



بنك الكويت المركزي
CENTRAL BANK OF KUWAIT



THE THIRTY-THIRD

ANNUAL REPORT

FOR THE FISCAL YEAR 2004/05

**The Annual Report of the Central Bank of Kuwait
for the Fiscal Year 2004/05**

INTRODUCTION

The fiscal year 2004/05 was fraught with domestic, regional and international developments and events. Monetary and banking developments in the country during that fiscal year reflect the continuous efforts of the Central Bank of Kuwait (CBK) in areas connected to drawing and implementing monetary policy and overseeing the local banking and financial system units subject to its supervision, in line with domestic, regional and world developments, and in contribution to further firming the bases of monetary stability and strengthening the financial positions of the above mentioned units.

Within CBK's efforts aimed at boosting competition among the local banking and financial system units, as well as encouraging them to enhance their performance, upgrade their services and further strengthen their financial positions according to free market mechanisms, the Council of Ministers approved on 11/4/2004 the proposal of CBK to lift the government guarantee of customers deposits at local banks. The lifting, at this stage, of the government guarantee of customers deposits comes in light of positive indicators witnessed in the country's overall economic and financial conditions, particularly in the position of its banking and financial system, and signifies that the exceptional conditions and circumstances which previously led the government to intervene in support of the banking system and to guarantee customers deposits at local banks have ceased to exist.

Furthermore, the CBK continued its efforts for regulating the activities of banks operating according to the provisions of the Islamic Sharia', following the issuance of Law No. (30) of 2003 on the 25th of May 2003, which added a special section on Islamic banks to the Third Chapter of Law No. (32) of 1968, concerning Currency, the Central Bank of Kuwait and the Organization of Banking Business. In this regard, CBK issued a special manual on Islamic banks, encompassing the rules, policies,

regulations and instructions for the supervision of Islamic banks on sound bases that take into consideration the technical aspects of Islamic banking in the State of Kuwait. The Kuwait Finance House became subject to CBK's supervision, as it was registered in CBK's Register of Islamic banks on 22 May 2004. That was followed by the registration of Boubyan Bank in the same Register on 30 November 2004. Added to this is the pursuance of the procedures for the transformation of the Kuwait Real-Estate Bank into an Islamic bank, and the issuance of CBK's preliminary approval in this regard on 21 March 2004.

On another front, the year 2004 witnessed the issuance of amendments to certain provisions of Law No. (32) of 1968 concerning Currency, the Central Bank of Kuwait and the Organization of Banking Business, by virtue of Law No. (28) of 2004 issued on 27 January 2004. These amendments encompassed enhancing CBK's capabilities in regard to consolidated supervision over the external branches and affiliated companies of local banks, and the exchange of information with external supervisory authorities in this regard, along with allowing foreign banks to enter the domestic market, and setting a requirement of a minimum ratio of nationals in the total labor force of the banking and financial units subject to CBK's supervision, in line with the efforts expended for increasing the participation of the national labor force in economic activity, in addition to imposing constraints on ownership concentrations in local banks, and setting diversified and gradual penalties for violations committed by the banking and financial system units subject to CBK's supervision.

Within the context of allowing foreign banks to open branches in the State of Kuwait, the branch of the BNP Paribas Bank was entered in CBK's commercial banks' register on 7 March 2005. Also, permissions were granted to Abu Dhabi National Bank on January 2005 and HSBC Bank in February 2005, for each to open a branch in the State of Kuwait. Allowing foreign banks to open branches in the State of Kuwait comes within CBK's efforts for firming up the basis of competition among the banking system units in the national economy.

This Annual Report presents the most significant domestic monetary and banking developments during the fiscal year 2004/05, CBK's efforts in firming up the bases of monetary stability in the country and further strengthening the financial position of the banking and financial system units subject to its supervision, in addition to the

Auditors' Report, and CBK's balance sheet and profit and loss account for the fiscal year 2004/05, as follows:

First: The Main Monetary and Banking Developments:

Developments in the State of Kuwait principal monetary and banking variables and aggregates during the fiscal year 2004/05, reflect CBK's efforts in drawing and implementing monetary policy aimed at firming the bases of monetary stability, as well as establishing the conditions conducive to further strengthening the financial position of the local banking and financial system units in the State of Kuwait. The following are the most significant monetary and banking developments during the fiscal year 2004/05:

1- Monetary Developments:

A- Money Supply:

During the fiscal year 2004/05, Money Supply in its broad definition (M2) recorded a marked growth of KD 1209.2 million or 10.8% to KD 12392.4 million at end of the mentioned fiscal year, against KD 11183.2 million at end of the fiscal year 2003/04. This growth resulted from the rise in both Quasi-money by KD 961.2 million or 11.9% (from KD 8044.6 million to KD 9005.8 million) and Money (the narrow definition of money supply M1) by KD 248 million or 7.9% (from KD 3138.6 million to KD 3386.6 million).

