Kuwait Foreign Petroleum Exploration Company K.S.C.

Exploring the World for Kuwait

Egypt, Tunisia, Sudan

Yemen

Pakistan

China, Indonesia

seventeenth

ANNUAL REPORT 1998

Australia

OUR HERITAGE

Kuwait Foreign Petroleum Exploration Company K.S.C. (KUFPEC), formed in April 1981, is a wholly-owned subsidiary of the Kuwait Petroleum Corporation (KPC) which is the holding company for the Kuwaiti oil sector. KPC is in turn wholly-owned by the Government of the State of Kuwait, and reports to the Government through the Supreme Petroleum Council. KUFPEC carries out its mission through subsidiaries incorporated in various countries worldwide.

OUR MISSION

The mission of KUFPEC as an integral part of KPC Group and as a Kuwaiti company is:

- To explore for, acquire, develop, produce and market hydrocarbon resources outside the State of Kuwait in an ultimately profitable manner.
- To develop the professional and technical abilities of all employees and particularly Kuwaiti nationals.
- To promote the interests and the image of the State of Kuwait in the countries in which it operates.

OUR VALUES

KUFPEC seeks to conduct all its operations and dealings with its co-venturers, associates and employees in accordance with the highest ethical standards, with a sincere concern for the effect of its activities on the environment and a commitment to develop and compensate its staff and contractors whoever and wherever they may be throughout the world in a fair and reasonable manner.

OUR RECORD

KUFPEC is active in eight countries, with established and profitable production operations in six of these. The Company employs 158 personnel, providing substantial employment for Kuwaiti nationals and local contractors and personnel in its foreign operations, and clean, efficient energy for consumers on three continents.

Contents

SUPREME PETROLEUM COUNCIL

KUWAIT PETROLEUM CORPORATION

Kuwait Foreign Petroleum
Exploration Company K.S.C.

Glossary

The following abbreviations are used in this report:

boe:	barrel of oil equivalent
boe/d:	barrel of oil equivalent per day
bpd:	barrels of oil per day
bcf:	billion cubic feet (of gas)
mscf:	thousand standard cubic feet (of gas)
mmscf:	million standard cubic feet (of gas)
mmscf/d:	million standard cubic feet per day
stb:	stock tank barrels
stb/d:	stock tank barrels per day
NGL's:	natural gas liquids

One barrel of oil is the energy equivalent of approximately 5.8 mscf of natural gas.

One Kuwaiti dinar is equivilent to about USD 3.3 as of December 31, 1998.

SUMMARY OF OPERATIONAL ACTIVITIES

Producing Inserts		Reserve Type	Wells Completed 1998	Wells Planned 1999	Operator	KUFPEC Working Interset	Total Field Production	KUFPEC Net shar (boe/d)
Yacheng, China	*	Gas	-	-	ARCO	14.70%	313.0 mmscf/d	9,862
Sidi El-Kilani, Tunisia		Oil	-	2	KUFPEC/KPC	45.00%	14,702 bpd	6,616
Harriet and Agincourt, Australia	*	Oil&Gas	6	7	Apache	19.28%	57.8 mmscf/d	1,920
							9,826 bpd	1,894
Anoa, Natuna A Block, Indonesia	*	Oil&Gas	3	3	Premier	33.33%	5,093 bpd	2,013
Jannah Block, Yemen		Oil	-	8	Hunt	20.00%	18,538 bpd	1,820
Kadanwari, Pakistan		Gas	1	1	LASMO	15.79%	70.7 mmscf/d	1,926
Yombo, Congo (Divested 1998)	*	Oil	n/a	n/a	CMS NOMECO	6.25%	n/a	-
Amal, Egypt (Divested 1998)	*	Oil	n/a	n/a	AMAPETCO	73.50%	292 bpd	101
East Shabwa Block, Yemen		Oil	4	8	TOTAL	14.29%	16,340 bpd	1,915
		TOTAL:	14	29				28,067

Total sales for the year: 10.492 mm boe, comprising 5.47 million barrels of oil, and 29.15 bcf of gas (1997: 11.455 mm boe)

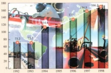
Non-Producing Interests	Reserve Type	wells completed 1998	wells planned 1999	Operator	KUFPEC Working Interest	Due Onstream
Ras El-Kanayes, Egypt	Gas	-	1	Repsol	36.36%	2000
Ras El-Hekma, Egypt	Gas	1	-	Repsol	36.36%	-
Seram Island, Indonesia	Oil	2	1	KUFPEC	92.5%	2001
North Kairouan Permit,Tunisia	Oil	-	1	KUFPEC	100%	-
Block B, Sudan	Oil	-	-	TOTAL	27.78%	-
	TOTAL:	3	3			

Legend:*- Offshore; •- First full year of Production; KPC-Kairouan Petroleum Company

Drilling Programme 1998	No. of Wells	Name	Country
Exploration wells			
Natuna Sea Block A	1	Pelikan-1	Indonesia
Ras El Hekma	1	JB 29-2	Egypt
	5	Koombana-1	Australia
		Gipsy-1	Australia
		Peck-1	Australia
		N.Harriet-1	Australia
		Rose-1	Australia
Appraisal wells			
Harriet	1	Rose-2	Australia
Seram	2	Oseil-2,4	Indonesia
Development wells			
East Shabwa	4	Kharir I 1,2,3,3.2,3.3	Yemen
Kadanwari	1	Kadanwari-10	Pakistan
Natuna Sea Block A	2	Natuna A18, A19	Indonesia

KUFPEC has a diversified portfolio of proven and probable reserves of 163.78 million boe, split 70% gas and 30% oil

Growth, Efficiency, Cash and Profitability

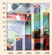


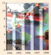
Shareholder Equity

In the face of record low oil prices and the worst oil glut in decades, KUFPEC demonstrated impressive flexibility. Profits for the year were KD 15 million and production averaged 28,067 boe/d.

Net Profit

Million Dinar



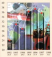


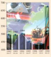
Net Production

Million boe

Although well below the previous year's record performance on both counts, 1998 performance remains above that of 1996 and all previous years and leaves the Company in an excellent position for future developments. The Company looks to the future from a solid cash position. Reserves, cash and short-term deposits, rose by year-end to a record high of U.S.$ 216-million, leaving the Company

Oil and Gas Reserve





in an excellent position for funding current commitments and new ventures. Following divestment of low-yield interests, the Company has planned an aggressive exploration and development campaign for 1999 to build reserves, increase operating efficiency and improve value in our core properties.

