الاتصالات السعودية
SAUDI TELECOM

a Saudi Joint Stock Company

Financial Statements for the Year Ended December 31, 2003

Saudi Telecom Company
(a Saudi Joint Stock Company)
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AUDITORS' REPORT

To the shareholders
Saudi Telecom Company
(A Saudi Joint Stock Company)
Riyadh, Saudi Arabia

We have audited the accompanying balance sheet of Saudi Telecom Company (A Saudi Joint Stock Company) as of December 31, 2003, and the related statements of income, shareholders' equity and cash flows for the year then ended, and notes 1 to 34 which form an integral part of these financial statements as prepared by the Company in accordance with Article 123 of the Regulations for Companies and presented to us with all the necessary information and explanations. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. 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 standards 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.

As discussed in Note 30 to the financial statements, the Company could not disclose segment reporting in the financial statements, as required by generally accepted accounting standards, due to this information being unavailable for external financial reporting. The Company is currently working on enabling its systems to provide segment information in accordance with the requirements of generally accepted accounting standards.

In our opinion, taking into consideration what has been discussed in the preceding paragraph, the financial statements present fairly, in all material respects, the financial position of Saudi Telecom Company as of December 31, 2003, and the results of its operations and its cash flows for the year then ended in conformity with generally accepted accounting standards appropriate to the nature of the Company, and comply with the relevant provisions of the Regulations for Companies and the articles of the Company as these relate to the preparation and presentation of these financial statements.

Deloitte & Touche
Bakr Abulkhair & Co.

Bakr A. Abulkhair
(License No. 101)
Thul-Hujja 17, 1424
February 8, 2004

Saudi Telecom Company
(a Saudi Joint Stock Company)
Balance Sheet as of December 31, 2003

	Notes	2003 SR'000	2002 SR'000
ASSETS			
Current assets:			
Cash and cash equivalents	3	3,281,115	1,941,866
Short-term investments	4	2,107,000	-
Accounts receivable, net	5	3,015,054	5,447,908
Inventories, net	6	303,839	410,655
Prepayments and other current assets	7	176,630	126,380
Total current assets		8,883,638	7,926,809
Non-current assets:			
Property, plant and equipment, net	8	31,906,679	32,018,244
Investments accounted for under the equity method	9	799,676	769,634
Other investments	10	79,696	112,090
Other non-current assets		102,521	86,066
Total non-current assets		32,888,572	32,986,034
Total assets		**41,772,210**	**40,912,843**
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current liabilities:			
Accounts payable	11	2,943,362	6,932,435
Other payables	12	2,498,831	1,877,707
Accrued expenses	13	2,498,642	2,213,404
Deferred revenue - current		1,481,533	1,582,984
Current portion of long-term borrowings	14	-	583,333
Total current liabilities		9,422,368	13,189,863
Non-current liabilities:			
Deferred revenue		1,379,251	1,681,080
Long-term borrowings	14	-	650,000
Employees' end of service benefits	15	1,575,953	1,382,570
Total non-current liabilities		2,955,204	3,713,650
Total liabilities		12,377,572	16,903,513
Shareholders' equity:			
Authorized, issued and outstanding shares: 300,000,000 shares, par value SR 50 per share	16	15,000,000	15,000,000
Legal reserve	17	2,362,449	1,509,923
Retained earnings		12,035,141	7,512,405
Unrealized loss on other investments	10	(2,952)	(12,998)
Total shareholders' equity		29,394,638	24,009,330
Total liabilities and shareholders' equity		**41,772,210**	**40,912,843**

The accompanying notes 1 to 35 form an integral part of these financial statements.

Saudi Telecom Company
(a Saudi Joint Stock Company)
Statement of Income for the Year Ended December 31, 2003
(Saudi Riyals in thousands)

	Notes	2003	2002
Operating Revenues			
Wireline		9,548,073	10,607,248
Wireless		17,743,945	12,939,817
Total operating revenues	18	27,292,018	23,547,065
Operating Expenses			
Government charges	19	(5,548,401)	(6,299,389)
Access charges		(1,823,441)	(1,763,532)
Employee costs	20	(3,673,235)	(3,456,375)
Depreciation	8	(3,812,966)	(3,265,293)
Administrative and marketing expenses	21	(1,671,981)	(2,569,454)
Repairs and maintenance		(1,561,982)	(1,405,318)
Total operating expenses		(18,092,006)	(18,759,361)
Operating Income		9,200,012	4,787,704
Other Income and Expenses			
Cost of manpower improvement program	22	(700,000)	(1,070,000)
Commissions	3, 4, 10	43,649	30,548
Earnings of investments accounted for under the equity method		51,923	123,162
Other, net	23	155,839	(233,330)
Other income and expenses, net		(448,589)	(1,149,620)
Net Income before Zakat		8,751,423	3,638,084
Provision for Zakat	24	(226,161)	(92,250)
Net Income		**8,525,262**	**3,545,834**
Earnings per share (SR)	28	**28.42**	**11.82**

The accompanying notes 1 to 35 form an integral part of these financial statements.