Regarding the factors affecting changes in money supply within the aggregate monetary position of the CBK and local banks ⁽¹⁾ during the fiscal year 2004/05, the above rise of KD 1209.2 million or 10.8% in Money Supply (M2) was essentially the result of the increase in the net domestic assets of these institutions by KD 189.7 million (2.2%) and their net foreign assets by KD 1019.5 million (40.1%). The mentioned increase in net domestic assets is attributable to the outcome of the rise in local banks' claims on the private sector by KD 1206.8

(1) Local banks in this report encompass the commercial banks (National Bank of Kuwait, Commercial Bank of Kuwait, Gulf Bank Al-Ahli Bank of Kuwait, the Bank of Kuwait and the Middle-East, Burgan Bank, the Bank of Bahrain and Kuwait branch, and the BNP-Paribas Bank branch), the specialized banks (the Industrial Bank of Kuwait, and the Kuwait Real-Estate Bank), in addition to banks operating according to the provisions of Islamic Sharia' (the Kuwait Finance House and Boubyan Bank).

million or 12.2%, the government accounts with the CBK and deposits with local banks⁽¹⁾ by KD 278.1 million or 27.3%, and other net claims of the CBK and local banks by KD 451 million or 13.6% on the one hand, and the decline in the local banks' claims on the government by KD 287.9 million or 9.4%, on the other. The above mentioned rise in net foreign assets during the fiscal year 2004/05 is attributable to the increase in both the CBK's net foreign assets by KD 258.4 million or 13.5%, and the net foreign assets of local banks by KD 761.1 million or 120.6%.

B- Domestic Interest Rates:

In light of CBK's continual monitoring of developments in domestic interest rates on the Kuwaiti dinar, so as to ensure their consistency with domestic economic and monetary developments on the one hand, and their alignment with trends in interest rates on major currencies -chiefly the US dollar to which the KD exchange rate is pegged within specific margins- on the other, the CBK made during the fiscal year 2004/05 seven consecutive increases to its discount rate, on the 1st of July, 4th of August, 22nd of September, 11th of November and 15th of December 2004, and on the 3rd of February and 23rd of March 2005. These raises totaled 200 basis points, thus bringing the discount rate to 5.25% at end of the fiscal year 2004/05, against 3.25% at end of the previous fiscal year. Worth noting is that the above consecutive increases in the discount rate came after that rate remained at a record low of 3.25% during the previous fiscal year, unchanged since 7 November 2002.

Available data on the averages of interest rates on customers KD deposits with local banks during the fiscal year 2004/05, indicate that after these averages recorded their lowest during the first quarter of the fiscal year 2004/05 (April-June 2004), whereby they reached 1.20% and 1.32% for the one-month and three-month deposits respectively, they trended upward to reach 1.69% for the one-month deposits and 1.91% for the three-month deposits during the fourth quarter of the mentioned fiscal year (January-March 2005), compared with 1.49% and 1.57% for the mentioned terms respectively, during the fourth quarter of the previous fiscal year (January-March 2004).

(1) Includes deposits of the Credit and Savings Bank

In the same direction, interest rates on customers' US dollar time deposits during the fiscal year 2004/05, recorded a rise which exceeded the increase witnessed in the interest rates on their counterparts in Kuwaiti dinar. Specifically, data indicate that the averages of interest rates on US dollar deposits at local banks rose to 1.94% for the one-month term and 2.11% for the three-month term, during the fourth quarter of the fiscal year 2004/05 (January-March 2005), compared with 1.03% and 1.17% respectively during the second quarter of that fiscal year (July-September 2004). Consequently, the margins in favor of KD deposits between the averages of interest rates on KD and US dollar deposits at local banks contracted gradually during the fiscal year 2004/05, and turned in favour of the US dollar during the fourth quarter of that fiscal year.

Also, the averages of interest rates on the KD interbank deposits followed a general uptrend during the fiscal year 2004/05, compared to the previous fiscal year. Mention can be made in this regard to the rise in the averages of interest rates on the interbank deposits for the three-month term, which rose from 0.92% during the first quarter of the fiscal year 2004/05 (April-June 2004), to 1.41% during the fourth quarter (of the mentioned fiscal year (January-March 2005)).

