



Chairman's Statement



Dear Shareholder,

ON MY AND YOUR BOARD OF DIRECTORS' BEHALF, I am pleased to present the Annual Report of United Gulf Bank B.S.C., for the financial year ended 31 December 2009.

The financial and economic conditions characterized as the 'panic of 2008' have ushered in an era of uncertainty. There are doubts regarding the global economy's recovery from the financial crisis and recession. Equally, there are uncertainties about the speed of recovery in various countries, despite the support and commitment from their Central Banks. The increasing number of financial institutions seeking restructuring or extension of their liabilities is a stark reminder that the impact of past excesses is still working its way through the global financial system. Governments are no longer willing to extend guarantees to quasi-public entities, partly because the global crisis has moderated, and partly because governments are realizing the fiscal and social cost of repeated bailouts. It is evident that real growth will commence only when there is lower unemployment and tangible evidence of restored consumer spending, independent of fiscal stimulus.

The ongoing lack of confidence and liquidity concerns during 2009 resulted in regional stock markets ending the year on a mixed note with four out of seven GCC bourses posting a gain. Saudi Arabia's Tadawul Al Share Index recorded a year on year increase of 27.5%, while the Bahrain Stock Exchange was the worst performing regional market with a negative return of 19.2%. The Kuwait Stock Exchange also had a lackluster performance with a drop of 9.9% in its price index during the course of 2009. The combined market capitalizations of the seven GCC bourses fell by 2.03% to US\$ 682.6 billion.

From the beginning of 2009, our expectations were that the year would be a challenging one for investment banking. The continued erosion in asset values added further pressure to many sectors and to the overall economic situation. Commercial banking and investment banking sectors were the hardest hit by the financial turmoil as financial institutions grappled with the issues of poorly performing loans and investments. Under these difficult circumstances, I am pleased to report that your Bank posted its twenty sixth year of positive performance in its 30 year history, with a net income of US\$ 20.1 million for 2009. While this is significantly below last year's results of US\$ 207.2 million, we note that the 2008 results included the exceptional gains resulting from the sale of Jordan Kuwait Bank.

UGB's performance in 2009

UGB's business model is based on the three pillars of asset management and investment banking, commercial banking, and financial brokerage, through its network of financial and non financial subsidiaries and associates in the MENA region. As part of our parent company's ongoing strategy to enhance shareholder value, UGB transferred its holdings in Gulf Bank Algeria and the Bank of Baghdad for US\$ 150 million in the first quarter of 2009. This resulted in UGB recording a gain of US\$ 26.2 million after expenses on this transaction.

Another significant divestment made by UGB during the year was the 17% consolidated stake in the Kuwait Clearing Company for US\$ 78.4 million, which resulted in a gain of US\$ 33.7 million after expenses.

Other contributors to revenues in 2009 came from investment related income, interest income and fees and commissions. Total revenue for 2009 was US\$ 124.5 million, down from US\$ 341.4 million in 2008.

The Bank's drive to reduce costs during the year resulted in a 28.3% fall in operating expenses to US\$ 40.5 million from US\$ 56.5 million in 2008. This reflects our commitment to observe the prudent financial discipline that is demanded by a difficult environment. It is also significant that the impairment loss on investments held in UGB's 'available for sale' book was significantly lower at US\$ 10.2 million compared to US\$ 56.6 million in 2008.

Other key performance indicators in 2009 include earnings per share of US 2.46 cents (2008: US 25.3 cents), a return on average equity of 3.4% (2008: 30.4%), and a return on average assets of 0.9% (2008: 7.5%). Assets under management at the end of 2009 were US\$ 7.2 billion (2008: US\$ 9 billion). As mandated by the Central Bank of Bahrain, the Bank became Basel II compliant on 1 January 2008. The capital adequacy ratio defined by these standards stood at 14.5% as at 31 December 2009 on a consolidated basis (2008: 17.2%).

UGB's regional network

Business and asset diversification has been the cornerstone of UGB's strategy for many years. This strategy provides a balance to our income streams and allows UGB to manage a varied and promising investment portfolio. As a result, while our primary focus continues to be in financial services companies, UGB also holds investments in sectors such as real estate, manufacturing, hospitality, healthcare, communication and education. UGB's strategy of expanding its asset management and investment banking capabilities across the GCC and MENA region is based on our ability to leverage the experience and market knowledge we have gained, through launching green-field or developing commercial banking businesses in Algeria, Syria, Jordan and Iraq.

