مؤسسة الخليج للإستثمار
Gulf Investment Corporation

Annual Report and Accounts 2001

Gulf Investment Corporation is a leading regional financial institution that was established under the auspices of the Gulf Cooperation Council and is equally owned by the governments of the six member states: Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates.

We are committed to provide a comprehensive range of financial services that support the development of private enterprise and economic growth in the Gulf region.

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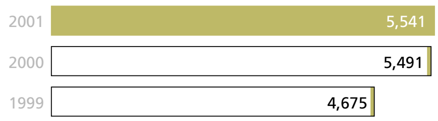
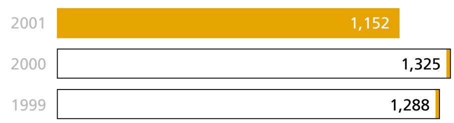
Financial Highlights

Net Income
(US$ million)

Total Assets
(US$ million)



Shareholders' Equity
(US$ million)



US$ million	**2001**	2000	1999
For the year			
Net Interest Income	**48.8**	6.7	22.2
Other Income	**51.7**	44.7	100.8
Operating Expenses	**26.9**	26.2	37.6
Income from Discontinued Operations	**26.7**	85.6	49.0
Net Income	**85.3**	111.7	120.4
At year end			
Total Assets	**5,541.0**	5,491.3	4,674.5
Trading Securities & Managed Funds	**220.6**	238.3	241.1
Investment Securities	**3,055.6**	2,986.3	2,182.6
Loans & Credit Funds	**487.9**	532.3	562.5
Deposits	**1,464.8**	1,630.4	1,309.5
Shareholders' Equity	**1,151.7**	1,324.8	1,288.1
Selected Ratios (%)			
Profitability			
Return on Paid-up Capital	**11.4**	14.9	16.1
Return on Average Shareholders' Equity	**8.3**	8.6	9.6
Capital			
BIS ratios			
– Total	**35.9**	33.7	39.5
– Tier 1	**35.8**	33.6	39.0
Shareholders' Equity as a % of Total Assets	**20.8**	24.1	27.6
Asset Quality			
Loans & Credit Funds as a % of Total Assets	**8.8**	9.7	12.0
Marketable Securities as a % of Total Assets	**55.0**	55.3	48.0
GCC and OECD country risks as % of Total Assets	**95.9**	95.7	95.5
Liquidity			
Liquid Assets Ratio	**71.7**	65.0	63.2

Note: Where necessary, prior years' comparative figures have been adjusted to conform with changes in presentation in the current year.

Board of Directors

Kingdom of Saudi Arabia
H.E. Dr. Ibrahim Al-Assaf
Chairman
Minister of Finance and National Economy

H.E. Hamad Al-Sayari §
Governor, Saudi Arabian Monetary Agency

Sultanate of Oman
H.E. Ahmed Macki *
Deputy Chairman
Minister of National Economy and
Deputy Chairman of the Financial Affairs and
Energy Resources Council

Mr. Darwish bin Ismail bin Ali Al-Bulushi §
Undersecretary of Financial Affairs
Ministry of Finance

State of Qatar
H.E. Yousef Hussain Kamal
Minister of Finance, Economy and Commerce

H.E. Abdulla Khalid Al-Attiya §
Governor, Qatar Central Bank

State of Kuwait
H.E. Dr. Yousef H. Al-Ebraheem
Minister of Finance and Minister of Planning
and Minister of State for Administrative
Development Affairs

Mr. Abdulmohsen Yousef Al-Hunaif §
Undersecretary, Ministry of Finance

United Arab Emirates
H.E. Dr. Mohammed Khalfan Bin Khirbash
Minister of State for Finance and Industry

Mr. Rashed Ahmed Rasheed §
Deputy General Manager
Emirates Management Services Corporation

Kingdom of Bahrain
H.E. Abdulla H. Saif
Minister of Finance and National Economy

Mr. Rashid Ismail Al Meer §
Director General
The Pension Fund Commission

Senior Management
Mr. Hisham Abdulrazzak Al Razzuqi
Chief Executive Officer

* Chairman of the Executive Committee
§ Member of the Executive Committee


State of Kuwait
Kingdom
of Bahrain
State of Qatar
United Arab Emirates
Kingdom of Saudi Arabia
Sultanate of
Oman

Chairman's Statement

On behalf of the Board of Directors, I have the privilege to present the Annual Report and Accounts of Gulf Investment Corporation for the year 2001.

2001 was a pivotal year for the Corporation with significant changes to the organization structure and operating activities. The divestiture of Gulf International Bank (GIB), the principal subsidiary in which the Corporation had a 72.45% ownership, was successfully concluded during the year. Additionally, in 2001, the board approved the implementation of a re-energized strategic action plan which, we are confident, will enable GIC to embark on a new phase in its growth as a stand-alone organization.

I am pleased to report that despite the organizational changes, and in a year of increased volatility within global financial markets, the core businesses within GIC achieved excellent results. While operating revenues almost doubled to US$ 100.5 million, relative to the previous year, related expenses remained at about the same level, thanks to the sharp focus and discipline in managing expenses. The increase in operating revenues can be primarily attributed to the significantly higher net interest income, generated from higher spreads yielded on the investment securities portfolio. The planned build up of this investment portfolio over the years, coupled with prudent management of its funding profile, resulted in the superior performance. The Corporation was also successful in stabilizing its revenue profile, by shifting emphasis away from exposures sensitive to market movements, and towards market-neutral and alternative investment strategies.

Although contributions from GIB were reduced by almost 70% year-on-year, net income prior to provisions declined by only 10%. This was principally due to the 125% increase in earnings from GIC's own global market and principal investing businesses, which compensated, to a large extent, the loss in earnings from GIB. Subsequent to the sale of GIB, the Corporation paid a special dividend of US$ 303.2 million to the shareholders, deducted from the US$ 1,324.8 million equity base of year end 2000. The shareholders utilized this amount as a partial settlement for the purchase of GIB. As of the 2001 year end, the Corporation's shareholders' equity stood at US$ 1,151.7 million and total assets reached US$ 5,541.0 million. At over 20% of total assets, the Corporation's solid capital base forms a key competitive advantage through which we aim to grow our business.

The new strategy, focusing on the principal investing activity, was developed with the goal of establishing GIC as a regional leader. The main premise of this strategy is for GIC to take advantage of attractive investment opportunities in energy, manufacturing and financial services among others, while paying close attention to deal flow and investment rates. The new strategy envisages diversification of revenue sources as well, primarily through the expansion of global market and fee based operations. Targeting improved operating efficiencies, steps were taken to realign certain business activities and consolidate support functions.

Looking forward, I am confident that, with the strategic initiatives taken in 2001, GIC is now well positioned to take advantage of the opportunities in the region and is capable of providing enhanced services to its customers. GIC will continue to play a lead role in supporting the economic growth and the development of private enterprise in the Gulf region.

In accordance with the relevant Articles of Association, the Minister of National Economy of the Sultanate of Oman, H.E. Ahmed Macki will take over the post of Chairman of the Board, and H.E. Yousef Hussain Kamal, Minister of Finance, Economy and Commerce of the State of Qatar, will assume the position of Deputy Chairman and Chairman of the executive committee. These changes will take effect from the date of the Corporation's General Assembly held on April 15, 2002. I welcome them to these positions and am confident that under their leadership Gulf Investment Corporation will continue to be a leading provider of diversified financial services in the region.

Dr. Ibrahim Al-Assaf
Chairman

2001 was a challenging year for GIC, both in terms of the global operating environment and the transformation within the organization. GIC's sound performance in 2001 proves, yet again, the Corporation's flexibility and resilience.

I am confident that with strategic initiatives taken in 2001, we will be able to enhance operating efficiency and further improve our financial performance.

The US$ 85.3 million net income earned in 2001 is indicative of our success in facing the challenges and taking advantage of the opportunities in a rapidly changing business environment. All our key businesses fared well, exceeding annual targets and previous year performances. The net income, generated from operating revenues of US$ 100.5 million, does not include an unrealized portion of US$ 45.5 million relating to increase in fair value of certain investment securities. On the basis of new accounting standards (IAS 39), the unrealized gain on the portfolio of securities held for sale was not included within the net income for the year, and represents a potential for future realizations. This is also indicative of the superior quality of holdings within the portfolio.

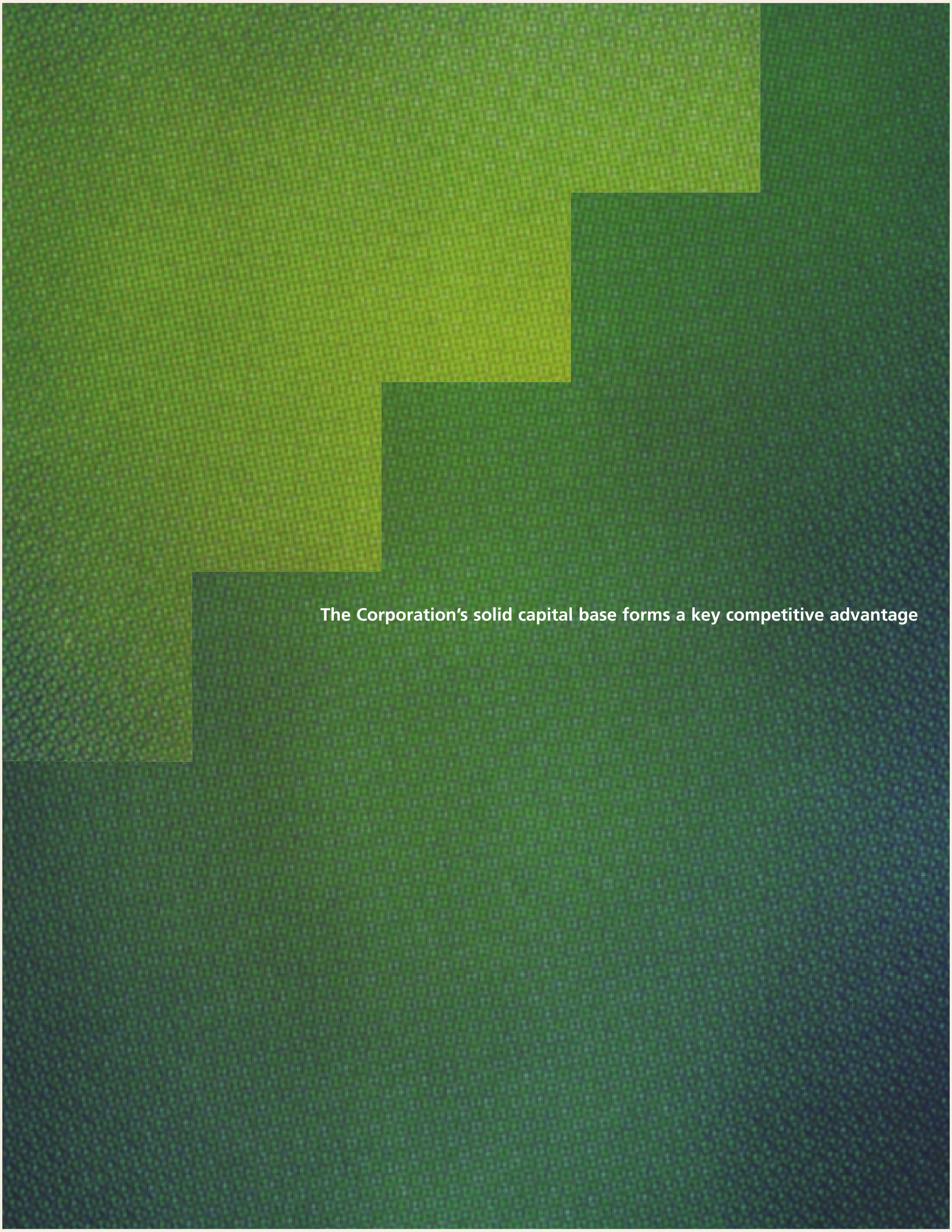
The sale of Gulf International Bank (GIB) reflects a high point in the Corporation's investment strategy based on the concept of investing, developing and divesting. GIB was acquired in 1991 by injecting almost US$ 450 million in capital, and over the past eleven years, under the ownership of GIC, GIB operations grew in scope and scale. In April 2001, the GIC board decided to separate the two entities by effecting a sale of GIB to the shareholders. The entire transaction was handled at an "arms length" basis, and as per the board approved terms, GIC was to obtain sale consideration of US$ 873.7 million, representing the carrying value of GIB at end of year 2000. Following a partial settlement made against the sale consideration, the outstanding balance earned a competitive 4.33% during 2001. As of December 31, 2001, US$ 577.1 million remained as due from shareholders. This outstanding balance is expected to be fully repaid in the next few years, through dividend payments made by GIC and GIB to shareholders.

The impact of the divestiture on GIC's earnings was moderated as the contributions from the Corporation's own principal investing and global market businesses more than doubled compared to a year ago. In light of the sale, and with the objective of optimizing capital utilization, GIC conducted a detailed strategic review of its operations, keeping in perspective the objectives and aspirations of the organization. Based on this reassessment, we have developed a blueprint for the planned and phased expansion of our business activities. The new strategy incorporates three key features:

- Focus will continue to be on the GCC region, with particular emphasis on expanding and restructuring the principal investing activity.
- The global markets investment business will continue to play a "return enhancement role".
- Additional resources will be allocated for the development of fee-based businesses.

Principal Investing will continue to play the central role in GIC's operations with the objective of achieving the Corporation's fundamental purpose. The thrust, however, will be towards achieving adequate deal flow and investment return rates, in line with the Corporation's commercial performance objectives. In this regard, fresh sectors or themes that promise greater potential for value realization will be targeted. These sectors include utilities, electricity in particular, financial services and selected manufacturing niches.

In addition to identifying new sectors, the principal investing team will strive to increase influence and participation in the management


The Corporation's solid capital base forms a key competitive advantage

of its project ventures. These initiatives were very much in evidence during 2001, when GIC played a key role in the capital restructuring of two of its major investments. In another instance, the GIC team made significant contributions with regards to effecting the successful merger of two portfolio companies – Al Rawabi Dairy and Emirates Poultry. Both these companies, based in the UAE, are expected to gain considerably from the synergies derived.

A number of GIC associate companies commenced commercial production during the year. These include Gulf Stone in Oman, Kuwait International Advanced Industries and Al Manar Plastics in Saudi Arabia. During 2001, GIC invested in Ras Laffan Power Company, an independent power producer (IPP) in Qatar with a 10% equity holding. The US$ 700 million project involves the development of a 750 megawatt power station on a Build, Operate and Transfer (BOT) basis that will also produce about 40 million imperial gallons of potable water daily.

Global Markets Investments have in the past, and will continue in future, to contribute to the profitability of the Corporation. In 2001, the spread income generated by the US$ 3.1 billion investment securities portfolio was the prime driver for the approximately sevenfold increase in net interest income. This portfolio made of superior grade debt securities forms a source of liquidity as well. Over the past few years, we have succeeded in stabilizing earnings, by shifting emphasis away from exposures sensitive to market movements towards market-neutral and alternative investment strategies. Exposure to the global equity markets were significantly reduced in 2001, and replaced by market-neutral strategy funds with superior risk-return characteristics. With the objective of maintaining diversity in our revenue source, the international private equity and credit fund portfolios are being gradually expanded.

GIC's success with alternative investment strategies is highlighted by the superior performance of its Alternative Strategies Fund (ASF). A conservatively managed multi strategy fund of funds, ASF was seeded with US$ 70 million by GIC in 1999, and has registered an average annual return of almost 10% since inception. As of 31st December 2001, the fund has attracted approximately US$ 150 million of additional investments from GIC's customer base.

With increasing strategic focus on the GCC region, GIC will leverage its deep knowledge of the region to the benefit of domestic and international clients who are interested in investing in the region's active capital markets. The newly created GCC Equities Unit is exploring initiatives for new investment products appropriate to the needs of prospective clients.

Fee based operations will be given particular emphasis in future and in this regard a Marketing unit and a Financial Advisory unit have been established. The objective of the Marketing team will be to efficiently deliver a range of financial products available in the regional and international markets to the Corporation's ever expanding client base.
The financial advisory service is well positioned to take advantage of the accelerated pace of privatizations within the GCC states and renewed interest in corporatizing the operations of family owned companies.
The Corporation will constantly endeavor to expand its sources of revenue from fees based business as such income entails low risk, diversifies revenue and puts little pressure on capital ratios.

Particular attention is being given to methods related to improving origination and distribution capabilities. We hope to accomplish this by gradually creating a presence in GCC markets. In the principal investing, client services, and financial markets activity mentioned above, GIC is working towards being recognized as the regional leader.

GIC is in the process of developing a performance based compensation package aimed at enhancing productivity and effectiveness across the organization. Emphasis is being placed on participation, entrepreneurship and knowledge sharing. These initiatives, coupled with the benefits derived from the realignment and consolidation of certain business and support functions, are bound to have a positive impact on bottom line and employee morale.

GIC's sound performance in 2001 represents the achievement of a dedicated and committed team of professionals. I am privileged to lead such a team and am confident that we will achieve our objectives and succeed in our new strategy to the benefit of our shareholders and the region we serve.

Hisham Abdulrazzak Al Razzuqi
Chief Executive Officer

The year witnessed a sharp slowing down of the world economy. The US economy, representing around 22% of the world economy, went officially into recession. Japan, the second largest economy, underwent negative growth. Europe sharply slowed down, with its largest economy, Germany, in recession. Hong Kong, Taiwan and Singapore, long considered star performers, witnessed negative growth. The GCC region – sharing in the impact of slowing world economic growth, suffered from the dual impact of lower oil prices and lower oil production and export. Nevertheless, efforts by the GCC governments to restructure their economies continued unabated.

The World Economy

The year started on a cautionary note. During 2000, major world equity markets performed poorly, especially in the US. The question at the beginning of the year was: is 2001 going to witness growth and vitality in the US so that equity markets perform better, or is it going to witness a "full" burst of a bubble that has been going on for several years? The Federal Reserve Board in the US started the year by giving its verdict on what to expect: a cut in the Federal Funds rate of 50 basis points in an unscheduled meeting on January 3. That meant that the Federal Reserve had decided that the risk was on the negative side of the growth equation.

