



بنك الكويت المركزي
CENTRAL BANK OF KUWAIT



**THE THIRTY-SECOND
ANNUAL REPORT**

FOR THE FISCAL YEAR 2003/04

The Annual Report of the Central Bank of Kuwait for the Fiscal Year 2003/04

INTRODUCTION

The Central Bank of Kuwait (CBK) pursued in the fiscal year 2003/04 its efforts in drawing and implementing the monetary policy, as well as enhancing the programs for the supervision and oversight of the banking and financial system units subject to its supervision; thus, contributing to firming the bases of monetary stability in the State of Kuwait and establishing an atmosphere that allows the banking and financial system units to keep abreast with domestic, regional and world developments, and to adjust to their reflections on the country's monetary and banking conditions.

Noticeable in this regard are the constant efforts aimed at developing the legal structure connected to CBK's areas of activity and the organization of banking business. In the forefront of these efforts are the amendments introduced to some provisions of Law No. (32) of year 1968 concerning currency, the Central Bank of Kuwait and the Organization of Banking Business, by the Law No. (30) of year 2003, issued on the 25th of May 2003, which adds a special section on Islamic banks to the third chapter of the mentioned Law No. (32) of year 1968, for the purpose of organizing Islamic Banks' activities on sound bases that take into account the special nature of Islamic banking. Furthermore, Law No. (28) of year 2004 was issued on the 27th of January 2004, to amend certain provisions of the mentioned Law No. (32) of year 1968. Particularly notable among these amendments are those relevant to permitting foreign banks to open branches in the State of Kuwait, which is consistent with nowadays era of free trade in financial services and the State of Kuwait's membership in the World Trade Organization (WTO), and allows national banks of the GCC member countries to open branches in the State of Kuwait.

During the fiscal year 2003/04, CBK played a prominent role in numerous areas which reflect its constant efforts in following up on the latest economic, monetary and banking developments on both the domestic and world levels, as well as its endeavors to enhance the competitive capabilities of the local banking and financial system. This CBK annual report presents an outline of the most significant domestic monetary and banking developments during the fiscal year 2003/04, in addition to the most important decisions issued by CBK, the systems it set up, and measures and operations it performed in all monetary and banking areas during that period,

including the most significant instructions and circulars it issued to the banking and financial system units subject to its supervision, and finally the Auditors Report, and both CBK's balance sheet and profit and loss account for the mentioned fiscal year, as follows:

First: The Main Monetary and Banking Developments

1- Monetary Developments:

CBK continued during the fiscal year 2003/04 its efforts in drawing and implementing the monetary policy aimed at firmly establishing the bases of monetary stability in the State of Kuwait. These CBK's efforts constitute a key aspect of the directions of the State's general economic policy, which is aimed at creating an atmosphere supporting the country's economic development efforts. The following are the most significant banking and monetary developments during the fiscal year 2003/04:

A- Money Supply:

During the fiscal year 2003/04, Money Supply in its broad definition (M2) recorded a marked growth of KD 1420.5 million or 14.6% to KD 11183.2 million at end of the mentioned fiscal year, against KD 9762.7 million at end of the fiscal year 2002/03. This increase resulted from the rise in both Money (the narrow definition of money supply M1) by KD 807.3 million or 34.6% (from KD 2331.3 million to KD 3138.6 million), and Quasi money by KD 613.2 million or 8.3% (from KD 7431.4 million to KD 8044.6 million).

Regarding factors affecting changes in money supply within the aggregate monetary position of CBK and local banks^(*) during the fiscal year 2003/04, the above rise in Money Supply (M2) was the outcome of the increase in net domestic assets of these institutions by KD 1470.8 million (20.5%) on the one hand, and the decline in their net foreign assets by KD 50.3 million (1.9%) on the other. The mentioned increase in net domestic assets reflects the outcome of the rise in local banks' claims on the private sector by KD 1834 million or 22.5%, and other net claims of CBK and local banks by KD 297 million or 8.7% on the one hand, and the decline in both the local banks' claims on the government by KD 100.8 million or 3.2%, and the government accounts with CBK and deposits with local banks by KD 34.6 million or 4.7%, on the other. As for the mentioned decrease in net foreign assets, it was essentially the outcome of the decline in CBK's net foreign assets by KD 278.7 million or 12.7% on the one hand, and the rise in net foreign assets of local banks by KD 228.4 million or 56.9% on the other.

