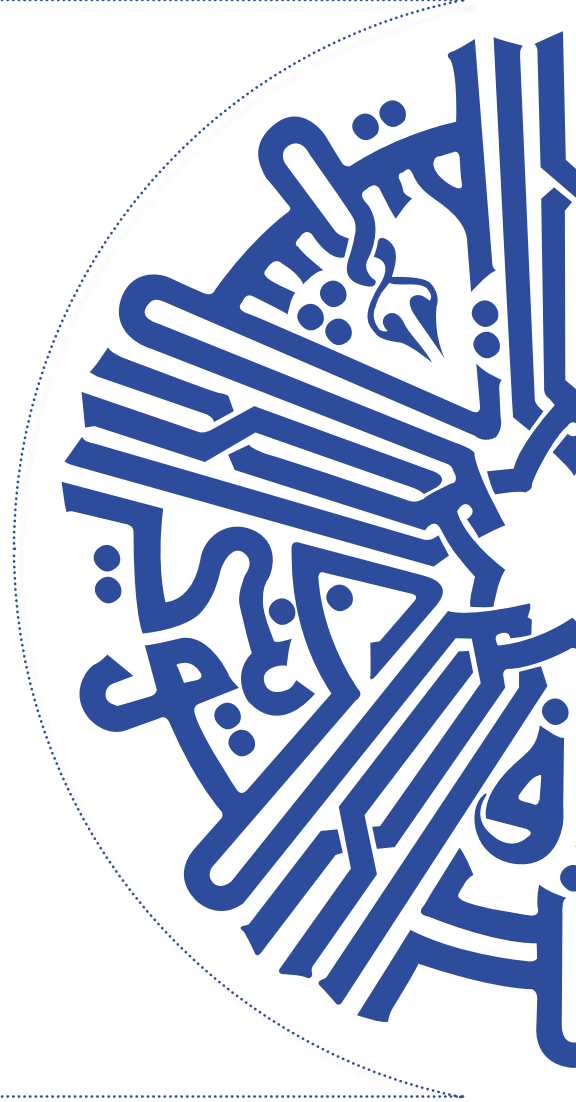


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**Notes To The
Financial
Statements And
Auditors Report**



Notes to the Financial Statement 31 March 2006

1- Constitution and activities

The Kuwait Fund for Arab Economic Development (“the Fund”) was established in December 1961 as a public institution incorporated in Kuwait with an independent juristic personality. The purpose of the Fund is to assist Arab and other developing countries in developing their economies by providing such countries with loans at preferential rates of interest and grants necessary for their development programs as well as providing loans to ministries and public institutions that undertake the execution of housing welfare projects in the State of Kuwait with all related infra structure, main services and public utilities.

These financial statements have been authorised for issue by the Board of Directors on 27 May 2006.

2. Significant accounting policies

The Minister of Finance issued a decree on 16 November 2005 to amend some of the Fund’s accounting policies in accordance with a resolution adopted by the Fund’s Board of Directors held on 2 June 2004.

The Fund management has postponed adoption of the revised accounting policies as it was not practical to apply them to the financial statements of the year ended 31 March 2006. Accordingly, these financial statements have been prepared based on the same accounting policies applied in the previous year.

The financial statements have been prepared under the historical cost measurement bases in accordance with Law No. 25 of 1974 as amended by decree enacting Law No. 18 of 1981 and No. 47 of 1988 and Law No. 31 of 2003.

2.1 Investments

Investments comprising quoted or otherwise readily realisable financial instruments are stated at the lower of cost or market value on an aggregate portfolio basis. Other investments are stated at cost less provision for any decline in value other than temporary, made on an individual basis.

2.2 Participations in development institutions

Participations in international and regional development institutions are stated at cost.

2.3 Development loans

Loans are stated at the amount of principal outstanding as of the date of the financial statements.

The Fund does not sell its loans and generally does not reschedule repayment terms of loans. If any payment of interest or principal is more than 30 days overdue, the right of further draw downs on all facilities to a country is then suspended. The Board of Directors has established a special reserve on a prudent basis to cover credit risks by transferring provisions needed from general reserve.

2.4 Property, plant, and equipment

Property, plant and equipment are fully depreciated in the year of acquisition. Gain on sale of property, plant, and equipment is shown under other income at its selling price.

2.5 Employees' terminal benefits

Provision is made for amounts payable to employees in accordance with internal regulations of the Fund and based on the employee's accumulated period of service at the balance sheet date. The Fund contributes to the social security of Kuwaiti staff as it accrues in accordance with Kuwait Social Security Law.