This cut in January was to be followed by 10 more cuts for a total of 475 basis points between January and December 2001. The US economy, which grew by 4.1% in 2000, grew by 1.2% in 2001.*

The year has also shown the importance of the role played by the US economy in the world. It has been a locomotive for world growth during the 1990's. It is credited with helping major Asian countries (Korea, Malaysia, Thailand and to some extent Indonesia) in overcoming their crisis in 1997-98. With the US economy showing signs of weakness at the beginning of the year, the prognosis, then, for world growth was not positive. European economies – especially the major ones in Germany and France – were unable to perform the locomotive role due to structural problems in the labor markets and a less developed entrepreneurial culture for growth and innovation. The Japanese economy continued to be mired in problems of increasing public debt, a worsening banking system suffering from a ballooning bad debts problem that was left to linger for years, and deflation.

After growing by 3.4% in 2000, the Euro area is expected to show 1.5% growth for the year, better than the US – which suffered from a bursting stock market bubble – but not adequate for it to become a leader for world growth. Japan, according to IMF estimates, will have negative growth for the year. In fact, among the G-7 economies (US, Japan, Germany, France Canada, UK and Italy), the UK is the only one expected to show growth of more than 2% in 2001 (at 2.2%) ≈.

It is debatable, therefore, if we could say that the world economy was in recession in 2001. According to the IMF, the world economy is expected to grow by 2.4%, but the United Nations Department of Economic and Social Affairs expects world economic growth of 1.4%. Other forecasters, especially major Wall Street firms, expect the world economy to grow by less than 2% in the year. Most economists would consider the world economy in recession if it grows by 2% or less. That is something that has not happened since the 1973-74 world recession.

* IMF World Economic Outlook, December 2001, and Consensus Economics Inc., April 2002

≈ Consensus Economics Inc., April 2002

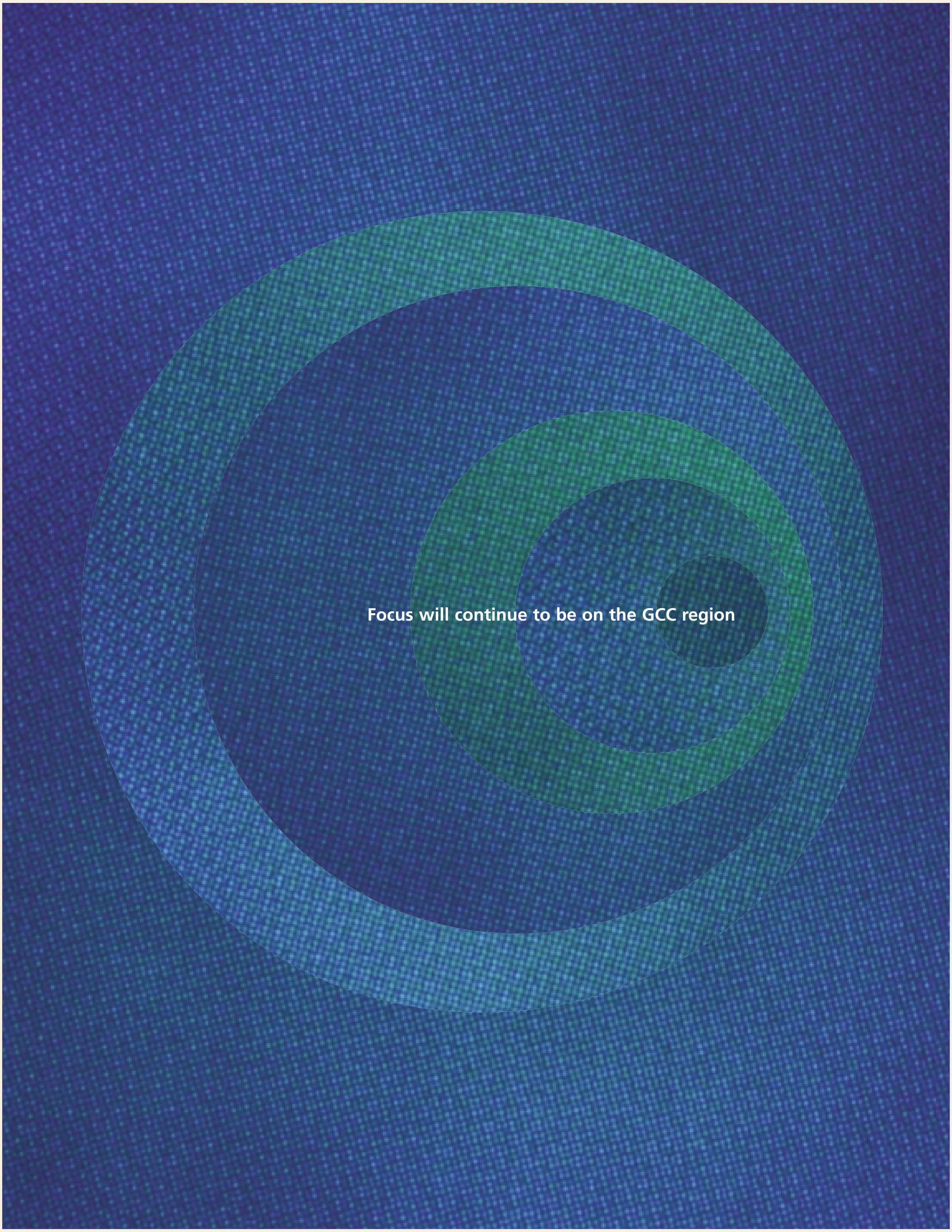

Focus will continue to be on the GCC region

Table 1 Global Stock Market Indexes (in local currencies)

	29 Dec 2000	31 Dec 2001	% Change 2001
DJIA	10,786.85	10,021.50	**-7.10**
S&P 500	1,320.28	1,148.08	**-13.04**
NASDAQ Composite	2,470.52	1,950.40	**-21.05**
FTSE 100	6,222.50	5,217.40	**-16.15**
DAX	6,433.61	5,160.10*	**-19.79**
CAC-40	5,926.42	4,624.58*	**-21.97**
Nikkei 225	13,785.69	10,542.62*	**-23.53**
Hang Seng	15,095.53	11,397.20	**-24.50**

* Last trading day was December 28, 2001

World Stock and Bond Markets

This rather gloomy world economic picture affected the performance of international capital markets. What started as US cyclical adjustment was exacerbated by the impact of the burst in the "technology bubble" and the events of September 11. And what happens in the US is always felt in other equity markets. A quick look at Table 1 shows that all major indexes in the main world equity markets went down for the year. Technology-dominated NASDAQ Composite suffered more than other equity indexes in the US: a drop of 21% vs. a drop of 13% and 7% for S&P 500 and the Dow Jones Industrial Average respectively. Japan suffered badly (-23.53%) because it was the worst performing major economy, with actual negative growth for the year.

The other significant sign in the world stock markets was the degree of volatility. This of course relates to the impact of the events of September 11 in the US and the dire mood that followed that totally unexpected and horrible terrorist act. The movement between the highest and lowest points of some of the equity indexes was more than 100% (NASDAQ Composite in the US). However, all major stock indexes witnessed volatility and sharp movements as Table 2 shows. The lackluster performance of the stock markets led many investors to look to "alternative investment" strategies. Hedge funds and other kinds with diversified strategies among short and long have boomed during the year. In addition, the bond markets represented a haven for investors who saw unacceptable market risk in equities. Indeed, bond markets have ended the year positively. In the US, corporate bonds returned 10.7% to investors (versus 9.1% in 2000), and mortgages returned 8.1% (less than the 11.3% for 2000)*. The US treasuries overall did well, with returns ranging from 7.8% for 2-year notes, 8.7% for 5-year notes, and 6.4% and 5.5% respectively for 10-year and 30-year bonds, but declining interest rates made bank deposits less attractive all over.

The GCC countries who are mainly capital exporters did not realize substantial returns on their international market portfolios. An open question is still the impact of September 11 events on the international capital movements and whether substantial repatriation of capital has taken or will take place, particularly for private investors in the region. It is too early to tell how much capital has been or will be repatriated but a sober analysis indicates that it will not be substantial. The absorptive capacity of the GCC capital markets is limited and ultimately the impact of the events of September 11 on basic capital movements to and from the region may be considered a blip rather than the start of a main trend.

Conditions in the Oil Markets

The oil markets finished the year 2000 on a buoyant note with an average oil price for the year at $28.44. The US economy and the global economy, however, continued to weaken through the year 2001 and consequently oil demand growth also weakened. In an effort to maintain a stable market, OPEC reduced production targets three times during the year. As a result of the events of September 11, airline

* Merrill Lynch

Table 2 World Stock Market Volatility During 2001

	High for the year		Low for the year		
World Indexes	Local Currency	Date	Local Currency	Date	**% change**
North America					
DJIA	11,337.92	21-May	8,235.81	21-Sep	**38**
S&P 500	1,373.73	30-Jan	965.80	21-Sep	**42**
NASDAQ Composite	2,859.15	24-Jan	1,423.19	21-Sep	**101**
Europe					
FTSE 100	6,334.50	30-Jan	4,433.70	21-Sep	**43**
XETRA DAX	6,795.14	31-Jan	3,787.23	21-Sep	**79**
CAC-40	5,998.49	31-Jan	3,652.87	21-Sep	**64**
Asia					
Nikkei 225	14,529.41	7-May	9,504.41	17-Sep	**53**
Hang Seng	16,163.99	1-Feb	8,934.20	21-Sep	**81**

Daily closing prices have been taken for this analysis

travel fell dramatically, retail sales plunged and job cuts increased.

The events in the oil markets during 2001 could be described as potentially very meaningful in determining the future course of prices. In October, OPEC asked non-OPEC producers to actively co-operate in maintaining a stable market environment. A meeting was held in Vienna in late October between OPEC and some key non-OPEC producers including Angola, Egypt, Kazakhstan, Mexico, Norway and Russia. This was followed by an OPEC meeting on November 14, where OPEC decided to trim output by around 1-1.5 million b/d provided non-OPEC producers came forward with a cut of some 500,000 b/d.

OPEC announced in a meeting held in Cairo in late December that it would reduce its output by 1.5 million b/d from January 1st and that leading independent producers including Russia, Norway and Mexico have agreed to production cuts of 462,500 b/d from January. It would appear that this agreement could conceivably usher in an era of greater co-operation between producers leading to stable and predictable prices for a vital commodity.

The supply demand equations are critical in determining oil price trends especially over the medium and the long-term, and these equations remain in favor of OPEC and, more particularly, Gulf producers. Increasing non-OPEC production played a significant role in the erosion of OPEC's market share over the past two decades. North America dominated non-OPEC supply in the early seventies, the North Sea and Mexico evolved as major producers in the eighties, and much of the new production in the nineties has come from the developing countries of Latin America, China, Vietnam, and Angola along with other African countries. Whereas non-OPEC production thus greatly influenced oil prices from the mid-seventies through the mid-nineties, both their reserves and future production capacities are now constrained. Some of the relevant statistics are illuminating. The proved oil reserves of OPEC countries are estimated to be in excess of 800 billion barrels or just under 80% of the global total. The non-OPEC reserves excluding the Former Soviet Union (FSU) are estimated to be only around 166 billion barrels, a number that has remained virtually unchanged from 1980 and has dropped significantly from 1990, while OPEC reserves have almost doubled during the past twenty years. Reserves have diminished in the US, Canada and Mexico, which have been offset only partially by rising reserves in the North Sea, Latin America and Africa. As oil consumption inexorably and steadily increases over the next twenty years particularly in developed economies (Exhibit 1), the demand for OPEC crude is expected to move significantly higher. Highly respected Western sources estimate that OPEC's share of global oil production will increase to 45% of the total in 2010 and to 50% in 2020 from a current level of 40%.*

* International Energy Outlook, US Department of Energy, 2000

Global Oil Demand MM b/d

	1998	1999	2000	2001	2002
Demand	73.5	75.3	75.9	76.0	76.6

Source: World Energy Outlook – 2001

Long Range Global Oil Demand MM b/d

	1990	2005	2010	2015	2020
Demand	66.0	83.9	93.5	103.4	115.0

Source: International Energy Outlook – US Department of Energy 2000

Estimated Production Capacities MM b/d

	1990	2005	2010	2015	2020
OPEC	27.2	40.6	45.1	50.8	58.8
of which:					
Gulf Countries	18.7	28.0	31.4	36.9	44.8
Non-OPEC	42.3	47.1	51.5	54.8	56.6
Total World	69.5	87.7	96.6	105.6	115.4

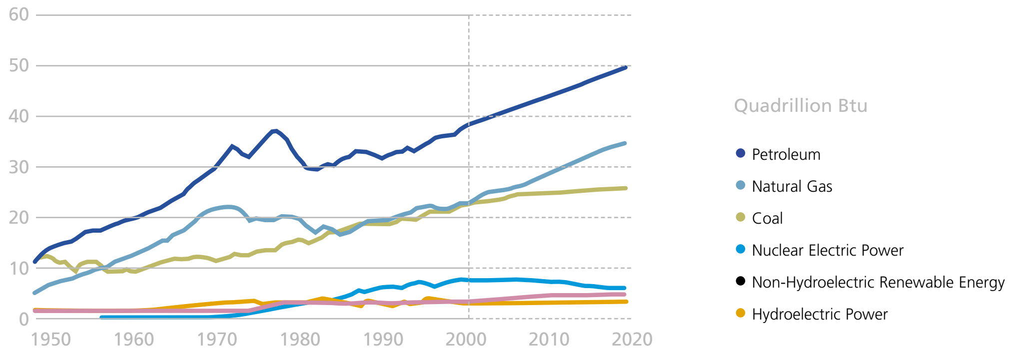
Source: International Energy Outlook – US Department of Energy 2000

Proven Reserves (Billion Barrels)

	1980	1990	1999	2000
OPEC	432.8	771.7	802.5	814.4
Non-OPEC	164.1	180.3	166.2	166.7
FSU	63.0	57.0	65.4	65.3
Total World	659.9	1,009.0	1,034.0	1,046.4

Source: BP, Statistical Review of World Energy – June 2001

Exhibit 1 Energy Consumption History and Outlook, 1949-2020



Source: U.S. Dept. of Energy, EIA, Annual Energy Review 2000

The need for stable oil markets and reasonable prices is paramount not only for the oil producers, who would need to invest heavily in order to build necessary production capacity, but for the consuming nations as well. OPEC's philosophy has revolved around these guiding principles for the past decade: that the price must be a fair one for both producers and consumers so that economic growth is not hindered in the consuming world without impacting living standards in producing countries. This theme of close co-operation between producers and consuming nations has been iterated by GCC oil ministers.

Economic developments in the GCC region

2000 was a very favorable year for Gulf economies for a variety of reasons. Obviously the main thrust was provided by rising oil prices which were supported by the beginning of economic reforms and a trend towards economic liberalization. That year saw GCC economies grow at double-digit rates in nominal terms and at some 5% in real terms. Consumer prices remained stable as they have been for some years now. Government budgets were balanced or even showed surpluses, current accounts turned positive, and trade balances, which are generally positive, improved further.

The performance in 2001 was less encouraging due to global economic slowdown. At the same time, oil prices remained generally resilient through the end of August 2001, propped up by OPEC's production cuts and amidst hopes that any recession would be short-lived with growth resuming in 2002. Current forecasts support the view that the main world economies – with the exception of Japan – would rebound in 2002. GCC economies have been affected by oil price erosion during 2001 as well as by some loss in export volume. The non-oil sector remained strong, however, offsetting, to a certain degree, the shortfall from the oil business. LNG production, aluminum smelting, petrochemicals, financial services and tourism continued with their expansion programs, although pricing pressure was felt by petrochemicals and LNG. GCC countries are aggressively pursuing the gas alternative to feed industries such as power generation, metallurgy, petrochemicals production and as fuel in a variety of end-uses.

GCC countries have always had positive trade balances. 2001 is likely to show close to breakeven performance for current account for GCC economies as a whole, with some showing surpluses. Interest rates have declined rapidly

Table 3 GCC Oil Prices US$/bbl

Oil Prices	1997	1998	1999	2000	**2001**
OPEC Basket	18.68	12.28*	17.47	27.60	**23.13**
Arab Light	18.71	12.20	17.45	26.81	**23.06**
Brent Crude	19.06	12.71	17.91	28.44	**24.46**

* In December 1998 the average price for OPEC Basket was US$ 9.67 per barrel
Source: Middle East Economic Survey, Volume XLV No. 1

Table 4 2001 GCC Exporters' Average Oil Prices (estimates) US$/bbl

Country	2000	**2001**
Kuwait	25.90	**21.00**
Oman	26.70	**23.00**
Qatar	27.60	**23.85**
Saudi Arabia	26.81	**23.06**
United Arab Emirates	27.70	**23.30**

Source: Middle East Economic Survey based on actuals and/or estimates

throughout the GCC region in line with the rate cuts in the United States. Exchange rates have remained stable. There has been some deterioration in the value of the assets held by GCC governments and private investors abroad as a result of the sharp reduction in equity values in the US, Europe and Japan. However, since most of the equity investments abroad were made by high net worth individuals, the impact on consumer spending may have been insignificant.

GCC leaders have been aware of the dangers inherent in excessive dependence on oil exports and government spending for a very long time, and gradual efforts have been ongoing since the seventies to diversify the economy. In recent years, many government and business leaders have argued forcefully for a change in orientation, which would switch the emphasis from production of hydrocarbons, both oil and gas, for export purposes to exploitation of hydrocarbons, especially gas, for building industries domestically. The various projects that are currently under planning or in the implementation stage provide a testimony to the welcome change in philosophy. In addition to privatization and incentives to investment, other bold initiatives are being planned that would greatly encourage economic activity and bolster capital markets. The GCC leaders have announced in their summit in Oman in December 2001 that they have agreed to unify regional customs tariffs at 5% from January 1, 2003 and adopt a single currency before January 1, 2010. Regional as well as international trade would receive a strong stimulus from these actions. It is worthwhile looking at developments in GCC countries that illustrate a continuing reform agenda and a desire for economic liberalization.

Bahrain

Bahrain has been a pioneer in the Gulf in building a thriving financial services industry with the active participation of major multinational banking, insurance companies and brokerage houses. Lacking the hydrocarbon wealth of its neighbors, Bahrain is vigorously pushing its program to attract foreign investment and to open up its stock exchange for all investors. Financial services, tourism, light manufacturing and information technology are the sectors that will continue to be emphasized with a view to attract private investment. Bahrain now permits foreign companies engaged in trade, tourism, banking and financial services to own land and buildings required for business activity. In selected industries 100% foreign ownership is now permitted, and foreign investors can also hold up to 49% equity in listed companies. Additionally, Bahrain allows other GCC companies to list their shares on its stock exchange. The government has committed itself to providing a tax-free environment for both individuals and companies.