Furthermore, an uptrend was witnessed during the fiscal year 2004/05 in the average interest rates on Public Debt Instruments, whereby the average of interest rates on the three-month Treasury Bills rose by 0.29 percentage point (from 1.69% in March 2004 to 1.98% in March 2005), and on the six-month Treasury Bills by 0.36 percentage point (from 1.83% in March 2004 to 2.19% in March 2005). During the same period, the average of interest rates on the one-year Treasury Bonds rose by 1.08 percentage point (from 2.75 % in March 2004 to 3.83% in March 2005).

C- The KD Exchange Rate:

Available data on the developments of the KD exchange rate during the fiscal year 2004/05 indicate that this rate maintained its manifest relative stability against the other major currencies, under the Kuwaiti dinar exchange rate policy, applied as of the beginning of 2003, which is based on pegging the exchange rate of the Kuwaiti

dinar against the US dollar within specific margins ($\pm 3.5\%$) around the parity exchange rate, set at 299.63 fils/dollar. During the fiscal year 2004/05, the difference between the highest and lowest exchange rates of the US dollar against the Kuwaiti dinar did not exceed 2.7 fils (294.70 fils and 292.00 fils) or 0.92%. In comparison with the parity rate, the farthest movement of the US dollar against the KD reached 7.67 fils (-2.6%), which is within the allowed ($\pm 3.5\%$) fluctuation band around the parity rate. The exchange rate of the US dollar against other major currencies witnessed more pronounced fluctuations during the mentioned fiscal year, whereby the difference between the highest and lowest exchange rates of the US dollar reached 16.8% against the Swiss franc, 15.5%, against the Euro, 12% against the Japanese yen, and 10.6% against the Sterling pound.

D- Bank Credit:

The balances of the utilized portion of cash credit facilities extended by local banks to the different domestic economic sectors reached KD 10075 million at end of the fiscal year 2004/05, i.e. a rise of KD 1129.2 million (12.6%), compared with KD 8945.7 million at end of the fiscal year 2003/04. This rise was the outcome of the increase in the balances of these facilities extended to the Real-Estate sector (by KD 629.2 million or 42.2%), the Personal Facilities sector (by KD 560.1 million or 15.5%), the Trade sector (by KD 185.2 million or 16.5%), and the Non-Bank Financial Institutions sector (by KD 27 million or 3.4%) on the one hand, and the decrease in the balances of these facilities extended to the sectors recorded under the "Others" item (by KD 197.9 million or 28.6%), the Construction sector (by KD 28.1 million or 4.4%), the Crude Oil and Gas sector (by KD 28.1 million or 34.5%) and the Agriculture and Fishing sector (by KD 17.7 million or 42.9%) on the other. As for the distribution of new KD credit facility agreements with residents during the fiscal year 2004/05, which reflect the changes in limits of existing credit facilities and the credit facilities extended to new clients, data indicate that the value of these facilities declined by KD 469.5 million or 9.6% to KD 4419.5 million during the fiscal year 2004/05, against KD 4888.9 million during the previous fiscal year.

E- Issuing of Public Debt Instruments:

The CBK manages the issuance of public debt instruments (Kuwaiti Treasury Bills and Bonds) on behalf of the Ministry of Finance since November 1987. During the fiscal year 2004/05, the CBK offered twenty-eight issues of Treasury Bills with a total nominal value of KD 2345.2 million (of which eleven issues of three-month maturity with a total nominal value of KD 621.2 million, and seventeen issues of six-month maturity with a total nominal value of KD 1724 million). During that fiscal year, thirty-one previous issues of these bills with a total nominal value of KD 2615.2 million reached maturity. As a result of these developments, the outstanding balance of Treasury Bills at end of the fiscal year 2004/05 declined by KD 270 million or 22.7% to KD 921 million, against KD 1191 million at end of the previous fiscal year.

Additionally, the CBK offered during the fiscal year 2004/05, fourteen issues of one-year term Treasury Bonds with a total nominal value of KD 1509 million. During the mentioned fiscal year, thirteen previous Treasury Bond issues with a total nominal value of KD 1270 million matured. Accordingly, the outstanding balance of Treasury Bonds rose at end of the fiscal year 2004/05 by KD 239 million or 18.8% to KD 1509 million, against KD 1270 million at end of the previous fiscal year

As a result of the above developments, the outstanding balance of public debt instruments (Kuwaiti Treasury Bills and Bonds) declined by KD 31 million or 1.3% to KD 2430 million at end of the fiscal year 2004/05, from KD 2461 million at end of the previous fiscal year. As for the distribution of the outstanding balances of public debt instruments among the various institutions holding them, local banks continued to account for the largest portion (92.8%) of the total balance of public debt instruments at end of the fiscal year 2004/05.

