

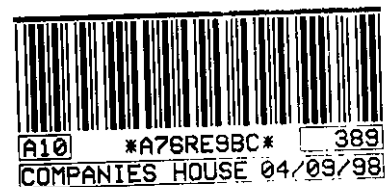
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KUWAIT PETROLEUM CORPORATION
STATE OF KUWAIT

FINANCIAL STATEMENTS
YEAR ENDED JUNE 30, 1997
WITH
AUDITOR'S REPORT

ARTHUR
ANDERSEN
AL-BAZIE & CO.
PUBLIC ACCOUNTANTS

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KUWAIT PETROLEUM CORPORATION
STATE OF KUWAIT

FINANCIAL STATEMENTS
YEAR ENDED JUNE 30, 1997
WITH
AUDITOR'S REPORT

CONTENTS

Auditor's report

Exhibit

Balance sheet

A

Statement of income and appropriations

B

Statement of cash flows

C

Pages

Notes to the financial statements

1 to 12



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Public Accountants

H.E. The Minister of Oil,
Chairman of the Board of Directors and
Members of the Board of Directors of
Kuwait Petroleum Corporation
State of Kuwait

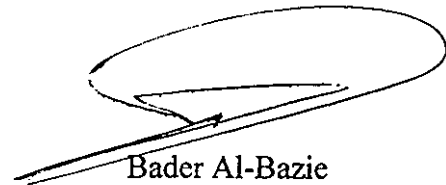
I have audited the accompanying balance sheet of Kuwait Petroleum Corporation as of June 30, 1997, and the related statements of income and appropriations and cash flows for the year then ended. These financial statements are the responsibility of the Corporation's management. My responsibility is to express an opinion on these financial statements based on the audit. I did not audit the financial statements of Kuwait National Petroleum Company K.S.C., Kuwait Oil Tanker Company S.A.K., Petrochemical Industries Company K.S.C., SFIC Holdings (Cayman) Inc. and Kuwait Oil Company K.S.C., which were accounted for in the accompanying financial statements under the equity method of accounting. The investment in these entities represents 21.34 % of total assets and the equity in their net profits represents 34.66 % of net profit for the year. These statements were audited by other auditors whose reports have been furnished to me and my opinion, insofar as it relates to the amounts included for those entities, is based solely on the reports of other auditors.

The audit was conducted in accordance with International Standards on Auditing. Those standards require that I 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. I believe that the audit conducted and the reports of other auditors provide a reasonable basis for my opinion.

In my opinion, based on my audit and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the financial position of Kuwait Petroleum Corporation as of June 30, 1997, and the results of its operations and its cash flows for the year then ended in conformity with International Accounting Standards.

Also in my opinion, the statements include the disclosures required by the Law Decree No. 6 of 1980, and I obtained the information I required to perform my audit. In addition, proper books of account have been kept, physical stocktaking was carried out in accordance with recognized practice, and the accounting information given in the Directors' Report is in agreement with the Corporation's books. According to the information available to me, there were no contraventions during the year of the Corporation's Law which might have materially affected the Corporation's financial position or results of its operations.

