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Central Bank of Bahrain

Financial Stability Directorate

Economic Report

2012

Economic Report 2012

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Preface

In addition to its regulatory functions, the Central Bank of Bahrain (CBB) monitors the performance of the Bahraini economy on a continuous basis. As part of this effort, the *Economic Report* is produced annually by the Financial Stability Directorate. It discusses international, regional, and domestic economic developments over the course of the year. It also covers monetary, financial, and capital market developments as well as public finances and the balance of payments.

Executive Summary

In 2012 the global economy faced a challenging environment and was unable to sustain a decent recovery. Overall growth was unbalanced with advanced economies faring rather well (aside from Europe). Emerging economies are delivered tempered but solid growth, yet have not experienced a significant rebound to reach pre-crisis growth levels. Total world output grew by 3.2%, while there were mixed inflation trends. Unemployment trends are concerning for the Euro Area, as the fallout of the Cypriot issue crystallises.

The GCC countries continued to reap the windfall of high oil revenues, which in turn have led to increased effectiveness of expansionary fiscal policies. The region performed strongly as oil prices averaged over USD 100 for the entirety of 2011 and 2012. GCC economies remained robust buoyed by sustained high government spending, fiscal and external surpluses coupled with a further recovery of the private sector.

Projections remain mixed for 2013, with global growth set at 3.3%, and inflation to decline only in advanced economies (1.7% down from 2.0% in 2012). Unemployment is Europe's main concern, while the outlook for key commodities appears to indicate a continuation of increasing prices.

The Bahrain economy registered a growth rate of 4.1% in nominal terms and a real growth rate of 3.4% in GDP. The growth witnessed was a continuation of the momentum from the second half of 2011 as well as recovery in some sectors while inflation remained within a reasonable range, indicating some increase in consumption. Domestic oil output increased, supporting the economy in general.

As the major employer and promoter of capital projects, the growth in government services and consumption positively affected the economy, particularly construction and manufacturing sectors. The hotels and restaurants and real estate sectors recovered in the face of the economic lull in 2011, while the trade sector declined in the face of weaker global demand.

Bahrain experienced a reversal of the minor deflation of 2011 with the consumer price index (CPI) increasing by 2.8% for 2012. The main contributors were a 12.2% increase in the prices of alcoholic beverages and tobacco as well as recreation and culture which grew by 20.5%. The stark increase in prices for recreation and culture is in line with the developments in growth witnessed during 2012. As the hotels and tourism sector rebounded during the year, prices increased significantly.

In 2012, monetary developments in Bahrain reflected regional trends as well as domestic economic developments. Given the Bahraini dinar's peg against the US dollar, domestic interest rates largely tracked US policy rates during the year which remained low as a measure to offset the economic downturn.

Money supply showed a mixed trend in 2012 compared to the increases witnessed in 2011. Currency in circulation (currency outside banks) registered a 4.8% growth in

2012, while M1 (currency in circulation plus demand deposits) declined by 1.0%. Despite the decrease in M1, M2 (M1 plus time and savings deposits) rose by 4.1%.

In 2012, there was a decrease in the number of financial institutions, and credit facilities extended. The aggregate balance sheets of banks and the number of employees in the financial sector decreased in 2012. The financial sector however, remains the single largest non-oil component of real GDP, accounting for 17.1%.

The aggregate balance sheet for the banking system (conventional and Islamic retail and wholesale banks) decreased in total by USD 10.8 billion, or 5.5%. Wholesale banks represented 61.5% of the total, while retail banks accounted for 38.5%.

In total, domestic banking assets amounted to USD 48.2 billion, registering an increase of USD 0.8 billion (1.7%). Foreign assets amounted to USD 138.1 billion, a decrease of USD 11.6 billion (7.7%). Domestic liabilities increased by 2.0% to reach USD 51.2 billion while total foreign liabilities decreased by 8.0% to reach USD 135.1 billion.

The banking systems assets over time have been mainly concentrated in GCC and European economies. However, over the period 2010-2012, the GCC share of total assets decreased from 29.5% to 23.8%. Europe’s share of total assets decreased from 29.3% to 27.3% for the same period. GCC assets experienced the largest decrease from 2010-2012. Assets in the Asia region increased from 7.6% in 2010 to 7.8% in 2012, while assets in the Americas increased from 8.9% to 11.0% for the same period. As in previous years, most assets are denominated in US dollars (56.9%).

Retail banks performed well, however, with total assets increasing by BD 1,628.4 million or 6.4% over 2011. The growth was due to an increase in domestic assets, which expanded by 8.0% to reach BD 15,180.2 million.

Outstanding credit facilities increased modestly for the majority of economic sectors in Bahrain. Total outstanding credit facilities extended by retail banks to the different sectors of the domestic economy amounted to BD 6,848.7 million at end-2012, up 6.3% from the BD 6,444.4 million at end-2011.

Although the Bahrain economy has diversified away from the oil sector, oil revenues continue to play a significant role in the governments’ fiscal balance. Oil prices remained consistently high during the year 2012, and as a result, government revenues increased modestly by 7.5% to reach BD 3,034.2 million, concurrently, government expenditure increased by 14.3% to reach BD 3,260.9 million during the same period.

Given the recent developments and increased government spending on social projects, the fiscal position of Bahrain has led to it recording a BD 226.7 million fiscal deficit before rollover. The fiscal deficit accounted for 2.0% of the gross domestic product (GDP) of Bahrain in 2012.

The size of Bahrain’s public debt (securities only) has increased during the year 2012 with the total debt outstanding at the end of 2012 amounting to BD 3,868.5 million, or 35.9% of GDP. The increase in total outstanding debt in 2012 stems mainly from the increased issuance of development bonds.

With regard to the external sector Bahrain's trend of current account surplus continued in 2012. It recorded a current account surplus of BD 835.4 million and accounts for 7% of GDP. Oil continues to comprise the major commodity of the kingdom's external trade, representing 77% of total exports and 67% of total imports.

The capital and financial account registered a net outflow of BD 880.0 million, Bahrain continues to be a net exporter of capital to the rest of the world. The capital account showed a net inflow of BD 37.6 million and the financial account registered a net outflow of BD 917.6 million.

Bahrain's net international investment position rose to BD 8,504.8 million in 2012 (a 10.6% increase over 2011). Foreign assets fell by 2.4% to BD 60,493.3 million in, while on the other hand, foreign liabilities decreased to BD 51,988.5 million in 2012 (a 4.3% decrease).

Chapter

1

1. International and Regional Economic Developments

Overview

A. World Economy

B. GCC Economies

Overview

In 2012 the global economy was unable to sustain a decent recovery as challenges and uncertainty intensified. Despite robust financial markets and confidence returning in several emerging economies, overall growth has continued to be too weak and the situation has even worsened in some countries. For 2013, the world economy is forecast to slow down.

In 2012, economic performance was not identical between the regions. Broadly, it was as follows:

- Economic fundamentals of the United States improved progressively. Real GDP was higher in 2012 than its 2011's level, driven by a gradual consolidation of private demand and by higher private consumption. The US economy experienced an upsurge in home purchases and non-residential investments. Monetary policy was marked by low interest rates and an improvement in the housing and labour markets. IMF data shows that the US stands out as one of the strongest of the advanced economies and its growth is forecast to be 1.9% in 2013 and 3% in 2014.

- In the Euro Area, the situation has worsened with the bailout of Cyprus. The Cyprus crisis added more uncertainty on the future of the area and confidence became shaky. Growth rates were revised by the IMF, moving from a positive growth of 0.25% to a contraction of 0.25% in 2013. It is noteworthy that the largest Euro Area economies, like France, Germany, Netherlands have also seen their outlook revised. This is due to decreasing competitiveness and low export activities. Europe enters the year 2013 facing a serious unemployment challenge. The unemployment rate increased to a record low of 11.8% in November 2012.

- With regard to emerging economies, they are delivering tempered but solid growth. Currently, they have still not experienced a significant rebound and have not yet reached pre-crisis growth levels. The drop in demand for commodities, especially from China and India, is the main factor behind the decrease in their growth rates. Moreover, the persistence of social and political unrest in some countries (Syria, Yemen, Egypt, Sudan and Libya) is also another reason behind the slowdown in MENA region.

- The GCC countries continued to reap the windfall of high oil revenues, which in turn have led to increased effectiveness of expansionary fiscal policies.

A. World Economy

1. Output

During 2012, world output grew by 3.2% (Table 1-1). This growth, however, was geographically uneven as it was more modest among advanced economies which grew at 1.2%, while emerging and developing economies experienced more robust growth with output rising by 5.3%.

Table 1-1: World Economic Growth

	2009	2010	2011	2012	2013*	2014*
World output	-0.5	5.3	4.0	3.2	3.3	4.0
Advanced Economies	-3.4	3.2	1.6	1.2	1.2	2.2
United States	-2.6	3.0	1.8	2.2	1.9	3.0
Euro Area	-4.1	1.9	1.4	-0.6	-0.3	1.1
Japan	-5.5	4.7	-0.6	2.0	1.6	1.4
Emerging & Developing Economies	2.7	7.6	6.4	5.1	5.3	5.7
China	9.2	10.4	9.3	7.8	8.0	8.2
India	6.8	11.2	7.7	4.0	5.7	6.2
Middle East and North Africa	3.0	5.5	4.0	4.8	3.1	3.7

** Forecasts*
Source: IMF, World Economic Outlook, April 2013.

As uncertainty persists and the global economy remains fragile, the projections for 2013 and 2014 show that the world economy will continue to grow more modestly with growth rates of 3.3% and 4.0% respectively.

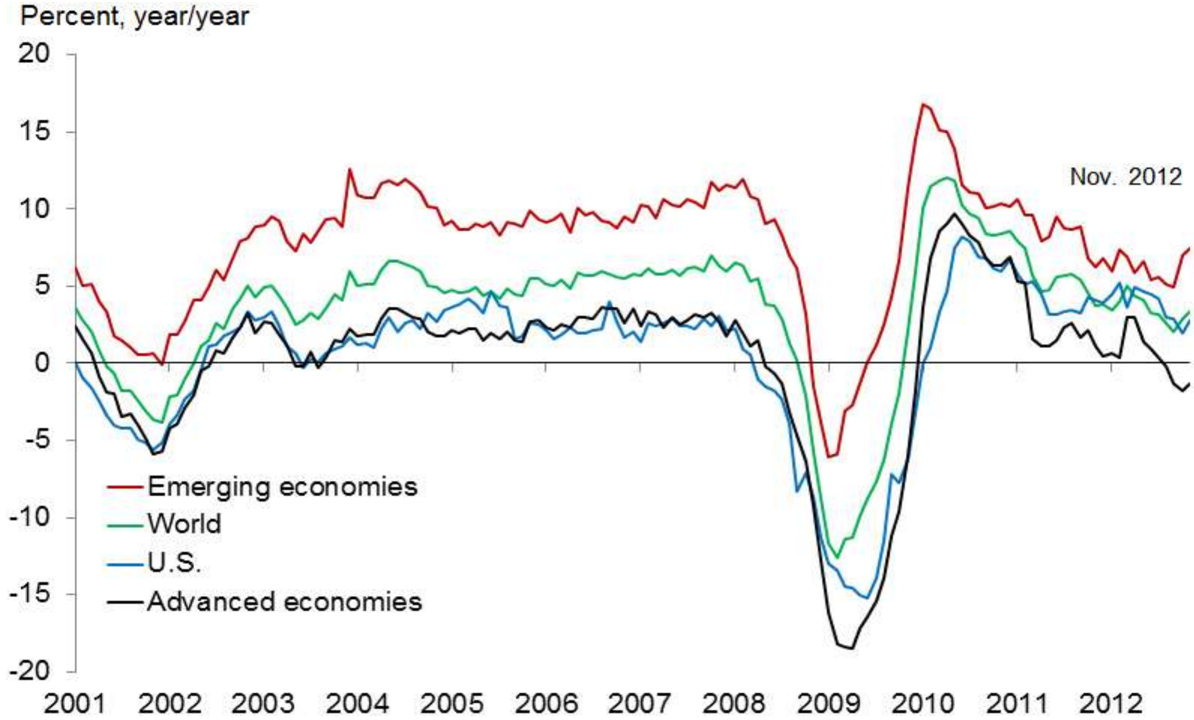
Advanced economies are expected to grow by 1.2% in 2013 and 2.2% in 2014. The United States experienced a higher than expected growth rate by 2.2% in 2012 despite the extensive fiscal drag and higher payroll taxes. The performance shows new optimism for the US and a restoration of investor confidence which seemed unrelated to global uncertainty. Japan also realised a high growth rate of 2.0% in the year, compared to a contraction of 0.6% of 2011 which was caused by the spillover effects of the Tsunami.

The Euro Area recorded a negative growth of 0.6% caused by a decline in exports for the larger economies (Germany and France). The area is forecast to experience a further negative growth rate in 2013 by 0.3%. This is mainly due to the sovereign debt crisis and its consequences on the overall economic performance of the region. Germany, the largest economy in Europe, is expected to grow by 1% in 2013 while France will probably stagnate and PIGSC countries will contract (not including Ireland) further as a result of the significant fiscal drag and weak economic performance.

Regarding emerging and developing economies, they are forecast to experience sustained growth at 5.3% for 2013 and 5.7% for 2014. According to the IMF, MENA countries recorded a growth rate by 4.8% in 2012 and will grow by 3.1% in 2013 and by 3.7% in 2014.

The growth rate of emerging and developing economies is supported by high growth in industrial production (Chart1-1). The US also recorded a positive growth rate; however, advanced economies are still posting a negative year-over-year industrial production growth rate.

Chart 1-1: Industrial Production Growth



Source: Netherland Bureau for Economic Policy Analysis/Haver Analytics

2. Inflation

For the year 2012, inflation, as measured by consumer prices, for advanced economies recorded a 2.0% growth, down from 2.7% in 2011 (Table 1-2). In general, inflation is expected to remain stable in both advanced and emerging economies, leaving central banks to focus on growth instead. As the table below shows consumer prices in emerging and developing markets was 5.9% during the year, lower than the 7.2% recorded in 2011.

Table 1-2: Consumer Prices, All items

	2008	2009	2010	2011	2012	2013*	2014*
Advanced Economies	3.4	0.1	1.5	2.7	2.0	1.7	2.0
Emerging and Developing Countries	9.5	5.3	6.1	7.2	5.9	5.9	5.6

**Forecasts*
Source: IMF, World Economic Outlook, April 2013.

The IMF forecasts that in 2013 there will be a 1.7% growth in consumer prices for advanced economies, while developing economies are expected to see inflation of 5.9%. The slowdown in inflation is due to expected decreases in food and energy prices which should be sustained.

Consumer prices are expected to decrease further in 2014 for advanced economies and emerging and developing countries as well.

3. Unemployment

In 2012, unemployment increased for advanced economies moving from 7.9% in 2011 to 8.0% in 2012 (Table 1-3). While unemployment rates in the United States and Japan have fallen compared to their levels in 2011, the situation in the Euro Area has worsened as the unemployment rate increased to reach 11.4%; higher than the 10.1% recorded in 2011. The sovereign debt crisis has considerably affected the labour market in Europe especially in PIIGS countries.

In first two months of 2013, overall European unemployment hit 12%. The youth unemployment rate was 23.9% (58.4% Greece; 55.7% Spain; 38.2% Portugal; 37.8% Italy; 30.8% Ireland). Many Cypriots (from all ages) are expected to worsen these numbers.

Table 1-3: Unemployment in Advanced Economies (%)

	2009	2010	2011	2012	2013*	2014*
Advanced Economies	8.0	8.3	7.9	8.0	8.2	8.1
United States	9.3	9.6	9.0	8.1	7.7	7.5
Euro Area	9.4	10.0	10.1	11.4	12.3	12.3
Japan	5.1	5.1	4.5	4.4	4.1	4.1

** Forecasts*
Source: IMF, World Economic Outlook, April 2013.

The IMF predicts that in 2013 unemployment rates for advanced economies will be at the level of 8.2% and then decrease slightly to 8.1% in 2014. In the US, average unemployment is expected to move from 8.1% in 2012 to 7.7% in 2013 and then to 7.5% in 2014. By contrast, unemployment rates are relatively low in Japan where it was 4.4% in 2012 and expected to decrease slightly in 2013 and 2014.

4. Exchange Rates

At end-2012, the Euro, the pound sterling and the Japanese Yen depreciated against the SDR from their levels at the end of 2011. While the pound sterling depreciated mildly by 2.51%, the Yen depreciated by 6.67% (Table 1-4). At the end of 2012, the US dollar’s rate appreciated against the SDR by 2.54%

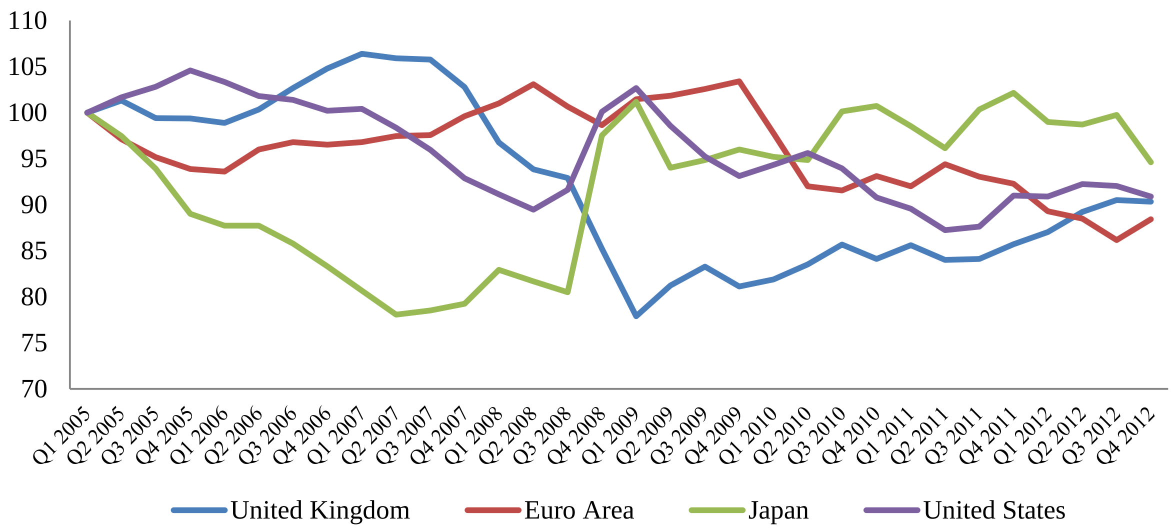
Table 1-4: Exchange Rates of Major Currencies against the SDR

Currencies	2011	2012			
		Q1	Q2	Q3	Q4
US dollar	1.57	1.55	1.51	1.54	1.53
Euro	1.145	1.16	1.2	1.19	1.16
Japanese Yen	124.995	127.26	120.34	119.63	133.34
Pound Sterling	0.995	1.03	1.02	1.05	1.02

Source: IMF, International Financial Statistics Database.

The real effective exchange rate (REER) is the exchange rate of a currency against a basket of world currencies adjusted for inflation. From the fourth quarter of 2011 until the fourth quarter of 2012, the real effective exchange rates of all the major currencies depreciated except for the pound sterling which appreciated by 5.36% (Chart 1-2). The Euro depreciated by 4.2% and the Japanese Yen depreciated by 7.35% while the US dollar depreciated mildly by 0.11%.

Chart 1-2: Real Effective Exchange Rates of Major Currencies (2005=100)

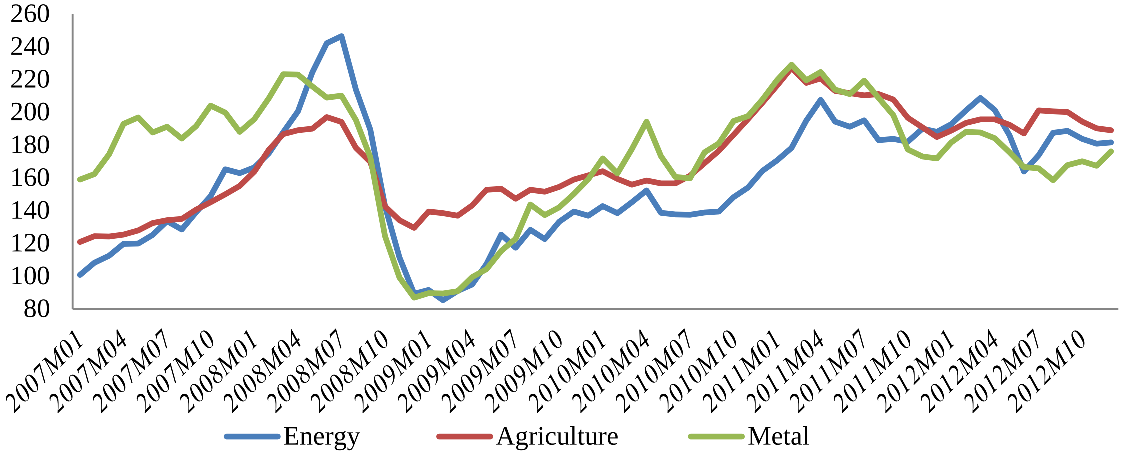


Source: IMF, International Financial Statistics Database.

5. Commodity Markets

Chart 1-3 below shows trends in the key commodity prices since the onset of the global financial crisis in 2007. It also shows that the year 2012 was marked by two phases: the first one is the first seven months of the year in which energy, agriculture and metal prices decreased sharply while the second phase witnessed a rebound in their prices.

Chart 1-3: Commodity price indices $US nominal, 2005=100



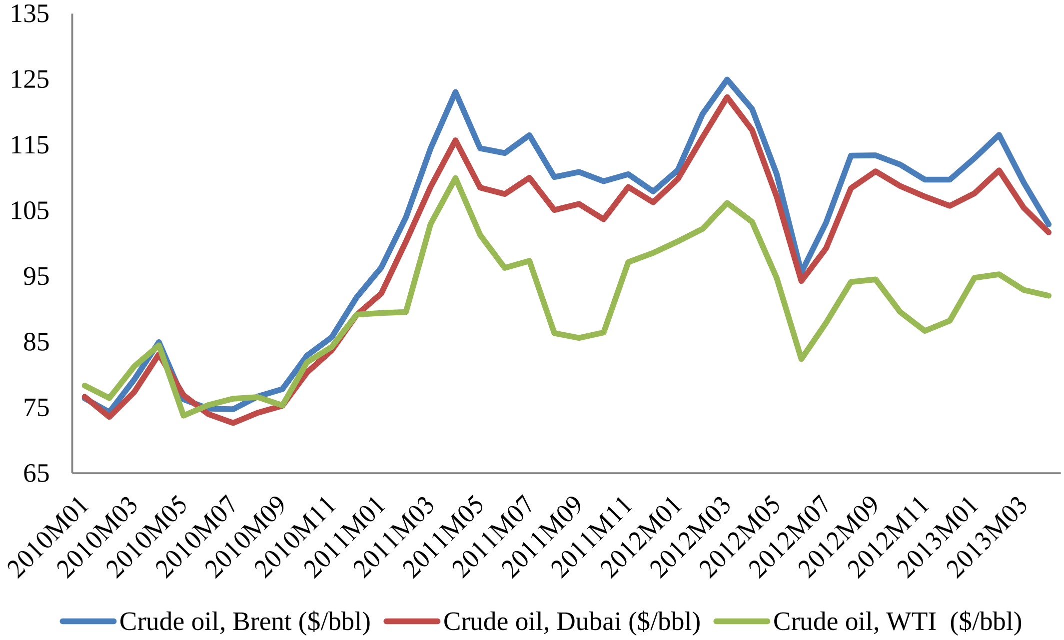
Source: World Bank

In this section we analyse the trend in commodity prices; notably crude oil, metals and agricultural commodities.