His Highness Sheikh Saad Al -Abdullah Al- Sabah
The Crown Prince and Prime Minister
of The State of Kuwait

His Highness Jaber Al-Ahmed Al-Sabah
The Amir
of the State of Kuwait

MESSAGE FROM THE Chairman

of the Board of Directors

MESSAGE FROM THE CHAIRMAN

It gives me great pleasure to report KUFPEC's continued delivery of value to the Shareholder, Kuwait Petroleum Corporation: profits for 1998 were KD 15 million (U.S.$ 51.6 million). With the close of the Company's fifth consecutive year of profitability, our cash position has been greatly augmented, assuring our ability to deliver exceptional strategic value.

Despite the Company's overall positive performance, 1998 was not a good year generally for the petroleum industry. The dramatic fall in oil prices, and lackluster medium-range and short-range price forecasts, have encouraged the Company to streamline operations. KUFPEC sold its production operations in Egypt and the Congo to pursue potentially more lucrative areas such as Indonesia's Seram Island and Anoa gas field.

The Company is aggressively building new pipelines with a view of increasing the value of our core properties. Following the example of the highly profitable South China Sea developments, new pipeline projects in Tunisia, Australia and Indonesia will enhance the value of our products, reduce transportation costs and, perhaps most importantly, cement relationships with our international co-partners and clients. Every yard of pipeline developed enhances KUFPEC's direct involvement in discovery, development and sales. With that, we increase the satisfaction of our customers and the international reputation of the Company and Kuwait.

The Company's relationships with our international partners and host country governments remain of foremost importance in all our business dealings. Throughout our areas of operation, KUFPEC prides itself in being a reliable, efficient and trustworthy co-partner and an exemplary corporate citizen.

Within Kuwait, the Company continues to take immense pride in the opportunities we provide to our national manpower. The intensive development of our human resources, ensuring that all employees achieve their maximum potential, guarantees that the Company will maintain the world-class management and technical staff that are required for the international marketplace.

In closing, I extend my profoundest appreciation to the Government Ministries of Kuwait, to our Shareholder, Kuwait Petroleum Corporation, to our sister companies within the KPC Group for their unfailing cooperation and dedication. And also, I extend thanks to each and every loyal KUFPEC employee for making the Company's continued success possible. May Almighty God continue to protect our beloved Kuwait, to bless it with continued success, progress and prosperity under the guidance and leadership of His Highness the Amir, and his faithful Heir Apparent.

Mahmoud Al-Rahmani
Chairman and Managing Director

Directors' Report on Activities

Year Ended December 31,1998

DIRECTORS' REPORT

The Directors are pleased to report a dynamic and profitable corporate performance for the year. In the face of an abrupt plunge of oil prices - to a more than 25-year low in real terms - the Company proved highly resilient and delivered a substantial after-tax profit of KD 15 million (U.S.$ 51.6-million). The Company ends the year in a very strong financial position. With a positive cash flow of KD 16.4 million (U.S.$ 56.0 million), KUFPEC's cash and short-term deposits, including those held by our parent, rose to KD 65.1 million (U.S.$ 216 million). The Company remains fully capable of funding all current commitments and is in an ideal position to acquire interests in new ventures in the near future.

Highlights

The Company's top performing interests, in relation to revenue, were the Yacheng field in the South China Sea, followed by Sidi El-Kilani in Tunisia, the Harriet field in Australia and Anoa in Indonesia. However, individual output of both Harriet and Anoa were exceeded by the combined performance of the Company's Jannah and East Shabwa fields in Yemen.

Revenues from KUFPEC's interests in Yemen are expected to increase further in 1999 as the Jannah and East Shabwa fields should respectively become the Company's third and fifth most lucrative properties. Collectively, revenue generated by the Yemeni fields should exceed that of Sidi El-Kilani in Tunisia.

Production, Exploration and Reserves

The increasing value of our interests in Yemen is the result of some of this year's most significant achievements: production commenced in the Kharir, Atuf NW and Wadi Taribah fields and production facilities were completed in the Halewah and Dhahab fields.

The year saw several substantial developments and discoveries, which will enhance the value of other properties in the near future. In Australia, development of the Wonnich gas field started and commercial quantities of gas and condensate were discovered in the Rose-1 well. In Indonesia, sales agreements were completed for gas from Natuna Block A, allowing for future development of Anoa gas field reserves. In Tunisia, the installation of an export pipeline in 1999 will lead to increase product value and a greater return on investment.

As a part of the KUFPEC's strategy of concentrating activities on core properties, the Company divested interests in two low-yield properties in Egypt and the Congo. At year's end, KUFPEC's portfolio consisted of seven producing properties, three developing properties, one appraisal property and a number of discoveries yet to be evaluated.

Collectively, KUFPEC's properties produced 28,067 boe/d and close to the budgeted forecast of 28,153 boe/d.

Directors' Report on Activities

Pipeline Properties

The Pipeline, a symbol of Value, Service and Commitment

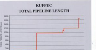
KUFPEC is dedicated to providing low-cost, clean and efficient energy to our customers throughout the world. Nothing demonstrates this commitment more than the Company's aggressive development of, and partnership in, several pipeline projects in our major producing areas.

Since the 1992 launch of our first pipeline - the 100-kilometer 12 - inch, Harriet Joint Venture offshore pipeline - the Company has seen improved revenues and has forged stronger relationships with our clients, our partners and with host country governments.

The cost savings of our pipeline projects are exemplified in one of our most recent developments, the 123-kilometer, 8-inch pipeline from Sidi El-Kilani to La Skhirra in Tunisia. By eliminating the need for transporting oil by truck, the pipeline will save approximately (U.S.$ 1.00 per barrel) on operating costs. With additional capacity to transport oil from future discoveries, the pipeline will also increase the value of any new developments in the area.

As well as cost savings and tariff revenues, the 16-inch Harriet undersea pipeline in the Company's Australian properties has produced stronger relationships. Once distant properties have been transformed into valuable assets as this pipeline has bridged the 100-kilometer gap between the Company and its customers. This direct and reliable connection has increased customer satisfaction and solidified KUFPEC's and Harriet partners reputation as a reliable gas supplies.

The Australian pipeline has provided for tariff revenue, as other operators in the area share in its use and it has made possible the development of several recently discovered gas fields, including the Wonnich field, which will be connected



in 1999.