The fiscal year 2004/05 also witnessed the continued retirement of the Debt Purchase Bonds, which are bonds issued against the debts purchased according to Law No. (14) of 1993 and the amendments thereof. At the end of the fiscal year 2004/05, the outstanding balance of these bonds reached KD 535.8 million, i.e. a decline of KD 245.2 million or 31.4% compared to KD 781 million at end of the previous fiscal year.

2 - Banking Developments:

The aggregate balance sheet of local banks reached KD 18713.8 million at end of the fiscal year 2004/05, against KD 19594 million at end of the fiscal year 2003/04, i.e. a decline of KD 880.2 million or 4.5%. This decline essentially reflects the decrease in the value of transactions in the interbank deposits market, attributed essentially to the decline in the value of interbank certificates of deposit, and the resulting noticeable decline in the balances of these deposits on both the assets and liabilities sides of the aggregate balance sheet of local banks at end of the fiscal year 2004/05, compared to the previous fiscal year. On the other hand, the balances of most remaining items on both the assets and liabilities sides of the aggregate balance sheet of local banks continued their growth during the fiscal year 2004/05. This can be highlighted as follows:

On the Assets Side:

- The rise in the balance of local bank claims on the private sector by KD 1206.8 million (12.2%) to KD 11108.8 million at end of the fiscal year 2004/05, against KD 9902 million at end of the fiscal year 2003/04. This rise resulted from the increase in the balances of both the utilized portion of cash credit facilities extended by local banks to the resident economic sectors by KD 1129.2 million (12.6%) to KD 10075 million at end of the fiscal year 2004/05, from KD 8945.7 million at end of the previous fiscal year, and the balances of other domestic investments by KD 77.6 million (8.1%) to KD 1033.9 million at end of the fiscal year 2004/05, against KD 956.3 million at end of the previous fiscal year.
- The rise in the balance of total foreign assets of local banks by KD 444.5 million (17.1%) to KD 3042.9 million at end of the fiscal year 2004/05, against KD 2598.4 million at end of the previous fiscal year. This rise was the outcome of the increase in the balances of local banks' deposits with foreign banks by KD 418.7 million (32.4%) and the foreign investments of local banks by KD 157.5 million (24%) on the one hand, and the decrease in the balances of credit facilities extended to non-residents by KD 132.3 million (22.3%) and other foreign assets by KD 0.6 million (1%) on the other.

- The decline in the balance of local banks' claims on the government by KD 287.9 million (9.4%) to KD 2786.7 million at end of the fiscal year 2004/05, against KD 3074.6 million at end of the previous fiscal year. The largest portion (81.6%) of this decline reflects the decrease of the balance of Debt Purchase Bonds by KD 246.3 million or 31.6% to KD 532 million at end of the fiscal year 2004/05, against KD 778.3 million at end of the previous fiscal year. Also, the balance of local banks' holdings of public debt instruments (Treasury Bills and Bonds) declined by KD 41.6 million (1.8%) to KD 2254.7 million at end of the fiscal year 2004/05, against KD 2296.3 million at end of the previous fiscal year.

On the Liabilities Side:

- The rise in the balances of the resident private sector's deposits with local banks by KD 1187.8 million (11.1%) to KD 11856 million at end of the fiscal year 2004/05, against KD 10668.2 million at end of the previous fiscal year. The mentioned increase resulted from the rise in balances of KD deposits by KD 1013.5 million (10.6%) to KD 10581.8 million at end of the fiscal year 2004/05, against KD 9568.3 million at end of the previous fiscal year, and the rise in foreign currency deposits by KD 174.3 million (15.8%) to KD 1274.2 million at end of the fiscal year 2004/05, against KD 1099.9 million at end of the previous fiscal year.
- The rise in the balances of shareholders' equity in local banks by KD 302.6 million (14.6%) to KD 2381.8 million at end of the fiscal year 2004/05, against KD 2079.2 million at end of the previous fiscal year.
- The decline in the balances of government deposits with local banks (which include the deposits of the Credit and Savings Bank), by KD 68.2 million (10.3%) to KD 594.6 million at end of the fiscal year 2004/05, against KD 662.8 million at end of the previous fiscal year
- The decrease in the balances of foreign claims on local banks by KD 316.6 million (16.1%) to KD 1651.8 million at end of the fiscal year 2004/05, against KD 1968.4 million at end of the previous fiscal year. This decrease was the

outcome of the decline in the balances of both foreign banks' deposits with local banks by KD 271.5 million (19%) and other foreign liabilities by KD 114.5 million (56.2%) on the one hand, and the rise in other foreign deposits by KD 69.5 million (20.7%) and on the other.