Earlier in 2001 the government created a new body, the Economic Development Board, to develop economic strategy and to attract private investment to the island. This was preceded by the establishment of the Higher Council for Economic Development to provide strategic direction to the economy and reinforce Bahrain's status as a regional services center. Some areas that require a special mention include the Islamic Banking sector. In just a few years, Bahrain has established itself as the global capital of interest-free Islamic Banking and now major banks like Citibank, Banque Nationale de Paris and the Arab Banking Corporation have established Islamic banking units. Islamic banks are now moving aggressively


Maintaining diversity in revenue sources

Table 5 OPEC Quotas During 2001 (in thousands)

Country	Effective as of January 1, 2002 New Production Level (b/d)	Decrease	Effective as of September 1, 2001 New Production Level (b/d)	Decrease	Effective as of April 1, 2001 New Production Level (b/d)	Decrease	Effective as of February 1, 2001 New Production Level (b/d)	Decrease
Algeria	**693**	**48**	741	32	773	32	805	48
Indonesia	**1,125**	**78**	1,203	52	1,255	52	1,307	78
Iran	**3,186**	**220**	3,406	146	3,552	146	3,698	219
Kuwait	**1,741**	**120**	1,861	80	1,941	80	2,021	120
Libya	**1,162**	**80**	1,242	54	1,296	45	1,350	81
Nigeria	**1,787**	**124**	1,911	82	1,993	82	2,075	123
Qatar	**562**	**39**	601	26	627	26	653	39
Saudi Arabia	**7,053**	**488**	7,541	324	7,865	324	8,189	486
UAE	**1,894**	**131**	2,025	88	2,113	88	2,201	132
Venezuela	**2,497**	**173**	2,670	116	2,786	116	2,902	174
Total	**21,701**	**1,500**	23,201	1,000	24,201	1,000	25,200	1,500

Source: www.opec.org

in the fields of private equity and mutual funds. Islamic banking complements offshore banking and conventional banking activities in Bahrain.

Aluminum Bahrain (ALBA) continues its activities in a profitable manner and is looking to further expansions. ALBA is among the largest aluminum producers in the world and has a production capacity of more than 500,000 tons of metal per year. Recently the government approved a $1.7 billion expansion that would enhance ALBA's capacity by an additional 50%. ALBA has also spurred the growth of a significant aluminum products industry in Bahrain.

Bahrain International Airport, home to Gulf Airways, continues its expansion programs and many landmark tourism projects are being implemented with the help of the private sector, one of them being the $800 million Durrat Al Bahrain resort. The decree of the International Court of Justice that awarded the Hawar Islands to Bahrain is expected to provide further stimulus to Bahrain's tourism industry which is mostly in the private sector domain.

Kuwait

Kuwait is one of the more prosperous countries in the Gulf and owes its prosperity to its extraordinary oil resources, for it has nearly 10% of the global resources with a small population base. Kuwait's economy still remains dominated by oil which accounts for over 90% of export earnings, 80% of budget revenues and over 40% of the GDP. Kuwait's policy makers have, therefore, embarked upon a structural reform program to reduce oil dependence, enhance the role of private sector, and encourage investment.

In March Kuwait's National Assembly approved the Foreign Direct Investment Law which provides for 100% direct ownership of a company by foreign investors, offers tax holidays and the establishment of an investment committee to expedite approvals and related administrative procedures. The Law is expected to be issued by the Amir in the near future with the necessary executive rules and regulations detailing its implementation. The banking sector is also expected to be opened up for outside participation, and a draft law has been approved by the government which will allow other GCC banks to operate in Kuwait. A draft law has also been approved to lower taxes on foreign companies to 25% from the current maximum of 55%. A draft law to permit portfolio investment has already been passed and it awaits the executive regulations detailing its implementation.

There are other interesting developments that merit a mention. Kuwait has signed a memorandum of understanding with Qatar under which one billion cubic feet a day of gas would be supplied to Kuwait from Qatar's enhanced gas utilization project. Discussions between Kuwait and Qatar are expected to commence soon on the proposed

Table 6 Gross Domestic Product for GCC Economies at current prices (US$ billion)

	1997		1998		1999		2000		**2001e**	
	Amount	Change	Amount	Change	Amount	Change	Amount	Change	**Amount**	**Change**
Bahrain	6.3	3.3%	6.2	-1.6%	6.6	6.5%	8.0	21.2%	**n/a**	**-**
Kuwait	30.2	-1.6%	25.4	-15.9%	29.8	17.3%	35.8	33.7%	**32.8**	**-8.5%**
Oman	15.8	3.3%	14.1	-10.8%	15.7	11.3%	19.8	26.1%	**20.3**	**2.5%**
Qatar	11.3	24.2%	10.3	-8.8%	12.2	18.4%	16.5	35.2%	**16.2**	**-1.8%**
Saudi Arabia	146.5	3.7%	128.4	-12.4%	139.4	8.6%	173.0	24.1%	**170.0**	**-1.7%**
United Arab Emirates	50.2	4.8%	47.2	-6.0%	54.7	15.9%	70.5	28.9%	**67.8**	**-3.8%**

e: Estimates (as reported by GCC Central Banks and Ministries of Finance/Planning sources)
Source: GCC Central Banks Publications

plan to build a 590-kilometer sub-sea pipeline. Kuwait's hydrocarbon resources are skewed towards oil, and gas is generally produced only as an associated by-product of extraction. Kuwait needs more gas for power generation and as feedstock for its petrochemicals investment plan. After successfully building a large and modern ethylene cracker in 1997, Kuwait has approved the construction of two massive petrochemical units. One will be a $2 billion olefins plant and the second a $1.4 billion aromatics plant; some of the gas will be used as a feedstock in the olefins unit. Kuwait is also likely to explore for gas in the Dorra field that it shares with Saudi Arabia in the Neutral Zone. Kuwait Oil Company plans to spend $3 billion on exploration activities in the Neutral Zone over the next five years.

Kuwait wants to modernize and expand its oil business and expects foreign technology and investment to play a meaningful role. In April 2000, the cabinet approved Project Kuwait which would involve international oil companies in the development of four oilfields in the north and two oilfields in the West. International oil companies are expected to invest around $7 billion under the proposed oil service agreements. Kuwait Petroleum Corporation has shortlisted nine IOCs for the role of operator and fifteen others have been prequalified to provide support services. Kuwait expects to raise its production capacity to 3 mm b/d by 2005 and 3.5 mm b/d by 2010. The National Assembly wants to introduce certain safeguards and involve itself in the approval process. The Supreme Petroleum Council and the Government must work with the National Assembly to implement Project Kuwait as it has become known. The Government remains confident that progress will be made during 2002.

Kuwait's privatization program is comprehensive and is expected to include the partial or total sale of Kuwait Airways, Petrochemicals Industries Company, Kuwait Oil Tankers Company and its stake in the Mobile Telecommunications Company. However, the discussions in the National Assembly indicated that further refinements were needed for the privatization law to be passed.

The inflow of UN compensation for the damage caused by the Iraqi occupation continued through 2001 and nearly $3 billion was received by Kuwaiti applicants (individuals and companies). Kuwaiti listed companies received $197.5 million during the year in addition to $90 million that was received in 2000. Since 1998, $6.3 billion in compensation has been paid to Kuwaiti companies and individuals altogether. The added liquidity is expected to boost aggregate demand and provide a boost to the economy. Some analysts consider the excellent performance of the Kuwait Stock Exchange in 2001 (up 26.8%), to be partly explained by the added liquidity and the impact on profitability of Kuwaiti companies receiving UN compensation payments.

Oman

Oman is another GCC country which has a relatively modest hydrocarbon wealth but has remained in the forefront of the reform drive. Oman was the first country in the Middle East to pioneer the independent power project concept when it successfully built the Al Manah power station in 1996. In 2001 Oman further expanded the scope of the private sector when final agreements were signed with the Dhofar Power Company (DPC) for the Salalah power project. A 20-year concession agreement grants DPC responsibility over the entire Salalah system. It will not only build a new 200 MW power station and upgrade the existing transmission system, but will also own and operate the transmission and distribution network along with responsibility for billing. This is the first privatization of a vertically integrated utility in the region. DPC has committed itself to investing $270 million in acquiring and expanding the existing power system. This is yet another pioneering feat on the part of Oman in the critical power sector in the Gulf, which is expected to be the focus of privatization and restructuring activity. Dhofar Power Company is 81% owned by the American PSEG Global. Oman is now working on new legislation that is expected to establish the framework for a comprehensive privatization of the electricity sector including creation of a regulatory body. Three existing power plants are to be sold off in the near future. Additionally, Oman is pressing ahead with plans to privatize its two large commercial airports at Seeb and Dhofar. Salalah port is already being operated by the private sector.

The Muscat Securities Market was among the first exchanges in the region to open up for foreign investors and the establishment of well-defined regulatory authority. Oman now permits foreigners to own up to 70% of the shares of companies listed on its exchange. Oman has revised its tax code and has aggressively lowered tax rates on companies with significant foreign holding to the same level as Omani owned companies.

Petroleum Development Oman continues with its Enhanced Oil Recovery (EOR) program and is investing over $200 million in a steam injection project. Fifteen international contractors have applied to pre-qualify. Oman is also likely to proceed with building a 750,000 b/d refinery at Sohar and five foreign contractors have been invited to submit proposals. Oman has remained in the forefront with respect to natural gas development. It developed the two train 6.6 million tons a year LNG project in near record time with foreign equity participation using the best available technology. Oman is also considering adding a third train which would enhance its LNG capacity to nearly 10 million tons. Oman is taking new initiatives in developing its gas reserves and expects to add another 10 trillion cubic feet to its reserves in the near future, raising gas reserves to 40 trillion cubic feet. Petroleum Development Oman has recently made two more promising gas discoveries.

The cornerstone of the diversification strategy is to establish large gas based industries with foreign and private participation and with the help of modern technology. The implementation of a giant fertilizer plant at Sur with Indian partners involving an outlay of nearly $1 billion is expected to commence in the near future. This plant will produce urea and ammonia for export to India. A methanol plant and a massive aluminum smelter is under consideration by the government. Some of the needed gas is likely to be provided by Qatar via a proposed pipeline project.

Qatar

Qatar is a small country in terms of population but its massive natural gas resources and their rapid development have granted it a very special status among the world's energy exporters. Whereas Qatar does produce and export nearly 700,000 barrels of oil per day, its hydrocarbon wealth stems from the great offshore gas reserves at North Field. The North Field was discovered in 1971 and is believed to be the largest known non-associated gas field outside the former Soviet Union. Qatar's proved reserves estimates are rapidly increasing as more definitive studies become available and currently stand at nearly 400 trillion cubic feet or a little over 7% of the global reserves.

It is obvious that Qatar's development plans would revolve around aggressive exploitation of its gas reserves. Qatar has made great achievements here with the active participation of foreign capital and technology provided by world-class multinationals. Qatar undertook its LNG program by investing over $10 billion in two large projects in which leading American, European and Japanese corporations have been involved in all aspects including equity participation and technology transfer. Both projects are currently profitable and produce over 14 million tons of LNG for export. Current expansion plans would more than double the capacity to 30 million tons or equivalent of nearly 712,000 b/d of oil by 2006, making Qatar one of the undisputed leaders in global LNG trade.

Table 7 Real GDP percentage Change in GCC Economies*

	Average 1984-93	1997	1998	1999	**2000**	**2001****
Bahrain	4.1	3.1	4.8	4.3	5.3	**3.3**
Kuwait	1.5	2.3	3.7	-1.7	1.7	**2.7**
Oman	6.3	6.2	2.7	-1.0	4.9	**6.5**
Qatar	0.7	25.4	6.2	5.3	11.6	**7.2**
Saudi Arabia	2.6	2.0	1.7	-0.8	4.5	**2.2**
United Arab Emirates	2.0	6.7	4.3	3.9	5.0	**5.0**

* Source: International Monetary Fund, World Economic Outlook - April 2002

** The reader should note that IMF staff estimates for **real GDP** are based on data supplied by the national authorities of the countries concerned. The figures for **nominal GDP** (Table 6) are taken also from official government sources. The reader should evaluate each set of figures accordingly

Rapid strides have been made in building the petrochemicals industry with comprehensive foreign participation which commenced production in 1980 with its first ethylene cracker. Today it produces a variety of products including MTBE, methanol and ethylene dichloride in addition to ethylene and polyethylene. Current plans include building a second ethylene complex at Mesaieed which would triple existing capacity with likely participation from existing foreign shareholders.

Qatar has a very ambitious gas development program that far transcends LNG export and petrochemicals manufacture. In co-operation with other GCC states including the UAE, Oman, Kuwait and Bahrain, Qatar is making rapid headway in joint projects that would commence the construction of gas pipelines that would cross international boundaries within the GCC and may eventually be extended to the Indian sub-continent. The Dolphin Project is the most advanced of the cross-border projects. The Dolphin Energy Limited, in which the UAE Offsets Group holds a 75.5% interest, has completed negotiations with Qatar Petroleum on a development and production sharing agreement of Qatari natural gas. The gas will be transported by a pipeline to Abu Dhabi, and from there to Dubai and Oman and eventually to Pakistan. When completed the pipeline will carry 2 billion cubic feet of gas per day. The front-end engineering and design contract was awarded in December. Additionally, Qatar is involved in discussions to provide gas to Kuwait as well as Bahrain in a separate project. In yet another development, Qatar may soon commence work on a large gas to liquids plant (GTL) which would convert gas to middle distillates. Bidding is expected to begin shortly on a $1 billion plant planned by Qatar Petroleum in partnership with South Africa's Sasol. The gas requirements will be provided by the enhanced gas utilization project, a joint venture to be set up between Qatar Petroleum and Exxon Mobil. Qatari gas developments are of significance to the entire GCC as regional use of its gas

Table 8 Consumer Price Index (Y/Y % Change)

	1997	1998	1999	2000	**2001e**
Bahrain	2.0	-1.0	-2.0	-0.7	**-1.2**
Kuwait	0.7	0.2	3.0	1.8	**0**
Oman	0.0	-0.5	1.0	-1.0	**-1.0**
Qatar	2.6	2.9	2.2	1.7	**-1.5**
Saudi Arabia	-0.4	-0.2	-1.3	-0.6	**-0.8**
United Arab Emirates	2.3	1.6	2.1	1.4	**1.2**

e: Estimates
Source: Official Sources

Table 9 GCC Trade & Current Account Balances (US$ million)

		1996	1997	1998	1999	2000*
Bahrain	Trade Balance	665	605	(29)	672	1,327
	Current Account	261	(31)	(778)	(340)	113
Kuwait	Trade Balance	6,997	6,530	1,903	5,571	12,730
	Current Account	7,107	7,931	2,215	5,062	14,865
Oman	Trade Balance	2,954	2,982	291	2,918	6,726
	Current Account	180	(40)	(2,971)	(192)	3,334
Qatar	Trade Balance	1,249	863	1,960	4,962	8,664
	Current Account	(1,246)	(1,679)	(455)	2,171	5,418
Saudi Arabia	Trade Balance	35,370	34,362	11,287	25,039	51,176
	Current Account	681	305	(13,150)	412	15,567
UAE	Trade Balance	7,760	7,399	550	4,754	12,722
	Current Account	6,650	6,310	(1,114)	3,488	11,594
Total GCC	Trade Balance	54,995	52,741	15,963	43,916	93,345
	Current Account	13,633	12,796	(16,253)	10,601	50,891

* Preliminary
Source: IMF; IFS, Central Bank of UAE and Qatar Central Bank

resources will spur domestic industry in other GCC states that would receive Qatar gas under planned pipelines. These pipelines would eventually lead to a GCC gas grid. The privatization program remains active. During the year, the Ras Laffan Electricity Company was established which will build and operate its first independent power and water plant in cooperation with AES of the US who is also a shareholder in the company. GIC is an equity holder in that company.

Saudi Arabia
Saudi Arabia's importance to GCC economies, or for that matter the whole world, cannot be overstated. Saudi Arabia's proved oil reserves exceed 260 billion barrels and amount to 26% of the global oil reserves. It is also endowed with significant gas reserves. Saudi Arabia is the single largest exporter of oil in the world and should remain so for the near future.

Saudi Arabia's achievements in non-oil sectors are also noteworthy. For a long time Saudi Arabia has successfully employed the strategy of gas utilization to develop its domestic industrial base. The petrochemicals industry is among the largest in the world and SABIC, a state controlled corporation, has rapidly become a global company with a string of subsidiaries with foreign partners. The eastern city of Jubail and its eastern provinces are powered by gas generators.

Saudi Arabia's natural gas initiative, as it is known, is thus of a very great significance, and has wide ranging implications for the entire region. The country undertook a massive expansion of its master gas system a few years ago but obviously intends to do more in this regard. In a bold and far-reaching step, in 1999, it invited IOCs to participate in the development of its entire gas sector. The initiative is a comprehensive plan which involves exploration of gas, the production, gathering and distribution of gas, the generation of electricity and water and the manufacture of petrochemicals for local and international markets.

Saudi Arabia expects that as a by-product of the gas initiative, its gas reserves would increase

Table 10 GCC Government Revenues & Expenditures (US$ million)

	1998			1999			2000			**2001 Budget**		
	Revenues	Expenditures	Deficit/ Surplus	Revenues	Expenditures	Deficit/ Surplus	Revenues	Expenditures	Deficit/ Surplus	**Revenues**	**Expenditures**	**Deficit/ Surplus**
Bahrain	1,473	1,874	(400)	1,756	1,925	(169)	2,785	2,771	14	**1,779**	**2,189**	**(410)**
Kuwait	9,182	13,260	(4,078)	17,212	13,169	4,043	16,190	10,395	5,795	**12,480**	**17,179**	**(4,699)**
Oman	4,802	5,778	(976)	4,677	5,888	(1,211)	5,955	6,908	(953)	**6,489**	**7,313**	**(824)**
Qatar	4,181(a)	4,642	(461)	4,196	4,775	(579)	6,399	5,191	1,208	**4,961**	**4,824**	**137**
Saudi Arabia	37,810	50,750	(12,940)	39,385	49,079	(9,694)	68,892	62,830	6,062	**57,410**	**57,410**	**0**
UAE(b)	5,349	5,828	(479)	5,220	5,900	(680)	5,631	6,295	(664)	**5,562**	**6,170**	**(608)**
Total GCC	62,797	82,131	(19,334)	72,446	80,736	(8,290)	105,852	94,390	11,462	**88,681**	**95,085**	**(6,404)**

(a) Includes US$ 650 million from the government sale of a 45% stake in Qatar Telecom
(b) Federal budget
Source: Official sources

substantially along with increased exports of natural gas liquids. The involvement of IOCs underscores the region's commitment to open its boundaries for more foreign investment in sectors of vital importance. Events have moved with remarkable speed and preliminary agreements have been signed to cover three core ventures. They cover gas development in three key geographical areas i.e. South Ghawar Area, Red Sea Area and Shaybah area with total future investment of around $25 billion. Eight IOCs have been included in the deal as three separate teams. These projects constitute the first major reopening of the Saudi petroleum sector to foreign companies since nationalization. During 2002, further negotiations are to take place prior to signing final Execution Agreements. Issues of projects IRRs and returns on IOCs investments are still under consideration.

