

CENTRAL BANK OF KUWAIT

**THE TWENTY SEVENTH
ANNUAL REPORT**

FOR THE FISCAL YEAR 1998/99

The Annual Report of the Central Bank of Kuwait for the Fiscal Year 1998/99

INTRODUCTION

During the fiscal year 1998/99, the efforts of the Central Bank of Kuwait (CBK) and the directions of the monetary policy continued to focus on strengthening the monetary stability in the country, so as to enhance the elements and opportunities for self-generated growth in the domestic economy. This was within the CBK efforts in drawing and implementing the monetary policy, enhancing its supervisory tools and methods, along with directing and rationalizing the credit policy of local banks* and investment companies subject to its supervision.

The CBK also pursued its monitoring of the economic and monetary developments locally and internationally, along with preparing reports and studies analyzing the reflections of these developments on the local monetary and banking conditions in particular and the economy in general. Accordingly, the CBK continued drawing and implementing appropriate policies and measures addressing these developments, for the purpose of firmly establishing the monetary stability in the national economy and strengthening its banking and financial system.

In order to provide basic monetary, banking and economic data on the State of Kuwait, in a form readily accessible to those interested in using or monitoring such information, and with the purpose of contributing to enhance transparency in the activities of the banking and financial system in particular and those of the domestic economy in general, the CBK maintained its various periodical publications - namely the Monthly Monetary Statistics, the Quarterly Statistical Bulletin and the Economic Report. Furthermore, the CBK continued to post the latest issues of these publications along with other up-to-date statistics and information on its internet homepage.

(*) The term local banks in this report covers commercial banks, specialized banks and the Kuwait Finance House.

During the fiscal year 1998/99, the CBK persevered as well in its efforts in the area of strategic enhancement of banking information technology, so as to increase the efficiency of the various systems it applies in this regard. On the other hand, within its sustained monitoring of the worldwide developments in payment and settlement systems, through which it targets the enhancement of these systems in the State of Kuwait, the CBK pursued its efforts in developing an integrated payment and settlement system characterized by speed, efficiency and security.

In its endeavours to avoid what has been labelled as the millennium problem and the unfavourable reflections thereof on computer systems in the banking and financial sector, the CBK pursued its continuous efforts, for the third consecutive year, in completing the necessary adjustments to several main systems applied both in-house and in the banking and financial units subject to its supervision, so as to make them year-2000 compatible. In this regard, the adjustment of software, hardware and applied systems was completed and simulation tests carried out to ensure their efficient operation at the turn of the millennium. Furthermore, the CBK continued in this regard to monitor the year 2000 preparedness of the units subject to its supervision, while requesting them to carry on testing and adapting their systems for handling any potential contingency at the start of year 2000.

This report provides an outline of the significant domestic monetary and banking developments during the fiscal year 1998/99, followed by a brief review of the most important measures taken and operations performed by the CBK during that period, then the Auditors Report on the CBK balance sheet statement as on 30 June 1999, and the profit and loss account of its activities for the fiscal year then ended, as follows:

First : The Main Monetary and Banking Developments

1- Monetary Developments:

Within its efforts in drawing and implementing the monetary policy and directing the credit policy of banks and domestic investment companies so as to maintain the monetary stability in the country, the CBK carries out a continual follow-up of the

domestic monetary and banking developments through a number of main monetary and banking aggregates and indicators. The following are among the most significant monetary developments during the fiscal year 1998/99:

A- The Domestic Interest Rates:

In furtherance of the monetary stability in the country, the CBK is keen to keep the KD interest rates both in line with the developments in international interest rates on major currencies, and consonant with the requirements of the domestic economic conditions. Consequently, the CBK continued during the fiscal year 1998/99 to monitor the developments in domestic interest rates and assess their conformity with the monetary policy objectives. In light of this monitoring the CBK decided to effect two cuts to the discount rate; the first by a half percentage point in 22 November 1998 and the second by a quarter percentage point in 7 March 1999, i.e. a total reduction of 0.75 percentage point from 7.50% to 6.75%.

It is noteworthy in this regard that the domestic interest rates structure links the maximum limits of interest rates on KD lending transactions to the discount rate within specific margins (which remained unchanged since their application on 25 April 1993). By virtue of the CBK decision on 30 January 1995, the floor of interest rates on KD deposits and savings accounts was abrogated and their determination was left to the interaction of supply and demand forces, as well as competition in the market of these deposits.

Available data on the developments in domestic interest rates show that the interest rates on customer KD deposits with local banks (excluding the Kuwait Finance House) displayed changes reflecting the reduction in discount rate. For example, the average interest rates on three-month customer deposits decreased to 5.24% during the fourth quarter of the fiscal year 1998/99 from 5.90% during the corresponding quarter of the previous fiscal year, i.e. a decline of 0.66 percentage point.