Second: Main Supervisory Measures and Instructions Issued by the CBK

CBK continued during the fiscal year 2004/05 its supervisory and oversight efforts aimed at further strengthening the positions of the banking and financial system units, and the firm establishment of sound professional practices in these units, so as to enhance their efficiency, along with keeping abreast of international standards for banking and financial activities. In this regard, during the fiscal year 2004/05, CBK issued several circulars, instructions and regulations to the banking and financial units subject to its supervision, most significant among which are the following:

- The circulars issued on 6/4/2004 to local banks, obliging them to provide CBK with the data concerning their shareholders (natural and juristic persons) whose direct or indirect equity in the bank exceeds 5% of its capital, and the circular issued on 19/4/2004 to investment companies obliging them to provide local banks with all information on investors holding shares in these banks, within the portfolios managed by the investment company.
- The circular issued on 3/5/2004 to local banks and investment companies concerning the principles of good governance in financial institutions.
- Two circulars issued on 3/5/2004 and 6/5/2004 to local banks and investment companies, setting the timeframe for their submission of periodic data, and obliging them to abide by that timeframe, so as to improve the flow of periodic data required for the fulfillment of CBK's objectives.
- The circulars issued on 6/5/2004, 8/6/2004, 14/7/2004 and 6/1/2005 to local banks and investment companies, introducing amendments to the rules and regulations for the extension of consumer loans and other installment loans, with a view to rationalizing the extension of these loans.

- The circular issued on 19/5/2004 to exchange companies concerning the necessity of liquidating the debit balances of partners' current accounts appearing in the accounts concerning partners' equity, whereby the balances under the partner's equity accounts shall be limited to the credit balances deposited in support of the company's activities,
- The circular issued on 8/6/2004 to local banks concerning amending the instructions regarding the Liquidity System according to the Maturity Ladder Approach.
- The circular issued on 10/8/2004 to local banks concerning the use of credit cards and the period for the repayment of debit balances resulting from the use of these cards.
- The circular issued on 10/1/2005 to local banks and investment companies, concerning compliance with the third International Accounting Standard (IAS 3), regarding the accounting treatment of goodwill resulting from acquisition.
- The circular issued on 11/1/2005 to local banks, concerning the set of guidelines taken into consideration by CBK in reviewing banks' applications for the exemption of any customer from the maximum credit concentration limit.
- The circular issued on 14/2/2005 to local banks and investment companies, concerning the regulations organizing the management of third parties portfolios, and prohibiting managers from using third parties' funds, within their management of clients' portfolios, to grant any forms of credit facilities to other parties. The circular also provided that, in case such situation exists, the outstanding balances of granted credit facilities shall be liquidated on maturity.

Third: Major Operations Performed by the CBK

CBK pursued its various banking activities during the fiscal year 2004/05 in the areas connected to currency issuance, clearing operations, and payment transfers between local banks. On the one hand, the value of currency issued by CBK rose during the fiscal year 2004/05, as the average value of issued currency and coins reached KD 582.9 million during that fiscal year, compared with an average of KD 543.1 million during the previous fiscal year. The balance of issued currency during the fiscal year

2004/05 reached its highest (KD 627.8 million) at end of February 2005 and its lowest (KD 537.6 million) at end of August 2004.

The total value of operations carried out through the CBK Clearing Room during the fiscal year 2004/05 rose to KD 7617.6 million for 1848 thousand transactions (cheques), or an average of KD 4122.3 per transaction, compared with KD 7297.8 million for 1723 thousand transactions (cheques), or an average of KD 4236.3 per transaction during the fiscal year 2003/04.

Also, during the fiscal year 2004/05, CBK continued its efforts for developing and updating the payments settlement between the banking and financial system units in the State of Kuwait. The fiscal year 2004/05 witnessed the start of actual operation of the Kuwait Automated Settlement System for Inter-Bank Payments (KASSIP). This new system, which replaced the special clearing system, consists of a group of operations and procedures which enable participants operating in the State of Kuwait to forward and receive payments through spot settlements, by applying the Real-Time Gross Settlement System (RTGS). The system contributes to facilitating commercial transactions, upgrading banking services, and enhancing the efficiency and smoothness of financial flows, so that they take place in a safer and more secure form, according to the highest worldwide standards. Settlement operations carried out between banks through the CBK during the fiscal year 2004/05 amounted to KD 70.1 billion, with a monthly average of KD 5838.7 million, against KD 61 billion and a monthly average of KD 5086.6 million during the previous fiscal year, i.e. an increase of KD 752.1 million or 14.8% in the monthly average.

