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The Financial Stability Report (FSR) is a semi-annual report prepared by the Central Bank of Bahrain's (CBB) Financial Stability Directorate (FSD). The FSR is available online in PDF format under the Publications and Data section on the CBB's website at http://www.cbb.gov.bh.

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Preface

A key objective of the Central Bank of Bahrain (CBB) is to ensure the continued soundness and stability of financial institutions and markets. As the single regulator for the Bahraini financial system, the CBB attaches utmost importance in fostering the soundness and stability of the financial system. The CBB recognizes that financial stability is critical to maintaining Bahrain's position as a regional financial center and ensuring that the sector continues to contribute significantly to growth, employment and development in Bahrain. The CBB defines financial stability as follows:

> *Financial stability can be defined as a situation where the financial system*[1] *is able to function prudently, efficiently and uninterrupted, even in the face of adverse shocks.*

This objective is the primary responsibility of CBB's Financial Stability Directorate (FSD), which conducts regular surveillance of the financial system to identify areas of concern and undertakes research and analysis on issues relating to financial stability. In pursuit of its objective of promoting financial stability, the CBB conducts regular financial sector surveillance, keeping a close watch on developments in individual institutions as well as in the system as a whole.

The Financial Stability Report (FSR) is one of the key components of CBB's financial sector surveillance framework. Produced semi-annually by the CBB's FSD, its principal purpose is macro-prudential surveillance, assessing the safety and soundness of the financial system as a whole (intermediaries, markets and payments/settlement systems). The ultimate objective of such macro-prudential analysis is to identify potential risks to financial stability and mitigate them before they develop into systemic financial turbulence.

Financial Soundness Indicators (FSIs) are used to monitor the banking financial sector on a continuous basis. The data appearing in report is compiled by CBB staff. Revisions and corrections of data can be made and incorporated in an updated electronic version of the report.

The FSR is prepared for the CBB management, reviewing recent trends and identifying areas of concern which require supervisory and policy attention. The FSR is also a tool aimed at informing the public.

This edition of the FSR contains 10 chapters divided into four parts as follows:

- Part I: National and international developments:
    - Chapter 1: International financial developments.
    - Chapter 2: Developments in Bahrain's financial sector and household sector.
- Part II: Developments in the banking sector:
    - Chapter 3: Performance of the banking sector.
    - Chapter 4: Performance of conventional banks.
    - Chapter 5: Performance of Islamic banks.
- Part III: Developments in the non-banking financial sector.

[1] A Financial System is comprised of the financial intermediaries, financial markets, and financial infrastructure.

- Chapter 6: Performance of the insurance sector.
- Chapter 7: Performance of capital markets.

- Part IV: Developments in the Payments and Settlements System , FinTech, and Cyber Security
  - Chapter 8: Performance of payment and settlement systems.
  - Chapter 9: FinTech and Financial Inclusion.
  - Chapter 10: Cyber Security.

In its continued effort to ensure financial stability and developing a financial stability mandate, the CBB has created The Financial Stability Committee (FSC) on 20th of July 2017 by Resolution number 49 for year 2017. The committee is chaired by H.E the Governor and has seven members from various directorates within the organization.

The main functions/Goals of the Committee are:

1- To create a Macroprudential Policy Framework
2- Look at Macroprudential Policy Tools to be considered for Macro financial risks
3- Discuss the risks that can affect the soundness of the financial sector.
4- Improve Banking Supervision tools on banking and financial services on a periodic basis to ensure best practices especially DSISBs /DSIFISs.
5- Strengthening relations on international level with other regulating entities to prevent cross-border leakages.

Executive Summary

Global Macro Financial Environment Overview

The global economic and financial conditions improved slightly and risks associated to this environment eased in the first half of 2018. In its World Economic Outlook, the International Monetary Fund (MF) is forecasting 3.7% growth in 2018 compared with the 3.6% forecasted last year.

Across major advanced economies, US economic growth increased to 2.8% in Q1/2018 from 2.6% in Q4/2017. The economic performance in Europe decelerated slightly during the first half of the year due to increased uncertainty following the Brexit. In Q1/2018, Euro Area (19 countries) and the European Union (EU) (28 countries) achieved a growth of 2.5%. The UK's GDP growth decreased from 1.3% in Q4/2017 to 1.2% in Q1/2018. The Brexit vote and its spill over effects had a negative impact on the economic activities of the UK economy. The BRIICS countries' growth was strong as it reached the level of 4.5% in Q1/2018 and in China economic growth continued to perform well as it achieved a growth rate of 6.8%.

The Non-Financial Sector Overview

The size of the banking sector assets in Bahrain was USD 188.2 billion as of June 2018 representing 5.3 times GDP in Q2 2018. Retail banking total assets continued growing to reach BD 32.1 billion (USD 85.4 billion) in June 2018 with GCC assets at 23.6% and Europe and American assets at 8.3%. The wholesale banking sector assets declined to USD 102.8 billion with concentrations in GCC (30.5%) and Europe (34.8%).

The total amount of credit given by the retail sector witnessed an increase of 10.3% since June 2017 moving from BD 8,021.0 million to BD 8,844.6 million in June 2018. Total deposits, increased to BD 17,631.2 million in June 2018, where 67.0% of them were domestic deposits. Money supply continued to grow with M2 standing at BD 10,628.8 million in end-June 2018 and M3 was at BD 12,402.3 million. Personal loans as a percentage of GDP increased to 31.7% in June 2018 reaching BD 3,932.8 million. Personal loans as a percentage of GDP increased to 39.5% in June 2018 reaching BD 4,911.8 million.

Banking Sector

The Capital adequacy ratio (CAR) for the banking sector stood at 18.8% in March 2018. The ratio has decreased from 19.4% in September 2017. Non-performing loans (NPL) ratio decreased from 5.7% in September 2017 to 5.5% in March 2018.

As at March 2018, return-on-assets (ROA) remained at 0.3% compared to March 2017. Return-on-equity (ROE) increased from 2.1% in March 2017 to 2.5% in March 2018. Between September 2017 and March 2018, the overall loan-deposit ratio increased from 67.9% to 72.7%. Liquid assets as a proportion of total assets remained nearly constant at 25.5% in March 2018 from 25.6% in September 2017.

Conventional Banks

The CAR for conventional retail banks decreased to 19.6% in March 2018. The NPL ratio also was stable with minor change from 5.8% to 5.9% between September 2018 and March 2018. Specific provisions as a proportion of NPL's showed a decrease from 49.5% to 47.8% over the same period. For local retail banks, the NPL's decreased to 4.2% in March 2018. For overseas retail banks, the NPL's increased to 9.4% in March 2018.

ROA for conventional retail banks reached 04% in March 2018. ROE for locally incorporated conventional banks was at 4.1%. The overall loan-deposit ratio for the segment increased to 73.4% in March 2018 from 70.8% in September 2017. Liquid assets as a proportion of total assets decreased by 2.2% over the period of September 2017 to March 2018 to reach 33.6%.

As for Wholesale banks, CAR for locally incorporated wholesale banks was 18.6% in March 2018, a decrease from the 19.2% registered in September 2017. NPL ratio decreased to 5.3% of total loans. The NPL ratio of locally-incorporated wholesale banks remained at 4.5% between September 2017 and March 2018. Overseas wholesale banks witnessed a decrease in its NPL ratio from 6.9 % to 6.0% over the same period. Specific provisions as a proportion of NPL's also witnessed a decrease to 59.9% over the same period.

ROA for the conventional wholesale banks was at 0.3% in March 2018. ROE for *local wholesale banks* was 2.1%. The overall loan-deposit ratio for conventional wholesale banks stood at 69.9%. Liquid assets for wholesale banks as a proportion of total assets increased by 1.3% to reach 23.2% in March 2018.

Islamic Banks

The CAR of Islamic retail banks decreased from 18.2% in September 2017 to 18.0% in March 2018. Non-performing Facilities (NPF) ratio increased from 9.0% 10.0 and specific provisioning decreased from 44.1% to 44.1% over the same period.

The ROA for Islamic retail banks increased to reach 0.2% in March 2018 compared to 0.1% in March 2017. Return on equity (ROE) increased from 1.1% to 1.5% for the same period. The volume of liquid assets available to Islamic retail banks increased from 11.5% of total assets in September 2018 to 14.5% in September 2018. The ratio of total facilities to deposits increased from 89.1% in September 2017 to 94.4% in March 2018.

As at end-September 2017, the CAR for Islamic wholesale banks decreased slightly from 18.8% in September 2017 to 18.5% March 2018. The NPF ratio for Islamic wholesale banks decreased to 1.4%. Specific provisioning for NPF's decreased from 95.8% to 75.7% over the same period.

ROA for Islamic wholesale banks increased from 0.2% in September 2017 to 0.3% in March 2018. ROE increased as well from 1.4% to 2.0% over the same period. Liquid assets of Islamic wholesale banks represented 21.0 of total assets. Additionally, the facilities deposit ratio increased from 61.4% in September 2017 to 67.9% in March 2018.

Insurance Sector

The Insurance sector in Bahrain is made up of two main segments: Conventional and Takaful. Total gross premiums registered at BD 82.1 million. The conventional local firms accounted for the largest segment of total gross premiums (52.4%), followed by Takaful (26.1%) and conventional overseas branches (21.5%).

As of March 2018, total assets of conventional insurance firms were BD 2,206.5 million (year-on-year growth of 7%). Takaful firms' assets at March 2018 experienced an annual growth by 16.4% reaching BD 184.0 million.

Viewing the concertation of the overall insurance industry, motor records the highest concentration in Gross Premiums (27.6%), Net Premiums Written (40.4%), and Net Claims (50.0%). Similarly for conventional insurance, motor insurance has the highest concentration for Gross Premiums (26.8%), Net Premiums Written (39.4%) and Net Claims (51.5%).

Takaful insurance companies have very high concentration on the Medical and Motor Insurance business lines. Gross Premiums for both sectors represented (70.0%), Net Premiums Written (90.8%), Gross Claims (84.7%), and Net Claims (95.0%).

Capital markets

As at June 2018, Bahrain Bourse recorded a total listing of 43 Companies, 18 Mutual funds and 15 Bonds and Sukuks. The Bahrain All-Share index reached 1,331.0 points in June 2018, while the Bahrain Islamic Index reached 958.1 points. Market capitalization of the Bahrain Bourse stood at BD 8.0 billion, and the price-earnings ratio (P-E ratio) stood at 9.5, a slight increase from the 9.4 attained in December 2017.

The majority of the value and the volume of shares traded in June 2018 was in the "Investment" sector whose traded shares by value represented 31.9% of total shares and by volume of shares represented 50.0%. The majority of the number of transactions in June 2018 (1,104 transactions and a 19.2% increase compared to June 2017) was attained by the "Commercial Banks".

As of June 2018, no major mergers & acquisitions were announced, and 42 public and private offerings occurred with a total value of USD 6.1 billion. Securities and Investment Co. remained the top broker, in terms of total value of shares traded, with more than 50% of the total market value in 2018.

Payments and Settlement System

The RTGS System provides for Payment and Settlement of Customer transactions as a value addition. The daily average volume of Bank transfers for the first half of 2018 (from 1st January, 2018 to 30th June, 2018) increased by 1.1% to 176 transfers compared to 174 transfers for the second half of 2017.

The daily average volume of ATM transactions for the first half of 2018 increased by 11.6% to 51,948 transactions per day compared to 46,549 transactions per day for the second half of 2017. The daily average value of ATM transactions for the first half of 2018 increased by 13.6% from BD4.4 million in the second half of 2017 to 5.0 million.

The daily average volume of cheques for the first half of 2018 decreased by 3.5% compared to the second half of 2017 from 13,294 cheques to 12,827 cheques. The value of those cheques similarly decreased by 2.5% over the same period from BD40.0 million to BD39.0 million.

FinTech and Financial Inclusion

Bahrain is repositioning itself to be a Financial Technology (FinTech) hub in the region combining conventional and Shari'ah compliant FinTech solutions. The CBB has established a dedicated Fintech Unit on the 22nd of October 2017 to ensure best services provided to individual and corporate customers in the financial sector. On 28th May, 2017, the CBB announced the issuance of the Regulatory Sandbox Framework that aims to provide a safe space where business can test FinTech innovative products and services. In April 2017 the CBB issued guidelines for Financing Based Crowdfunding Regulations for both conventional and Islamic lending. In February 2018, Bahrain FinTech Bay (BFB) was launched providing an ecosystem dedicated to further develop and accelerate FinTech firms and drive innovation in Bahrain. A number of digital wallets were launched in the Kingdom allowing users to make instant payments via smart phones and also facilitate the collection of payments electronically.

Cyber Security

Cyber risk is steadily evolving into a main threat to all industries. Its impact however on the financial services industry is growing into an individually recognised risk by all financial institutions. The CBB addresses these risks through the Cyber Security Survey conducted for the retail banking system. The survey response rate was at 100% and based on the survey, 76% of banks reported that their cyber-security strategy has been approved by their Board of Directors, 88% of banks measure the effectiveness of the implementation of risk management practices, and 92% of banks reported that they conduct cyber security training to their staff.

Part I:

Developments in the International and Domestic Financial Markets

1. Developments in the International Financial Markets

Chapter

1

Key Points

- The global economic outlook continues to improve but many challenges remain.
- Financial conditions in the advanced economies remain accommodative.
- Stock markets indices reached new record levels in the first half of the year and Equity markets in Europe rebounded strongly.

1.1 Overview

Global economic activity showed signs of recovery with improvement in consumer confidence and investor' sentiments supported by growth in emerging markets and advanced economies. Despite the increase of interest rates by the Federal Reserve Board, monetary policy remained accommodative in the US and other advanced economies with the aim to support economic growth. In the face of the anticipated exit of the UK from the Euro Area, overall environment showed some signs of resilience in the beginning of 2018. In the following section, recent trends in the global economy are highlighted and the major financial and economic indicators during the previous six months are looked at.

1.2 Global Macro-financial Environment

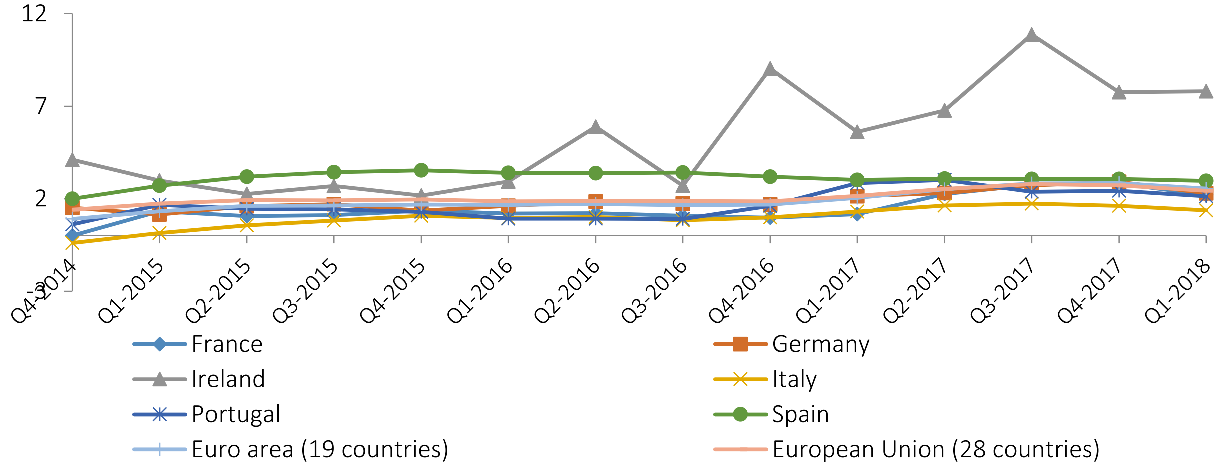
Despite the political and geopolitical risks that have added some risk to financial market, the global economic and financial conditions improved slightly and risks associated to this environment eased in the first half of 2018. In its World Economic Outlook, the International Monetary Fund (MF) is forecasting 3.7% growth in 2018 compared with the 3.6% forecasted last year.