Saudi Telecom Company
(a Saudi Joint Stock Company)
Statement of Cash Flows for the Year Ended December 31, 2003
(Saudi Riyals in thousands)

	2003	2002
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	8,525,262	3,545,834
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	3,812,966	3,265,293
Provision for doubtful accounts	345,855	1,726,115
Losses on disposal/sale of property, plant and equipment	25,315	367,092
Undistributed earnings of investments accounted for under the equity method	(30,042)	(102,483)
Changes in:		
Accounts receivable	2,086,999	(1,097,793)
Inventories	106,816	36,889
Prepayments and other current assets	(50,250)	(29,062)
Other non-current assets	(16,455)	(14,152)
Accounts payable	(3,989,073)	523,134
Other payables	603,876	(484,745)
Accrued expenses	285,238	(200,239)
Deferred revenue	(403,280)	(21,340)
Employees' end of service benefits	193,383	(45,775)
Net cash provided by operating activities	11,496,610	7,468,768
CASH FLOWS FROM INVESTING ACTIVITIES		
Capital expenditures	(4,672,768)	(5,780,155)
TEP6 close out adjustment, net	946,052	-
Short-term investments	(2,107,000)	-
Maturity of government bonds	13,691	13,685
Proceeds from sale of investment in Inmarsat, net	28,749	-
Net cash used for investing activities	(5,791,276)	(5,766,470)
CASH FLOWS FROM FINANCING ACTIVITIES		
Dividends paid	(3,132,752)	(896,114)
Repayments of borrowings	(1,583,333)	(1,666,667)
Proceeds from short-term borrowings	350,000	450,000
Proceeds from long-term borrowings	-	550,000
Net cash used for financing activities	(4,366,085)	(1,562,781)
NET INCREASE IN CASH AND CASH EQUIVALENTS	1,339,249	139,517
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	1,941,866	1,802,349
CASH AND CASH EQUIVALENTS AT END OF YEAR	**3,281,115**	**1,941,866**

The accompanying notes 1 to 35 form an integral part of these financial statements.

Saudi Telecom Company
(a Saudi Joint Stock Company)
Statement of Changes in Shareholders' Equity for the Year Ended December 31, 2003
(Saudi Riyals in thousands)

	Notes	Common Shares	Legal Reserve	Retained Earnings	Unrealized (Loss) / Gain on Other Investments	Total Shareholders' Equity
Balance at December 31, 2001		**12,000,000**	**1,155,340**	**7,321,154**	**(2,208)**	**20,474,286**
Net income		-	-	3,545,834	-	3,545,834
Transfer to share capital		3,000,000	-	(3,000,000)	-	-
Transfer to legal reserve	17	-	354,583	(354,583)	-	-
Unrealized loss on investment	10	-	-	-	(10,790)	(10,790)
Balance at December 31, 2002		**15,000,000**	**1,509,923**	**7,512,405**	**(12,998)**	**24,009,330**
Net income		-	-	8,525,262	-	8,525,262
Dividends	29	-	-	(3,150,000)	-	(3,150,000)
Transfer to legal reserve	17	-	852,526	(852,526)	-	-
Unrealized gain on investment	10	-	-	-	10,046	10,046
Balance at December 31, 2003		**15,000,000**	**2,362,449**	**12,035,141**	**(2,952)**	**29,394,638**

The accompanying notes 1 to 35 form an integral part of these financial statements.

1 GENERAL

Saudi Telecom Company (the "Company") was established as a Saudi Joint Stock Company pursuant to Royal Decree No. M/ 35, dated 24 Dhul Hujja 1418 H (April 21, 1998) which authorized the transfer of the telegraph and telephone division of the MoPTT (hereinafter referred to as "Telecom Division") with its various components and technical and administrative facilities to the Company, and in accordance with the Council of Ministers' Resolution No. 213 dated 23 Dhul Hujja 1418 H (April 20, 1998) the Company's Articles of Association (the "Articles") were approved. The Company was wholly owned by the Government of the Kingdom of Saudi Arabia (the "Government"). Pursuant to the Council of Ministers' Resolution No. 171 dated 2 Rajab 1423 H (September 9, 2002), the Government sold 30% of its shares (refer to Note 16).

The Company commenced its operations as Kingdom-wide provider of telecommunications services on 6 Muharram 1419 H (May 2, 1998), and received its commercial registration number 101050269 as a Saudi Joint Stock Company on 4 Rabi Awal 1419 H (June 29, 1998).

The Company provides a range of telecommunications services which includes mobile, fixed local, national and international telephone services, telex, telegraph, data transmission, leased lines, public telephones, public network and radio paging services.

The Company is the sole entity engaged in the provision of telecommunications services within, to and from the Kingdom. In accordance with the Council of Ministers' Resolution No. 171, referred-to above, it has been approved that the telecommunications sector be opened for competition by partially liberalizing the mobile and fixed line services. The Company continuously reviews in detail all of the telecom regulatory authorities' releases and what is being conducted for opinion seeking and discussion in accordance with the Company's Articles and relevant Government decisions. The Company takes the regulatory and administrative actions it finds necessary to protect its rights that are guaranteed by Government decisions, including the licensing for mobile competition, opening of the fixed line market and related matters. This also includes continuous follow-up on negotiations between the Kingdom and the World Trade Organization. During 2003, the Communications and Information Technology Commission (CITC) issued licenses for Very Small Aperture Terminals (VSAT), and also announced plans to issue licenses for the provision of data services in the Kingdom during 2004.

2 SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies adopted by the Company are summarized below:

a) Period of the financial statements

The Company's financial year begins on January 1 and ends on December 31, according to the Company's Articles.

b) Preparation of the financial statements

The financial statements are prepared in accordance with accounting standards generally accepted in the Kingdom.

