Audit Report

OIG-04-021

Audit of the Exchange Stabilization Fund's Fiscal Years 2003 and 2002 Financial Statements

February 18, 2004

Office of Inspector General

Department of the Treasury

Contents

SECTION I –

REPORT OF THE OFFICE OF INSPECTOR GENERAL

To the Assistant Secretary for International Affairs:

We audited the Exchange Stabilization Fund's (ESF) Statements of Financial Position as of September 30, 2003 and 2002, and the related Statements of Income and Retained Earnings, and Cash Flows for the years then ended.

Management's Responsibilities

Management is responsible for (1) preparing the financial statements in conformity with accounting principles generally accepted in the United States of America, (2) establishing and maintaining internal control, and (3) complying with applicable laws and regulations.

Scope of Audits

We conducted our audits in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits 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.

Our responsibility is to express an opinion on the financial statements based on our audits. We believe that our audits provide a reasonable basis for our opinion and our conclusions on internal control and compliance with laws and regulations.

In planning and conducting our audit of ESF's financial statements, we considered its internal control over financial reporting. Specifically, we obtained an understanding of the design of ESF's internal control, determined whether these internal controls had been placed in operation, assessed control risk, and performed tests of controls in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Consequently, we do not provide an opinion on internal control.

As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of ESF's compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. We limited our tests of compliance to these provisions and did not test compliance with all laws and regulations applicable to ESF. We caution that noncompliance may occur and not be detected by these tests and that such testing may not be sufficient for other purposes. Providing an opinion on compliance with laws and regulations was not an objective of our audit and, accordingly, we do not express such an opinion.

We have read the information in the Policy and Operations Statements and assessed whether such information, or the manner of its presentation, is materially inconsistent with the information, or the manner of its presentation, in the financial statements.

Results of Audits

Opinion on the Financial Statements

In our opinion, the financial statements present fairly, in all material respects the financial position of ESF as of September 30, 2003 and 2002, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Our audits were conducted for the purpose of expressing an opinion on ESF's financial statements referred to above. The information contained in the Policy and Operations Statements of ESF is presented for the purpose of additional analysis and is not a required part of the financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the financial statements, and accordingly, we express no opinion on it. However, we compared this information for consistency with the financial statements and, based on this limited work, we found no material inconsistencies.

Internal Control

Internal control is a process, effected by management and other personnel, designed to provide reasonable assurance that the following objectives are met:

- Reliability of financial reporting - transactions are properly recorded, processed, and summarized to permit the preparation of the financial statements in accordance with accounting principles generally accepted in the United States of America, and the safeguarding of assets against loss from unauthorized acquisition, use, or disposition; and

- Compliance with applicable laws and regulations that could have a direct and material effect on the financial statements.

Because of limitations inherent in any internal control, errors or fraud may occur and not be detected. Also, projection of any evaluation of internal control to future periods is subject to the risk that internal control may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

Our consideration of internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. However, we noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses as defined above.

Compliance with Laws and Regulations

The results of our tests of compliance with laws and regulations disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards.*

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We have reviewed our report with the financial management of ESF. Based on mutual agreement, we are issuing this report as final. Should you or your staff have any questions, you may contact me at (202) 927-5400 or a member of your staff may contact Mike Fitzgerald, Director, Financial Audits, at (202) 927-5789. We appreciate the cooperation and the courtesy extended to our staff.

This report is intended solely for the information and use of the management of ESF, the Department of the Treasury, the Office of Management and Budget, and the Congress, and is not intended to be and should not be used by anyone other than these specified parties. However, this report is available as a matter of public record.