State of Kuwait
August 26, 1997



Bader Al-Bazie
Licence No. 1-A
Member of Andersen Worldwide

KUWAIT PETROLEUM CORPORATION
STATE OF KUWAIT
BALANCE SHEET
June 30, 1997

<u>ASSETS</u>	Note	1997 KD (thousands)	1996 KD (thousands)
Current assets:			
Cash and deposits at banks	3	1,501,835	1,185,457
Trade receivables		298,576	314,688
Inventories	4	103,930	103,955
Advance to Ministry of Finance		560,922	392,326
Amounts due from subsidiaries		289,401	254,382
Other receivables and prepayments	5	40,525	38,111
Total current assets		<u>2,795,189</u>	<u>2,288,919</u>
Investments:			
Subsidiaries and associates		2,214,828	2,148,711
Neutral zone concession		38,528	35,115
Securities	6	2,027,491	1,705,354
		<u>4,280,847</u>	<u>3,889,180</u>
Loans to subsidiaries	7	680,551	931,684
Finance advances to subsidiary	8	407,972	544,653
Fixed assets:			
Cost		2,641	2,351
Accumulated depreciation		(2,239)	(1,881)
		<u>402</u>	<u>470</u>
		<u>8,164,961</u>	<u>7,654,906</u>
<u>LIABILITIES AND OWNER'S EQUITY</u>			
Current liabilities:			
Trade payables		820	41
Other payables and accruals	9	23,792	18,571
Amounts due to Ministry of Oil	10	281,398	268,243
Amounts due to subsidiaries		129,214	133,771
Profit available for distribution	11	1,232,523	783,622
Total current liabilities		<u>1,667,747</u>	<u>1,204,248</u>
Other provisions		3,779	3,338
Other non-current liabilities	12	95,244	90,397
Owner's equity:			
Authorized and paid-in capital		2,500,000	2,500,000
Statutory reserve	13	622,744	485,789
Capital reserve	14	232,945	232,945
General reserve	15	1,589,529	1,589,529
Provision for replacement and renewal of fixed assets	16	1,298,691	1,298,691
Foreign currency translation adjustments	17	154,282	249,969
Total Owner's equity		<u>6,398,191</u>	<u>6,356,923</u>
		<u>8,164,961</u>	<u>7,654,906</u>

The accompanying notes are an integral part of the financial statements

KUWAIT PETROLEUM CORPORATION
STATE OF KUWAIT

STATEMENT OF INCOME AND APPROPRIATIONS
For the year ended June 30, 1997

	Note	1997 KD (thousands)	1996 KD (thousands)
Sales		7,093,027	5,866,260
Cost of sales		(6,628,104)	(5,469,566)
Gross trading profit		464,923	396,694
Net results of subsidiaries and associates	18	512,316	167,217
Investment income		118,364	104,016
Interest income		148,826	162,456
Other income	19	140,701	74,377
		1,385,130	904,760
General and administrative expenses		13,464	12,209
Other costs and expenses	20	2,123	21,788
		15,587	33,997
Net profit for the year		1,369,543	870,763
Proposed appropriations:			
Statutory reserve	13	136,955	87,076
Directors' remuneration		65	65
Profit available for distribution	11	1,232,523	783,622
		1,369,543	870,763

The accompanying notes are an integral part of the financial statements

KUWAIT PETROLEUM CORPORATION
STATE OF KUWAIT

STATEMENT OF CASH FLOWS
For the year ended June 30, 1997

	1997 KD <u>(thousands)</u>	1996 KD <u>(thousands)</u>
Cash flows from operating activities		
Net profit for the year	1,369,543	870,763
Adjustments for:		
Depreciation	361	430
Realization of unamortized gain on assets	(39,856)	-
Provisions no longer required	(7,762)	(16,644)
Gain on sale of subsidiary	(21,925)	-
Investment income	(118,364)	(104,016)
Interest income	(148,826)	(162,456)
Net change in provision for subsidiaries' and associates' losses	-	(9,763)
Net results of subsidiaries and associates	(512,316)	(167,217)
Provision for employees' termination benefits	441	279
Operating profit before working capital changes	<u>521,296</u>	<u>411,376</u>
Decrease (increase) in trade receivables	16,112	(52,533)
Decrease in other receivables and prepayments	2	10,570
Decrease in inventories	25	57,719
(Increase) decrease in amounts due from subsidiaries	(35,019)	5,583
(Decrease) increase in amounts due to subsidiaries	(4,557)	125,167
Increase in net amounts due to Ministry of Oil	13,155	63,103
Increase (decrease) in trade payables	779	(156)
Increase (decrease) in other payables and accruals	<u>5,156</u>	<u>(6,138)</u>
Net cash from operating activities	<u>516,949</u>	<u>614,691</u>
Cash flows from investing activities		
Increase in neutral zone concession	(3,413)	(2,431)
Interest received	147,679	155,852
Dividends from subsidiaries, associates and other investments	226,099	154,283
Advance to Ministry of Finance	(168,596)	(154,748)
Repayment of subsidiaries' loans	251,133	-
Proceeds from sale of shares in sub-subsidiary	384,151	-
Net increase in investment in subsidiaries	(51,089)	(16,671)
Finance advances to subsidiary	136,681	(28,508)
Net proceeds from sale of subsidiary	45,494	-
Purchase of fixed assets	(293)	(316)
Net increase in investment in securities	<u>(314,375)</u>	<u>(225,471)</u>
Net cash from (used in) investing activities	<u>653,471</u>	<u>(118,010)</u>