Saudi Arabia needs more gas urgently to meet growing demand for electricity, which is estimated to increase by 5.5% per year in addition to meeting feedstock requirement for the petrochemicals industry. The government has shown enthusiasm for the participation of the private sector in the power and water generating industries as well. By 2020 investment requirements for these sectors are expected to top US$ 140,700 billion.* This will require not only the involvement of the domestic private sector but foreign investment as well along with technology transfer. The Council of Ministers has also approved the establishment of a new and separate ministry to manage water resources.

The restructuring of the power sector continues. The Saudi Electricity Company, which was incorporated two years ago by absorbing regional utilities, is drafting a master plan for the whole sector. Saudi Arabia is in the process of establishing a regulatory body for the power sector. It will be a fully autonomous entity with its own legal status and financial independence. This will be an important step in the reform process of the power sector. The regulatory authority will have a 12-member board and will be managed by a governor. It will be responsible for reviewing costs and tariffs of the power sector with a view to ensure a reliable and quality supply of power at reasonable rates. It will also have the power to issue licenses for new projects. It will generate cash flows in the form of remuneration for services provided to companies working in the sector and from penalties imposed on companies that fail to meet standards established by service providers including generators, transmission companies and distributors. In the meanwhile, one of the SABIC entities, Sadaf Petrochemicals, is moving forward with the first IPP in Saudi Arabia by building a 240 MW captive power plant, another SABIC subsidiary is considering a 1000 MW plant.

The reform process has permeated every significant aspect of commercial legislation. In November a new regulatory body was created to run industrial cities and technology parks. The Minister of Finance revealed in May that the Supreme Economic Council was discussing a draft law to regulate the Saudi capital market and to establish a Securities Commission to act

* Meed 22, March 2002

Table 11 GCC Stock Markets Price Indices (Y/Y % Change)

	1996	1997	1998	1999	2000	**2001**
Bahrain (BSE)	16.6	49.3	-5.3	1.1	-18.4	**-2.5**
Kuwait (KSE)	39.1	39.2	-40.3	-8.9	-6.5	**26.8**
Oman (MSN)	26.1	141.1	-52.5	9.5	-19.6	**-24.4**
Qatar (DSM)	11.4	33.8	35.1	-0.4	-8.0	**37.2**
Saudi Arabia (TASI)	11.9	27.9	-27.8	43.6	11.3	**7.8**
UAE (NBAD)	15.3	32.5	9.4	-17.9	-18.3	**23.6**

Source: Official Sources

as independent regulator. This will promote the development of an active corporate bond market and spur stock market activities. The Saudi Arabian General Investment Authority (SAGIA), created by law in April 2000, continues to make progress in attracting foreign investment and has awarded licenses for projects with projected investments exceeding $10 billion. It is also taking steps to reduce the scope of the negative list of projects not permitted for full foreign ownership.

Privatization of some state owned and state controlled corporations such as SABIC, Saudia and STC is being studied.

United Arab Emirates

The UAE in many ways presents a unique situation in the Gulf. It is a federation of seven states, enjoys large oil and gas reserves, which are mostly concentrated in the Emirate of Abu Dhabi; it has a vibrant international city in Dubai, which excels in tourism, retail business and financial services. Other Emirates, although smaller, are trying hard to attract industry, business as well as tourism. With its practical approach and dynamism, the UAE is among the richest states in the Middle East.

It was the Emirate of Abu Dhabi that first commenced the gas export business from the Gulf when the ADGAS LNG project was commissioned in the seventies. ADGAS has undergone improvements and expansions and further capacity increases are planned. In the gas sector, however, the UAE is attracting attention for yet another first, namely the first cross-border gas pipeline that is moving closer to implementation. The UAE Offsets Group, owned by the Abu Dhabi government and which helps foreign defense contractors find investment opportunities, has signed a groundbreaking $3.5 billion deal with Qatar to receive up to 2 billion cubic feet of gas per day which will be supplied by a sub-sea pipeline from Qatar's prolific North Field and dedicated processing plants to Abu Dhabi and then on to final buyers, which include Dubai, Oman, and possibly Pakistan

Table 12 GCC Stock Markets Capitalization (year-end)

	1996		1997		1998		1999		2000		**2001**	
	$bn	% of GDP	$bn	% of GDP	$bn	% of GDP	$bn	% of GDP	$bn	% of GDP	**$bn**	**% of GDP**
Bahrain (BSE)	5.1	83.6	7.7	122.2	6.8	102.7	7.2	109.1	6.6	88.0	**6.6**	**n/a**
Kuwait (KSE)	21.9	71.4	29.8	98.7	18.9	75.1	19.6	66.0	19.4	54.2	**24.3**	**74.1**
Oman (MSN)	4.2	27.5	8.8	55.8	5.9	41.8	5.9	37.8	3.5	20.2	**4.5**	**22.2**
Qatar (DSM) (a)	2.1	23.2	2.6	23.0	5.4	52.4	5.5	45.1	5.2	36.4	**7.3**	**45.1**
Saudi Arabia (TASI)	45.9	32.5	59.5	40.6	42.7	33.3	61.1	43.8	68.0	41.2	**73.3**	**43.1**
UAE (NBAD) (b)	13.5	28.2	21.0	41.8	26.2	55.5	26.8	49.0	21.9	31.1	**27.8**	**41.0**

(a) Official market started on May 26, 1997

(b) Dubai's official market started on March 26, 2000 & Abu Dhabi's official market started on November 15, 2000

Source: Official Sources

at a later stage. Gas demand in the UAE has virtually doubled in the past five years and could double further in the next five years. Dolphin is thus critical to UAE's Northern Emirates, especially Dubai which has limited gas resources and a thriving economy. In addition to Dolphin, the UAE's petroleum industry, which includes foreign partners, is investing massive funds in onshore gas development, natural gas liquids production and refinery projects. One of the main reasons behind the galloping gas demand in the UAE is the surging power demand which is rising at nearly 10% a year. Both consumer demand and industrial demand are soaring as elsewhere in the Gulf countries. Water demand is also rising in tandem. The power sector's investment needs in the GCC region are great; they exceed $100 billion for the next ten years alone.

The power sector has thus rightly become a principal focus for privatization and for attracting foreign investment. Private power has proved its case for higher efficiency with successful IPPs. Abu Dhabi made a bold beginning by establishing the Abu Dhabi Water and Electricity Authority (ADWEA) in 1998. Events have moved with remarkable speed since. Within six months ADWEA offered a 40% stake to an American company to run the country's first IPP, the existing Taweelah A2 project. The second IPP was awarded in 2000 to a French-Belgian alliance to refurbish and expand another existing unit. The third is the massive Shuweihat project which involves building a 5000 MW and 3000 million gallons a day plant in phases. The first phase, which would involve building about a third of the project at a cost of $2 billion, has started. Plans for Abu Dhabi's fourth IPP at Umm Al Nar are now underway. It is estimated that UAE's power needs could just about double by 2010 which graphically illustrates the potential for the private sector to participate in this vital business in the UAE as elsewhere in the GCC. Obviously, such huge investments could not be met by budgetary allocations.

Growing heavy industry including aluminum smelting and petrochemicals is among the drivers of power demand. Dubai has successfully built its aluminum industry behind Dubal, a giant public sector undertaking that compares in size with Bahrain's ALBA. Both are planning further large-scale expansions that would cost billions of dollars. The UAE, which was a little slow in making downstream hydrocarbon investments, is rapidly catching up in the areas of refining and petrochemicals. During 2001 it built its first world-class ethylene-polyethylene plant with the participation of a Scandinavian company. Another joint stock company has been established to invest in more downstream petrochemicals plant with participation from private and foreign investors.

One reason behind UAE's dynamic growth has been the quality infrastructure services offered. The Dubai Port Authority intends to undertake further expansion programs at its sea-ports and the airport at Dubai. Similar expansion plans are ongoing at the Abu Dhabi Airport as well. Emirates Airlines, which has won numerous Best Airline awards, continues its extraordinary expansion plans. It recently announced a $15 billion aircraft purchase deal, equal to Dubai's GDP, that would include planes from both Boeing and Airbus. It is noteworthy that Emirates will be the launch airline for the Airbus A380 double-decker jumbo jet. Emirates is planning to expand its fleet from 36 planes to around 100 by 2010, partly financed by the successful bond issue worth $400 million in the Dubai Financial Market. Dubai is also vigorously continuing its program to maintain its status as a regional tourism and retailing center. One of the more notable projects is the prestigious Palm Island project that would build artificial islands and resorts at a cost of $3 billion, which is considered the largest such project in the region. Real estate leasing rules are being aggressively liberalized in Dubai. The government of Dubai has approved partial foreign ownership of real estate on 99-year lease basis. This law encourages foreign investors as it applies to non-resident investors.

Our financial goal

To maximize long-term shareholder value through consistently superior financial performance while maintaining strong financial condition.

Our financial performance objective

To consistently achieve target earnings growth and return on equity, with an appropriate dividend payout.

Our financial condition objective

To efficiently manage the various forms of risks associated with our business and maintain strong asset quality, capital base and liquidity.

Net Income Analysis

For the Gulf Investment Corporation, 2001 was an eventful year, with significant changes in operating activities and organization structure. The sale of Gulf International Bank (GIB), the principal subsidiary in which the Corporation had a 72.45% ownership, was successfully concluded during the year. Additionally, as a part of the new strategic initiative, business structures were realigned and support functions consolidated. Despite these events, the core businesses within GIC achieved excellent results, exceeding 2001 targets and previous year performances.

Gulf Investment Corporation's consolidated net income for 2001, at US$ 85.3 million, represented a return on equity of 8.3%. On a comparative basis, the net income for the previous year was US$ 111.7 million. The year-on-year decline can be attributed primarily to the sale of GIB and subsequent reduction in earnings from this discontinued activity. Another factor that adversely impacted earnings was the US$ 303.2 million reduction in the capital base, which was utilized by GIC's shareholders towards partial settlement of GIB sale proceeds. The loss in earnings from the divestiture was, however, partially offset by the approximate 125% increase in net contributions from GIC's own global markets and project investment activities.

Net Interest and Similar Income

The Corporation's interest and similar income for the year, at US$ 272.7 million, was almost 13% higher than the US$ 242.2 million earned in 2000. This increase, coupled with a lower interest expense for the year, resulted in the more than sevenfold increase in net interest income.

The principal contributor to the interest income category was the investment securities portfolio. This was supplemented by proceeds from loans and credit funds, earnings on the outstanding receivable from shareholders, and income from the money book.

Average net spreads within the investment securities portfolio more than doubled relative to prior year levels. The strategy to build up and actively manage this portfolio over the past years was rewarded during 2001, given the favorable interest rate environment. Most of the increase was derived from higher net spreads, the increase in volumes within this portfolio being insignificant.

Another factor contributing towards the increase in interest income was the approximate 4.3% return earned on the outstanding due from shareholders, following the sale of GIB. Details of this transaction are provided in notes 4 and 9 of the financial statements.

Following the strategic decision to reduce the loan portfolio, volumes during 2001 were approximately 23% lower than the previous year, on average. This resulted in lower earnings, although net spreads increased. The credit funds portfolio, yielding higher spreads, is being gradually expanded as a substitute for the loan portfolio.

The Corporation's interest rate sensitivity gap is set out in Note 23 to the Financial Statements. Exposure to interest rate risk is restricted due to the limited mismatch between the repricing of a majority of the Corporation's assets and liabilities.


Well positioned to take advantage of the accelerated pace of privatizations within the GCC

Other Operating Income
Other operating income rose to US$ 51.7 million during the year under review, an increase of over 15% relative to the US$ 44.7 million achieved in 2000. In addition to higher returns from the projects and equity participations activity, realization of gains on the sale of securities available for sale contributed to the increase. A detailed breakdown is available in Note 18 to the Financial Statements. The key constituents of other operating income are discussed below.

Net gain on trading securities decreased to US$ 10.0 million from US$ 12.2 million in the previous year. As a consequence of the management decision to exit all international equity exposures, the adverse impact of the downturn in global equity markets was minimized. Early in the third quarter of 2001, equity trading was curtailed while investments in market-neutral strategies were increased. Despite this prudent move, losses incurred during the first half of the year negatively impacted trading income.

Gain on available-for-sale securities totaled US$ 5.9 million during the year, largely generated on the sale of debt securities within the investment portfolio. Besides a favorable interest rate environment, the superior quality of holdings enhanced the market value of securities, contributing to higher profits.

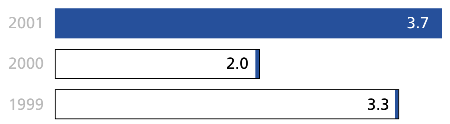
The US$ 8.6 million generated from the investments in equity funds was almost 41% higher than that of 2000. Given the lackluster performance of the global private equity sector, the performance of this portfolio is commendable and can be attributed largely to the fund selection process, level of diversification maintained, and phased investment in past years.

The projects and equity participations business sustained the growth in earnings, with a 36% increase in revenues over prior year. Income from this activity climbed to US$ 19.1 million for the year under review, representing GIC's share of profits from unconsolidated subsidiary and associated companies. In addition to the US$ 19.1 million, profits of US$ 0.4 million were realized on the sale of certain project investments. The principal investing team continuously interacts with the business sector in the region, enabling us to have first hand knowledge and take advantage of opportunities as they appear. This dynamic and flexible approach, together with a policy of adherence to strict financial and business discipline while evaluating and managing project investments, has led to sound performance of this business. It should be noted that many of the project participations are grass root in nature and still in their gestation periods. Earnings from such participations are expected to grow with the maturing of these projects.

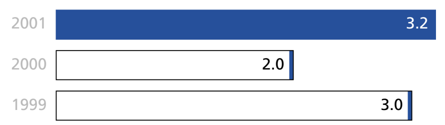
Dividend income of US$ 5.5 million is composed of receipts from holdings within private equity participations, equity portfolios and project investments.

For the year, fees, commissions and sundry income totaled US$ 2.3 million compared to US$ 2.6 million in 2000. The Corporation is committed to expanding its sources of revenue from fee based businesses. In this regard, two key units have been established – Financial Advisory and Marketing. The financial advisory service is well positioned to take advantage of the accelerated pace of privatizations within the GCC states and renewed interest in corporatizing the operations of family-owned companies.

Operating Income as a Multiple of Operating Expenses



Net Revenue as a Multiple of Operating Expenses



The marketing team aims to deliver a range of financial products available in the international markets, to a regional clientele, in addition to the sale of internally developed GCC investment products to clients in and outside the region.

Operating Expenses

Management of expenses remains a priority for the Corporation. We continue to maintain a sharp focus and discipline in our spending. Staff costs, the major component of operating expenses, is expected to decrease further in the coming years, following the restructuring completed during 2001 as a result of which staff levels were reduced by approximately 12%. Additionally, the management of non-capital resources, including personnel and technology, have been grouped within a shared services function, enhancing efficiency and control.

While operating income almost doubled, related expenses increased by a mere 3% over prior year. Productivity, expressed in terms of total operating income as a multiple of operating expenses, improved to 3.7 in 2001 from 2.0 in 2000. Net revenue, after reducing loss provisions for the year, as a multiple of operating expenses also increased to 3.2 in 2001 from 2.0 in the previous year. Amortization of goodwill, excluded from the operating expenses aggregate in computing the ratios mentioned above, was marginal. Inclusion of these expenses will not have a material impact on the above ratios.

Operating expenses are made up of employee compensation and benefits, occupancy, information technology, and other expenses. Staff costs include incentive compensation, which varies in accordance with individual as well as Corporate performance. Information technology costs include expenditure relating to ongoing enhancement of computer systems.

Provisions for Credit Losses

We maintain provisions to absorb losses inherent in our traditional extensions of credit that we believe are probable and that can be reasonably estimated. Given the varied nature of businesses, these may arise from our lending, treasury and investment activities. Estimating losses is inherently uncertain and depends on many factors, including general macroeconomic and political conditions, rating migration, risk concentrations, structural changes within industries, and other external factors such as legal and regulatory requirements. The Corporation periodically reviews such factors and reassesses the adequacy of the provisions.

Net charge for the year in provisions for credit losses amounted to US$ 13.8 million compared to a write back of US$ 1.0 million during 2000. The majority of provisions for the year related to potential losses within the private equity funds portfolio and the investments in regional project ventures.

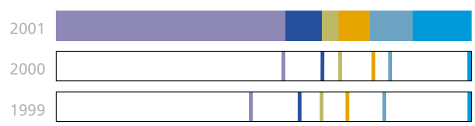
Discontinued Operations

Following finalization of the transaction relating to the sale of Gulf International Bank to the shareholders during the Board of Directors meeting held on October 13, 2001, the Board approved GIC's share of net income earned by GIB for the period from January 1, 2001 to April 30, 2001 to be added to GIC's net income for the year. In the year 2000, contributions from GIB totaled US$ 85.6 million. Details of this transaction are provided in Note 4 of the financial statements.

Balance Sheet Analysis

Recognizing the diverging strategic objectives of the two entities, the Board made the decision to establish GIC and GIB as two distinct institutions with separate missions. Over the past 11 years, under the ownership of GIC, GIB has grown in scope and scale and constituted a major portion

Asset Mix by Category (Continuing Operations)



	2001	2000	1999
Investment Securities	55.1	54.4	46.7
Loans & Credit Funds	8.8	9.7	12.0
Trading Securities & Managed Funds	4.0	4.3	5.2
Project Participations & Equity Funds	7.6	7.8	6.2
Placements & Other Interest Bearing Assets	10.3	4.3	9.1
Other Asset Categories	14.2	19.5	20.8

of GIC activities. At the end of 2000, GIB's share of total assets reached US$ 14,111.5 million or 72% of the consolidated assets of the Corporation. Subsequent to the sale, the Corporation's total asset base reduced to US$ 5,541 million at the end of 2001 from US$ 19,602.8 million at year end 2000. On a stand-alone basis, excluding the discontinued activity, GIC's overall assets grew by a moderate US$ 50 million or 1% year-on-year. During the second half of 2001, GIC developed a strategy of planned expansion, effectively leveraging its core competencies. In the short to medium term GIC will seek opportunities to build the balance sheet, commensurate with its capital base and in line with the desired risk profile.