A. Economic Performance

The economic performance in Europe decelerated slightly during the first half of the year due to increased uncertainty following the Brexit, which amplified volatility and raised new concerns in the global financial markets. In Q1/2018, Euro Area (19 countries) and the European Union (EU) (28 countries) achieved a growth of 2.5%. This performance was driven by the surprizing economic boom in Ireland, which achieved 7.8% of growth in the first quarter of 2018. Moreover, Investments reached pre-crisis level and are an important supportive factor for growth together with domestic demand. Spain has achieved a moderate economic performance as GDP growth reached 3.0% for Q1/2018, which was a lowest since Q2/2015. In Q1/2018, Portugal registered a growth rate of 2.1% and Italy continues improving its economic performance as it achieved a growth of 1.4%.

Regarding the two largest economies in the Eurozone, their performances have also slowed in the first quarter of 2018 as compared to the one of the previous year. Germany experienced moderate economic activities in the first quarter of 2018 with GDP growth reach 2.3% and France also achieved growth rate of 2.2% in the same period.

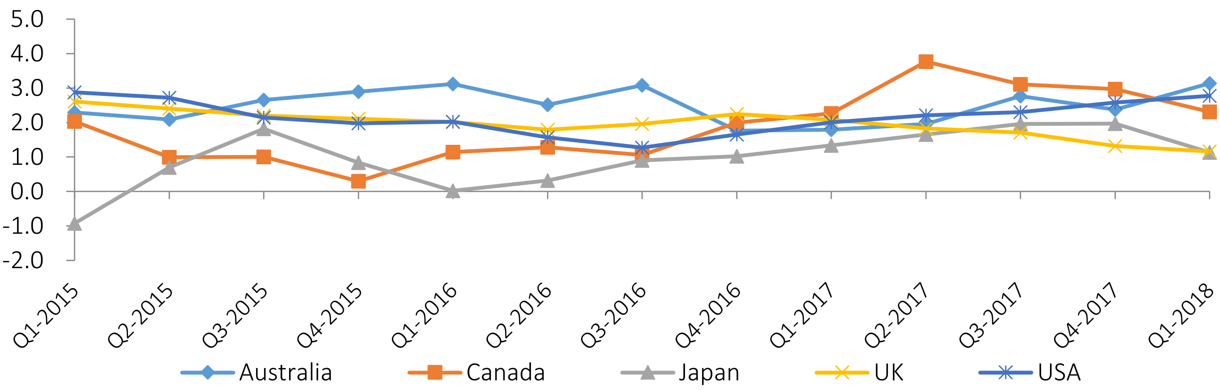
Chart 1-1: Real GDP Growth in Selected Europeans countries (Quaterly%) Seasonally adjusted*



**Growth rate compared to the same quarter of previous year, seasonally adjusted*
Source: OECD Quarterly National Accounts.

In the US as economic growth increased to 2.8% in Q1/2018 from 2.6% in Q4/2017. The US economy was boosted by the restore of confidence and the improvement of consumer sentiments. The UK's GDP growth decreased from 1.3% in Q4/2017 to 1.2% in Q1/2018. The Brexit vote and its spill over effects had negative impact on the economic activities of the UK economy. Australia's economic performance continued its upward trend as GDP growth was 3.1% in Q3/2017 from 2.8% in Q4/2017. For Japan, economic growth improved from 2.0% in Q4/2017 to 1.1% in Q1/2018.

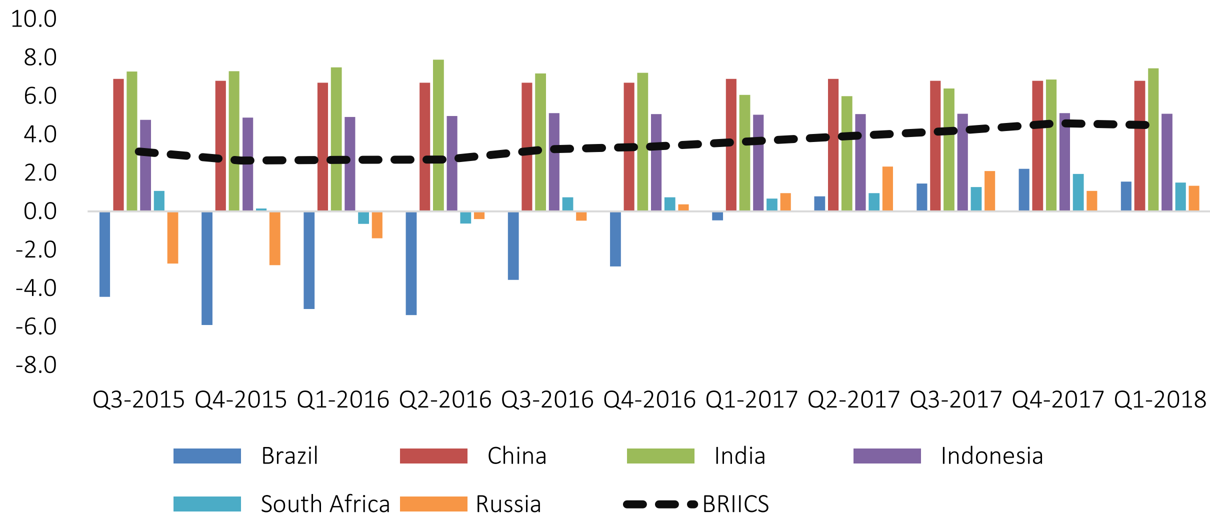
Chart 1-2: Real GDP Growth in Advanced Economies (Quaterly%)*



** Growth rate compared to the same quarter of previous year, seasonally adjusted*
Source: OECD Quarterly National Accounts

As for emerging economies (Chart 1-3), the BRIICS countries' growth was strong as it reached the level of 4.47% in Q1/2018. In China, despite the highly indebted local governments and the financial sector that continues to pose a significant downside risk, economic growth continued to perform well as it achieved a growth rate of 6.8%, similar like the previous two quarters. However, the IMF recently warned about the growing debt-dependency of the world's second biggest economy with China's debt levels posing a stability risk. Brazil's economic performance has shown some signs of recovery after the country fell into recession for the twelfth consecutive quarter. The Brazilian growth stands at 1.6% at Q1/2018. Similarly, Russia shifted from a long period of recession to a positive growth in the first quarter of 2018 as it achieved a growth of 1.3%.

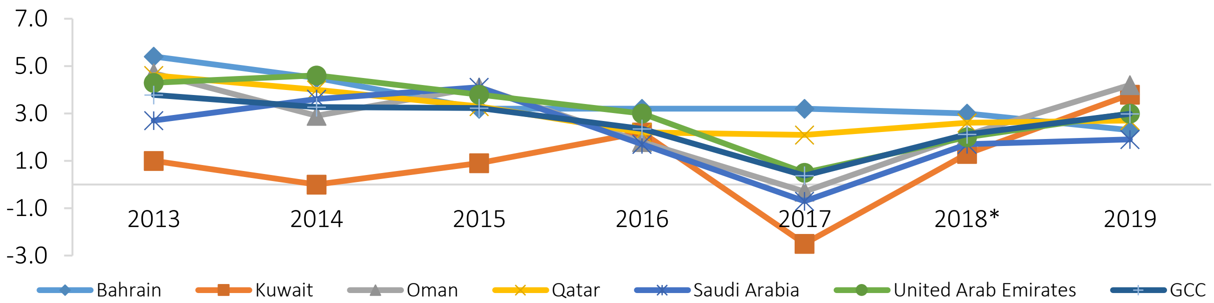
Chart 1-3: Quaterly Real GDP Growth in BRIICS (Quaterly%)*



*Growth rate compared to the same quarter of previous year, seasonally adjusted.
*Data on Russia is not available since the 4th quarter of 2015.
Source: OECD Quarterly National Accounts.

Regionally, the drop of energy prices followed by the continuing uncertainty in the global economy have affected the growth of Gulf Cooperation Council (GCC) economies. However, the recent policy actions taken by the governments were fruitful as the growth rate was expected to be around 2.12%, the highest since 2016. Projections for 2019 show that the economic condition will improve and the regional economy will grow at a moderate rate of growth of 2.98%.

Chart 1-4: Real GDP Growth in GCC Countries (Annual percent change)

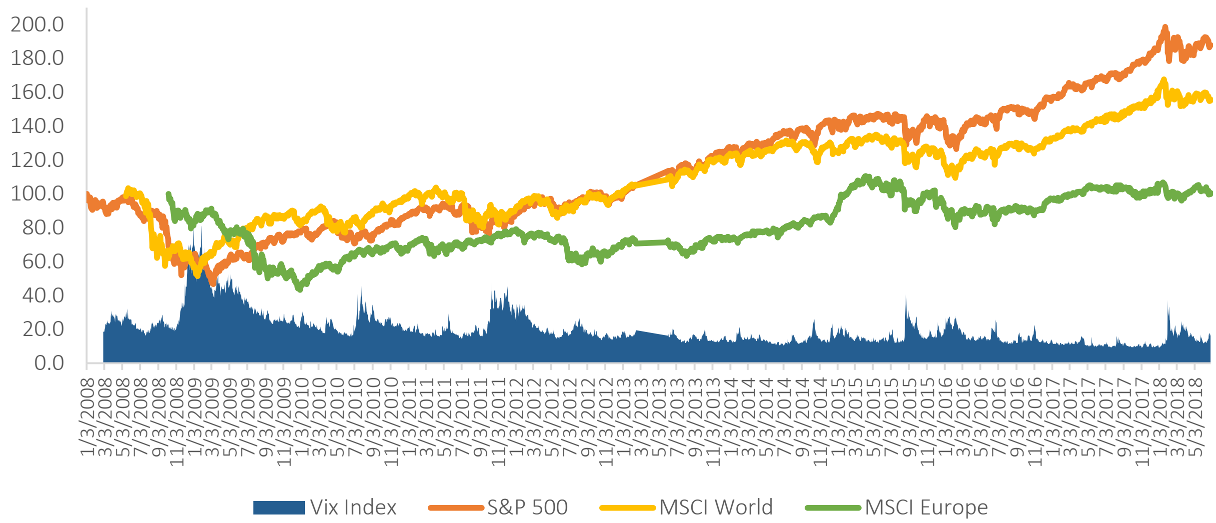


*Forecasts.
Source: IMF Regional Economic Outlook, October 2017.

B. Financial Markets

Equity prices have risen across a range of advanced economies. Indices reached new record levels following the presidential election in the US, France and Austria. Equity prices in the Euro Area recovered strongly, supported by signs of economic activities, improving business and consumer confidence. Similarly, the S&P 500 has risen by around 30% since early 2016, reaching a high record since 2007.

Chart 1-5: Global Equity Market Indices (Re-indexed to January 2008)



Source: Bloomberg.

2. Developments in Bahrain's Financial and non-Financial Sector

Chapter 2

Key Points

- The retail banking sector assets showed an increase to 85.4 billion USD and wholesale banking sector assets decreased to 102.8 billion USD as of end June 2018.
- The volume of credit showed an increase to 8,844.6 million in June 2018.
- Household debt and Business debt ratio increased.
- Construction permits decreased and commercial licenses dropped.

2.1 Overview

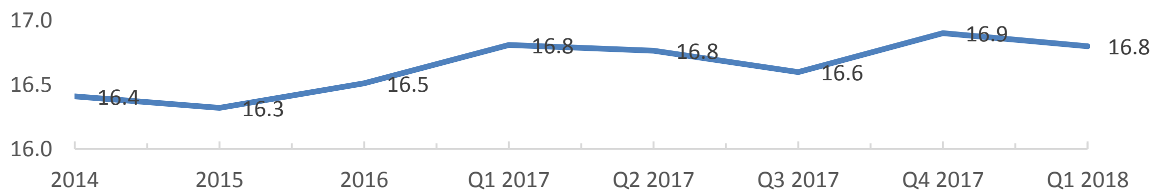
This chapter assesses the recent developments of the Bahraini financial and non-financial sectors and the resilience of the local banking sectors since the last FSR. The financial condition and performance of financial institutions depend to a large extent on the financial condition of their customers (households and enterprises) and their vulnerabilities to changes in the economic environment.

The assessment requires an evaluation of the financial condition and performance of non-financial entities: households, business enterprises, as well as the construction and real estate sector. Households and business enterprises are the major customers of financial institutions. Not only are they sources of deposits, they represent major sources of demand for financial sector products and services

2.2 The Financial Sector

Bahrain position as a regional financial center has been essential to the development of its economy where the financial sector has come to play a significant role in economic activity and employment creation. The banking sector is currently the largest non-oil contributor to GDP representing 16.7% of real GDP as of 2017. By Q1 2018, the banking sector represented 16.8% of real GDP.

Chart 2-1: Size of the Banking Sector to GDP (%)



Source: Information and e-Government Authority (IGA).

As of June 2018, 386 banks and financial instititions were licneded by the CBB. The banking sector in Bahrain was made up of 100 banks, categorized as follows:

- 29 retail banks (including 6 Islamic retail banks); 13 locally incorporated and 16 branches of foreign banks
- 71 wholesale banks (including 16 Islamic wholesale banks); 30 locally incorporated and 41 branches of foreign banks

As of June 2018, there are 286 non-banking financial institutions operating in Bahrain, including investment business firms, insurance companies (including Takaful and Re-Takaful firms), Representative Offices for conventional banks and specialized licenses.

The insurance industry continued to grow during the past few years. Insurance contribution increased to 5.4% of GDP by end of 2017 and 5.6% by Q1 2018. As of June 2018, the insurance market in Bahrain now comprises of 24 locally-incorporated firms and 12 overseas firms carrying out insurance, reinsurance, takaful and retakaful. These institutions offer all basic and modern insurance services such as medical and health insurance and long-term insurance (life and savings products).

Bahrain’s first Islamic commercial Bank, Bahrain Islamic Bank, was established in 1979 and since that, Bahrain has become the home to the Accounting and Auditing Organization for Islamic Financial Institutions, International Islamic Financial Market, and Islamic International Rating Agency, and the Bahrain Institute of Banking and Finance. In 2014, the Global Islamic Finance Report (GIFR) reveals that Bahrain was ranked fourth over 40 countries by Islamic Finance Country Index (IFCI).

2.1.1 The Size of the Banking Sector

The size of the assets of the banking sector in Bahrain was USD 188.2 billion as of June 2018 representing 5.3 times GDP by the end of the second quarter of 2018. The banking sector started as 11.3 times GDP in 2007 and by Q2 2018, the banking sector was 5.3 times of GDP. The change of the size of the banking sector times GDP is attributed to a decrease in the wholesale banking sector along an increase in GDP. Table 2-1 below shows that the change of the size of wholesale banking sector to GDP. The decrease in the size of the banking sector between 2008 and 2011 the is attributed to the wholesale banks adjusting their business models to the international financial crisis and the European debt crisis during these periods.

As for the retail banking sector, it remained between 2.3 to 2.6 times of GDP over the same period. The retail banking sector has continued to grow over the years (USD 49.5 billion in 2007 to USD 85.4 billion in Q2 2018) along with the growth in GDP.