During the fiscal year 2004/05, CBK processed on behalf of ministries and governmental institutions, 8268 banking drafts amounting to KD 629.1 million, against 8221 banking drafts valued at KD 593.9 million during the previous fiscal year 2003/04.

The foreign banking transactions processed by CBK, to the benefit of ministries and governmental institutions, in the form of documentary credits as well as bills and drafts for collection during the fiscal year 2004/05, are shown in the following table:

Particulars	No.	Value (in KD)
First- Documentary Credits:		
1- <u>Opened:</u>		
-Local	1	3,877,560/319
-Foreign	78	21,463,827/400
2- <u>Paid:</u>		
-Local	3	9,939,321/542
-Foreign	204	47,477,164/204
3- <u>Amended:</u>		
-Local	-	
-Foreign	51	
Second- Collection Transactions:		
Bills for Collection		
a- Incoming	32	189,570/563
b- Paid-up	22	50,904/514
Third- Drafts for Collection:		
a- Collected	151	1,044,877/553
b- Purchased	-	-

Fourth: Labor force at CBK

The CBK continued during the fiscal year 2004/05 its efforts toward enhancing the efficiency of its banking cadres, and raising their professional capabilities. The CBK took in this regard several measures and decisions during the mentioned fiscal year, most important among which were the following:

1. During the fiscal year 2004/05, 37 Kuwaiti graduates (of which 16 holding university degrees and 21 holding the diploma of applied sciences) were accepted as trainees for positions at the CBK. Furthermore, during the same fiscal year, 59 individuals (of which 58 Kuwaitis) were hired. Also, 16 Kuwaiti trainees who completed their training programs during the fiscal year 2004/05 were confirmed in their jobs at the CBK. By the end of the fiscal year 2004/05, the total number of CBK staff reached 785 employees, of which 623 were Kuwaitis.
2. During the fiscal year 2004/05, the CBK organized 127 specialized training courses in the State of Kuwait in cooperation with domestic training institutions, and sent 506 of its employees to these courses. Furthermore, CBK

sent 79 of its employees to 66 training courses abroad, in coordination with a number of specialized training bodies.

3. During the fiscal year 2004/05, CBK sent 145 of its employees abroad to attend 80 conferences and meetings held at the Gulf, Arab and international levels.
4. During the fiscal year 2004/05, CBK enrolled several of its employees for the High Diploma in Banking Studies at the Institute of Banking Studies in the State of Kuwait. Furthermore, CBK sent a number of staff members from its various departments on scholarships abroad, to obtain masters and doctorate degrees.

Finally, during the fiscal year 2004/05, CBK sustained its efforts in making available information and data on the economic, monetary and banking developments in the State of Kuwait, whereby CBK continued preparing and publishing its various periodicals (monthly, quarterly) as well as its economic and annual reports in both Arabic and English, in addition to updating its internet homepage.

31/7/2005

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Fifth :

**The Central Bank of Kuwait Balance Sheet
and Profit & Loss Account for the Fiscal Year
Ended 31 March 2005**

AUDITORS REPORT

We have examined the financial statements of the Central Bank of Kuwait (CBK). Our examination included such tests of the accounting records and such other auditing procedures as we considered necessary. We obtained all the information and explanations which we deemed necessary for the purpose of our examination.

In our opinion, the financial statements give a true and fair view of the real financial position of the CBK on 31 March 2005 and of the results of its operations for the year then ended, in compliance with Law No. 32 of 1968 and amendments thereof.

Furthermore, in our opinion, proper books of account have been kept and the financial statements are in accordance therewith, and an inventory was duly carried out.

Bader Abdullah Al-Wazan

Register of Accountants & Auditors
License No. 62 A -
Bader & Partners
of PRICE WATERHOUSE COOPERS

Waleed Abdul-Wahab Al-Oseimi

Register of Accountants & Auditors
License No. 68 A -
Al-Aiban, Al-Osaimi & Partners
of ERNST & YOUNG

1 May 2005
State of Kuwait

CENTRAL BANK OF KUWAIT

Balance Sheet As On

Assets	Note	31 March 2005	31 March 2004
Gold		31,736,332	31,736,332
Cash, Current and Call Accounts in Foreign Currency with Banks and other Financial Institutions		214,616,795	138,316,615
Deposits and Investments in Foreign Currency	3	1,962,831,700	1,764,299,800
Other Assets	4	13,179,118	10,796,938
		2,222,363,945	1,945,149,685
Accounts Managed by the CBK on Behalf of the Government of the State of Kuwait and Contra Accounts	10	3,306,463,837	3,644,924,611