The Corporation's strategic focus continues to be on the GCC states and their major trading partners in the industrialized world. Note 26 to the Financial Statements sets out the geographic distribution of the Corporation's assets.

The following sections provide details on the key asset categories within GIC's continuing operations.

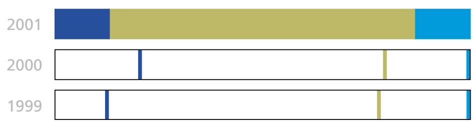
Investment Securities
Focusing on the Corporation's continuing operations, investment securities remained the principal asset category, comprising 55% of overall assets at end of 2001. The investment securities portfolio is composed mostly of investment grade marketable debt securities. The objectives of this portfolio include the provision of stable coupon/spread income, risk diversification, provision of a loan substitute and a reserve of additional liquidity. Investments in equities, at US$ 13.6 million, form less than 0.5% of this portfolio.

Investment securities totaled US$ 3,055.6 million at December 31, 2001 as against US$ 2,986.3 million at end of 2000. The investment securities portfolio includes securities available for sale of US$ 1,930.6 million and securities held to maturity of US$ 1,125.0 million. The held to maturity portfolios, carried at amortized cost, had a market value of US$ 1,134.5 million at year end 2001, reflecting an unrealized gain of US$ 9.5 million. The available for sale securities are carried at market value. In line with the new accounting standards, approximately US$ 30.0 million in net unrealized gains, relating to available for sale investment securities have been included in shareholders' equity. The significant increase in market value is indicative of the superior quality holdings within the portfolio. A credit risk analysis of the investment securities portfolio is provided in the risk management section on page 38 and other details, including ratings profile, are contained in Note 7 to the Financial Statements.

Loans and Credit Funds
This category includes loans and advances of US$ 245.8 million and investments in credit funds of US$ 242.1 million. In line with the new strategic focus, management decided to reduce exposures within the loan book, resulting in approximately 30% reduction in outstanding loans compared to prior year end. Investments in credit funds increased by 33% year-on-year, reflecting renewed emphasis in such investment vehicles. Credit funds, yielding higher spreads vis-à-vis GIC's loan portfolio, primarily consist of exposures rated better than investment grade, and are managed by experienced international fund managers. As of 31 December 2001, loans and advances were entirely to customers within the GCC countries, of which just under 50% were to GCC country governments. There were no significant concentrations by industrial sector at the year end. Investments in credit funds were distributed among several managers within North America.

Based on contractual maturities at the balance sheet date, over 86% of the outstanding loans

Loan Maturity Profile



	2001	2000	1999
Within 1 year	13.1	20.2	12.4
1 to 5 years	73.5	59.2	65.6
Over 5 years	13.4	20.6	22.0

and investments in credit funds was due to mature within five years, with 13% due to mature within one year. Details of the maturity profile are given in Note 22 to the Financial Statements and other details including loss provisions made are contained in Note 8.

Total loan loss provisions including loan guarantees amounted to US$ 8.1 million at December 31, 2000. Counterparty specific provisions amounted to US$ 4.8 million while general provisions were US$ 3.3 million. The entire US$ 4.8 million specific provisions were made against loans, guarantees and related exposures pertaining to project investments. Specific provisions for loans are made to the full extent of the estimated potential loss while general provisions are maintained to cover possible future losses which as yet have not been specifically identified. It is the Corporation's policy to write off loans after all reasonable restructuring and collection activities have taken place and the possibility of further recovery is considered to be remote. As of December 31, 2001, there were no non performing syndicated loans within GIC's loan book.

Trading Securities and Managed Funds
The trading securities and managed funds portfolio of US$ 220.6 million at December 31, 2001 is made up of externally managed funds totaling US$ 214.9 million and a proprietary equity trading portfolio of US$ 5.7 million. The externally managed funds are principally invested in market-neutral and alternative investment strategies, well diversified in terms of manager and strategy. The 15% year-on-year increase in such investments reflect the continued shift away from exposures sensitive to market fluctuations. GIC, in association with internationally reputed managers, have introduced similar alternative strategy investment themes for regional customers. During the past two years, the increase in client funds under management to US$ 150 million is indicative of the success GIC has had with alternative investment approaches.

The proprietary equity trading desk focuses on the GCC region and at the end of 2001 the entire US$ 5.6 million represented GCC exposures. GIC is committed to the gradual expansion of this portfolio, taking advantage of its unique knowledge of the region. Details of the Corporation's trading portfolio are given in Note 6 to the Financial Statements. Trading securities and managed funds are accounted for at market value.

Placements and Other Interest Bearing Assets
Placements totaled US$ 390.7 million at the 2001 year end. Reciprocity is a key feature of our placement policy. Notes 22 and 26 to the Financial Statements provide the maturity profile and geographic distribution of placements, respectively. The entire US$ 390.7 million had a maturity within three months. Only 9.0% of total placements were with non-bank financial institutions. Other liquid assets including securities purchased under resale agreements, cash and bank balances amounted to US$ 179.4 million at December 31, 2001.

Equity Funds
Equity funds amounted to US$ 117.9 million at December 31, 2001. The portfolio is principally invested in equity investments of a structured finance nature with a wide range of externally managed private equity funds. These funds invest in leveraged and unleveraged acquisitions, privatizations, recapitalizations, rapidly growing companies, expansion financings, turnaround situations, and other special equity situations.

With the exception of listed equity investments, where fair value is reliably discernible, investments in equity funds are carried at cost. Provisions for other than temporary decline in value, determined on an individual basis, amounted to US$ 21.3 million at the 2001 year end. The US$ 8.6 million increase in provisions relate primarily to expected value diminution pertaining to investments made in the telecom and technology sector. Details on equity funds are provided in Note 10 to the financial statements.

Investments in Projects and Equity Participations

Investments in projects and equity participations amounted to US$ 302.3 million at the end of 2001. This category includes a mix of investments in an unconsolidated GCC subsidiary, equity stakes in GCC companies and an international equity participation. During the year the Corporation invested US$ 27 million in three new projects. An additional provision of US$ 4.5 million was made during the year for this asset category. Detailed analysis of the portfolio, including a breakdown of unconsolidated subsidiary and associated companies, is contained in Note 11 to the Financial Statements. A list of the Corporation's direct investments is also given on page 64.

Receivable From Shareholders

The receivable from shareholders of US$ 577.1 million at the end of 2001 represents the outstanding portion of the proceeds from the sale of GIB. The shareholders intend to repay this outstanding over the next few years through dividends received from GIB and the Corporation. Notes 4 and 9 to the financial statements provide additional details.

Property, Plant, Equipment and Other Assets

Including property, plant and equipment, total other assets amounted to US$ 209.5 million at December 31, 2001. Of this US$ 31.4 million related to property, plant and equipment. The remaining US$ 178.1 million comprised accrued interest receivable, goodwill arising on acquisitions, revaluation gain on derivatives, pension fund, accounts receivable, prepaid expenses and other miscellaneous assets. Details are set out in Notes 12 and 13 of financial statements.

A more detailed discussion on liquidity and funding, the various risks associated with our business activities, and capital strength is included in the Risk Management section that follows.


Principle investing continues to play a central role

Risk Management

The financial goal of the Corporation is to consistently earn competitive returns, while maintaining risks within acceptable levels. Recognizing the relationship between returns and risk, the management of risk forms an integral part of the Corporation's strategic objective. The continuous and rapidly changing business environment has increased the complexity and diversity of risks. The goal of risk management is not to avoid risks, but to understand and manage them.

The various business activities of the Corporation generate a wide spectrum of risks. The four primary risks assessed are credit, market, liquidity and operational. Management of these risks through investment in knowledge and systems has been a priority at GIC. A combination of competent and experienced staff, quantitatively based analytical tools, and ongoing investment in technology are the key resources used to manage our risks effectively. The qualitative and quantitative techniques utilized to optimize the risk return profile incorporate information from the past, trends in the present business environment, and expectations of the future.

Risk management begins with management defining its risk appetite. This is followed by a three step process: identifying and measuring the various risks generated, monitoring and controlling them, and finally optimizing in relation to return.

The primary function of the independent Risk Management Division is to develop and maintain a common risk management framework that serves as a basis for setting policies and limits and for enhancing GIC's ability to manage risks, evaluate performance and allocate capital. This unit acts as a critical link between management and the risk taking divisions – assisting management in defining / quantifying its risk appetite and then effectively communicating this to the risk takers and ensuring that the risk taking activity is within management's acceptable levels.

Within the Corporation, responsibility for management of risks is not restricted to a single division. The philosophy adopted has been to encourage a culture of prudent risk management across all business and support areas.

From a perspective of control, the process of risk management is facilitated through a set of independent functions in addition to the Risk Management Division. These units, which report directly to senior management, include Financial Control, Internal Audit, Compliance and Credit. This multi faceted approach aids the effective management of risks by identifying and monitoring risks from a variety of perspectives.

The process of managing the four risk categories are discussed in more detail in the following sections.

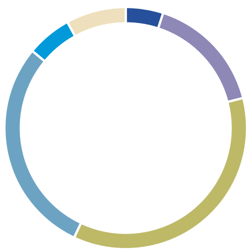
Credit Risk

Credit risk is the possibility of loss arising from the failure of an obligor to completely fulfill its contractual obligations. In its various on and off-balance sheet business activities, the Corporation seeks opportunities to take credit risk prudently and manage it effectively to achieve competitive returns. Credit risk is managed concurrently at the transaction, obligor and portfolio levels.

An activity-wise breakdown of the principal sources of credit risk is illustrated in the pie chart on page 35. The proportions reflect Credit Risk Weighted Exposure, computed based on BIS capital adequacy guidelines.

The primary tool used in the management of credit risk is a set of well defined credit policies and procedures. In addition to communicating management's risk appetite in the form of limits for country, product, industry and obligor, these policies detail the process of measurement,

Sources of Credit Risk
(Weighted Credit Risk Exposure)



	percent
Placements & Short term Balances	6
Investment Securities	15
Loans & Credit Funds	37
Projects, Equity Participations & Equity Funds	29
Other Asset Categories	8
Off Balance Sheet Items	5

Principal Investing
(Projects) by industry

	percent
Chemicals	31
Construction Materials	9
Distributors	7
Financial Services	6
Food Products	7
Metals & Mining	15
Diversified	12
Telecommunications	8
Other	5

monitoring and reporting. The stringent credit approval framework mandates a rigorous and thorough evaluation of creditworthiness of each obligor, after which limits are approved at the highest levels in the management hierarchy. A country risk review system is utilized to set country limits. Additionally, limits for product and industry are also defined to ensure broad diversification of credit risk. Credit policies and procedures are designed to identify, at an early stage, exposures which require more detailed monitoring and review. The credit risk management process utilizes statistical methods as well, to estimate expected and unexpected loss amounts for the various business activities.

Although business units are responsible for maintaining exposures within limits, actual exposures are continuously monitored by independent control functions including Risk Management, Financial Control, Compliance and Internal Audit. Technology is a key element in the monitoring process and in this regard, cutting edge systems, capable of close to real time monitoring and control of risk taking activities, are being effectively utilized.

As of end 2001, the key components of the Corporation's total credit exposure were loans and credit funds; principal equity investments and equity funds; and investment securities. Within the portfolio of loans and advances, there has been a deliberate emphasis on GCC countries, a region whose dynamics we comprehend well and where we have a better understanding of the inherent risks. Approximately 49% of loans were to GCC country governments, the remaining exposed to diverse industrial sectors. Credit funds, managed by a range of experienced and highly rated fund managers, are invested in superior quality debt securities, predominantly rated investment grade or better.

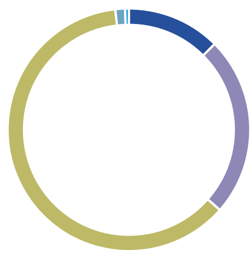
Over the years, the principal investing activity has reviewed over 350 investment proposals and as of December 31, 2001 had invested in about 10% of these. A rigorous evaluation process is followed prior to executing any investment. As is highlighted in the graph above, a healthy diversification across industry sectors is maintained within this portfolio. With regards to the investment securities portfolio, the rating profile, illustrated in the graph on page 36, highlights the superior quality of assets held.

Off-balance sheet Financial Instruments

In the normal course of its business, the Corporation utilizes derivative and foreign exchange instruments to meet the financial needs of its customers, to generate trading revenues and to manage its exposure to market risk.

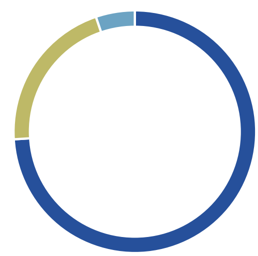
For derivative and foreign exchange transactions, procedures similar to on balance sheet products are used for measuring and monitoring credit risk. Credit risk weighted exposure to off balance sheet products amounted to about 5% of total credit risk weighted exposure.

Rating Profile –
Investment Securities Portfolio



	percent
AAA / Aaa rated debt securities	12.5
GCC Government securities	24.0
Debt securities of other investment grade issuers	61.7
Other debt securities	1.3
Equities	0.5

Market Risk Constituents – Overall



	percent
Interest Rate Risk	74.0
Equity Risk	20.8
Foreign Exchange Risk	5.2

This amount represents the mark-to-market or replacement cost of these transactions. In terms of maturity, over 90% of trading foreign exchange and interest rate contracts were short term with maturities within one year. Credit risk amounts arising from these transactions relate to major banks. Off balance sheet transactions also include credit-related contingent items designed to meet the financial requirement of the Corporation's customers. A detailed credit risk analysis of credit-related contingent items, derivatives and foreign exchange products is set out in Notes 24 and 25 to the financial statements.

Although detailed and thorough analysis is conducted prior to taking on credit risk, unforeseen events could trigger a decline in the creditworthiness associated with a transaction, resulting in loss. Adequate levels of provisions are set aside to cover such losses. The Corporation's provisioning philosophy, including numerical analysis, is discussed in the financial review section on page 29.

Market Risk

Market risk is the possibility of loss in value of financial instruments, resulting from an adverse change in market factors. Within the Corporation, market risk is made up of three key risk constituents – interest rate risk, equity risk and foreign exchange risk. A breakdown, based on risk constituents, is provided above for the combined mark-to-market and investment activities. The percentages reflect average VaR amounts, considered independently, and ignore the effects of diversification across risk classes.

Market risk is measured, monitored and managed, both on a notional basis, and using a Value at Risk (VaR) concept. Quantitative statistical methods combined with judgement and experience are used to effectively manage market risk. A system of limits and guidelines restrain the risk taking activity with regard to individual transactions, net positions, volumes, maturities, concentrations, maximum allowable losses, and ensure that risks are within the acceptable levels in terms of notional amounts. The VaR based system provides a more dynamic measure of market risk capturing, in a timely manner, the impact of changes in environment on the value of the portfolio of financial instruments.

VaR is calculated and reported to senior management on a daily basis at various levels of consolidation including portfolio, business unit and Corporation. The average, minimum and maximum value at risk amounts for the combined mark-to-market and investment activities are tabulated on page 37. These VaR measures are based on a 95% confidence level, 25 day holding period, and using exponentially weighted historical market data. A profile of daily VaR is charted on page 37.

At US$ 20.1 million, the average overall VaR for 2001 was almost 50% higher than the average

2001 Value at Risk – 25 day holding period, 95% confidence level (US$ 000's)

	Average	Minimum	Maximum	**31 Dec 2001**
Interest rate	19,092	14,287	28,613	**21,670**
Equity	5,366	3,833	8,724	**4,147**
Foreign Exchange	1,358	655	2,460	**1,207**
Total	**20,060**	**15,176**	**29,945**	**23,231**

Profile of daily VaR – 25 day holding period, 95% confidence level

overall for 2000. The increase can be attributed primarily to the volatility within the global interest rate markets. As is illustrated in the profile of daily VaR above, total VaR increased significantly during the third quarter of 2001 and continued to climb through to the year end. The impact of equity VaR on overall VaR was minimized again during 2001 as a result of reduced exposures to the global equity markets. The impact of FX exposures on total VaR was not material. At year end 2001, the overall VaR was US$ 23.2 million.

Scenario analysis is an essential component of the market risk management framework. The assumption of normality on which the statistical models are based may become invalid due to the occurrence of certain events. Future scenarios, which result in a breakdown of the historical behavior and relationships between risk constituents, are projected, and potential loss amounts are determined. Most of these scenarios are derived from macroeconomic events of the past, modified with the expectations for the future.

Liquidity Risk

Liquidity risk is the risk of being unable to meet financial obligations at reasonable prices.

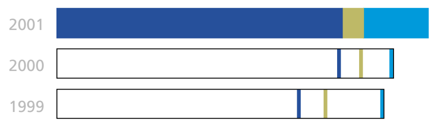
Liquidity risk arises due to:

1. **Cash flow illiquidity,** arising from the potential inability to procure funds at reasonable rates and required maturities.
2. **Asset illiquidity,** relating to the possibility of having to sell assets on a forced basis.

The Corporation adopts a conservative approach to liquidity management with an objective of maintaining sufficient levels of funds and funding capacity to meet our commitments, both on and off balance sheet. In addition to historical data and current information, a vital element in our liquidity measurement methodology is to forecast future scenarios of a tightening in liquidity due to adverse events which may affect both the Corporation and the wider financial system. Extreme event scenarios are evaluated both on the assets and liability side.

Risk Management continued

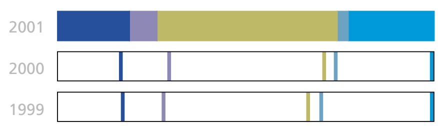
Liquid Assets Ratio



Percent

	2001	2000	1999
Investment securities	55.1	54.4	46.7
Trading securities & management funds	4.1	4.3	5.2
Placements & other liquid assets	12.5	6.3	11.3
Total	71.7	65.0	63.2

Diversified sources of funding



Percent

	2001	2000	1999
GCC deposits	19.2	16.7	17.2
International deposits	7.3	13.0	10.8
Repo financing	47.8	41.0	38.4
Term financing	2.9	2.9	3.4
Shareholders' funds & others	22.8	26.4	30.2

GIC considers that a strong capital position is integral to its ability to manage liquidity by ensuring its secure and continuous access to deposits from both customers and banks. Liquidity controls are in place to closely monitor the profile of future cash flows from maturing assets and liabilities to ensure that the resultant liquidity requirements are within prudently established limits.