Nowhere has the Company's reputation been enhanced more than in our most profitable venture, the world-class Yacheng undersea gas pipeline in the South China Sea, the second longest undersea gas pipeline in the world. The 778-kilometer, 28-inch diameter connection between the Yacheng fields and the territory of Hong Kong cuts through typhoon-prone waters guaranteeing that the territory's power needs will be met until well into the 21st Century.

By early into the new century, less than ten years since the construction of the first 100-kilometer pipeline, the Company will have overseen the development of over 1650-kilometers of new development on three continents. By adding value to our product, cementing partnerships and maximizing the potential of our core properties, these pipelines will help to assure the long-term profitability of the Company and continued delivery of value for the Shareholder.

	YACHENG	YACHENG	HARRIET	HARRIET-E SPAR	NATUNA BLOCK A	SIDI EL KILANI
LOCATION TO	Hong Kong	Hainan Island	I) Dampier-Bunbury Natural Gas Pipeline. II) Goldfields Gas Transmission Pipeline.		Singapore	La Skhirra
SUBSEA OR LAND	Subsea	Subsea	Subsea	Subsea	Subsea	Land
SIZE (inches)	28"	14"	12"	16"	28"	8"
LENGTH (km)	778km	91km	100km	100km	471km	123km
CAPACITY	520mmscf/d	140mmscf/d	170mmscf/d	295mmscf/d	600mmscf/d	24,000 bpd
OIL/GAS	Gas	Gas	Gas	Gas	Gas	Oil
DATE COMMISSIONED OR TO BE COMPLETED	Sept 1995	Sept 1995	July 1992	April 1999	April 2001	March 1999
INTEREST OWNERS	KUFPEC 14.7% ARCO 34.3% CNOOC 51.0%	KUFPEC 14.7% ARCO 34.3% CNOOC 51.0%	HJV 100%	HJV 30% ESJV 70%	NATUNA SEA BLOCK B 36.19% KAKAP BLOCK 22.24% NATUNA SEA BLOCK A 41.39% • PREMIER 27.39% • KUFPEC 13.00%	KUFPEC 45% ETAP 55%
REMARKS	The Hong Kong Pipeline is the second longest offshore gas P/L and throughput can be increased to 760 mmscf/d with installation of an intermediate compressor station. The pipeline provides gas storage and allows for continuous delivery of gas during periods (a few days) of production downtime.	Transports gas and condensate to Hainan Island.	Harriet Joint Venture owns 100% and has entered into a contract with East Spar for East Spar to use spare capacity by paying a tariff.	This line will be used jointly by E spar Joint Venture and Harriet Joint Venture for gas sales and potentially by third parties who will pay a tariff.	Est. Cost: $424 million. This gas pipeline is being built by three permit (PSC) holders in the Natuna Sea for joint use for gas sales to Singapore.	Pipeline will eliminate the requirement for trucking oil and save approx. U.S. $ 1.00/ barrel operating cost. The pipeline has spare capacity to transport oil from further discoveries in North Kairouan and has potential to earn tariff revenue for the transport of third party oil.

Directors' Report on Activities

China, Yacheng

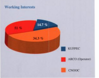
China, Yacheng

The Company's largest revenue generator, the (U.S.$ 1.1 billion) Yacheng offshore gas project, continued to provide Hong Kong and China with clean and efficient energy.

This was the third operational year for the 778-kilometer 28-inch undersea gas pipeline to the buyer, Castle Peak Power Company, and for the 91-kilometer 14-inch undersea pipeline to Hainan Island. Production expectations for the year were met with gas sales averaging 313 mmscf/d and 1,405 stb/d of condensate. Similar production rates of 315 mmscf/d and 1,259 stb/d of condensate are forecast for 1999.

During the year, KUFPEC's South China Sea operations generated over one-third of the Company's total revenue and almost 80 percent of revenues from gas sales. The pipeline's 40-year operational life and our solid relationship with our clients, CAPCO and FCCH, and our co-venturers, ARCO and the China National Offshore Oil Corporation, assure that the Yacheng fields will remain the Company's key investment

	1998	1997	1996
Gas sales mmscf/d	313	329	202



" Teamwork at it's best". Installation work at shorebase of Yacheng gas field.

for the foreseeable future.

During 1998 work commenced on reprocessing the 3D seismic survey and reservior engineering studies. These studies will provide greater definition of the structure, faults and reserves in order to select bottom hole locations for additional development drilling planned in early 2000 .

Directors' Report on Activities

Indonesia

Indonesia

The Company has two interests in Indonesia. Offshore, Natuna Sea Block A, contains the producing Anoa field and is located 1,200-km north of Jakarta, adjacent to the Indonesian Malaysian sea border. The onshore Seram Island concession, in Eastern Indonesia, contains the Oseil field.

Seram Island

1998 was a banner year for development of the Seram Island project. The Company successfully completed negotiations with the Indonesian government, extending the Production Sharing Agreement for up to 20 years beyond the previous expiry date of November 1999. KUFPEC also acquired the interests of its co-venturer, ARCO, raising the Company's interest in Seram operations to 92.5 percent. The other (co-venturs), Sherrit and SANTOS have retained their respective interests of 5 percent and 2.5 percent.

The drilling of two appraisal wells on the Oseil structure has raised the likelihood of the economic viability of oil development. The Oseil-2 well tested for 22 API oil at a rate of 650 stb/d. Oseil-4 tested at a rate of 6,300 stb/d.

The Oseil discoveries herald the first use of underbalanced drilling technology in South East Asia. The technology allowed the highly fractured carbonate reservoir to be drilled without loss of drilling fluid, and permitted the removal of cuttings as well as the identification of the thickness of the oil interval.

Considerable work is planned on the Seram field for 1999 including: completion of Oseil 1, 2 and 4, and the completion of Environmental and Front-End Engineering Design (FEED) studies. A crude value optimization study is underway to determine markets for Oseil crude and to determine the best options for pre-sale upgrading and sale value enhancement. Installation of production facilities in 2000, with first production in late 2000, is currently being planned.

Natuna Sea Block A

Significant progress was made in gas sale negotiations between the partners, Pertamina and the Singapore buyer, Sembawang

Preparing OSEIL-1 for installation of pressure gauge.

Engineering and Construction Pte Ltd. With a 22-year gas sale agreement to be signed in early 1999, gas production from Anoa will become increasingly important.

To accommodate the expected gas development and sales, Pertamina has granted the Company a 20-year extension on the current production sharing contract for Block A, which was previously set to expire in 2009. Gas sales should start in 2001 and are expected to reach a plateau of 120 mmscf/d.

Tenders for construction of the 28-inch, 580-km, subsea pipeline and associated laterals to the connecting field were issued late in the year. The contract should be awarded in early 1999.