/s/
William H. Pugh
Deputy Assistant Inspector General for Financial Management
and Information Technology Audits
December 5, 2003

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The Department of the Treasury

The Secretary of the Treasury
Office of International Affairs
Office of Management
Office of Accounting and Internal Control
Office of Financial Management

SECTION II –

EXCHANGE STABILIZATION FUND FISCAL YEARS 2003 AND 2002 FINANCIAL STATEMENTS

Exchange Stabilization Fund
Policy and Operations Statements
Fiscal Year 2003

The Nature and Function of the Exchange Stabilization Fund

The Gold Reserve Act of 1934 established a fund to be operated by the Secretary of the Treasury, with the approval of the President. Section 10 of the Act provided that "For the purpose of stabilizing the exchange value of the dollar, the Secretary of the Treasury, with the approval of the President, directly or through such agencies as he may designate, is authorized, for the account of the fund established in this section, to deal in gold and foreign exchange and such other instruments of credit and securities as he may deem necessary to carry out the purpose of this section." To this end, the Congress, in 1934, appropriated to the Exchange Stabilization Fund (ESF) the sum of $2 billion out of the increment resulting from the reduction in the "weight of the gold dollar." Subsequent amendments to the Gold Reserve Act approved the operation of the ESF through June 30, 1945. Section 7 of the Bretton Woods Agreements Acts, approved July 31, 1945, continued its operations permanently.

The Bretton Woods Agreements Act also directed the Secretary of the Treasury to pay $1.8 billion from the ESF to the International Monetary Fund (IMF), for the initial U.S. quota subscription in the IMF, thereby reducing the ESF's appropriated capital to $200 million.

Reflecting termination of the fixed exchange rate system, legislation enacted in 1976 (P.L. 94-564, effective April 1, 1978, the date of entry into force of the Second Amendment of the IMF Articles of Agreement) amended the language of Section 10 of the Gold Reserve Act to specify that the ESF is to be utilized as the Secretary "may deem necessary to and consistent with the United States obligations in the International Monetary Fund." In 1977, P.L. 95-147 further amended Section 10 of the Gold Reserve Act. Following codification, Section 10 now provides as follows:

> Consistent with the obligations of the Government in the International Monetary Fund on orderly exchange arrangements and a stable system of exchange rates, the Secretary or an agency designated by the Secretary, with the approval of the President, may deal in gold, foreign exchange, and other instruments of credit and securities the Secretary considers necessary. However, a loan or credit to a foreign entity or government of a foreign country may be made for more than 6 months in a 12-month period only if the President gives Congress a written statement that unique or emergency circumstances require the loan or credit be for more than 6 months (31 U.S.C. 5302 (b)).

Pursuant to the Special Drawing Rights Act of 1968 (P.L. 90-349, amended by P.L. 94-564, which was approved October 18, 1976 and became effective April 1, 1978), Special Drawing Rights (SDRs) allocated by the IMF to the United States or otherwise acquired by the United States are resources of the ESF.

Section 286p of Title 22 of the United States Code allows for SDRs to be monetized/demonetized through the issuance/redemption by the Secretary of the Treasury of SDR certificates to the Federal Reserve Banks in exchange for dollars. The total amount of SDR certificates outstanding cannot exceed the dollar equivalent of ESF (i.e., U.S.) holdings of SDRs; such certificates are a liability of the ESF.

Foreign Currency Operations

During fiscal year 2003, the ESF engaged in no market transactions.

a. Euros and Japanese Yen

The ESF had a net valuation gain of $2.2 billion for both Euro and Japanese Yen. The interest earnings were in the amount of $265.4 million equivalent on its euro assets and $0.4 million equivalent on its yen assets.

b. Mexico

In December 2003, the Treasury and Federal Reserve Bank of New York renewed the Exchange Stabilization Agreement with Mexico for another year to December 2004.

SDR Operations

In January 2003, the United States sold to Argentina in a transaction arranged by the IMF SDR 740.9 million from the SDR holdings of the ESF. The dollar proceeds of the sale amounted to $1 billion.

As of September 30, 2003, U.S. holdings (assets) of SDRs totaled SDR 8.4 billion ($12.1 billion equivalent), a net decrease of SDR 416.3 million during Fiscal Year 2003. However, the dollar value had a net increase of $352.8 million, resulting primarily from a net valuation gain of $919.6 million and $348.1 million for SDRs received from the IMF as remuneration on the U.S. reserve position in the IMF. The ESF reimbursed the Treasury's General Fund for the dollar value of this remuneration. The ESF earned interest of $207.0 million equivalent on its SDR holdings.