^(*) Local banks in this report encompass commercial and specialized banks, in addition to Kuwait Finance House, unless otherwise specified.

B- The Domestic Interest Rates:

In light of CBK's continual monitoring of developments in the domestic interest rates on the Kuwaiti dinar, so as to ensure their consistency with the domestic economic and monetary developments on the one hand and their alignment with the trends in interest rates on major currencies on the other, CBK maintained during the fiscal year 2003/04 the discount rate at its level of 3.25% recorded at end of the previous fiscal year.

Available data on the averages of interest rates on customers KD and US dollar deposits with local banks during the fiscal year 2003/04, indicate a decline in the averages of interest rates on these deposits. The interest rates on customers' US dollar time deposits during the mentioned fiscal year recorded a decline surpassing the decline in interest rates on the Kuwaiti dinar deposits. This led to a broadening of the margins existing in favour of KD deposits, as the margin existing in favor of KD deposits between the averages of interest rates on KD and US dollar deposits at local banks for the one-month and 3-month terms during the fiscal year 2003/04 reached 0.81 and 0.83 percentage point respectively, against 0.72 and 0.74 percentage point for these two terms respectively, during the previous fiscal year.

Furthermore, the averages of interest rates on the KD interbank deposits of local banks (not including Kuwait Finance House) witnessed a decline during the fiscal year 2003/04, as these averages decreased by 0.45 percentage point (from 2.75% to 2.30%) for the one-month term, and by 0.37 percentage point (from 2.76% to 2.39%) for the three-month term.

As for the average interest rates on Public Debt Instruments, a decline was recorded during the fiscal year 2003/04 in the average of interest rates on the three-month Treasury Bills by 0.39 percentage point (from 2.64% to 2.24%) and six-month Treasury Bills by 0.26 percentage point (from 2.65% to 2.39%). Also, the average of interest rates on the one-year Treasury Bonds declined by 0.44 percentage point (from 3.19% to 2.75%) during the mentioned fiscal year, compared to the fiscal year 2002/03.

C- The KD Exchange Rate:

CBK started on 5 January 2003 the application of a new KD exchange rate policy, by virtue of the Decree No. 266 of 2002, issued on 5 October 2002. According to this policy, the exchange rate of the Kuwaiti dinar has been pegged to the US dollar within a margin not exceeding 3.5% on both sides of the parity exchange rate of the Kuwaiti dinar against the US dollar, set by CBK at 299.63 fils/dollar. The application of this new policy was in response to the decision

taken by the leaders of the GCC member countries during the meetings of the 22nd Session of the GCC Supreme Council on 31 December 2001 in Muscat, Sultanate of Oman, with regard to completing the common pegging of the member States' currencies against the US dollar, as a step toward fulfilling the requirements for the establishment of the GCC monetary union and the launching of the GCC single currency in year 2010.

Available data on the developments of the KD exchange rate during the fiscal year 2003/04 indicate that it maintained its manifest relative stability against the other major currencies, under the new 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 of the Kuwaiti dinar against the US dollar, set at 299.63 fils/dollar. During the mentioned fiscal year, the difference between the highest and lowest exchange rates of the US dollar against the Kuwaiti dinar did not exceed 6.77 fils (300.64 fils and 293.87 fils) or 2.3%. Furthermore, the difference between the highest exchange rate of the US dollar against the KD, and the parity rate (299.63 fils/dollar), reached one fils (0.3%) during the mentioned fiscal year. Meanwhile, the difference between the lowest exchange rate of the US dollar against the KD, and the parity rate, reached 5.76 fils (1.9%). The exchange rate of the US dollar against other major currencies witnessed more pronounced fluctuations during that period, whereby the difference between the highest and lowest exchange rates of the US dollar reached 22.7% against the Sterling pound, 20.8% against the Euro, 16.5% against the Swiss franc, and 14.6% against the Japanese yen.