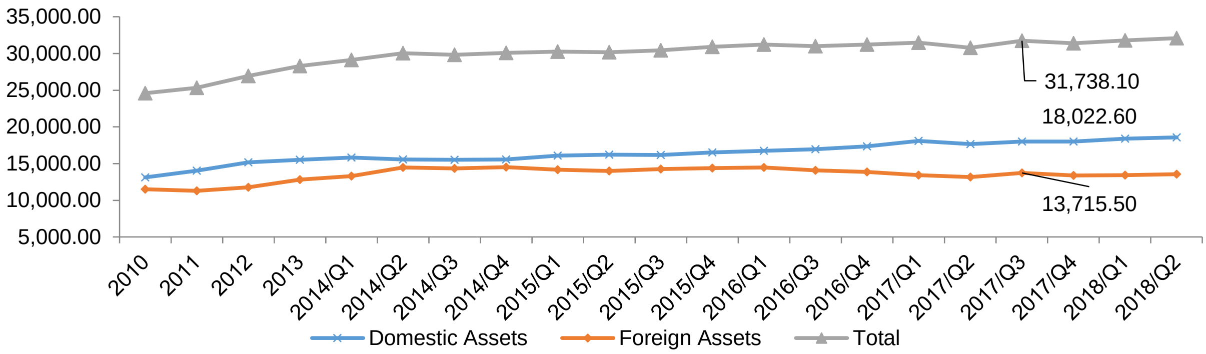
Table 2-1: Evolution of the size of the Banking sector in Bahrain

	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Q1 2018*	Q2 2018*
Banking Sector (USD billion)	245.8	252.4	221.8	222.2	197.1	186.3	192.0	189.3	191.0	186.1	187.4	189.1	188.2
times GDP	11.3	9.8	9.7	8.6	6.8	6.1	5.9	5.7	6.1	5.8	5.3	5.4	5.3
Retail Sector (USD billion)	49.5	63.5	59.7	65.5	67.4	71.7	75.3	80.0	82.2	83.0	83.5	84.6	85.4
times of GDP	2.3	2.5	2.6	2.5	2.3	2.3	2.3	2.4	2.6	2.6	2.4	2.4	2.4
Wholesale Sector (USD billion)	196.3	188.9	162.0	156.7	129.7	114.6	116.7	109.3	108.8	103.0	104.0	104.5	102.8
times of GDP	9.0	7.3	7.1	6.1	4.5	3.7	3.6	3.3	3.5	3.2	2.9	3.0	2.9

** Using 2017 current GDP estimates.*
Source: CBB Monthly Statistical Bulletin.

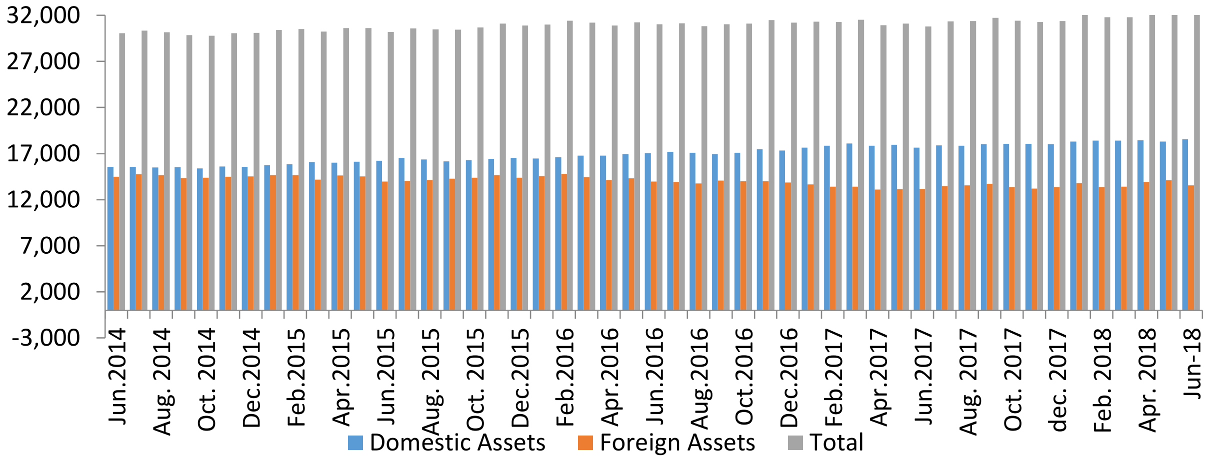
Despite the global uncertainty and the troubles in MENA region, retail banking total assets continued growing since December 2007 to reach BD 32.1 billion (USD 85.4 million) in June 2018 (see Chart 2-2).

Chart 2-2: Retail Banks' Assets (BD million)



Source: CBB Monthly Statistical Bulletin.

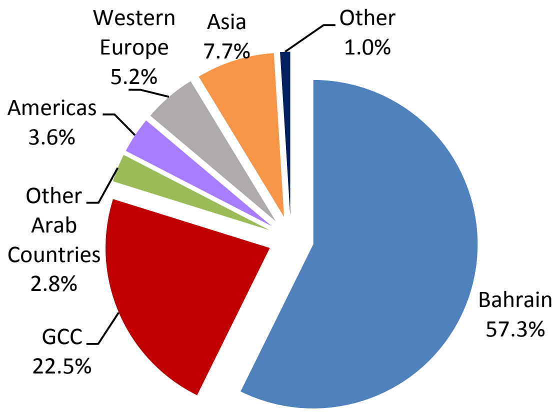
Chart 2-3: Categorization of Retail Banks' Assets (BD million)



Source: CBB Monthly Statistical Bulletin.

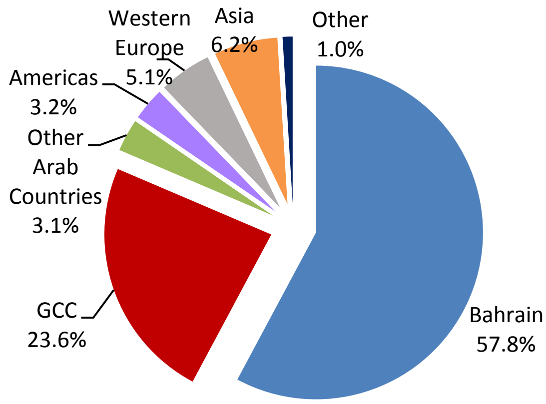
The share of GCC assets of total retail banking assets was 23.6%. The level of Europe and American contribution in retail banking showed a slight decline (8.3%). This shows that the retail-banking sector in Bahrain is relatively exposed to foreign risk from GCC countries and lightly exposed to foreign risk from Europe and U.S.

Chart 2-4: Retail Banks' Assets (%) by Geographical Classification (June2017)*



** For conventional and Islamic retail banks.*
Source: CBB Monthly Statistical Bulletin.

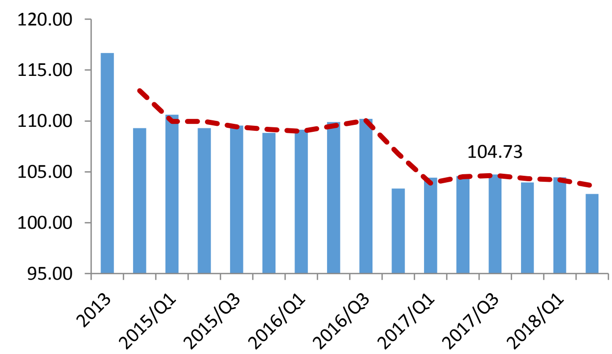
Chart 2-5: Retail Banks' Assets (%) by Geographical Classification (June 2018)*



** For conventional and Islamic retail banks.*
Source: CBB Monthly Statistical Bulletin.

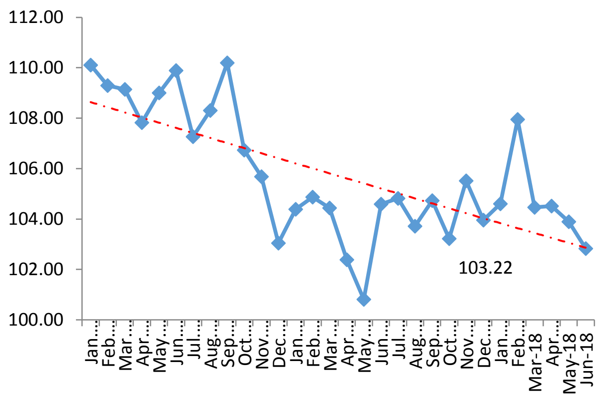
The wholesale banking sector declined from USD 104.6 billion by end of June 2017 to USD 102.8 in June 2018 (See Charts 2-6 and 2-7).

Chart 2-6: Wholsale Banks' Assets (USD Billion)*



--- Moving average trendline
** For conventional and Islamic wholesale banks.*
Source: CBB Monthly Statistical Bulletin.

Chart 2-7: Wholsale Banks' Assets(USD Billion)*

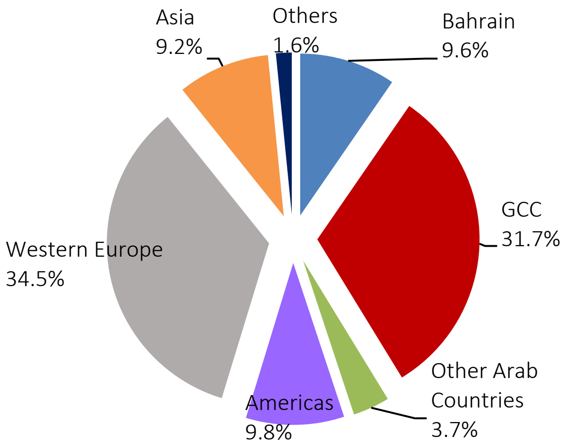


--- Linear Trendline
** For conventional and Islamic wholesale banks.*
Source: CBB Monthly Statistical Bulletin.

According to the geographical classification of wholesale banks' assets, wholesale banks are exposed to foreign risk from Western Europe and the GCC countries:

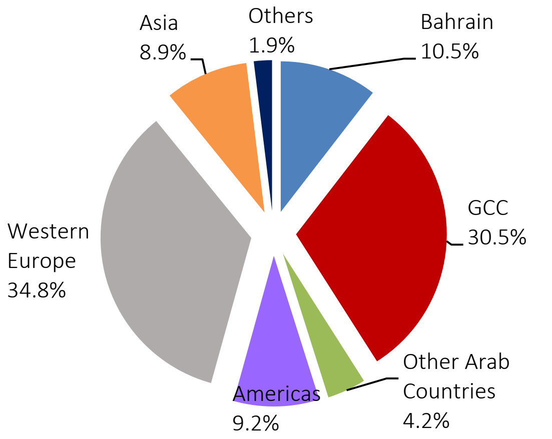
- The share of America's total assets decreased slightly to 9.2% in June 2018. This is lower than the total American asset's in June 2017.
- The share of Europe's total assets increased to 34.8%.
- Asian assets decreased from 9.2% to 8.9% in June 2018.
- GCC total assets continued to decrease to a low of 30.5% in June 2018, they represent a smaller portion of Wholesale bank assets now compared to Europe.

Chart 2-8: Wholesale Banks Assets by Geographical Classification (June 2017)*



** For conventional and Islamic retail banks.*
Source: CBB Monthly Statistical Bulletin.

Chart 2-9: Wholesale Banks Assets by Geographical Classification (June 2018)*

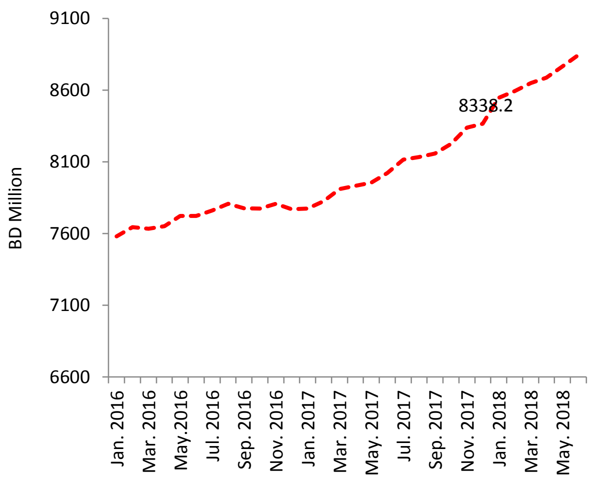


** For conventional and Islamic retail banks.*
Source: CBB Monthly Statistical Bulletin.

2.1.2 Credit Developments

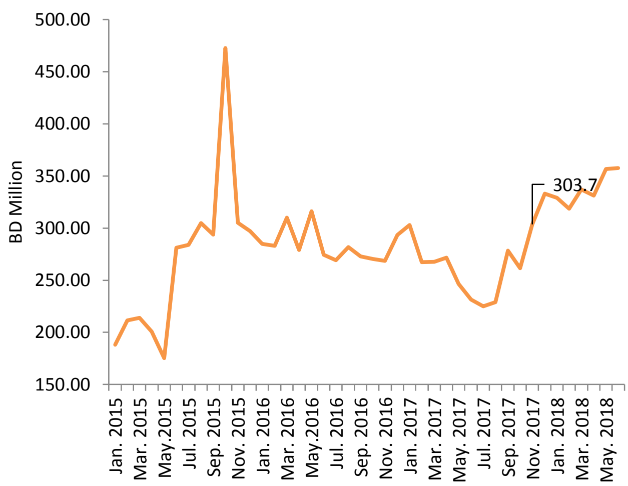
The total amount of credit given to the private sector (business and personal) by retail sector witnessed a considerable increase since June 2017 moving from BD 8,021.0 million to BD 8,844.6 million in June 2018 (Chart 2-11). The high credit growth reveals the growth of the economic activities and the restore of confidence in the Kingdom of Bahrain. Regarding retail banks' lending to the general government, there was an increase to BD 357.7 million at end-June 2018, from BD 231.5 million at end-June 2017.

Chart 2-10: Loans to the Private Sector (BD Million)*



Source: CBB Monthly Statistical Bulletin.
***Excluding securities.*

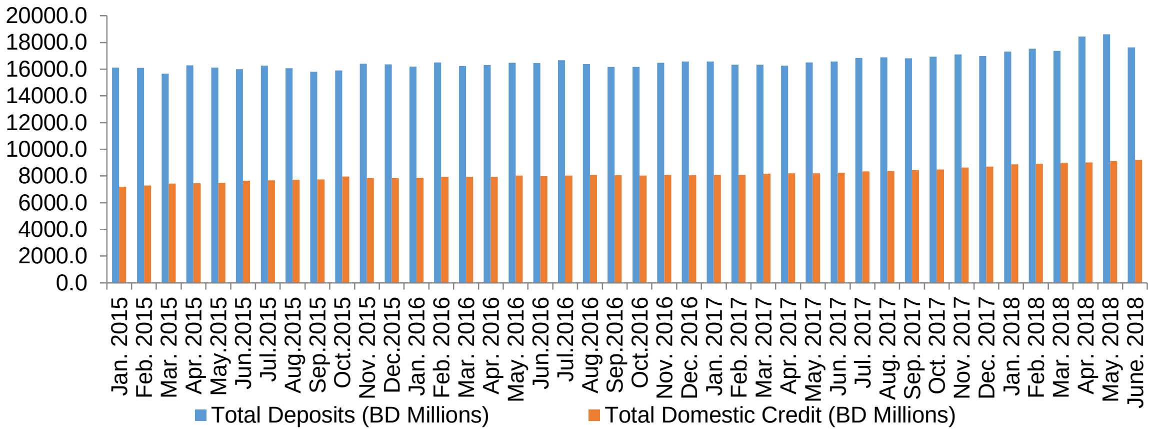
Chart 2-11: Loans to General Government (BD Million) *



Source: CBB Monthly Statistical Bulletin.
***Excluding securities.*

As for total deposits, they increased to BD 17,631.2 million in June 2018, where 67.0% of them were domestic deposits. This was parallel to the total domestic credits, which moved from BD 8,876.2 million at end-January 2018 to 9,202.3 in June 2018 (Chart 2-12).