During 2009, UGB increased its stake in KIPCO Asset Management Company (KAMCO), our flagship Kuwaiti subsidiary, to 85.5%. KAMCO is Kuwait's leading asset manager with over US\$ 7.6 billion in assets under management. KAMCO posted almost a 422% increase in net income to US\$ 21.1 million during 2009, up from US\$ 4.2 million in 2008. The company achieved this increase through realizing gains on sales of investments 'available for sale' and its dividend income. KAMCO's three business divisions consist of asset management, financial services, and investment advisory and research.

The firm was appointed by KIPCO as the sole and exclusive acquisition advisor for KIPCO's KD 100 million Acquisition Program which is committed to supporting the national economy. This program is targeting Kuwaiti companies identified as having growth potential, through cash acquisitions, asset swaps, or subscription in capital increases. KAMCO's shortlisting in the 'Best Asset Management House' category at the *Banker Middle East Industry Awards 2009* by

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a jury comprising industry experts, rating agencies and independent consultants, is a testimony to its in-depth equity research capabilities. It is also significant that KAMCO was the only company from Kuwait to be nominated in the ‘Best Asset Management House’ category in those awards.

During 2009, UGB acquired an additional 14% stake in the North Africa Holding Company (NAFH), a Kuwait-based company that is a private equity partner in startup ventures and former state-controlled companies in emerging North African countries. NAFH’s net income for 2009 was US\$ 9.5 million, compared to a loss of US\$ 34.4 million in 2008. Despite the challenging environment, NAFH realized solid earnings from the value of its trading securities and dividend income.

2009 was a year of expansion for UGB’s Syrian commercial banking operation, Syria Gulf Bank (SGB), which UGB co-founded in September 2006 with a 24% stake. Five new branches were opened during the year as SGB continued to build its brand recognition campaign. SGB’s progress was recognized when it won ‘The Best Bank in Syria 2009’ award from *The Banker* magazine. The award measures overall results, including qualitative achievements and strategic initiatives.

A leading factor in SGB’s performance during the year was its adoption of a new corporate philosophy where it combined excellence with market-leading products, and a strong visual identity to forge brand recognition and a closer relationship with consumers. It is remarkable that within three years, SGB has established such a strong image within the Syrian market. In January 2010, UGB acquired an additional 7% stake in the bank, signifying its belief in the future prospects of SGB.

UGB’s Tunisian subsidiary, Tunis International Bank (TIB), set a historical record in 2009 when it posted an income of US\$ 30.9 million – its highest ever consolidated operating total. This is an increase of 15.7% over the US\$ 26.7 million achieved in 2008. The strong revenues came from the sale of stakes in investments, net interest income, fees and commissions, dividend income and foreign exchange gains. Loan loss provisions of US\$ 10.8 million dampened an otherwise stellar performance and resulted in net income decreasing to US\$ 12.6 million for 2009, compared to US\$ 19.9 million in 2008.

Other important investments in UGB’s diversified non financial portfolio are United Real Estate Company (one of the largest real estate companies in Kuwait in the business of real estate investment and property development, as well as the management of commercial hospitality and entertainment properties in and outside Kuwait), United Networks Company (a communications company in Kuwait), Kuwait Education Fund (a fund investing in education related companies and projects), and the United Industries Company (a holding company holding various industrial and commercial interests).

Within the framework of the KIPCO Group’s restructuring plan, UGB was to use the proceeds of the US\$ 725 million gained from the sale of its regional banks to acquire a maximum 20% equity stake in Burgan Bank by subscribing to a special rights share issue. This deal was subject to procuring the necessary regulatory approvals including a Kuwaiti Amiri Decree. The Decree was not received within the Central Bank of Kuwait’s stipulated deadline of 31 December 2008, and consequently, this aspect of the transaction could not be completed. Burgan Bank is still moving forward with the regulatory process to increase its capital, and UGB stands by its intention to invest in the equity as it will provide opportunities for enhancing its asset management and investment banking business.