(Continued on the following page)

KUWAIT PETROLEUM CORPORATION
STATE OF KUWAIT

STATEMENT OF CASH FLOWS
For the year ended June 30, 1997

	1997 KD <u>(thousands)</u>	1996 KD <u>(thousands)</u>
Cash flows from financing activities		
Increase in non-current liabilities	4,847	2,264
Profits distributed	<u>(783,622)</u>	<u>(729,588)</u>
Net cash used in financing activities	<u>(778,775)</u>	<u>(727,324)</u>
Foreign currency translation adjustments	<u>(75,267)</u>	<u>9,932</u>
Net increase (decrease) in cash and deposits at banks	316,378	(220,711)
Cash and deposits at banks at beginning of the year	<u>1,185,457</u>	<u>1,406,168</u>
Cash and deposits at banks at end of the year	<u><u>1,501,835</u></u>	<u><u>1,185,457</u></u>

The accompanying notes are an integral part of the financial statements

KUWAIT PETROLEUM CORPORATION
STATE OF KUWAIT

NOTES TO THE FINANCIAL STATEMENTS
June 30, 1997

1. Organization and activities

Kuwait Petroleum Corporation (the Corporation) is wholly owned by the Government of the State of Kuwait. The Corporation was established by the Law Decree No. 6 of 1980 which came into effect on January 27, 1980. The Corporation's principal activities include exploration, drilling, production, storage, refining, processing, transportation, distribution and marketing of crude oil, natural gas, chemical, petrochemical and associated products. All of the Corporation's activities, except for marketing of Kuwait crude oil and petroleum products, are carried out through its subsidiaries and associates. The principal subsidiaries and associates are set out in Note 26.

Crude oil produced in the State of Kuwait becomes the property of the Government of Kuwait, which reimburses the production costs of the producing subsidiary. The Corporation purchases crude oil and natural gas from the Government of Kuwait in accordance with the terms of the Decree issued on January 17, 1981.

With effect from July 1, 1995, the Corporation entered into a commercial processing agreement with one of its subsidiaries, Kuwait National Petroleum Company (KNPC), whereby the Corporation sells crude oil and feedstock to KNPC for refining, and then buys back from KNPC refined products. Prices for these transactions are determined by the agreement.

In addition, and as part of the agreement, the Corporation sold all the stock of crude oil and petroleum products held at the refineries on July 1, 1995 to KNPC.

2. Significant accounting policies

The financial statements are prepared in accordance with Law Decree No. 6 of 1980 and International Accounting Standards. Significant accounting policies are summarized as follows:

a. Accounting convention

The financial statements are prepared under the historical cost convention.

b. Depreciation

The cost of fixed assets is depreciated on a straight-line basis over the expected useful lives of the assets.

c. Investments

Investments are valued as follows:

- Managed portfolios at the lower of aggregate cost or market value.
- Treasury bills at cost. Any premium or discount on issue is amortized, on a straight-line basis, from the date of purchase until maturity.
- Non-marketable securities at cost less provision for any permanent decline in value of such securities.
- Subsidiaries and associates in accordance with the equity method of accounting, with provision being made for losses incurred by such entities.
- Neutral zone production concession assets at cost.

d. Inventories

Crude oil is valued at the lower of average cost or market value at year-end. The cost of crude oil to the Corporation is determined by the Government of Kuwait in accordance with the Decree issued on January 17, 1981.

Liquefied petroleum gas and finished products are valued at the lower of cost or net realizable value. Cost is determined using the weighted average method on an individual product basis.

e. Employees' termination benefits

Provision is made for amounts payable to employees under the Kuwait Labor Law, Kuwait Social Security Law and the Corporation's terms of employment.

f. Petroleum personnel provident fund scheme

Provision is made for the Corporation's and its Kuwait subsidiaries' contribution to the petroleum personnel provident fund scheme in accordance with the terms of the provident fund plan for Kuwaiti personnel employed in the oil sector, which represents a defined benefit plan.

g. Foreign currencies

Foreign currency transactions are recorded in Kuwaiti Dinars at the previous month's average rates of exchange. Monetary assets and liabilities denominated in foreign currency at the balance sheet date are translated to Kuwaiti Dinars at the rates of exchange prevailing on that date. Exchange differences arising from the translation of the financial statements of subsidiaries and associates together with loans that, in substance, form part of the Corporation's net investment in such entities are accumulated in a separate component of owner's equity (foreign currency translation adjustments) until the disposal of the subsidiary or associate. Other exchange differences are reported as part of the results for the year.

h. Sales

Sales are recognized at the date title passes to the customer in accordance with the contract of sale.

