furniture, equipment and motor vehicles	8.8	6.9	1.9	2.5
	37.6	13.6	24.0	26.2

There were no significant additions or disposals during the year. The depreciation charge for the year is US\$ 2.7 million (2003: US\$ 2.8 million).

### 11 Other Assets

(US\$ million)	2004	2003
Accrued interest, fees and commissions	94.6	78.0
Derivative assets used for hedging	6.8	54.7
Employees' end of service benefit asset	32.4	28.9
Goodwill arising on acquisitions	28.1	22.2
Prepayments	1.0	1.0
Trade receivables	0.1	-
Other, including accounts receivable	7.5	6.9
	<b>170.5</b>	<b>191.7</b>

### 12 Deposits

(US\$ million)	2004	2003
Deposits from Central Banks	409.7	308.9
Deposits from other banks	1,202.5	914.3
Islamic deposits	392.5	490.6
Other deposits	352.6	190.2
	<b>2,357.3</b>	<b>1,904.0</b>

At December 31, 2004 deposits from GCC Country Governments, Central Banks and other institutions headquartered in the GCC States amounted to US\$ 1,502.6 million (2003: US\$ 1,329.9 million).

### 13 Term Finance

(US\$ million)	2004	2003
Saudi Riyal Floating rate loan due in 2004	-	160.0
GIC Floating Rate Note due in 2007	300.0	300.0
GIC Floating Rate Note due in 2009	500.0	-
	<b>800.0</b>	<b>460.0</b>

### 14 Other Liabilities

(US\$ million)	2004	2003
Accrued interest	87.2	52.5
Derivative liabilities used for hedging	111.7	72.4
Employees' end of service benefits	35.4	31.4
Other provision	3.5	3.6
Other, including accounts payable and accrued expenses	12.7	12.4
	<b>250.5</b>	<b>172.3</b>

## Notes to the Financial Statements (continued)

For the year ended December 31, 2004

### 15 Shareholders' Equity

**15.1** The authorised and issued capital comprises of 2.1 million shares of US\$ 1,000 each (2003: 2.1 million shares of US\$ 1,000 each). The paid up capital is US\$ 750 million (2003: US\$ 750 million).

**15.2** In accordance with the Kuwait Commercial Companies' Law and the Corporation's Articles of Association, 10 percent of the net income for the year is required to be transferred to the non-distributable compulsory reserve until the reserve reaches a minimum of 50 percent of share capital.

**15.3** In accordance with the Corporation's Articles of Association, 10% of the net income for the year is required to be transferred to the voluntary reserve. The transfer to this reserve can be discontinued by a resolution adopted in the general assembly meeting of the shareholders.

**15.4** The unrealised gain on available-for-sale assets comprises the cumulative net change in the fair value of available-for-sale assets held by the Corporation.

### 16 Other Operating Income

(US\$ million)	2004	2003
Net gain on trading securities and managed funds	34.3	28.6
Net gain on investment securities	6.0	0.8
Net gain on sale of investment in projects and equity participations	0.3	-
Net gain on disposal of available-for-sale investments transferred from shareholders' equity	14.4	3.6
Income from equity funds	11.4	5.1
Income from projects and equity participations	26.2	26.0
Profit on foreign exchange	0.3	0.6
Dividend income	10.4	6.6
Fees, commissions and sundry income	14.1	15.9
	<b>117.4</b>	<b>87.2</b>

### 17 Provision for Impairment Losses

(US\$ million)	2004	2003
Equity funds	(5.8)	(5.7)
Projects and equity participations	(0.7)	(25.5)
Loans and loan guarantees	0.3	0.2
Investment securities	1.1	3.0
Accounts receivables	-	(3.0)
	<b>(5.1)</b>	<b>(31.0)</b>

### 18 Extraordinary Item

This represents compensation received from the United Nations Compensation Commission ("UNCC") in settlement of the claim filed by the Corporation for losses incurred as a result of the Iraqi invasion and occupation of Kuwait in 1990.

### 19 Retirement and other terminal benefits

The Corporation has defined voluntary contribution and end of service indemnity plans which cover all its employees. Contribution to the voluntary plan is based on a percentage of pensionable salary and consists of contribution by employees and a matched contribution up to a certain limit by the Corporation. Contribution to the end of service indemnity plan is based on a percentage of pensionable salary and number of years of service by the employees. The amounts to be paid as the end of service benefits are determined by reference to the amounts of the contributions and investment earnings thereon. The Corporation also pays contributions to government defined contribution pension plan for certain employees in accordance with the legal requirements in Kuwait.