As of September 30, 2003, cumulative allocations to (liabilities of) the United States totaled SDR 4.9 billion ($7.0 billion equivalent). These liabilities would come due only in the event of liquidation of, or U.S. withdrawal from, the SDR Department of the IMF, or cancellation of SDRs.

There were $2.2 billion of SDR certificates that had been issued to the Federal Reserve System prior to Fiscal Year 2003 and remained outstanding at the end of the Fiscal Year.

Income and Expense

Interest revenue totaled $597.1 million, consisting of $124.2 million in interest on dollar holdings invested in U.S. Government securities, $207.0 million equivalent in interest on SDR holdings, and $265.8 million equivalent in interest on foreign currency investments.

Interest expense totaled $119.4 million, which included $118.8 million in interest charges on SDR Allocations and $0.6 million paid by the ESF to the Treasury General Fund on the dollar counterpart of SDRs received as remuneration on the U.S. reserve position in the IMF.

Department of the Treasury
Exchange Stabilization Fund
Statement of Financial Position
(In Thousands)

As of September 30	2003	2002
Assets		
Cash and Cash Equivalents (Note 2)		
U.S. Government Securities	$ 10,502,415	$ 9,716,954
Foreign Currency Denominated Assets	6,056,320	5,064,341
Total Cash and Cash Equivalents	16,558,735	14,781,295
Other Foreign Currency Denominated Assets (Note 3)	3,543,260	2,915,630
Special Drawing Right Holdings (Note 4)	12,062,467	11,709,606
Investment Securities, Held to Maturity (Note 5)	8,951,912	8,065,561
Accrued Interest Receivable	102,567	118,965
Total Assets	$ 41,218,941	$ 37,591,057
Liabilities and Equity		
Liabilities		
Certificates Issued to Federal Reserve Banks (Note 6)	2,200,000	2,200,000
Special Drawing Right Allocations (Note 4)	7,005,299	6,480,559
Accrued Expenses and Other	18,181	24,396
Total Liabilities	$ 9,223,480	$ 8,704,955
Equity		
Appropriated Capital	200,000	200,000
Retained Earnings	31,795,461	28,686,102
Total Equity	31,995,461	28,886,102
Total Liabilities and Equity	$ 41,218,941	$ 37,591,057

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

Department of the Treasury
Exchange Stabilization Fund
Statement of Income and Retained Earnings
(In Thousands)

Years Ended September 30	2003	2002
Interest Revenue:		
Interest on U. S. Government Securities	$ 124,232	$ 183,878
Interest on Foreign Currency Denominated Assets	193,875	212,235
Interest on Special Drawing Right Holdings	206,976	256,129
Interest on Investment Securities	71,970	55,780
Total Interest Revenue	597,053	708,022
Interest Expense		
Interest on Special Drawing Right Allocations	118,820	144,566
Interest on Special Drawing Right Received as Remuneration by the U.S. Treasury	577	1,008
Total Interest Expense	119,397	145,574
Net Interest Revenue	477,656	562,448
Net Gains		
Gains on Valuation of Special Drawing Rights	395,793	137,022
Gains on Valuation of Foreign Currency Denominated Assets	2,236,334	493,932
Total Net Gains	2,632,127	630,954
Other Expenses		
International Monetary Fund Annual Assessment	424	678
Net Income	$ 3,109,359	$ 1,192,724
Retained Earnings, Beginning of Year	$ 28,686,102	$ 27,493,378
Retained Earnings, End of Year	$ 31,795,461	$ 28,686,102

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

Department of the Treasury
Exchange Stabilization Fund
Statement of Cash Flows
(In Thousands)