5.1. Crude Oil

As Chart 1-4 below illustrates, oil is the most important commodity price that increased during the period 2010-2012. In March 2012, Brent crude (the international marker) topped USD 124.92 per barrel which is the highest level since July 2008 and then declined to reach USD 95.58 per barrel in July 2012. This decline is mainly due to weak demand from developing economies as a result of their slowing growth. Heightened concerns about the European sovereign debt crisis added to this decline at the time. During 2012, crude oil averaged USD 111.97 per barrel.

Chart 1-4: Crude Oil Prices (US dollars)



Source: World Bank

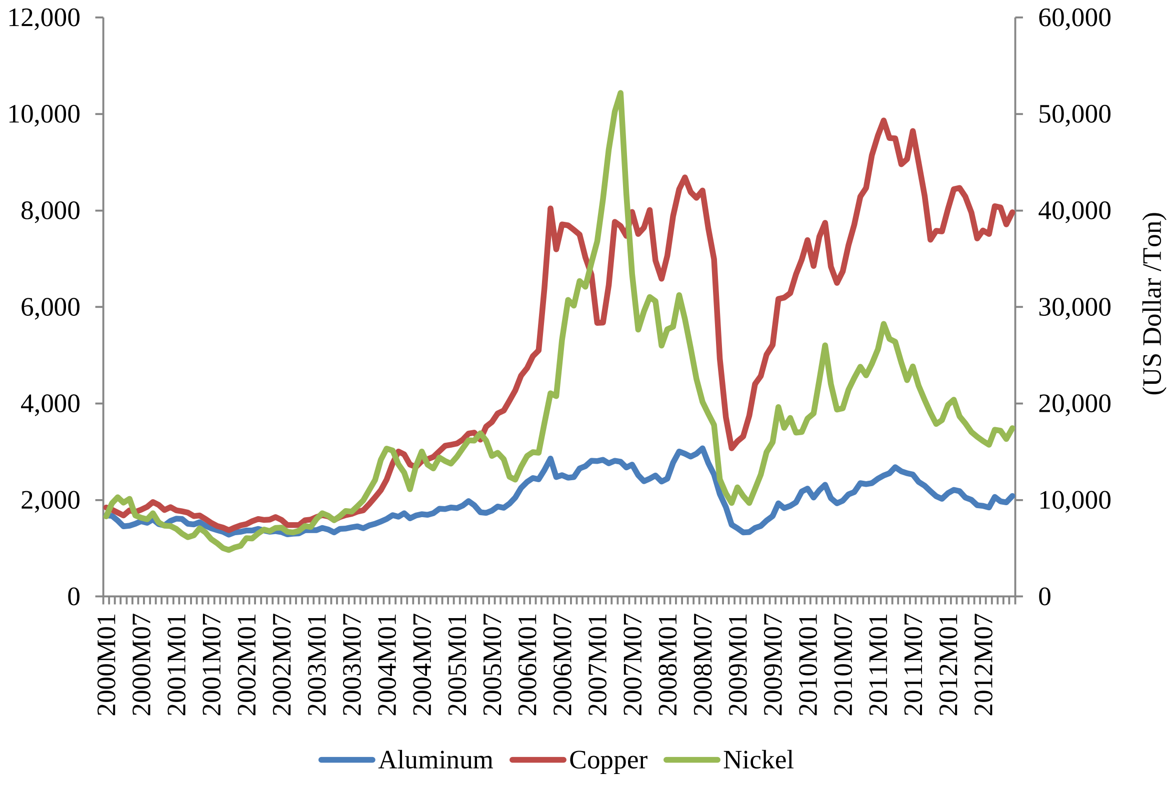
According to the world bank forecast, nominal oil prices are expected to average US$102 per barrel during 2013 and 2014 as supplies accommodate moderate demand growth.

5.2. Metal Markets

During the first half of 2012, most commodity prices notably energy and metals have witnessed a steady decline. Two reasons explain this decline. First, the level of demand from China, which currently consumes nearly 45% of the world's metal output, decreased considerably and second the European sovereign debt troubles which also reduced further the demand for metals.

In August 2012, aluminium prices declined to reach US$ 1,845.4 per tonne, mainly because of a persistent global surplus and high stocks. Copper prices have also declined in June 2012 due to weakening import demand by China but its levels are higher than that of the period 2000-2008. Regarding nickel (right axis of chart 1-5), prices increased slightly in 2012 but remain less volatile than aluminium and copper.

Chart 1-5: Metal Prices



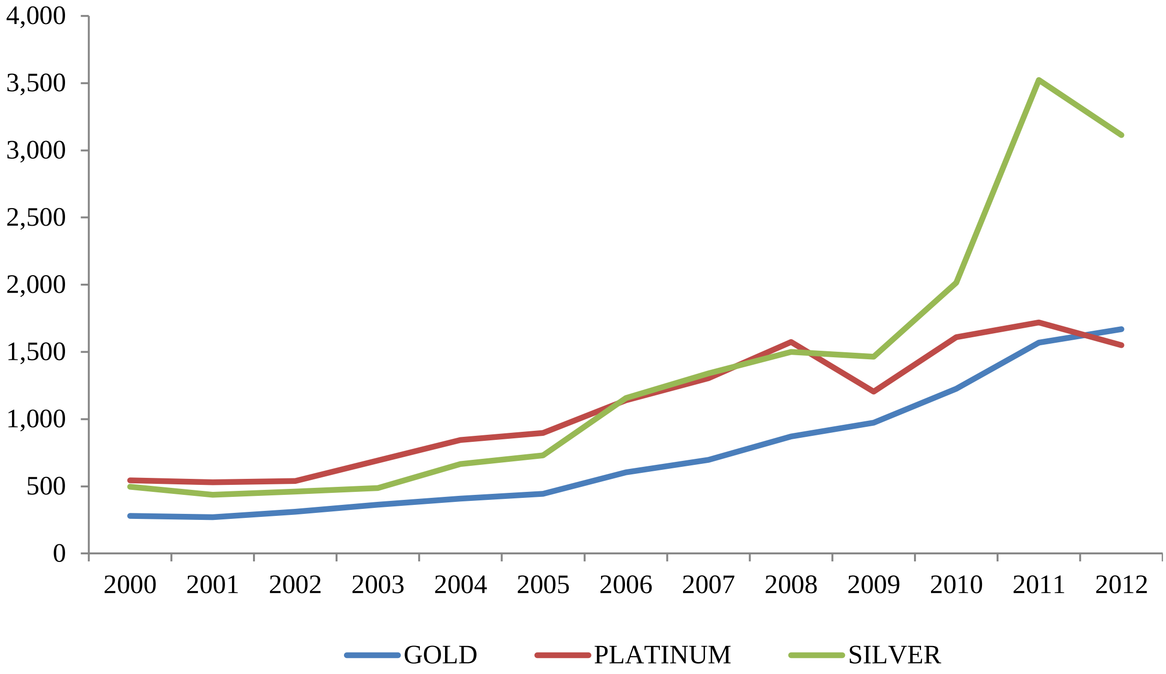
Source: World Bank

According to World Bank forecasts, metal prices will increase slightly in 2013. Aluminium prices are expected to increase by 3% annually until 2015; nickel prices are also expected to increase by 3% in 2013, while copper prices are expected to decline by 2% and 10% in 2013 and 2014 respectively.

Average prices of precious metals have increased continually since 2000 (chart 1-6). In 2012, the growth rate of their prices was less significant than the previous years.

While platinum and silver prices decreased by 9.8% and 11.6% respectively in 2012, gold prices increased by 6.4% in the same year.

Chart 1-6: Precious Metal prices



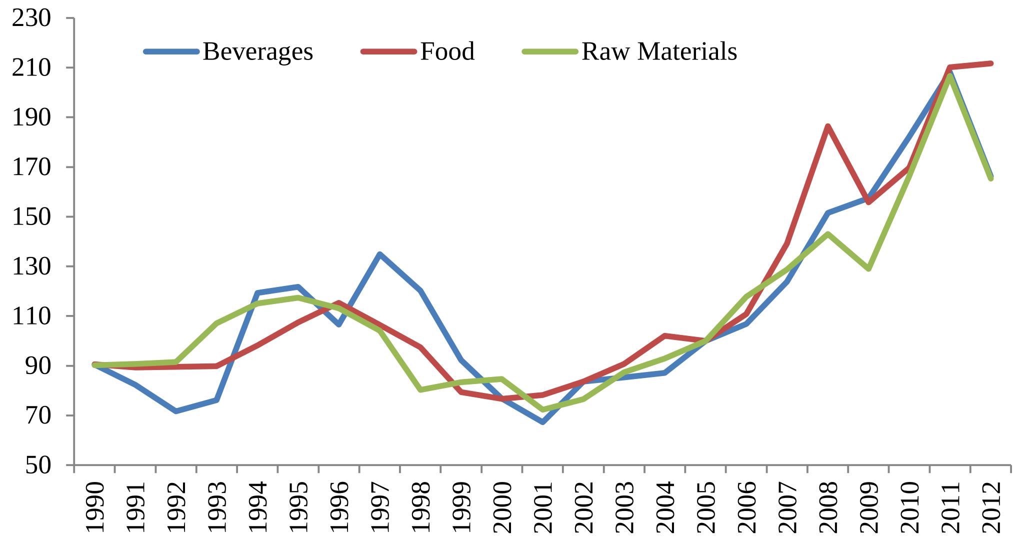
Source: World Bank

5.3. Agriculture and Food

High oil prices and harsh weather conditions in many regions (drought, floods, and earthquakes) have led to an unprecedented rise in international agriculture prices. In spite of this, inflation levels have generally been subdued as a result of weak international growth. As shown in Chart 1-7 below, food and beverages, agriculture raw materials have largely exceeded record levels set in 2008.

While beverages and raw material prices decreased by almost 30% compared to 2011, food prices continue its vertical path. According to the World Bank‘s agricultural price index, overall prices fell by about 7% in 2012.

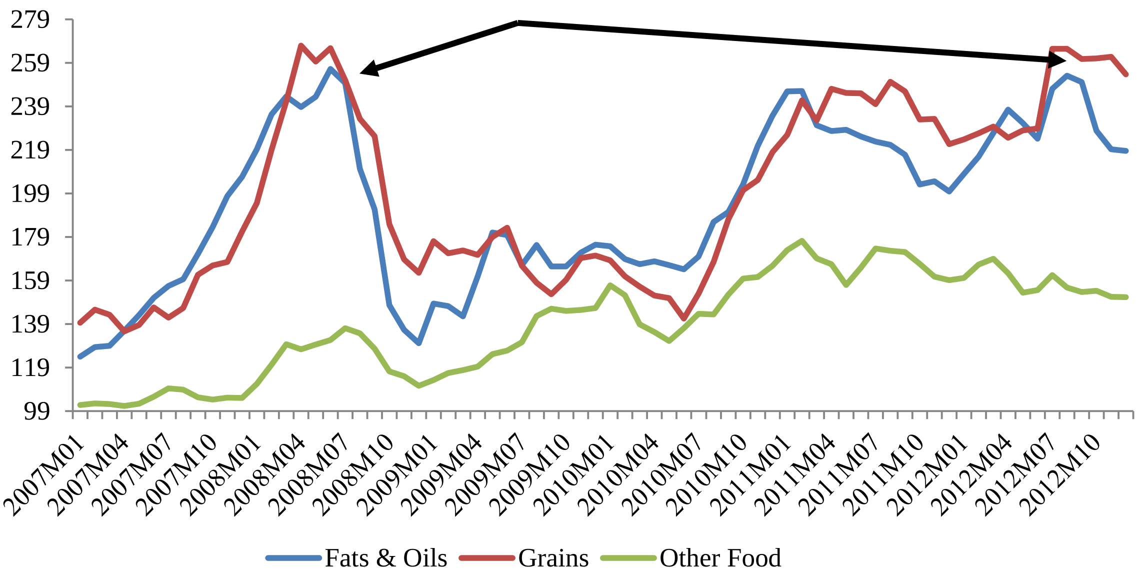
Chart 1-7: Agriculture Price Indices



Source: World Bank

The chart 1-8 below shows the volatility in food prices since 2007. It indicates that following a considerable decline of prices between 2008 and mid-2010, food prices of the first half of 2012 reached a new record and they have found their highest level since March 2008.

Chart 1-8: Food price indices $US nominal, 2005=100



Source: World Bank

According to the World Bank forecasts, most commodity prices are estimated to fall slightly in 2013. It is also forecast that crude oil will average USD102 per barrel in 2013, which is 3% lower than in 2012. Agricultural commodity prices are also forecast to decrease: food by 3.2%, beverages by 4.7%, and raw materials by 2.2%. Metal prices are expected to rise slightly but still average 14% lower than in 2011.

B. GCC Economies

The GCC region performed strongly in 2012 thanks to high oil prices which were above USD 100 for the entirety of 2011 and 2012. GCC economies remained robust buoyed by sustained high government spending as well as a further recovery of the private sector.

Fiscal policy remains expansionary and monetary policy is effective as the GCC currencies are pegged to the US dollar. Significant hydrocarbon revenues contributed to large fiscal and external surpluses despite strong import growth and fiscal expansion.

Nowadays, the current market environment in the GCC remains generally favourable due to the solid fiscal and economic performance of the region. Moreover, the liquidity situation of the GCC's financial institutions is expected to be sufficient to buffer regional asset sales from downsizing European banks.

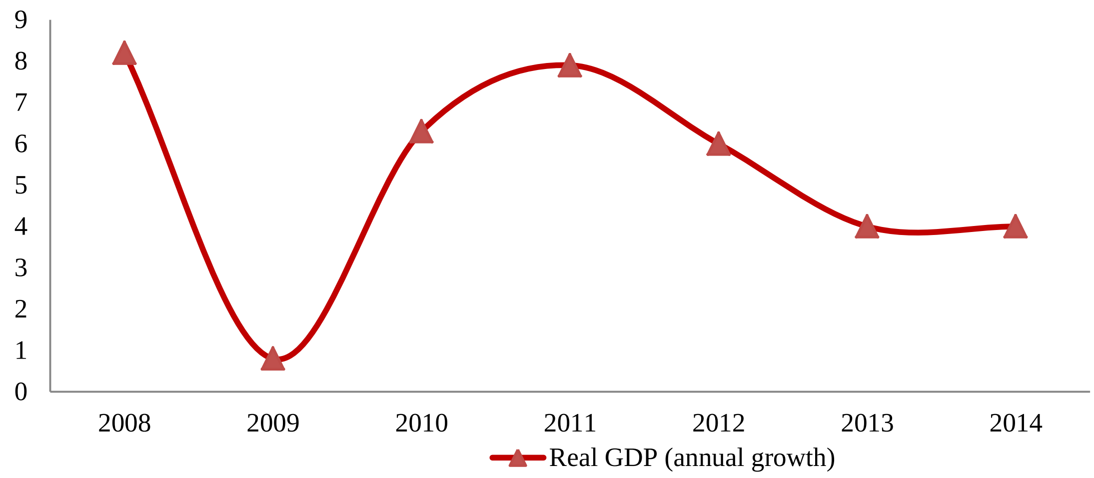
1. Macroeconomic indicators of GCC Economies

Despite the continuing uncertainty in the global economy, the GCC economies experienced growth at a level of 6.0% in 2012. The projections for 2013 and 2014 show that the regional economy will continue to grow at a moderate growth rate of 4.0% (Chart 1-9) mainly due to crude oil production.

At the individual country level, Saudi Arabia experienced the highest growth rate at 6.8% followed by Qatar at 6.6%, Kuwait at 5.1%, Oman at 5%, and finally the UAE and Bahrain grew by 3.9% in 2012.

Bahrain's real GDP growth is expected to grow at 3.2% in 2013. This will boost further Bahrain's economy and will help offset the losses in 2011.

Chart 1-9: Real GDP Growth in GCC



Source: IMF Regional Economic Outlook

With regard to non-oil GDP growth for the GCC, which is a more distinguishing measure of overall economic activity, it remained robust at the level of 5.9% in 2012 despite a decrease from 7.0% in 2011. In 2013, non-oil GDP growth for the GCC is forecast to be at the level of 5.5%. All the GCC countries experienced a robust non-oil growth in 2012. Bahrain's non-oil growth remains stable in 2012 at the level of 1.9%.

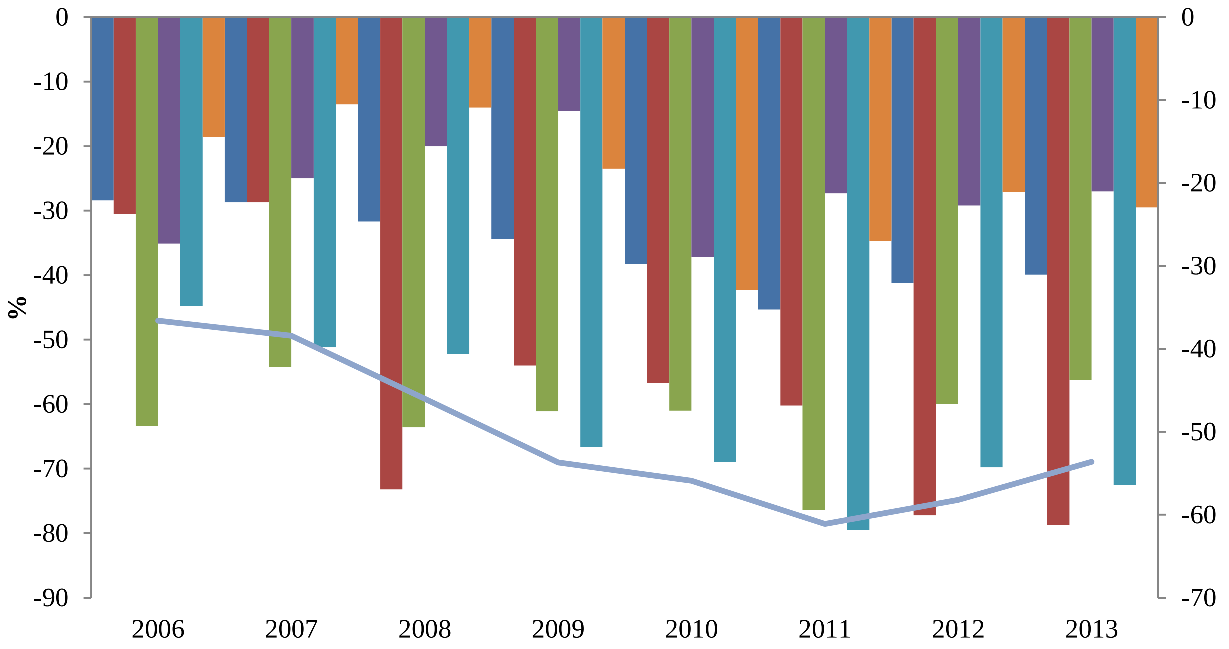
With regard to oil GDP, the GCC is projected a high growth rate of 4.8% in 2012 but less significant to the 7.9% recorded in 2011. At an individual country level, Kuwait had the highest projected oil GDP growth at 8.4%, followed by UAE at 5.3 and Saudi Arabia at 4.5% for the year 201٢. Bahrain had the lowest oil GDP at 2.6% during 2012.

3. Fiscal Policy in GCC

The increase in oil prices has prompted a sharp rebound in regional external and fiscal surpluses. In 2012, the GCC general government fiscal surplus witnessed an increase of 14.6% compared to its level in 2011 (12.7%). The IMF's projection for 2013 suggests that the general government fiscal balance for all GCC countries will drop to 11.2%.

The GCC government non-oil fiscal balance is projected to improve slightly, moving from -61.1% in 2011 to -58.2% in 2012 (Chart 1-10). This illustrates the importance of oil for the fiscal balance and the low contribution of non-oil sectors towards the government budget.

Chart 1-10: General Government Non-oil Fiscal balance (% of non-oil GDP)



Source: IMF Regional Economic Outlook

1-Central government.
2-Consolidated accounts of the federal government and the emirates Abu Dhabi, Dubai, and Sharjah.

Table 1-5: Crude Oil Production (million barrels per day)

	2006	2007	2008	2009	2010	2011	Projections	
							2012*	2013*
Bahrain	0.2	0.2	0.2	0.2	0.18	0.19	0.19	0.21
Kuwait	2.6	2.6	2.7	2.3	2.6	2.66	2.9	2.8
Oman	0.7	0.7	0.8	0.8	0.9	0.88	0.91	0.92
Qatar	0.8	0.8	0.8	0.8	0.8	0.76	0.74	0.71
Saudi Arabia	9.2	8.8	9.2	8.4	8.4	9.56	10.05	10.05
United Arab Emirates	2.6	2.5	2.6	2.3	2.4	2.55	2.69	2.71
GCC	16.2	15.7	16.2	14.8	14.9	16.6	17.48	17.4

Source: IMF Regional Economic Outlook

Total government revenue (excluding grants) of the GCC is projected to increase to 49.3% of GDP in 2012 from 48.4% in 2011 and is expected to drop slightly to 47.7.0% of GDP in 2013. Regarding general government non-oil revenue, it represented 17.8% of the GDP of the GCC countries in 2011 and is expected to grow to 19.1% in 2012 and then fall to 17.6% in 2013.

In line with the rise in oil prices, total government gross debt is expected to decrease to 11.8% of GDP in 2012 and is expected to drop further to 11.4% of GDP in 2013. At an individual level, all GCC countries are projected a decrease in their gross debt to GDP in 2012.

In 2012, the current account balance for the GCC countries is estimated to see significant improvements due to rising oil prices and production levels. The GCC current account surplus is projected to increase in 2012 reaching USD 350.3 billion.

The current account balance is expected to fall to 23.6% of GCC's GDP in 201۳. Bahrain and UAE are the only GCC countries that are expected to undergo a rise in their current account balance (% of GDP) from 9.9% to 10.5% and 9.3% to 10.1% respectively between 2012 and 2013. .