The preparation of financial statements requires management to make estimates and assumptions that affect the financial position and operating results. Actual results could differ from those estimates.

c) Revenue recognition

Revenue is recognized when services are rendered based on the access to, or usage of, the exchange network and facilities. Usage revenues are based upon minutes of traffic processed, applying rates approved by CITC.

- Charges billed in advance are deferred and recognized over the period the services are rendered.
- Unbilled revenue is recognized in the period to which it relates.
- Revenue is recognized upon collection when collectability is highly uncertain.
- Non-refundable up-front activation fees received from subscribers are deferred and recognized over the estimated service lives of the subscribers.

d) Financial instruments

Financial instruments include: cash, investments, accounts receivable and payable, other receivables and payables and short and long-term borrowings.

e) Cash and cash equivalents

Cash and cash equivalents consist of cash on hand, balances with banks and all highly liquid investments with a maturity of 90 days or less when purchased. Cash and cash equivalents are stated at cost.

f) Accounts receivable

Accounts receivable are shown at their net realizable values, which represents billings and unbilled usage revenues net of allowances for doubtful accounts. An allowance is created for doubtful accounts.

g) Allowance for doubtful accounts

The Company reviews its accounts receivable for the purpose of creating the required allowances against doubtful accounts. When creating the allowance, consideration is given to the type of service rendered (mobile, land line, telex, international settlements, …etc), age of the receivable, the Company's previous experience in debt collection and the general economic situation.

h) Inventories

- Inventories, which are principally cables, spare parts and consumables, are stated at weighted average cost, net of allowances. Inventory items that are considered an integral part of the network assets, such as emergency spares which cannot be removed from the exchange, are recorded within property, plant and equipment. Inventory items held by third parties responsible for upgrading and expanding the network are recorded within 'capital work in progress'.

- The Company creates allowance for obsolete and slow-moving inventories, based on a study of the movement of the major inventory categories. When such an exercise is impractical, the allowance will be based on groups or categories of inventory items, taking into consideration the items which may require significant reductions in their values.

i) Property, plant and equipment and depreciation

1. Prior to May 2, 1998, the Telecom Division did not maintain sufficiently detailed historical information to record property, plant and equipment based on the historical cost method. Consequently all property, plant and equipment transferred by the Telecom Division on May 2, 1998 has been included in these financial statements at a valuation which was performed by the Company with the assistance of independent international and local valuation experts. The principal bases used for valuation are as follows:

- Land	Appraised value
- Buildings, plant and equipment	Depreciated replacement cost

2. Other than what is mentioned in (1) above, property, plant and equipment acquired by the Company are recorded at historical cost.

3. Cost of the network comprises all expenditures up to the customer connection point, including contractors' charges, direct material, labor and commission costs, if appropriate, up to the date the relevant assets are placed in service.

4. Property, plant and equipment, excluding land, are depreciated on a straight line basis over the following estimated useful lives:

	Years
Buildings	22 – 30
Telecommunications plant and equipment	5 – 25
Other assets	5

5. Repairs and maintenance costs are expensed as incurred, except to the extent that they increase productivity or extend the useful life of an asset, in which cases they are capitalized.

6. The Company reviews its property, plant and equipment annually to determine whether any of the assets are impaired, and provides for any impairment in their values which is other than temporary. The amount of impairment will be recognized in the income statement for the period when such determination is made, and property, plant and equipment is reported net of provision.

j) Software Costs

- Costs of operating systems and application software purchased from vendors are capitalized if they meet the capitalization criteria, which include productivity enhancement or a noticeable increase in the useful life of the asset. These costs are amortized over the estimated period of the provided benefits.

- Internally developed operating systems software costs are capitalized if they meet the capitalization criteria, which include the dedication of a defined internal work group to develop the software and the possibility to readily identify related costs. These costs are amortized over the estimated period of the provided benefits.

- Internally developed application software costs are recognized as expense as incurred, and where the costs of operating systems software cannot be identified separately from the associated hardware costs, then the operating systems software costs are recorded as part of the hardware.

- Subsequent additions, modifications or upgrades of software programs, whether operating or application packages, are expensed as incurred.

- Software training and data-conversion costs are expensed as incurred.

k) Investments accounted for under the equity method

The Company accounts for investments in entities in which it has a significant influence under the equity method. Under the equity method, the Company records the investment at acquisition cost and is adjusted subsequently by the Company's share in the income (loss) of the investee, the investee's distributed dividends and any increase in the investee's share capital, to reflect the Company's relative share in the investee's net assets. These investments are presented in the balance sheet as non-current assets, and the Company's relative share in the income (loss) of the investee is presented in the statement of income.

l) Other investments

- Available for sale marketable securities are carried at fair value, which is based on market value when available. However, if fair value cannot be determined, due to non-availability of an active exchange market or other indexes through which market value can reasonably be determined, then cost will be considered as the fair value. Unrealized gains and losses are shown as a separate component within shareholders' equity in the balance sheet and in the statement of changes in shareholders' equity. Losses resulting from other than temporary declines in fair values below costs are recorded in the income statement of the period in which the declines occur.
- Investments held to maturity are recorded at cost and adjusted for amortization of premiums and accretion of discounts, if any. Provision is made for any permanent decline in value.
- Gains and loses resulting from sales of available for sale securities are recorded in the period of sale, and previously recorded unrealized gains and losses are reversed.