3. Cash and deposits at banks

	1997 KD (thousands)	1996 KD (thousands)
Cash and current accounts at banks	106	89
Short-term deposits at banks	1,501,729	1,185,368
	<u>1,501,835</u>	<u>1,185,457</u>

4. Inventories

	1997 KD (thousands)	1996 KD (thousands)
Finished petroleum products	8,354	6,193
Crude oil	95,576	97,762
	<u>103,930</u>	<u>103,955</u>

5. Other receivables and prepayments

	1997 KD (thousands)	1996 KD (thousands)
Sundry receivables	7,880	8,355
Accrued income	28,910	26,494
Prepaid expenses	1,254	1,403
Deferred expenses	2,481	1,859
	<u>40,525</u>	<u>38,111</u>

6. Securities

	1997 KD (thousands)	1996 KD (thousands)
Managed portfolios	1,926,825	1,378,128
Treasury bills and bonds	100,666	334,988
	<u>2,027,491</u>	<u>1,713,116</u>
Provision for decline in value of managed portfolios	-	(7,762)
	<u>2,027,491</u>	<u>1,705,354</u>

7. Loans to subsidiaries

	1997 KD (thousands)	1996 KD (thousands)
KP North Sea Holdings Limited	-	172,281
Subsidiaries of Petrochemical Industries		
Holdings N.V.	680,551	759,403
	<u>680,551</u>	<u>931,684</u>

The above loans are denominated in foreign currencies. The repayment terms of the loans extend beyond June 30, 1998 with interest rates varying from nil to 8.3% per annum.

8. Finance advances to subsidiary

	1997 KD (thousands)	1996 KD (thousands)
Balance at beginning of the year	544,653	482,966
Advances to finance capital projects	61,407	24,791
Repayment of capital advances	(84,850)	(76,342)
Amounts (repaid) advanced to purchase opening oil inventories based on new agreement	(113,238)	113,238
Balance at end of the year	<u>407,972</u>	<u>544,653</u>

Finance advances consist of advances for capital projects and purchase of inventories by KNPC. No interest is charged on amounts advanced to finance major capital projects. As agreed with KNPC, amounts advanced to finance capital projects are repaid in line with the related depreciation charge for the major capital projects.

9. Other payables and accruals

	1997 KD (thousands)	1996 KD (thousands)
Payroll and annual leave	1,301	1,270
Marine payables	17,920	14,386
Other payables	4,571	2,915
	<u>23,792</u>	<u>18,571</u>

10. Amounts due to Ministry of Oil

Amounts due to the Ministry of Oil represent the net amounts payable for purchases of crude oil and natural gas, and certain activities performed by the Corporation and its subsidiaries on behalf of the Ministry of Oil (as described in Note 21). Production costs, including extraordinary items of Kuwait Oil Company K.S.C., are charged to this account.

During the year ended June 30, 1993, an agreement was reached with the Ministry such that part of the costs charged to the Ministry resulting from the Iraqi invasion would be repaid over a period of thirty-six months. The repayment is in the form of a monthly deduction from the cost of crude oil supplied by the Ministry to the Corporation. The remaining five installments which were outstanding as of June 30, 1995 were paid during the year ended June 30, 1996.

11. Profit available for distribution

	1997 KD (thousands)	1996 KD (thousands)
Balance at beginning of the year	783,622	729,588
Profit distributed during the year	(783,622)	(729,588)
Profit for the year available for distribution	1,232,523	783,622
Balance at end of the year	<u>1,232,523</u>	<u>783,622</u>

12. Other non-current liabilities

Other non-current liabilities represent amounts transferred from local subsidiaries. The amounts are interest free and do not have a fixed repayment date.