31 MARCH 2005 (KD)

Equity and Liabilities	Note	31 March 2005	31 March 2004
Capital - Fully Paid Up		5,000,000	5,000,000
General Reserve Fund	5	199,210,110	192,177,640
Special Account	6	264,515,536	250,223,818
Profit For the Year		28,174,945	14,064,941
Currency Issued	7	626,111,682	594,884,176
Government Accounts		700,725,710	354,399,106
Local Banks' Current Accounts and Deposits with the CBK	8	311,465,169	472,661,749
International Institutions		37,841,005	21,446,419
Deposits on Documentary Credits	10	20,810,081	25,783,034
Other Liabilities	9	28,509,707	14,508,802
		2,222,363,945	1,945,149,685
Accounts Managed by the CBK on Behalf of the Government of the State of Kuwait and Contra Accounts	10	3,306,463,837	3,644,924,611

The attached notes from 1 to 13 constitute part of these financial statements.

CENTRAL BANK OF KUWAIT

**PROFIT & LOSS ACCOUNT FOR
THE FISCAL YEAR ENDED 31 MARCH 2005
(KD)**

	<u>Note</u>	<u>2004/05</u>	<u>2003/04</u>
Interest & Income from Investments		50,728,862	41,249,867
Interest and Commission Expenses		<u>(4,705,131)</u>	<u>(13,970,178)</u>
Other Income		46,023,731	27,279,689
Operating Income		230,871	3,007,813
Operating Expenses	11	46,254,602	30,287,502
		<u>(18,079,657)</u>	<u>(16,222,561)</u>
Net Profit		<u>28,174,945</u>	<u>14,064,941</u>
Disposed of according to Article 17, of Law No. 32 of 1968 and its amendments, as follows:			
to the Government Account	5	14,087,473	7,032,471
to the CBK General Reserve Fund	5	14,087,472	7,032,470
		<u>28,174,945</u>	<u>14,064,941</u>

The attached notes from 1 to 13 constitute part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

1- Activities:

The Central Bank of Kuwait (CBK), is incorporated in Kuwait by Law No. 32 of 1968 and amendments thereof. The CBK is a public institution with an independent juristic personality, and is entrusted with issuing the local currency on behalf of the State of Kuwait, ensuring the stability of the Kuwaiti currency and its free convertibility into other currencies, directing the monetary and credit policies, and the supervision of the banking and financial system, in addition to serving as banker and financial advisor to the Government.

2- Significant Accounting Policies:

These financial data were prepared in accordance with Law No. 32 of 1968 and amendments thereof. The applied significant accounting policies are as follows:

(a) Gold:

In accordance with the Amiri Decree of 4 July 1978, gold is valued at KD 12.500 per fine ounce.

(b) Revenue Recognition:

Interest receivable and payable are recognized on a time proportion basis, taking into account the principal outstanding and the rate applicable.

(c) Capital Expenditure:

Capital expenditure is charged to expenses in the year of authorization.

(d) Foreign Currencies:

In accordance with Article 48 of Law No. 32 of 1968 and amendments thereof, and the Amiri Decree of 4 July 1978, all assets and liabilities in foreign currencies are revalued at the exchange rates prevalent on the date of the preparation of the balance sheet, and the resulting gains or losses taken to the special account.

3- Deposits and Investments in Foreign Currencies (KD):

	<u>2004/05</u>	<u>2003/04</u>
Deposits with Foreign Banks and Institutions	1,958,452,450	1,759,880,050
Central Banks facilities to the International Bank for Reconstruction and Development	4,379,250	4,419,750
	<u>1,962,831,700</u>	<u>1,764,299,800</u>

4- Other Assets (KD):

	<u>2004/05</u>	<u>2003/04</u>
Interest Receivable on Deposits	8,218,800	5,023,867
CBK's Share in the Capital of the Industrial Bank of Kuwait	2,511,210	2,511,210
Prepaid Expenses	126,847	201,630
Advance Payments	222,665	346,578
Other Debit Balances	2,099,596	2,713,653
	<u>13,179,118</u>	<u>10,796,938</u>

5- General Reserve Fund:

In accordance with Article 17, paragraphs 3 (a) and (b), of Law No. 32 of 1968 and amendments thereof, the net profits of the CBK shall be paid into the General Reserve Fund until the balance of the fund amounts to twenty-five million Kuwaiti Dinars, unless the Board of Directors recommends and the Minister of Finance approves further increases in the Fund. In 1985, the Board recommendation to increase the fund to KD 179 million was approved by the Minister of Finance and Economy. In accordance with the Board decision dated on 5 May 2003, and the approval of the Minister of Finance on 7 May 2003, it was agreed to increase the balance of CBK General Reserve Fund by KD 116 million to KD 295 million, by transferring half of CBK net annual profits to the Fund balance, whereby half of the annual profits are transferred to the Fund, following the approval of the CBK financial data by the Minister of Finance.