Chart 2-12: Total Deposits and total Domestic Credit (BD Million)



Source: CBB Monthly Statistical Bulletin.

2.1.3 Net Foreign Assets

The net foreign asset (NFA) position of the banking system is the value of the assets that the banking system owns abroad (Foreign Assets) minus the value of the domestic assets owned by foreigners (Foreign Liabilities). A positive NFA balance means that the system is a net lender, while a negative NFA balance shows that it is a net borrower.

Looking at the NFA position by banking segment we will see that, as of June 2018, the position is negative for conventional banks (retail and wholesale) and Islamic retail banks (net borrowers), while it is positive for Islamic wholesale banks (net lenders). As of June 2018, the NFA position for retail banks was *negative* USD 3,348.2 million. For wholesale banks, the NFA position was also *negative* USD 417.6 million.

Table 2-2: Net Foreign Assets Postion by Banking Segment (June 2018)

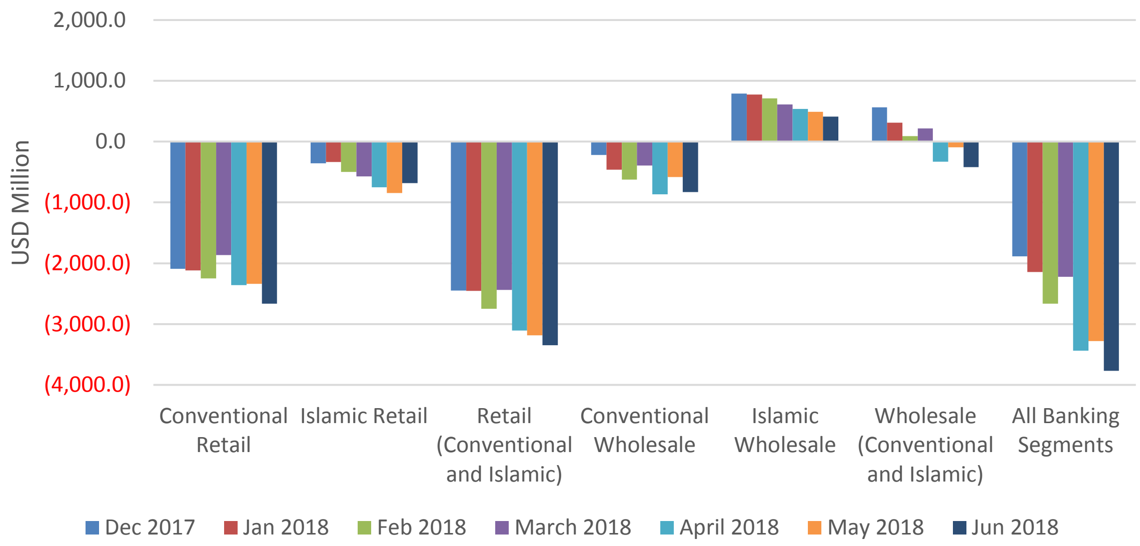
USD million

Banking Segment	Foreign Assets	Foreign Liabilities	Net Foreign Assets
Conventional Retail	33,340.9	36,006.6	(2,665.7)
Islamic Retail	2,669.1	3,351.6	(682.5)
Retail (Conventional and Islamic)	**36,010.0**	**39,358.2**	**(3,348.2)**
Conventional Wholesale	87,056.8	87,885.7	(828.9)
Islamic Wholesale	5,015.2	4,603.9	411.3
Wholesale (Conventional and Islamic)	**92,072.0**	**92,489.6**	**(417.6)**
Total Banking Segments	**128,082.0**	**131,847.8**	**(3,765.8)**

Source: CBB.

While the foreign assets for some banking segments have been increasing steadily with an upward trend, there is also an increase in foreign liabilities which leads to the increasing negative NFA position. The NFA for wholesale banks (Conventional and Islamic) turned negative in April 2018. Islamic Wholesale remains the only banking segment with positive NFA, yet the amount is decreasing.

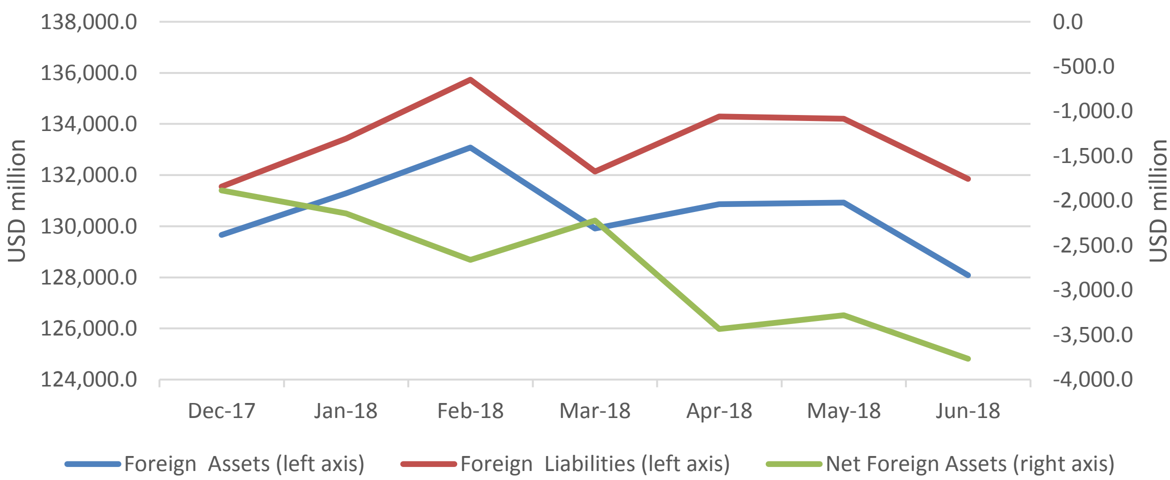
Chart 2-13: Net Foreign Assets Position by Banking Segment



Source: CBB.

Looking at the NFA position for the overall banking sector, data shows that there is a continuous downward trend as seen in the graph below. The NFA position of every banking segment is seen in the Box below.

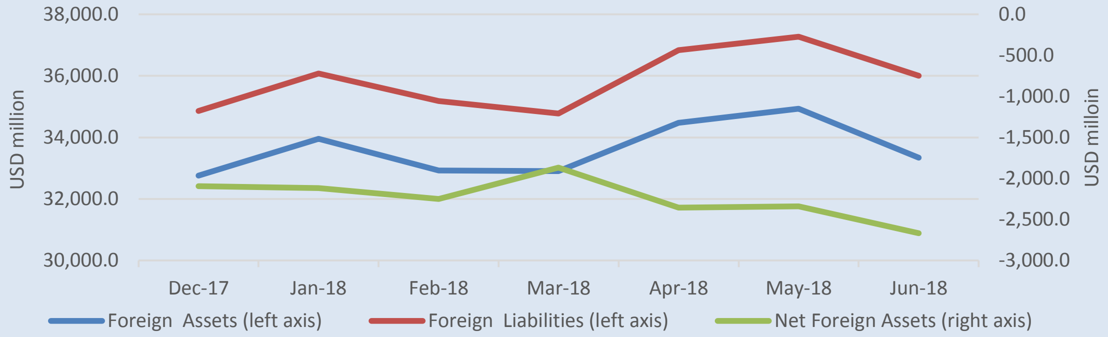
Chart 2-14: Net Foreign Assets of the Overall Banking Sector



Source: CBB.

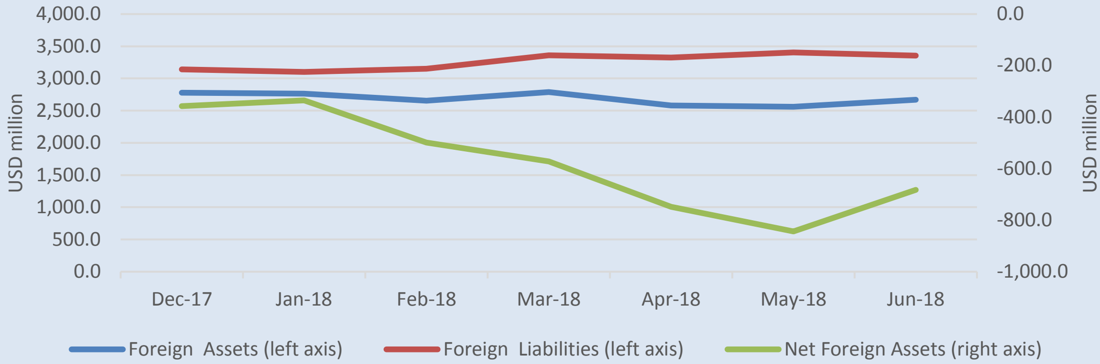
Box 1: Net Foreign Asset Charts by Banking Segment

Box 1 Cart 1: Conventional Retail's Net Foreign Assets



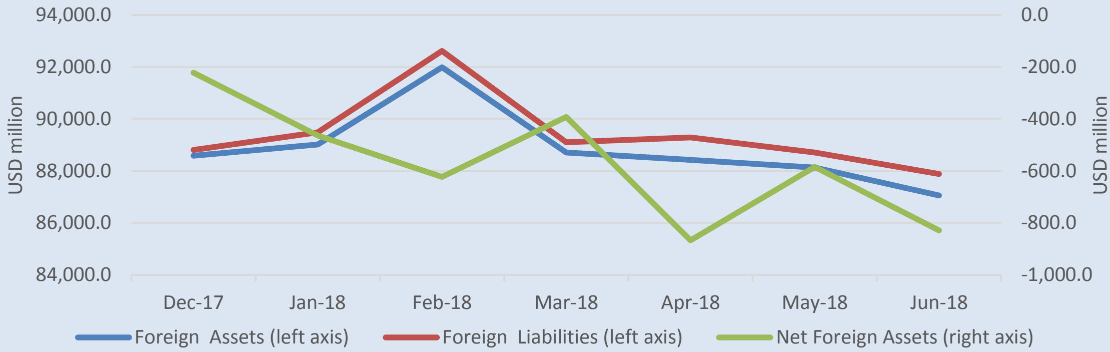
Source: CBB.

Box 1 Cart 2: Islamic Retail's Net Foreign Assets



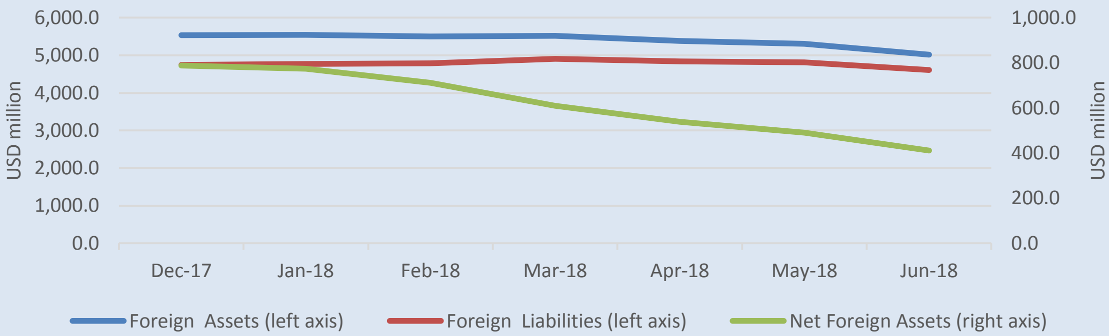
Source: CBB.

Box 1 Cart 3: Conventional Wholesale's Net Foreign Assets



Source: CBB.

Box 1 Cart 4: Islamic Wholesale's Net Foreign Assets

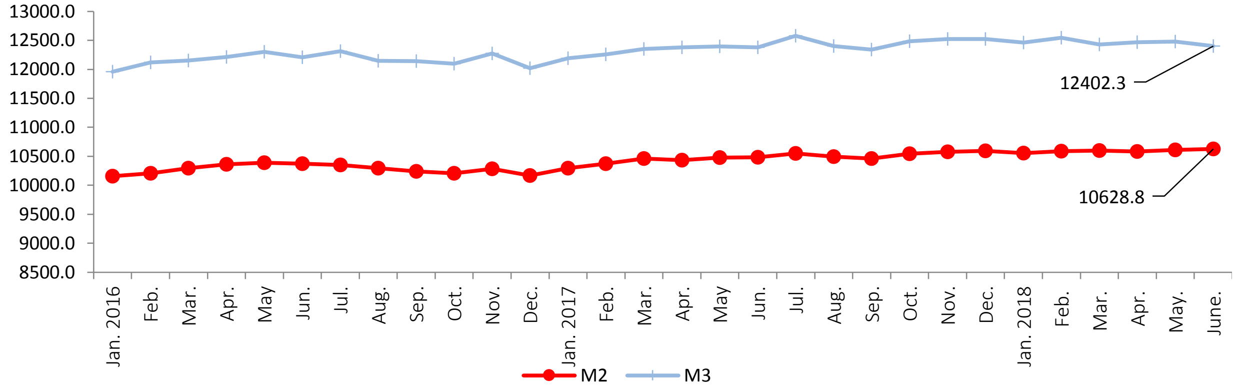


Source: CBB.

2.3 Monetary indictors

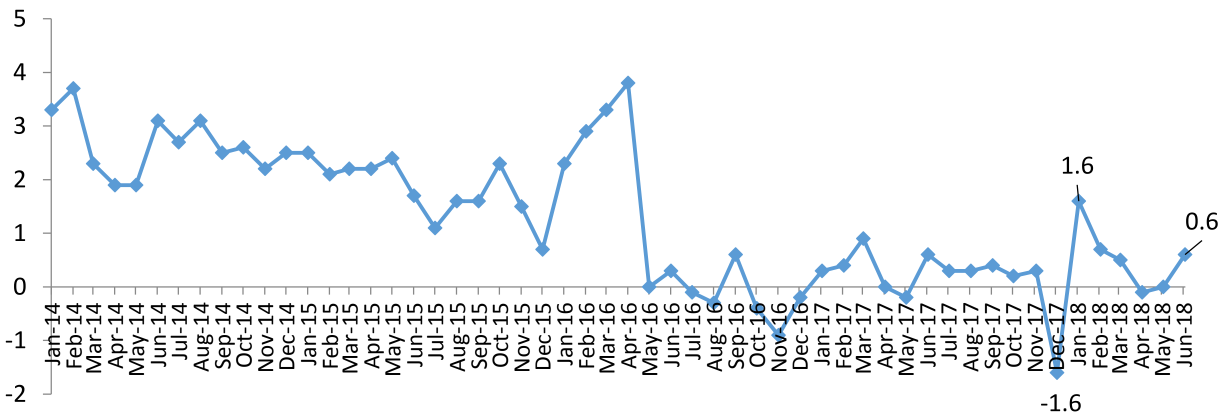
Money supply continued to grow. M2 stood at BD 10,628.8 million in end-June 2018, 0.5% higher than its value of November 2017. M3 was at BD 12,402.3 million in end-June 2018, 1.0% higher than in November 2017 (Chart 2-15).

Chart 2-15: Money Supply (BD Billion) from Jan. 2016 to June 2018



Source: CBB Monthly Statistical Bulletin.