Data on the average interest rates on customer deposits with local banks show that the margins favouring the KD between the averages of interest rates on these deposits in KD on the one hand, and in US dollar on the other hand during the fiscal year 1998/99,

reached 0.60 percentage point (between 5.32% and 4.72%), 0.83 percentage point (between 5.58% and 4.75%), 1.09 percentage point (between 5.84% and 4.75%), 1.14 percentage point (between 5.95% and 4.81%) for the one-month, three-month, six-month, and twelve-month terms respectively.

The average interest rates on the interbank KD deposits of local banks during the fiscal year 1998/99 were in general lower than their previous fiscal year levels. For example, the average interest rates on three-month deposits reached 6.75% during the fiscal year 1998/98 compared to 7.23% during the previous fiscal year, i.e. a decrease of 0.48 percentage point.

The average interest rates on the three-month and six-month Kuwaiti Treasury Bills decreased, in turn, below their previous fiscal year levels. The average interest rates for the above mentioned terms reached 6.44% and 6.60% respectively during the fiscal year 1998/99, from 6.96% and 7.13% respectively during the previous fiscal year.

B- Money Supply:

Available data show that money supply in its broad definition (M2) stood at KD 7805.1 million at end of the fiscal year 1998/99 compared to KD 7550.7 million at end of the previous fiscal year, i.e. an increase of KD 254.3 million or 3.4%. The largest portion of this increase was focused in the increase of KD 195.3 million (or 3.1%) in Quasi-money, and a lesser increase of KD 59.1 million (4.7%) in Money (the narrow definition of money supply M1). This increase is mostly attributable to the increase of KD 53.2 million or 6% in sight deposits (within the private sector deposits with local banks), along with a slight increase of KD 5.8 million or 1.6% in currency in circulation (from KD 357.8 million to KD 363.3 million).

As for money supply components, the balances of private sector deposits with local banks amounted to KD 7441.5 million at end of the fiscal year 1998/99, i.e. an increase of KD 248.5 million or 3.5%, above their level of KD 7192.9 million at end of the previous fiscal year. This increase resulted from the total growth in KD deposits by KD 236.9 million or 3.8% (from KD 6248 million to KD 6484.9 million) and foreign

currency deposits by KD 11.6 million or 1.2% (from KD 944.9 million to KD 956.6 million). The growth in KD deposits was the outcome of the increase in all elements of these deposits without exception, whereby sight deposits increased as mentioned above, along with the increase in savings deposits (KD 134.7 million or 11.8%), time deposits (KD 36 million or 0.9%) and certificates of deposit (KD 12.9 million or 21.8%).

Concerning the factors affecting changes in money supply within the aggregate monetary position of the CBK and local banks at end of the fiscal year 1998/99, the above mentioned increase in money supply (M2) totalling KD 254.3 million was the outcome of the increase in both net domestic assets of these institutions by KD 205.2 million and their net foreign assets by KD 49.1 million. The increase in net foreign assets was the outcome of the increase in net foreign assets of local banks by KD 68.3 million, and the decrease in net foreign assets of the CBK by KD 19.1 million. The most significant developments in net domestic assets was the increase in the claims of local banks on the private sector (most of which in credit facilities) by KD 344.7 million, and the slight increase in claims on the government by KD 6.9 million. This increase was the outcome of the redemption of a portion of the local banks portfolio of Debt Purchase Bonds together with the Purchase Bonds of the Real Estate Portfolio of the Kuwait Finance House by KD 164.8 million, in addition to the increase in the holdings of these banks of Public Debt Instruments by KD 171.7 million.

C- The KD Exchange Rate:

The CBK pursued the implementation of the KD exchange rate policy based on tying the KD exchange rate to a special basket of currencies of countries with major trade and financial relations with the State of Kuwait. Throughout more than twenty-four years of application, this policy proved its effectiveness in maintaining the relative stability of the KD exchange rate against the major currencies, thereby contributing to alleviating the pressure on domestic prices caused by fluctuations in the exchange rates of world currencies. Under this policy, the relative stability of the KD exchange rate against the US dollar, compared to the exchange rates of major currencies, was more pronounced during the fiscal year 1998/99 compared to the previous fiscal year.

The relative stability in the KD exchange rate during the fiscal year 1998/99 is concluded from comparing the movements of the US dollar exchange rate against the Kuwaiti dinar on the one hand, and against the major currencies on the other hand. This comparison shows that the movements of the US dollar exchange rate against the Kuwaiti dinar were within very narrow margins, as the highest and lowest exchange rates of the US dollar against the dinar did not exceed 0.83% and 1.11% during the fiscal year 1998/99. Meanwhile, the US dollar fluctuated by much higher rates against other major currencies, as the highest and lowest exchange rates of the US dollar against these currencies reached, for example, 5.57% and 12.47% against the Japanese yen, 5.03% and 8.08% against the Swiss franc, 5.22% and 6.86% against the Deutsche mark, 5.22% and 6.80% against the French franc, and 1.92% and 3.67% against the Sterling pound.