Years Ended September 30	2003	2002
Cash Flows from Operating Activities:		
Interest Received on U.S. Government Securities	$ 124,232	$ 185,647
Interest Received on Foreign Currency Denominated Assets	204,911	219,071
Interest Received on Investment Securities	97,249	67,962
Net Gain on Valuation of Foreign Currency Denominated Assets	2,236,334	493,932
Other	(32,534)	(29,126)
Net Cash Provided by Operating Activities	2,630,192	937,486
Cash Flows from Investing Activities:		
Net Increase in Foreign Currency Denominated Assets	(627,630)	(326,931)
Net Increase in Investment Securities	(886,351)	(1,219,844)
Purchases of Special Drawings Rights Received as Remuneration by the U.S. Treasury and Related Interest	(348,779)	(482,932)
Sales of Special Drawings Rights	1,010,008	0
Net Cash Used in Investing Activities	(852,752)	(2,029,707)
Net Increase (Decrease) in Cash and Cash Equivalents	1,777,440	(1,092,221)
Cash and Cash Equivalents at Beginning of Year	14,781,295	15,873,516
Cash and Cash Equivalents at End of Year	$ 16,558,735	$ 14,781,295

Reconciliation of Net Income to Net Cash Provided by Operating Activities

	2003	2002
Net Income	$ 3,109,359	$ 1,192,724
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:		
Increase in Special Drawing Right Holdings Due to Valuation	(919,609)	(301,928)
Net Interest Received in Special Drawing Rights	(94,481)	(5,409)
Decrease in Accrued Interest Receivable	16,398	7,556
Increase in Special Drawing Right Allocations Due to Valuation	524,740	165,014
Decrease in Accrued Expenses and Other	(6,215)	(120,471)
Total Adjustments	(479,167)	(255,238)
Net Cash Provided by Operating Activities	$ 2,630,192	$ 937,486

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

NOTES TO THE FINANCIAL STATEMENTS

Note 1. Summary of Significant Accounting Policies

The Exchange Stabilization Fund (ESF) was established as a result of the Gold Reserve Act of 1934, as amended, to be operated by the Secretary of the Treasury, with the approval of the President, consistent with the obligations of the U.S. Government in the International Monetary Fund (IMF) on orderly exchange arrangements and a stable system of exchange rates. To this end, the Secretary of the Treasury may deal in gold, foreign exchange, and other instruments of credit and securities.

A. Basis of Accounting & Presentation

The ESF has historically prepared its financial statements in accordance with generally accepted accounting principles, based on accounting standards issued by the Financial Accounting Standards Board (FASB), the private-sector standards-setting body. The Federal Accounting Standards Advisory Board (FASAB) was designated by the American Institute of Certified Public Accountants (AICPA) as the standards-setting body for financial statements of federal government entities, with respect to the establishment of generally accepted accounting principles. FASAB has indicated, however, that financial statements prepared based upon accounting standards published by the FASB may also be regarded as in accordance with generally accepted accounting principles for those federal entities, such as the ESF, that have issued financial statements based upon FASB accounting standards in the past. Accordingly, consistent with historical reporting, the ESF financial statements are presented in accordance with accounting standards published by the FASB. In accordance with generally accepted accounting principles, the preparation of financial statements requires the use of management estimates.

B. Fair Values of Financial Instruments

Cash and Cash Equivalents, which consist of U.S. Government securities and Foreign Currency Denominated Assets (FCDA), are reported in the Statement of Financial Position at amounts that approximate their fair values. The fair value of Investment Securities is based upon quoted market prices (See Note 5). FCDA, Other FCDAs, Special Drawing Right (SDR) Holdings, and SDR Allocations have been revalued in the Statement of Financial Position, using current exchange rates, to amounts which approximate fair value. The SDR Certificates issued to Federal Reserve Banks (FRB) are reflected on the Statement of Financial Position at their face value. It is not practicable to estimate the fair value of these Certificates issued to FRBs since these Certificates contain no specific terms of repayment.

C. Translation of Foreign Currency Denominated Assets and Liabilities

In accordance with Statement on Financial Accounting Standards (SFAS) No. 52, "Foreign Currency Translation, FCDA and liabilities are revalued daily to reflect current exchange rates in effect as of the reporting date. The gains or losses resulting from changes in exchange rates are reported separately in the Statement of Income and Retained Earnings.