4. Monetary Indicators

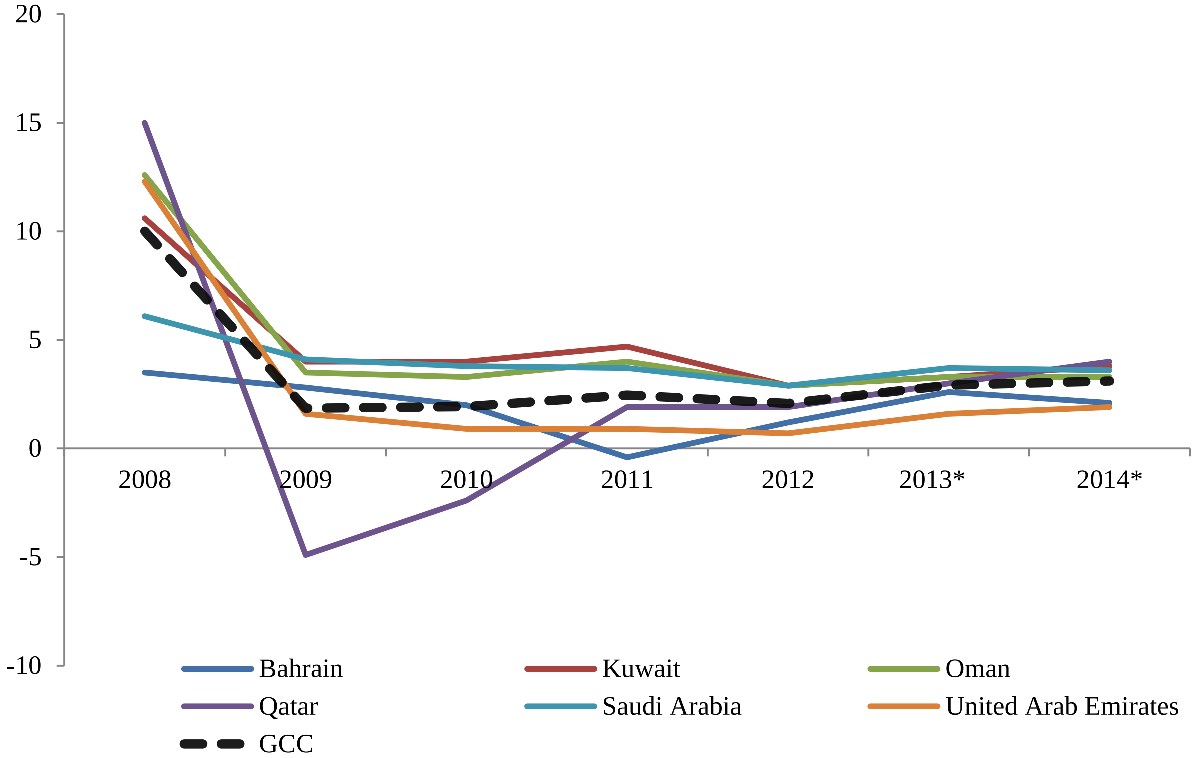
Aside from Kuwait, which is pegged to a basket of currencies, the monetary policy for the rest of the GCC countries is one of a fixed exchange rate regime with the US dollar.

4.1. Inflation

After a high 10.01% inflation rate in 2008, the GCC inflation rate decreased drastically to become to 1.93% in 2010 and 2.46% in 2011, and is decreased further in 2012 to reach the level of 2.08% in 2012 (Chart-1-11).

The IMF estimates that inflation will accelerate slightly to 2.91% in 2013 and 3.12 in 2014. At an individual country level, the CPI in 2012 ranged between a low of 0.7% for UAE and a high of 2.9% in Kuwait, KSA and Oman.

Chart 1-11: Inflation in GCC countries



**Forecasts*
Source: IMF, World Economic Outlook, April 2013.

4.2. Liquidity

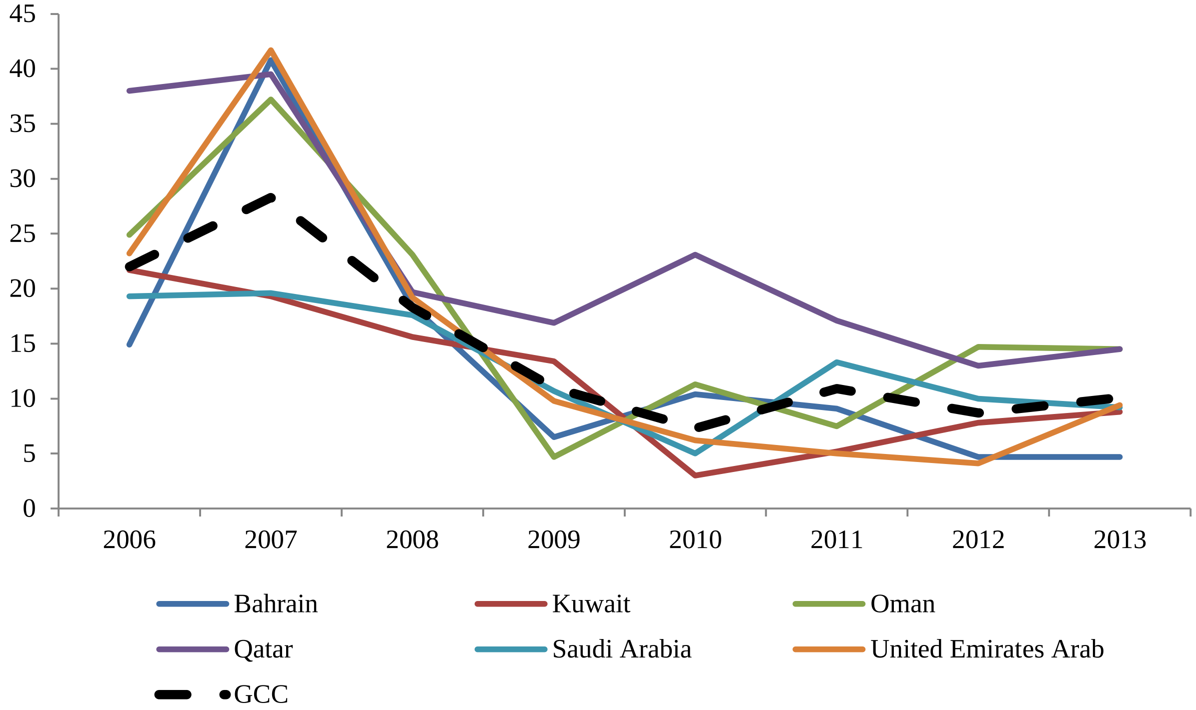
Liquidity in the GCC is captured by broad money. From a monetary policy point of view, higher broad money reflects eased liquidity conditions in the financial system which reveals strong economic activity during the year.

As illustrated in Chart 1-12, broad money supply in the GCC decreased sharply from 2007 to 2010, from a growth rate of 28.3% to 7.3%. This is a consequence of the global crisis which contracted regional liquidity and reduced access to financing. In 2011, broad money is expected to grow to reach 10.9% and decline slightly to 10.2% in 2012. By country, Saudi Arabia, Kuwait and Oman are the only countries forecasted with a positive growth in broad money in 2012. The three other countries are expected to face negative growth.

The strength in oil prices and huge oil-export revenues have allowed the GCC countries to earn ample foreign exchange reserves to counterbalance any currency fluctuation.

As Chart 1-13 illustrates, the level of gross official reserves for the GCC countries increased substantially during the period 2006-2010 (95.7%). The level increased from USD 278.1 billion in 2006 to USD 652.10 billion in 2011.

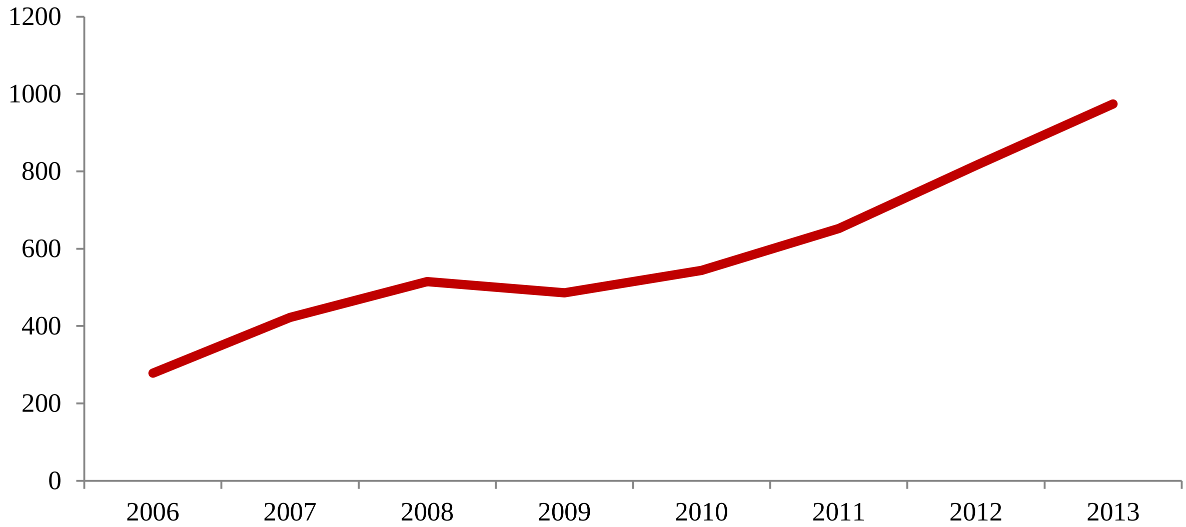
Chart 1-12: Broad Money Growth (%)



Source: IMF Regional Economic Outlook

IMF projections show that gross official reserves will continue to grow by 25.0% in 2012 then and 19.5% in 2013 to reach the record level of USD 974.2 billion.

Chart 1-13: Gross Official Reserves in GCC (Billion US dollars)



Source: IMF Regional Economic Outlook

Chapter

2

2. Bahrain's Economic Performance

Overview

A. Growth in Bahrain

B. Policy Developments

C. Private Sector Developments

Overview

For the year 2012, the Bahrain economy registered a growth rate of 4.1% in nominal terms and a real growth rate of 3.4% in GDP. The growth witnessed was a continuation of the momentum from the second half of 2011 as well as recovery in some sectors. The re-basing of real GDP to 2010 prices has helped show a more relevant benchmark for growth. Inflation remained within a reasonable range, indicating some increase in consumption, while domestic oil output increased, supporting the economy in general.

A. Growth in Bahrain

1. GDP Growth

Bahrain's nominal GDP grew by 4.1% in 2012, mainly due to a resumption in growth of the hotels and restaurants, construction and manufacturing sectors, which grew by 37.4%, 3.0% and 3.6% respectively. This indicates that there has been some recovery in the major sectors of interest in the Bahrain economy. The financial sector contributed 15.8% of GDP in 2012, and grew at an increased rate of 5.0% during the year, while government services continued to grow by 10.1% to account for 11.4% of GDP (Table 2-1).

Table 2-1: Gross Domestic Product (GDP) at Current Prices, 2011-2012

(BD Million)

	2011*	2012*	% Change	% Share (2012)
GDP at Current Prices	**10,963.2**	**11,414.2**	**4.1**	**100**
Non-Financial Corporations	7,895.4	8,113.7	2.8	71.1
Of which:				
-Crude Petroleum & Natural Gas	2,957.31	2,811.0	-4.9	24.6
-Manufacturing	1,675.10	1,735.7	3.6	15.2
-Construction	669.01	688.9	3.0	6.0
-Transportation and Communication	656.33	726.9	10.8	6.4
-Trade	447.63	465.8	4.1	4.1
-Hotels & Restaurants	201.68	277.1	37.4	2.4
-Real Estate & Business Activities	562.70	580.6	3.2	5.1
Financial Corporations	1,712.97	1,797.9	5.0	15.8
Government Services	1,180.18	1,299.7	10.1	11.4

** Provisional data*

Source: Central Informatics Organisation (CIO)

As the major employer and promoter of capital projects, the growth in government services and consumption positively affected the non-financial sector, particularly construction and manufacturing sectors, which grew in light of the increased capital spending. The hotels and restaurants and real estate sectors recovered in the face of the economic lull in 2011, while the trade sector declined in the face of weaker global demand.

In real terms, Bahrain's GDP grew by 3.4%, up from the 1.9% in 2011 (Table 2-2). In absolute dinar terms, real GDP rose from BD 9,848.7 million to BD 10,186.5 million over the period.

Table 2-2: Gross Domestic Product (GDP) at Constant Prices, 2011-2012

(BD Million)

	2011*	2012*	% Change	% Share (2012)
GDP at Constant Prices	**9,848.7**	**10,186.5**	**3.4**	**100**
Non-Financial Corporations	6,828.7	7,008.6	2.6	68.8
Of which:				
-Crude Petroleum & Natural Gas	2,114.9	1,935.3	-8.5	19.0
-Manufacturing	1,443.8	1,576.7	9.2	15.5
-Construction	665.6	688.0	3.4	6.8
-Transportation and Communication	667.2	716.2	7.3	7.0
-Trade	443.6	460.8	3.9	4.5
-Hotels & Restaurants	215.8	272.0	26.0	2.7
-Real Estate & Business Activities	562.1	578.2	2.9	5.7
Financial Corporations	1,685.5	1,744.6	3.5	17.1
Government Services	1,152.9	1,234.9	7.1	12.1

** Provisional Data*
Source: Central Informatics Organisation (CIO)

The non-financial corporations sector, which accounted for 68.8% of real GDP, grew by 2.6% in 2012. The largest increase in the non-financial sector was in the hotels and restaurants sector, which grew by 26.0%, reaffirming its rebound since its moderation in 2011. The oil sector shrunk by 8.5% due to interruptions in output during the year.

Financial corporations, the largest non-oil contributor to GDP grew by 3.5% and accounted for 17.1% of GDP in 2012. As mentioned earlier, government services expanded remained a key sector and expanded by 7.1% during the year.

2. Oil Sector

As a result of interruptions to the production at the Abu Sa'afa oil field, total crude oil production decreased from 69.5 million barrels in 2011 to 63.3 million barrels in 2012. Despite the decrease in total production, there was a rise in the production at Awali oil field (Bahrain Oilfield). Production at the Bahrain Oilfield rose from a total of 15.5 million barrels at end 2011 to 16.6 million barrels at end 2012, a 6.8% increase. On the other hand, due to an a breakage of submerged pipes, there was an unplanned interruption to the production in the Abu Sa'afa oil field in the first and second quarters of 2012. Total production dropped from 53.9 million barrels in 2011 to 46.7 million barrels in 2012. Despite this however, refined oil production increased from 96.0 million barrels in 2011 to 101.1 million barrels in 2012, a 5.3% increase (Table 2-3).

Table 2-3: Crude Oil Production and Refining

(Barrels Thousands)

	2011	2012	2012			
			Q1	Q2	Q3	Q4
Total Crude Oil	**69,452**	**63,302**	**15,736**	**14,203**	**16,295**	**17,068**
Bahrain Oilfield	15,516	16,576	4,121	4,091	4,206	4,158
Abu Sa'afa Oilfield	53,936	46,726	11,615	10,112	12,089	12,910
Refined Oil Production	**96,026**	**101,103**	**24,609**	**25,870**	**25,301**	**25,323**

Source: National Oil and Gas Authority (NOGA)

In conjunction with the Bahrain authorities, Tatweer Petroleum's[1] production and development activities are well under way with its team largely comprised of individuals from the state-owned Bahrain Petroleum Company ("BAPCO"), together with employees from both Occidental and Mubadala. The company also continues to hire additional local employees. In the Bahrain oil field, Tatweer drilled a total of 254 wells in 2012, and is on target to drill in excess of 180 additional new oil wells in 2013.

Tatweer Petroleum is responsible for all of Bahrain's onshore domestic field activities including operation of the Awali field and the Khuff gas reservoir. Tatweer Petroleum's strategic aim is to double the production of oil from the onshore field within five years and triple the production of oil within ten years. Tatweer Petroleum embarked on this strategic aim at the end of 2009. This is line with the Economic Vision 2030 and the Bahrain government's strategy of moving towards diversifying its source of income.

3. Consumer Prices

During 2012 Bahrain experienced a reversal of the minor deflation of 2011 (Table 2-4). The recovery in the consumer price index (CPI) was broad based, but mainly due to a 12.2% increase in the prices of alcoholic beverages and tobacco during the year. The other main contributor was the price category of recreation and culture which grew by 20.5%. During the year, there was a decline of 3.3% in the Housing, Water, Electricity & Fuels segment and a 4.1% decline in the communication segment.

The stark increase in prices for recreation and culture is in line with the developments in growth witnessed during 2012. As the hotels and tourism sector rebounded during the year, prices increased significantly.

[1] Occidental, MDC Oil and Gas (Bahrain Field) LLC ("Mubadala") and the National Oil and Gas Authority of Bahrain ("NOGA") announced the creation of a new state-owned joint operating company, Tatweer Petroleum-Bahrain Field Development Company WLL ("Tatweer Petroleum").

Table 2-4: Consumer Price Index (2006 = 100)

Major Group of Commodities and Services	2011	2012
Food and Non-Alcoholic Beverages	135.5	140.7
Alcoholic Beverages, Tobacco	124.5	139.7
Clothing & Footwear	108.7	111.0
Housing, Water, Electricity & Fuels	94.8	91.7
Furnishing, Household Equipment and Maintenance	115.4	121.1
Healthcare Services	109.2	110.3
Transport	107.3	111.9
Communication	92.3	88.5
Recreation & Culture	112.8	135.9
Education	114.8	116.9
Restaurants	113.9	115.6
Miscellaneous	131.2	135.9
General Index	**111.6**	**114.7**
Inflation	**-0.4**	**2.8**

Source: Central Informatics Organisation

B. Policy Developments

1. Tamkeen

Bahrain's efforts in improving it labour force are evident in the work of the Labour Fund "Tamkeen". Throughout 2012, Tamkeen continued to promote small medium enterprise (SME) business growth and invested in the human capital through various programmes and initiatives. These initiatives focus on human capital and the private sector.

In 2012, Tamkeen increased its support for Bahrainis and institutions in Bahrain to BD 46 million, whilst the total number of beneficiaries reached 75,000. It provided support to more than 610 private sector institutions, including job placements for more than 1,000 Bahrainis. Tamkeen classifies the schemes it operates into two main segments; human capital development and private sector support. Human capital development includes schemes to assist Bahrainis achieve qualifications, while on the enterprise support scheme assistance is provided to improve business standards.

2. International Indices

Bahrain's sovereign debt ratings, affirmed by solicited ratings agencies Standard and Poor's (S&P) and Fitch Ratings stand at BBB both with a stable outlook. Relative to other BBB rated peers, Bahrain has performed admirably, with a high GDP per capita (BD 8,828.5), lower debt burden and overall solid net asset position.

Furthermore, Bahrain was ranked 35th out of 144 countries worldwide compared to 37th out of 142 countries in 2011 for its overall global competitiveness ranking in the World Economic Forum's Global Competitiveness Report 2012/2013.

In terms of economic freedom, Bahrain was ranked 12th out of 177 economies in the Heritage Foundation/Wall Street Journal's index of economic freedom. In terms of the Arab world, Bahrain topped the list of the most economically free nations in the with the score of 8.1 compared with a score of 8.0 in last year's report, keeping its position at the first place as reported by the Fraser Institutes *Economic Freedom of the Arab World* report. The report cited Bahrain's status as a financial hub and its relaxed regulations as well as the well-established services that it has built over the years as its main advantages. Bahrain has topped this index for the past eight years now.

Finally, Bahrain ranked in the 75.8 percentile of the World Bank's *Worldwide Governance Indicators*, the highest in the Middle East, a testament to the strong regulatory structure in place.

3. Infrastructure and Housing

Bahrain benefits from an adequate level of infrastructure for the size of its economy. The latest major development was the Khalifa Bin Salman Port, which was inaugurated in 2009. It is the first multi-functional facility that provides import, export and re-exports and value added services. The port is occupies 110 hectares of reclaimed land and is also linked to the road leading to the King Fahad Causeway.

The Ministry of Works has signed a contract for the Muharraq sewage treatment plant. The plant is expected to have an initial design capacity of approximately 100,000 cubic metres per day. Construction of the plant is expected to take approximately 30 months. Subsequently, a series of connection sewers will be built to link existing wastewater pumping stations directly into the main sewer trunk. In addition, a limited local connection network will also feed directly into the plant.

In terms of housing, Bahrain's been pursuing an affordable housing project, which involves a public private partnership (PPP) for the long term development, design, engineering, construction and hard facilities management, maintenance and financing of affordable housing. The Project will be undertaken upon three sites located at Buhair, Al Lawzi and Islands 13 and 14 in the Northern Town of Bahrain respectively. 3,100 social houses together with approximately 1,050 affordable houses and apartments are expected to be built.

The affordable housing project is only part of the Government's overall housing scheme, which has the intention of delivering affordable housing to low and middle income Bahraini families. Bahrain aims to provide a further 4,000 housing units with added initiatives and projects.

At the end of 2012, 31 housing projects were on-going and were at various stages of development. It is expected that 5,324 houses and 778 flats will be delivered all over the country. There are also 19 new housing projects that are being planned to provide 8,911 houses, 254 flats and 16 plots of land.

Bahrain and Qatar have agreed to build a 40-kilometre marine causeway, to be known as the 'Friendship Bridge'. The causeway serves the purpose of boosting Bahrain's tourism sector and strengthening its business ties with Qatar. The Bahrain-Qatar causeway project is currently in the detailed design phase; and a commencement date will be determined once the design is completed and approved. The total cost of the project is expected to be U.S.$5 billion, and any financing is expected to be repaid from the income generated from commissioning the bridge.

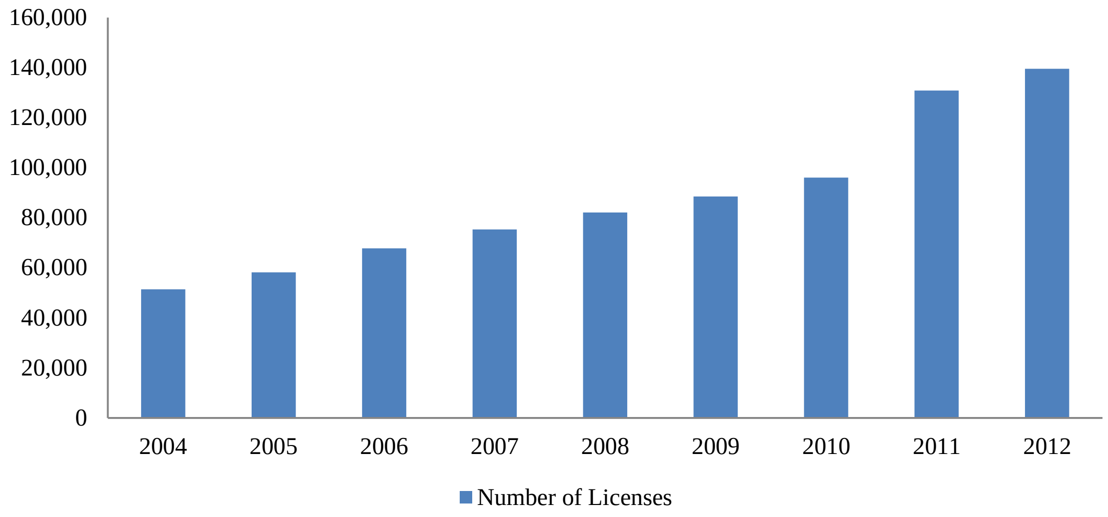
In anticipation of the causeway being built, Bahrain has laid plans to develop resorts, business parks and other facilities in proximity to the location of the causeway. The combined causeways linking Qatar to Saudi Arabia (via Bahrain) will further strengthen Bahrain's role as a regional hub for foreign transport and trading companies.