D- Bank Credit:

During the fiscal year 1998/99, the CBK pursued its supervisory efforts in guiding and rationalizing the credit policies of banks and investment companies, so as to ensure their abidance by the CBK instructions regarding the rules, principles, controls and procedures for extending credit facilities.

The following table shows the value of KD-denominated credit facilities (including consumer loans) extended by local banks to residents during the fiscal year 1998/99 compared to the previous fiscal year, and their relative distribution by sector. These agreements reflect the limits of KD credit facilities extended to new clients or the increase in the limits of credit facilities extended to existing ones.

| Particulars | 1998/99 | | 1997/98 | |
|--|-----------------------|-------------------------------|-----------------------|-------------------------------|
| | Value (KD Million) | Relative Importance (%) | Value (KD Million) | Relative Importance (%) |
| Total Extended Credit Facilities: | 3167.8 | 100.0 | 2721.1 | 100.0 |
| Trade | 982.8 | 31.0 | 820.6 | 30.2 |
| Personal Facilities | 634.0 | 20.0 | 547.7 | 20.1 |
| Real Estate | 433.0 | 13.7 | 320.9 | 11.8 |
| Construction | 402.9 | 12.7 | 269.2 | 9.9 |
| Industry | 205.8 | 6.5 | 155.0 | 5.7 |
| Consumer Loans | 200.2 | 6.3 | 223.1 | 8.2 |

| | | | | |
|---------------------------------|-------|-----|-------|-----|
| Non-bank Financial Institutions | 118.1 | 3.7 | 234.1 | 8.6 |
| Others | 191.0 | 6.0 | 150.1 | 5.5 |

As highlighted in that table, the KD credit facilities extended to residents during the fiscal year 1998/99 totalled KD 3167.8 million, i.e. an increase of KD 446.7 million or 16.4%, compared to KD 2721.1 million during the previous fiscal year. Trade came in the forefront of the sectors benefitting from this increase (KD 982.8 million or 31%), followed by personal facilities (KD 634 million or 20%), real estate (KD 433 million or 13.7%), construction (KD 402.9 million or 12.7%), industry (KD 205.8 million or 6.5%), consumer loans (KD 200.2 million or 6.3%), non-bank financial institutions (KD 118.1 million or 3.7%), and the “Others” sector (KD 191 million or 6%).

The balances of utilized cash credit facilities extended to residents in KD and foreign currencies totalled KD 4924.7 million at the end of the fiscal year 1998/99, i.e. an increase of KD 259.3 million or 5.6% above their level of KD 4665.4 million at end of the previous fiscal year. As for the sectoral distribution of these balances, personal facilities came first (KD 1685.4 million or 34.2%, out of which consumer loans amounted to KD 542.9 million or 11% of the total), followed by real estate (KD 955.8 million or 19.4%), trade (KD 865.6 million or 17.6%), construction (KD 376.6 million or 7.6%), industry (KD 370.2 million or 7.5%), “Others” sector (KD 369 million or 7.5%), non-bank financial institutions (KD 291.5 million or 5.9%) and, finally, the agriculture and fishing sector (KD 10.2 million or 0.3%).

E- Issuing Public Debt Instruments:

During the fiscal year 1998/99, the CBK issued -on behalf of the Ministry of Finance- 26 issues of three-month and six-month Treasury Bills with a nominal value of KD 1602.7 million. Meanwhile, 29 issues of these bills with a nominal value of KD 1840.7 million matured during the same year. Thus, the outstanding balance of Treasury Bills fell by KD 238.1 million (28.1%) to a nominal value of KD 608.9 million at end of the fiscal year 1998/99.

Furthermore, the CBK made sixteen issues of one-year, two-year and three-year term Treasury Bonds whose total value stood at KD 1430 million. The interest rate on these bonds ranged from 6.5% to 7.25% for the one-year term, and reached 6.625% and

6.75% for the two-year and three-year terms respectively. Meanwhile, thirteen previous Treasury Bond issues of a nominal value of KD 967 million matured, bringing the outstanding balance of Treasury Bonds to KD 1658.4 million, i.e. an increase of KD 463 million (38.7%).

As a result of the above developments, the outstanding balance of public debt instruments (Treasury Bills and Bonds) rose to KD 2267.3 million at end of the fiscal year 1998/99, i.e. an increase of KD 224.9 million or 11% above their level of KD 2042.4 million at end of the previous fiscal year.

2- Banking Developments:

During the fiscal year 1998/99, local banks continued strengthening their structures, in terms of relying on more developed professional bases with regard to sources and uses of funds, to embark upon a new phase of a sustainable balanced growth. The characteristics of this professional structure are clearly evidenced in the direction taken by these banks for the continual enhancement of their financing role in the domestic economy through extension of bank credit to all sectors of the domestic economy, while abiding by the CBK instructions and regulations concerning the rules and principles for the provision of such facilities aimed at rationalizing the credit policies of these banks.