2.6 Revenue recognition

Interest income on marketable bonds, treasury bills, bonds and certificates of deposit, is recognised on time proportion basis. Dividend income is recognised when received in cash by the Fund or its investment managers. Interest on loans is accrued at contractual rates on the balance of principal outstanding. Interest received in cash is taken to income, and the balance, representing overdue interest and accrued interest not yet due, are suspended and included in other liabilities.

2.7 Foreign currencies

The functional currency of the Fund is the Kuwaiti Dinar. Foreign currency transactions are recorded at the rates of exchange ruling at the dates of the transactions. All assets and liabilities in foreign currencies at the balance sheet date are translated into Kuwaiti Dinars at the year-end rates of exchange. Any resulting gains or losses are taken to the general reserve.

2.8 Cash and cash equivalents

Cash and cash equivalents comprise of current accounts and demand deposits placed with banks.

9.9 Grants and technical assistance

Grants and technical assistance that the Fund provides are deducted from general reserve on disbursement. The cost of technical assistance is deducted from development loans granted to projects that prove feasible and which the Fund decides to finance.

2.10 Fiduciary accounts

The utilized amounts of grants and technical assistance granted by the Government of the State of Kuwait, which are managed by the Fund, are treated as off-balance sheet items. Income and expenses of these grants are not included in the Fund's books of account.

3- Investments

	31 March 2005	31 March 2006
Marketable securities and financial instruments, including cash balances in investment portfolios	1,224,639,917	1,095,339,567
Other investments	608,670,504	708,338,617
Provision for decline in value of investment	(107,449,850)	(105,881,636)
	<u>1,725,860,571</u>	<u>1,697,796,548</u>

Movements in provision for the decline in value of investment are as follows:

	31 March 2005	31 March 2006
Balance as at 1 April	135,822,488	107,449,850
Used during the year	(37,102,677)	(1,831,535)
Provision during the year	8,730,039	263,321
Balance as at 31 March	<u>107,449,850</u>	<u>105,881,636</u>

The market value of marketable securities and financial instruments, including cash balances in investment portfolios is KD 1,276,790,916 as of 31 March 2006 (31 March 2005: KD 1,331,845,684).

4- Participations in development institutions

Amount subscribed for 31 March 2006	Name of Institution	31 March 2005	31 March 2006
169,700,000	Arab Fund for Economic and Social Development	169,700,000	169,700,000
14,615,925	Arab Bank for Economic Development in Africa	14,615,925	14,615,925
59,647,206	African Development Fund	53,782,055	56,421,838
2,000,000	The Inter-Arab Investment Guarantee Corporation	2,000,000	2,000,000
34,041,442	African Development Bank	3,056,445	3,155,157
52,247,120	International Development Association	40,129,538	43,545,810
13,288,591	International Fund for Agricultural Development (IFAD)	9,934,899	10,448,611
<u>345,540,284</u>		<u>293,218,862</u>	<u>299,887,341</u>

All participations in development institutions are in the name of the State of Kuwait except for participation in The Inter - Arab Investment Guarantee Corporation which is in the name of the Fund.

5- Development loans

	31 March 2005	31 March 2006
Loans and direct credit commitments	3,559,690,353	3,727,054,224
Undisbursed loans	(779,217,050)	(773,103,765)
Loans disbursed	2,780,473,303	2,953,950,459
Loans repaid	(1,499,771,409)	(1,601,571,214)
Balance of principal outstanding	1,280,701,894	1,352,379,245

Undisbursed amounts include an amount of KD 8,433,684 as of 31 March 2006 (31 March 2005: KD 23,152,434) which represents irrevocable guarantees given to third parties on behalf of borrowers.

A special reserve for non-performing loans of KD 37,520,253 has been made as of 31 March 2006 (31 March 2005: 29,697,804) as follows:

	31 March 2005	31 March 2006
Total non-performing loans	162,175,299	228,344,656
Undisbursed amounts	(15,587,604)	(19,850,331)
	146,587,695	208,494,325
Repayments	(54,834,295)	(89,764,505)
	91,753,400	118,729,820

The balance comprises of:

Overdue installments	41,310,691	47,799,246
Installments not overdue	50,442,709	70,930,574
	91,753,400	118,729,820

The geographical distribution of loans is as follows:

	31 March 2005	31 March 2006
Arab countries	689,508,673	722,623,031
East & South Asia and the Pacific	177,709,453	201,040,143
West Africa	137,239,525	149,198,690
Central, South and East Africa	121,340,765	119,661,979
Central Asia and Europe	106,044,789	112,077,048
Caribbean and Latin America	48,858,689	47,778,354
	<u>1,280,701,894</u>	<u>1,352,379,245</u>