Chart 2-16: Monthly Inflation in 2014-June 2018 (CPI%)*



**Growth rate compared to the same month of previous year, seasonally adjusted.*
Source: IGA.

Generally speaking, the inflation rate in consumer prices has always been relatively stable in Bahrain, not exceeding 4.0% since 2014. According to Information and E-Government Authority (IGA), inflation increased from 0.3% in November 2017 to 0.6% in June 2018. The largest increases came from the “food and non-alcoholic beverages”, and the “transportation” sectors.

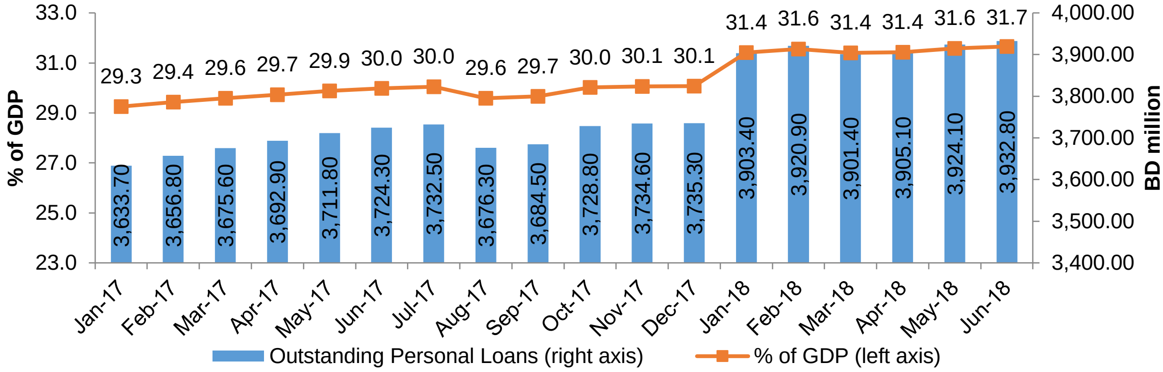
2.4 The Households Sector

The household sector in Bahrain plays an important role in financial stability and the overall economy. The household sector can allocate funds to financial assets through bank deposits and securities, and to non-financial assets from land and other fixed assets. It can also receive funds from financial and non-financial institutions. The construction and real estate sector plays a huge importance on economic developments and is a good indicator of macroeconomic conditions in the country.

2.4.1 Household Debt Ratio

Outstanding personal loans, used as a proxy for household borrowing, for the period shows that the household debt saw an increase throughout the period between January 2017 and June 2018 (Chart 2-17).

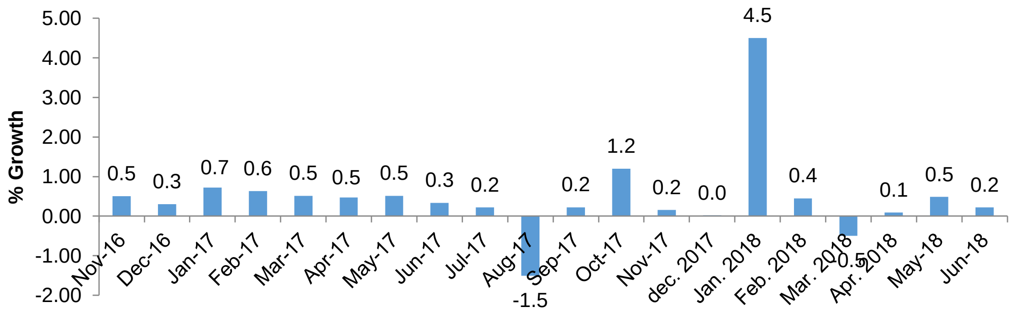
Chart 2-17: Personal Loans and Advances (Volume and % of GDP)



**Using 2017 GDP (Provisional data).*
Source: CBB Monthly Statistical Bulletin.

Personal loans as a percentage of GDP remained fairly stable from January 2017 to June 2018. Starting at 29.3% (BD 3,633.7 millIon) in January 2017 the personal loans as a percentage of GDP increased to 31.7% in June 2018 (BD 3,932.8 millIon). There was a 5.3% increase in outstanding personal loans between November 2017 and June 2018.

Chart 2-18: Growth Rate of Total Personal Loans and Advances (%)



Source: CBB Monthly Statistical Bulletin.

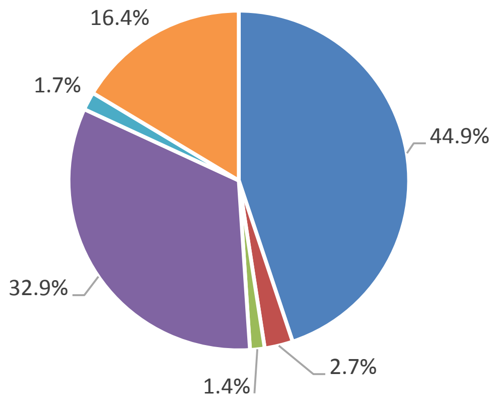
The growth rate in total personal loans saw a decrease between Feburary 2018 and June 2018, rising from 0.4% to 0.2% respectively. The highest growth rate was in personal loans of 4.5% in Janaury 2018 since November 2016. The two main contributors to personal loans as seen in chart 2-19 were personal loans secured by property mortgages which makes up 44.9% of the total personal loans followed by personal loans secured with salary assignments at 32.9% of total personal loans as of end of June 2018.

Table 2-3: Personal Loans Breakdown

BD million	Nov. 2017-June 2018							
	Nov.	Dec.	Jan.	Feb.	Mar.	Apr.	May	June
Total	3,734.6	3,735.3	3,903.4	3,920.9	3,901.4	3,905.1	3,924.1	3,932.8
Secured by Property Mortgage	1,602.4	1,613.6	1,769.6	1,783.9	1,768.7	1,750.5	1,757.8	1,764.9
Secured by Vehicle Title	116.4	114.9	111.2	109.2	108	107.3	105.2	105.7
Secured by Deposits	55.9	52.9	57.5	52.2	53.5	51.4	55.0	54.5
With Salary Assignment	1,281.7	1,278.3	1,290.1	1,288.2	1,295.9	1,305.5	1,307.8	1,295.6
Credit Card Receivables	86.1	86.1	86.4	85.6	82.9	85.9	65.1	67.8
Other	592.1	589.5	588.6	601.8	592.4	604.5	633.2	644.3

Source: CBB Monthly Statistical Bulletin.

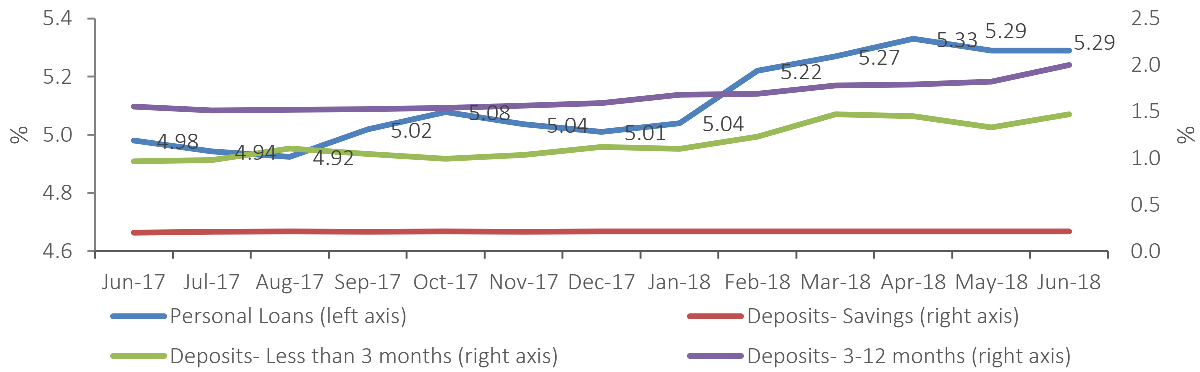
Chart 2-19: Personal Loans Breakdown (June 2018)



Source: CBB Monthly Statistical Bulletin.

Interest rates on personal loans started off at 4.98% in June 2017 and then increased to 5.29% in June 2018 (Chart 2-20). The chart also shows the retail deposit rate for: Saving deposits, time deposits less than 3 months, and time deposits 3 months to 12 months over the same period.

Chart 2-20: Retail Banks- Average Interest Rates on Personal Loans and Interest rates on Deposits (%)

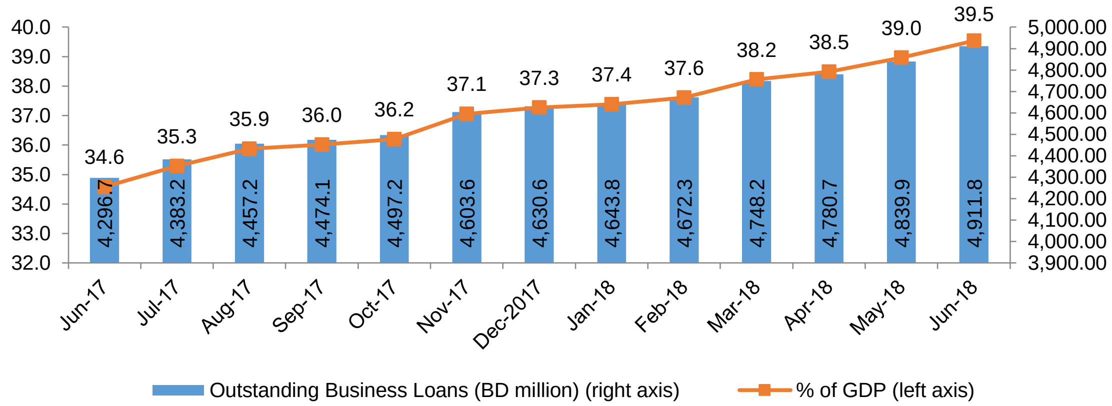


Source: CBB Monthly Statistical Bulletin.

2.4.2 The Bahraini Corporate Sector

Business loans and advances grew between November 2017 and June 2018 from BD 4,603.6 million in November 2017 to BD 4,911.8 million in June 2018 (Chart 2-21). Outstanding business loans as a percentage of GDP increased by 2.4% during this period, ending at 39.5% in June 2018.

Chart 2-21: Business Loans and Advances (Volume and % of GDP)



Source: CBB Monthly Statistical Bulletin.

For the past seven months, the main contributor to the increase in business loans was the loans to the construction and real estate sector. The biggest contributors to business loans in June 2018 are the 'construction and real estate sector' (36.2%) followed by 'trade' (23.4%) and then 'other sectors' (17.6%) (Chart 2-22).

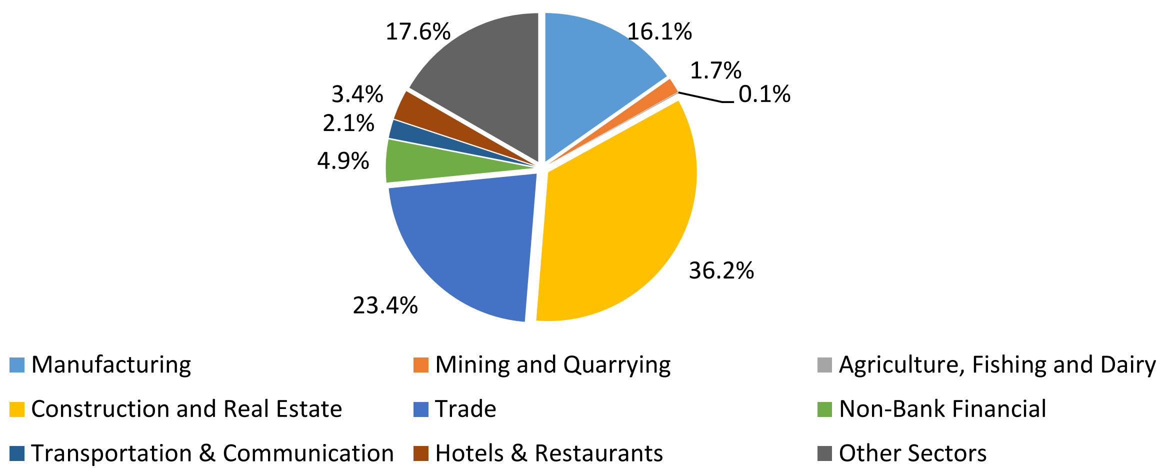
Table 2-4: Business Loans by Sector

Sectors	Nov. 2017-June 2018							
	Nov	Dec	Jan	Feb	Mar	Apr	May	June
Total	**4,603.6**	**4,630.6**	**4,643.8**	**4,672.3**	**4,748.2**	**4,780.7**	**4,839.9**	**4,911.8**
Manufacturing	695.1	717.8	732.5	747.6	778.5	778.9	805.4	790.1
Mining and Quarrying	50.2	59.7	62.2	79.9	74.1	69.4	71.9	85.3
Agriculture, Fishing and Dairy	7.4	8.1	7.8	7.4	7.1	6.5	5.5	5.3
Construction and Real Estate	1,631.7	1,698.3	1,697.7	1,686.6	1,712.0	1,741.3	1,759.1	1,777.0
Trade	1,151.0	1,125.4	1,145.4	1,141.7	1,147.4	1,149.2	1,152.3	1,148.1
Non-Bank Financial	217.8	222.2	211.0	202.4	208.9	210.9	214.1	241.2
Transportation & Communication	121.1	97.2	100.5	99.9	100.2	105.2	104.1	103.4
Hotels & Restaurants	170.6	172.4	170.5	174.0	168.2	168.7	170.3	167.8
Other Sectors	850.4	799.1	787.2	806.7	820.2	824.5	831.6	864.8

Source: CBB Monthly Statistical Bulletin.

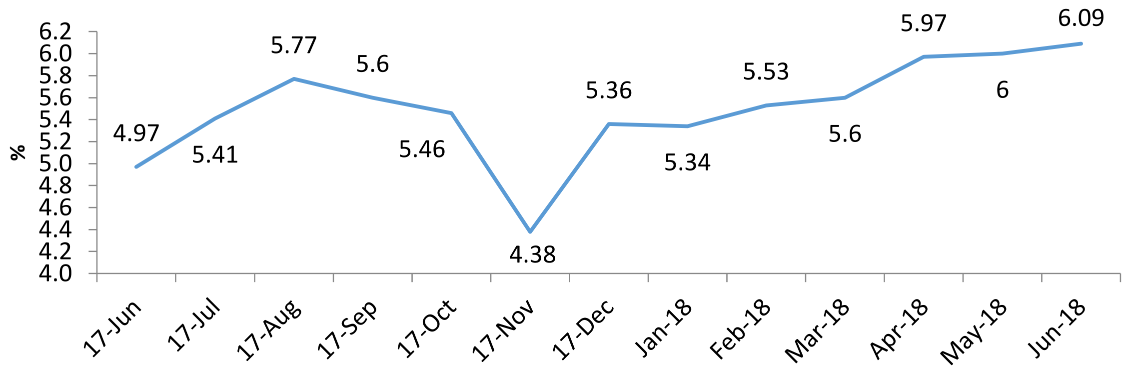
Average interest rates on business loans fluctuated throughout the period. It was at its peak in June 2018 at 6.09%, and at its lowest in November at 4.38% (Chart 2-22).

Chart 2-22: Business Loans by Sector June 2018



Source: CBB Monthly Statistical Bulletin.

Chart 2-23: Retail Banks' Average Interest Rates on Business Loans (%)



Source: CBB Monthly Statistical Bulletin.