Available data show that the aggregate balance sheet of local banks amounted to KD 13046.6 million at end of the fiscal year 1998/99, thus recording a marked growth of KD 163.1 million or 1.3%, compared to its level of KD 12883.4 million at end of the previous fiscal year. This growth is attributable to a number of developments in the elements of this balance sheet on both sides of assets and liabilities. The following are the most significant among these developments:

- ◆ The rise in claims on the private sector by KD 344.7 million or 6.8% to KD 5437.5 million at end of the fiscal year 1998/99, compared to KD 5092.8 million at end of the previous fiscal year. This rise was the outcome of the total increase in both the balances of utilized cash credit facilities extended to the domestic economic sectors by KD 259.3 million or 5.6% (from KD 4665.4 million to KD 4924.7 million) and the investments of local banks in local shares and bonds by KD 85.4 million (20%).

Worthy of note is that this rise in claims on the private sector and the increase in both above mentioned components of these claims, namely cash credit facilities and investments in local shares and bonds, led to the rise in their relative importance in the total assets to 41.7%, 37.7% and 3.9% respectively at end of the fiscal year 1998/99 compared to 39.5%, 36.2% and 3.3% respectively at end of the previous fiscal year.

- ◆ The stability in claims on the government as they recorded a slight increase of KD 6.9 million or 0.2% to KD 4217.1 million at end of the fiscal year 1998/99, compared to KD 4210.3 million at end of the previous fiscal year. This increase was the outcome of the increase in the balances of Public Debt Instruments (Treasury Bills and Bonds) by KD 171.7 million or 9% (from KD 1910.6 million to KD 2082.3 million) on the one hand, and the decrease in the balances of both Debt Purchase Bonds and Purchase Bonds of the Real Estate Portfolio of the Kuwait Finance House by KD 164.8 million or 7.2% (from KD 2299.7 million to KD 2134.9 million) on the other hand. Accordingly, the relative importance in the total assets decreased for both the total claims on the government and the Debt Purchase Bonds (together with the Purchase Bonds of the Real Estate Portfolio) to 32.3% and 16.4%, but rose for Public Debt Instruments to 16% at end of the fiscal year 1998/99, compared to 32.7%, 17.8% and 14.8% for these three elements respectively at end of the previous fiscal year.
- ◆ The tangible decrease in foreign assets by KD 272.8 million or 13.7% to KD 1715.1 million from KD 1987.9 million. This decrease was the outcome of the decline in foreign investments (KD 128.3 million or 28.6%), deposits with foreign banks (KD 125 million or 19.1%), credit facilities extended to non-residents (KD 4.6 million or 0.6%), and other foreign assets (KD 14.7 million or 33.1%).
- ◆ The growth in private sector deposits with local banks by KD 248.5 million or 3.5% (from KD 7192.9 million to KD 7441.5 million). This growth was the outcome of the increase both in KD-deposits by KD 236.9 million or 3.8% (from KD 6248 million to KD 6484.9 million) and foreign currency deposits by KD 11.6 million or 1.2% (from KD 944.9 million to KD 956.6 million). On the other hand, the mentioned increase in KD deposits represents the sum of the increase in all elements of these deposits as illustrated above.

- ◆ The increase in shareholders' equity by KD 87.4 million or 6.2% to KD 1494.7 million at end of the fiscal year 1998/99 from KD 1407.2 million at end of the previous fiscal year.
- ◆ The decrease in foreign liabilities by KD 341 million or 23.7% (from KD 1440.6 million to KD 1099.5 million), was totally ascribable to the decrease in foreign banks deposits with local banks by KD 362.6 million or 26.3%.

Second: Significant Measures Taken and Supervisory Instructions Issued by the CBK

During the fiscal year 1998/99, the CBK continued to take measures and issue instructions as needed in enhancing the tools and methods for overseeing and supervising the banking and financial units subject to its supervision, along with directing their credit policy, so as to ensure their abidance by the sound professional banking and financial practices in conformity with the objectives of the monetary policy regarding the achievement of monetary stability in the country and the enhancement of the soundness of its banking system. In this context, the CBK issued during the fiscal year 1998/99 a number of decisions and instructions to the banking and financial units subject to its supervision. The following were among the most significant of these decisions and instructions:

- 1- The circular issued on 19/7/1998 instructing banks to accurately determine their requirements for national currency notes from the CBK, and to take all necessary measures to ensure the validity and soundness of these notes in their transactions with customers.
- 2- The circular issued on 10/9/1998 instructing Kuwaiti banks to notify the CBK of any financial transactions which they may be entering into with international institutions facing severe financial crises, upon these transactions taking place.
- 3- The circular issued on 27/9/1998 to local banks concerning the accounting treatment of the amortization of goodwill, which provided for such amortization to be carried out by drawing on the financial results of the year in which the acquisition leading to the appearance of goodwill takes place. Yet, the circular mentioned the possibility of

granting approval to requests for extending the amortization period up to 20 years.