The total cost of retirement and other end of service benefits included in staff expenses for the year ended December 31, 2004 amounted to US\$ 3.4 million (2003: US\$ 3.2 million).

### 20 Dividend

The Board of Directors have recommended a dividend of US\$ 120 per share for the year ended December 31, 2004 (2003: US\$ 100 per share). For the year 2003, a special dividend of US\$ 100.0 million was also paid. These will be utilized to settle receivable from shareholders (see note 7).

## Notes to the Financial Statements (continued)

For the year ended December 31, 2004

### 21 Asset and Liability Maturity Profile

(US\$ million)	Within 3 months	3 months to 1 year	1 to 5 years	Over 5 years	Total
<b>At December 31, 2004</b>					
<b>Assets</b>					
Cash and bank balances	10.7	-	-	-	10.7
Placements and money market funds	549.4	9.9	-	8.7	568.0
Trading securities and managed funds	18.8	-	-	568.8	587.6
Investment securities	234.0	579.2	2,251.6	1,571.3	4,636.1
Loans and credit funds	59.4	82.6	148.4	201.1	491.5
Receivable from shareholders	90.0	30.0	74.2	-	194.2
Equity funds	6.8	2.4	45.6	112.2	167.0
Investments in projects and equity participations	-	-	-	407.0	407.0
Property and other fixed assets	-	-	-	24.0	24.0
Other assets	74.2	34.7	1.0	60.6	170.5
<b>Total assets</b>	<b>1,043.3</b>	<b>738.8</b>	<b>2,520.8</b>	<b>2,953.7</b>	<b>7,256.6</b>
<b>Liabilities and shareholders' equity</b>					
Securities sold under repurchase agreements	2,033.6	494.1	-	-	2,527.7
Deposits	2,101.5	255.8	-	-	2,357.3
Term finance	-	-	800.0	-	800.0
Other liabilities	71.4	140.5	-	38.6	250.5
Shareholders' equity	-	-	-	1,321.1	1,321.1
<b>Total liabilities and shareholders' equity</b>	<b>4,206.5</b>	<b>890.4</b>	<b>800.0</b>	<b>1,359.7</b>	<b>7,256.6</b>
<b>At December 31, 2003</b>					
<b>Total assets</b>	<b>727.9</b>	<b>856.3</b>	<b>2,852.5</b>	<b>2,258.6</b>	<b>6,695.3</b>
<b>Total liabilities and shareholders' equity</b>	<b>3,470.8</b>	<b>1,677.5</b>	<b>303.5</b>	<b>1,243.5</b>	<b>6,695.3</b>

The asset and liability maturity profile is based on contractual repayment arrangements and as such does not take account of the effective maturities of deposits and of borrowers' right to prepay obligations with or without prepayment penalties.

### 22 Asset and Liability Repricing Profile and Effective Interest Rates

(US\$ million)	Within 3 months	3 months to 1 year	Over 1 year	Non-interest bearing items	Total	Effective interest rate %
<b>At December 31, 2004</b>						
<b>Assets</b>						
Cash and bank balances	10.7	-	-	-	10.7	-
Placements and money market funds	549.4	9.9	-	8.7	568.0	3.06
Trading securities and managed funds	-	-	-	587.6	587.6	-
Investment securities :						
Fixed rate	127.4	289.3	63.4	(1.6)	478.5	5.96
Floating rate	2,266.1	1,618.9	-	-	3,885.0	2.80
Equities & Funds	-	-	-	272.6	272.6	-
Loans and credit funds	404.2	88.1	-	(0.8)	491.5	2.41
Receivable from shareholders	90.0	30.0	74.2	-	194.2	3.64
Equity funds	-	-	-	167.0	167.0	-
Investment in projects and equity participations	-	-	-	407.0	407.0	-
Property and other fixed assets	-	-	-	24.0	24.0	-
Other assets	-	-	-	170.5	170.5	-
<b>Total assets</b>	<b>3,447.8</b>	<b>2,036.2</b>	<b>137.6</b>	<b>1,635.0</b>	<b>7,256.6</b>	
<b>Liabilities &amp; shareholders' equity</b>						
Securities sold under repurchase agreements	2,033.6	494.1	-	-	2,527.7	2.09
Deposits	2,101.5	255.8	-	-	2,357.3	2.44
Term finance	800.0	-	-	-	800.0	2.77
Other liabilities	-	-	-	250.5	250.5	-
Shareholders' equity	-	-	-	1,321.1	1,321.1	-
<b>Total liabilities and shareholders' equity</b>	<b>4,935.1</b>	<b>749.9</b>	<b>-</b>	<b>1,571.6</b>	<b>7,256.6</b>	
Derivative instruments	389.0	(389.0)	-	-	-	-
Interest rate sensitivity gap	(1,098.3)	897.3	137.6	63.4	-	-
<b>Cumulative interest rate sensitivity gap</b>	<b>(1,098.3)</b>	<b>(201.0)</b>	<b>(63.4)</b>	<b>-</b>	<b>-</b>	
<b>At December 31, 2003</b>						
Interest rate sensitivity gap	(631.0)	80.8	780.5	(230.3)	-	-
<b>Cumulative interest rate sensitivity gap</b>	<b>(631.0)</b>	<b>(550.2)</b>	<b>230.3</b>	<b>-</b>	<b>-</b>	