Credit ratings

UGB is rated by both Capital Intelligence Ltd and Moody’s Investor Services. In an economic climate where downgrades are increasingly common, it is a reflection of the soundness of UGB’s strategy and management that the Bank’s investment grade ratings remains unchanged.

In August 2009, Capital Intelligence reaffirmed its assignment of a BBB+ long term rating and A2 short term rating, with a ‘stable outlook.’ UGB’s financial strength was also affirmed at BBB+. In September 2009, Moody’s reaffirmed its Baa3/Prime-3 deposit rating and D+ bank financial strength rating. While the outlook remained negative, Moody’s stated that this was more of a systemic issue driven by the ‘increasingly challenging operating environment for investment banking and asset management.’

Liquidity

UGB’s liquidity position continues to be strong. In order to strengthen it further and also to demonstrate its support, in October 2009 our parent company, KIPCO, placed KD 40 million (US\$ 140 million) in a one year deposit with UGB at an arm’s length arrangement. Our liquidity continues to be monitored on a daily basis, in accordance with the Central Bank of Bahrain’s requirements.

Corporate governance

UGB’s corporate governance framework is centered on the fundamental premise that it is critical for creating long term value for our stakeholders. The Bank aspires to the highest standards of ethical conduct and best practices in reporting results with accuracy and transparency and maintaining full compliance with the laws, rules and regulations that govern its businesses in different jurisdictions. Our tradition of financial strength, good governance, conservative management and depth of expertise allow us to contribute towards creating a more stable financial sector within our region.

Chairman's Statement

Continued

UGB is also committed to maintaining excellent external and internal professional relationships. We maintain proactive dialogue with the regulators, our shareholders, credit rating agencies and the business communities where we operate. The strong, integrated working relationship between the Bank's Board of Directors, its Senior Management team and our Board and Management committees help UGB's efficiency and performance.

After twelve successful years at the helm of UGB as the Managing Director, Mr Masaud Hayat stepped down from this position at the end of 2009 to accept the role of Managing Director at Burgan Bank, Kuwait. I thank Mr Hayat for guiding the Bank successfully through challenging times. His contribution to UGB's progress has been immense and we are grateful that he continues to remain on the Board of Directors to share his valuable expertise.

In March 2010 Mr Mohammad Haroon retired as Acting Chief Executive Officer after twenty nine years of service to UGB. I thank Mr Haroon for his loyalty and contribution towards the progress and success of the Bank, and am delighted that he has agreed to continue his association as Advisor and Secretary to the Board of Directors. His knowledge and business focus is invaluable to UGB. I also welcome Mr David Rhodes who was appointed as Chief Executive Officer to UGB in March 2010, having previously served as Group Head for KIPCO's financial services businesses. Given his experience and expertise, I am confident he will continue UGB's track record of creating shareholder value and profitability.

As of 31 December 2009, Directors own 636,600 shares (636,600 shares in 2008) and Executive/Senior Management own 1,043,735 shares (1,906,597 shares in 2008) of the Bank, through the exercise of stock options. The staff of UGB have been granted 36.5 million shares, under the Bank's employee stock option plan as approved at the EGM held on 24 March 2004.

Thanks

On behalf of the Board, I extend our gratitude and best wishes to His Majesty, King Hamad Bin Isa Al Khalifa, His Royal Highness, Prince Khalifa bin Salman Al Khalifa, the Prime Minister of the Kingdom of Bahrain and His Royal Highness, Prince Salman Bin Hamad Al Khalifa, the Crown Prince and Deputy Supreme Commander of the Kingdom of Bahrain. Our gratitude is also extended to the Central Bank of Bahrain and its Governor H E Mr Rasheed Mohammed Al Maraj, the Wholesale Banking Supervision Directorate, the Capital Markets Supervision Directorate, the Ministry of Industry and Commerce, the Bahrain Stock Exchange and the Kuwait Stock Exchange, whose support and guidance are sincerely appreciated.

I thank our shareholders and all stakeholders for their faith and continued support, and extend my appreciation to our management and staff who have maintained their commitment and loyalty in contributing to our achievements and success. Based on our combined effort, I have no doubt that we can meet the goals that we have set for ourselves.



Faisal Al Ayyar
Chairman