D- Bank Credit:

The balances of the utilized portion of cash credit facilities extended by local banks to the different economic sectors recorded a noticeable rise of KD 1719 million (23.6%) during the fiscal year 2003/04, from KD 7298.6 million at end of the fiscal year 2002/03 to KD 9017.6 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 most economic sectors, ahead of which the "Personal Facilities" sector (by KD 863 million or 31.3%), the sectors under the "Others" item (by KD 219.5 million or 46.3%), the Non-Bank Financial Institutions sector (by KD 214.4 million or 32.5%) and the Real Estate sector (by KD 151.9 million or 11.4%) on the one hand, and the decrease in the balances of these facilities extended to the Industry sector (by KD 39.3 million or 6.8%) on the other. As for the distribution of new KD credit facility agreements with residents during the fiscal year 2003/04, 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 rose by KD 185.9 million or 4% to KD 4888.9 million during the fiscal year 2003/04, against KD 4703.1 million during the previous fiscal year.

E- Issuance of Public Debt Instruments:

Since November 1987, CBK issues public debt instruments (Kuwaiti Treasury Bills and Bonds) on behalf of the Ministry of Finance. CBK pursued during the fiscal year 2003/04 its efforts in issuing public debt instruments, as it made thirty-four issues of Treasury Bills with a total nominal value of KD 3082.5 million (of which sixteen issues of three-month maturity and a total nominal value of KD 1188.5 million, and eighteen issues of six-month maturity and a total nominal value of KD 1894 million). During that fiscal year, thirty-six previous issues of these bills with a total nominal value of KD 3401.5 million reached maturity. As a result of these developments, the outstanding balance of Treasury Bills at end of the fiscal year 2003/04 declined by KD 319 million or 21.1% to KD 1191 million, against KD 1510 million at end of the previous fiscal year.

Regarding Treasury Bonds, CBK made during the fiscal year 2003/04, fourteen issues of one-year term Treasury Bonds with a total nominal value of KD 1415 million. During the mentioned fiscal year, eleven previous Treasury Bond issues with a total nominal value of KD 1055 million matured. Accordingly, the outstanding balance of Treasury Bonds rose at end of the fiscal year 2003/04 by KD 360 million or 39.6% to KD 1270 million, against KD 910 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) rose by KD 41 million or 1.7% to KD 2461 million at end of the fiscal year 2003/04, from KD 2420 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, relevant data indicate that local banks continued to account for the largest portion (93.3%) of the total balance of public debt instruments at end of the fiscal year 2003/04.

2 - Banking Developments:

The aggregate balance sheet of local banks rose by KD 2536.9 million or 14.9% to KD 19598.3 million at end of the fiscal year 2003/04, against KD 17061.4 million at end of the fiscal year 2002/03. This rise is essentially imputable to several developments in the items of that balance sheet, most significant among which are the following:

On the Assets Side:

- The rise in the balance of local banks' claims on the private sector by KD 1834 million (22.5%) to KD 9973.9 million at end of the fiscal year 2003/04, against KD 8139.9 million at end of the fiscal year 2002/03. This rise resulted from the increase in the balances of both the utilized portion of cash credit facilities extended by local banks to the domestic economic sectors by KD 1719 million (23.6%) to KD 9017.6 million at end of the fiscal year 2003/04, from KD 7298.6 million at end of the previous fiscal year, and other domestic investments by KD 115 million (13.7%) to KD 956.3 million at end of the fiscal year 2003/04, against KD 841.3 million at end of the previous fiscal year.
- The rise in the balance of total foreign assets of local banks by KD 233.2 million (9.8%) to KD 2601.6 million at end of the fiscal year 2003/04, against KD 2368.4 million at end of the previous fiscal year. This rise resulted from the increase in the balances of credit facilities extended to non-residents by KD 140 million (15.3%), foreign investments by KD 59.7 million (10%), other foreign assets by KD 17.7 million (45.8%), and local banks' deposits with foreign banks by KD 15.8 million (1.9%).
- The decline in the balance of local banks' claims on the government by KD 100.8 million (3.2%) to KD 3074.6 million at end of the fiscal year 2003/04, against KD 3175.4 million at end of the previous fiscal year, as the balance of Debt Purchase Bonds decreased by KD 197.2 million or 20.2% to KD 778.3 million at end of the fiscal year 2003/04, against KD 975.5 million at end of the previous fiscal year. In return, the balance of local banks' holdings of Public Debt Instruments (Treasury Bills and Bonds) rose by KD 96.4 million (4.4%) to KD 2296.3 million at end of the fiscal year 2003/04, against KD 2199.9 million at end of the previous fiscal year.