C. Private Sector Developments

1. Property and Real Estate Developments

There has been continued growth in the number of commercial licenses issued and operating in Bahrain. For the year 2012, the total number of commercial licences stood at 139 thousand, an alight increase of 1.7% over the level in 2011 (Chart 2-1). The number of new commercial licenses issued in 2012 was 8,689. The largest numbers of licenses issued were to the wholesale and retail trade (including repair of motor equipment) sub-segment, where 4,229 licenses were issued.

Chart 2-1: Total Number of Commercial Registration Licenses



Source: Ministry of Industry and Commerce

With the continued capital investment in housing, the construction sector somewhat flourished during 2012. With existing projects continuing from previous years, data on permits points to a minor slowdown.

In 2012, a total of 7,319 construction permits were issued, a decrease of 5.8%, over 2011 (Table 2-8). The decline was mainly due to a decrease in "Addition" permits, which constitute the majority of total construction permits. Given the amount of new projects, which include housing, the decline in additions is to be expected. New construction permits decreased slightly during 2012, while renovations increased slightly.

Table 2-5: Construction Permits by Type

Construction Permits by Permit Type	2011	2012
Addition	4,119	3,866
Demolition	605	501
Demolition and New Construction	57	52
New Construction	2,137	2,030
Reclamation	8	6
Renovation	844	864
Total	**7,770**	**7,319**

Source: Ministry of Municipalities Affairs and Agriculture.

2. Telecommunications

According to the "Telecommunications Market Indicators Report"[2] released by the Telecommunications Regulatory Authority (TRA) in December 2012, the telecoms sector represented approximately 4% of GDP in 2011. Also, the sector had an annual gross turnover of BD 406 million during the period. The drill down of the revenues by services shows that mobile revenues was the major source of retail revenues to the telecom sector, representing 46% of total revenues. This was followed by international calls (22%), leased lines (15%), internet (12%) and telephony (5%).

For the same year, it was estimated that approximately 2,700 employees worked in the telecoms sector, which is a 50% growth in the number of employees in the sector since liberalisation in 2003. Bahrainis constituted 80% of total employment in the sector and females constituted 28% of the workforce. The report notes that Bahrain ranks very well compared to its GCC peers in terms of fixed (wired) broadband penetration in the GCC and fixed telephony line penetration. International indices show Bahrain to perform well in the ICT sector overall in relation to both the region and as well as globally (Table 2-6).

Table 2-5: ICT Rankings

Index Name	Publication	World Rank 2012	Arab Rank 2012	GCC Rank 2012
ICT Development Index (IDI)	International Telecommunications Union (ITU)	40	2	2
The Networked Readiness Index	World Economic Forum	27	1	1
The Global Competitiveness Report	World Economic Forum	37	6	6
Global Innovation Index	Co-published by INSEAD and the World Intellectual Property Organization (WIPO)	41	3	3

Sources listed in the Table.

[2] The "Telecommunications Market Indicators Report" presents market data with for the previous year, in this case, the 2012 report drills down 2011 developments.

Chapter 3

3. Monetary Developments

Overview

A. Money Supply Developments

B. Domestic Interest Rates

C. Exchange Rate Developments

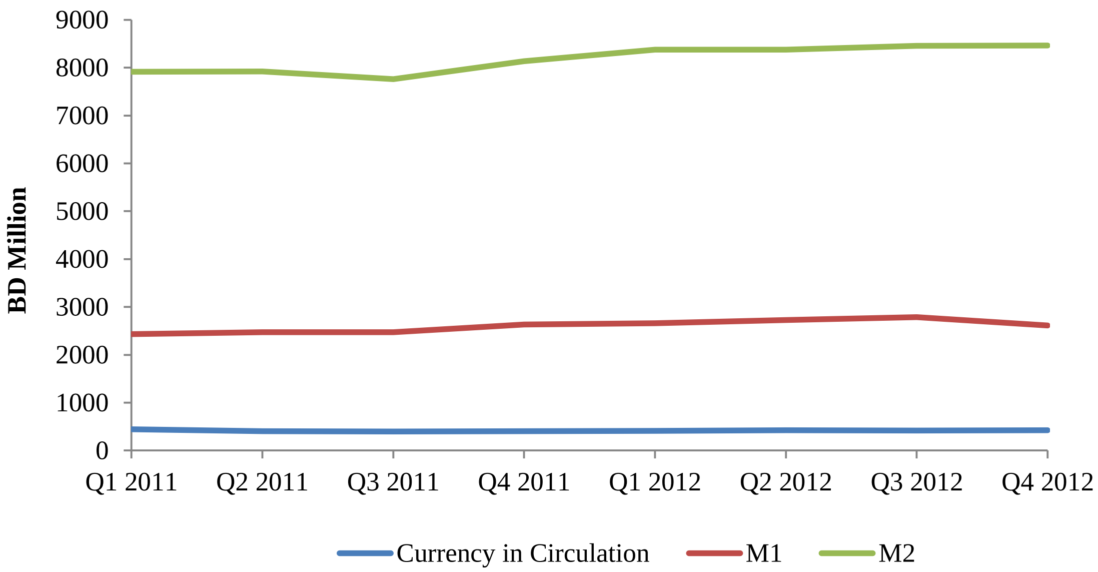
Overview

In 2012, monetary developments in Bahrain reflected regional trends as well as domestic economic developments. Given the Bahraini dinar's peg against the US dollar, domestic interest rates largely tracked US policy rates during the year which remained low as a measure to offset the economic downturn. Also, the exchange rate of the dinar against other currencies largely reflected the movements of the US dollar against those currencies.

A. Money Supply Developments

Money supply showed a mixed trend in 2012 compared to the increases witnessed in 2011. Currency in circulation (currency outside banks) registered an increase of BD 19.2 million (4.8% growth) to reach BD 421.4 million in 2012 compared with BD 402.2 million in 2011 (Table 3-1). M1 (currency in circulation plus demand deposits) declined by 1.0% from BD 2,636.9 million in 2011 to BD 2,611.1 million in 2012. Despite the decrease in M1, M2 (M1 plus time and savings deposits) rose by BD 329.7 million (4.1% increase) from BD 8,135.1 million at end 2011 to BD 8,464.8 million at end 2012.

Chart 3-1: Money Supply



Source: Central Bank of Bahrain

The growth in money supply, M2 growth, was mainly due to increases in private sector time and saving deposits (local and foreign currency). In 2012, total private sector deposits (demand deposits as well as time and savings deposits) amounted to BD 8,043.4 million an increase of 4.0% and accounted for 95.0% of M2. Time and saving deposits increased by 6.5% and largely contributed to the growth of M2. Private sector demand deposits, however, decreased by 2.0% from BD 2,234.7 million at end 2011 to BD 2,189.7 million at end 2012.

Table 3-1: Money Supply

(BD Million)

End of Period	Currency Outside Banks 1	Deposits [1/]			M1	M2	M3
		Private Sector		General Government[2/] 4	(1+2)	(M1+3)	(M2+4)
		Demand 2	Time and Savings 3				
2011	402.2	2,234.7	5,498.2	1,858.9	2,636.9	8,135.1	9,994.0
2012	421.4	2,189.7	5,853.7	1,970.3	2,611.1	8,464.8	10,435.1

1/ BD and Foreign Currency deposits of resident non-banks at Central Bank of Bahrain and Retail Banks
2/ Central Government, the Social Insurance System and the Central Bank of Bahrain
Source: Central Bank of Bahrain

A breakdown of private sector deposits (Retail banks only) by currency shows that M2 growth has been mainly driven by increases in savings deposits denominated in both Bahraini dinar and foreign currency while time deposits were driven by deposits denominated in foreign currency.

During 2012, Bahraini dinar and foreign currency saving deposits grew by 23.9% and 3.8% to reach BD 1,619.7 million and BD 111.1 million respectively. Foreign currency time deposits followed, growing by 5.7% (Table 3-2). Foreign currency demand deposits decreased by 9.7% during the same period.

At the end of 2012, the broadest measure of money (M3), increased by BD 441.1 million or by 4.4% from BD 9,994.0 million at end 2011 to BD 10,435.1 million at end 2012. From the context of deposits, M3 includes general government deposits (with both the Central Bank of Bahrain and retail banks) which increased by BD 111.4 million or 6.0% from BD 1,858.9 million in 2011 to BD 1,970.3 million in 2012.

Table 3-2: Private Sector Deposits by Currency

(BD Million)

Deposit Type	2011	2012	Change (%)
Demand			
BD	1,547.2	1,569.1	1.4
Foreign Currency	687.5	620.6	-9.7
Savings			
BD	1,307.5	1,619.7	23.9
Foreign Currency	107.0	111.1	3.8
Time			
BD	2,877.8	2,895.4	0.6
Foreign Currency	1,101.9	1,164.3	5.7
CBB Liabilities to Non-Banks (BD and Foreign Currency)	104.0	63.2	-39.2
Total	**7,732.9**	**8,043.4**	**4.0**
As a Share of M2 (%)	**95.1**	**95.0**	**-0.1**

Source: Central Bank of Bahrain

In terms of domestic liquidity, as also defined by M3, the growth was largely due to an increase in domestic claims. During 2012, domestic claims increased by BD 377.1 million or 4.5% to reach a total of BD 8,773.0 million. In addition, net foreign assets increased by BD 64.0 million or 4.0% to reach a total of BD 1,662.1 million (Table 3-3). Despite the overall increase in NFA, retail banks witnessed a decline from BD 1.9 million in 2011, to a net liability position of BD 181.9 million. This change was due mainly to increased funding from wholesale banks' head offices to their respective licenses in Bahrain. Also, there has been increase in funding from foreign banks to domestic banks in Bahrain, which has caused the net liability position.

Table 3-3: Factors Affecting Domestic Liquidity

(BD Million)

Factor	2011	2012	Change (%)
Domestic Liquidity (M3)	**9,994.0**	**10,435.1**	**4.4**
Factors Affecting Liquidity			
Net Foreign Assets	**1,598.1**	**1,662.1**	**4.0**
a) CBB	1,596.2	1,844.0	15.5
b) Retail Banks	1.9	-181.9	-9,673.7
Domestic Claims	**8,395.9**	**8,773.0**	**4.5**
c) Claims on Government	2,114.2	2,360.8	11.7
d) Claims on Private Sector [1]	7,525.6	7,994.2	6.2
e) Other Assets (Net)	-1,243.9	-1,582.0	-27.2

1/ Includes Loans and Holdings of Securities
Source: Central Bank of Bahrain

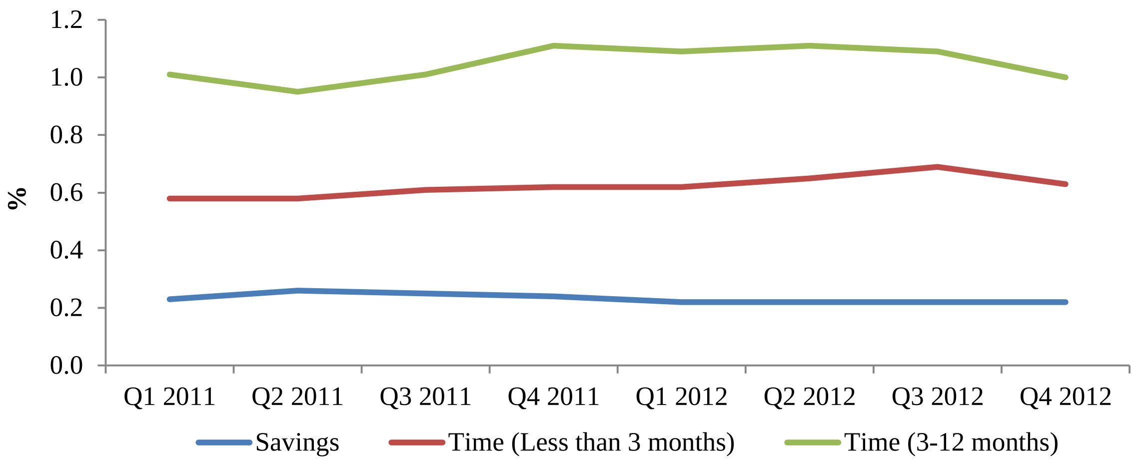
At the end of 2012, 84.1% of M3 was in the form of domestic claims and 15.9% in the form of net foreign assets. In terms of domestic claims, claims on government, claims on the private sector, and other assets accounted for 22.6%, 76.6% and -15.1%[3] of M3 respectively. Retail banks' net foreign assets account for -1.7% of M3.

B. Domestic Interest Rates

Interest rates in Bahrain have mainly followed US interest rates due to the dinar-dollar peg. In terms of deposits, weighted average retail bank rates on long term time deposits (3-12 months) decreased slightly from 1.09% at the start of 2012 to 1.0% by the end of the year; shorter term time deposits (less than 3 months) increased from 0.62% to 0.63% for the same period (Table 3-4). Rates on savings accounts remained unchanged at 0.22%.

[3] *Figure is minus because assets exceeded liabilities on the "other assets (net)" category.*

Chart 3-2: Weighted Average Deposit Rates of Retail Banks



Source: Central Bank of Bahrain

In general, deposit rates in Bahrain have been shown to be sensitive to US monetary policy. Rates on savings accounts were higher at the end of 2011 and have subsequently reduced during 2012.

Table 3-4: Deposit Interest Rates

(% per annum)

Deposits	End-2011	2012			
		Q1	Q2	Q3	Q4
Time[1/]					
a) <3 months	0.62	0.62	0.65	0.69	0.63
b) 3-12 months	1.11	1.09	1.11	1.09	1.00
Savings	0.24	0.22	0.22	0.22	0.22

1/ Deposits in the BD 10,000-50,000 range, for period indicated, beginning with June, 1998.
Source: Central Bank of Bahrain

On the lending side, weighted average rates for total business loans increased from 4.64% at the beginning of 2012 to 4.94% by year-end (Table 3-5). Rates for all sectors showed an increase by end of the year except for the manufacturing sector which registered a decrease.

Table 3-5: Interest Rates on Business Loans

(% per annum)

Sector	End-2011	2012			
		Q1	Q2	Q3	Q4
Construction and real estate	5.04	4.99	6.43	5.07	5.24
Manufacturing	4.81	3.93	4.65	3.73	3.45
Trade	4.94	4.64	4.89	5.24	5.00
Other[1/]	4.11	4.52	4.41	5.05	4.96
Total Business[2/]	**4.86**	**4.64**	**4.81**	**4.84**	**4.94**

1/ Includes non-banks financial and other services
2/ Excludes overdraft approvals
Source: Central Bank of Bahrain

In contrast, weighted average rates for total personal loans decreased from 6.27% to 5.96% for the same period (Table 3-6). This is due to decreases in rates for loans secured by deposits and unsecured loans by salary assignment. Loans secured by mortgages and vehicle titles increased for the period.

According to the data, personal loans secured by deposits were affected most by the interest rate reduction, as rates decreased from 7.92% at the beginning of 2012 to 4.82% by year-end. Rates on unsecured personal loans (by salary assignment) also decreased from 6.14% to 5.89% for the same period. Lending rates on "other" forms of unsecured lending decreased also from 11.03% to 10.47%.

Table 3-6: Interest Rates on Personal Loans

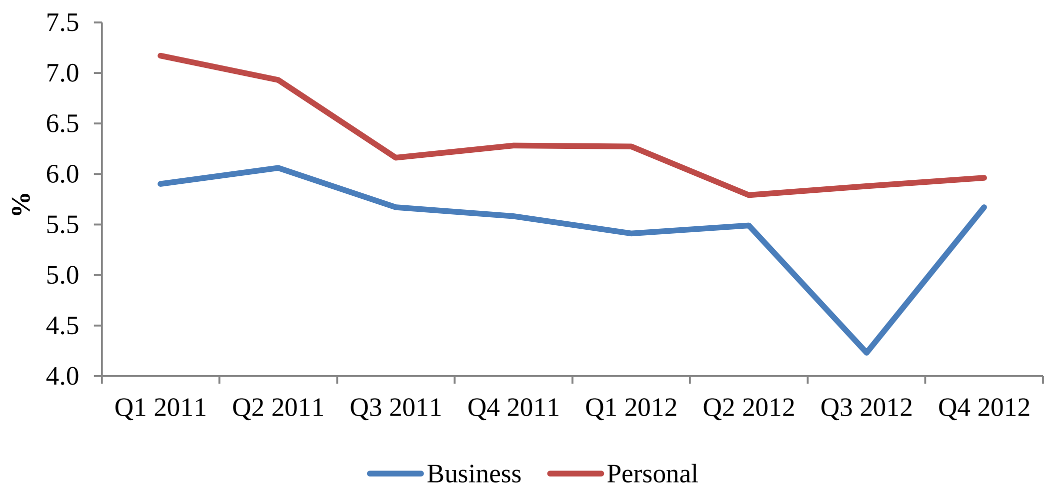
(% per annum)

Personal Lending Type	End-2011	2012			
		Q1	Q2	Q3	Q4
Secured by:					
by Mortgages	6.71	6.47	7.33	7.77	6.48
Vehicles Title	8.41	6.77	7.48	5.61	7.34
By Deposits	7.03	7.92	8.19	4.98	4.82
Unsecured:					
Salary Assignment	6.21	6.14	5.65	5.72	5.89
Other	18.49	11.03	18.48	11.73	10.47
Total Personal [1/]	**6.28**	**6.27**	**5.79**	**5.88**	**5.96**
Credit Cards	**20.38**	**20.47**	**20.49**	**20.56**	**20.65**

1/ Includes other types of personal loans not shown separately
Source: Central Bank of Bahrain

Rates on loans secured by vehicle titles increased from 6.77% to 7.34%. Loans secured by mortgages increased slightly from 6.47% to 6.48% for the same period

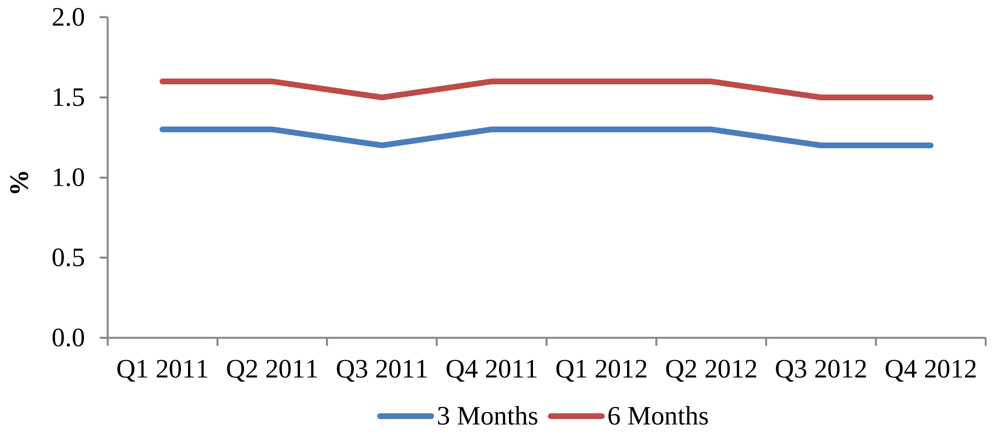
Chart 3-3: Personal and Business Interest Rates



Source: Central Bank of Bahrain

Average interbank rates remained stable during the course of 2012 and are reflective of retail banks' demand for liquidity in Bahrain. The unchanged rates are also a result of the US Fed keeping rates within the same range during 2012.

Chart 3-4: Money Market Rate/Interbank Rate



Source: Central Bank of Bahrain

Average short term interbank rates (3 month) fell slightly from 1.3% in the first quarter of 2012 to 1.2% at the end of the year. Longer term interbank rates (6 month) fell from 1.6% in the first quarter to 1.5% by end of the year (Chart 3-4).

C. Exchange Rate Developments

During 2012, the Bahraini dinar appreciated against the Japanese yen while it depreciated against Pound Sterling, Euro and Swiss Franc (Table 3-7).

Table 3-7: BD Exchange Rate against major currencies 1/

	End-2011	2012			
		Q1	Q2	Q3	Q4
Saudi Riyal	0.100	0.100	0.100	0.100	0.100
Kuwaiti dinar	1.349	1.353	1.341	1.339	1.337
UAE Dirham	0.102	0.102	0.102	0.102	0.102
Omani Riyal	0.977	0.977	0.977	0.977	0.977
Qatari Riyal	0.103	0.103	0.103	0.103	0.103
US dollar	0.376	0.376	0.376	0.376	0.376
Pound Sterling	0.581	0.598	0.586	0.608	0.608
Euro	0.486	0.501	0.471	0.484	0.497
Japanese Yen 2/	4.800	4.500	4.700	4.800	4.000
Swiss Franc	0.399	0.416	0.392	0.400	0.412

1/Interest rates as at the last working day of each period
2/ Per 1000 Units
Source: Central Bank of Bahrain

Chapter
4

4. Financial Sector Developments

Overview

In 2012, the effects of the financial crisis continued to recede in Bahrain. Despite that, there was a decrease in the number of financial institutions, and credit facilities extended. However, the aggregate balance sheets of banks and the number of employees in the financial sector decreased in 2012.

A. Bahrain Financial System

There were 405 banks and financial institutions operating in Bahrain in 2012 compared to 415 in 2011 (Table 4-1).

Table 4-1: Total Number of Licenses (2011 vs. 2012)

License Type	2011	2012
Retail Banks	**30**	**29**
Islamic	*6*	*6*
Conventional	*24*	*23*
Wholesale Banks	**76**	**74**
Islamic	20	20
Conventional	56	54
Insurance Companies and Organisations	**154**	**152**
Investment Business Firms	**49**	**49**
Specialised Licensees	**89**	**79**
Money Changers	18	17
Fund Administrators	1	2
Registrar License	1	1
Registered Administrators	3	1
Financing Companies	8	8
Representative Offices	33	26
Islamic Banks	*3*	*1*
Conventional Banks	*13*	*11*
Investment Business	12	9
Insurance	5	5
Microfinance Companies	2	2
Trust Service Providers	3	3
Provider of Ancillary Services	17	16
Islamic	1	1
Conventional	13	12
Insurance	3	3
Societies	2	2
Registered Professional Body	1	1
Capital Market Brokers	**17**	**22**
Licensed Exchanges	2	2
Licensed Clearing, Settlement and Central Depository system	1	1
Licensed Securities Dealer	1	1
Licensed Securities Broker-Dealer	5	9
Licensed Securities Clearing Member	3	5
Stockbrokers	5	4
Total	**415**	**405**

Source: Central Bank of Bahrain

The licensing framework for banks and financial institutions operating in Bahrain has remained largely unchanged. However, the Central Bank of Bahrain ("CBB") is yet receiving many applications from local and international applicants to be members of BFX and BCDC subsequent to their establishment in 2010.