m) Zakat

The Company calculates and reports zakat provision in its financial statements in accordance with Zakat rules and principles, and the instructions of the Department of Zakat and Income Taxes (DZIT). Adjustments arising from final zakat assessments are recorded in the year in which such assessments are made.

n) Employees' end of service benefits

- Employee's end-of-service provision is calculated based on the present value of the liabilities, using unbiased assumptions and a suitable discount rate.
- End of service benefits are calculated for each employee in accordance with the terms and conditions of Saudi Labor and Workman Law, and are payable as a lump sum to the employee upon termination of his contract.

o) Foreign currency transactions

- The Company maintains its financial records in Saudi Riyals and records transactions in foreign currencies at the appropriate rate of exchange prevailing at the date of the transaction.
- Balances of monetary assets and liabilities denominated in foreign currencies of specific amounts are translated using rates of exchange prevailing at the balance sheet date.
- Gains and losses arising on the settlement of foreign currency transactions, and unrealized gains and losses resulting from the translation to Riyals of foreign currency denominated monetary balances are recorded in the statement of income.

p) Government charges

Government charges are the costs incurred for the right to operate the Kingdom's telecommunications services, including use of the frequency spectrum. Government charges are accrued in the relevant periods.

q) Access charges

Access charges represent the costs to connect to foreign carriers' networks for calls made by the Company's subscribers. Access charges are recognized in the periods of relevant calls.

r) Administrative and marketing expenses

Administrative and marketing expenses are expensed as incurred when it is not possible to determine the relevant benefiting periods, otherwise they will be charged to the relevant periods.

s) Earnings per share

Earnings per share are calculated by dividing net income for the financial period by the weighted average number of shares outstanding during the period.

3 CASH AND CASH EQUIVALENTS

Surplus cash arising during the year is invested in short-term deposit accounts. The average rate of commission received during 2003 on deposit accounts maturing in less than 90 days was 1.8% (2002: 2.3%). Total commission earned during the year on these accounts was SR 32.8 million (2002: SR 22.5 million). Commission earned on current accounts was SR 4.2 million (2002: SR 6.7 million).

Cash and cash equivalents at the end of the year include balances of collection accounts at various banks. As per agreements with the banks those balances are to be transferred to the Company's main account on the fourth day of the subsequent month.

At the end of the year, cash and cash equivalents consisted of the following:

	2003 SR '000	2002 SR '000
Collection accounts	2,447,985	1,904,994
Short-term deposits	768,000	-
Disbursement accounts	65,130	36,872
	3,281,115	1,941,866

4 SHORT-TERM INVESTMENTS

During the fourth quarter of 2003 surplus cash was invested in short-term deposits with maturity periods greater than 90 days. The average rate of commission on these deposits is 2.3%. Total commission earned during 2003 on these deposits was SR 6.2 million.

5 ACCOUNTS RECEIVABLE, NET

(a) Accounts receivable, net of allowance for doubtful accounts, consisted of the following:

	2003 SR '000	2002 SR '000
Trade accounts receivable	2,887,117	5,738,401
Unbilled revenue	884,399	1,221,602
	3,771,516	6,960,003
Allowance for doubtful accounts	(756,462)	(1,512,095)
	3,015,054	5,447,908

Due to the increased use of prepaid mobile cards (Sawa), the improvement in collection rates from customers during 2003, and the Company's efforts in implementing customers credit limits, the Company conducted during the fourth quarter of 2003 a review of the allowance for doubtful accounts which resulted in a change in the method of estimating the appropriate level of the allowance for doubtful accounts, to be in line with the aforementioned developments.

(b) The Company has agreements with foreign network operators, whereby amounts receivable from and payable to the same foreign network operator are subject to the right of set off. At December 31, 2003 and 2002, the net amounts included in accounts receivable and accounts payable were as follows:

	2003 SR '000	2002 SR '000
International accounts receivable, net	550,817	566,426
International accounts payable, net	892,544	935,504

6 INVENTORIES, NET

Movement in inventories during the year was as follows:

	2003 SR '000	2002 SR '000
Balance at beginning of the year	410,655	447,544
Additions	310,959	435,684
Usage	(397,572)	(445,097)
	324,042	438,131
Inventory allowance	(20,203)	(27,476)
Balance at end of the year	303,839	410,655

7 PREPAYMENTS AND OTHER CURRENT ASSETS

Prepayments and other current assets consisted of the following:

	2003 SR '000	2002 SR '000
Advances to suppliers	69,137	60,612
Deferred costs	43,096	23,199
Prepaid rent	28,641	17,639
Prepaid insurance	22,491	18,922
Other	13,265	6,008
	176,630	126,380