2.4.3 Construction and Real Estate

The total number of construction permits issued by the Ministry of Municipality & Agricultural Affairs has seen a decrease from Q1 2017 to Q2 2018, with a total of 1,968 and 1,533 permits issues respectively.

Table 2-5: Selected Construction Permits by Type

	2017:Q1	2017:Q2	2017:Q3	2017:Q4	2018:Q1	2018:Q2
Renovation	168	122	109	129	162	170
Reclamation	8	3	3	7	1	7
New Construction	900	705	633	640	613	733
Demolition and New Construction	9	5	6	6	10	7
Demolition	136	130	93	105	116	97
Addition	747	618	516	477	566	519
Total	**1,968**	**1,583**	**1,360**	**1,364**	**1,468**	**1,533**

Sources: Ministry of Municipality Affairs and Agriculture.

2.5 Overall assessment of the Bahraini Financial sector and non-Financial Sector.

Bahrain's financial sector was influential in fostering economic growth and creating employment opportunities. Bank loans continued their growth with mortgage loans growing steadily. Overall funding conditions have improved and demand for loans has accelerated in Bahrain. Banks operating in Bahrain are well capitalized, funding and liquidity buffers are well above minimum required standards, and non-performing loans continue to drop. Regulatory changes in recent years have helped to improve prudential standards for retail and wholesale banks (conventional and Islamic). All these changes have been beneficial for financial stability and will further strengthen the position of Bahrain as a financial center.

Part II:

Performance of the Banking Sector

3. Overall Banking Sector

Chapter

3

Key Points

- A decline in capital positions.
- Non-performing loans (NPL's) decreased slightly.
- Loan portfolios remain concentrated in some sectors despite the decrease in some sectors, but no significant change from previous quarter
- Stable positive earnings for banks.
- Liquidity position remains resilient.

3.1 Overview

In this chapter, the performance of the banking sector in the Kingdom of Bahrain is analysed and assessed. This chapter offers macro prudential analysis of the entire banking sector based on a set of selected Financial Soundness Indicators (FSIs).[2] The banking sector in Bahrain is divided into four segments: conventional retail (CR), conventional wholesale (CW), Islamic Retail (IR), and Islamic wholesale (IW). The performance of each banking segment will be analysed in Chapters 4 and 5.

Annex 1 presents selected FSIs for the different banking segments. Annex 2 presents selected graphs showing the development of selected indicators over time.

Unless indicated otherwise, Chapter 3, 4, and 5 of the report analyzes data covering the period between end-September 2017 and end-March 2018.

3.2 Overall Banking Sector Performance

Decrease in Capital Adequacy Ratio [3]

The Capital adequacy ratio (CAR) for the banking sector stood at 18.8% in March 2018. The ratio has decreased from 19.4% in September 2017. The core capital ratio (ratio of Tier 1 capital to risk-weighted assets) showed a decrease from 18.1% in September 2017 to 17.4% in March 2018. Whereas the leverage ratio (ratio of assets over capital) remained the same at 6.9% during the same period.

[2] This chapter does not contain a section on stress testing. Stress Testing exercises are performed separately in an internal report to obtain information on the potential quantitative impact of hypothetical scenarios on selected Bahraini Domestically Systemically-Important Banks (DSIB's).

[3] The capital adequacy ratio relates total capital to risk-weighted assets (RWA). The discussion excludes overseas retail banks, which do not have prescribed capital levels or ratios.

Table 3-1 Capital Provision Ratios *

Indicator	Sep. 2017	Mar. 2018
CAR (%)	19.4	18.8
Tier 1 CAR (%)	18.1	17.4
Leverage (Assets/Capital) (Times)	6.9	6.9

** For Locally Incorporated Banks only.*

Source: CBB.

Decrease in NPL's

The Non-performing loans (NPL) ratio has been flat remaining within the same range. The NPL ratio decreased from 5.7% in September 2017 to 5.5% in March 2018. The specific provisions as a proportion of NPL's showed decrease to 52.1% in March 2018 from 57.0% in September 2017.

Table 3-2: NPL Ratios

Indicator	Sep. 2017	Mar. 2018
NPL's (% Total Loans)	5.7	5.5
Specific provisions (% of NPL's) *	57.0	52.1

** Specific provisions as a percentage of NPL's are calculated as specific provisions divided by gross impaired loans.*

Source: CBB.

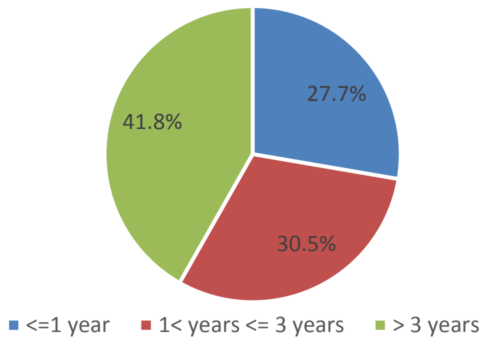
Data on NPL's by time segment (up to 1 year, 1 year to 3 years, and over 3 years) shows that the majority of NPL's in the banking sector are for over 3 years (41.8% of total of total NPL's). NPL's for over 3 years represented 2.3% of total gross loans. NPL's that are non-performing for up to 3 years represented 58.2% of total of total NPL's. Specific provisioning for NPL's increases as they are non-performing for longer periods of time. As seen in Table 3-3, NPL's for a period for more than 3 years are provisioned by 63.4%.

Table 3-3: NPL Ratios and Specific Provisions by Time Period

	Up to 1 year	1 up to 3 years	Over 3 years	Total
NPL's (% Total Loans)	1.5	1.7	2.3	5.5
Specific Provisions (% of NPL's)	39.1	50.8	63.4	52.1

Source: CBB.

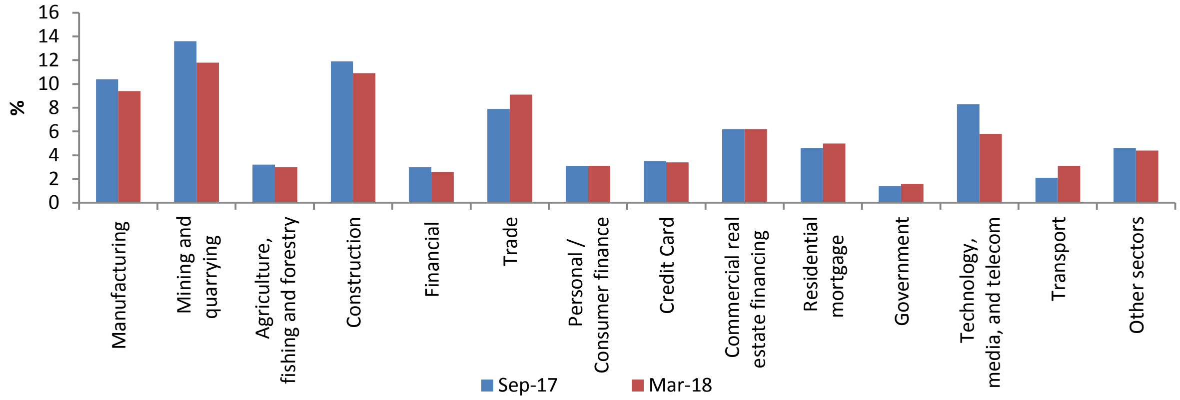
Chart 3-1: NPL's by Time Period



Source: CBB.

Data on the sectoral breakdown of NPL's as a percentage loans in each sector shows some sectors experiencing an increase in impairment, while some experience a decrease and others remaining unchanged (Table 3-4 and Chart 3-2). The overall changes though have been very minimal. The highest increase was in "Trade" by 1.2% followed by "Transport" by 1.0%. The highest decrease was in "Technology, media and telecommunications" by 2.5%.

Chart 3-2: NPL Ratios by Sectors (%)



Source: CBB.

Table 3-4: NPL Ratios by Sector (%)

	Sep. 2017	Mar. 2018	Change
Manufacturing	10.4	9.4	(1.0)
Mining and quarrying	13.6	11.8	(1.8)
Agriculture, fishing and forestry	3.2	3.0	(0.2)
Construction	11.9	10.9	(1.0)
Financial	3.0	2.6	(0.4)
Trade	7.9	9.1	1.2
Personal / Consumer finance	3.1	3.1	0
Credit Card	3.5	3.4	(0.1)
Commercial real estate financing	6.2	6.2	0
Residential mortgage	4.6	5.0	0.4
Government	1.4	1.6	0.2
Technology, media and telecommunications	8.3	5.8	(2.5)
Transport	2.1	3.1	1
Other sectors	4.6	4.3	(0.3)

Source: CBB.

Loan portfolios unchanged and concentrated in some sectors

The loan portfolio of *the banking system* remains concentrated in four sectors with no major change in the exposure to the sectors with no sector exceeding a 20% exposure. "Other Sectors"[4] represented the maximum exposure with 15.1% of total loans in March 2018, an increase from the 13.6% in September 2017. "Manufacturing" was close behind, with 15.0% exposure in March 2018.

[4] The "other sectors" category includes sectors such as "private banking", "services", "tourism", and "utilities".

Table 3-5: Lending Distribution (% Total Loans)*

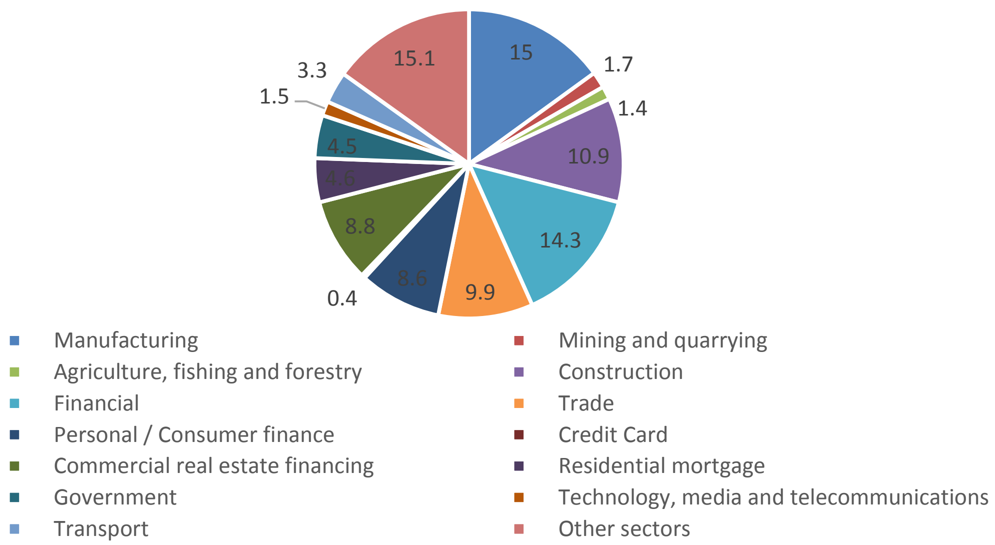
	Sep. 2017	Mar. 2018	Change
Manufacturing	15.4	15.0	(0.4)
Mining and quarrying	1.6	1.7	0.1
Agriculture, fishing and forestry	1.6	1.4	(0.2)
Construction	10.5	10.9	0.4
Financial	14.0	14.3	0.3
Trade	10.4	9.9	(0.5)
Personal / Consumer finance	8.3	8.6	0.3
Credit Card	0.3	0.4	0.1
Commercial real estate financing	9.0	8.8	(0.2)
Residential mortgage	4.1	4.6	0.5
Government	4.7	4.5	(0.2)
Technology, media and telecommunications	1.5	1.5	0
Transport	4.9	3.3	(1.6)
Other sectors	13.6	15.1	1.5
Top Two Sectors (%)	**29.4**	**30.0**	**0.6**
Real Estate/ Construction Exposure (%) **	**23.6**	**24.3**	**0.7**

** Figures may not add to a hundred due to rounding.*
*** Real Estate/Construction exposure is calculated as the share of the construction, commercial real estate financing, and residential mortgages sectors of total lending.*
Source: CBB.

The "Financial" sector represented 14.3% of total loans up from 14.0% in September 2017. "Personal/Consumer Finance as percentage of total finance" increased slightly from 8.3% in September 2017 to 8.6% in March 2018.

The top two recipient sectors "Manufacturing" and "Other" jointly represented 30.0% of loans in March 2018, increasing from 29.4% in September 2017. Exposure to real estate/ construction was 24.3% of total lending in March 2018, an increase from 23.6% registered in September 2017.

Chart 3-3: Lending Distribution (% Total loans)



Source: CBB.

Profitability remains stable

The overall banking sector's profitability indicators have been positive and constant from March 2017 to March 2018 and remain robust. As of end-March 2018, return-on-assets (ROA) was unchanged from 0.3% in March 2017. Return-on-equity (ROE) increased from 2.1% in March 2017 to 2.5% in March 2018. Net interest income (as a % of total income) stood at 55.0% in March 2018, a decrease from 58.5% in March 2017. In addition, operating expenses as a proportion of total income was 57.5% in March 2018, a decrease from the 65.0% registered in March 2017.

Table 3-6: Profitability

	Mar. 2017	Mar. 2018
ROA (%)*	0.3	0.3
ROE (%) **	2.1	2.5
Net Interest Income (% Total Income)***	58.5	55.0
Operating Expenses (% Total Income)	65.0	57.5

** ROA = ratio of net income to assets.*

*** ROE = ratio of net profit to tier 1 capital (for Locally Incorporated Banks only).*

**** Net interest income only for Conventional Banks.*

Source: CBB.

Liquidity position stays resilient

Between September 2017 and March 2018, the overall loan-deposit ratio increased from 67.9% in September 2017 to 72.7% in March 2018. Liquid assets as a proportion of total assets slightly decreased to reach 25.5%, over the same period.

Table 3-7: Liquidity

	Sep. 2017	Mar. 2018
Liquid Asset Ratio (%)	25.7	25.5
Loan-Deposit Ratio (%)	67.9	72.7

Source: CBB.

3.3 Overall Assessment of the Banking Sector

The financial soundness indicators show that the Banking Sector witnessed a decrease in capital adequacy ratio. Capital adequacy ratios for the banking sector decreased from 19.4% in September 2017 to 18.8% in March 2018. NPL’s have shown a slight decrease between the periods of September 2017 to March 2018, from 5.7% to 5.5%, yet remain stable within the same range. Profitability has remained constant with ROA being at 1.3% and ROE at 5.7%. Liquidity has stood at the same level between September 2017 and March 2018.

In the following two chapters (chapters 4 and 5) of the FSR, the FSIs of the four banking sectors (Conventional Retail, Conventional Wholesale, Islamic Retail, and Islamic Wholesale) are analysed to assess the performance of the sectors in the banking system in Bahrain.

4. Conventional Banks

Chapter 4

Key Points

- A decrease in capital positions of conventional banks.
- Non-performing loans (NPL's) for conventional retails banks increased slightly, while NPL's for conventional wholesale banks decreased.
- Loan portfolios in conventional retail and wholesale banks remain concentrated despite the decrease in some sectors.
- Increases in earnings for conventional retail banks
- Slight increases in liquidity for conventional wholesale banks and decreases for conventional retail banks.

4.1 Overview

This chapter analyses the banking sector under the following categories: conventional retail banks (section 4.2), conventional wholesale banks (section 4.3). Section 4.4 provides an overall assessment of the conventional banking industry. Unless specified otherwise, the analysis in this chapter is based on consolidated financial data (Bahraini and non-Bahraini operations), as at end-September 2017 and compared with end-March 2018.