Note 1. Summary of Significant Accounting Policies (continued)

D. U.S. Government Securities

ESF invests dollars in excess of its immediate needs in overnight, non-marketable U.S. Government securities issued by the Treasury. The interest rate paid on the investments is the overnight repurchase agreement rate as established by the Bureau of Public Debt.

Note 2. Cash and Cash Equivalents

Cash equivalents are short-term, highly liquid investments that are both readily convertible to known amounts of cash, and so near their maturity that they present insignificant risk of change in value due to changes in interest rates. Generally, only investments with original maturities of three months or less qualify under that definition. U.S. Government securities and FCDAs with original maturities of three months or less, except for foreign currencies acquired under swap agreements with developing countries, are treated as cash equivalents.

The ESF invests a portion of its European Euro holdings through repurchase agreements in securities issued by, and backed by the full faith and credit of, the Federal Republic of Germany. As of September 30, 2003 and September 30, 2002 the amounts of repurchase agreements were approximately $1.9 billion and $1.5 billion respectively. These repurchase agreements are considered to be FCDAs with original maturities of three months or less, which are treated as cash equivalents, as discussed above. Such investments are made by the Federal Reserve Bank of New York (FRBNY), as fiscal agent of the Treasury, in connection with the ESF’s participation in such repurchase agreements. In this capacity, FRBNY enters into agreements under which German government securities are purchased from, and subsequently resold to, private counterparties. Such transactions are settled through a tri-party agent, Deutsche Bank. The securities are held by Deutsche Bank for FRBNY pending resale and are not transferred back to a private counterparty upon resale until cash has been received. The FRBNY instructs the tri-party agent on matters related to these investments. The amounts held as of September 30, 2003 and September 30, 2002 were as follows:

Note 2. Cash and Cash Equivalents (Continued)

September 30 (In Thousands)	**2003**	**2002**
Cash and Cash Equivalents:		
U. S. Government Securities	$10,502,415	$ 9,716,954
FCDAs:		
European Euro	$ 4,638,633	$ 3,767,445
Japanese Yen	$ 1,417,687	$ 1,296,896
Total Foreign Currency Denominated Assets	$ 6,056,320	$ 5,064,341
Total Cash and Cash Equivalents	$16,558,735	$14,781,295

Note 3. Other FCDAs

Operations of the ESF result in the holding of various foreign currencies. The ESF normally invests its foreign currency holdings in interest bearing assets issued by or held through foreign governments or monetary authorities. Other FCDAs are assets with maturities greater than three months, and include any foreign currencies acquired under swap agreements with various countries (See Note 7).

September 30 (In Thousands)	**2003**	**2002**
Other FCDAs:		
European Euro	$ 3,543,260	$ 2,915,630
Total Other FCDAs	$ 3,543,260	$ 2,915,630

Note 4. SDRs

The SDR is an international reserve asset created by the IMF. It was created as a supplement to existing reserve assets, and on several occasions SDRs have been allocated by the IMF to members participating in the IMF's SDR department. Its value as a reserve asset derives, essentially, from the commitments of participants to hold and accept SDRs and to honor various obligations connected with its proper functioning as a reserve asset.

Note 4. SDRs (Continued)

Pursuant to the Special Drawing Act of 1968, as amended, SDRs allocated to or otherwise acquired by the United States are resources of ESF. SDRs, once allocated, are permanent resources unless:

a. they are canceled by an 85 percent majority decision of the total voting power of the Board of Governor's;

b. the SDR Department of the IMF is liquidated;

c. the IMF is liquidated; or

d. the United States chooses to withdraw from the IMF or terminate its participation in the SDR Department.

Except for the payment of interest and charges on SDR allocations to the United States, the payment of the ESF's liability related to the SDR allocations is conditional on events listed above, in which the United States has a substantial or controlling voice. Allocations of SDRs were made on January 1, 1970, 1971, 1972, 1979, 1980 and 1981. Since 1981, the IMF has made no further allocations of SDRs. As of September 30, 2003 and September 30, 2002, the amounts of SDR allocations was the equivalent of $7 billion and $6.5 billion, respectively.