6- Accrued income and sundry receivables

	31 March 2005	31 March 2006
Accrued interest on loans	82,184,348	86,334,096
Accrued income on investment	13,713,134	11,188,491
Accrued income on time deposits	5,850,638	11,369,155
Sundry receivables	1,232,230	1,298,064
	<u>102,980,350</u>	<u>110,189,806</u>

7- Accounts payable and other liabilities

	31 March 2005	31 March 2006
Loan Interest in suspense	82,184,348	86,334,096
Public Authority for Housing Welfare	48,946,530	53,539,697
Other payables and accrued expenses	2,803,454	2,618,915
	<u>133,934,332</u>	<u>142,492,708</u>

Interest in suspense represents provisions against accrued interest on non-performing loans. Included in this amount is overdue interest of KD 17,308,862 as of 31 March 2006 (31 March 2005: KD 12,549,039).

The balance due to the public Authority for Housing Welfare represent appropriation from the Fund's net profit in accordance with Article 3 bis of law 25 of 1974 added by law 31 of 2003 and Board of Directors resolution dated 6 September 2004(Note 11).

8- Authorized and paid-up capital

In accordance with article 3 of Law 25 of 1974 as amended by Law 31 of 2003, the authorised and paid-up capital is KD 2,000,000,000, which was determined at end of the financial year 1997-1998.

9- General reserve

In accordance with article 3 and 3 bis of Law 25 of 1974 as amended by Law 31 of 2003, the net profit for the year is transferred to general reserve after deducting a percentage not exceeding 25% of the fund's net profit to be transferred to the Public Authority for Housing Welfare.

10- Special Reserve

To cover credit risk on a prudent basis, the Board of Directors has established a special reserve. During the year ended 31 March 2006 an amount of KD 7,882,449 was transferred (31 March 2005: KD 3,674,062) to special reserve in respect of amounts that were overdue from certain countries.

11- The Public Authority for Housing Welfare

In accordance with article 3 and 3 bis of law 25 of 1974 as amended by law 31 of law 31 of 2003 and accordance with Board of Directors resolution in its fourth meeting held on 6 September 2004 to transfer between 5% to 25% of the net profit for the year to the Public Authority for Housing Welfare.

12- Income from investments

	31 March 2005	31 March 2006
Income from investments	92,175,716	136,395,740
Income from deposits and certificates of deposit	12,151,491	22,767,822
	<u>104,327,207</u>	<u>159,163,562</u>

13- Staff costs

	31 March 2005	31 March 2006
Salaries and cash benefits	5,482,557	5,907,182
Training	337,995	362,341
End of service indemnity and leave expenses	165,005	235,046
Social and health insurance	436,056	487,171
	<u>6,421,613</u>	<u>6,991,740</u>
Number of staff (employees)	<u>388</u>	<u>401</u>

14- Commitments

	31 March 2005	31 March 2006
Uncalled capital - investments (Note 3)	100,077,708	138,225,996
Uncalled capital – participations in Development institutions (Note 4)	43,500,327	45,652,943
Undisbursed loans (Note 5)	779,217,050	773,103,765

15- Government grants - off balance sheet items

The undisbursed government grants received from the Government of the State of Kuwait, and which is managed by the Fund, was KD 20,349,343 as of 31 March 2006 (31 March 2005: KD 11,283,562).

Independent Auditor's Report

We have audited the attached balance sheet of Kuwait Fund for Arab Economic Development - Kuwaiti Public Institution - as at 31 March 2006 and the related statements of income, cash flows and changes in equity for the year then ended.

Respective responsibilities of the management and auditor

These financial statements are the responsibility of the Fund'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 International Standards on Auditing. Those Standards require that we plan and perform our 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 statements 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 Fund as of 31 March 2006, and of the results of its operations, and its cash flows for the year then ended in accordance with the accounting policies set out in Note 2 and comply with Law 25 of 1974 as amended by Laws 18 of 1981 and 47 of 1988 and Law 31 of 2003.

Furthermore, in our opinion proper books of account have been kept by the Fund and the financial statements are in accordance therewith, and a physical count was duly carried out.

Without qualifying our opinion, we draw attention to note (2) to the financial statements, which explain that the Fund's management decided to postpone application of the revised accounting policies adopted by the Board of Directors at its meeting held on 2 June 2004 and which were approved by a Minister of Finance decree on 16 November 2005. Accordingly, these financial statements were prepared using the same accounting policies as the previous year.

Bader A. Al Wazzan

Licence No. 62A

PricewaterhouseCoopers

Kuwait, 27 May 2006