This chapter offers macroprudential analysis of the conventional banking sector based on a set of selected Financial Soundness Indicators (FSIs).[5]

4.2 Conventional Retail Banks

Decrease in capital adequacy [6]

The CAR for conventional retail decreased from 20.4% in September 2017 to 19.6% in March 2018. The core capital ratio (ratio of Tier 1 capital to risk-weighted assets) showed a decrease from 18.8% in September 2017 to 18.1% in March 2018, whereas the leverage ratio (ratio of assets over capital) increased to 6.7% during the same period. The ratio of non-performing loans (NPL's) net provisions to capital increased to reach 7.0% in March 2018 from 6.6% in September 2017.

[5] This chapter does not contain a section on stress testing. Stress Testing exercises are performed separately in an internal report to obtain information on the potential quantitative impact of hypothetical scenarios on selected Bahraini Domestically Systemically-Important Banks (SIB's).

[6] The capital adequacy ratio relates total capital to risk-weighted assets (RWA). The discussion excludes overseas retail banks, which do not have prescribed capital levels or ratios.

Table 4-1: Local CR Banks' Capital Provisions Ratios *

Indicator	Sep. 2017	Mar. 2018
CAR (%)	20.4	19.6
Tier 1 CAR (%)	18.8	18.1
Leverage (assets/capital)(times)	6.5	6.7
NPL's net of provisions to capital (%)	6.6	7.0

** For Locally Incorporated Banks only.*

Source: CBB.

Non-performing loans remain stable

NPL ratio showed a slight increase to 5.9% in March 2018 from 5.8% in September 2017. The specific provisions as a proportion of NPL's showed a decrease to 47.8% in March 2018 from 49.5% in September 2017. For *local retail banks*, the NPL's slightly decreased to 4.2% in March 2018. For *overseas retail banks*, the NPL's increased from 8.5% in September 2017 to 9.4% in March 2018.

Table 4-2: CR Banks' NPL Ratios

Indicator	Sep. 2017	Mar. 2018
NPL's (% Total Loans)	5.8	5.9
NPL's Local Banks (%)	4.5	4.2
NPL's Overseas Banks (%)	8.5	9.4
Specific Provisions (% of NPL's) *	49.5	47.8

** Specific provisions as a percentage of NPL's are calculated as specific provisions divided by gross impaired loans.*

Source: CBB.

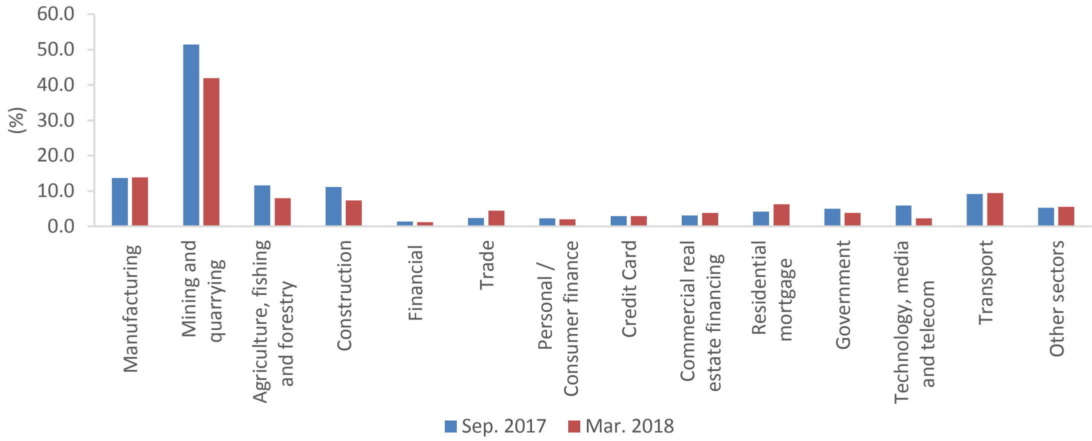
Available data on the sectoral breakdown of NPL's shows some sectors experiencing an increase in impairment, while some experience a decrease (Table 4-3 and Chart 4-1). The highest increase was in "Trade" by 2.1%, and the highest decrease was in "Mining and Quarrying" by 9.5%.

Table 4-3: CR Bank's NPL Ratios by Sector (%)

	Sep. 2017	Mar. 2018	Change
Manufacturing	13.7	13.8	0.1
Mining and quarrying	51.4	41.9	(9.5)
Agriculture, fishing and forestry	11.6	7.9	(3.7)
Construction	11.2	7.4	(3.8)
Financial	1.4	1.2	(0.2)
Trade	2.4	4.5	2.1
Personal / Consumer finance	2.3	2.0	(0.3)
Credit Card	2.9	2.9	0.0
Commercial real estate financing	3.1	3.8	0.7
Residential mortgage	4.2	6.2	2.0
Government	5.0	3.8	(1.2)
Technology, media and telecommunications	5.9	2.3	(3.6)
Transport	9.1	9.5	0.4
Other sectors	5.2	5.5	0.3

Source: CBB.

Chart 4-1: CR Banks' NPL Ratios by Sector (%)



Source: CBB.

Loan portfolios remain concentrated

The loan portfolio of *retail banks* remains concentrated with fairly small, if any, changes in the composition of the loans. The top recipient of loans remains to be the "Commercial real estate financing" sector accounting for 18.4% of total loans in March 2018, compared with 19.0% in September 2017. The "Personal/Consumer finance" sector represented 12.7% of total loans and the "Manufacturing" sector represented 13.6%. The "Others" sector decreased by 0.8% from 16.2% in September 2017 to 15.4% in March 2018.

Table 4-4: CR Bank's Lending Distribution by Sector (% Total Loans)*

	Sep. 2017	Mar. 2018	Change
Manufacturing	14.9	13.6	(1.3)
Mining and quarrying	0.9	1.1	0.2
Agriculture, fishing and forestry	0.2	0.2	0.0
Construction	4.2	4.0	(0.2)
Financial	7.5	9.5	2.0
Trade	10.2	10.0	(0.2)
Personal / Consumer finance	12.6	12.7	0.1
Credit Card	0.7	0.7	0.0
Commercial real estate financing	19.0	18.4	(0.6)
Residential mortgage	7.5	8.2	0.7
Government	1.9	2.5	0.6
Technology, media and telecommunications	2.3	1.9	(0.4)
Transport	1.7	1.7	0.0
Other sectors	16.2	15.4	(0.8)
Top Two Sectors (%)	**35.2**	**33.8**	**(1.4)**
Real Estate/ Construction Exposure (%) **	**30.7**	**30.7**	**0.0**

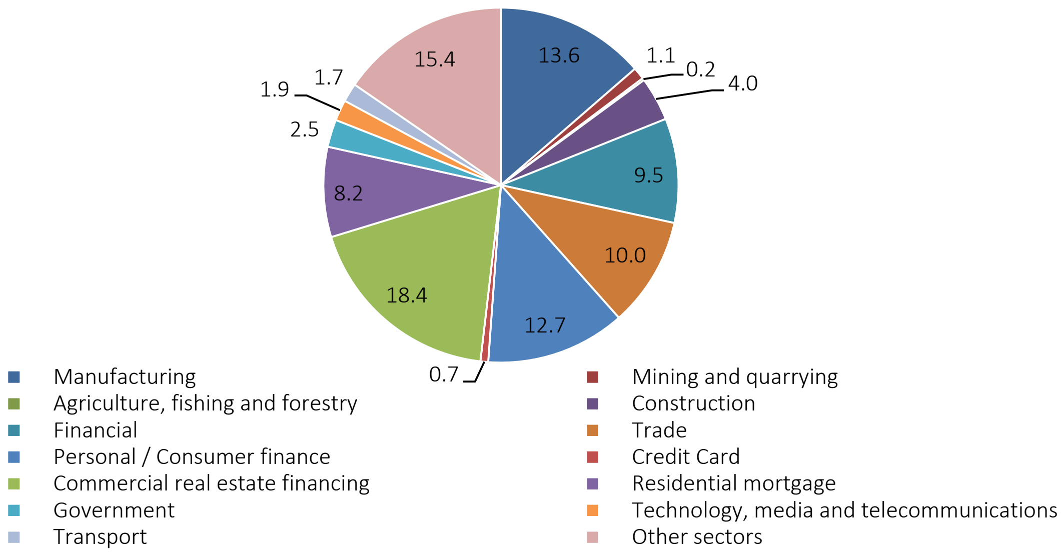
** Figures may not add to a hundred due to rounding.*

*** Real Estate/Construction exposure is calculated as the share of the construction, commercial real estate financing, and residential mortgages sectors of total lending.*

Source: CBB.

The top two recipient sectors, "Commercial real estate financing" and "Other sectors," jointly represented 33.8% of loans in March 2018. Exposure to real estate/construction was unchanged at 30.7% of total lending in March 2018.

Chart 4-2: CR Banks' Lending Distribution by Sector (% Total Loans)



Source: CBB.

The loan portfolio of *locally incorporated retail banks* remains concentrated with the top recipient of loans being the "Commercial real estate financing" sector accounting for 18.8% of total loans in March 2018, a decrease from 19.9% in September 2017. The "Others" [7] sector represented 13.8% of total loans, down from 15.1%, while the "Manufacturing" sector also represented 13.8% of total loans over the same period, a decrease from 14.3%. The top two recipient sectors "Commercial real estate financing" and "Manufacturing" jointly represented 32.6% of loans in March 2018 a decrease from the 35.0% in September 2017. Exposure to real estate/construction was 34.8% of total lending in March 2018, a slight decrease from the 35.2% registered in September 2017.

[7] The "others sectors" category includes sectors such as "private banking", "services", "tourism", and "utilities".

Table 4-5: Local CR Bank's Lending Distribution by Sector (% Total Loans)

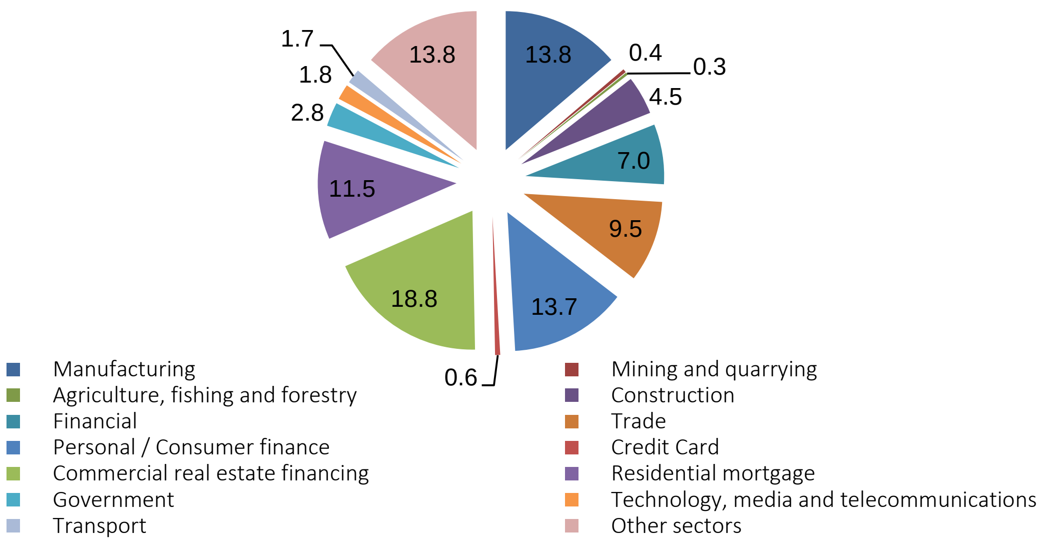
	Sep. 2017	Mar. 2018	Change
Manufacturing	14.3	13.8	(0.5)
Mining and quarrying	0.1	0.4	0.3
Agriculture, fishing and forestry	0.2	0.3	0.1
Construction	4.8	4.5	(0.3)
Financial	5.9	7.0	1.1
Trade	9.5	9.5	0.0
Personal / Consumer finance	13.6	13.7	0.1
Credit Card	0.6	0.6	0.0
Commercial real estate financing	19.9	18.8	(1.1)
Residential mortgage	10.5	11.5	1.0
Government	2.1	2.8	0.7
Technology, media and telecommunications	2.1	1.8	(0.3)
Transport	1.4	1.7	0.3
Other sectors	15.1	13.8	(1.3)
Top Two Sectors (%)	**35.0**	**32.6**	**(2.4)**
Real Estate/ Construction Exposure (%) **	**35.2**	**34.8**	**(0.4)**

** Figures may not add to a hundred due to rounding.*

*** Real Estate/Construction exposure is calculated as the share of the construction, commercial real estate financing, and residential mortgages sectors of total lending.*

Source: CBB.

Chart 4-3: Local CR Bank's Lending Distribution by Sector (% Total Loans)



Source: CBB.

The numbers as of end-March 2018 continue to show high concentration of risk for *overseas retail banks* (Table 4-6 and Chart 4-4). The top recipient of loans, excluding the "Others" sector, was the "Commercial Real Estate Financing" sector with 17.7% of total loans in March 2018, an increase from the 17.2% in March 2017.

Table 4-6: Overseas CR Bank's Lending Distribution by Sector (% Total Loans)

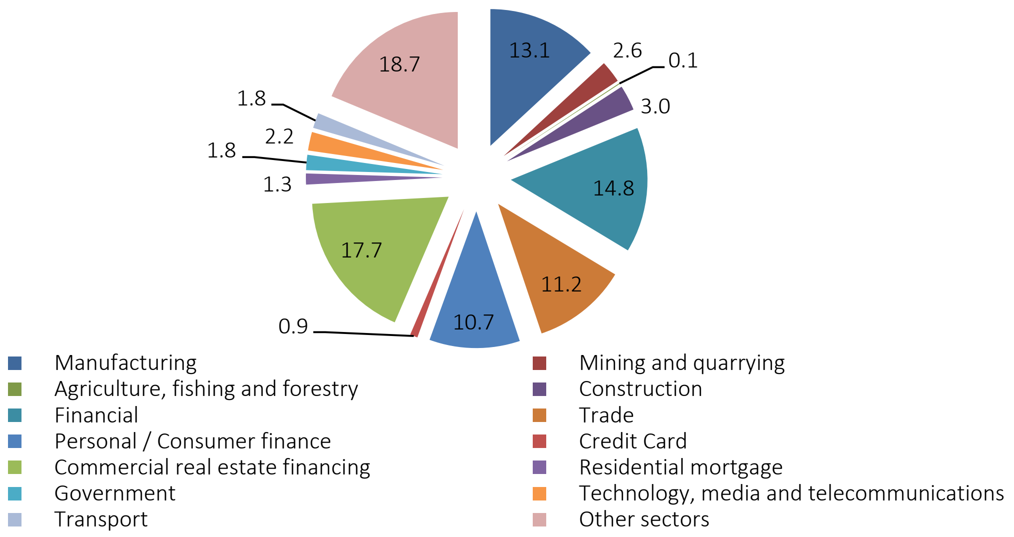
	Sep. 2017	Mar. 2018	Change
Manufacturing	16.4	13.1	(3.3)
Mining and quarrying	2.7	2.6	(0.1)
Agriculture, fishing and forestry	0.0	0.1	0.1
Construction	3.1	3.0	(0.1)
Financial	10.7	14.8	4.1
Trade	11.7	11.2	(0.5)
Personal / Consumer finance	10.7	10.7	0.0
Credit Card	0.9	0.9	0.0
Commercial real estate financing	17.2	17.7	0.5
Residential mortgage	1.3	1.3	0.0
Government	1.7	1.8	0.1
Technology, media and telecommunications	2.7	2.2	(0.5)
Transport	2.4	1.8	(0.6)
Other sectors	18.5	18.7	0.2
Top Two Sectors (%)	**35.7**	**36.4**	**0.7**
Real Estate/ Construction Exposure (%) **	**21.6**	**22.0**	**0.4**

** Figures may not add to a hundred due to rounding.*

*** Real Estate/Construction exposure is calculated as the share of the construction, commercial real estate financing, and residential mortgages sectors of total lending.*

Source: CBB.