The repricing profile is based on the remaining period to the next interest repricing date. The repricing profiles of floating rate investment securities and loans incorporate the effect of interest rate swaps used to modify the interest rate characteristics of specific transactions.

## Notes to the Financial Statements (continued)

For the year ended December 31, 2004

### 23 Commitments and Contingent Liabilities

In the usual course of meeting the requirements of customers, the Corporation has commitments to extend credit and provide financial guarantees and letters of credit to guarantee the performance of customers to third parties. The credit risk on these transactions is generally less than the contractual amount. The table below sets out the notional principal amounts of outstanding commitments and the risk-weighted equivalents calculated in accordance with the capital adequacy guidelines of the Bank for International Settlements.

#### Credit Risk Amounts

(US\$ million)	2004		2003	
	Notional principal amount	Risk-weighted equivalent	Notional principal amount	Risk-weighted equivalent
Transaction-related contingent items	50.2	50.2	95.4	95.4
Undrawn loan commitments and underwriting commitments under note issuance and revolving facilities	6.1	1.5	7.4	1.8
	<b>56.3</b>	<b>51.7</b>	102.8	97.2

The above commitments and contingent liabilities have off balance-sheet credit risk because only origination fees and accruals for probable losses are recognized in the balance sheet until the commitments are fulfilled or expired. Many of the contingent liabilities and commitments will expire without being advanced in whole or in part. Therefore, the amounts do not represent expected future cash flows.

### 24 Derivatives and Foreign Exchange Products

Derivatives and foreign exchange instruments are utilised by the Corporation to meet the needs of its customers, to generate trading revenues and as part of its asset and liability management (ALM) activity to hedge its own exposure to market, interest rate and currency risk.

In the case of derivative transactions the notional principal typically does not change hands. It is simply a quantity, which is used to calculate payments. While notional principal is a volume measure used in the derivatives and foreign exchange markets, it is neither a measure of market nor credit risk. The Corporation's measure of credit exposure is the cost of replacing contracts at current market rates should the counterparty default prior to the settlement date. Credit risk amounts represent the gross unrealised gains on transactions before taking account of any collateral held or any master netting agreements in place.

#### Hedge accounting

Interest rate swaps under which the Corporation pays a fixed rate and receives a floating rate are used in fair value hedges of fixed interest securities available-for-sale.

As at the balance sheet date the notional amount of interest rate swaps used to hedge interest rate risk amounted to US\$ 2,415.3 million (2003: US\$1,837.9 million) and its net fair value was a swap loss of US\$ 113.2 million (2003: US\$ 73.7 million). The corresponding gain on the hedged fixed income securities amounted to US\$ 110.2 million (2003: US\$ 71.0 million).

### Trading activities

The table below summarises the aggregate notional, net fair value and credit risk amounts of foreign exchange and derivative financial instruments held for trading.