- 4- The circular issued on 27/9/1998 to all investment companies regarding the accounting treatment of the amortization of goodwill resulting from acquiring shares in companies and institutions for the purpose of gaining controlling interest in them. The circular provided for carrying out that amortization according to international accounting principles and standards, conditional upon the amortization period not exceeding five years. However, if backed by proper justifications, this period may be extended to twenty years.
- 5- The circular issued on 28/9/1998 to all exchange companies concerning regulations and standards regarding opening branches or establishing new exchange companies.
- 6- The circular issued on 8/10/1998 to all banks and investment companies stating that the suspension of credit facilities extended for the purpose of trading in securities also applies to facilities extended for that purpose by drawing on the customers' funds within the framework of management of third parties' funds.
- 7- The circular issued on 2/11/1998 to all banks concerning the rules and regulations of opening branches inside and outside Kuwait.
- 8- The circular issued on 24/12/1998 to local banks, investment and exchange companies with regard to achieving proper preparedness for testing the year-2000 compatibility of their systems and informing the CBK of the results of these tests; along with laying down emergency plans for the year 2000, at latest by end of June 1999.
- 9- The circular issued on 8/2/1999 to banks and investment companies allowing the resumption of the extension of margin facilities and other loans and credit facilities for the purpose of trading on the Kuwait Stock Exchange, subject to quantitative and qualitative controls which reflect the importance of the establishment by these institutions of a clearly defined policy in the extension of the mentioned credit facilities and their adoption of distinct standards regarding the composition and management of securities portfolios, whether for their own account or on behalf of customers. In the case of banks, these quantitative controls are based on the value of the total credit extended to residents and the bank's capital in its broad definition; for investment companies, these controls are related to the shareholders equity and the customer's credit position.

- 10- The circular issued on 1/3/1999 to all local banks, in support of the CBK instructions on 10/4/1997 which obligated these banks to extend all consumer loans in the form of term loans, and to liquidate all outstanding overdraft balances.
- 11- The circular issued on 20/4/1999 to all local banks, which provided for obtaining the CBK approval of any candidate for the position of “Chief Internal Auditor” or the equivalent thereof.
- 12- The circular issued on 29/4/1999 to all local banks and investment companies concerning the results of testing the main and ancillary computer system applications for year-2000 compatibility, and the possibility of encountering problems or difficulties which may adversely affect the safe transition to year 2000.
- 13- The circular issued on 12/5/1999 to all investment companies operating in compliance with the principles of Islamic Sharia’, which abrogated “Article Third” of the instructions concerning the conditions of appointment and competence of the Sharia’ Supervisory Board in these companies; noting that the mentioned article required obtaining the Ministry of Awqaf and Islamic Affairs’ endorsement of proposed candidates for the membership of the mentioned Board, before their names are presented for approval by the company’s general assembly.
- 14- The circular issued on 31/5/1999 to exchange companies prohibiting them from engaging into transactions involving taking positions in foreign currencies, or speculating in currencies, goods or precious metals whether for their own account or on behalf of third parties, in addition to asserting the obligation on the partners of these companies to ensure that the balances of the latter’s accounts with any local or foreign financial institution cover at any time the total value of cheques and transfers drawn on these accounts, along with the necessity to present the CBK with a quarterly statement of these accounts endorsed by the company’s external auditors, at latest by the tenth day of the month following the period covered by the statement.
- 15- The circular issued on 1/6/1999 to all local banks and investment companies amending the method of calculating general allowances on credit facilities for which no specific allowance was made.

16- The circular issued on 21/6/1999 to all investment companies concerning their abidance by the provisions of the various supervisory instructions issued by the CBK.

Third: Major Operations Performed by the CBK

- 1- The monthly average volume of currency and coins issued during the fiscal year 1998/99 amounted to KD 409.1 million. The volume of issued currency reached its highest level during that fiscal year (KD 472.9 million) in March 1999, and its lowest level (KD 369.3 million) in August 1998.
- 2- The total value of the banking sector operations carried out through the CBK Clearing Room during the fiscal year 1998/99 decreased to KD 3.9 billion, i.e. an average KD 2416.4 per transaction, from KD 4.4 billion, i.e. an average KD 2522.4 per transaction during the fiscal year 1997/98.
- 3- During the fiscal year 1998/99, the CBK processed 8892 banking drafts amounting to KD 427.5 million compared to 8693 drafts valued at KD 478.3 million during the previous fiscal year.
- 4- During the fiscal year 1998/99, the CBK continued issuing public debt instruments -on behalf of the Ministry of Finance - thus making 26 issues of three-month and six-month Treasury Bills valued at KD 1602.7 million, and sixteen issues of one-year, two-year and three-year Treasury Bonds valued at KD 1430 million. Meanwhile, 29 Treasury Bill issues valued at KD 1840.7 million, and thirteen Treasury Bond issues valued at KD 967 million matured during the same fiscal year, as mentioned above.
- 5- The CBK buying and selling transactions with banks and investment companies in the secondary market for Public Debt Instruments during the fiscal year 1998/99 reached 20 transactions for buying Treasury Bills valued at KD 123.9 million and 15 transactions for selling Treasury Bills valued at KD 112.3 million, while no transactions were carried out for selling or buying Treasury Bonds. Furthermore, the CBK concluded one agreement valued at KD 15 million with the above mentioned institutions for the repurchase of these instruments. Consequently, the volume of

CBK's buying and selling transactions in the secondary market for Public Debt Instruments, in addition to repurchase operations, reached KD 251.2 million.