6- Special Account (KD):

	<u>2004/05</u>	<u>2003/04</u>
Balance at Beginning of the Year	250,223,818	161,280,126
Net difference in foreign currency , resulting from revaluation of cash assets and liabilities in foreign currencies	11,395,659	88,943,692
Profit resulting from withdrawal of currency notes from circulation (fourth issue)	2,896,059	-
Balance at End of the Year	<u>264,515,536</u>	<u>250,223,818</u>

The special account represents the net profits accumulated as a result of revaluation of cash assets and liabilities in foreign currencies, and profit resulting from the withdrawal of currency notes from circulation, based on Article 48 of Law No. 32 of 1968 and amendments thereof, and the Amiri Decree of 4 July 1978.

7- Currency Issued (KD):

	<u>2004/05</u>	<u>2003/04</u>
Net Currency Produced	1,087,161,435	972,173,243
Less: Currency in the CBK's Vaults	(461,049,753)	(377,289,067)
	<u>626,111,682</u>	<u>594,884,176</u>

Net currency produced represents the total of currency printed, reduced by currency destroyed.

8- Local Banks Current Accounts and Deposits with the CBK (KD):

	<u>2004/05</u>	<u>2003/04</u>
Current Accounts	186,465,169	171,161,749
Deposits	125,000,000	301,500,000
	<u>311,465,169</u>	<u>472,661,749</u>

9- Other Liabilities (KD):

	<u>2004/05</u>	<u>2003/04</u>
Accrued Expenses	2,695,010	2,282,812
Other Credit Balances	25,814,697	12,225,990
	<u>28,509,707</u>	<u>14,508,802</u>

Other credit balances include provisions for employees' leave pay and termination benefits and credit accounts of non-banking institutions.

10- Accounts Managed by the CBK on Behalf of the Government of the State of Kuwait and Contra Accounts (KD):

	<u>2004/05</u>	<u>2003/04</u>
a- Accounts Managed by the CBK on Behalf of the Government of Kuwait	3,239,299,318	3,532,753,655
b- Contra Accounts:		
Documentary Credits	44,006,763	83,414,967
Memorial Notes and Coins	1,586,704	1,624,739
Forward Transactions on Behalf of the Kuwait Investment Authority	-	5,933,297
Collections According to the Law No. 41 of 1993	21,571,052	21,197,953
	<u>67,164,519</u>	<u>112,170,956</u>
	<u>3,306,463,837</u>	<u>3,644,924,611</u>

On 31 March 2005, deposits of KD 20,810,081 (KD 25,783,034: 2004) were held against the documentary credits referred to above.

11- Operating Expenses (KD):

	<u>2004/05</u>	<u>2003/04</u>
Employee Costs	11,404,078	11,205,891
Administrative and Computer Costs	1,344,599	1,408,587
Purchases of Furniture, Equipment and Vehicle	962,692	88,360
Production and Shipment of Currency	1,083,814	1,483,264
Sundry Expenses	1,173,880	1,104,499
Construction Costs	2,110,594	931,960
	<u>18,079,657</u>	<u>16,222,561</u>

12- Compensation Claims:

The Board of Directors of the United Nations Compensation Committee issued its decision No. (153) on 13 March 2002, approving the compensation of the CBK for damages sustained as a result of the Iraqi occupation, for an amount of US \$ 117,797,000 equivalent to KD 36,266,162, from a total claim presented by the CBK on 7 February 1994 for an amount of US \$ 245.756.758 equivalent to KD 73,132,296 as on the date of presenting the claim.

During the fiscal year 2004/05, CBK received no partial payments of the approved compensation (noting that in the fiscal year ended on 31 March 2004, an amount of KD 2,912,522 was received after deduction of the Ministry of Finance 3% share in the compensation).

The CBK records compensation amounts as revenues, effective as on their date of receipt

13- Promissory Notes Held:

On 31 March 2005, promissory notes held by the CBK in safe custody on behalf of international institutions totaled KD 386,535,254 (KD 353,578,592: 2004).

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