Lower than expected downtimes resulted in an average daily oil production rate for the year of 5,093 stb/d, exceeding the forecast of 4,338 stb/d. Successful development drilling during 1998 is expected to result in an average daily production rate of 6,206 stb/d for 1999..

Directors' Report on Activities

Australia

Australia

The great potential of the Harriet group of fields, located 70 kilometers offshore Western Australia, moved closer to realization in 1998. New discoveries, sales contracts, field and pipeline development, and better than expected reservoir performance in the present year have encouraged plans for an aggressive drilling program in 1999.

Despite their potential, the development of the Harriet fields, which include Harriet, Agincourt, Alkimos, Campbell, Rosette, Sinbad and Wonnich, was restricted in the past due to their remote location and distance from potential markets. This has changed rapidly as recent mining developments in Western Australia have created an ever expanding market and the domestic demand for natural gas is expected to double within the next decade.

In 1998 new supply contracts were signed with Great Central Mines, Boral Energy and Wiluna Gold Mines and sales to our existing clients- Alinta, Normandy Power Limited, Alcoa,EPIC Energy and Centaur Nickel- continued.

To satisfy a growing consumer base, the Company pursued an intense exploration and development program in 1998. Prospective structures were explored with the Shelly (3D) and Denise (2D) seismic surveys. Significant new explorations were made on prospects approximately ten kilometers east of the main Harriet field, which were discovered in the previous year's seismic surveys. The Gypsy-1 well discovered a new oil-bearing reservoir and the Rose-1 well yielded potentially commercial gas condensate reserves in three reservoirs. These were subsequently delineated by an appraisal well and a third exploration well, Lee-1, will test the third prospect early in 1999.

KUFPEC's interest in the nearby Varanus Island production processing facility, one of the few such facilities in the area, put the company in an excellent position in regard to future developments. Capacity of the Varnus Island facility is more than sufficient to handle all of KUFPEC's present and expected production. Also the facility earns additional tariff revenue

Work on new platform facilities for additional development of HARRIET area fields.

from other companies operating in the nearby fields.

The Company's capability to profit from economies of scale will be further enhanced with the completion of a 16-inch, 100-kilometer pipeline in 1999. This sub-sea pipeline will dramatically increase gas sale capacity and will allow the Company to gain further revenue from expected third party use. Gas is currently sent to the main transmission system through a 12-inch, 100-kilometer pipeline.

Development of the Wonnich gas fields continued through 1998 and the development will reach productive capacity by mid-1999. The Company's share of the Wonnich reserve is 34 bcf of gas, including oil. Production will be fed to the Varanus Island facility through a 30-kilometer pipeline and will enhance the value of both Wonnich and Varanus.

Daily production for the Harriet fields averaged 9,826 stb/d of oil and 57.8 mmscf/d of gas.

The area surrounding the Harriet fields will be the Company's single largest exploration venture in 1999. Seismic surveys, both 2D and 3D, will be performed over 850 kilometers and the drilling of up to eight new exploration wells is planned.

Directors' Report on Activities

Yemen

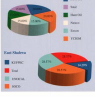
Yemen

The Company's investments in Yemen continue to grow in importance. Considerable field development in 1998 should pay off in the coming year as the combined oil production from the East Shabwa and Jannah fields is expected to make this program KUFPEC's second largest source of revenue by the end of the millennium.

East Shabwa

This was the first full year of production for the East Shabwa Block, which produced at an average daily rate of 16,164 stb/d. Positive performance has encouraged the Company to plan to continue with increased development work in 1999.

First phase development of the Kharir field was completed during 1998 with the drilling of three new oil development wells and one water injection well. Additional development of the Kharir field is planned for 1999 with the drilling of six oil development wells and two water injection wells. The Company plans to expand water handling from approximately 15,000 bwp/d to 50,000 bwp/d.



Phase two development of the Atuf field is scheduled for 1999 and will include the drilling of two additional oil development wells and one water injection well, which will enhance reserve recovery.

Production is exported through a 12-inch, 54-kilometer, pipeline connecting Kharir to Canadian Occidental's Masila Block Crude Oil Transfer Facility, and from there on to the Al-Mukalla export terminal in the Gulf of Aden.

Jannah

The Jannah Block includes the Halewah, Dhahab, Al Nasr, Aser and Jannah fields. In 1998, the Halewah and Dhahab fields produced at an average rate of 18,538 stb/d.

During 1998 gas injection facilities were installed at Dhahab and Long Term Production Phase (LTPP) facilities to handle production from all Jannah fields were installed at Halewah. The LTPP facilities provide for a crude processing capacity of 50,000 stb/d and also include gas injection compression for gas injection into the reservoir to maintain reservoir pressure maintenance. Additional plans for enhanced reserve recovery include the drilling of eight additional Halewah development wells in 1999.

The large Al Nasr field development continued during 1998 and the first phase is scheduled for completion during the first half of 1999 and the second phase late 1999. The second phase development will include water injection facilities and the expansion of crude gas and water separation facilities at Halewah to about 70,000 stb/d.

Production from the Jannah Permit is anticipated to increase in 1999 to an average rate of about 45,700 stb/d mainly due to the addition of production from the Al Nasr field..

Directors' Report on Activities

Tunisia

Tunisia

The Sidi El-Kilani oil field in the North Kairoun Permit is currently Tunisia's second-largest oil producer. The field showed a better- than- expected reservoir performance in 1998. The field produced at an average daily rate of 14,702 stb/d, approximately 2,000 stb/d more than predicted.

In terms of revenue generated, Sidi El-Kilani is the Company's top producing oil investment. In 1998 it produced approximately 44 percent of revenue from oil sales and 22 percent of the Company's total revenue. Production at Sidi El-Kilani is managed by Kairouan Petroleum Company, a 50/50 joint venture between KUFPEC and our co-venturer, Enterprise Tunisienne d'Activities Petrolieres (ETAP).

Oil production is trucked from Sidi El-Kilani with about 90 percent going to Compagnie Franco-Tunisienne des Petroles pipeline facilities at Sidi El-Itayem and the remainder directly to the La Skhirra Export Terminal. To increase production value, and reduce wellhead - to - market costs, the Company commenced construction of an 8-inch, 123-kilometer pipeline from Sidi El-Kilani to La Skhirra. The pipeline is scheduled to be completed in the first quarter of 1999. Its extended lifespan and through put capacity will easily accommodate any additional oil from expected future discoveries.