A measure of the Corporation's liquidity coverage is highlighted in the following paragraphs.

Liquid Assets Ratio

At 71.7%, the liquid asset ratio reflects the high level of liquid assets maintained in the balance sheet. Comparatively, the ratio at year end 2000 was 65.0%. The ratio is computed by determining the proportion of total assets that can be readily converted into cash, without incurring undue capital losses. Liquid assets include bank balances, money market instruments, securities purchased under resale agreements, placements and securities. Investment securities, constituting over three quarters of the liquid assets, are primarily made up of superior grade debt securities which are readily realizable.

Diversified sources of funding

The Corporation's solid financial condition, augmented by its good standing in the regional and international markets, contributed towards achieving the objective of extending and diversifying its funding base. GIC is planning to execute a medium term financing arrangement, similar to the existing SAR 600 million five year syndicated loan facility maturing in 2004. This will further enhance the Corporation's funding structure. As the chart above illustrates, we are continuously trying to achieve an optimal mix of sources of funding.

Over the years, the Corporation has applied its marketing skills to develop a reliable source of deposits, both regionally and in international markets. At December 31, 2001, deposits from various sources totaled US$ 1,464.8 million, of which deposits from GCC governments and central banks and other institutions headquartered in the GCC states amounted to US$ 1,060.3 million.

Maturity profile of assets and liabilities

A detailed breakdown of the maturity profile by individual asset and liability category is provided in Note 22 to financial statements. At December 31, 2001, roughly 28.6% of total assets were due to mature within 12 months. Over 58% of assets with longer maturities were readily realizable securities. The maturity profile is based on contractual repayment arrangements and as such does not take account of effective maturities of deposits. The Corporation's GCC retention record shows that short maturity deposits from GCC governments, central banks and other regional financial institutions have been regularly renewed over the past decade.

Credit Rating

The investment grade debt ratings were reaffirmed, by both Moody's and Standard & Poor's, for the year under review.

	Moody's	Standard & Poor's
Long-term Deposits	Baa2	BBB+
Short-term Deposits	P3	A2
Bank Financial Strength (BFSR)	C–	-

These ratings reflect the Corporation's strong capital position, its ownership structure and position in the Gulf region, good profitability, asset quality, loan loss experience, the high level of professionalism of our staff and effective management.

Capital Strength

Capital represents the shareholder's investment and is a key strategic resource which supports the Corporation's risk taking business activities. In line with the Corporation's financial objective, management strives to deploy this resource in an efficient and disciplined manner to earn competitive returns. Capital also reflects financial strength and security to the Corporation's creditors and depositors. Capital management is fundamental to GIC's risk management philosophy, and takes into account economic and regulatory requirements.

Regulatory Capital

With the divestiture in 2001 of Gulf International Bank, the Corporation's principal subsidiary, there was a substantial decrease in aggregate risk weighted exposure. Consequently, as of December 31, 2001, the capital adequacy ratios were significantly higher than the minimum regulatory requirements.

At the end of the year under review, the Total and Tier 1 capital ratios were 35.9% and 35.8% respectively. For reasons of comparability, the prior years' figures provided in the table reflect ratios on a stand-alone basis for GIC, excluding exposures with the subsidiary GIB.

With the objective of optimizing capital allocation, GIC has developed a program of phased and gradual growth to be executed over the next few years. This build up will be governed predominantly on risk-return objectives.

BIS Capital Ratio Computations

US$ Million	**2001**	2000	1999
Tier 1 capital (A)	**1,128.1**	1,302.8	1,288.0
Total capital base (B)	**1,131.9**	1,308.5	1,304.8
Risk Weighted Exposure (C)	**3,155.0**	3,879.6	3,300.0
BIS Capital ratios (%)			
Tier 1 capital ratio (A/C*100)	**35.8**	33.6	39.0
Total capital ratio (B/C*100)	**35.9**	33.7	39.5

Prior years' numbers are for GIC alone (excluding GIB)

Economic Capital

In addition to maintaining capital reserves based on regulatory requirements, economic capital sufficiency based on internal models is also determined. The economic capital computation process has three fundamental objectives: determine economic capital sufficiency, in addition to regulatory capital adequacy; assist in equitable / standardized performance measurement of businesses, on a 'real' (risk adjusted) basis; and assist in optimizing resource allocation to achieve target risk adjusted ROE for the Corporation. Economic capital computations are based on extreme scenarios, and cover all types of risks.

Operational Risk

Operational risk is the potential for financial and reputational loss arising from a breakdown in internal controls, operational processes or the various systems that support them. It also includes human errors, criminal acts and natural disasters. Operational risk factors can be categorized into internal and external. Internal risk factors are managed through the establishment of effective infrastructure and controls within the Corporation. External risk factors are managed by anticipating the occurrence of adverse events, preparing contingency plans and implementing sound back-up systems.

Internal Audit & Control

The Internal Audit Division plays an important role in the risk management process, particularly in managing operational risk. Operational risk is managed through an effective infrastructure of internal controls including systems and procedures to monitor transactions, positions, confirmations and documentation. The Internal Audit Division ensures that these control mechanisms, which cover the front and back office functions, are adhered to and adequately functioning. In addition to internal audits, the Corporation's system of internal controls is examined and evaluated by external auditors, as required by the local regulatory body.

The influence of technology has increased substantially over the recent past and this trend is likely to accelerate in future. Keeping this in perspective, considerable resources have been allocated to managing the system side of operational risk. An EDP audit function within the Internal Audit Division works in close conjunction with the Risk Management Division to oversee system risk issues.

Financial Statements

Financial Statements

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Auditors' Report

The Shareholders, Gulf Investment Corporation G.S.C., State of Kuwait
We have audited the accompanying balance sheet of Gulf Investment Corporation G.S.C. ["the Corporation"] as at December 31, 2001 and the related statements of income, changes in shareholders' equity and cash flows for the year then ended.

Respective responsibilities of management and auditors
These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audit.

Basis of opinion
We conducted our audit in accordance with the International Standards on Auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

Opinion
In our opinion, the financial statements present fairly, in all material respects, the financial position of the Corporation as at December 31, 2001 and of the results of its operations and its cash flows for the year then ended, in accordance with International Accounting Standards as adopted by the International Accounting Standards Board.

Other regulatory matters
We further report that we have obtained all the information and explanations that we required for the purpose of our audit and the financial statements include the information required by the Kuwait Commercial Companies Law of 1960, as amended, and the Corporation's articles and memorandum of association. In our opinion, proper books of account have been kept by the Corporation, an inventory count was carried out in accordance with recognized procedures and the accounting information given in the report of the Chairman agrees with the books of account. We have not become aware of any contravention, during the year ended December 31, 2001, of the Kuwait Commercial Companies Law of 1960, as amended, or of the Corporation's articles and memorandum of association, or of Law No. 32 of 1968, as amended, concerning currency, the Central Bank of Kuwait and the organization of banking business and its related regulations, that would materially affect the Corporation's activities or its financial position.

KPMG.

KPMG
Public Accountants
Kuwait
April 15, 2002

Balance Sheet

As at December 31, 2001

US$ million	Note	2001	2000
Assets			
Cash and bank balances		**2.9**	4.7
Placements	5	**390.7**	221.6
Securities purchased under resale agreements		**176.5**	9.1
Trading securities and managed funds	6	**220.6**	238.3
Investment securities	7	**3,055.6**	2,986.3
Loans and credit funds	8	**487.9**	532.3
Investment in GIB	4	**-**	873.7
Receivable from shareholders	9	**577.1**	-
Equity funds	10	**117.9**	109.0
Investment in projects and equity participations	11	**302.3**	316.6
Property, plant and equipment	12	**31.4**	33.5
Other assets	13	**178.1**	166.2
Total assets - continuing operations		**5,541.0**	5,491.3
Discontinued operations	4	**-**	14,111.5
Total assets		**5,541.0**	19,602.8
Liabilities and shareholders' equity			
Liabilities			
Securities sold under repurchase agreements		**2,651.0**	2,250.9
Deposits	14	**1,464.8**	1,630.4
Term finance	15	**160.0**	160.0
Other liabilities	16	**113.5**	125.2
Total liabilities - continuing operations		**4,389.3**	4,166.5
Discontinued operations	4	**-**	14,111.5
Total liabilities		**4,389.3**	18,278.0
Shareholders' equity			
Share capital		**750.0**	750.0
Reserves		**356.2**	574.8
Unrealized gain on available-for-sale assets		**45.5**	-
Total shareholders' equity	17	**1,151.7**	1,324.8
Total liabilities and shareholders' equity		**5,541.0**	19,602.8

The accompanying notes are an integral part of the financial statements.

Dr. Ibrahim Abdulaziz Al-Assaf
Chairman

Hisham Abdulrazzak Al Razzuqi
Chief Executive Officer

Statement of Income

For the year ended December 31, 2001

US$ million	Note	**2001**	2000
Interest and similar income		**272.7**	242.2
Interest expense and similar charges		**(223.9)**	(235.5)
Net interest income		**48.8**	6.7
Other operating income	18	**51.7**	44.7
		100.5	51.4
Provision for impairment losses	19	**(13.8)**	1.0
Staff cost		**(18.3)**	(18.9)
Premises		**(2.2)**	(1.3)
Reversal of restructuring provision		**1.6**	-
Amortization of goodwill		**(1.2)**	(0.1)
Other operating expenses		**(8.0)**	(6.0)
Net income from continuing operations		**58.6**	26.1
Discontinued operations	4	**26.7**	85.6
Net income for the year		**85.3**	111.7

The accompanying notes are an integral part of the financial statements.

Statement of Changes in Shareholders' Equity

For the year ended December 31, 2001

US$ million	Capital	Reserves Compulsory reserves	Voluntary reserves	Retained earnings	Subtotal reserves	Unrealized gain on available-for-sale assets	Total
Balance as at January 1, 2000	750.0	124.6	124.6	288.9	538.1	-	1,288.1
Dividend for 1999	-	-	-	(75.0)	(75.0)	-	(75.0)
Net income for the year	-	-	-	111.7	111.7	-	111.7
Transfer to compulsory reserve	-	11.2	-	(11.2)	-	-	-
Transfer to voluntary reserve	-	-	11.2	(11.2)	-	-	-
Balance as at December 31, 2000	**750.0**	**135.8**	**135.8**	**303.2**	**574.8**	**-**	**1,324.8**
Balance as at January 1, 2001	750.0	135.8	135.8	303.2	574.8	-	1,324.8
Change in accounting policy (refer note 3)	-	-	-	(0.7)	(0.7)	10.0	9.3
Restated balance as at January 1, 2001	750.0	135.8	135.8	302.5	574.1	10.0	1,334.1
Change in fair value of available-for-sale assets	-	-	-	-	-	41.4	41.4
Net gains on disposal of available-for-sale assets transferred to income statement	-	-	-	-	-	(5.9)	(5.9)
Transfer to shareholders (refer note 4)	-	-	-	(303.2)	(303.2)	-	(303.2)
Net income for the year	-	-	-	85.3	85.3	-	85.3
Transfer to compulsory reserve	-	8.5	-	(8.5)	-	-	-
Balance as at December 31, 2001	**750.0**	**144.3**	**135.8**	**76.1**	**356.2**	**45.5**	**1,151.7**

The accompanying notes are an integral part of the financial statements.

Statement of Cash Flows

For the year ended December 31, 2001

US$ million	2001	2000
Cash flows from operating activities before discontinued operations:		
Net income for the year	**85.3**	111.7
Adjustments to reconcile net income to net cash inflow/(outflow) from operating activities:		
Income from GIB	**(26.7)**	(85.6)
Income receivable from the shareholders (see note 9)	**(16.2)**	-
Provision for impairment losses	**13.8**	(1.0)
Amortization of goodwill	**1.2**	0.1
Gain on sale of investment securities	**(5.6)**	(0.9)
Income from projects and equity participations	**(16.3)**	(15.0)
Amortization of premium on investment securities	**0.9**	3.4
Depreciation	**3.1**	0.9
Increase in fair value of available-for-sale investments	**(19.3)**	-
Decrease in trading securities	**17.7**	2.7
Increase in other assets and other liabilities (net)	**(25.4)**	(3.2)
Net cash inflow from operating activities – continuing operations	**12.5**	13.1
Cash flows from investing activities before discontinued operations:		
(Increase)/decrease in placements	**(169.1)**	142.8
(Increase)/decrease in securities purchased under resale agreements	**(167.4)**	29.5
Decrease in loans and credit funds	**44.5**	31.4
Sale and maturity of investment securities	**432.6**	292.4
Purchase of investment securities	**(448.6)**	(1,098.2)
Increase in investment in equity funds	**(6.7)**	(27.3)
Decrease/(increase) in investment in projects and equity participations	**30.8**	(123.4)
Purchase of property, plant and equipment	**(1.1)**	(18.0)
Dividend received	**36.2**	36.2
Net cash outflow from operating activities – continuing operations	**(248.8)**	(734.6)
Cash flows from financing activities before discontinued operations:		
Increase in deposits and repurchase agreements	**234.5**	777.3
Dividend paid	**-**	(75.0)
Net cash inflow from financing activities – continuing operations	**234.5**	702.3
Decrease in cash and cash equivalents	**(1.8)**	(19.2)
Cash and cash equivalents at beginning of year	**4.7**	23.9
Cash and cash equivalents at end of year	**2.9**	4.7

Cash and cash equivalents comprise cash and bank balances.
The cash flow effect of discontinued operations is detailed in note 4.
The accompanying notes are an integral part of the financial statements.

1 Incorporation and Activity

The Gulf Investment Corporation G.S.C. ("Corporation") is an investment company incorporated in Kuwait as a Gulf Shareholding Company. It is equally owned by the governments of the six member states of the Gulf Co-operation Council ("GCC") – Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates. The Corporation is engaged in all aspects of investment banking activities.

The Corporation is domiciled in Kuwait and its registered office is at Jaber Al Mubarak Street, Al Sharq, Kuwait. The total number of staff employed by the Corporation as at December 31, 2001 was 136 (2000: 154).

The financial statements were authorized for issue by the Board of Directors on April 15, 2002.

2 Statement of Accounting Policies

2.1 Statement of compliance

The financial statements have been prepared in accordance with International Accounting Standards ("IAS") as adopted by the International Accounting Standards Board ("IASB"), interpretations issued by the Standing Interpretations Committee of the IASB and the requirements of the Kuwait Commercial Companies Law of 1960, as amended, Ministerial Order No.18 of 1990, Law No. 32 of 1968 concerning currency, the Central Bank of Kuwait and the Organisation of Banking Business and subsequent amendments thereto and the Corporation's articles and memorandum of association.

2.2 Basis of presentation

The Corporation's functional currency is United States Dollars and figures presented in the financial statements are rounded to the nearest million.

The financial statements are prepared on a fair value basis for derivative financial instruments, financial assets and liabilities held for trading, and available-for-sale assets, except those for which a reliable measure of fair value is not available. Other financial assets and liabilities and non-financial assets and liabilities are stated at amortized cost or historical cost.

Except as explained in note 3, the accounting policies have been consistently applied by the Corporation and are consistent with those used in the previous year.

2.3 Subsidiaries

Subsidiaries are those enterprises controlled by the Corporation. Control exists when the Corporation has the power, directly or indirectly, to govern the financial and operating policies of an enterprise so as to obtain benefits from its activities.

Gulf International Bank ("GIB") in which the Corporation had a 72.45% shareholding was the only material subsidiary held by the Corporation until it was sold to the Corporation's shareholders (see note 4). As at December 31, 2000, GIB had total assets of US$ 15.1 billion and shareholders' equity of US$ 1.2 billion. Investment in other subsidiary companies is not material to the financial statements of the Corporation. Accordingly, these subsidiaries are included under 'Investment in Projects and Equity Participations' and are accounted for using the equity method.

2.4 Financial instruments

(i) Classification

Trading instruments are those that the Corporation principally holds for the purpose of short-term profit taking. These include money market funds, trading securities and managed funds, derivative contracts that are not designated as effective hedging instruments, and liabilities from short sales of financial instruments. All trading derivatives in a net receivable position (positive fair value), as well as options purchased, are reported as part of other assets. All trading derivatives in a net payable position (negative fair value), as well as options written, are reported as part of other liabilities.

Originated loans and receivables are loans and receivables created by the Corporation providing money to a debtor other than those created with the intention of short-term profit taking. Originated loans and receivables comprise deposits with banks and financial institutions, securities purchased under resale agreements, loans and advances to customers (other than purchased loans), receivables from shareholders and debt instruments purchased at original issuance.

Held-to-maturity assets are financial assets with fixed or determinable payments and fixed maturity that the Corporation has the intent and ability to hold to maturity. These include credit funds and certain debt instruments.

Available-for-sale assets are financial assets that are not held for trading purposes, originated by the Corporation, or held-to-maturity. Available-for-sale instruments include certain investment securities, equity funds and certain investment in projects.

(ii) Recognition

The Corporation recognizes financial assets held to maturity, held for trading and available-for-sale assets on the trade date i.e. the date it commits to purchase the assets. From this date any gains and losses arising from changes in fair value of the assets are recognized.

Originated loans and receivables are recognized on the settlement date.

(iii) Measurement

Financial instruments are measured initially at cost, including transaction costs.

Subsequent to initial recognition all trading instruments and all available-for-sale assets are measured at fair value, except that any instrument that does not have a quoted market price in an active market and whose fair value cannot be reliably measured is stated at cost, including transaction costs, less impairment losses (see note 2.14).

All non-trading financial liabilities, originated loans and receivables and held-to-maturity assets are measured at amortized cost less impairment losses (see note 2.14). Amortized cost is calculated on the effective interest rate method. Premiums and discounts, including initial transaction costs, are included in the carrying amount of the related instrument and amortized based on the effective interest rate of the instrument.

(iv) Fair value measurement principles

The fair value of financial instruments is based on their quoted market price (bid price for assets and offer price for liabilities) at the balance sheet date without any deduction for transaction costs. If a quoted market price is not available, the fair value of the instrument is estimated using pricing models or discounted cash flow techniques or market price of similar financial instruments.