The CBB has provided licenses for 10 new institutions in 2012 versus 21 new institutions in 2011. The majority of license provided were for the capital market sector (Table 4-2).

Table 4-2: New Licenses Issued (2011 vs. 2012)

License Type	2011	2012
Banks	**1**	**0**
Islamic	0	0
Conventional	1	0
Insurance Companies	**2**	**4**
Islamic	0	0
Conventional	2	4
Investment Business Firms	**4**	**1**
Islamic	1	0
Conventional	3	1
Specialised Licensee	**4**	**0**
Capital Markets	**10**	**5**
Total	**21**	**10**

Source: Central Bank of Bahrain

B. Aggregate Banking System

The aggregate balance sheet for the banking system (conventional and Islamic retail and wholesale banks) decreased in total to reach USD 186.3 billion by the end of 2012, compared to USD 197.1 billion at the end of 2011, a decrease of USD 10.8 billion, or 5.5% (Table 4-3). Wholesale banks represented 61.5% of the total, while retail banks accounted for 38.5%.

Table 4-3: Aggregate Balance Sheet of the Banking System

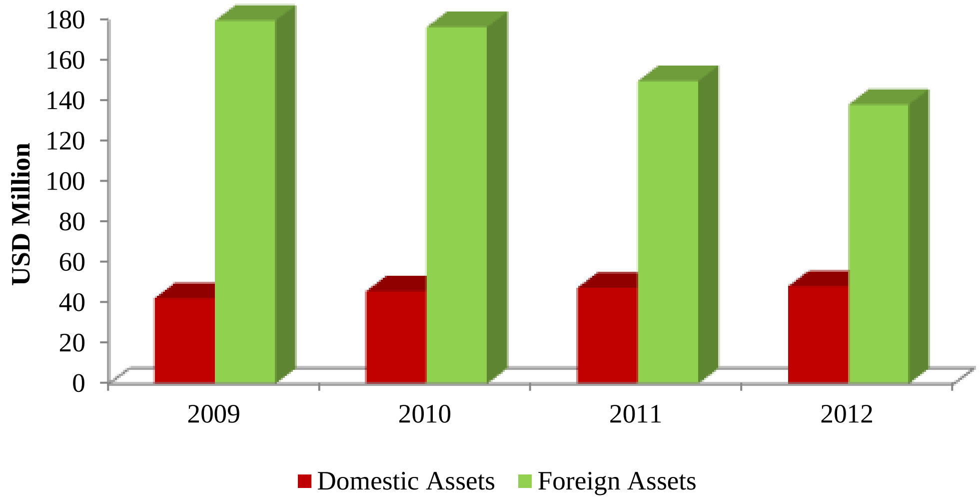
(USD Billion)

Items	Year-end		% Change
	2011	2012	
Retail Banks	67.4	71.7	6.4
Wholesale Banks	129.7	114.6	-11.6
Total	**197.1**	**186.3**	**-5.5**

Source: Central Bank of Bahrain

In total, domestic banking assets amounted to USD 48.2 billion at the end of 2012 compared to USD 47.4 billion at the end of 2011, registering an increase of USD 0.8 billion (1.7%). Foreign assets amounted to USD 138.1 billion at the end of 2012 compared to USD 149.7 billion at the end of 2011, a decrease of USD 11.6 billion (7.7%).

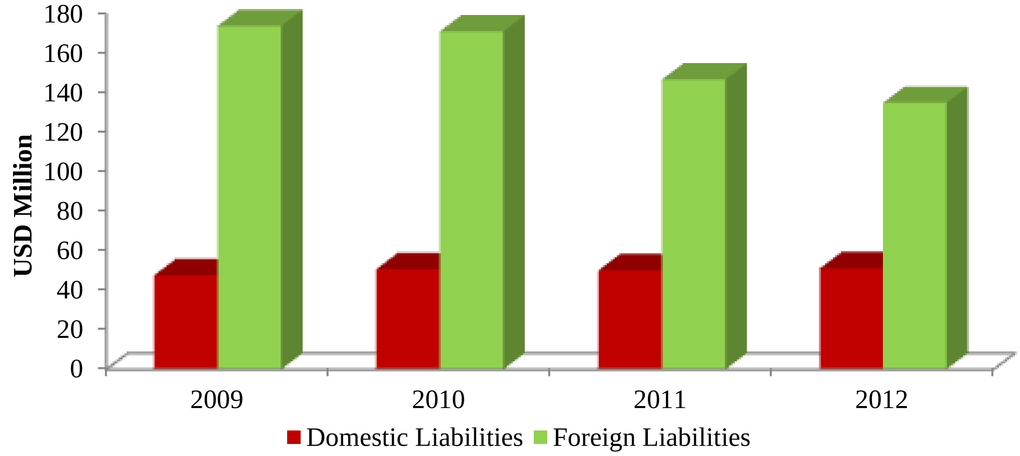
Chart 4-1: Domestic and Foreign Assets of the Banking System



Source: Central Bank of Bahrain

Domestic liabilities increased to USD 51.2 billion at the end of 2012 compared to USD 50.2 billion at the end of 2011, an increase of USD 1.0 billion (2.0%). Total foreign liabilities decreased at the end of 2012 by USD 11.8 billion (8.0%) to reach USD 135.1 billion against USD 146.9 billion at the end of 2011.

Chart 4-2: Domestic and Foreign Liabilities of the Banking System



Source: Central Bank of Bahrain

The banking systems assets over time have been mainly concentrated in GCC and European economies. However, over the period 2010-2012, the GCC share of total assets decreased from 29.5% to 23.8%. Europe’s share of total assets decreased from 29.3% to 27.3% for the same period (Table 4-4). GCC assets experienced the largest decrease from 2010-2012. Assets in the Asia region increased from 7.6% in 2010 to 7.8% in 2012, while assets in the Americas increased from 8.9% to 11.0% for the same period.

Table 4-4: Geographical Classification of the Banking System's Assets/Liabilities

(USD Billion)

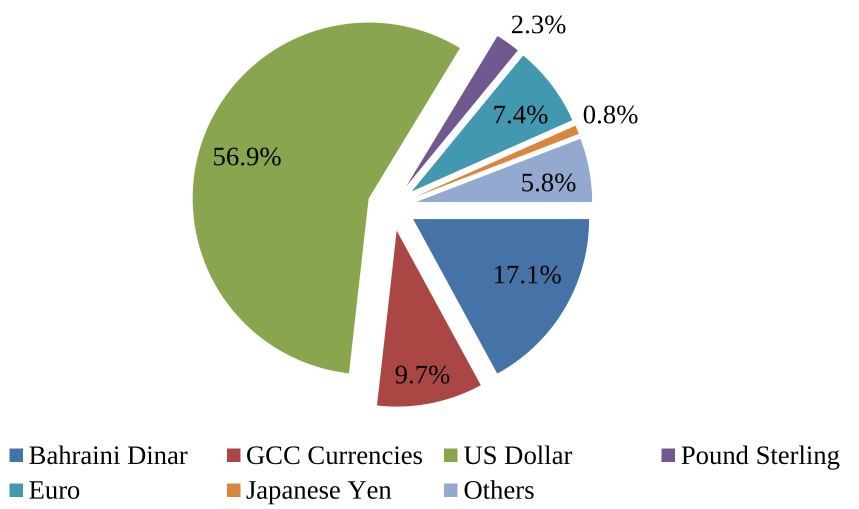
Items	Year					
	2010		2011		2012	
	Assets	Liabilities	Assets	Liabilities	Assets	Liabilities
Kingdom of Bahrain	45.8	50.8	47.4	50.2	48.2	51.2
GCC	65.5	54.6	57.0	53.5	44.3	59.9
Other Arab Countries	6.8	14.1	6.6	12.1	5.7	12.3
Americas	19.7	13.0	19.3	8.6	20.4	6.3
Western Europe	65.0	71.3	52.8	55.9	50.9	43.5
Asia	16.9	16.1	11.9	14.7	14.5	11.7
Other	2.5	2.3	2.1	2.1	2.3	1.4
Total	**222.2**	**222.2**	**197.1**	**197.1**	**186.3**	**186.3**

Source: Central Bank of Bahrain

The trends for liabilities between end-2010 and end-2012 indicate that GCC at 32.2% accounts for the largest percentage of total liabilities. This is followed by Bahrain and Europe which in 2012 account for 27.5% and 23.3% of total liabilities respectively.

In 2012, as in previous years, most assets are denominated in US dollars (56.9%). This is due to the fixed exchange rate regime, which adds to the certainty and predictability of banking business. Bahraini dinar assets accounted for 17.1% of total assets followed by the GCC and Euro currencies which contributed for 9.7% and 7.4% of total assets respectively (Chart 4-3).

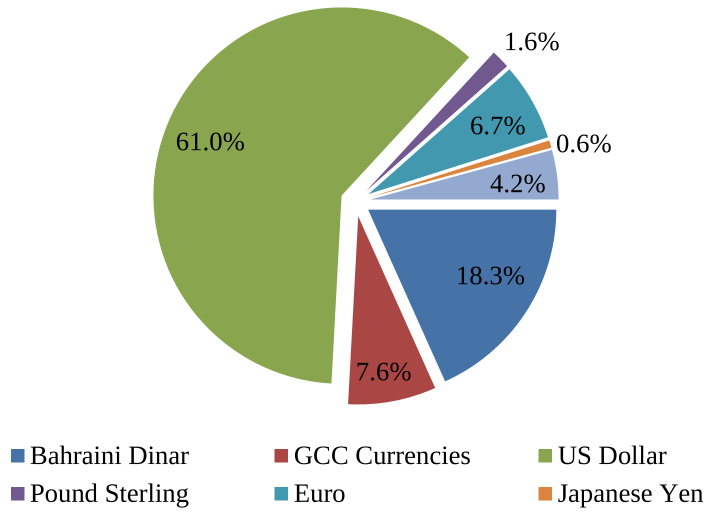
Chart 4-3: Currency Structure of the Banking System's Assets, 2012



Source: Central Bank of Bahrain

Similarly, the liabilities by currency are mostly of US dollar, accounting for 61.0% of total liabilities, down from 64.6% in 2011. This is followed by the Bahraini dinar and the GCC currencies which accounted for 18.3% and 7.6% of total liabilities respectively (Chart 4-4).

Chart 4-4: Currency Structure of the Banking System's Liabilities, 2012



Source: Central Bank of Bahrain

1. Retail Banks

Total assets of retail banks (including foreign assets) stood at BD 26,963.6 million at end-December 2012, an increase of BD 1,628.4 million or 6.4% over 2011 (Table 4-5). This growth was due to an increase in domestic assets, which expanded by 8.0% from BD 14,057.0 million at end-2011 to BD 15,180.2 million at end-2012.

Table 4-5: Aggregate Balance Sheet of Retail Banks - Assets

(BD Million)

Items	2011	2012	Change (amount BD)	Change (%)
Total Domestic Assets	**14,057.0**	**15,180.2**	**1,123.2**	**8.0**
Cash	106.8	101.1	-5.7	-5.3
CBB	1,005.4	1,299.8	294.4	29.3
Banks [1/]	2,576.5	2,677.2	100.7	3.9
Private Non-Banks [2/]	7,525.6	7,994.2	468.6	6.2
General Government				
Loans	225.4	198.0	-27.4	-12.2
Securities	1,888.8	2,162.8	274.0	14.5
Other	728.5	747.1	18.6	2.6
Foreign Assets	**11,278.2**	**11,783.4**	**505.2**	**4.5**
Total Assets	**25,335.2**	**26,963.6**	**1,628.4**	**6.4**

1/ Includes Head Offices and Affiliates
2/ Loans and Holdings of Securities
Source: Central Bank of Bahrain

The major contributors to the growth in domestic assets were claims on private non-banks, which increased by BD 468.6 million (6.2%) from BD 7,525.6 million at end-

2011 to BD 7,994.2 million at end-2012 followed by claims on CBB, which increased by BD 294.4 million (29.3%) from BD 1,005.4 million at end-2011 to BD 1,299.8 million at end-2012.

Claims on general government securities also increased by 14.5% to reach BD 2,162.8 million for the same period. In addition, foreign assets increased by BD 505.2 million (4.5%) to reach BD 11,783.4 million.

At the end of 2012, total domestic liabilities stood at BD 14,998.3 million, 6.7% higher than the BD 14,058.9 million recorded in 2011 (Table 4-6). Total foreign liabilities (including capital and reserves) increased by 6.1% from BD 11,276.3 million at end-2011 to BD 11,965.3 million at end-2012. Most of the expansion in domestic liabilities were in liabilities to private non-banks, which increased by BD 350.4 million (4.6%) followed by general government, which increased by BD 222.1 million (11.5%). Liabilities to banks and capital and reserves also increased by BD 182.3 million (9.1%) and BD 109.6 (5.7%) respectively.

Table 4-6: Aggregate Balance Sheet of Retail Banks - Liabilities

(BD Million)

Items	2011	2012	Change (amount)	Change (%)
Total Domestic Liabilities	**14,058.9**	**14,998.3**	**939.4**	**6.7**
Central Bank of Bahrain	263.5	241.4	-22.1	-8.4
Banks	1,999.0	2,181.3	182.3	9.1
Private Non-Banks [2/]	7,651.2	8,001.6	350.4	4.6
General Government [2/]	1,939.6	2,161.7	222.1	11.5
Other	282.2	379.3	97.1	34.4
Capital & Reserves	1,923.4	2,033.0	109.6	5.7
Foreign Liabilities [1/]	**11,276.3**	**11,965.3**	**689.0**	**6.1**
Total Liabilities	**25,335.2**	**26,963.6**	**1,628.4**	**6.4**

1/ Includes Capital and Reserves.
2/ Includes some non-deposit (non-monetary) liabilities.
Source: Central Bank of Bahrain

2. Wholesale Banks

The aggregate balance sheet for wholesale banks shrank in 2012. Aggregate data indicates that total wholesale bank assets decreased by 11.7% to reach USD 114.6 billion at the end of 2012, down from USD 129.7 billion at end of 2011 (Table 4-7). The decrease in total assets was mainly due to a decrease in total foreign assets, which decreased from USD 119.7 billion at end-2011 to USD 106.7 billion at end-2012 or by 10.8%.

Table 4-7: Aggregate Balance Sheet of Wholesale Banks - Assets

(USD Million)

Items	2011	2012	Change (amount)	Change (%)
Total Domestic Assets	**10,068.7**	**7,879.9**	**-2,188.8**	**-21.7**
Banks [1/]	4,547.1	4,288.9	-258.2	-5.7
Private Non-Banks [2/]	2,354.7	1,951.9	-402.8	-17.1
General Government [2/]	241.6	197.8	-43.8	-18.1
Other	2,925.3	1,441.3	-1,484.0	-50.7
Total Foreign Assets	**119,667.5**	**106,730.8**	**-12,936.7**	**-10.8**
Banks	13,211.9	12,467.5	-744.4	-5.6
Non-Banks	45,590.7	29,090.8	-16,499.9	-36.2
Securities	26,750.1	25,939.9	-810.2	-3.0
H.O. & Affiliates	29,436.6	30,739.4	1,302.8	4.4
Other	4,678.2	8,493.2	3,815.0	81.5
Total Assets	**129,736.2**	**114,610.7**	**-15,125.5**	**-11.7**

1/ Includes Head Offices and Affiliates
2/ Includes Securities
Source: Central Bank of Bahrain

On the foreign side, claims on banks decreased by 5.6% from USD 13.2 billion in 2011 to USD 12.5 billion in 2012. Claims on non-banks, which decreased by USD 1.6 billion (36.2%) to reach USD 29.1 billion was the biggest contributor to the decrease in foreign assets followed by securities decreasing by USD 0.8 billion (3.0%) to reach USD 25.9 billion.

Similarly, total domestic assets declined by 21.7% during the same period, from USD 10.1 billion in 2011 to USD 7.9 billion in 2012. The decrease was driven by a drop in claims on private non-banks, banks and general government by USD 402.8 million (17.1%), USD 258.2 million (5.7%) and USD 43.8 million (18.1%) respectively.

With regard to wholesale bank liabilities, most of the decrease during 2012 was also in foreign liabilities, which declined by 11.7% from USD 116.9 billion at end-2011 to USD 103.3 billion at end-2012 (Table 4-8). The main contributors to that decrease in foreign liabilities were liabilities to head office and affiliates, banks and securities which decreased by 28.8%, 12.8% and 20.3% respectively.

Table 4-8: Aggregate Balance Sheet of Wholesale Banks-Liabilities

(USD Million)

Items	2011	2012	Change (amount)	Change (%)
Total Domestic Liabilities	**12,826.6**	**11,359.0**	**-1,467.6**	**-11.4**
Banks 1/	5,614.9	5,376.1	-238.8	-4.3
Private Non-Banks	935.9	799.9	-136.0	-14.5
General Government	313.8	445.0	131.2	41.8
Other 2/	5,962.0	4,738.0	-1,224.0	-20.5
Total Foreign Liabilities	**116,909.6**	**103,251.7**	**-13,657.9**	**-11.7**
Banks	33,697.6	29,390.6	-4,307.0	-12.8
Non-Banks	19,728.5	20,955.9	1,227.4	6.2
Securities	3,640.3	2,899.7	-740.6	-20.3
H.O. & Affiliates	42,821.6	30,468.3	-12,353.3	-28.8
Other 2/	17,021.6	19,537.2	2,515.6	14.8
Total Liabilities	**129,736.2**	**114,610.7**	**-15,125.5**	**-11.7**

1/ Includes Head Offices and Affiliates
2/ Includes Capital and Reserves
Source: Central Bank of Bahrain

Domestic liabilities decreased by 11.4% to reach USD 11,359.0 million. The decreases in domestic liabilities were mostly in the liabilities to banks and private non-banks which decreased by 4.3% and 14.5% respectively.

3. Islamic Banks

Bahrain hosts one of the world's oldest Shari'a compliant financial sectors, which has grown significantly over the past few years. Islamic banking continued to grow due to the increasing interest in Islamic products and services. In 2010, the CBB has authorised the formation and marketing of "Hyperion Australian Equity Islamic Fund", the first Shari'a-compliant offshore fund comprised of the country's stocks.

Aggregate assets of Islamic banks (retail and wholesale banks) rose by 3.5% during 2012 with the overall increase being fuelled by an expansion in foreign assets (Table 4-9).

Table 4-9: Aggregate Balance Sheet of Islamic Banks - Assets

(USD Million)

Items	2011	2012	Change (amount)	Change (%)
Total Domestic Assets	**12,646.5**	**12,823.5**	**177.0**	**1.4**
Cash	67.2	94.3	27.1	40.3
Investment with Banks [2/]	3,809.9	3,515.4	-294.5	-7.7
Investment with Private Non-Banks	6,559.0	6,684.1	125.1	1.9
Investment with Government	556.2	673.9	117.7	21.2
Other	1,654.2	1,855.8	201.6	12.2
Total Foreign Assets	**12,050.8**	**12,738.5**	**687.7**	**5.7**
Investment with Banks	1,588.0	1,390.0	-198.0	-12.5
Investment with Private Non-Banks	1,821.6	1,777.1	-44.5	-2.4
Securities	2,341.2	2,539.4	198.2	8.5
H.O. & Affiliates	5,961.7	6,105.0	143.3	2.4
Other	338.3	927.0	588.7	174.0
Total Assets [1/]	**24,697.3**	**25,562.0**	**864.7**	**3.5**

1/ Includes Unrestricted Investment Accounts
2/ Includes Head Offices and Affiliates
Source: Central Bank of Bahrain

Foreign securities increased by 8.5% from USD 2,341.2 million to USD 2,539.4 million for the same period. Head office and affiliates also increased, growing by 2.4%, from USD 5,961.7 million in 2011 to USD 6,105.0 million in 2012.

In terms of domestic assets, investments with private non-banks and government have been the major contributors growing by 1.9% and 21.2% respectively. In contrast, investments with banks had a decrease, declining by 7.7% to reach USD 3,515.4 million.

Unlike assets, liabilities are growing faster on the domestic side, increasing by 6.6%, mostly led by increases in private non-banks (Table 4-10). Liabilities to private non-banks grew by 13.1% from USD 6,399.0 million in 2011 to 7,237.2 million in 2012.

Foreign liabilities increased by a total of 0.2%, led by liabilities to banks, which increased by 21.8% from USD 3,180.2 million in 2011 to 3,875.0 million in 2012. Liabilities to capital and reserve had the major decrease, dropping by 6.0% followed by other liabilities and head office and affiliates which decreased by 87.1% and 5.9% respectively.

Table 4-10: Aggregate Balance Sheet of Islamic Banks – Liabilities

(USD Million)

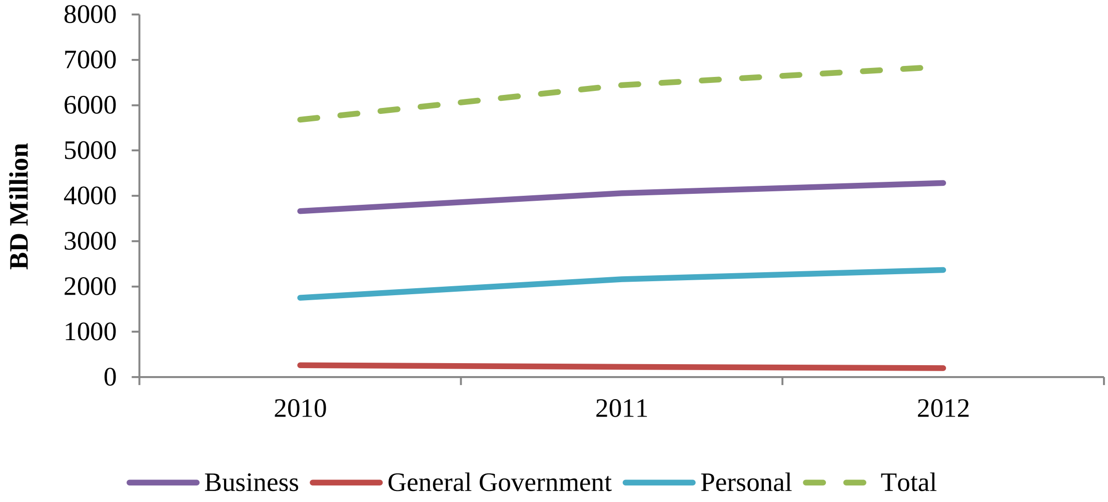
Items	2011	2012	Change (amount)	Change (%)
Total Domestic Liabilities	**12,821.8**	**13,662.4**	**840.6**	**6.6**
Banks [2/]	2,432.9	2,447.0	14.1	0.6
Private Non-Banks	6,399.0	7,237.2	838.2	13.1
General Government	580.4	640.1	59.7	10.3
Capital and Reserves	3,001.7	2,781.6	-220.1	-7.3
Other	407.8	556.5	148.7	36.5
Total Foreign Liabilities	**11,875.5**	**11,899.6**	**24.1**	**0.2**
Banks	3,180.2	3,875.0	694.8	21.8
Non-Banks	1,918.2	1,907.8	-10.4	-0.5
H.O. & Affiliates	1,040.5	979.0	-61.5	-5.9
Capital and Reserves	5,421.6	5,097.3	-324.3	-6.0
Other	315.0	40.5	-274.5	-87.1
Total Liabilities [1/]	**24,697.3**	**25,562.0**	**864.7**	**3.5**

1/ Includes Unrestricted Investment Accounts
2/ Includes Head Offices and Affiliates
Source: Central Bank of Bahrain

C. Domestic Credit

Credit facilities have been showing a modest increase for the majority of economic sectors in Bahrain. Total outstanding credit facilities extended by retail banks to the different sectors of the domestic economy amounted to BD 6,848.7 million at end-2012, up 6.3% from the BD 6,444.4 million at end-2011 (Chart 4-5).