KUFPEC, is the sole exploration operator on the North Kairoun permit and ETAP can elect to participate, with up to 55 percent interest on any future discoveries. In 1998, the Exploration Permit has been extended for an additional year until July, 2000.

Development of the 123 kilometer pipeline from Sidi El-Kilani to La-Skhirra will reduce operating costs by about U.S.$ 1.00 per barrel.

	1998	1997	1996
Oil Production bpd	14,702	15,017	18,076

Working Interests

Operator: Kairouan Petroleum Company, a 50/50 joint venture between KUFPEC and ETAP

Discovery	April 1989
First Production	December 1992
Cumulative Production	29.89 Million Barrels

Directors' Report on Activities

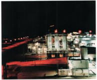
Pakistan

Pakistan

Performance at the Kadanwari gas field, located in the remote Tajjal Permit area 330-kilometers north-east of Karachi, was on par with that of the previous year. The field produced at an average daily sales rate of 70 mmscf/d same as the previous year.

The Company made significant progress on the project to install wellhead compression on three wells with completion expected in mid-1999. An additional development well, K-10, was drilled in 1998, confirming the presence of gas in a previously untested eastern fault block . K-10 production has commenced at a flow rate of 25 mmscf/d, and a further development well in this faulted block is planned for 1999.

In addition, in order to enhance the investment in field gas processing facilities, the Company along with Kadanwari joint veture partners entered into a letter agreement with the Miano group, operator of the nearby Miano field, to utilize the excess capacity available at Kadanwari's processing facilities. The additional processing of Miano gas at Kadanwari will reduce operating costs and extend the economic production life of the field, yielding positive results. A final decision on the proposal will be made in 1999 pending the confirmation of the Miano development, and sales gas contract with SSGC which is a Pakistany government utility company.



KADANWARI gas plant, Pakistan.

	1998	1997	1996
Gas Production mmscf/d	70.0	70.5	80.0
Wells Completed	1	1	1

Working Interests

Acquired	July 1987
Discovery	September 1989
First Production	May 1995

Directors' Report on Activities

Egypt and Sudan

Egypt and Sudan

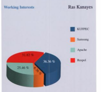
As well as interests in Tunisia, the Company retains interests in two other African properties: the Ras Kanayes field in Egypt and the largest exploration permit in Africa, located in southern Sudan.

Egypt, Ras Kanayes

The Ras Kanayes concession is located on the Mediterranean coastline in the Western Desert region, 200-kilometers west of Alexandria. Thus far the area has yielded three gas discoveries in wells Ja 26, Ja 27 and Ja 28.

During the year, KUFPEC and partners- Apache, Samsung and the operator, Respol- began development of the most promising field, Ja 27. A delineation well was drilled and development of gas reserves is scheduled for 1999- with first production scheduled for 2000.

The development plan calls for two wells from the Ja 27 field,



Siesmic Vibroseis unit in Ras Kanayes Permit-Egypt

which will yield approximately 25mmscf/d. Total reserves are estimated at 70.3 bcf gas and 5.2 mmstb of condensate, of which the Company's share is 12.6 bcf and 0.9 mmstb respectively. The Company is studying measures to increase reserves by raising the productivity of the Ja 26 and Ja 28 discoveries.

Sudan

KUFPEC retains a 27.78 percent working interest in a potentially lucrative 118,348 square kilometer property in southern Sudan. However, with continuing civil unrest in the area, concern for Company employees and property has postponed any new exploration or development.

The Company and our partners - TOTAL, Marathon and Sudan's Public Petroleum Corporation- hold a firm belief in the area's potential and remain hopeful that the situation will be stabilized.

Directors' Report on Activities

Adminstration and Staffing

Administration and Staffing

The Company's Head Office in the heart of Kuwait City continues to provide support to its management, three regional offices, customers and partners.

KUFPEC's policy of providing high-quality employment opportunities for Kuwaiti nationals reached an important milestone this year and the majority of head office personnel are now Kuwaiti. This represents a more than 30-percent increase since the beginning of the decade. To achieve the Company's long-term goal of attaining a full Kuwaiti workforce, especially within Kuwait, special emphasis continues to be given to advancing the skills of Kuwaiti nationals.

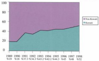
The Company continues to place the highest priority on the development of employees and management. The industry is increasingly knowledge-driven. By assuring that all employees remain abreast of the rapid advancements in development technology, management science and administrative processes- we assure the future of the Company.

The Company's close-knit, multinational, multi-disciplinary team remains a source of great pride. KUFPEC is dedicated to the development of all staff, at all levels- both inside Kuwait and in our regional offices.

The Future

Continued excess supply and lower than expected demand

Head Office Staff



Inhouse technical training course (KUFPEC Head Office)

indicate little room for improved oil prices in the short-term. As such, the Company is forecasting a profitable but restrained performance in 1999, with marginally lower revenues.

The streamlining of operations which began in earnest this year with the divestment of properties in the Congo and Egypt will be followed with the implementation of considerable development plans in core properties, particularly those in Indonesia, Australia and Yemen. This will result in a short-term negative cash flow for 1999. However it will increase the dynamism and value of the Company and its properties in the new millenium and KUFPEC's value to the shareholder.

The preceding five years of profitability have positioned the Company for increased growth, with ample reserves to cover operating expenses, exploration and development and acquisition of new ventures to allow for the replenishing of reserves.

While current producing interests assure that the Company will see positive revenues and profits well into the 21st century, the Company must re-invest in new exploration or acquisitions to replace the decline in current reserves. We will, in the meantime, continue to pursue our existing interests to the greatest extent possible with the full support of the Shareholder in all current and prospective relationships.

ARTHUR ANDERSEN AL-BAZIE & CO. PUBLIC ACCOUNTANTS

KUWAIT FOREIGN PETROLEUM EXPLORATION COMPANY K.S.C. (CLOSED) AND SUBSIDIARIES
STATE OF KUWAIT

The Shareholder
Kuwait Foreign Petroleum Exploration Company K.S.C. (Closed)
State of Kuwait

I have audited the accompanying consolidated balance sheet of Kuwait Foreign Petroleum Exploration Company K.S.C. (Closed) and Subsidiaries as of December 31, 1998, and the related consolidated statements of profit and loss and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. My responsibility is to express an opinion on these financial statements based on the audit.

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 provides a reasonable basis for my opinion.

In my opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Kuwait Foreign Petroleum Exploration Company K.S.C. (Closed) and Subsidiaries as of December 31, 1998, and the results of their operations and their 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 Commercial Companies Law and the Company's Articles of Association, 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 books of account. According to the information available to me, there were no contraventions during the year of either the Commercial Companies Law or of the Company's Articles of Association which might have materially affected the Group's financial position or results of its operations.