8 PROPERTY, PLANT AND EQUIPMENT, NET

(SR '000)	Land and Buildings	Telecommunications Plant and Equipment	Other Assets	Capital Work In Progress	Total 2003	Total 2002
Gross book value						
At beginning of the year	8,659,957	41,868,972	1,067,629	1,830,182	53,426,740	48,804,291
TEP6 close out adjustment	-	(1,154,132)	-	163,712	(990,420)	-
Additions	127,342	654,959	97,897	3,792,570	4,672,768	5,758,530
Transfers	273,972	3,260,337	-	(3,534,309)	-	-
Disposals	(1,158)	(478,713)	(39,079)	-	(518,950)	(1,136,081)
At end of the year	9,060,113	44,151,423	1,126,447	2,252,155	56,590,138	53,426,740
			-			
Accumulated depreciation						
At beginning of the year	3,311,505	17,358,246	738,745	-	21,408,496	18,933,817
TEP6 close out adjustment	-	(44,368)	-	-	(44,368)	-
Charge for the year	203,464	3,475,734	133,768	-	3,812,966	3,265,293
Disposals	(254)	(454,606)	(38,775)	-	(493,635)	(790,614)
At end of the year	3,514,715	20,335,006	833,738	-	24,683,459	21,408,496
Net book value	5,545,398	23,816,417	292,709	2,252,155	31,906,679	32,018,244

(a) Land and buildings shown above include land of SR 2,312 million as of December 31, 2003 (2002: SR 2,312 million).

(b) In accordance with the Royal Decree referred to in Note (1), ownership of assets had been transferred to the Company as of May 2, 1998, however, transfer of legal ownership of certain land is in progress. By January 2004, value of land for which legal ownership has been transferred into the Company' name amounted to SR 1,191 million. Ownership transfer of the remaining lands with value amounting to SR 1,121 million is in progress.

(c) During 2003, the Company capitalized loan commissions totaling SR 19.3 million into property, plant and equipment at a commission rate of 3.12% (2002: SR 56.4 million at a commission rate of 3.78%).

(d) The Telecommunications Expansion Project 6 (TEP6) close out adjustment represents the effect of the agreement reached with the project's contractor during December, 2003 to close out all matters relating to this project and reconcile the contractor's entitlements retained by the Company.

(e) As a result of providing the network with more advanced technologies, the Company revised during the fourth quarter of 2003 some of the estimated useful lives of the telecommunications plant and equipment which resulted in additional depreciation expense amounting to SR 474 million for the year of 2003.

9 INVESTMENTS ACCOUNTED FOR UNDER THE EQUITY METHOD

Investments accounted for under the equity method of accounting consist of the following:

	Ownership	2003 SR '000	2002 SR '000
Arab Satellite Communications Organization ("Arabsat")	36.66%	768,485	739,634
Arab Submarine Cables Company Ltd	40%	31,191	30,000
		799,676	769,634

Arabsat

This organization was established during April 1976 by member states of the Arab League. Arabsat offers a number of services to member states, as well as to all public and private sectors within its coverage area, principally the Middle East.

Current services offered include regional telephony (voice, data, fax and telex), television broadcasting, regional radio broadcasting, restoration services and leasing of capacity on an annual or monthly basis.

During 2001, two of the satellites of Arabsat became defective, and claims were raised to the insurance companies for compensation of the resulting loss. Based on the settlement reached with the insurance companies, the resulting loss will not have a material effect on the Company's financial statements.

Arab Submarine Cables Company Ltd.

Arab Submarine Cables Company Ltd. has been formed for the purpose of construction, lease, management and operation of a submarine cable connecting the Kingdom and the Republic of Sudan for telecommunications between them and any other countries. The operational activities of the Arab Submarine Cables Company Ltd. commenced during June 2003.

10 OTHER INVESTMENTS

(a) Other investments consist of the following:

	2003 SR '000	2002 SR '000
Available for sale – at market value:		
Investment in Newskies	24,014	13,919
Investment in New ICO	33	82
	24,047	14,001
Available for sale – at cost:		
Investment in Intelsat Ltd	55,649	55,649
Investment in Inmarsat	-	28,749
	55,649	84,398
Held to maturity:		
Government bonds	-	13,691
Total other investments	79,696	112,090

(b) The balance of unrealized holding losses relating to investments valued at market value was SR 2.9 million at December 31, 2003 (SR 12.9 million at December 31, 2002).

(c) The investment in Intelsat Ltd is still within the category of investments valued at cost, due to non-commencement of trading in its shares.

(d) The Company sold its investment in Inmarsat during December 2003 for SR 55.8 million which resulted in a gain of SR 27 million.

(e) During 1999, the Government issued bonds to the Company in exchange for amounts due for telecommunication services provided. The bonds were issued at face value with commission rates ranging from 6.29% to 7.12% and maturities through August 2003. Repayments of principal and commission were received every six months throughout the life of these bonds. Total commission earned on these bonds for 2003 from the beginning of the year to maturity in August 2003 amounted to SR 0.4 million (2002: SR 1.3 million).

11 ACCOUNTS PAYABLE

Accounts payable consists of the following:

	2003 SR '000	2002 SR '000
Government charges	832,448	3,724,526
Capital	827,467	1,945,598
Trade	390,903	326,807
International settlements	892,544	935,504
	2,943,362	6,932,435

Certain accounts payable balances are set off against accounts receivable balances related to international settlements, as explained in Note (5-b).

12 OTHER PAYABLES

Other payables consist of the following:

	2003 SR '000	2002 SR '000
Supplier retentions	645,960	853,911
Manpower improvement program	700,256	-
Settlement of seconded employees' entitlements	699,136	711,604
Provision for Zakat	226,017	92,354
Other	227,462	219,838
	2,498,831	1,877,707

The Company recognized in the statement of income for 2001 the total estimated liability on the Company which represents 50% of the total amount toward the settlement of the MoPTT seconded employees' pension entitlements, in accordance with the Council of Ministers' Resolution No. 75 dated 5 Rabi Awal 1422 H (May 28, 2001).