On the Liabilities Side:

- The rise in the balances of resident private sector's deposits with local banks by KD 1421.5 million (15.4%) to KD 10668.2 million at end of the fiscal year 2003/04, against KD 9246.7 million at end of the previous fiscal year. The mentioned increase resulted from the rise in balances of KD deposits by KD 1115.1 million (13.2%) to KD 9568.3 million at end of the fiscal year 2003/04, against KD 8453.2 million at end of the previous fiscal year, and foreign currency deposits with these banks by KD 306.4 million (38.6%) to KD 1099.9 million at end of the fiscal year 2003/04, against KD 793.5 million at end of the previous fiscal year.

- The rise in the balances of shareholders' equity in local banks by KD 243.1 million (13.2%) to KD 2079.2 million at end of the fiscal year 2003/04, against KD 1836.2 million at end of the previous fiscal year.
- The rise in the balances of foreign claims on local banks by KD 4.8 million (0.2%) to KD 1971.6 million at end of the fiscal year 2003/04, against KD 1966.8 million at end of the previous fiscal year. This rise was the outcome of the increase in the balances of other foreign liabilities by KD 55.7 million (36.8%) and other foreign deposits by KD 25.6 million (8.3%) on the one hand, and the decline in the balances of foreign banks' deposits with local banks by KD 76.5 million (5.1%) on the other.

Second: Significant Supervisory Measures and Instructions Issued by CBK

CBK exercises its role in the supervision and oversight of the banking and financial system units, through the off-site monitoring and on-site inspections of these units, within its efforts for enhancing the strength of the banking and financial sector in the State of Kuwait. Furthermore, CBK is keen on rationalizing the credit policies of units subject to its supervision, along with following up these units' compliance with CBK's rules, regulations and supervisory instructions. In this regard, CBK issued during the fiscal year 2003/04 several circulars, instructions and regulations to the banking and financial units subject to its supervision, most significant among which are the following:

- The circular issued to local banks on 8 May 2003, regarding local banks' dealings in foreign exchange operations, particularly CBK's coverage of US dollar transactions of local banks' customers.
- The circular issued to local banks and investment companies on 14 May 2003, regarding credit facilities extended for the execution of works and projects outside the State of Kuwait.
- The circular issued to local banks and investment companies on 3 June 2003, regarding the addition of a special section on Islamic banks to the third chapter of Law No. 32 of year 1968, concerning Currency, the Central Bank of Kuwait and the Organization of Banking Business.
- The circular issued to local banks and investment companies on 14 June 2003, regarding the banking risks system and the regulations issued for its application, which

took into account the nature of financing operations carried out by Islamic banks and investment companies operating in accordance with the provisions of the Islamic Sharia.

- The circular issued on 13 October 2003 to local banks, regarding the code of good practice for the management and supervision of operating risks in banks.
- The circular issued on 6 November 2003 to local banks, regarding the obligation for banks to abide by the measures concerning opening accounts to non-Kuwaiti workers in non-governmental bodies.
- The circular issued on 24 December 2003 to local banks, regarding verifying the identity of persons making deposits to accounts of local banks' clients.
- The circular issued on 14 January 2004 to local banks and investment companies, regarding subjecting credit facilities extended to financial institutions by local banks and investment companies, to the maximum set limits for credit concentrations.
- The circular issued on 22 February 2004 to local banks, regarding the explanatory definitions provided by local banks about plastic cards' operations.