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

State of Kuwait
March 10, 1999

Consolidated Balance Sheet

Year Ended December 31, 1998

Exhibit A

	Note	1998 KD	1997 KD
ASSETS			
Current assets:			
Cash and short-term deposits		4,524,108	48,770,053
Funds held by parent	3	60,617,000	-
Accounts receivable and prepayments	4	8,034,441	8,870,099
Investment in unconsolidated subsidiary company	5	181,374	-
Inventories	6	3,346,490	5,283,350
Total current assets		76,703,413	62,923,502
Other non-current assets		26,187	23,449
Oil and gas properties:	7		
Producing properties		79,520,047	88,663,821
Work-in-progress		22,263,739	13,358,510
		101,783,786	102,022,331
Fixed assets:			
Cost		2,114,676	2,317,493
Less: Accumulated depreciation		(1,740,581)	(1,894,633)
		374,095	422,860
		178,887,481	165,392,142
LIABILITIES AND SHAREHOLDER'S EQUITY			
Current liabilities:			
Accounts payable and accruals	8	8,274,299	5,848,277
Provision for taxation		185,500	9,569
Due to parent and its subsidiary companies		415	14,742
Total current liabilities		8,460,214	5,872,588
Provision for restoration expenses	9	2,822,550	3,745,132
Other non-current liabilities		654,326	554,087
Provision for employees' terminal benefits		730,955	745,926
Shareholder's equity:			
Capital	10	200,000,000	200,000,000
Statutory reserve	11	1,824,126	1,824,126
Voluntary reserve		1,824,126	1,824,126
Foreign currency translation adjustments	12	5,267,230	8,557,144
Accumulated losses - Exhibit B		(42,696,046)	(57,730,987)
Total shareholder's equity		166,219,436	154,474,409
		178,887,481	165,392,142

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

Mahmoud Abdulla Al-Rahmani
Chairman and Managing Director

Khaled Abdulla M. Hussain
EAMD Finance, Administration, Commercial and

Consolidated Statement Of Profit And Loss

Year Ended December 31, 1998

Exhibit B

	Note	1998 KD	1997 KD
Income:			
Operations		43,292,027	52,570,973
Interest		4,204,780	2,455,134
Gain on sale of subsidiary and concession	13	3,605,199	-
Others		198,146	196,161
		51,300,152	55,222,268
Expenses:			
Operations		10,163,374	8,723,803
Exploration		3,539,799	4,899,965
General and administrative	14	2,471,792	2,716,205
Depreciation, depletion and amortization		16,375,905	17,495,051
Provision for restoration expenses	9	202,182	314,914
Foreign currency exchange loss		427,989	31,059
		33,181,041	34,180,997
Profit for the year before taxation		18,119,111	21,041,271
Taxation	15	(3,084,170)	(3,148,796)
Net profit for the year		15,034,941	17,892,475
Accumulated losses at beginning of the year		(57,730,987)	(75,623,462)
Accumulated losses at end of the year - Exhibit A		(42,696,046)	(57,730,987)

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

Consolidated Statement Of Cash Flows

Year Ended December 31, 1998

Exhibit C

	1998 KD	1997 KD
Cash flows from operating activities		
Profit for the year before taxation	18,119,111	21,041,271
Adjustments for:		
Depreciation, depletion and amortization	16,375,905	17,495,051
Write-offs of oil and gas properties	3,539,799	4,899,965
Loss on disposal of fixed assets	1,680	139
Gain on sale of subsidiary and concession	(3,605,199)	-
Interest income	(4,204,780)	(2,455,134)
Provision for restoration expenses	202,182	314,914
Provision for employees' terminal benefits	(14,971)	78,466
Operating profit before working capital changes	30,413,727	41,374,672
Decrease in accounts receivable and prepayments	501,237	7,241,943
Decrease (increase) in inventories	972,896	(1,219,095)
Increase in accounts payable and accruals	2,834,572	740,625
Cash generated from operations	34,722,432	48,138,145
Income taxes paid	(2,908,239)	(3,809,371)
Net cash from operating activities	31,814,193	44,328,774
Cash flows from investing activities		
Proceeds from sale of fixed assets	440	4,175
Purchase of fixed assets	(200,004)	(131,874)
Purchase of investment in unconsolidated subsidiary company	(181,374)	-
Proceeds from sale of subsidiary and concession	6,064,519	-
Increase in funds held by parent	(60,617,000)	-
Additions to oil and gas properties	(22,833,970)	(21,558,604)
Decrease in amounts due from joint venture participants	-	2,889,423
(Increase) decrease in other non-current assets	(5,962)	1,625
Interest received	4,081,272	2,053,525
Net cash used in investing activities	(73,692,079)	(16,741,730)
Cash flows from financing activities		
(Decrease) increase in amounts due to parent and its subsidiary companies	(14,327)	7,868
Effect of foreign currency translation	(2,353,732)	3,563,716
Net (decrease) increase in cash and short-term deposits	(44,245,945)	31,158,628
Cash and short-term deposits at beginning of the year	48,770,053	17,611,425
Cash and short-term deposits at end of the year	4,524,108	48,770,053

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

Notes to Consolidated Financial Statements

Year Ended December 31, 1998

1. Organization and nature of activities

Kuwait Foreign Petroleum Exploration Company (KUFPEC) K.S.C. (Closed) "the Company" was registered in Kuwait in 1981 as a wholly owned subsidiary of Kuwait Petroleum Corporation (KPC). It is engaged in the exploration and development of oil and gas outside Kuwait.

2. Significant accounting policies

a) **Accounting convention**
The financial statements are prepared under the historical cost convention.

b) **Basis of consolidation**
The consolidated financial statements incorporate the financial statements of KUFPEC K.S.C. (Closed) and its wholly owned subsidiary companies (Note 17). Subsidiaries are those companies which are controlled by KUFPEC K.S.C (Closed). Significant intercompany balances, transactions and profits are eliminated on consolidation.

c) **Oil and gas accounting**
Oil and gas exploration and producing activities are accounted for using the 'successful efforts' method of accounting. Under this method, geological and geophysical costs are expensed as incurred during the exploration phase. Exploratory drilling costs are tentatively capitalized pending determination of whether the well finds proved reserves. Wells which are assigned proved reserves remain capitalized. All other exploratory wells and exploration expenditure including licence fees are expensed. All expenditure for development, including seismic geological and geophysical studies, wells, related plant and equipment and mineral interest in properties is capitalized. Such expenditure is depreciated, depleted and amortized using the unit-of-production method.