On a daily basis, the IMF calculates the value of the SDR using the market value, in terms of the U.S. dollar, of each of the four freely usable weighted currencies, as defined by the IMF. These currencies are the U.S. dollar, the European Euro (components consist of the French and German weights), the Japanese yen, and the pound sterling. The ESF's SDR holdings and allocations are revalued monthly based on the SDR valuation rate calculated by the IMF, and an unrealized gain or loss on revaluation is recognized.

During Fiscal Years (FY) 2003 and 2002, the ESF purchased, at the prevailing rates, $348.1 million and $371.8 million, respectively, equivalent of SDRs received from the IMF by the General Fund of the U.S. Government as remuneration (interest) on the U.S. reserve position in the IMF, and paid the General Fund $.6 million and $1.7 million in FY 2003 and 2002, respectively, in interest on dollars due the General Fund in return for SDRs received as remuneration. ESF sold SDRs to Argentina in FY 2003 in the amount of $1 billion. ESF did not sell or purchase SDRs from participating members during FY 2002.

The following charts reflect the actual activity (i.e. amounts paid and received) related to SDRs during fiscal years 2003 and 2002.

Note 4. SDRs (Continued)

September 30, 2003	**SDR**	**Dollar Equivalent**
Special Drawing Rights (In Thousands**):**		
Beginning Balance:	8,852,873	$11,709,606
Interest Received on Holdings	162,460	221,699
Interest Paid on Allocations	(92,393)	(126,139)
Remunerations	254,846	348,069
IMF Annual Assessment	(270)	(369)
Sales	(740,985)	(1,010,008)
Net Gain on Valuation of Holdings	-	919,609
Ending Balance:	8,436,531	$12,062,467

September 30, 2002	**SDR**	**Dollar Equivalent**
Special Drawing Rights (In Thousands**):**		
Beginning Balance:	8,471,101	$10,919,337
Interest Received on Holdings	212,944	272,147
Interest Paid on Allocations	(121,218)	(154,897)
Remunerations	290,596	371,778
IMF Annual Assessment	(550)	(687)
Sales	-	-
Net Gain on Valuation of Holdings	-	301,928
Ending Balance:	8,852,873	$11,709,606

Note 5. Investments and Related Interest

In accordance with SFAS 115, "Accounting for Certain Investments in Debt and Equity Securities", securities that the ESF has both the positive intent and ability to hold to maturity are classified as investment securities held to maturity and carried at historical cost, adjusted for amortization of premiums and accretion of discounts. Interest on investment securities, amortization of premiums, and accretion of discounts are reported in interest on investment securities.

The following schedule shows investment securities at their amortized cost and by year of maturity as of September 30, 2003 and September 30, 2002. In March 2002, French Bonds and French Notes were purchased as investment securities. The investment securities maturing after one year are the German bonds, French bonds and French notes. There are no securities maturing after ten years.

Note 5.   Investments and Related Interest (Continued)

September 30	**2003**	**2002**
Securities, Held to Maturity (In Thousands)**:**		
All Securities (at Amortized Cost)		
German Bonds	$1,116,848	$ 930,474
German Bubills	286,800	238,712
French Bonds	320,270	248,774
French Notes	170,142	187,170
Japanese T – Bills	3,634,258	3,326,712
Japanese Financing Bills	3,423,594	3,133,719
Total Amortized Cost	$8,951,912	$8,065,561
Maturing Within 1 Year		
Fair Value:		
German Bonds	$ 196,458	$ 115,132
German Bubills	286,813	238,827
French Bonds	84,898	43,174
French Notes	39,150	64,256
Japanese T-Bills	3,634,139	3,326,695
Japanese Financing Bills	3,423,630	3,133,709
Total Fair Value	$7,665,088	$6,921,793
Amortized Cost:		
German Bonds	$ 189,833	$ 110,222
German Bubills	286,800	238,712
French Bonds	81,616	40,296
French Notes	37,843	61,952
Japanese T – Bills	3,634,258	3,326,712
Japanese Financing Bills	3,423,594	3,133,719
Total Amortized Cost	$7,653,944	$6,911,613