Where discounted cash flow techniques are used, estimated future cash flows are based on management's best estimates and the discount rate is a market related rate at the balance sheet date for an instrument with similar terms and conditions. Where pricing models are used, inputs are based on market related measures at the balance sheet date.

The fair value of derivatives that are not exchange-traded is estimated at the amount that the Corporation would receive or pay to terminate the contract at the balance sheet date taking into account current market conditions and the current creditworthiness of the counterparties.

(v) Gains and losses on subsequent measurement

Gains and losses arising from a change in the fair value of available-for-sale assets are recognized directly in shareholders' equity. When the financial assets are sold, collected or otherwise disposed of, the cumulative gain or loss recognized in shareholders' equity is transferred to the income statement.

Gains and losses arising from a change in the fair value of trading instruments are recognized in the statement of income.

(vi) Derecognition

A financial asset is derecognized when the Corporation loses control over the contractual rights that comprise the asset. This occurs when the rights are realized, expired or are surrendered. A financial liability is derecognized when it is extinguished.

Held-to-maturity, available-for-sale assets and assets held for trading are derecognized using trade date accounting. The Corporation uses the weighted average method to determine the gain or loss on derecognition.

Originated loans and receivables are derecognized on the day they are transferred by the Corporation.

(vii) Offsetting

Financial assets and liabilities are offset and the net amount is reported in the balance sheet when the Corporation has a legally enforceable right to set off the recognized amounts and the transactions are intended to be settled on a net basis.

2.5 Placements

Placements are accounted as originated loans and receivables.

2.6 Repurchase and resale arrangements

The Corporation enters into purchases (sales) of investments under agreements to resell (repurchase) substantially identical investments at a certain date in the future at a fixed price. The amounts paid are recognized as securities purchased under resale agreements. Investments sold under repurchase agreements continue to be recognized in the balance sheet and are measured in accordance with the accounting policy for either assets held for trading or held-to-maturity or available-for-sale, as appropriate. The proceeds from the sale of the investments are reported as part of liabilities as securities sold under repurchase agreements.

The difference between the sale and repurchase considerations is recognized on an accrual basis over the period of the transaction and is included in interest.

2.7 Trading securities and managed funds

Trading securities and managed funds are accounted as trading assets.

2.8 Investment securities

Debt instruments that the Corporation has the intent and ability to hold to maturity are accounted as held-to-maturity assets.

Debt instruments purchased at original issuance are accounted as original loans and receivables.

Investment securities which are not held-to-maturity investments or debt instruments which are not purchased at original issuance are classified and accounted as available-for-sale assets.

2.9 Loans and credit funds

Loans and advances to customers originated by the Corporation are carried at amortized cost less specific and general provision for impairment (see note 2.14).

Credit funds are accounted as held-to-maturity assets and are carried at amortized cost less impairment losses (see note 2.14).

2.10 Equity funds
Investments in equity funds are classified and accounted as available-for-sale investments. Provision is made for any impairment losses (see note 2.14) on an individual investment basis and is recognized in the statement of income.

2.11 Investment in projects and equity participations
Investment in enterprises in which the Corporation holds 20% or more of the voting capital and/or exercises significant control or influence over the financial and operating policies ("associates") are accounted for using the equity method. Provision is made for any impairment losses and recognized in the income statement.

Other investments in projects and equity participations are classified as available-for-sale assets. Provision is made for any impairment losses (see note 2.14) on an individual investment basis and is recognized as set out in note 2.14.

2.12 Property, plant and equipment and related depreciation
Property, plant and equipment are carried at cost less accumulated depreciation and impairment losses (see note 2.14). Depreciation is computed on a straight-line basis over the estimated useful life of each asset category as follows:

Buildings	20 years
Installations	5 – 10 years
Office equipment	3 – 4 years
Furniture	4 – 6 years
Motor vehicles	3 years

2.13 Amortization of goodwill
Goodwill arising on acquisition of an associate, jointly controlled entity or subsidiary company represents the excess of the cost of the acquisition over the fair value of the net identifiable assets acquired. Goodwill is stated at cost less accumulated amortization and impairment losses (see note 2.14). Goodwill is amortized over its useful life not exceeding twenty years.

2.14 Impairment
Property, plant and equipment, goodwill and financial assets are reviewed at each balance sheet date to determine whether there is objective evidence of impairment. If any such indication exists, the asset's recoverable amount is estimated.

Property, plant, equipment and goodwill
An impairment loss is recognized whenever the carrying amount of an asset exceeds its recoverable amount. The recoverable amount of assets is the greater of their net selling price and value in use. The impairment losses are recognized in the statement of income.

Originated loans and advances, receivables and held-to-maturity assets
The recoverable amount of originated loans and advances, receivables and purchased loans that are classified as held-to-maturity, is calculated as the present value of the expected future cash flows, discounted at the instrument's original effective interest rate. Short-term balances are not discounted.

Loans and advances and receivables are carried at amortized cost less specific and general allowances for uncollectibility. Specific provision for impairment is established if there is objective evidence that the Corporation will not be able to collect all amounts due. The amount of specific provision is determined as the difference between the carrying amount and the recoverable amount of the asset. General provision for impairment is made in accordance with the instructions of the Central Bank of Kuwait dated December 18, 1996, as amended.

If in a subsequent period the amount of an impairment loss decreases and the decrease can be linked objectively to an event occurring after the write-down, the write-down or allowance is reversed through the income statement.

Financial assets remeasured to fair value directly through shareholders' equity
The recoverable amount of an equity instrument is its fair value. The recoverable amount of debt instruments and purchased loans remeasured to fair value is calculated as the present value of expected future cash flows discounted at the current market rate of interest. Where an asset remeasured to fair value directly through shareholders' equity is impaired, and a write down of the asset was previously recognized directly in shareholders' equity, the write down is transferred to the income statement and recognized as part of the impairment loss. Where an asset measured to fair value directly through shareholders' equity is impaired, and an increase in the fair value of the asset was previously recognized in shareholders' equity, the increase in fair value of the asset recognized in shareholders' equity is reversed to the extent the asset is impaired. Any additional impairment loss is recognized in the income statement.

If in a subsequent period the amount of an impairment loss decreases and the decrease can be linked objectively to an event occurring after the write-down, the write-down is reversed through the income statement.

2.15 Other provisions
Other provisions are recognized in the balance sheet when the Corporation has a legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation.

2.16 Fiduciary activities
Assets managed for third parties or held in trust or in a fiduciary capacity are not treated as assets of the Corporation and accordingly are not included in these financial statements.

2.17 Hedge accounting
A hedging relationship exists where:
- at the inception of the hedge there is formal documentation of the hedge;
- the hedge is expected to be highly effective;
- the effectiveness of the hedge can be reliably measured;
- the hedge is highly effective throughout the reporting period; and
- for hedges of a forecasted transaction, the transaction is highly probable and presents an exposure to variations in cash flows that could ultimately affect net profit or loss.

Where there is a hedging relationship between a derivative instrument and a related item being hedged, the hedging instrument is measured at fair value. The treatment of any resultant gains and losses is set out below.

The fair value of derivative hedging instruments is calculated in the same way as the fair value of trading instruments (refer accounting policy 2.4 (iv)).

Where a derivative financial instrument hedges the exposure to changes in the fair value of a recognized asset or liability, the hedged item is stated at fair value in respect of the risk being hedged. Gains or losses on remeasurement of both the hedging instrument and the hedged item are recognized in the income statement.

Where a derivative financial instrument hedges the exposure to variability in the cash flows of recognized assets or liabilities (or homogeneous groups/portfolios thereof) or anticipated transactions or firm commitments, the effective part of any gain or loss on remeasurement of the hedging instrument is recognized directly in shareholders' equity. The ineffective part of any gain or loss is recognized in the income statement.

When a hedged anticipated transaction or firm commitment results in the recognition of an asset or liability, the cumulative gain or loss on the hedging instrument recognized in shareholders' equity is removed from shareholders' equity and included in the initial measurement of the asset or liability. Otherwise the cumulative gain or loss recognized in shareholders' equity is transferred to the income statement at the same time that the hedged transaction affects net profit or loss and included in the same line item as the hedged transaction.

When a hedging instrument or hedge relationship is terminated but the hedged transaction is still expected to occur, the cumulative gain or loss recognized in shareholders' equity remains in shareholders' equity and is recognized in accordance with the above policy. If the hedged transaction is no longer expected to occur, the cumulative gain or loss recognized in shareholders' equity is recognized in the income statement immediately.

2.18 Interest, fee income and dividend income
Interest income and expense is recognized on an accrual basis taking into account the effective yield of the asset or an applicable floating rate. Interest income includes the amortization of any discount or premium or other difference between the initial carrying amount of an interest bearing instrument and its amount at maturity calculated on an effective interest rate basis. Fee income is recognized when earned. Dividend income is recognized when the right to receive payment is established.

2.19 Foreign currency
The reporting currency of the Corporation is the US Dollar. The share capital of the Corporation is also denominated in US Dollars. Transactions in foreign currencies are converted to US Dollars at the rate of exchange prevailing at the date of the transaction. Foreign currency monetary assets and liabilities are converted into US Dollars at market rates of exchange prevailing on the balance sheet date. Realized and unrealized foreign exchange gains and losses are included in the statement of income. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated to US Dollars at foreign exchange rates ruling at the dates the values were determined. Non-monetary assets and liabilities denominated in foreign currency that are stated at historical cost or amortized cost, are recorded at the exchange rate ruling at the date of transaction.

3 Change in Accounting Policy
During the year the Corporation adopted IAS 39 Financial Instruments: *Recognition and Measurement.*

The adoption of IAS 39 has resulted in the Corporation recognizing available-for-sale assets at fair value, making provision for impairment of loans and advances, receivables, available-for-sale assets and held-to-maturity investments based on present value of expected cash flows, amortizing premiums and discounts on purchase of debt instruments based on the effective interest rate method, changing the method of accounting for hedging transactions and recognizing all derivative financial instruments as assets or liabilities at fair value. This change has been accounted for by adjusting the opening balance of retained earnings. In accordance with the transition requirements of IAS 39 prior year comparatives have not been adjusted.

The adoption of IAS 39 has resulted in a debit adjustment, as at January 1, 2001, to retained earnings of US$ 0.7 million and to unrealized gain on available-for-sale of US$ 10.0 million. For the year ended December 31, 2001 the net profit decreased by US$ 3.0 million as a result of the adoption of IAS 39.

4 Investment in GIB/Discontinued Operations
In the Board of Directors meeting of the Corporation held on April 7, 2001, a decision was made to sell the Corporation's 72.45% holding in Gulf International Bank ("GIB") to the Corporation's shareholders. The sale consideration was fixed at GIB's carrying value in the books of the Corporation as at December 31, 2000 of US$ 873.7 million, less approved dividend of US$ 36.2 million. The shareholders also approved distribution of retained earnings of US$ 303.2 million, which was utilized as partial settlement of the sale consideration. No gain/loss arose on the sale of GIB.

In the Board of Directors meeting held on October 13, 2001, it was decided that in addition to the net sale consideration, the Corporation is entitled to receive US$ 26.7 million being 72.45% of GIB's net income for the period from January 1, 2001 to April 30, 2001. This is recognized by the Corporation in the statement of income under discontinued operations.

For the year ended December 31, 2000 GIB earned income of US$ 297.0 million, incurred operating expenses and provision of US$ 168.5 million, resulting in net income before tax and minority interest of US$ 128.5 million. During 2000 GIB's cash inflow from operating activities was US$ 65.3 million, cash inflow from investing activities was US$ 110.9 million, and cash outflow from financing activities was US$ 541.0 million.

5 Placements

Placements at December 31, 2001 included placements with non-bank financial institutions amounting to US$ 35.0 million (2000: US$ 0.4 million).

6 Trading Securities and Managed Funds

US$ million	2001	2000
Managed funds	**214.9**	186.9
Equities	**5.7**	45.9
Listed debt securities	**-**	5.5
	220.6	238.3

7 Investment Securities

Debt and other interest bearing instruments available-for-sale

US$ million	2001	2000
AAA/Aaa rated debt securities	**321.2**	315.3
GCC Government securities	**120.3**	112.1
Debt securities of other investment grade issuers	**1,436.2**	1,474.4
Other debt securities	**39.3**	20.0
	1,917.0	1,921.8

Debt and other interest bearing instruments held-to-maturity

US$ million	2001	2000
AAA/Aaa rated debt securities	**60.9**	63.2
GCC Government securities	**613.7**	582.8
Debt securities of other investment grade issuers	**448.9**	415.2
Other debt securities	**1.5**	3.3
	1,125.0	1,064.5

Equity investments available-for-sale

US$ million	2001	2000
Listed equity investments	**3.3**	-
Unlisted equity investments	**10.3**	-
	13.6	-
Total	**3,055.6**	2,986.3

Investment securities amounting to US$ 2,651.0 million (2000: US$ 2,250.9 million) are pledged as security in respect of borrowings under securities sold under repurchase agreements.

8 Loans and Credit Funds

US$ million	2001	2000
Loans and advances to customers	**245.8**	350.0
Credit funds	**242.1**	182.3
	487.9	532.3

Loans and advances to customers at December 31, 2001 include lendings to GCC Country Governments of US$ 120.4 million (2000: US$ 195.1 million).

There were no significant concentrations by industrial sector at December 31, 2001 and at December 31, 2000.

a) Provision for loan losses

The movements in the provision for loan losses were as follows:

US$ million	2001	2000
Balance at beginning of the year	**4.8**	6.0
Net write back for the year	**(0.1)**	(1.2)
Balance at end of the year	**4.7**	4.8

b) Provision for loan guarantees

US$ million	2001	2000
Balance at beginning of the year	**2.6**	9.6
Net charge/(write back) for the year	**0.8**	(7.0)
Balance at end of the year	**3.4**	2.6

9 Receivable from Shareholders

This primarily represents the unpaid balance from sale of GIB to the shareholders (see note 4). The executive committee of the shareholders of the Corporation have in a meeting held on December 26, 2001 approved the payment of this outstanding balance from any future dividends receivable by the shareholders from GIB and from the Corporation. The outstanding balance carries a rate of return to be computed annually. The rate for 2001 was 4.33%.

10 Equity Funds

US$ million	2001	2000
Listed equity investments	**19.9**	21.3
Unlisted equity investments	**119.3**	100.4
	139.2	121.7
Provision for impairment	**(21.3)**	(12.7)
	117.9	109.0

Unlisted equity securities held by the equity funds are carried by the Corporation at cost less any impairment losses, since fair value of these investments cannot be reliably determined. There is no active market for these investments and there have not been any recent transactions that provide evidence of the current fair value.

The following is a summary of movements in the balance of provisions for impairment of equity funds.

US$ million	2001	2000
Balance at the beginning of year	**12.7**	6.8
Charge for the year	**8.6**	5.9
Balance at end of the year	**21.3**	12.7

11 Investment in Projects and Equity Participations

US$ million	2001	2000
Project investments equity accounted	**107.2**	132.0
Other project investments and equity participations	**216.8**	201.8
	324.0	333.8
Provision for impairment	**(21.7)**	(17.2)
	302.3	316.6

a) Investments equity accounted

Details of investment in projects which are equity accounted are as follows:

	Registered capital US$ million	Share of capital held %	Carrying value US$ million 2001	Carrying value US$ million 2000
Bitumat Company Ltd.	6.7	100.0	**21.8**	16.9
Gulf Industrial Investment Co.	50.0	50.0	**37.8**	72.8
Bahrain Industrial Pharmaceutical Co.	2.8	40.0	**0.7**	0.9
The National Titanium Dioxide Co.	46.7	33.0	**25.1**	21.5
Assafwah Poultry Co.	13.0	30.9	**4.1**	2.7
Al Manar Plastics Product Co.	3.5	30.0	**1.0**	1.0
Emirates Modern Poultry Co.	11.8	25.4	**-**	5.1
Kuwait International Advanced Industries Co.	6.5	25.0	**1.6**	1.6
Dhofar Fisheries Industries Co.	13.0	23.8	**3.1**	3.1
Celtex Weaving Mills Co.	8.0	23.0	**1.2**	1.8
Rawabi Emirates (PJSC)	11.8	22.5	**10.8**	-
Al Rawabi Dairy Co.	9.5	20.0	**-**	4.6
			107.2	132.0

During the year, Gulf Industrial Investment Company ("GIIC") reduced its capital from US$ 110 million to US$ 50 million and decided to distribute US$ 60 million to its shareholders. As at December 31, 2001 the Corporation had received US$ 10 million and the unpaid balance of US$ 20 million is reported as part of the other assets. Also, during the year, Al Rawabi Dairy Company and Emirates Modern Poultry Company merged to form Rawabi Emirates (PJSC).

b) Other project investments and equity participations

US$ million	2001	2000
Listed investments	**22.2**	3.7
Unlisted investments	**194.6**	198.1
	216.8	201.8

Unlisted investments are carried at cost less any impairment losses, since the fair value of these investments cannot be reliably determined. There is no active market for these investments and there have not been any recent transactions that provide evidence of the current fair value.

c) Provision for impairment in investment in projects and equity participations

The movement in the provisions was as follows:

US$ million	2001	2000
Balance at beginning of year	**17.2**	15.5
Net charge for the year	**4.5**	1.7
Balance at end of the year	**21.7**	17.2

12 Property, Plant and Equipment

US$ million	Cost	Accumulated depreciation	**Net book value 2001**	Net book value 2000
Building and installations	24.1	1.2	**22.9**	23.0
Furniture, equipment and motor vehicles	19.2	10.7	**8.5**	10.5
	43.3	11.9	**31.4**	33.5

There were no significant additions or disposals during the year. The depreciation charge for the year is US$ 3.1 million (2000: US$ 0.9 million).

13 Other Assets

US$ million	**2001**	2000
Accrued interest, fees and commissions	**68.1**	82.5
Receivable from GIIC (refer note 11)	**20.0**	-
Derivative assets used for hedging	**0.4**	0.4
Derivative instruments held for trading	**-**	0.4
Employees' end of service benefit asset	**29.7**	31.6
Goodwill arising on acquisitions	**23.7**	22.0
Prepayments	**1.0**	1.3
Other, including accounts receivable	**35.2**	28.0
	178.1	166.2

14 Deposits

US$ million	**2001**	2000
Deposits from Central Banks	**303.0**	234.5
Deposits from other banks	**871.5**	1,206.0
Other deposits	**290.3**	189.9
	1,464.8	1,630.4

At December 31, 2001 deposits from GCC Country Governments and Central Banks and other institutions headquartered in the GCC States amounted to US$ 1,060.3 million (2000: US$ 918.3 million).