Chart 4-5: Domestic Credit by Sectors



Source: Central Bank of Bahrain

Total domestic credit increased by 13.5% by end-2011 and followed by 6.3% at end-2012. Private sector credit (business and personal) shows a similar pattern, with an increase of 5.6% and 9.5% respectively in 2012, indicating that the lending to households and business enterprises has expanded.

Outstanding facilities to the business sector increased by 5.6% from BD 4,056.8 million at end-2011 to BD 4,282.7 at end-2012. During 2012, business lending expanded by 1.3% from BD 4,229.5 million in the first quarter of 2012 to BD 4,282.7 million in the last, despite the increases; it decreased the share of total domestic credit to 62.5%. Business credit showed increases during the all quarters of 2012.

In terms of composition, the private sector (business and personal combined) received the bulk of domestic credit, ranging from 96.5% to 97.1% of total loans from end-2011 to end-2012 (Table 4-11). The business sector accounts for the majority of credit facilities extended, yet its share of total credit has been declining. As a percentage of total credit facilities, outstanding business sector credit accounted for 62.5% at end-2012, down from 63.0% in 2011 and down from 64.5% in 2010.

Table 4-11: Domestic Credit by Sector 1/

(BD Million)

Sectors	End-2010		End-2011		End-2012	
	Value	% Share	Value	% Share	Value	% Share
Business	3,663.7	64.5	4,056.8	63.0	4,282.7	62.5
General Government	261.5	4.6	225.5	3.5	197.9	2.9
Personal	1,751.4	30.9	2,162.1	33.5	2,368.1	34.6
Total	**5,676.6**	**100.0**	**6,444.4**	**100.0**	**6,848.7**	**100.0**

1/ Excluding Securities
Source: Central Bank of Bahrain

Outstanding credit facilities to the personal sector increased by 9.5% from BD 2,162.1 million at end-2011 to BD 2,368.1 million at end-2012. Personal loans showed a 5.4% increase in the second quarter of 2012 compared to first quarter. Personal sector credit facilities accounted for 34.6% at end-2012, increasing from 33.5% in 2011 and 30.9% in 2010. Credit to general government is typically low in comparison, accounting for 2.9% in 2012, lower than the 3.5% in 2011 and 4.6% in 2010. Outstanding government credit decreased by 13.8% to BD 225.5 million at end-2011, compared with BD 261.5 million at end-2010. However, by the end of 2012, lending to general government decreased by 12.2% to reach BD 197.9 million.

Table 4-12: Business Loans by Sector

(BD Million)

Sectors	2012*							
	Q1		Q2		Q3		Q4	
	Value	%	Value	%	Value	%	Value	%
Manufacturing	542.0	8.2	537.5	7.9	558.7	8.1	537.5	7.8
Mining & Quarrying	11.2	0.2	11.1	0.2	10.0	0.1	8.9	0.1
Agriculture, Fishing & Dairy	8.9	0.1	10.5	0.2	9.6	0.1	11.5	0.2
Construction & Real Estate	1,781.6	27.1	1,765.9	26.0	1,760.5	25.4	1,641.7	24.0
Trade	851.6	12.9	909.8	13.4	912.0	13.2	960.0	14.0
Non-Bank Financial	333.0	5.1	335.4	4.9	330.0	4.8	327.9	4.8
Other Sectors, of which:	701.2	10.6	711.8	10.5	821.6	11.8	795.2	11.6
Transport & Comm.	179.5	2.7	202.2	3.0	269.5	3.9	248.7	3.6
Hotels & Restaurants	164.1	2.5	141.0	2.1	141.6	2.0	143.8	2.1
Total Business Loans	**4,229.5**	**64.2**	**4,282.0**	**63.1**	**4,402.4**	**63.5**	**4,282.7**	**62.5**

**Percentages are expressed as a share of total loans*
Source: Central Bank of Bahrain

In the fourth quarter of 2012, loans to the construction and real estate segment accounted for the largest share of business loans (38.3%), with the trade sector being in second place at 22.4%. Most of the growth in business loans in 2012 occurred in the trade and transportation and communication sectors.

Salary assigned loans represented the largest proportion of personal loans throughout 2012, reaching highs of 43.4% at the end of the year. Salary assigned loans and those secured by property mortgage made up for 73.5% of all personal loans by the end of 2012.

Table 4-13: Personal Loans by Sector

(BD Million)

Sectors	2012*							
	Q1		Q2		Q3		Q4	
	Value	%	Value	%	Value	%	Value	%
Secured by:								
Property Mortgage	681.2	10.3	702.3	10.3	714.9	10.3	713.1	10.4
Vehicle Title	88.7	1.4	92.6	1.4	96.3	1.4	98.2	1.4
Deposits	27.1	0.4	26.3	0.4	23.6	0.3	25.8	0.4
Salary Assignment	919.7	14.0	984.1	14.5	997.3	14.4	1,028.2	15.0
Credit Card Receivables	63.1	1.0	67.2	1.0	71.7	1.0	73.8	1.1
Other	370.1	5.6	394.3	5.8	392.2	5.7	429.0	6.3
Total personal loans	**2,149.9**	**32.7**	**2,266.8**	**33.4**	**2,296.0**	**33.1**	**2,368.1**	**34.6**

**Percentages are expressed as a share of total loans*
Source: Central Bank of Bahrain

D. Mutual Funds

The mutual funds industry in Bahrain has been declining in line with the rest of the financial sector. Retail and wholesale banks, representative offices, investment business firms, and other institutions market their approved mutual funds to both individual and institutional investors.

The total amount of outstanding investments for all institutions decreased by 8.9%, from USD 8,378.2 million in 2011 to USD 7,632.8 million in 2012 (Table 4-14). The drop in the value of mutual funds reflected the decline in the global value and amount of investment in securities.

Table 4-14: Mutual Funds – Total Outstanding Investments, 2012

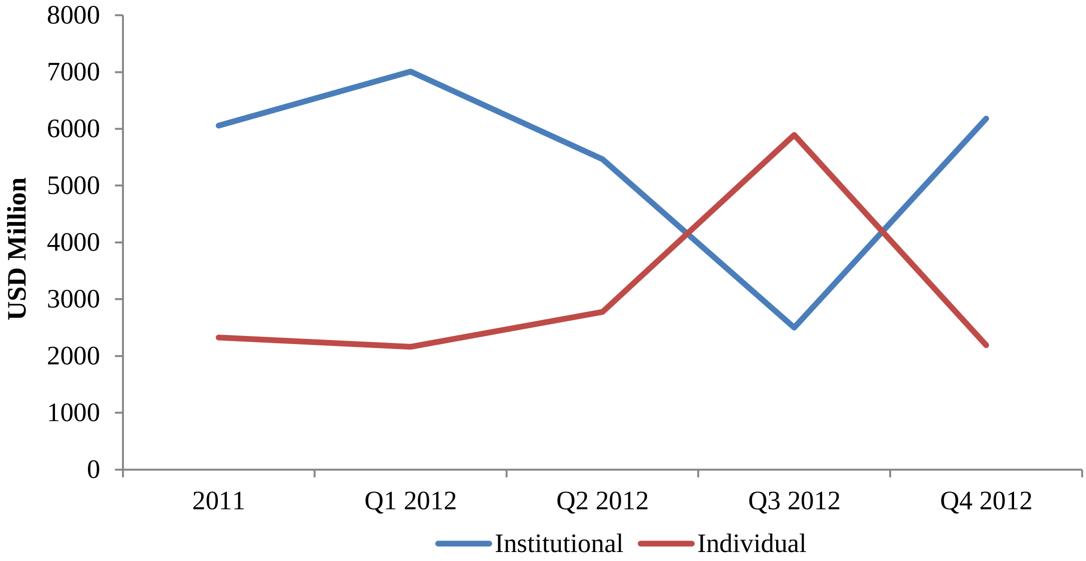
(USD Million)

Type of Institution	2011	2012			
		Q1	Q2	Q3	Q4
Retail Banks	2,356.8	2,751.9	2,337.8	2,340.0	2,399.6
Wholesale Banks	1,710.0	1,495.2	1,452.4	1,558.6	1,476.7
Investment Business Firms	1,017.3	1,232.3	501.2	580.0	582.2
Representative Offices	0.0	0.0	0.0	0.0	0.0
Foreign Licensed Banks and Financial Institutions	3,271.4	3,669.3	3,931.3	3,894.0	3,154.0
Insurance	22.7	25.4	21.7	21.1	20.3
Grand Total	**8,378.2**	**9,174.1**	**8,244.4**	**8,393.7**	**7,632.8**

Source: Central Bank of Bahrain

At the end of 2012, retail banks had USD 2,399.6 million outstanding in mutual fund investments, wholesale banks had USD 1,476.7 million outstanding, and other institutions (excluding retail and wholesale banks) had USD 3,756.5 million outstanding. The biggest year on year decreases were in investment business firms (42.8%), wholesale banks (13.6%) and foreign licensed banks and financial institutions (3.6%) categories. On the other hand, retail banks increased by 1.8% for the period.

Chart 4-6: Individual and Institutional Mutual Fund Investments



Source: Central Bank of Bahrain

During 2012, mutual fund investments to institutional investors witnessed an increase while investment to individual investors had a drop (Chart 4-6). Amounts invested in by institutional investors increased by 2.1% from USD 6,055.1 million in 2011 to USD 6,180.0 million in 2012. In contrast, individual investments have shown a different pattern during the year. During 2012, individual investments in mutual funds fell by 5.8%, from USD 2,323.1 million in 2011 to USD 2,187.7 million in 2012 mainly due to a 53.5% decrease in individual wholesale bank investments in mutual funds.

E. Manpower Survey

The CBB annual manpower survey showed a drop in the number of employees in the financial sector (banks and non-banks) of 0.4% following the 2.0% decrease in 2011 (Table 4-15). Total employment in banks (retail banks, wholesale banks and representative offices only) reached 8,011 at the end of 2012, compared to 8,352 at the end of 2011, indicating a decrease of 4.1%. Bahrainis represented 74.3% of the work force in the banking sector compared with 73.6% in 2011.

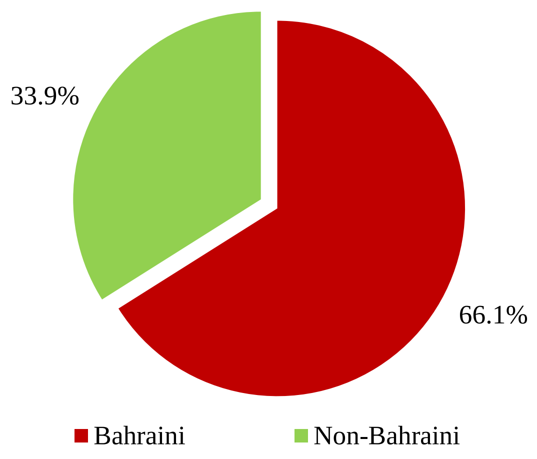
Table 4-15: Number of Employees in the Financial Sector 2012

Institution Type	Bahraini		Non-Bahraini		Total
	Male	Female	Male	Female	
Banking Sector	**3,746**	**2,204**	**1,716**	**345**	**8,011**
Retail Banks	2,800	1,589	753	174	5,316
Wholesale Banks	933	600	941	165	2,639
Representative Offices	13	15	22	6	56
Non-Bank Financial Sector	**1,831**	**1,085**	**2,029**	**606**	**5,551**
Locally Incorporated Insurance Firms	611	381	408	108	1,508
Insurance Related Activities	139	154	332	106	731
Specialised Licensees*	850	407	1,053	338	2,648
Of which: Money Changers	*191*	*64*	*720*	*246*	*1,221*
Financing Companies / Microfinance Institutions	*330*	*230*	*106*	*25*	*691*
Capital Markets	54	42	37	3	136
Of which: Licensed Securities Brokers	*12*	*0*	*3*	*0*	*15*
Investment Business Firms	177	101	199	51	528
Supporting Institutions	**208**	**179**	**45**	**15**	**447**
Total	**5,785**	**3,468**	**3,790**	**966**	**14,009**

** Includes provider of Ancillary Services, Trust Service Providers and Registered Administrators.*
Source: Central Bank of Bahrain

Bahraini employment in the financial sector decreased by 0.3% while non-Bahraini employment decreased by 0.6%. Bahrainis represented 66.1% of the total number of employees in the financial sector (Chart- 4-7).

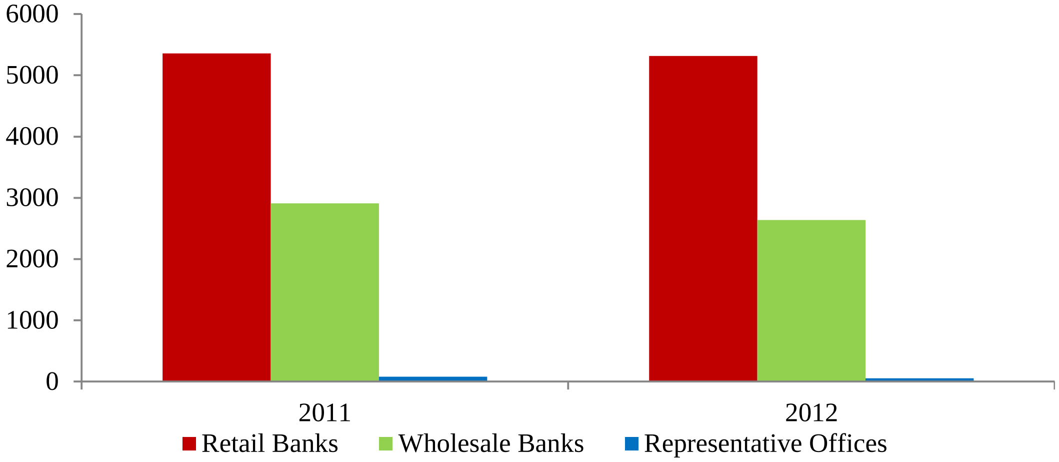
Chart 4-7: Bahraini and Non-Bahraini Employment in the Financial Sector, 2012



Source: Central Bank of Bahrain

The chart below (Chart 4-8) breaks down the banking sector into retail banks, wholesale banks, and representative offices. Wholesale banks, retail banks and representative had decreases in employment of 9.4%, 0.8% and 29.1% respectively.

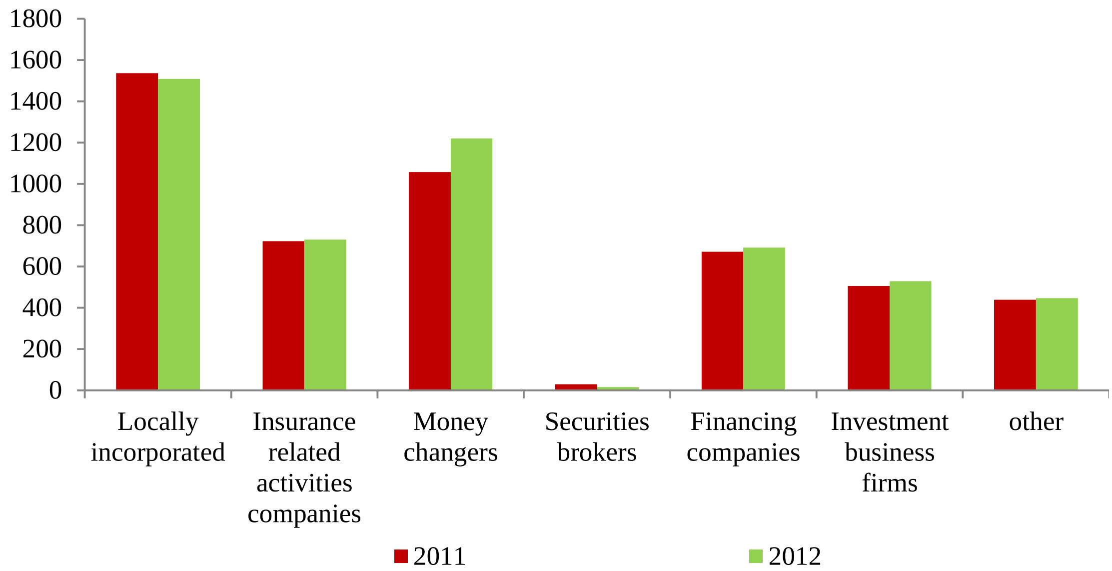
Chart 4-8: Employment in the Banking Sector



Source: Central Bank of Bahrain

Total employment in the non-bank financial sector reached 5,551 at end-2012, compared with 5,271 at end-2011, an increase of 5.3%. Bahrainis accounted for 52.5% of the total in the non-bank financial sector. The biggest increase in employment in the non-banking sector was in money changers which increased by 15.5%, while locally incorporated insurance firms decreased the most by 1.8% (Chart 4-9).

Chart 4-9: Employment in the Non-Banking Sector



Source: Central Bank of Bahrain.

Chapter

5

5. Bahrain Bourse

Overview

A. Main Trading Indices

B. Developments in Market Capitalisation and Share Issue Base

C. Trading Activities

D. Nationalities of Investors

E. Price Movements

F. New Companies Listed on the Bahrain Bourse

Overview

The global economy was showing early signs of a slowdown and despite a year of uncertainty, the U.S. stock market performed surprisingly well, posting double-digit gains in 2012. All of the major U.S. stock indices finished 2012 solidly in positive territory. The biggest winner was the technology-dominated Nasdaq composite, which gained 15.9%. That's a vast improvement from a year ago, when the tech-heavy index fell 1.8%. The S&P 500 gained more than 13.4%. The worst performer of the four major indices was the Dow Jones industrial average, which rose 7.3%. A total of 128 companies went public – the second-highest IPO total in the last five years. Stocks also got a boost from an improvement in the jobs market.

Despite all the turmoil across Europe, only the Greek and the Spanish stock markets ended in the red. The Greek market was down 2.5% for the year, while the Spanish market fell 1.9%, according to MSCI data. The major markets of Germany, France and the UK were up 28.1%, 19.1%, and 11%, respectively, through to December 28.

Asian equity markets, except for China, once again delivered the best returns for global investors. Government bond yields have moved lower adding some capital gains to the ever-lower income yields, while corporate and peripheral Eurozone government bonds made more substantial gains as credit risk perceptions declined and equity markets rose.

The seven stock markets operating within GCC are noted for posting mixed performance. The index of Dubai Financial Market grew by 20% in 2012. Abu Dhabi Stock Exchange came second with a growth of 9.5%. The Saudi Stock Exchange grew by a notable 6% and was the most active in trading thanks to Saudi investors. However, the rest of bourses grew either rather slightly or negatively, like 2% and 1% in the cases of Kuwait and Muscat, respectively. The Qatari Exchange dropped by 5% in 2012.

The Bahrain Bourse posted a decline of 6.8% for the year. Performance amongst the sectors all suffered decreases with the exception of the "services" sector according to the Bahrain All Share Sub-Indices, which increased by 8.2%. The biggest decline was in the "industrial" sector (34.0%).

After a small decrease in January 2012, the index increased from February 2012 to April 2012. The index then decreased from until August 2012. In September 2012, the index had a minor increase followed by a decrease until November 2012. The index increased in December 2012 by 16.8 points (1.6%)

The Bahrain Bourse continues to make efforts to strengthen its ties with other stock markets in an effort to offer a more attractive and profitable investment environment especially after the events that the Kingdom witnessed.

The number of companies listed on the exchange in 2012 remained at 47.

A. Main Trading Indices

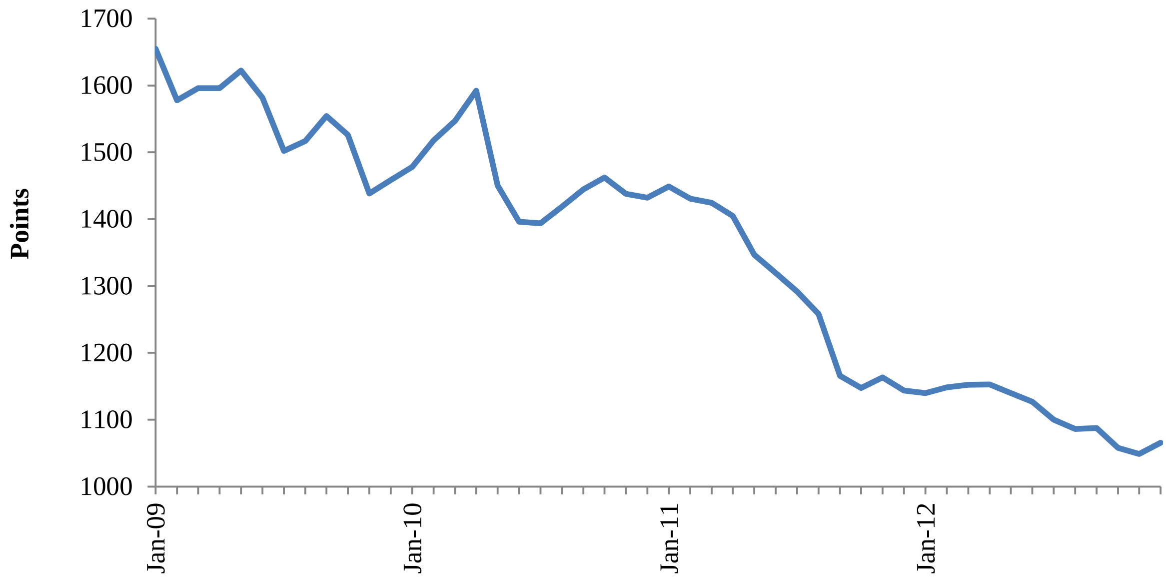
The Bahrain All Share Index closed at the end of the year at 1,065.61 points recording a year on year decrease of 6.8%. All sectors witnessed a year on year decrease in 2011 with the exception of the "services" sector that reported an increase of 8.2%. The "industrial" sector reported the biggest decline of 34.0%. The Dow Jones Bahrain and Esterad Indices decreased by 8.67 points (8.8%) and 115.68 points (9.5%) from end-2011 respectively.

