

Foreign Exchange and Economic Policy in Kuwait⁽¹⁾

The topic of my speech today concerns foreign exchange and economic policy in Kuwait. As you know, Kuwait was faced with a severe crisis during the past year as a result of the Iraqi invasion and occupation. Therefore, I feel it is important first to briefly explain the steps taken by the Central Bank of Kuwait after the liberation in order to restore the banking and financial system. These steps will define the environment that will influence the flow of funds within the Kuwaiti economy on the one hand, with the rest of the world on the other.

The Iraqi invasion and occupation on the second of August 1990 interrupted the normal flow of foreign currencies and KD funds into the Kuwaiti economy in several ways. The KD was taken from the flow equation, except for limited amounts exchanged for citizens and others in exile, to help them meet their living expenses. In addition, the flow of foreign exchange from the oil sector stopped, and our foreign assets became subject to freeze orders which imposed various degrees of limitation on access to them,

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depending on the particular jurisdictions, and the types of assets involved.

Perhaps you have noticed that income from our official foreign investments has grown close to the oil earnings of the state during recent years. The importance of our foreign investment was underlined during the past year, after the Iraqi invasion led to the cessation of oil exports, and Kuwait had to rely on investments to finance government functions and commitments overseas. This was made possible through the cooperation of various friendly authorities, in spite of the general freeze on our assets.

As most of you know, we worked immediately after the invasion to reconstruct the books of the Central Bank and other Kuwaiti banks. Then we developed arrangements to start meeting the Kuwaiti banks' obligations towards international banks and financial institutions. Meanwhile, we started planning for the post-liberation period, including the printing of new currency notes and means of meeting any liquidity pressures on the banks. We also prepared specific instructions regarding the resumption of bank operations after the liberation, with emphasis on efficiency of operations and preservation of depositors' rights.

Upon introduction of the new currency notes on March 24, 1991, the Central Bank also introduced certain restrictions on withdrawals and transfers. Due to technical and logistical considerations, a limit of four thousand Kuwaiti dinars per month for every individual was set for withdrawals from bank account and transfers into foreign currency. This limit did not cover transfers needed for legitimate economic activity, and exceptions were made for humanitarian purposes.

The limit on withdrawals and transfers was raised to six thousand KD last July, then it was removed completely on August 3rd. The removal was based on our firm belief in a free market economy, and on our conviction that lengthy and extensive controls are harmful and counterproductive. We also anticipated an upsurge of inflation, in view of the damage to the ports and transport system, and the supply network. Our data indicate that the consumer price index jumped to 85% in the early months after liberation, compared with less than two percent during 1989/90. Now we believe inflationary pressures have eased considerably, with the domestic price indicators during the two weeks ending on September 7, 1991 registering an increase of only 12.8% over the base period of May 1990.