15 Term Finance

US$ million	**2001**	2000
Saudi Riyal Floating rate loan due in 2004	**160.0**	160.0

16 Other Liabilities

US$ million	**2001**	2000
Accrued interest	**48.0**	71.1
Derivative liabilities used for hedging	**20.1**	2.1
Employees' end of service benefits	**34.3**	40.5
Other provision	**3.4**	2.6
Other, including accounts payable and accrued expenses	**7.7**	8.9
	113.5	125.2

17 Shareholders' Equity

17.1 The authorized and issued capital comprises 2.1 million shares of US$ 1,000 each (2000: 2.1 million shares of US$ 1,000 each). The paid up capital is US$ 750 million (2000: US$ 750 million).

17.2 In accordance with the Kuwait Commercial Companies' Law and the Corporation's Articles of Association, 10% of the net income for the year is required to be transferred to the non-distributable compulsory reserve until the reserve reaches a minimum of 50% of share capital.

17.3 No transfer is made to the voluntary reserve for the year ended December 31, 2001 based on a resolution adopted in the General Assembly meeting of the shareholders.

17.4 Unrealized gain on available-for-sale assets comprises the cumulative net change in fair value of available-for-sale assets held by the Corporation.

18 Other Operating Income

US$ million	2001	2000
Net gain on trading securities and managed funds	**10.0**	12.2
Net (loss)/gain on investment securities	**(0.3)**	0.9
Net gain on sale of investment in projects and participations	**0.4**	1.0
Net gain on disposal of available-for-sale investments transferred from shareholders' equity	**5.9**	-
Income from equity funds	**8.6**	6.1
Income from projects and equity participations	**19.1**	14.0
Profit on foreign exchange	**0.2**	0.5
Dividend income	**5.5**	7.4
Fees, commissions and sundry income	**2.3**	2.6
	51.7	44.7

19 Provision for Impairment Losses

US$ million	2001	2000
Equity funds	**(8.6)**	(5.9)
Projects and equity participations	**(4.5)**	(1.7)
Loans and loan guarantees	**(0.7)**	8.2
Investment securities	**-**	0.4
	(13.8)	1.0

20 Retirement and Other Terminal Benefits

The Corporation has defined voluntary contribution and end of service indemnity plans which cover all of its employees. Contribution to the voluntary plan is based on a percentage of pensionable salary and consists of contribution by employees and a matched contribution up to a certain limit by the Corporation. Contribution to the end of service indemnity plan is based on a percentage of pensionable salary and number of years of service by the employees. The amounts to be paid as the end of service benefits are determined by reference to the amounts of the contributions and investment earnings thereon. The Corporation also pays contributions to government defined contribution pension plan for certain employees in accordance with the legal requirements in Kuwait.

The total cost of retirement and other end of service benefits included in staff expenses for the year ended December 31, 2001 amounted to US$ 3.0 million (2000: US$ 3.3 million).

21 Dividends

A dividend of US$ 100 per share for the year ended December 31, 2001 (2000: nil) was approved by the shareholders in the General Assembly meeting held on April 15, 2002. This will be utilized to settle receivable from shareholders (See note 9).

22 Asset and Liability Maturity Profile

US$ million	Within 3 months	3 months to 1 year	1 to 5 years	Over 5 years	Total
At December 31, 2001					
Assets					
Cash and bank balances	2.9	-	-	-	2.9
Placements	390.7	-	-	-	390.7
Securities purchased under resale agreements	114.7	61.8	-	-	176.5
Trading securities and managed funds	-	-	-	220.6	220.6
Investment securities	271.0	478.0	1,930.0	376.6	3,055.6
Loans and credit funds	28.6	35.2	358.5	65.6	487.9
Receivable from shareholders	75.0	-	-	502.1	577.1
Equity funds	5.0	-	12.6	100.3	117.9
Investments in projects and equity participations	-	-	22.1	280.2	302.3
Property, plant and equipment	-	-	-	31.4	31.4
Other assets	75.9	48.6	6.5	47.1	178.1
Total assets	**963.8**	**623.6**	**2,329.7**	**1,623.9**	**5,541.0**
Liabilities and Shareholders' equity					
Securities sold under repurchase agreements	1,414.9	1,236.1	-	-	2,651.0
Deposits	1,261.8	163.0	40.0	-	1,464.8
Term finance	-	-	160.0	-	160.0
Other liabilities	35.9	20.0	10.3	47.3	113.5
Shareholders' equity	75.0	-	-	1,076.7	1,151.7
Total liabilities and shareholders' equity	**2,787.6**	**1,419.1**	**210.3**	**1,124.0**	**5,541.0**
At December 31, 2000					
Total assets					
Continuing operations	376.5	345.1	2,643.2	2,126.5	5,491.3
Discontinued operations	4,697.4	1,802.2	3,875.6	3,736.3	14,111.5
	5,073.9	**2,147.3**	**6,518.8**	**5,862.8**	**19,602.8**
Total liabilities and shareholders' equity					
Continuing operations	3,198.9	771.4	160.0	1,361.0	5,491.3
Discontinued operations	11,213.2	1,594.7	886.5	417.1	14,111.5
	14,412.1	**2,366.1**	**1,046.5**	**1,778.1**	**19,602.8**

The asset and liability maturity profile is based on contractual repayment arrangements and as such does not take account of the effective maturities of deposits as indicated by the Corporation's deposit retention records and of borrowers' right to prepay obligations with or without prepayment penalties. Formal liquidity controls are based on contractual asset and liability maturities.

23 Asset and Liability Repricing Profile and Effective Interest Rates

US$ million	Within 3 months	3 months to 1 year	Over 1 year	Non-interest bearing items	Total	Effective interest rate %
At December 31, 2001						
Assets						
Cash and bank balances	2.9	-	-	-	2.9	-
Placements	390.7	-	-	-	390.7	2.30
Securities purchased under resale agreements	114.7	61.8	-		176.5	2.58
Trading securities and managed funds	-	-	-	220.6	220.6	-
Investment securities:						
Fixed rate	197.7	365.4	1,426.3	-	1,989.4	6.23
Floating rate	861.3	191.3	-	-	1,052.6	3.20
Equities	-	-	-	13.6	13.6	-
Loans and credit funds	347.1	142.4	-	(1.6)	487.9	3.62
Receivable from shareholders	75.0	-	502.1	-	577.1	4.33
Equity funds	-	-	-	117.9	117.9	-
Investment in projects and equity participations	-	-	-	302.3	302.3	-
Property, plant and equipment and other assets	-	-	-	209.5	209.5	-
Total assets	**1,989.4**	**760.9**	**1,928.4**	**862.3**	**5,541.0**	
Liabilities and Shareholders' equity						
Securities sold under repurchase agreements	1,414.9	1,236.1	-	-	2,651.0	3.39
Deposits	1,261.8	203.0	-	-	1,464.8	2.90
Term finance	160.0	-	-	-	160.0	4.02
Other liabilities	-	-	-	113.5	113.5	-
Shareholders' equity	75.0	-	-	1,076.7	1,151.7	-
Total liabilities and shareholders' equity	**2,911.7**	**1,439.1**	**-**	**1,190.2**	**5,541.0**	
Derivative instruments	48.2	(48.2)	-	-	-	
Interest rate sensitivity gap	(874.1)	(726.4)	1,928.4	(327.9)	-	
Cumulative interest rate sensitivity gap	**(874.1)**	**(1,600.5)**	**327.9**	**-**	**-**	
At December 31, 2000						
Continuing operations:						
Interest rate sensitivity gap	(1,722.3)	(334.4)	1,776.5	280.2	-	
Cumulative interest rate sensitivity gap	(1,722.3)	(2,056.7)	(280.2)	-	-	
Discontinued operations:						
Interest rate sensitivity gap	(1,557.3)	1,773.4	575.9	(792.0)	-	
Cumulative interest rate sensitivity gap	(1,557.3)	216.1	792.0	-	-	

The repricing profile is based on the remaining period to the next interest repricing date. The repricing profiles of floating rate investment securities incorporate the effect of interest rate swaps used to modify the interest rate characteristics of specific transactions. The general provision for loan losses is deducted from non-interest bearing assets.

24 Commitments and Contingent Liabilities

In the usual course of meeting the requirements of customers, the Corporation has commitments to extend credit and provide financial guarantees and letters of credit to guarantee the performance of customers to third parties.The credit risk on these transactions is generally less than the contractual amount.The table below sets out the notional principal amounts of outstanding commitments and the risk-weighted equivalents calculated in accordance with the capital adequacy guidelines of the Bank for International Settlements (BIS).

	2001		2000	
US$ million	**Notional principal amount**	**Risk-weighted equivalent**	Notional principal amount	Risk-weighted equivalent
Transaction-related contingent items	**59.8**	**59.8**	62.3	62.3
Undrawn loan commitments and underwriting commitments under note issuance and revolving facilities	**50.1**	**12.5**	86.7	21.7
Total	**109.9**	**72.3**	149.0	84.0

The above commitments and contingent liabilities have off balance-sheet credit risk because only origination fees and accruals for probable losses are recognized in the balance sheet until the commitments are fulfilled or expired. Many of the contingent liabilities and commitments will expire without being advanced in whole or in part. Therefore, the amounts do not represent expected future cash flows.

25 Derivatives and Foreign Exchange Products

Derivatives and foreign exchange instruments are utilized by the Corporation to meet the needs of its customers, to generate trading revenues and as part of its asset and liability management (ALM) activity to hedge its own exposure to market, interest rate and currency risk.

In the case of derivative transactions the notional principal typically does not change hands. It is simply a quantity which is used to calculate payments. While notional principal is a volume measure used in the derivatives and foreign exchange markets, it is neither a measure of market nor credit risk. The Corporation’s measure of credit exposure is the cost of replacing contracts at current market rates should the counterparty default prior to the settlement date. Credit risk amounts represent the gross unrealized gains on transactions before taking account of any collateral held or any master netting agreements in place.

Hedge accounting

Interest rate swaps under which the Corporation pays a fixed rate and receives a floating rate are used in fair value hedges of fixed interest securities available-for-sale.

As at the balance sheet date the notional amount of interest rate swaps used to hedge interest rate risk amounted to US$ 378.3 million (2000: US$ 375.6 million) and its net fair value was a swap loss of US$ 20.1 million (2000:US$ 8.5 million).

Trading activities

The table below summarizes the aggregate notional, net fair value and credit risk amounts of foreign exchange and derivative financial instruments held for trading.

US$ million	Notional amounts	Net fair values	Credit risk amounts
As at December 31, 2001			
Foreign exchange contracts:			
Unmatured spot, forward and futures contracts	268.5	268.6	0.2
Options purchased	38.9	-	-
Options written	38.9	-	-
Total	**346.3**	**268.6**	**0.2**
Interest rate contracts:			
Interest rate swaps	142.7	0.3	1.1
Total	**142.7**	**0.3**	**1.1**
Grand Total	**489.0**	**268.9**	**1.3**
As at December 31, 2000			
Foreign exchange contracts:			
Unmatured spot, forward and futures contracts	680.6	680.7	16.5
Options purchased	7.4	-	-
Total	**688.0**	**680.7**	**16.5**
Interest rate contracts:			
Interest rate swaps	107.1	-	0.4
Total	**107.1**	**-**	**0.4**
Grand Total	**795.1**	**680.7**	**16.9**

Counterparty analysis

US$ million	Banks	Other	Total
At December 31, 2001			
Credit risk amounts			
OECD countries	1.0	-	1.0
GCC countries	-	-	-
Other countries	0.3	-	0.3
Total	**1.3**	**-**	**1.3**
At December 31, 2000			
Credit risk amounts			
OECD countries	6.4	-	6.4
GCC countries	0.1	6.2	6.3
Other countries	-	4.2	4.2
Total	**6.5**	**10.4**	**16.9**

Credit risk is concentrated on major OECD-based banks.

Maturity analysis

US$ million	Year 1	Years 2 & 3	Years 4 & 5	Over 5 Yrs	Total
At December 31, 2001					
Notional amounts					
Foreign exchange contracts	346.3	-	-	-	346.3
Interest rate contracts	94.6	30.0	18.1	-	142.7
Total	**440.9**	**30.0**	**18.1**	**-**	**489.0**
At December 31, 2000					
Notional amounts					
Foreign exchange contracts	688.0	-	-	-	688.0
Interest rate contracts	58.1	20.0	29.0	-	107.1
Total	**746.1**	**20.0**	**29.0**	**-**	**795.1**

26 Geographical Distribution of Risk Assets

US$ million	Cash and bank balances and placements	Securities purchased under resale agreements	Trading, investment securities and managed funds	Loans, credit funds and receivable from shareholders
GCC	287.4	-	802.4	822.9
Middle East and North Africa	-	-	10.9	-
Europe	60.0	176.5	1,045.7	-
North America	25.9	-	1,221.4	242.1
Asia	20.3	-	195.8	-
Total	**393.6**	**176.5**	**3,276.2**	**1,065.0**

US$ million	Equity funds, investment in projects & equity participations	Commitments and contingent liabilities	**2001 Total**	2000 Total
GCC	289.8	109.9	**2,312.4**	1,700.4
Middle East and North Africa	-	-	**10.9**	10.0
Europe	31.7	-	**1,313.9**	1,214.0
North America	96.5	-	**1,585.9**	1,415.9
Asia	2.2	-	**218.3**	226.7
Total	**420.2**	**109.9**	**5,441.4**	4,567.0

An analysis of derivatives and foreign exchange products is set out in note 25.

27 Fair Value Information

As at the balance sheet date the fair value of financial assets and financial liabilities that are not carried at fair value is not materially different from their carrying amounts, except for debt and other interest bearing instruments held-to-maturity (see note 7), whose fair value is US$ 9.5 million higher than its carrying value (2000: US$ 12.1 million lower than its carrying value).

Fair value is the amount at which an asset, liability or financial instrument could be exchanged or settled between knowledgeable parties in an arm's length transaction. Underlying the definition of fair value is the presumption that the Corporation is a going concern without any intention, or need, to liquidate, curtail materially the scale of its operations or undertake a transaction on adverse terms.

28 Related Party Transactions

During the year certain transactions were conducted with the parties that have a direct or indirect relationship with the Corporation's shareholders. These comprised standard money market, foreign exchange, investment, lending and securities transactions and were conducted on an arm's length basis at open market prices. The volume of such transactions is disclosed in respective notes to the financial statements.

In addition to the above, during the year the Corporation sold its investment in GIB to its shareholders (see note 4 and note 9).

29 Comparatives

Where necessary, comparative figures have been adjusted to conform with changes in presentation in the current year.

Direct Investments in the GCC Region

Direct Investments in the GCC Region

	Location	Total Shareholders' Equity (US$ million)	GIC's Share of Capital (%)
Non-consolidated subsidiary and associated companies			
Bitumat Company	Saudi Arabia	21.8	100.0
Gulf Industrial Investment Company	Bahrain	75.5	50.0
Bahrain Industrial Pharmaceutical Company	Bahrain	1.8	40.0
National Titanium Dioxide Company (CRISTAL)	Saudi Arabia	76.0	33.0
Assafwa Poultry Company	Oman	13.0	30.9
Al-Manar Plastic Product Company	Saudi Arabia	3.5	30.0
Kuwait International Advanced Industries	Kuwait	4.6	25.0
Dhofar Fisheries Industries Company	Oman	10.0	23.8
Celtex Weaving Mills Company	Bahrain	5.08	23.0
Rawabi Emirates (PJSC) (previously Al Rawabi Dairy Co. & Emirates Modern Poultry Co.)	UAE	47.6	22.5
Equity participations			
Gulf Stone Company	Oman	4.6	19.5
Cosmoplast Industrial Company	UAE	30.4	19.0
Qatar Briquetted Iron Company (QABICO)	Qatar	0.6	16.3
Advanced Electronics Company	Saudi Arabia	52.6	15.0
National Environmental Services Company (NESCO)	Kuwait	2.7	15.3
Arab Pesticides Industries Company (MOBEED)	Saudi Arabia	3.8	12.5
National Petrochemical Industries Company	Saudi Arabia	139.8	12.0
Interplast	UAE	28.7	11.1
Arab Qatari Company for Dairy Products	Qatar	14.8	10.8
Al-Salam Aircraft Company	Saudi Arabia	2.6	10.0
Gulf Ferro Alloys Company (Sabayek)	Saudi Arabia	20.4	10.0
Jarir Marketing Company	Saudi Arabia	95.9	10.0
National Aluminum Products Company	Oman	13.3	10.0
Ras Laffan	Oman	17.4	10.0
Zamil Industrial Investment Company (ZIIC)	Saudi Arabia	112.7	10.0
National Pharmaceutical Industries Company	Kuwait	11.0	8.7
Securities & Investment Company	Bahrain	36.9	8.0
Al-Jubail Chemical Industrial Company (JANA)	Saudi Arabia	55.6	7.5
Gulf Aluminium Rolling Mill Company	Bahrain	97.3	5.7
Arabian Industrial Fibers Company (Ibn Rushd)	Saudi Arabia	712.2	4.7
International Fish Farming Company	UAE	83.4	4.0
United Power Company	Oman	131.5	2.7
Oasis International Leasing Company	UAE	147.0	2.0
Thuraya Satellite Telecommunications Company	UAE	435.4	1.6
Qatar Telecom (Q-TEL)	Qatar	497.4	0.6

Corporate Directory

Senior Management
Chief Executive Officer
Hisham Abdulrazzak Al Razzuqi

Global Markets

Acting Head of Global Markets & Head of Proprietary Asset Management
Jamal Al Saeed

Head of GCC Equities
Abdulrahman Al Saeed

Head of Marketing
Hamza Behbehani

Fixed Income
Abdulaziz Al Mulla

Treasury
Martin Joy

Money Market
Mathew Abraham

Principal Investing

Head of Corporate Finance
Mahmoud Rateb

Head of GCC Diversified Projects
Khaled Al Awadi

Corporate Office

Head of Economics & Strategy
Dr. Soliman Demir

Head of Financial Control & Risk Management
Nabil Guirguis

Head of Internal Audit
Anthony W. Ede

Shared Services

Head of Shared Services & Head of Human Resources
Mohammed Al Sanie

Head of Information Technology
Hani Al Shakhs

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Shawki Khalaf

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