Gross Unrealized		
Holdings Gain (Loss):		
German Bonds	$ 6,625	$ 4,910
German Bubills	$ 13	$ 115
French Bonds	$ 3,282	$ 2,878
French Notes	$ 1,307	$ 2,304
Japanese T-Bills	$ (119)	$ (17)
Japanese Financing Bills	$ 36	$ (10)
Total Gross Unrealized Net Holdings Gain	$ 11,144	$ 10,180

Maturing after 1 Year through 5 Years (German and French Bonds/Notes)

Fair Value:		
German Bonds	$ 832,458	$ 486,050
French Bonds	254,297	221,173
French Notes	141,412	132,732
Total Fair Value	$1,228,167	$ 839,955
Amortized Cost:		
German Bonds	$ 773,061	$ 457,344
French Bonds	238,654	208,478
French Notes	132,299	125,218
Total Amortized Cost	$1,144,014	$ 791,040
Gross Unrealized		
Holdings Gain:		
German Bonds	$ 59,397	$ 28,706
French Bonds	$ 15,643	$ 12,695
French Notes	$ 9,113	$ 7,514
Total Gross Unrealized Holdings Gain	$ 84,153	$ 48,915

(Maturing after 5 Years through 10 Years (German Bonds only)

Total Fair Value	$ 172,790	$ 387,369
Total Amortized Cost	$ 153,954	$ 362,908
Total Gross Unrealized Holdings Gain	$ 18,836	$ 24,461

Note 6. Certificates Issued to Federal Reserve Banks

The Special Drawing Rights Act of 1968 authorized the Secretary of the Treasury to issue certificates, not to exceed the value of SDR holdings, to the FRB in return for interest free dollar amounts equal to the face value of certificates issued (SDR monetization). The certificates may be issued for the purpose of financing the acquisition of SDRs from other countries or to provide resources for financing other ESF operations. Certificates issued are to be redeemed by ESF at such times and in such amounts as the Secretary of the Treasury may determine (SDR demonetization).

As of September 30, 2003 and September 30, 2002 the amounts of SDR certificates outstanding were $2.2 billion, while the values of SDR holdings were $12.1 billion and $11.7 billion, for differences of $9.9 billion and $9.5 billion respectively. During FY 2003 and 2002, ESF transacted no monetizations or demonetizations.

Note 7. Foreign Currency Agreements

Foreign Currency Agreements represent swap agreements between Treasury and various countries that provide for drawings of dollars by those countries and/or drawings of foreign currencies by Treasury. Treasury enters into these agreements through the ESF. Any balances the ESF may hold under such agreements are held for other than trading purposes and are included in as Other FCDA's in the Statement of Financial Position (See Note 3). ESF is exposed to credit risk on foreign currency agreements in the event of default by counterparties to the extent of any amounts that have been recorded in the Statement of Financial Position. Market risk occurs as a result of fluctuations in currency exchange rates. The ESF is not exposed to market risk on foreign currency agreements that could occur as a result of fluctuations in currency exchange rates. Under these agreements, the ESF will receive an agreed upon amount in dollars upon maturity regardless of currency fluctuations.

ESF's foreign currency agreements and guarantees consisted of the following at September 30, 2003 and September 30, 2002:

a. In April 1994, Treasury signed the North American Framework Agreement, which includes an Exchange Stabilization Agreement (ESA), with Mexico. The ESA provides for a $3 billion standing swap line. The amounts and terms (including the assured source of repayment) of any new borrowings under the North American Framework Agreement would need to be negotiated. There were no drawings outstanding on these agreements as of September 30, 2003 and 2002. In December 2003, the Treasury and FRB extended this agreement to December 2004.

b. On August 4, 2002, the Treasury entered into a swap agreement with Uruguay to provide temporary financial support from the ESF prior to the receipt of Uruguay of disbursements from the IMF and other international financial institutions. The ESF provided a $1.466 billion credit to Uruguay on August 5, and Uruguay made full repayment by August 9. Uruguay paid the ESF $271 thousand in interest on this credit.