The Council of Ministers' Resolution No. 198 dated 18 Rajab 1424 H (September 15, 2003) approved the system of exchanging benefits between the Civil and Military Pension System and the Social Security System. The above estimated liability will be reconciled on the basis of the actual number of employees who choose either to terminate their services or settle their pension entitlements.

13 ACCRUED EXPENSES

Accrued expenses consist of the following:

	2003 SR '000	2002 SR '000
Capital	1,174,499	1,190,856
Trade	319,776	213,377
Employee accruals	840,939	645,743
Other	163,428	163,428
	2,498,642	2,213,404

14 BORROWINGS

During 2001, the Company entered into a syndicated loan agreement for SR 2,500 million at a commission rate equivalent to the Saudi Inter-bank Offered Rate (SIBOR) plus 0.45% per annum, to be utilized for expansion and infrastructure projects. An amount of SR 1,150 million was utilized from this loan during 2001 and 2002.

During the fourth quarter 2003, the Company made an early settlement of all outstanding loan balances, and as a result the balance of outstanding borrowings was zero as of December 31, 2003.

The Company has unutilized and renewable short-term facilities with three local banks amounting to SR 1,500 million, with maturities between June and December 2004, and commission rates equivalent to SIBOR plus 0.45% - 0.55% per annum.

Commissions incurred on borrowings have been capitalized into property, plant and equipment, as explained in Note (8-c).

The movement in borrowings was as follows:

	2003 SR '000	2002 SR '000
Balance at January 1	1,233,333	1,900,000
Drawings during the year	350,000	1,000,000
Repayments during the year	(1,583,333)	(1,666,667)
Balance at December 31	-	1,233,333

15 EMPLOYEES' END OF SERVICE BENEFITS

The movement in employees' end of service benefits was as follows:

	2003 SR '000	2002 SR '000
Balance at January 1	1,382,570	1,428,345
Charge during the year	222,146	356,960
Settlements made during the year	(28,763)	(402,735)
Balance at December 31	1,575,953	1,382,570

There are no assets designated specifically to cover this liability, instead it is paid out of operating cash flows as and when employees leave the Company.

Following are the assumptions used in calculating the present value of the employees' end-of-service provision:

(a) Annual salaries progression at a rate of 5% with a maximum limit representing the employee's average salary scale.

(b) Average retirement age of 55 years for all employees.

(c) Discount rate of 6%, which represents the average yield on long-term government bonds as at the balance sheet date.

16 SHARE CAPITAL

The Company's capital amounting to SR 15,000,000,000 is fully paid and divided into 300,000,000 shares at par value of SR 50 each. The Council of Ministers' Resolution No. 171 dated 2 Rajab 1423 H (September 9, 2002) approved offering part of the Company's shares for public subscription according to the terms and rules of such resolution, and delegated the authority to the Public Investment Fund to implement the controls and procedures required to sell the shares in coordination with the concerned parties. 90,000,000 of the Company's shares were offered for public subscription of which 60,000,000 shares were appropriated for Saudi nationals, 15,000,000 shares to the Public Pension Fund and 15,000,000 shares to the General Organization for Social Security. The offered share price was SR 170 with total sales proceeds of SR 15,300,000,000 which were deposited to the Public Investment Fund account. The subscription period commenced on 13 Shawwal 1423 H (December 17, 2002) and ended on 3 Dhul Quada 1423 H (January 6, 2003).

17 LEGAL RESERVE

The Company appropriates 10% of annual net income as legal reserve until such reserve equals 50% of issued share capital. This reserve is not available for distribution to the Company's shareholders. During 2003, the Company appropriated an amount of SR 852.5 million (2002: SR 354.6 million).

18 OPERATING REVENUES

Operating revenues consist of the following:

	2003 SR '000	2002 SR '000
Usage charges	21,192,855	18,088,982
Subscription fees	4,759,453	4,238,013
Activation fees	822,554	768,772
Other	517,156	451,298
	27,292,018	23,547,065

19 GOVERNMENT CHARGES

The Company is charged by the Government for the right to operate as the Kingdom-wide provider of telecommunications services, on the basis of net revenue. Net revenue is defined as total operating revenues less access charges as reflected in the statement of income. The Government charges were calculated as follows:

	2003 SR '000	2002 SR '000
Commercial provisioning	5,093,715	5,881,554
License fees	254,686	217,835
Frequency spectrum	200,000	200,000
	5,548,401	6,299,389

The following illustrates the basis on which the Government charge is calculated:

(a) Commercial Provisioning

Effective January 1, 1999 the Government charges are calculated as follows:

For 1999, 2000 and 2001; 20% of net revenue (as defined above).

For 2002; 27% of net revenue (as defined above).

For 2003 and thereafter; 20% of net revenue (as defined above), in accordance with the amendment per the Council of Ministers' Resolution No. 171 referred to in note (1) above. The Resolution provides for considering the reduction in the percentage after opening the telecommunication sector for competition.

(b) License Fees

License fees were determined as 1% of net revenue (as defined above). A portion of this fee will be used to finance the operations of CITC.

(c) Frequency Spectrum

A fixed fee of SR 200 million per annum. This fee will continue until such time that CITC establishes new telecom regulations.