Table 5-1: Bahrain Bourse Indices

BSE Indices	Q4 2011	Q4 2012	Change (Point)	Change (%)
Bahrain All Share Index	**1,143.69**	**1,065.61**	**-78.08**	**-6.8**
Commercial Banks	1,814.05	1,792.20	-21.85	-1.2
Investment	697.30	646.20	-51.10	-7.3
Insurance	1,852.03	1,718.03	-134.00	-7.2
Services	1,148.99	1,242.75	93.76	8.2
Industrial	1,055.17	696.26	-358.91	-34.0
Hotels and Tourism	3,573.71	3,468.87	-104.84	-2.9
Dow Jones Bahrain Index	98.20	89.53	-8.67	-8.8
Esterad Index	**1,218.26**	**1,102.58**	**-115.68**	**-9.5**

Source: Bahrain Bourse

Chart 5-1: Performance of Bahrain All Share Index, 2009-2012



Source: Bahrain Bourse

B. Developments in Market Capitalisation

Market Capitalisation of the BSE stood at BD 5.9 billion by the end of 2012, down from the BD 6.3 billion million in 2011, a decrease of 6.4% (Table 5-2). Similar to the Bahrain All Share Index, the decrease was in all sectors with the exception of the "services" sector with an increase in market capitalisation of 8.1%. The largest decrease was in the "industrial" sector with a decrease of 34.0% from BD 954 million in 2011 to BD 629 million at end of 2012.

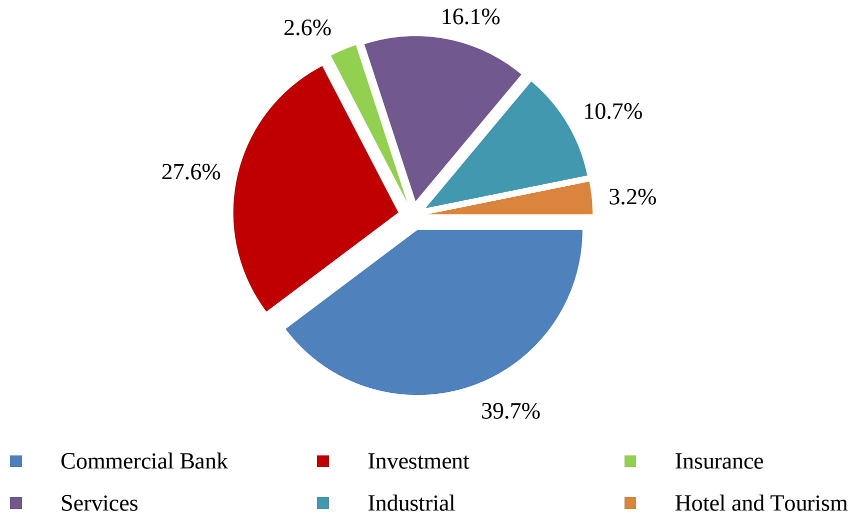
Table 5-2: Market Capitalisation by Sector

	2011	2012	Change (%)	% Weight (Current Year)
Total Market Capitalisation	**6,254,410,719**	**5,855,641,334**	-6.4	100.0
Commercial Banks	2,393,210,243	2,327,593,590	-2.7	39.7
Investment	1,679,550,059	1,617,333,595	-3.7	27.6
Insurance	164,480,545	152,623,990	-7.2	2.6
Services	871,781,382	942,791,466	8.1	16.1
Industrial	953,842,995	629,373,276	-34.0	10.7
Hotels and Tourism	191,545,495	185,925,417	-2.9	3.2

Source: Bahrain Bourse

The "commercial bank", "investment" and "services" sectors are the largest sectors in terms of market capitalisation in 2012 accounting for 83.4% of total market capitalisation (Chart 5-2).

Chart 5-2: Market Capitalisation by Sector, 2012



Source: Bahrain Bourse

As for companies, the largest company in terms of market capitalisation at end-2012 was Ahli United Bank (AUB) with BD 1.2 billion, accounting for 19.7% of total market capitalisation. In 2012, the 5 largest companies accounted for 57.1% of total market capitalisation (Table 5-3).

Table 5-3: Table: Largest Companies by Market Capitalisation (2012)

Company	Market Capitalisation (BD)	% of Total Market
AUB	1,154,234,520	19.7
ALBH	613,440,000	10.5
BATELCO	581,760,000	9.9
ABC	539,336,200	9.2
NBB	453,340,800	7.7
TOTAL	**3,342,111,520**	**57.1**

Source: Bahrain Bourse

C. Trading Activities

The volume of shares traded in 2012 increased to 627.7 million shares (20.7%) compared to BD 520.2 million shares in 2011 (Table 5-4). The value of shares traded increased by 3.8% in comparison to the previous year, reaching BD 110.2 million in 2012 compared from BD 105.0 million in 2011.

Table 5-4: Daily Traded Averages

	2011	2012	Change (%)
Total Trading Days	**245**	**248**	**1.2**
Value of Shares Traded (BD Million)	105.0	110.2	5.0
Daily Average Value of Shares Traded (BD)	**428,433**	**444,531**	**3.8**
Volume of Shares Traded (Million)	520.2	627.7	20.7
Daily Average No. of Shares Traded (Million)	**2.1**	**2.5**	**19.0**
Number of Transactions	11,818	10,168	-14.0
Daily Average No. of Transactions	**48**	**41**	**-14.6**

Source: Bahrain Bourse

Moreover, most of the trading activity in terms of value and volume was concentrated in the “commercial banks” sector with a trading value of BD 68.5 million comprising 62.2% of the total value of shares trading and a trading volume of 452.5 million shares comprising 72.1% of the volume of shares traded in the market (Table 5-5 and Table 5-6). The value of shares traded for the sector increased by 37.0% compared with 2011 whilst the volume of shares decreased by 67.7% (Table 5-5 and Table 5-6).

Table 5-5: Trading Value by Sector

	2011	2012	Change (%)	% Weight (Current Year)
Total Trading Value (BD)	**104,966,160**	**110,243,688**	**5.0**	**100.0**
Commercial Banks	50,003,570	68,518,725	37.0	62.2
Investment	20,346,887	9,265,765	-54.5	8.4
Insurance	1,164,081	811,825	-30.3	0.7
Services	20,008,379	15,790,970	-21.1	14.3
Industrial	9,236,238	7,120,650	-22.9	6.5
Hotels and Tourism	1,186,604	644,920	-45.6	0.6
Non-Bahraini	0	0	0.0	0.0
Closed	0	52,343	-	0.0
Preferred Shares	3,020,401	8,038,490	166.1	7.3

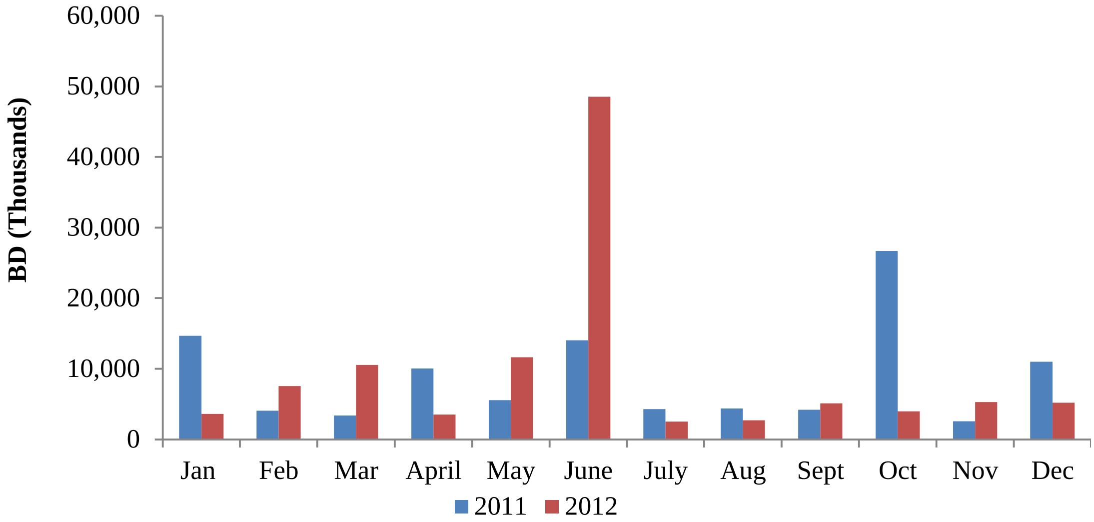
Source: Bahrain Bourse

Table 5-6: Trading Volume by Sector

	2011	2012	Change (%)	% Weight (Current Year)
Total Trading Volume (shares)	**520,223,918**	**627,707,657**	**20.7**	**100.0**
Commercial Banks	269,771,059	452,493,842	67.7	72.1
Investment	144,727,582	51,951,010	-64.1	8.3
Insurance	3,799,574	3,181,362	-16.3	0.5
Services	60,848,874	48,952,066	-19.6	7.8
Industrial	13,635,740	12,953,637	-5.0	2.1
Hotels and Tourism	7,411,146	4,660,772	-37.1	0.7
Non-Bahraini	0	0	-	0.0
Closed	0	124,626	-	0.0
Preferred Shares	20,029,943	53,390,342	166.6	8.5

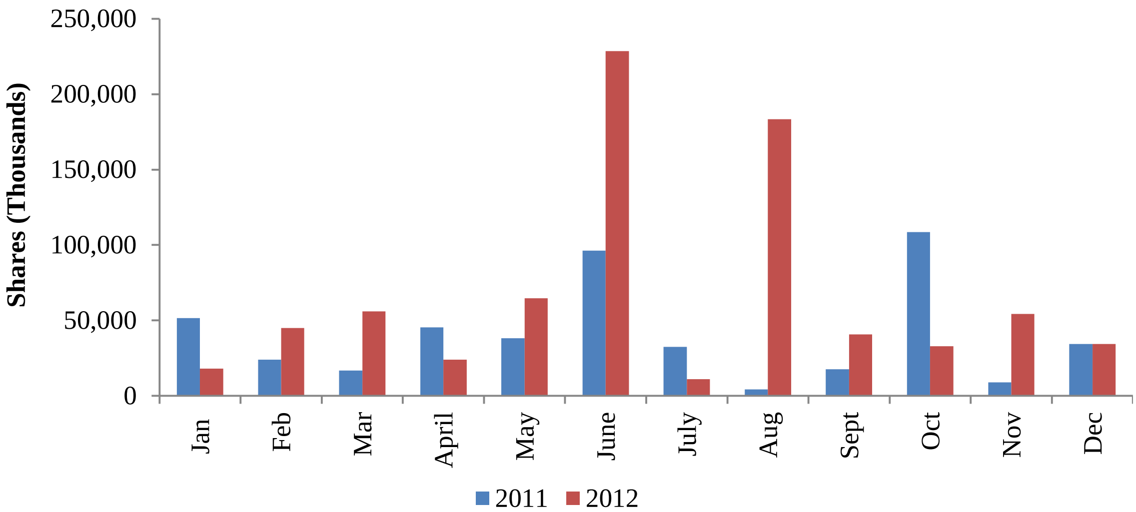
Source: Bahrain Bourse

Chart 5-3: Value of Shares Traded



Source: Bahrain Bourse

Chart 5-4: Volume of Shares Traded



Source: Bahrain Bourse

In terms of listed companies, the most active company by value was Ahli United Bank (AUB), with BD 50.0 million traded (45.4% of total value of shares traded). Next came Ithmaar Bank (ITHMR) with BD 8.6 million constituting 7.8% of the total value of shares traded, then Aluminium Bahrain (ALBH) with BD 7.1 million and 6.4% of total value of shares traded, followed Bahrain Telecommunications Company (BATELCO) with BD 6.7 million constituting 6.1% of the total value of shares traded, and finally came bank of Bahrain and Kuwait (BBK) with BD 4.3 million constituting 3.9% of the total value of shares traded (Table 5-7).

Table 5-7: Most Active Companies by Value, 2012

Company	Value (BD)	% From Total Market
AUB	50,023,017	45.4
ITHMR	8,589,367	7.8
ALBH	7,055,827	6.4
BATELCO	6,749,251	6.1
BBK	4,301,458	3.9
Total	**76,718,920**	**69.6**

Source: Bahrain Bourse

As for most active companies by volume, Ahli United Bank (AUB) had the most traded shares with 221.1 million shares traded translating to 35.2% of total volume, then came Ithmaar Bank (ITHMR) with 147.2 million constituting 23.5% of the total volume of shares traded, then Al Salam Bank (SALAM) with 56.8 million and 9.1% of total volume of shares traded, followed by Bahrain Telecommunications Company (BATELCO) with 6.0 million constituting 2.6% of the total volume of shares traded, and finally Gulf Finance House (GFH) with 15.4 million constituting 2.5% of the total volume of shares traded (Table 5-8).

Table 5-8: Most Active Companies by Volume, 2012

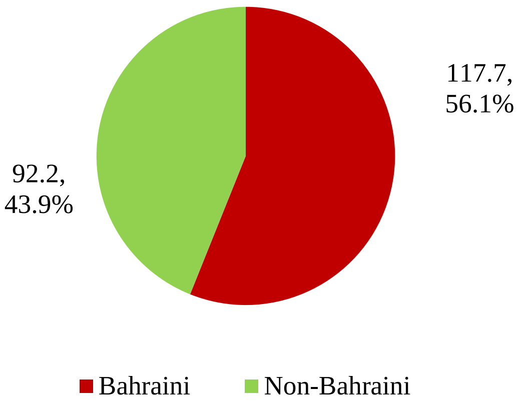
Company	Volume	% of Total Market
AUB	221,122,282	35.2
ITHMR	147,210,169	23.5
SALAM	56,834,253	9.1
BATELCO	16,006,395	2.6
GFH	15,410,270	2.5
Total	**446,583,369**	**72.4**

Source: Bahrain Bourse

D. Nationalities of Investors

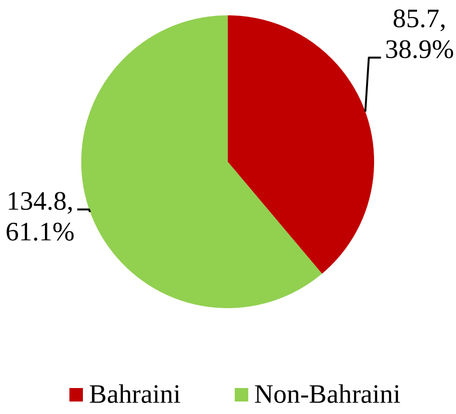
Bahraini investors accounted for 38.9% of the total value of traded shares (buy and sell) in 2012; a significant decrease from the 56.1% in 2011 (Chart 5-5 and 5-6). The market witnessed a total of BD 85.7 million in the value of shares traded by Bahraini investors in 2012 compared to BD 117.7 million in 2011. On the other hand, the total value of traded shares (buy and sell) for non-Bahrainis increased from 43.9% (BD 92.2 million) in 2011 to 61.1% (BD 134.8 million) in 2012.

Chart 5-5: Trading Value of Investors' Participation (BD million), 2011



Source: Bahrain Bourse

Chart 5-6: Trading Value of Investors' Participation (BD million), 2012



Source: Bahrain Bourse

E. Price Movements

During 2012, the market breadth showed that the decliners outperformed the advancers by a margin of 21:16 (the price of 16 stocks went up, 21 went down) and 10 remained unchanged compared to the decliners outperforming the advancers by a margin of 30:3 and 16 unchanged for 2011 (Table 5-9).

Table 5-9: Market Breadth

	2011	2012
Advancers	3	16
Decliners	30	21
Unchanged	16	10
Total	**49**	**47**

Source: Bahrain Bourse

Ithmaar Bank (ITHMR) was ranked the top advancer in 2011 with 161.5% in price change followed by United Investment Gulf Company (UGIC) (59.6%), Esterad Investment Company (ESTERAD) (56.8%), Seef Properties (SEEF) (43.8%), and Bahrain Cinema Company (CINEMA) (28.2%).

As for the top 5 decliners, Inovest (INOVEST) was the biggest decliner with 39.1% annual decrease in price followed by Bahrain Middle East Bank (BMB) (-36.0%), Aluminium Bahrain (ALBH) (-34.6%), Al Baraka Banking Group (BRKA) (-29.4%), and Arab Insurance Group (ARIG) (-22.2%)

Table 5-10: Top Bahrain Bourse Advancers, 2011

Advancers	%	Rank
ITHMR	161.5	1
UGIC	59.6	2
ESTERAD	56.8	3
SEEF	43.8	4
CINEMA	28.2	5

Source: Bahrain Bourse

Table 5-11: Top Bahrain Bourse Decliners, 2011

Decliners	%	Rank
INOVEST	-39.1	1
BMB	-36.0	2
ALBH	-34.6	3
BARKA	-29.4	4
ARIG	-22.2	5

Source: Bahrain Bourse

F. New Companies Listed on the Bahrain Bourse

The number of listed companies (including international cross-listings) at the end of 2012 decreased to 47, compared to 49 in at end of 2011 (Table 5-10). The number of mutual funds and Bonds and Sukuks also decreased to 26 and 8 respectively. Only one preference share was listed on the exchange in 2012 similar to 2011.

Table 5-12: Bahrain Bourse Summary of Listings

	end 2011	end 2012
Number of Companies	49	47
Number of Mutual Funds	31	26
Number of Bonds and Sukuks	11	8
Preferred Shares	1	1

Source: Bahrain Bourse

Chapter
6

6. Public Finance

Overview

A. Revenues

B. Expenditure

C. Issuance of Public Debt Instruments

Overview

Although the Bahrain economy has diversified away from the oil sector, oil revenues continue to play a significant role in the governments' fiscal balance. Oil prices remained consistently high during the year 2012, and as a result, government revenues increased modestly by 7.5% to reach BD 3,034.2 million compared to BD 2,821.7 million at the end of 2011. Government expenditure increased by 14.3% to reach BD 3260.9 million during the same period, up from BD 2,853.0 million in 2011.

Given the recent developments and increased government spending on social projects, the fiscal position of Bahrain has weakened, recording a BD 226.7 million fiscal deficit before rollover. The fiscal deficit accounted for 2.0% of the gross domestic product (GDP) of Bahrain in 2012.

Table 6-1: Summary of Public Finance

(BD Million)

	2008	2009	2010	2011*	2012*
Revenues	**2,677.6**	**1,708.0**	**2,175.6**	**2,821.7**	**3,034.2**
Oil & Gas	2,284.5	1,417.8	1,852.1	2,479.1	2,645.4
Non-Oil	363.6	261.9	294.9	242.6	332.4
Grants	29.5	28.4	28.6	100.0	56.4
Expenditure	**2,060.3**	**2,082.2**	**2,635.4**	**2,853.0**	**3,260.9**
Current	1,552.0	1,692.3	1,868.0	2,412.2	2,523.9
Project	508.3	389.9	767.4	440.8	737.0
Strategic Projects	**70.0**	**72.0**	**0.0**	**0.0**	**0.0**
Surplus/Deficit Before Rollover	**547.3**	**(446)**	**(459.8)**	**(31.3)**	**(226.7)**
As a % of GDP	**5.7**	**(5.2)**	**(4.8)**	**(0.3)**	**(2.0)**
Rollover for the Period					
Project	150.0	206.9	291.0	279.8	276.6
Current	25.2	72.6	22.4	20.0	0.0
Total Rollover	**175.2**	**279.5**	**313.4**	**299.8**	**276.6**
Net Surplus/Deficit After Rollover	**372.1**	**(725.6)**	**(773.2)**	**(311.1)**	**(503.3)**
As a % of GDP	**3.8**	**(8.4)**	**(8.0)**	**(2.8)**	**(4.4)**

** Provisional data*
Source: Ministry of Finance

A. Revenues

Total revenues increased in 2012 by 7.5% to reach BD 3,034.2 million from BD 2,821.7 million in 2011 (Table 6-2). The increases on the revenue side are largely attributed to Oil and Gas and Taxation and Fees segments, which increased by 6.7% and 29.0% respectively. Other revenue sub-segments witnessed variations in performance; (Fines, Penalties & Miscellaneous) and (Government Goods and Services) increased by 201.1% and 11.4% respectively, while (Grants) and (Investment & Government Properties) decreased by 43.6%, and 2.0% respectively.

Table 6-2: Government Revenue

(BD Million)

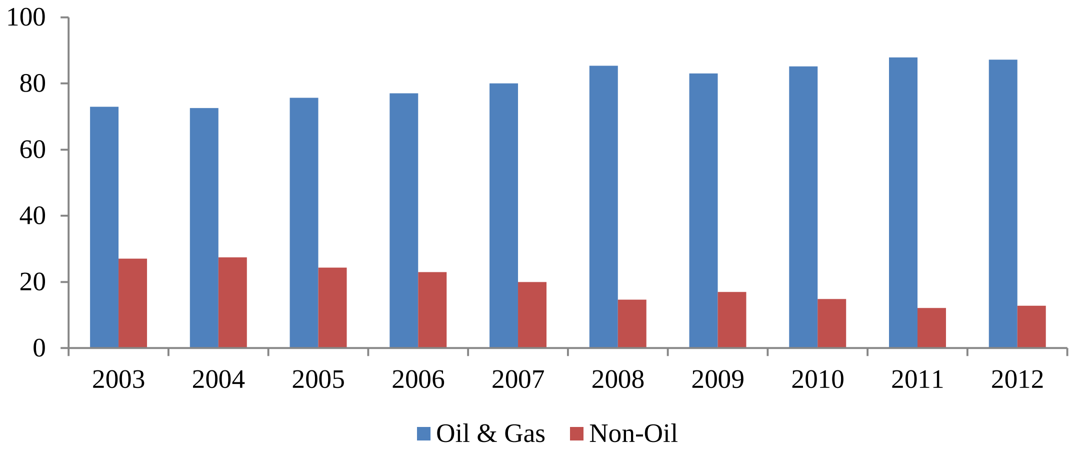
Items	2011	2012	Change (%)
Oil & Gas	2,479.1	2,645.4	6.7
Taxation & Fees	168.7	217.7	29.0
Government Goods & Services	40.4	45.0	11.4
Investments & Government Properties	15.3	15.0	(2.0)
Grants	100.0	56.4	(43.6)
Sale of Capital Assets	0.3	0.7	133.3
Fines, Penalties & Misc.	17.9	53.9	201.1
Total Revenue	**2,821.7**	**3,034.2**	**7.5**

Source: Ministry of Finance

Oil and gas revenues amounted to BD 2,645.4 million (87.2% of total revenues) in 2012 compared with BD 2479.1 million (87.9% of total revenues) in 2011 (Chart 6-1).

Notwithstanding on-going efforts to diversify sources of revenue, oil and gas remains the largest contributor to total revenue. It is anticipated that the share of non-oil revenue to total revenue will modestly increase over the next years, mainly due to the steady growth trend of non-oil GDP.