13. Statutory reserve

	1997 KD (thousands)	1996 KD (thousands)
Balance at beginning of the year	485,789	398,713
Transfer for the year	136,955	87,076
Balance at end of the year	<u>622,744</u>	<u>485,789</u>

As required by Article 12 of the Law Decree No. 6 of 1980, 10% of net annual profit is transferred to statutory reserve. Such transfers discontinue when the reserve equals half the capital.

14. Capital reserve

The capital reserve mainly represents the difference between the Corporation's cost of acquisition of its original subsidiaries, which were transferred by the Government of Kuwait, and their net asset values at December 31, 1979.

15. General reserve

As required by Article 12 of the Law Decree No. 6 of 1980, 10% of the annual profit was appropriated to general reserve. This appropriation ceased with effect from June 30, 1995.

16. Provision for replacement and renewal of fixed assets

	1997 KD (thousands)	1996 KD (thousands)
Balance at beginning and end of the year	<u>1,298,691</u>	<u>1,298,691</u>

Article 10 of the Law Decree No. 6 of 1980 states that the Corporation may provide an amount of its profits to meet the costs of replacement and renewal of the Corporation's and its subsidiaries' fixed assets, after approval of the Supreme Council for Petroleum. The provision is based on the difference between depreciation, calculated on the historical cost of fixed assets of the Corporation and its Kuwaiti subsidiaries, and depreciation calculated on the replacement cost of the assets using their insured values. No appropriations were made for the years ended June 30, 1994 through 1997.

17. Foreign currency translation adjustments

	1997 KD (thousands)	1996 KD (thousands)
Balance at beginning of the year	249,969	331,651
Net exchange differences for the year	(95,687)	(81,682)
Balance at end of the year	<u>154,282</u>	<u>249,969</u>

18. Net results of subsidiaries and associates

This amount represents the Corporation's share in the net results of subsidiaries and associates as follows:

	1997 KD <u>(thousands)</u>	1996 KD <u>(thousands)</u>
Kuwait National Petroleum Company K.S.C.	132,428	81,879
Kuwait Oil Tanker Company S.A.K.	18,352	8,431
Petrochemical Industries Company K.S.C.	30,737	39,990
Kuwait Foreign Petroleum Exploration Company K.S.C.	14,399	4,958
Kuwait Aviation Fuelling Company K.S.C.	5,597	4,298
Kuwait Santa Fe for Engineering and Petroleum Projects Company - K.S.C.	362	452
SFIC Holdings (Cayman) Inc.	293,130	24,439
KP North Sea Holdings Limited	-	24,294
Kuwait Petroleum Corporation (Liberia)	(2)	(1)
Kuwait Petroleum Corporation (Western Hemisphere)	19	107
Kuwait Petroleum Corporation (Far East)	31	(2)
Gulf Industrial Investment Company E.C.	7,675	8,139
Petrochemical Industries Holdings N.V.	(3,095)	2,594
Compagnie d'Investment dans les technologies Avancees	1,585	2,117
KPC Holdings (Aruba) AEC	10,837	(34,798)
Kuwait Drilling Company K.S.C.	261	320
	<u>512,316</u>	<u>167,217</u>

Included in the Corporation's share in the net results of SFIC Holdings (Cayman) Inc. is the gain of US \$ 788 million (KD 237 million) realized on the issuance in an initial public offering of 40 million shares of SFIC Holdings' subsidiary, Santa Fe.

19. Other income

	1997 KD <u>(thousands)</u>	1996 KD <u>(thousands)</u>
Recovery of financing costs	56,731	56,514
Gain on sale of subsidiary	21,925	-
Provisions no longer required	7,762	16,644
Miscellaneous income	54,283	1,219
	<u>140,701</u>	<u>74,377</u>

The gain on sale of subsidiary relates to the sale of KP North Sea Holdings (KPNSH) effective July 1996.

On formation of KPNSH, certain fixed assets relating to SFIC Holdings (Cayman) Inc. were sold to KPNSH at a price that exceeded the net book value of the assets. That excess was being amortized to income over the remaining useful lives of the assets. Miscellaneous income includes the unamortized balance of KD 39.8 million which was realized on the sale of KPNSH.