Third: Major Operations Performed by CBK

1. The average value of currency and coins issued during the fiscal year 2003/04 reached KD 544.1 million, compared with an average of KD 485.2 million during the previous fiscal year. The value of issued currency reached its highest during the fiscal year 2003/04 in November 2003 (KD 641.8 million), and its lowest (KD 489 million) in August 2003.
2. The total value of banking sector operations carried out through CBK Clearing Room during the fiscal year 2003/04 rose above its level during the fiscal year 2002/03, as it reached KD 7297.8 million (an average of KD 4236.3 per transaction), compared with KD 5442.7 million (an average of KD 3331.6 per transaction) during the previous fiscal year. Meanwhile, settlement operations carried out between banks through CBK during the fiscal year 2003/04 amounted to KD 61 billion, with a monthly average of KD 5086.6 million, against KD 51.8 billion and a monthly average of KD 4319.1

million during the previous fiscal year, i.e an increase of KD 767.5 million or 17.8% in the monthly average.

3. During the fiscal year 2003/04, CBK processed 8221 banking drafts amounting to KD 593.9 million, against 8330 banking drafts valued at KD 483.4 million during the previous fiscal year 2002/03.
4. During the fiscal year 2003/04, CBK processed foreign banking transactions, on behalf of ministries and governmental institutions, namely documentary credits as well as bills and drafts for collection, as shown in the following table:

| Particulars | No. | Value (in KD) |
|---|-----|----------------|
| First- Documentary Credits: | | |
| 1- <u>Opened:</u> | | |
| -Local | | |
| -Foreign | 83 | 45,001,463/247 |
| 2- <u>Paid:</u> | | |
| -Local | 3 | 932,353/844 |
| -Foreign | 216 | 79,689,811/941 |
| 3- <u>Amended:</u> | | |
| -Local | 1 | |
| -Foreign | 58 | |
| Second- Collection Transactions: | | |
| Bills for Collection | | |
| a- Incoming | 24 | 174,448/648 |
| b- Paid-up | 23 | 156,902/287 |
| Third- Drafts for Collection: | | |
| a- Collected | 127 | 461,516/175 |
| b- Purchased | - | - |

Fourth: The Labour Force at CBK

CBK continued, during the fiscal year 2003/04, its efforts aimed at enhancing the efficiency of its banking cadres, and raising their scientific and professional levels. 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 2003/04, 31 Kuwaiti graduates (of which 18 holding university degrees and 13 holding the diploma of applied sciences) were accepted as trainees for positions at CBK. Furthermore, 67 employees (of which 54 Kuwaiti employees) were appointed. Also, 15 Kuwaiti trainees who completed their training programmes were confirmed in their jobs at CBK, during the fiscal year 2003/04. Consequently, the total number of CBK staff reached 772 employees, of which 601 Kuwaiti employees, during the fiscal year 2003/04.
2. During the fiscal year 2003/04, CBK organized 103 specialised training courses in the State of Kuwait in cooperation with domestic training institutions, and sent 336 of its employees to these courses. Furthermore, CBK sent 59 of its employees to 50 training courses abroad, so as to develop the performance of CBK staff and enhance their scientific and practical levels, in line with training needs and work requirements.
3. During the fiscal year 2003/04, CBK sent 110 of its employees abroad to attend 48 conferences and meetings held on various topics at the Gulf, Arab and international levels.
4. During the fiscal year 2003/04, 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 three staff members from its various departments on study missions abroad, to obtain masters and doctorate degrees.

Within CBK's efforts in the area of information technology and systems, the development and upgrading of information technology and programs applied at the Central Bank continued during the fiscal year 2003/04, so as to keep abreast with best relevant practices and world standards. In this regard, and within the preparations for developing a secure and efficient system for payments settlement between the banking and financial system units in the State of Kuwait, the fiscal year 2003/04 witnessed the continuation of CBK's efforts for establishing this system and laying down the rules and regulations for its usage, along with the initiation of operation tests. Live operation of the system, which is referred to as the 'Kuwait Automated Settlement System for Inter-Bank Payment' (KASSIP), is expected to start in the fiscal year 2004/05.