Chart 6-1: Oil and Non-Oil Revenues as a % of Total Revenues



Source: Ministry of Finance

B. Expenditure

Total expenditures increased by 14.2% in 2012 to reach BD 3260.9 million. Total current expenditure amounted to BD 2523.9 million. The fastest growing component of current expenditure was Manpower, which grew by 19.8%. This was followed by Consumables and Services which increase by 17.7% and 7.9% respectively (Table 6-3).

As for project expenditure, it amounted to BD 737.0 million, experiencing a 67.1% increase.

Table 6-3: Government Current Expenditure (2011 vs. 2012)

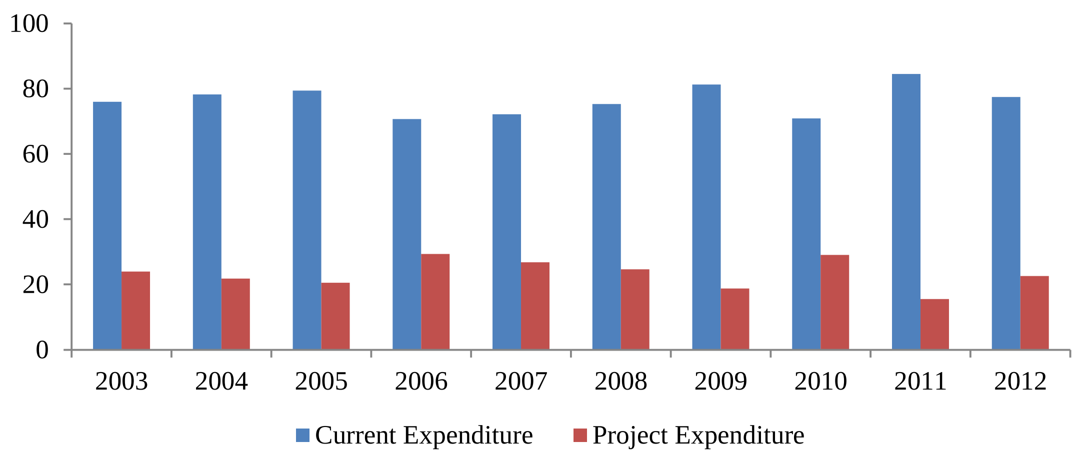
(BD Million)

Items	2011	2012	Change (%)
Manpower	1,005.0	1,204.2	19.8
Services	170.2	183.7	7.9
Consumables	93.7	110.3	17.7
Assets	30.3	30.7	1.3
Maintenance	59.0	60.8	3.1
Transfers	634.8	581.7	(8.4)
Grants and Subsidies	419.2	352.5	(15.9)
Total Current Expenditure	**2,412.2**	**2,523.9**	4.6

Source: Ministry of Finance

Expenditure data for 2012 shows that most of government spending was in the form of current expenditure, which constituted 77.4% of total expenditure, down from 84.5% in 2011 (Chart 6-2).

Chart 6-2: Current and Project Expenditure as a % of Total Expenditure



Source: Ministry of Finance

C. Issuance of Public Debt Instruments

The size of Bahrain's public debt (securities only) has increased during the year 2012. Total debt outstanding at the end of 2012 amounted to BD 3,868.5 million, 22.1% higher than the level at the end of 2011 and accounted for 33.9% of GDP (Table 6-4). The increase in total outstanding debt in 2012 stems mainly from the growth in development bonds (Chart 6-3).

Chart 6-3: Public Debt Instruments

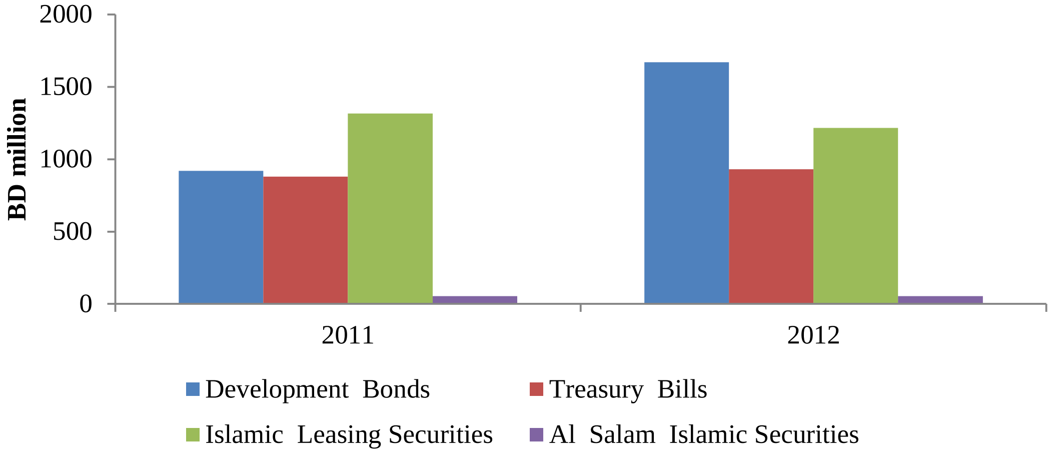


Table 6-4: Summary of Public Debt Instruments

(BD Million)

	2011	2012			
		Q1	Q2	Q3	Q4
Total Outstanding	3,169.5	3,219.5	3,219.5	3,778.5	3,868.5
% of GDP	28.9	28.2	28.2	33.1	33.9
Development Bonds	920.0	920.0	920.0	1,484.0	1,669.0
Treasury Bills	880.0	930.0	930.0	930.0	930.0
Islamic Leasing Securities	1,315.5	1,315.5	1,315.5	1,310.5	1,215.5
Al Salam Islamic Securities	54.0	54.0	54.0	54.0	54.0

Source: Central Bank of Bahrain

The range of conventional instruments includes three month (91 day) treasury bills which are issued on a weekly basis, six month (182 day) treasury bills, which are issued on a monthly basis and development bonds, which are issued when required. The total outstanding amount of development bonds was BD 1,669.0 million in 2012 compared to BD 920.0 million in 2011. The total outstanding amount for T-bills (short and long term) as of December 31, 2012 was BD 930.0 million which is a 5.7% growth from the outstanding balance as of the same time the previous year (Table 6-5). During 2012, new T-bill issues amounted to BD 2,160.0 million as BD 2,110.0 million matured, leaving an outstanding balance of BD 930.0 million.

Table 6-5: Summary of Conventional Public Debt Instruments

(BD Million)

End of Period	Development Bonds 1/			Treasury Bills 2/			Outstanding Balance
	Matured	New Issue	Balance	Matured	New Issue	Balance	
2010	0.0	920.0	975.0	1,285.0	1,440.0	570.0	1,545.0
2011	55.0	0.0	920.0	1,580.0	1,890.0	880.0	1,800.0
2012	0.0	749.0	1,669.0	2,110.0	2,160.0	930.0	2,599.0

1/ Development bonds have a maturity of 5 years and 30 years
2/ Treasury bills have a maturity of 91 and 182 days.
Source: Central Bank of Bahrain

The outstanding balance of Islamic securities as of December 31, 2012 was BD 1,269.5 million, a 7.3% decrease from the BD 1,369.5 million as of December 31, 2011 (Table 6-6). Islamic securities are comprised of Islamic Leasing (Ijara) Securities, which are short term and can be denominated in either US dollar or Bahrain dinar, and Al Salam Islamic Securities, which are long term and dinar denominated.

Table 6-6: Summary of Islamic Public Debt Instruments

(BD Million)

End of Period	Islamic Leasing Securities 1/			Al Salam Islamic Securities 2/			Outstanding Balance
	Matured	New Issue	Balance	Matured	New Issue	Balance	
2010	120.0	120.0	860.0	126.0	144.0	36.0	896.0
2011	216.5	672.0	1,315.5	168.0	186.0	54.0	1,369.5
2012	500.0	400.0	1,215.5	216.0	216.0	54.0	1,269.5

1/ Islamic leasing securities have a maturity of 3, 4, 6 to 10 years for BD & US dollar
2/ Al Salam Islamic securities have a maturity of 91 days
Source: Central Bank of Bahrain

The balance on the Islamic leasing securities declined to BD 1,215.5 million in December 2012 compared to BD 1,315.5 million in December 2011. This is due to a higher amount of securities maturing (BD 500.0 million) in comparison to new securities that were issued (BD 400.0 million).

The level of Al Salam Islamic Securities outstanding balance remained at BD 54.0 million between 2011 and 2012. The amount of Al Salam securities that matured in 2012 was BD 216.0 million, while the amount issued during the year reached a total of BD 216.0 million, yielding to a balance of BD 54.0 million.

Chapter

7

7. Foreign Trade and Balance of Payments

Overview

A. Current Account

B. Capital and Financial Account

C. International Investment Position (IIP)

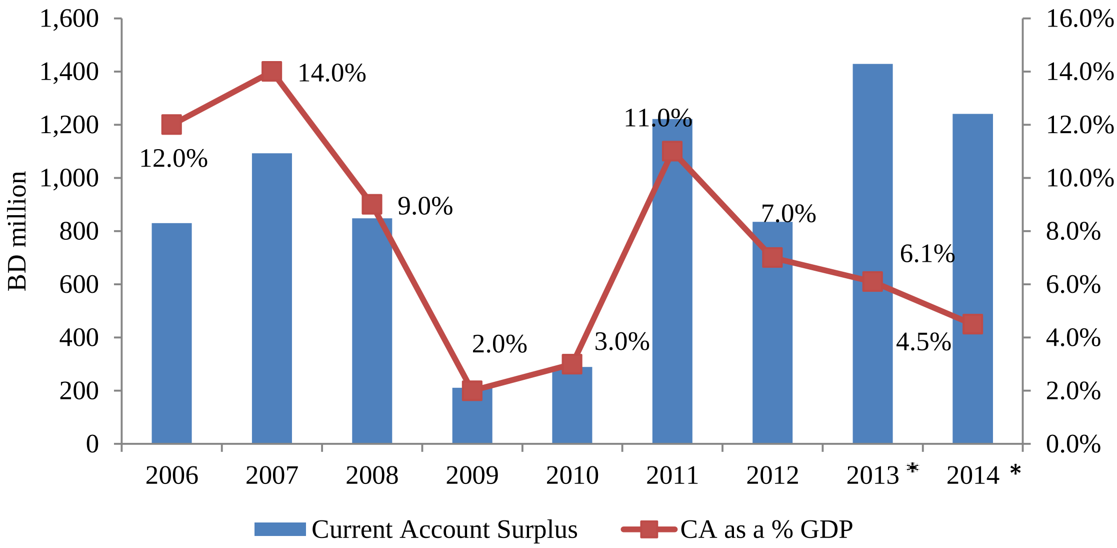
Overview

Bahrain, as a free market economy with no trade and capital restrictions, is one of the major trade and financial hubs in the region. Bahrain's location, as well as a strong transport and communications infrastructure, has helped boost Bahrain's international trade and capital movements. Therefore, external trade plays a critical role in the Bahraini economy. Main imports include commodity imports for domestic consumption while main exports include crude oil, aluminium, and refined products.

A. Current Account

The kingdom of Bahrain's trend of current account surplus continued in 2012 (Chart 7-1). It recorded a current account surplus of BD 835.4 million in 2012. The CA declined by 31.6% from BD 1220.9 million in 2011 (11% of GDP) to BD 835.4 million in 2012 (7% of GDP) (Chart 7-1).

Chart 7-1: Current Account Balance



** IMF projections*
Source: Central Bank of Bahrain.

1. Balance on Goods

The Current Account surplus decreased from the end of 2011 balance mainly due to the decline in the balance of goods by BD 378.1 million, and the relative increase in the accounts of net income payments by 27.4 BD million and current transfers by BD 9.2 million. Oil continues to comprise the major commodity of the kingdom's external trade, representing 77% of total exports and 67% of total imports.

2. Balance on Services, Income and Transfers

The accounts of services, income, and transfers experienced relatively minor changes. However, the services' sub-accounts, financial services and transportation increased by 21.4% and 16.2% respectively. On the income account, other investment income outflows increased by 39.7% from BD 272.7 million in 2011 to BD 381.0 million in 2012. Net current transfers abroad, which are comprised of workers' remittances, remained relatively unchanged, experiencing a mere 1.2% increase.

Table 7-1: Balance of Payments*

Items	BD Million		
	2010	2011	2012
1. Current Account (a+b+c+d)	**289.5**	**1,220.9**	**835.4**
a. Goods	**993.7**	**2,932.9**	**2,554.8**
General Merchandise	**923.7**	**2,836.7**	**2,454.8**
Exports (fob)	5,131.3	7,388.5	7,432.8
- Oil	3,828.0	5,824.5	5,712.8
- Non-Oil	1,303.3	1,564.0	1,720.0
Imports (fob)	-4,207.6	-4,551.8	-4,978.0
- Oil	-2,027.8	-2,808.5	-3,358.0
- Non-Oil	-2,179.8	-1,743.3	-1,620.0
Repairs on goods	**70.0**	**96.2**	**100.0**
b. Services (net)	**805.4**	**474.3**	**503.5**
- Transportation	16.3	32.7	38.0
- Travel	321.9	119.0	121.0
- Communication Services	282.8	215.1	218.0
- Financial Services (Including Insurance)	178.3	100.5	122.0
- Other Business Services	6.1	7.0	4.5
c. Income (net)	**-892.3**	**-1,415.5**	**-1,442.9**
Investment Income	-892.3	-1,415.5	-1,442.9
- Direct Investment Income	-785.2	-1,274.8	-1,201.5
- Portfolio Income	-16.0	132.0	139.7
- Other Investment Income	-91.1	-272.7	-381.0
d. Current Transfers (net)	**-617.3**	**-770.8**	**-780.0**
- Workers' Remittances	-617.3	-770.8	-780.0
2. Capital and Financial Account (net) (a+b)	**-329.8**	**-1,248.1**	**-880.0**
a. Capital Account (net)	**18.8**	**28.6**	37.6
- Capital Transfers	18.8	28.6	37.6
b. Financial Account (1+2+3+4)[1/]	**-348.6**	**-1,276.7**	**-917.6**
1. Direct Investment	**-67.0**	**-42.4**	**-11.7**
- Abroad	-125.6	-336.0	-346.8
- In Bahrain	58.6	293.6	335.1
2. Portfolio Investment (net)	**1,788.2**	**2,099.2**	**1,444.9**
- Assets	771.4	1,941.7	1,030.7
- Liabilities	1,016.8	157.6	414.2
3. Other Investment (net)	**-1,588.7**	**-3,554.3**	**-2,097.6**
- Assets	1,030.1	6,515.1	1,056.3
- Liabilities	-2,618.8	-10,069.3	-3,153.9
4. Reserve Assets (net)	**-481.1**	**220.8**	**-253.2**
3. Errors and Omissions	**40.3**	**27.2**	**44.5**

1/ Financial transactions. A negative sign means net outflows/increases in external assets.
** Provisional Data*
Source: Central Bank of Bahrain

3. Trade Balance

The overall level of trade in Bahrain witnessed a 13.5% decline in 2012. The decrease in the trade balance was mainly due to the surge in imports, which recorded a growth rate of 9.4% between 2011 and 2012.

As a result, the trade surplus contracted to BD 2,454.8 million in 2012 (Table 7-2), down from a surplus of BD 2,836.7 million in 2011. The oil trade surplus decreased from BD 3,016.0 million in 2011 to BD 2,354.8 million in 2012. Moreover, Bahrain recorded a non-oil trade surplus of BD 100 million, contrary to last year's non-oil trade deficit of BD 179.3 million.

Oil exports accounted for 76.9% of total exports in 2012, a modest decrease from 78.7% of total exports in 2011. In terms of imports, oil imports accounted for 67.5% of total imports in 2012, an increase from the 61.7% ratio in 2011.

Table 7-2: Foreign Trade*

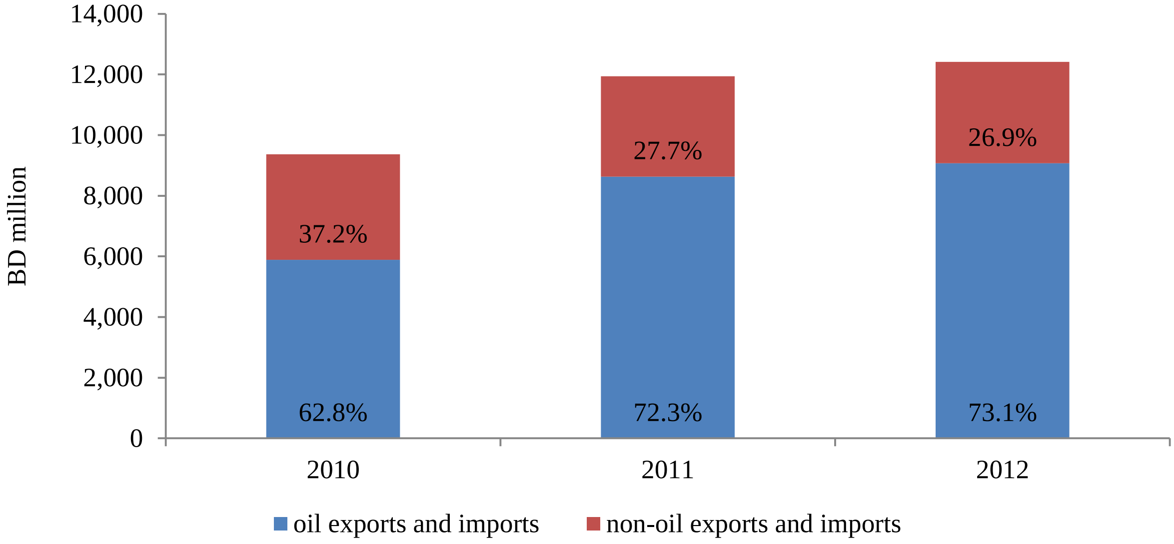
(BD Million)

Main Groups	2011	2012	% Change	Relative Share 2012 (%)
Total Exports	**7,388.5**	**7,432.8**	**0.6**	**100**
Oil Exports	5,824.5	5,712.8	(1.9)	76.9
Non-Oil Exports	1,564.0	1,720.0	10.0	23.1
Total Imports	**4,551.8**	**4,978.0**	**9.4**	**100**
Oil Imports	2,808.5	3,358.0	19.6	67.5
Non-Oil Imports	1,743.3	1,620.0	(7.1)	32.5
Trade Balance	**2,836.7**	**2,454.8**	**(13.5)**	**-**

** Provisional data*

Source: National Oil and Gas Authority and Central Informatics Organisation

Chart 7-2: Oil Trade as a Share of Total Trade



Source: Central Bank of Bahrain

B. Capital and Financial Account

The capital and financial account registered a net outflow of BD 880.0 million in 2012, compared with an outflow of BD 1,248.1 million in 2011. Bahrain continues to be a net exporter of capital to the rest of the world.

The capital account showed a net inflow of BD 37.6 million in 2012 compared to BD 28.6 million in 2011. The financial account registered a net outflow of BD 917.6 million in 2012 compared to BD 1,276.7 million in 2011.

Direct investment in Bahrain increased from BD 293.6 million in 2011 to 335.1 in 2012, reflecting an increased appetite for investment in the kingdom. On the other hand, direct investment abroad recorded an outflow of BD 346.8 million in 2012 compared to BD 336.0 million in 2011.

Bahraini portfolio investments showed a net inflow of BD 1,444.9 million in 2012 compared to a BD 2,099.2 million net inflows recorded in 2011. The other investments category showed a net outflow of BD 2,097.6 million in 2012 compared to BD 3,554.3 million in 2011.

C. International Investment Position (IIP)

Bahrain's net international investment position rose from BD 7,686.7 million at the end of 2011 to BD 8,504.8 million in 2012 (a 10.6% increase) (Table 7-3). Foreign assets fell by 2.4% from BD 61,985.8 million at end-2011 to BD 60,493.3 million in 2012.

On the other hand, foreign liabilities decreased from BD 54,299.1 million in 2011 to BD 51,988.5 million in 2012 (a 4.3% decrease).

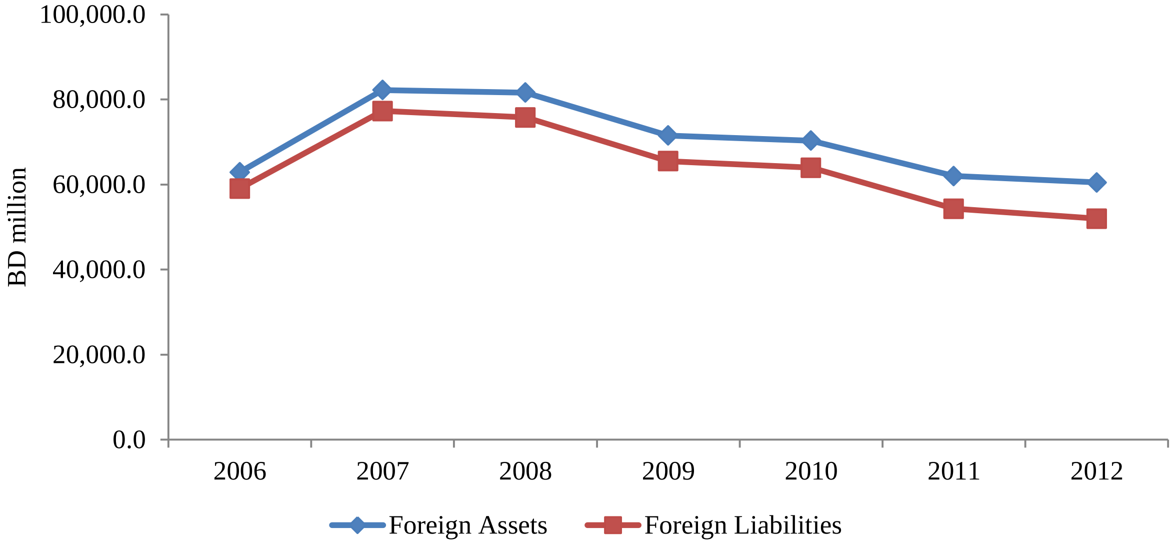
Table 7-3: International Investment Position (IIP) **

(BD Million)

Items	2010	2011	2012
IIP, net	**6,375.0**	**7,686.7**	**8,504.8**
Foreign Assets	**70,327.3**	**61,985.8**	**60,493.3**
Direct Investment Abroad	2,963.9	3,299.9	3,646.7
Portfolio Investment	14,552.3	12,610.6	11,579.9
Other Investment*	50,897.3	44,374.1	43,317.8
Reserve Assets	1,913.8	1,701.2	1,948.9
Foreign Liabilities	**63,952.3**	**54,299.1**	**51,988.5**
Direct Investment in Bahrain	5,697.9	5,991.5	6,326.6
Portfolio Investment	5747.0	5,904.6	6,412.8
Other Investment*	52,507.4	42,403.0	39,249.1

** Includes loans, currency, and deposits.*
Source: Central Bank of Bahrain.

Chart 7-3: International Investment Position (IIP)



Source: Central Bank of Bahrain.