20. Other costs and expenses

	1997 KD (thousands)	1996 KD (thousands)
Provision for doubtful debts	2,066	154
Financial charges	45	-
Prior year expense	-	546
Foreign currency exchange loss	-	21,088
Other expenses	12	-
	<u>2,123</u>	<u>21,788</u>

21. Activities on behalf of the Ministry of Oil

The Corporation and its subsidiaries perform certain activities on behalf of the Ministry of Oil primarily in relation to: (a) the exploration for and production of crude oil and natural gas in the State of Kuwait, and (b) the local marketing (within the State of Kuwait) of refined products and liquefied petroleum gas.

22. Financial instruments

In the normal course of business, the Corporation uses primary financial instruments such as cash and deposits, investments, receivables and payables. The Corporation does not make use of derivative financial instruments.

- Fair values

Except for managed portfolios whose fair value amounted to KD 1.9468 billion at June 30, 1997, the carrying amounts of financial instruments approximate their fair values due to the short maturities and the nature of such instruments.

- Credit risk

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation causing the other party to incur a financial loss. The financial instruments which potentially subject the Corporation to credit risk consist of cash and deposits at banks, investments and receivables. The Corporation's bank balances and investments are placed with highly reputed financial institutions. The Corporation deals mainly with major international, state owned and large independent oil companies, and all receivables are presented net of allowance for doubtful debts.

Interest rate risk

Deposits at banks are mainly denominated in U.S. Dollars and Kuwaiti Dinars. The deposits earn interest between 5 % to 7.5 % p.a. and mature within 3 months to 1 year from the balance sheet date.

23. Segment information

The Corporation operates substantially in only one geographical segment, the State of Kuwait, and in one business segment, the marketing and distribution of petroleum products.

24. Contingent asset

The Corporation is pursuing claims against Iraq for the recovery of losses suffered by the Corporation during the Iraqi invasion. The accompanying financial statements do not include amounts related to these potential claims.

25. Comparative figures

Certain of the prior year amounts have been reclassified to conform with the current year presentation.

26. Subsidiaries and associates

a) Principal directly and wholly-owned subsidiaries incorporated in the State of Kuwait

	Authorized Capital KD (thousands)	Paid-up Capital KD (thousands)	Shareholder's equity KD (thousands)	Principal activities
Kuwait Oil Company K.S.C.	30,188	30,188	639,757	Exploration for and production of crude oil and natural gas in the State of Kuwait including processing and export.
Kuwait National Petroleum Company K.S.C.	260,000	260,000	381,668	Refining, LPG manufacturing, export and local marketing of refined products.
Kuwait Oil Tanker Company S.A.K.	200,000	200,000	215,606	Operations of a fleet of crude oil tankers and liquefied petroleum gas and oil product carriers.
Petrochemical Industries Company K.S.C.	315,000	315,000	323,488	Production of petrochemical products and their distribution and marketing.
Kuwait Foreign Petroleum Exploration Company K.S.C.	200,000	200,000	133,018	Exploration and development of oil and gas outside the State of Kuwait.

Kuwait Santa Fe for Engineering and Petroleum Projects Company K.S.C.	1,000	1,000	2,968	Principal activities
				Provision of design, engineering and related services to the petroleum industry.
Kuwait Aviation Fuelling Company K.S.C.	30	30	10,179	Supply of aviation fuel.

b) Principal directly and wholly-owned subsidiaries incorporated outside the State of Kuwait

	Country of incorporation	Paid-up Capital KD (thousands)	Shareholder's equity KD (thousands)	Principal activities
SFIC Holding Inc.	(Cayman) Cayman Islands	14	181,956	International contract drilling.
KP Holdings (Aruba) AEC	Aruba	602,238	413,543	Refining and marketing of refined products.

	<u>Country of incorporation</u>	<u>Paid-up Capital KD (thousands)</u>	<u>Shareholder's equity KD (thousands)</u>	<u>Principal activities</u>
Petrochemical Industries Holdings N.V.	Netherlands Antilles	9,697	(201,849)	Investment in other companies and financing activities.
Gulf Industrial Investment Company (E.C.)	Bahrain	36,070	41,178	Production of iron ore pellets.

c) Principal associates

<u>Name of Company</u>	<u>Country of incorporation</u>	<u>Proportion held</u>	<u>Nature of business</u>
Kuwait Drilling Company K.S.C	Kuwait	49%	Contract drilling.