(US\$ million)	Notional amounts	Net fair values	Credit risk amounts
<b>As at December 31, 2004</b>			
<b>Foreign exchange contracts</b>			
Unmatured spot, forward and futures contracts	1,156.5	0.9	1.1
<b>Interest rate contracts</b>			
Interest rate swaps	27.9	-	0.1
	<b>1,184.4</b>	<b>0.9</b>	<b>1.2</b>

#### As at December 31, 2003

<b>Foreign exchange contracts</b>			
Unmatured spot, forward and futures contracts	654.3	0.5	0.7
<b>Interest rate contracts</b>			
Interest rate swaps	35.8	-	0.4
	<b>690.1</b>	<b>0.5</b>	<b>1.1</b>

### Counterparty analysis

(US\$ million)	Banks	Total
<b>At December 31, 2004</b>		
<b>Credit risk amounts</b>		
OECD countries	1.0	1.0
GCC countries	0.2	0.2
	<b>1.2</b>	<b>1.2</b>
<b>At December 31, 2003</b>		
<b>Credit risk amounts</b>		
OECD countries	0.6	0.6
GCC countries	0.5	0.5
	<b>1.1</b>	<b>1.1</b>

## Notes to the Financial Statements (continued)

For the year ended December 31, 2004

### 24 Derivatives and Foreign Exchange Products (continued)

#### Maturity analysis

(US\$ million)	Year 1	Years 2 & 3	Total
<b>At December 31, 2004</b>			
<b>Notional amounts</b>			
Foreign exchange contracts	1,156.5	-	1,156.5
Interest rate contracts	27.9	-	27.9
	<b>1,184.4</b>	<b>-</b>	<b>1,184.4</b>

#### At December 31, 2003

<b>Notional amounts</b>			
Foreign exchange contracts	654.3	-	654.3
Interest rate contracts	10.0	25.8	35.8
	<b>664.3</b>	<b>25.8</b>	<b>690.1</b>

### 25 Geographic Distribution of Risk Assets

(US\$ million)	Cash and bank balances, placements and money market funds and securities purchased under resale agreements	Trading, investment securities and managed funds	Loans and advances and receivable from shareholders
GCC	496.5	903.2	235.7
Other Middle East and North Africa	-	10.2	-
Europe	81.5	2,060.4	195.0
North America	0.6	2,074.3	255.0
Asia	0.1	175.6	-
	<b>578.7</b>	<b>5,223.7</b>	<b>685.7</b>

(US\$ million)	Equity funds, investment in projects & equity participations	Commitments and contingent liabilities	2004 Total	2003 Total
GCC	373.3	56.3	2,065.0	1,967.9
Other Middle East and North Africa	34.4	-	44.6	10.6
Europe	30.7	-	2,367.6	2,047.5
North America	105.8	-	2,435.7	2,349.9
Asia	29.8	-	205.5	204.3
	<b>574.0</b>	<b>56.3</b>	<b>7,118.4</b>	<b>6,580.2</b>

An analysis of derivatives and foreign exchange products is set out in note 24.

### 26 Fair Value Information

As at the balance sheet date the fair value of financial assets and financial liabilities that are not carried at fair value is not materially different from their carrying amounts, except for debt and other interest bearing instruments held-to-maturity (see note 5), whose fair value is US\$ 7.4 million higher than its carrying value (2003: US\$ 8.5 million higher than its carrying value) and certain unlisted equity securities whose fair value cannot be reliably determined (see note 8).

Fair value is the amount at which an asset, liability or financial instrument could be exchanged or settled between knowledgeable parties in an arm's length transaction. Underlying the definition of fair value is the presumption that the Corporation is a going concern without any intention, or need, to liquidate, curtail materially the scale of its operations or undertake a transaction on adverse terms.

### 27 Related Party Transactions

During the year certain transactions were conducted with parties that have a direct or indirect relationship with the Corporation's shareholders. These comprised standard money market, foreign exchange, investment, lending and securities transactions and were conducted on an arm's length basis at open market prices. The volume of such transactions are disclosed in respective notes to the financial statements.

### 28 Fiduciary Activities

At December 31, 2004 third party assets under management amounted to US\$ 104.9 million (2003: US\$ 412.4 million). These assets are managed in a fiduciary capacity and are therefore excluded from the balance sheet.

### 29 Comparatives

Where necessary, comparative figures have been adjusted to conform with changes in presentation in the current year.