20 EMPLOYEE COSTS

Employee costs consist of the following:

	2003 SR '000	2002 SR '000
Salaries and allowances	2,774,926	2,647,502
Incentives and rewards	246,998	8,943
Social security	227,131	222,515
End of service benefits	222,063	356,960
Medical insurance	145,386	178,952
Other	56,731	41,503
	3,673,235	3,456,375

21 ADMINISTRATIVE AND MARKETING EXPENSES

Administrative and marketing expenses consist of the following:

	2003 SR '000	2002 SR '000
Allowance for doubtful accounts (refer to Note 5)	345,855	1,726,115
Consultancy	182,786	167,697
Commissions on sales of prepaid mobile cards	431,389	156,758
Printing of telephone cards and stationery	173,005	118,111
Utilities	130,342	110,381
Other	408,604	290,392
	1,671,981	2,569,454

22 COST OF MANPOWER IMPROVEMENT PROGRAM

The amount shown in 2003 statement of income represents the cost of implementing the third phase of the Company's manpower improvement program which was initiated during 2001. The number of employees covered by the third phase of this program was 1,096. The following schedule shows the cost of each of the three phases:

	Implementation Date	Cost SR '000
First phase	2001	600,208
Second Phase	2002	1,070,000
Third phase	2003	700,000
Total		2,370,208

23 OTHER INCOME AND EXPENSES, NET

Other income and expenses consist of the following:

	2003 SR '000	2002 SR '000
Miscellaneous income	30,906	23,314
Gain on sale of investment in Inmarsat	27,095	-
Losses on disposal of property, plant and equipment	(25,315)	(367,092)
Bad debts recovered	87,257	23,213
Other, net	35,896	87,235
	155,839	(233,330)

24 ZAKAT

(a) Zakat base

	2003 SR '000	2002 SR '000
Share capital – beginning of the year	15,000,000	12,000,000
Additions:		
Retained earnings – beginning of the year	7,512,405	7,321,154
Legal reserve – beginning of the year	1,509,923	1,155,340
Provisions – beginning of the year	3,177,923	3,363,514
Adjusted net income	9,046,415	3,689,996
Total additions	21,246,666	15,530,004
Deductions:		
Net property, plant & equipment and capital work in progress (limited to shareholders' equity before Zakat)	(31,906,679)	(24,112,370)
Investments	(879,372)	(881,724)
Non-current deferred costs	(102,521)	(86,066)
Total deductions	(32,888,572)	(25,080,160)
Zakat base	3,358,094	2,449,844

Since the Zakat base is less than the adjusted net income, the Zakat rate of 2.5% is applied to adjusted net income to determine the Zakat charge.

(b) Zakat provision

	2003 SR '000	2002 SR '000
Balance at beginning of the year	92,354	339,775
Amounts paid during the year	(92,498)	(339,671)
Charge for the year	226,161	92,250
Balance at end of the year	226,017	92,354

The Company obtained certificates from the Department of Zakat and Income Tax confirming the receipt of zakat returns for the years stated below, with no differences reported to date:

Year	Zakat Provision SR '000
1999	141,916
2000	98,669
2001	99,190
2002	92,250

25 RELATED PARTY TRANSACTIONS

Government agencies

The Company provides various voice, data and administrative services to the Government.

Government agencies accounted for approximately 2.3% of total operating revenues in 2003 (2002: 3%). Billed revenues and expenses related to Government agencies in 2003 (including Government charges discussed in Note 19) amounted to SR 625 million and SR 5,719 million, respectively (2002: SR 698 million and SR 6,388 million respectively).

Effective during the second quarter of 2003, and in accordance with the Council of Ministers' Resolution No. 171 referred to in Note (1), the Company settles the amounts due to the Government as government charges against accumulated receivable balances due from Government for usage of the Company's telecom services.

Amounts payable to Government agencies at December 31, 2003 totaled SR 967 million (2002: SR 3,842 million). Amounts receivable from Government agencies at December 31, 2003 are not material (2002: SR 2,510 million) due to the settlement mentioned above.

Investments accounted for under the equity method

During the year, the Company incurred charges of approximately SR 35 million from Arabsat with respect to satellite utilization (2002: SR 37 million).

26 COMMITMENTS AND CONTINGENCIES

Commitments

(a) The Company enters into commitments during the ordinary course of business for major capital expenditures, primarily in connection with its telephony network expansion programs. As of December 31, 2003, outstanding capital expenditure commitments approximated SR 1,927 million (2002: SR 1,641 million).

(b) Land and buildings are leased for use in the Company's operations under operating lease commitments expiring at various future dates. During 2003, total rent expense under operating leases amounted to SR 69 million (2002: SR 30 million).

Contingencies

(a) During 2001 the Company contracted with a local contractor to build and operate payphones on build, operate and transfer basis (BOT) for a period of seven years. A dispute arose between the two parties during execution of the agreement resulting in the contractor filing claims by the end of 2002 against the Company and the Company filing counter-claims.

(b) In the normal course of business, the Company is subject to proceedings, lawsuits and other claims.

However, the above matters mentioned in (a) and (b) are not expected to have a material impact on the Company's financial position or the results of its operations as reflected in the financial statements.