Provision is made for restoration expenses related to abandonment of fields based on estimated costs over the estimated remaining commercial reserves of the relevant field on a unit-of- production basis.

d) **Ceiling test**
The net carrying amounts of oil and gas properties are assessed against the aggregate future net revenues expected to be derived from the estimated remaining commercial reserves. A provision is made where the capitalized costs of the properties are unlikely to be fully recovered from the future net revenue.

e) **Inventories**
Crude oil is valued at the lower of cost or net realizable value. Other inventories comprising mainly of spare parts, materials and supplies are valued at cost, determined principally on a weighted average cost basis, less allowance for any obsolete or slow moving items.

f) **Joint ventures**
Where the Group's oil and gas exploration and producing activities are conducted jointly with others, the financial statements reflect only the proportionate interest in such activities.

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

h) **Revenue recognition**
Revenue from the sale of oil and gas is recognized on completion of the sale transaction.

i) **Royalties**
Royalties are accounted for in the statement of profit and loss in the same period as the income to which they relate and are included within operating expenses.

j) **Foreign currencies**
Foreign currency transactions are recorded in Kuwaiti Dinars at the approximate rates of exchange prevailing at the time of the transactions. 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 are reported as part of the results for the year. Assets and liabilities, both monetary and non-monetary of foreign subsidiaries are translated at the exchange rates prevailing at the balance sheet date. Operating results of such subsidiaries are translated at average rates of exchange for the subsidiary's period of operations.The resulting exchange differences are accumulated in a separate section of shareholder's equity (foreign currency translation adjustments) until the disposal of the subsidiary.

Notes to Consolidated Financial Statements

Year Ended December 31, 1998

Significant accounting policies (Continue)

k) **Employees' terminal benefits**
Provision is made for amounts payable to employees under the Kuwait State Labor Law, the Kuwait Social Security Law and the Company's terms of employment. The provision is based on the accumulated period of service for each employee at the balance sheet date.

l) **Taxes on income**
Certain of the Company's subsidiaries are subject to taxes on income in various foreign jurisdictions. Taxes payable are provided on taxable profits at the current rate. Provision for deferred taxation is made for the timing differences between financial and income tax reporting, when required.

3. Funds held by parent

Funds held by parent represent surplus funds generated from operations and advanced to KPC. There are no restrictions on these funds and interest is earned based on the prevailing market rates.

4. Accounts receivable and prepayments

	1998 KD	1997 KD
Trade receivables	3,945,285	3,092,754
Other receivables	663,889	1,109,889
Accrued interest	587,270	463,762
Due from joint venture participants	2,530,384	3,833,764
Prepaid expenses	307,613	369,930
	8,034,441	8,870,099

5. Investment in unconsolidated subsidiary company

During the year, the Group acquired a 100% equity interest in Atlantic Richfield Seram Limited (ARCO), a company incorporated under the laws of the Bahamas and owns a 52.5% interest in the Seram joint venture. The subsidiary has been excluded from consolidation as it was acquired and held exclusively with a view to its disposal in the near future. In the opinion of management, the net realizable value of the investment is not less than its carrying amount which represents the cost of acquisition.

6. Inventories

	1998 KD	1997 KD
Crude oil	953,910	1,746,022
Spare parts, materials and supplies	2,392,580	3,537,328
	3,346,490	5,283,350

Spare parts, materials and supplies are used in operations and are not held for re-sale.

7. Oil and gas properties

	1998 KD	1997 KD
Cost:		
Balance at beginning of the year	203,609,242	186,950,603
Exploration and development expenditure during the year	24,698,978	18,339,388
Disposals	(33,069,832)	-
Write-offs	(3,539,799)	(4,899,965)
Currency translation effects	(1,865,008)	3,219,216
Balance at end of the year	189,833,581	203,609,242

Notes to Consolidated Financial Statements

Year Ended December 31, 1998

7. Oil and gas properties (continue)

Depreciation, depletion and amortization:

	1998 KD	1997 KD
Balance at beginning of the year	101,586,911	84,275,863
Charge for the year	16,134,640	17,311,048
On disposals	(29,671,756)	-
Balance at end of the year	88,049,795	101,586,911
Net book value	101,783,786	102,022,331

In accordance with the policy outlined in Note 2 (d), a ceiling test was carried out at December 31, 1998 using unescalated and undiscounted estimates of future net revenues derived from oil and gas prices, exchange rates and cost levels ruling at that date.

8. Accounts payable and accruals

	1998 KD	1997 KD
Joint venture accruals	7,322,690	4,753,768
Royalties payable	-	54,024
Withholding tax	185,214	132,936
Accrued payroll and leave pay	339,881	477,666
Others	426,514	429,883
	8,274,299	5,848,277

9. Provision for restoration expenses

	1998 KD	1997 KD
Balance at beginning of the year	3,745,132	3,430,218
Charged to profit and loss	202,182	314,914
Released on sale of permits	(1,124,764)	-
Balance at end of the year	2,822,550	3,745,132

10. Capital

Authorized, issued and fully paid up capital consists of 200,000,000 shares of KD 1 each (1997 - 200,000,000 shares).

11. Statutory reserve

This reserve is not available for distribution except in cases stipulated by law and the Company's Articles of Association

12. Foreign currency translation adjustments

	1998 KD	1997 KD
Balance at beginning of the year	8,557,144	4,993,428
Net exchange differences for the year	(2,353,732)	3,563,716
Relating to disposal of subsidiary and concession	(936,182)	-
Balance at end of the year	5,267,230	8,557,144

Notes to Consolidated Financial Statements

Year Ended December 31, 1998

13. Gain on sale of subsidiary and concession

	1998 KD	1997 KD
Gain on sale of subsidiary	2,215,438	-
Gain on sale of Amal concession	1,389,761	-
	3,605,199	-

On January 1, 1998, the Group sold its wholly owned subsidiary, KUFPEC (Congo) Limited. The subsidiary's net assets that were included in the consolidated balance sheet at December 31, 1997 amounted to KD 2,497,929. The subsidiary's revenues and net profit that were recognized in the 1997 consolidated statement of profit and loss were KD 2,452,657 and KD 545,900 respectively.