(US\$ million)	Location	Total Shareholders' Equity	GIC's Share of Capital (%)
<b>Non-consolidated subsidiary and associated companies</b>			
Bitumat Company	Saudi Arabia	18.1	100.0
Gulf Paramount for Electric Services WLL	Kuwait	4.0	92.5
Gulf Industrial Investment Company	Bahrain	84.2	50.0
Delta Gulf Services (DGS)	UAE	0.6	50.0
Bahrain Industrial Pharmaceutical Company	Bahrain	1.8	40.0
National Titanium Dioxide Company (CRISTAL)	Saudi Arabia	110.9	33.0
A'ssaifa Poultry Farms SAOG	Oman	10.4	30.9
Al-Manar Plastic Products Company	Saudi Arabia	1.0	30.0
Kuwait International Advanced Industries Co.	Kuwait	9.8	25.0
Interplast Company Limited	UAE	60.6	23.5
Celtex Weaving Mills Company	Bahrain	5.3	23.0
Rawabi Emirates (PJSC)	UAE	62.6	22.5
Al Ezzel Power Project	Bahrain	0.7	45.0
Wataniya Telecom Algeria	Algeria	172.0	20.0
Technical Supplies & Services Co.	UAE	15.6	25.0
Oman Fiber Optic Co.	Oman	13.2	25.0
GIC Technology Partnership	Kuwait	5.1	80.0
Gulf Stones Company	Oman	2.7	20.0
Advanced Electronics Company (AEC)	Saudi Arabia	56.8	20.0

**Equity Participations**

Arab Pesticide Industries Company (MOBEED)	Saudi Arabia	4.1	12.5
National Petrochemical Industrialization Company	Saudi Arabia	138.5	12.0
Arab Qatari Company for Gairy Products	Qatar	15.6	10.8
Al-Salam Aircraft Company	Saudi Arabia	65.1	10.0
Gulf Ferro Alloys Company (Sabayek)	Saudi Arabia	8.8	10.0
Jarir Marketing Company	Saudi Arabia	112.9	10.0
National Aluminium Products Company	Oman	14.8	10.0
Ras Laffan Power Company	Qatar	126.7	10.0
Zamil Industrial Investment Company (ZIC)	Saudi Arabia	134.1	10.0
National Pharmaceutical Industries Company	Kuwait	5.0	6.5
Securities & Investment Company (SICO)	Bahrain	50.5	8.0
Al-Jubail Chemical Industrial Company (JANA)	Saudi Arabia	50.3	7.5
Gulf Aluminium Rolling Mill Company (GARMCO)	Bahrain	103.3	5.9
Arabian Industrial Fibers Company (Ibn Rushd)	Saudi Arabia	482.5	4.7
International Fish Farming Company	UAE	54.8	4.0
United Power Company	Oman	126.0	2.3
Oasis International Leasing Company (WAHA)	UAE	146.9	2.0
Thuraya Satellite Telecommunications Company	UAE	325.7	1.6
Qatar Telecom Company (Q-TEL)	Qatar	909.1	0.6
Al-Razi Holding Co.	Kuwait	172.2	2.0

**Senior Management**

Chief Executive Officer &amp; General Manager

**Hisham Abdulrazzaq Al-Razuqi**

Deputy General Manager &amp; Head of Finance &amp; Administration

**Rashid Bin Rasheed****Global Markets**

Head of Global Markets

**Riccardo Ricciardi**

Head of Treasury

**Mahmood Al-Aradi**

Head of Debt Capital Markets

**Abdulaziz Al-Mulla**

Funding &amp; Liquidity

**Martin Joy**

Money Markets

**Mathew Abraham**

Head of Business Development

**Malek Al-Ajeel**

Alternative Investments

**Romeo Briones**

GCC Fund Management

**Waleed Al-Braikan**

GCC Client Portfolios

**Talal Al-Tawari****Principal Investing**

Head of Utilities &amp; Financial Services &amp; Corporate Finance

**Shafic Ali**

Head of Corporate Finance

**Mahmoud Rateb**

Head of Manufacturing Projects

**Khaled Al-Qadeeri**

Head of GCC Diversified Projects

**Mohammad Al-Melhem****Finance & Administration**

Head of Human Resources

&amp; Administration

**Hani Al-Meer**

Head of Financial Control

**Hazem El-Rafie**

Head of Information Technology

**Hani Al-Shakhs**

Head of Operations

**Shawki Khalaf**

Head of Communications

&amp; Public Relations

**Qais Al-Shatti**

Head of Economics &amp; Strategy

**Dr. Soliman Demir**

Head of Risk Management

**Nabil Guirguis**

Head of Internal Audit

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