27 FINANCIAL INSTRUMENTS

The carrying values of all financial instruments approximate their fair values at December 31, 2003 and 2002, as discussed below:

- For cash and cash equivalents, accounts receivable and payable and other receivables and payables, fair value is deemed to approximate their carrying amount due to their short-term nature.
- For marketable equity instruments, fair value is based on quoted market prices.
- For Government bonds and borrowings, fair value is based on discounted cash flows.
- For all other investments, fair value is based on management estimates.

The Company does not utilize derivative financial instruments to manage foreign currency exchange and commission rate risks due to factors explained below.

The Company manages its cash flows by controlling the timing between its cash inflows and outflows. Surplus cash is invested to increase the Company's commission income through holding balances in short-term bank deposit accounts, but the related commission rate risk is not considered to be significant. Consequently, the Company has not used derivative financial instruments to mitigate exposure to commission rate risk.

The Company believes that it is not exposed to significant exchange rate risk since the Company's functional currency is the Saudi Riyal, which is the principal currency in which the Company transacts and it is currently fixed, within a narrow range, against the U.S. dollar.

Financial instruments that subject the Company to concentrations of credit risk consist primarily of temporary cash balances and accounts receivable. The Company does not consider itself exposed to a concentration of credit risk with respect to accounts receivable due to its diverse customer base (residential, professional, large business and public entities) operating in numerous industries and located in many regions.

The Company deposits its cash balances with a number of major high credit quality financial institutions and has a policy of limiting its balances deposited with each institution. It does not believe that there is a significant risk of non-performance by these counter parties.

The Company does not believe that it is exposed to significant risks in relation with the aforementioned.

28 EARNINGS PER SHARE

Basic earnings per share have been calculated by dividing net income for the period by the weighted average number of shares outstanding during the period.

29 DIVIDENDS

On April 12, 2003 the Board of Directors, in its capacity as the Ordinary General Assembly of the Company, approved the distribution of dividends amounting to SR 750 million, being 5% of the paid-up capital. These dividends were paid during the second quarter of 2003 to the shareholder outstanding at December 31, 2002 (the Government).

The Board of Directors approved on July 17, 2003 the distribution of semi-annual dividends of SR 8.00 per share for the six-month period ended June 30, 2003. These dividends were paid by the end of the third quarter 2003.

30 SEGMENT INFORMATION

The telecommunications sector is a service sector with rapidly evolving technologies. The Company has commenced identifying and restructuring its operating segments in ways that accomplish the best efficiency levels within the scope of the developments in organizing the telecommunications sector by the CITC, which have recently accelerated resulting in important changes in the identification and segregation of telecom services segments. The latest development was segregating the data and VSAT as separate services having their own regulations.

The Company has achieved a level of progress in this regard despite the long time usually required for the completion of these types of operations and the resulting significant systems changes, due to the complexity of telecom services, particularly the interconnections between these services, which constitute an important part of the requirements to identify revenues, expenses and assets of each segment to properly evaluate segment performance.

The Company is currently working on concluding the readiness of its systems and procedures, and developing its administrative and accounting systems to facilitate the allocation of assets according to its operating segments, to comply with the requirements of the relevant accounting standard issued by the Saudi Organization of Certified Public Accountants. It is expected that this will be accomplished gradually.

31 REDUCTION IN SERVICE RATES

The concerned parties have approved the proposal raised by the Company's Board of Directors for the reduction of service rates for some of its services. These reductions took effect on different dates during 2003, the latest being on April 1, 2003.

32 LICENSE

Within the scope of regulating the telecommunications sector, CITC issued in December 2003 a license to the Company to provide telecommunications services. The Company has raised its objections to the concerned parties on what it considers affecting some of its rights.

33 SUBSEQUENT EVENTS

The Board of Directors in its meeting of 21 Dhul Hujja 1424 H (February 12, 2004) proposed the distribution of semi-annual dividends of SR 14.00 per share for the six month period ended December 31, 2003, resulting in a total dividend of SR 22.00 per share for the year.

34 RECLASSIFICATION

Certain of the 2002 comparative figures have been adjusted to conform with the classifications used in 2003.

35 INTERIM FINACIAL STATEMENTS (UNAUDITED)

Following are the quarterly income statements:

	First Quarter		**Second Quarter**		**Third Quarter**		**Fourth Quarter**	
	2003	**2002**	**2003**	**2002**	**2003**	**2002**	**2003**	**2002**
Total operating revenues	6,705,510	5,407,681	6,302,836	5,843,092	7,044,526	6,237,931	7,239,146	6,058,361
Total operating expenses	(4,452,470)	(4,303,544)	(4,412,127)	(4,589,289)	(4,651,059)	(4,698,254)	(4,576,350)	(5,168,274)
Operating income	**2,253,040**	**1,104,137**	**1,890,709**	**1,253,803**	**2,393,467**	**1,539,677**	**2,662,796**	**890,087**
Other income and expenses, net	59,085	49,250	48,830	(1,068,797)	66,388	101,581	(622,892)	(231,654)
Net income before zakat	**2,312,125**	**1,153,387**	**1,939,539**	**185,006**	**2,459,855**	**1,641,258**	**2,039,904**	**658,433**
Provision for zakat	(52,974)	(34,901)	(50,779)	-	(62,632)	(87,497)	(59,776)	30,148
Net income	**2,259,151**	**1,118,486**	**1,888,760**	**185,006**	**2,397,223**	**1,553,761**	**1,980,128**	**688,581**
Earnings per share	7.53	3.73	6.30	0.62	7.99	5.18	6.60	2.30