Furthermore, CBK sustained during the fiscal year 2003/04 its efforts in making available information and data on the economic, monetary and banking developments in the State of Kuwait, whereby CBK continued to prepare, publish and distribute its various periodicals (monthly, quarterly) and economic and annual reports in both Arabic and English, while constantly updating its internet homepage and developing its contents.

Fifth :

**The Central Bank of Kuwait
Balance Sheet and Profit & Loss Account
for the Fiscal Year Ended 31 March 2004**

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 CBK on 31 March 2004 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

Ahmed Mohamad Al-Aiban

Register of Accountants & Auditors

License No. 65 A -

Al-Aiban, Al-Osaimi & Partners

of ERNST & YOUNG

26 April 2004
State of Kuwait

Balance Sheet As On

| Assets | Note | 31 March 2004 | 31 March 2003 |
|---|-------------|--------------------------|--------------------------|
| Gold | | 31,736,332 | 31,733,427 |
| Cash, Current and Call Accounts in Foreign Currency with Banks and other Financial Institutions | | 138,316,615 | 309,254,045 |
| Deposits and Investments in Foreign Currency | 3 | 1,764,299,800 | 1,852,966,240 |
| Other Assets | 4 | 10,796,938 | 5,711,623 |
| | | 1,954,149,685 | 2,199,665,335 |
| Accounts Managed by CBK on Behalf of the Government of the State of Kuwait and Contra Accounts | 10 | 3,644,924,611 | 3,848,438,349 |

31 MARCH 2004 (KD)

| Capital and Liabilities | Note | 31 March 2004 | 31 March 2003 |
|--|-------------|--------------------------|--------------------------|
| Capital - Fully Paid Up | | 5,000,000 | 5,000,000 |
| General Reserve Fund | 5 | 192,177,640 | 179,000,000 |
| Special Account | 6 | 250,223,818 | 161,280,126 |
| Profit For the Year | | 14,064,941 | 26,355,280 |
| Currency Issued | 7 | 594,884,176 | 589,112,587 |
| Government Accounts | | 354,399,106 | 388,135,383 |
| Local Banks' Current Accounts and Deposits with CBK | 8 | 472,661,749 | 810,843,291 |
| International Institutions | | 21,446,419 | 2,359,875 |
| Deposits on Documentary Credits | 10 | 25,783,034 | 25,404,214 |
| Other Liabilities | 9 | 14,508,802 | 12,174,579 |
| | | 1,945,149,685 | 2,199,665,335 |
| Accounts Managed by CBK on Behalf of the Government of the State of Kuwait and Contra Accounts | 10 | 3,644,924,611 | 3,848,438,349 |

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 2004
(KD)**

| | Note | 2003/04 | 2002/03 |
|--|------|-------------------|-------------------|
| Interest & Income From Investments | | 41,249,867 | 68,113,923 |
| Interest and Commission Expenses | | (13,970,178) | (41,799,067) |
| | | 27,279,689 | 26,314,856 |
| Other Income | 12 | 3,007,813 | 13,280,931 |
| Operating Income | | 30,287,502 | 39,595,787 |
| Operating Expenses | 11 | (16,222,561) | (13,240,507) |
| Net Profit | | 14,064,941 | 26,355,280 |
| Net Profit For the Year shall be disposed of according to Article 17, of Law No, 32 of 1968 and its mendments, as follows: | | | |
| to the Government Account | 5 | 7,032,471 | 13,177,640 |
| to CBK General Reserve Fund | 5 | 7,032,470 | 13,177,640 |
| | | 14,064,941 | 26,355,280 |

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. 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>2003/04</u> | <u>2002/03</u> |
|---|-----------------------------|-----------------------------|
| Deposits with Foreign Banks and Institutions | 1,759,880,050 | 1,848,469,540 |
| Central Banks facilities to the International Bank for Reconstruction and Development | 4,419,750 | 4,496,700 |
| | <u><u>1,764,299,800</u></u> | <u><u>1,852,966,240</u></u> |