6- During the fiscal year 1998/99, the CBK processed all foreign banking transactions, on behalf of ministries and government bodies, namely documentary credits as well as bills and drafts for collection, as shown in the following table (value in KD):

| Particulars | No. | Value |
|---|-----|----------------|
| First- Documentary Credits: | | |
| 1- Opened: | | |
| -Local | - | - |
| -Foreign | 106 | 28,355,212/205 |
| 2- Paid: | | |
| -Local | 3 | 954,515/662 |
| -Foreign | 205 | 81,687,359/477 |
| 3- Amendments: | | |
| -Local | 1 | - |
| -Foreign | 102 | - |
| Second- Collection Transactions: | | |
| Bills for Collection | 140 | 868,10/536 |
| - In-coming | 77 | 340,434/120 |
| - Paid-up | | |
| Third- Drafts for Collection: | | |
| - Collection | 304 | 638,800/703 |
| - Purchased | - | - |

Fourth: The Labour Force at the CBK

In its endeavours to upgrade the efficiency of staff members, qualify national bankers and increase the percentage of Kuwaiti staff in the total labour force, the CBK pursued during the fiscal year 1998/99 its efforts in developing human resources, through continuing to adopt employment and training policies that aim to attract qualified Kuwaiti cadres to join

the bank and encourage them to take up work in the local banking industry. In addition to the CBK efforts in upgrading its organizational structure by establishing new sections within some of its offices and departments, preparing and endorsing job descriptions reflecting the latest amendments to the minimum requirements for such jobs, along with introducing new job titles, numerous developments in manpower at the CBK occurred during the fiscal year 1998/99, most significant among which were the following:

- 1- The total labour force at the CBK numbered 683 (of which 477 Kuwaitis) at end of the fiscal year 1998/99, compared to 686 (of which 470 Kuwaitis) at end of the previous fiscal year, reflecting a rise in the percentage of Kuwaitis in the CBK to 69.8% from 68.5%, and a decrease in the percentage of expatriates (including unskilled labour) to 30.2% from 31.5%. If unskilled labour are excluded from the comparison, the percentage of Kuwaitis reaches 76.9%. On the other hand, the percentage of Kuwaitis in leadership and supervisory posts at the CBK stood at 93.3%.

- 2- During the fiscal year 1998/99, 53 staff members were appointed at the CBK, of which 46 Kuwaitis (86.8%). Also, 17 Kuwaiti graduates holding university degrees and four Kuwaiti graduates holding the diploma of applied sciences were accepted as trainees for grooming in their relevant jobs at the CBK. On the other hand, 12 Kuwaiti trainees were confirmed in the jobs they were nominated for in the CBK departments and offices during that fiscal year. Of those trainees, 5 were among those accepted in the training programmes for the fiscal year 1997/98; the remaining were among those accepted for training during the fiscal year 1998/99.

- 3- Within the context of the CBK annual training plan reflecting the bank's training requirements which are determined through the joint cooperation of its departments and offices, 20 training programmes were prepared and implemented during the fiscal year 1998/99, and 264 staff members benefitted from these in-house training programmes.

With regard to the specialized training courses organized by the CBK for its staff members during the fiscal year 1998/99 in cooperation with other institutions in Kuwait and abroad, 115 staff members were sent to attend 25 of such courses at international banking institutions abroad; meanwhile, 38 CBK staff members were sent on 31 specialized training courses held in cooperation with training institutions in Kuwait.

Regarding CBK participation in conferences and meetings held at the international, Arab and Gulf countries levels in the areas of economics, banking, finance and other areas of relevance to the CBK activity, 57 staff members of the CBK took part during the fiscal year 1998/99 in 32 of such official conferences and meetings.

- 4- In the area of the educational and training activities held in cooperation with the Institute of Banking Studies (IBS) during the fiscal year 1998/99, 9 Kuwaiti staff members of the CBK were on IBS enrollment for the two-year high diploma in banking studies, (three of them were in the first year and six in the second year). A total of 10 staff members benefitted from the special educational syllabi presented by the IBS to the banking and financial sector according to the free selection syllabus system.

Concerning the specialized banking training courses, English language courses and short courses presented by the IBS, 163 staff members of the CBK were sent to attend these programs during the fiscal year 1998/99.