Effective June 1, 1998, the Group disposed of its Amal concession which was part of KUFPEC (Egypt) Limited. The net liabilities of the concession that were included in the consolidated balance sheet at December 31, 1997 amounted to KD 511,642. The revenues recognized relating to this concession from January 1, 1998 until June 1, 1998 were KD 122,568 (1997 - KD 789,104) and the net loss was KD 377,361 (1997 - KD 278,768 net profit).

14. General and administrative expenses

Included in general and administrative expenses is Directors' fees in the amount of KD 24,500, which are subject to the approval of the Shareholder's General Assembly (1997 - KD 24,500).

15. Taxation

	1998 KD	1997 KD
Current tax	3,084,170	3,395,256
Deferred tax	-	(246,460)
	3,084,170	3,148,796

16. Financial instruments

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

- **Estimation of fair values**
  The carrying amounts of the financial instruments are a reasonable estimate of the fair values because of the short maturity of such instruments.

- **Credit risk**
  The financial instruments which potentially subject the Group to credit risk consist of short-term deposits and receivables. The Group places its cash with various reputed financial institutions and avoids credit concentration. The Group also deals with oil majors and state owned oil companies.

- **Interest rate risk**
  The only financial assets or financial liabilities subject to fluctuation in interest rates are short-term deposits and funds held by parent which earn interest at prevailing market rates. All other balances are non-interest bearing.

17. Principal subsidiary companies

The principal wholly owned subsidiaries of Kuwait Foreign Petroleum Exploration Company K.S.C. (Closed) that are included in the accompanying consolidated financial statements are:

Notes to Consolidated Financial Statements

Year Ended December 31, 1998

17. Principal subsidiary companies (continue)

Name of company	Country of incorporation
- KUFPEC Services, K.S.C. (Closed)	Kuwait
- KUFPEC (China) Inc.	Panama
- KUFPEC (Italy) Limited	United Kingdom
- KUFPEC (Egypt) Limited	Cayman Islands
- KUFPEC (Indonesia) Limited	Cayman Islands
- KUFPEC (Algeria) Limited	Cayman Islands
- KUFPEC (Pakistan) Limited	Cayman Islands
- KUFPEC (Sudan) Limited	Cayman Islands
- KUFPEC (Tanzania) Limited	Cayman Islands
- KUFPEC (Tunisia) Limited	Cayman Islands
- KUFPEC (Malaysia) Limited	Cayman Islands
- KUFPEC (Yemen) Limited	Cayman Islands
- KUFPEC (Aden) Limited	Cayman Islands
- KUFPEC (Sumatra) Limited	Cayman Islands
- KUFPEC (Vietnam) Limited	Cayman Islands
- KUFPEC (Luanda) Ltd.	Cayman Islands
- International Energy Development Corporation (Congo) Limited	Bermuda
- International Energy Development Corporation (Egypt) Limited	Bermuda
- International Energy Development Corporation (Sudan) Limited	Bermuda
- International Energy Development Corporation N.A. Holdings N.V.	Netherlands
- Energy Development Corporation B.V.	Netherlands
- KUFPEC Australia Pty Limited	Australia
- KUFPEC (Italy) B.V.	Netherlands
- KUFPEC (Finance) B.V.	Netherlands
- Varanus Pty Limited	Australia
- KUFPEC (Perth) Pty Ltd.	Australia

18. Oil and gas reserves

The oil and gas reserves at the balance sheet date are as follows:

	1998 Oil MMBBL	1998 Gas BCF	1997 Oil MMBBL	1997 Gas BCF
Proven reserves	20.49	574.15	25.88	374.43
Probable reserves	10.60	89.88	9.9	55.37
	31.09	664.03	35.85	429.80

Notes to Consolidated Financial Statements

Year Ended December 31, 1998

Proven reserves are the quantities of crude oil, natural gas and natural gas liquids which geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic and operating conditions.
Probable reserves are those additional reserves which are not yet proven but together with proven reserves are estimated to have a 50% or better chance of being technically and economically producible.

Oil reserves include the oil equivalent of natural gas liquids. Oil and gas reserves cannot be measured exactly since estimation of reserves involves subjective judgment and arbitrary determinations. Therefore, all estimates are subject to periodic revision.

19. Capital commitments

Commitments under various joint ventures for future exploration and development expenditure amount to approximately KD 99.5 million (1997 - KD 47 million).

20. Contingent asset

The Company has pursued a claim against Iraq for the recovery of the total losses sustained as a result of the invasion and occupation of Kuwait in 1990 - 91. Accordingly, a claim for U.S.$ 14,843,000 (KD 4,446,294) was lodged with the Public Authority for Assessment of Compensation (PAAC) through Kuwait Petroleum Corporation which has been approved and sent to the UNCC. The accompanying financial statements do not include amounts related to this potential claim.

21. Contingent liabilities

a) At December 31, 1998, KUFPEC Australia had a first floating cross charge over its assets covering the company's interest in the Palm Valley gas field. All participants have executed and registered similar cross charges in favor of other participants, to cover potential payment defaults to the joint venture. Similarly, pursuant to the company's interest in a joint venture in Australia encompassing production from the Harriet Field and various exploration permits, the company has entered into three deeds of cross charge in favor of each of the other participants for the purpose of securing the company's obligations under the Joint Venture Agreement. Each cross charge, a form of joint collateral, represents a first lien over the company's interest in the venture. The charges extend over the entire interest of the company in the venture, subject to a maximum limit of Australian $ 250 Million (KD 46 million).

b) Taxes and penalties were assessed against a certain branch of KUFPEC Indonesia in respect of employee and withholding taxes for 1992 and 1993. The taxes and penalties are under objection or planned appeal. The branch has not accrued the amount of taxes and penalties as management believes that these matters will ultimately be resolved with no material impact on the branch's financial position. No assessment has yet been received for subsequent years.

c) At December 31, 1998, the Group had outstanding letters of guarantee in the amount of U.S.$ 92,380,951 (KD 27,858,400).

22. Current economic conditions

Many Asia Pacific countries, including Indonesia in which a certain subsidiary operates, are experiencing severe economic difficulties relating to currency devaluations, volatile stock markets and slow downs in economic growth. The subsidiary's future operations may be significantly affected by the continuation of these economic conditions. For economic conditions to improve, fiscal and monetary action needs to be undertaken by the Government and others. Such action is beyond the control of the subsidiary. At the date of these financial statements, the management of the subsidiary do not believe that there is any measurable specific impact on the recoverability of assets of the subsidiary which represent approximately 4% of the consolidated assets, or on the ability of the subsidiary to meet its financial obligations as they fall due.

Kuwait Foreign Petroleum
Exploration Company K.S.C.

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