4- Other Assets (KD):

| | <u>2003/04</u> | <u>2002/03</u> |
|---|--------------------------|-------------------------|
| Interest Receivable on Deposits | 5,023,867 | 2,204,807 |
| CBK's Share in the Capital of the Industrial Bank of Kuwait | 2,511,210 | 2,511,210 |
| Prepaid Expenses | 201,630 | 105,336 |
| Advance Payments | 346,578 | 88,594 |
| Other Debit Balances | 2,713,653 | 801,676 |
| | <u>10,796,938</u> | <u>5,711,623</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 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.

6- Special Account (KD):

| | <u>2003/04</u> | <u>2002/03</u> |
|--|---------------------------|---------------------------|
| Balance at Beginning of the Year | 161,280,126 | 40,243,255 |
| Net difference in foreign currency , resulting from revaluation of cash assets and liabilities in foreign currencies | 88,943,692 | 121,036,871 |
| Balance at End of the Year | <u>250,223,818</u> | <u>161,280,126</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>2003/04</u> | <u>2002/03</u> |
|--------------------------------|---------------------------|---------------------------|
| Net Currency Produced | 972,173,243 | 957,360,435 |
| Less: Currency in CBK's Vaults | (377,289,067) | (368,247,848) |
| | <u>594,884,176</u> | <u>589,112,587</u> |

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

| 8- Local Banks Current Accounts and Deposits with CBK (KD): | | |
|--|--------------------|--------------------|
| | 2003/04 | 2002/03 |
| Current Accounts | 171,161,749 | 97,343,291 |
| Deposits | 301,500,000 | 713,500,000 |
| | 472,661,749 | 810,843,291 |

| 9- Other Liabilities (KD): | | |
|-----------------------------------|-------------------|-------------------|
| | 2003/04 | 2002/03 |
| Accrued Expenses | 2,282,812 | 2,034,441 |
| Other Credit Balances | 12,225,990 | 10,140,138 |
| | 14,508,802 | 12,174,579 |

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

| 10- Accounts Managed by CBK on Behalf of the Government of the State of Kuwait and Contra Accounts (KD): | | |
|---|----------------------|----------------------|
| | 2003/04 | 2002/03 |
| a- Accounts Managed by CBK on Behalf of the Government of Kuwait | 3,532,753,655 | 3,692,165,661 |
| b- Contra Accounts: | | |
| Documentary Credits | 83,414,967 | 123,605,918 |
| Memorial Notes and Coins | 1,624,739 | 1,655,353 |
| Forward Transactions on Behalf of the Kuwait Investment Authority | 5,933,297 | 6,032,197 |
| Collections According to the Law No. 41 of 1993 | 21,197,953 | 24,979,220 |
| | 112,170,956 | 156,272,688 |
| | 3,644,924,611 | 3,848,438,349 |

On 31 March 2004, deposits of KD 25,783,034 (against KD 25,404,214 in 2003) were held against the documentary credits referred to above.

| 11- Operating Expenses (KD): | | |
|---|-------------------|-------------------|
| | 2003/04 | 2002/03 |
| Employee Costs | 11,205,891 | 9,926,253 |
| Administrative and Computer Costs | 1,408,587 | 1,109,743 |
| Purchases of Furniture, Equipment and Vehicle | 88,360 | 102,648 |
| Production and Shipment of Currency | 1,483,264 | 1,069,958 |
| Sundry Expenses | 1,104,499 | 950,033 |
| Construction Costs | 931,960 | 81,872 |
| | 16,222,561 | 13,240,507 |

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 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 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, the received partial payments of the approved compensation, totaled KD 2,912,522 (against KD 13,183,658 in 2003) after deduction of the Ministry of Finance 3% share in the compensation.

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

13- Promissory Notes Held:

On 31 March 2004, promissory notes held by CBK in safe custody on behalf of international institutions totaled KD 353,578,592 (against KD 337,910,736 in 2003).

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