Fifth :
The Central Bank of Kuwait Balance Sheet
and Profit & Loss Account for the Fiscal Year
Ended 30 June 1999

REPORT OF THE AUDITORS

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 state of affairs of the CBK on 30 June 1999 and of the results of its operations for the year then ended, in compliance with Law No. 32 of 1968 as amended by Law No. 130 of 1977.

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.

Ahmad Mohamad Al-Aiban

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

21 July 1999
State of Kuwait

CENTRAL BANK OF KUWAIT

BALANCE SHEET AS ON

| Assets : | Note | 30 June 1999 | 30 June 1998 |
|--|-------------|-------------------------|-------------------------|
| Gold | | 31,732,140 | 31,732,140 |
| Cash, and Current and Call Accounts in Foreign Currency with Banks and Financial Institutions | | 142,259,609 | 177,980,762 |
| Investments and Deposits in Foreign Currency | 3 | 961,261,035 | 944,372,741 |
| Deposits, Loans and Current Accounts with Local Banks and Financial Institutions in KD | 4 | 5,239,851 | 5,826,334 |
| Other Assets | 5 | 5,202,403 | 5,908,805 |
| | | 1,145,695,038 | 1,165,820,782 |
| Accounts Managed by the CBK on Behalf of the Government of the State of Kuwait and Contra Accounts | 11 | 4,692,099,657 | 4,648,518,592 |

30 JUNE 1999 (KD)

| Capital and Liabilities | Note | 30 June 1999 | 30 June 1998 |
|--|-------------|-------------------------|-------------------------|
| Capital - Fully Paid Up | | 5,000,000 | 5,000,000 |
| General Reserve Fund | 6 | 179,000,000 | 179,000,000 |
| Special Account | 7 | 97,329,327 | 110,738,780 |
| Profit For the Year | | 36,829,836 | 42,116,091 |
| Currency Issued | 8 | 423,788,385 | 405,157,942 |
| Government Accounts | | 203,230,327 | 176,154,604 |
| Local Banks' Accounts and Deposits with the CBK | 9 | 144,266,019 | 206,217,885 |
| International Institutions | | 2,497,611 | 2,182,115 |
| Deposits on Documentary Credits | 11 | 20,496,332 | 22,331,703 |
| Other Liabilities | 10 | 33,257,201 | 16,922,064 |
| | | 1,145,695,038 | 1,165,820,782 |
| Accounts Managed by the CBK on Behalf of the Government of the State of Kuwait and Contra Accounts | 11 | 4,692,099,657 | 4,648,518,592 |

The attached notes from 1 to 14 constitute a part of these financial statements.

**PROFIT & LOSS ACCOUNT FOR
THE YEAR ENDED 30 JUNE 1999**

| | Note | 1998/99 (Ending 30 June) | 1997/98 (Ending 30 June) |
|---|------|-----------------------------|-----------------------------|
| Interest & Income From Investments | | 51,819,715 | 59,416,034 |
| Interest and Commission Expenses | | (3,922,647) | (4,095,679) |
| Provisions Against Bad Debt & Investments | | (392,549) | (852,299) |
| | | 47,504,519 | 54,468,056 |
| Other Income | | 304,025 | 307,169 |
| Operating Income | | 47,808,544 | 54,775,225 |
| Operating Expenses | 12 | 10,978,708 | 12,659,134 |
| Profit For the Year to be Transferred to the Ministry of Finance in Accordance with Article 17, paragraph 3 (b), of Law No. 32 of 1968 amended by the Law No. 130 of 1977 | | 36,829,836 | 42,116,091 |

The attached notes from 1 to 14 constitute a 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 as amended by Law No. 130 of 1977. The CBK is a public institution with an independent juristic personality, and is entrusted with the issue of the local currency on behalf of the State of Kuwait, the security of the stability of the Kuwaiti currency and its free convertibility into other currencies, directing the monetary and credit policies, the supervision of the banking and financial system and serving as banker and financial advisor to the Government.

2- Significant Accounting Policies:

These financial statements have been prepared in accordance with Law No. 32 of 1968 as amended by Law No. 130 of 1977. The applied significant accounting policies are as follows:

(a) Gold:

In accordance with the Amiri Decree of 9 July 1978, gold is valued at KD 12.500 per fine ounce.

- (b) Long-term Investments:** Long-term investments which comprise bonds of foreign governments and Kuwaiti Dinar local bonds are stated at cost, adjusted for any premium or discount as appropriate, with provision for any permanent decline in value on an individual basis.

(c) Revenue Recognition:

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

(d) Capital Expenditure:

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

(e) Foreign Currencies:

In accordance with Article 48 of Law No. 32 of 1968 (as amended by Law No. 130 of 1977) and the Amiri Decree of 9 July 1978, all assets and liabilities in foreign currencies at the balance sheet date are translated into Kuwait Dinars at the year end rates of exchange and resulting gains or losses are taken to a special account.

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

| | 30 June 1999 | 30 June 1998 |
|--|---------------------------|---------------------------|
| Deposits with Banks and Foreign Institutions | 956,622,335 | 939,775,091 |
| Bonds of Foreign Governments | 4,598,700 | 4,597,650 |
| | <u>961,261,035</u> | <u>944,372,741</u> |

4- Deposits & Loans in KD with Local Banks and Financial Institutions (KD):

| | 30 June 1999 | 30 June 1998 |
|-----------------------------|-------------------------|-------------------------|
| Loan | 6,484,699 | 6,678,633 |
| Provision for Doubtful Debt | (1,244,848) | (852,299) |
| | <u>5,239,851</u> | <u>5,826,334</u> |

5- Other Assets (KD):

| | 30 June 1999 | 30 June 1998 |
|---|-------------------------|-------------------------|
| Interest Receivable on Deposits and other Assets | 1,469,390 | 1,929,276 |
| CBK's Share in the Capital of the Industrial Bank of Kuwait | 2,511,210 | 2,511,210 |
| Other Debit Balances | 883,643 | 1,350,035 |
| Prepaid Expenses | 338,160 | 118,284 |
| | <u>5,202,403</u> | <u>5,908,805</u> |

6- General Reserve Fund:

In accordance with Article 17, paragraphs 3(a) and 3(b), of Law No. 32 of 1968 (as amended by Law No. 130 of 1977) the net profit 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.

7- Special Account (KD):

| | 30 June 1999 | 30 June 1998 |
|--|--------------------------|---------------------------|
| Balance at Beginning of the Year | 110,738,780 | 104,598,597 |
| Net Profit (loss) on Foreign Exchange Resulting From Revaluation of Assets and Liabilities in Foreign Currencies | (13,409,453) | 6,140,183 |
| Balance at End of the Year | <u>97,329,327</u> | <u>110,738,780</u> |

The special account represents the net profit accumulated as a result of revaluation of all 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 (as amended by Law No. 130 of 1977) and the Amiri Decree of 9 July 1978.

8- Currency Issued (KD):

| | 30 June | 30 June |
|-------------------------------------|--------------------|--------------------|
| | 1999 | 1998 |
| Net Currency Produced | 999,402,256 | 1,045,777,526 |
| Less : Currency in the CBK's Vaults | 575,613,871 | 640,619,986 |
| | 423,788,385 | 405,157,540 |

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

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

| | 30 June | 30 June |
|------------------|--------------------|--------------------|
| | 1999 | 1998 |
| Current Accounts | 49,516,019 | 110,717,885 |
| Deposits | 94,750,000 | 95,500,000 |
| | 144,266,019 | 206,217,885 |

10- Other Liabilities (KD):

| | 30 June | 30 June |
|-----------------------|-------------------|-------------------|
| | 1999 | 1998 |
| Accrued Expenses | 922,692 | 1,395,085 |
| Other Credit Balances | 32,334,509 | 15,526,979 |
| | 33,257,201 | 16,922,064 |

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

11- Accounts Managed by the CBK on Behalf of the Government of the State of Kuwait and Contra Accounts:

| | 30 June 1999 | 30 June 1998 |
|---|-----------------------------|-----------------------------|
| Accounts Managed by the CBK on Behalf of the Government | 4,586,019,873 | 4,471,251,424 |
| Contra Accounts: | | |
| Letters of Credit | 73,449,912 | 143,607,803 |
| Memorial Notes and Coins | 1,321,080 | 1,390,359 |
| Forward Transactions on Behalf of the Kuwait Investment Authority | 6,151,421 | 6,154,426 |
| Repayments According to the Law No. 41 of 1993 | 25,157,371 | 26,114,580 |
| | <u>106,079,784</u> | <u>177,267,168</u> |
| | <u>4,692,099,657</u> | <u>4,648,518,592</u> |

On 30 June 1999, deposits of KD 20,496,332 (against KD 22,331,703 on 30 June 1998) were held against the letters of credit referred to above.

12- Operating Expenses (KD):

| | 30 June 1999 | 30 June 1998 |
|--|-------------------------|-------------------------|
| Employee Costs | 8,600,020 | 8,469,031 |
| Administrative and Computer Costs | 680,826 | 1,103,731 |
| Purchases of Furniture, Equipment and Vehicles | 147,758 | 594,124 |
| Production and Shipment of Currency | 554,897 | 1,511,754 |
| Sundry Expenses | 995,207 | 980,494 |
| | <u>10,978,708</u> | <u>12,659,134</u> |

13- Compensation Claims:

The CBK has submitted a claim amounting to KD 73,132,296 to the Public Authority for the Assessment of Compensation for losses suffered as a result of the Iraqi invasion and occupation of the State of Kuwait.

14- Promissory Notes Held:

On 30 June 1999, promissory notes held by the CBK in safe custody on behalf of international institutions totaled KD 483,390,121 (against KD 391,736,079 on 30 June 1998).

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