Chart 4-4: Overseas CR Bank's Lending Distribution by Sector (% Total Loans)



Source: CBB.

The top two recipients of loans ("Commercial Real Estate Financing" and "Other Sectors") jointly accounted for 36.4% of total loans. Exposure to real estate/ construction was 22.0% of total lending in March 2018, increasing from 21.6% in September 2017.

Growth in profitability

Profitability of the banks was positive, and, as at end-March 2018, return-on-assets (ROA) increased to reach 0.4%. ROA for *locally incorporated banks* slightly increased by 0.1% to 0.6% in March 2018 from 0.5% in March 2017. For *overseas banks*, ROA also increased from a loss of 0.3% in March 2017 to 0.1% in March 2018. Return-on-equity (ROE) for *locally incorporated banks* increased from 3.8% to 4.1% over the same period. Net interest income (as a % of total income) increased from 72.4% in March 2017 to 73.6% in March 2018. Operating expenses as a proportion of total income decreased significantly from 72.6% in March 2017 to 48.6% in March 2018.

Table 4-7: CR Banks' Profitability

	Mar. 2017	Mar. 2018
ROA (%) *	0.2	0.4
ROA Locally Incorporated Banks (%)	0.5	0.6
ROA Overseas Banks (%)	(0.3)	0.1
ROE (%) **	3.8	4.1
Net Interest Income (% Total Income)	72.4	73.6
Operating Expenses (% Total Income)	72.6	48.6

** ROA = ratio of net income to assets.*

*** ROE = ratio of net income to tier 1 capital (for Locally Incorporated Banks only).*

Source: CBB.

Liquidity position remains stable

Between September 2017 and March 2017, bank deposits decreased while non-bank deposits increased for retail banks. Bank deposits as % of total deposits decreased to 19.8% in March 2018 from 21.7% in September 2017. Non-bank deposits as % of total deposits increased to 80.2% over the same period from 78.3%. The overall loan-deposit ratio for the segment increased from 70.8% in September 2017 to 73.4% in March 2018. Liquid assets as a proportion of total assets decreased over the same period to reach 33.6%. Similarly, liquid assets as a proportion of the short-term liabilities presented a decrease from 45.3% to 42.4% over this period.

Table 4-8: CR Bank's Liquidity

	Sep. 2017	March 2018
Liquid Asset Ratio (%)	35.8	33.6
Loan-Deposit Ratio (%)	70.8	73.4
Non-Bank Deposits (% of Total Deposits)	78.3	80.2

Source: CBB.

The decrease in the liquid asset ratio was due to the decline in the liquid assets of conventional retail locally incorporated banks. The liquid asset ratio for locally incorporated retail banks decreased from 32.0% September 2017 to 28.0% in March 2018. However, conventional retail overseas banks saw an increase in their liquid asset ratio from 42.9% in September 2017 to 44.3% in March 2018.

4.3 Conventional Wholesale Banks

Decrease in capital adequacy [8]

As at end-March 2018, the regulatory capital adequacy ratio for locally-incorporated wholesale banks was 18.6%, a decrease from the 19.2% registered in September 2017. The core capital ratio (ratio of Tier 1 capital to risk-weighted assets) also decreased by 0.6% from 18.2% in September 2017 to 17.6% recorded in March 2018. Furthermore, the leverage ratio (ratio of assets over capital) also witnessed a minor decrease from 7.0% in September 2017 to 6.8% in March 2018. Finally, the ratio of non-performing loans (NPL's) net of provisions to capital decreased from 5.6% in September 2017 to 5.3% in March 2018.

Table 4-9: Local CW Bank's Capital Provisions Ratios *

Indicator	Sep. 2017	Mar. 2018
CAR (%)	19.2	18.6
Tier 1 CAR (%)	18.2	17.6
Leverage (Assets/Capital)(times)	7.0	6.8
NPL's Net of Provisions to Capital (%)	5.6	5.3

** For Locally Incorporated Banks only.*
Source: CBB.

Non-performing loans decline for overseas banks

As at end-March 2018, loans classified as non-performing as a % of gross loans decreased slightly from 5.6% in September 2017 to 5.3%. The NPL ratio of l*ocally-incorporated wholesale banks* remained unchanged at 4.5%. Additionally, *overseas wholesale* banks witnessed a decrease in its NPL ratio from 6.9% to 6.0% over the same period.

Table 4-10: CW Bank's NPL Ratios

Indicator	Sep. 2017	Mar. 2018
NPL's (% Total Loans)	5.6	5.3
NPL's Local Banks (%)	4.5	4.5
NPL's Overseas Banks (%)	6.9	6.0
Specific provisions (% of NPL's) *	64.9	59.9

** Specific provisions as a percentage of NPL's are calculated as specific provisions divided by gross impaired loans.*
Source: CBB.

Specific provisions as a proportion of NPL's also witnessed a decrease as well from 64.9% in September 2017 to 59.9% in March 2018.

[8] The capital adequacy ratio relates total capital to risk-weighted assets. The discussion excludes overseas wholesale banks, which do not have prescribed capital levels or ratios.

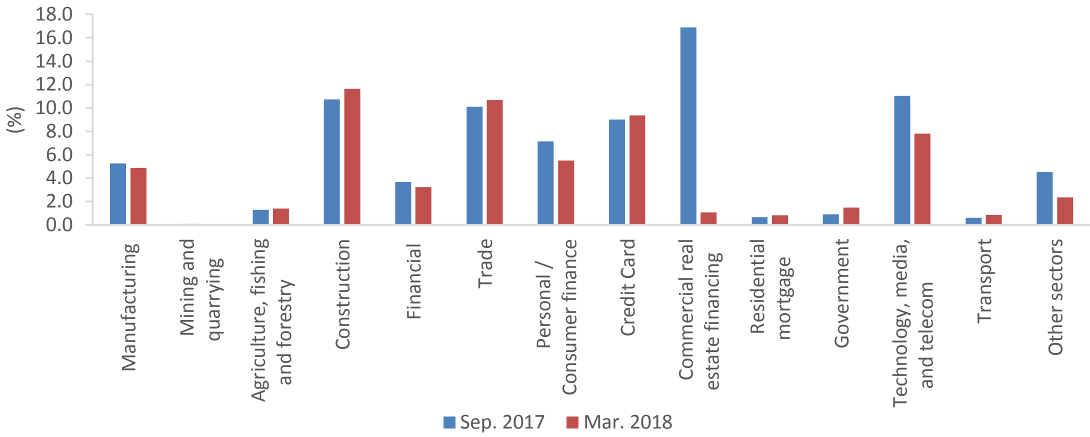
Table 4-12 depicts data on the sectoral breakdown of impaired loans, it demonstrates that impairment in "Construction" was the highest between all sectors at 11.6% followed by the "Trade" sector with an impairment of 10.7%. The biggest increase was seen in the "Construction" sector which increased by 0.9%. The greatest decrease in impairment was found in the "Commercial Real Estate and Financing" sector which decreased by 15.8%.

Table 4-11: CW Bank's NPL Ratios by Sector (%)

	Sep. 2017	Mar. 2018	Change
Manufacturing	5.3	4.9	(0.4)
Mining and quarrying	0.1	0.0	(0.1)
Agriculture, fishing and forestry	1.3	1.4	0.1
Construction	10.7	11.6	0.9
Financial	3.7	3.2	(0.5)
Trade	10.1	10.7	0.6
Personal / Consumer finance	7.1	5.5	(1.6)
Credit Card	9.0	9.4	0.4
Commercial real estate financing	16.9	1.1	(15.8)
Residential mortgage	0.7	0.8	0.1
Government	0.9	1.5	0.6
Technology, media and telecommunications	11.0	7.8	(3.2)
Transport	0.6	0.9	0.3
Other sectors	4.5	2.4	(2.1)

Source: CBB.

Chart 4-5: CW Bank's NPL Ratios by Sector (%)



Source: CBB.

Loan portfolios remains concentrated despite decreases in some sectors

An examination of lending patterns as at end-March 2018 shows that, for conventional wholesale banks, the top recipient of loans remains to be the "Financial" sector, which accounted for 19.0% of total loans in March 2018 representing a decrease of 0.3% compared to September 2017 (Table 4-12 and Chart 4-6).

Table 4-12: CW Bank's Lending Distribution by Sector (% Total Loans)*

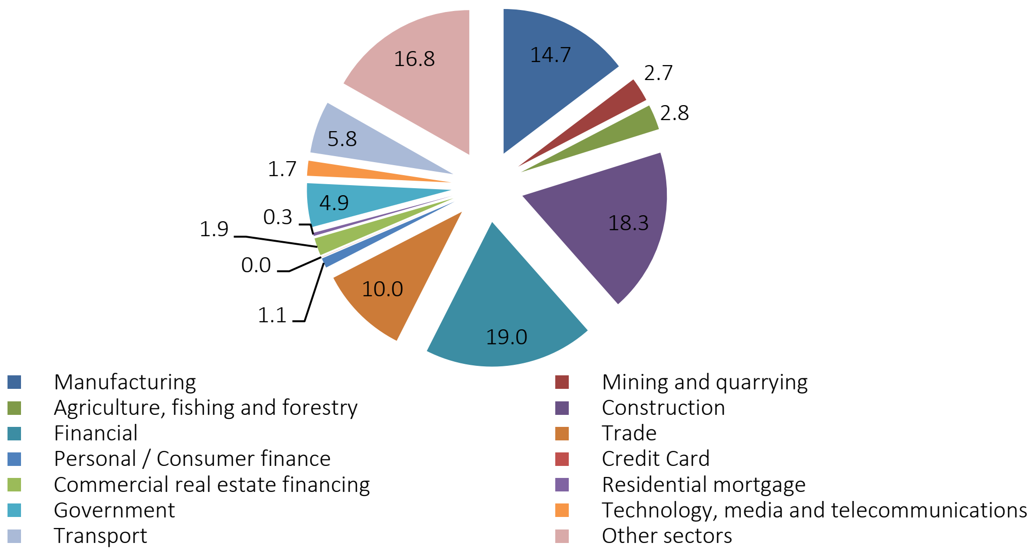
	Sep. 2017	Mar. 2018	Change
Manufacturing	13.7	14.7	1.0
Mining and quarrying	2.5	2.7	0.2
Agriculture, fishing and forestry	3.3	2.8	(0.5)
Construction	16.4	18.3	1.9
Financial	19.3	19.0	(0.3)
Trade	11.3	10.0	(1.3)
Personal / Consumer finance	1.1	1.1	0.0
Credit Card	0.0	0.0	0.0
Commercial real estate financing	2.0	1.9	(0.1)
Residential mortgage	0.4	0.3	(0.1)
Government	6.2	4.9	(1.3)
Technology, media and telecommunications	1.3	1.7	0.4
Transport	9.6	5.8	(3.8)
Other sectors	12.9	16.8	3.9
Top Two Sectors (%)	**35.7**	**37.3**	**1.6**
Real Estate/ Construction Exposure (%) **	**18.7**	**20.6**	**1.9**

** Figures may not add to a hundred due to rounding.*

*** Real Estate/Construction exposure is calculated as the share of the construction, commercial real estate financing, and residential mortgages sectors of total lending.*

Source: CBB.

Chart 4-6: CW Bank's Lending Distribution by Sector (% Total Loans)



Source: CBB.

The top two sectors in Conventional Wholesale Banks' Lending as a % of total loans are the "Construction" and "Financial" sectors, they jointly account for 37.3% of total lending in March 2018.

For *locally-incorporated wholesale banks,* the top recipient of loans is the "Financial" sector, which accounted for 22.1% of total loans in March 2018, representing a slight decrease of 0.4% from the 22.5% in September 2017 (Table 4-13 and Chart 4-7).

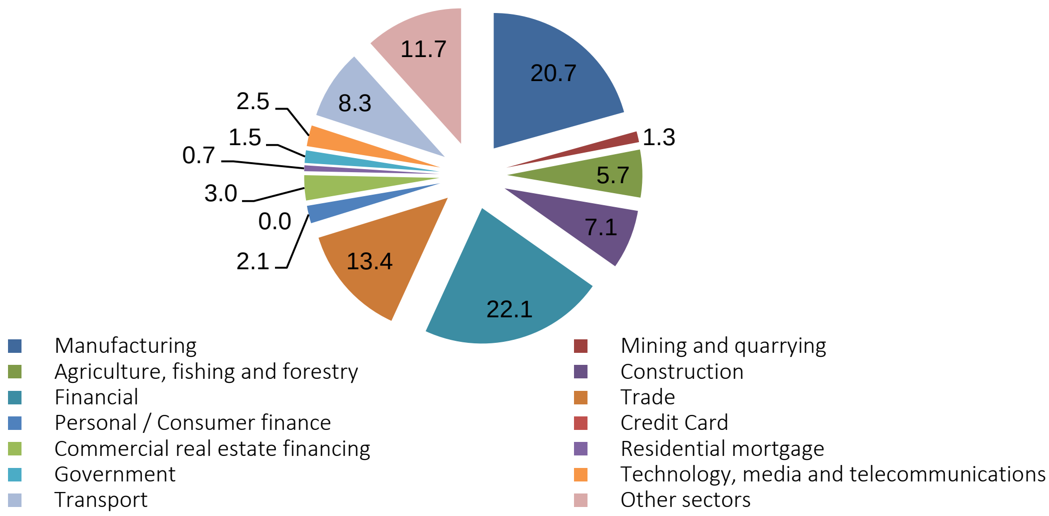
Table 4-13: Local CW Bank's Lending Distribution by Sector (% Total Loans)

	Sep. 2017	Mar. 2018	Change
Manufacturing	19.0	20.7	1.7
Mining and quarrying	1.0	1.3	0.3
Agriculture, fishing and forestry	6.3	5.7	(0.6)
Construction	7.5	7.1	(0.4)
Financial	22.5	22.1	(0.4)
Trade	14.8	13.4	(1.4)
Personal / Consumer finance	1.8	2.1	0.3
Credit Card	0.0	0.0	0.0
Commercial real estate financing	2.0	3.0	1.0
Residential mortgage	0.7	0.7	0.0
Government	3.8	1.5	(2.3)
Technology, media and telecommunications	1.0	2.5	1.5
Transport	9.3	8.3	(1.0)
Other sectors	10.2	11.7	1.5
Top Two Sectors (%)	**41.5**	**42.8**	**1.3**
Real Estate/ Construction Exposure (%) **	**10.3**	**10.9**	**0.6**

** Figures may not add to a hundred due to rounding.*
*** Real Estate/Construction exposure is calculated as the share of the construction, commercial real estate financing, and residential mortgages sectors of total lending.*
Source: CBB.

The highest two sectors continue to be the "Financial" and "Manufacturing" accounting for 42.8% of total lending in March 2018, an increase of 1.3% from the September 2017 level. The real estate/ construction exposure also increased from 10.3% 10.9% in the same period.

Chart 4-7: Local CW Bank's Lending Distribution by Sector (% Total Loans)



Source: CBB.

While observing *overseas wholesale banks*, the top recipient of loans in March 2018 was the "Construction" sector, with 29.1% of total loans, followed by the "Other" sector, with 21.7% of total loans, with increases of 3.4% and 5.9% respectively from their September 2017 levels (Table 4-14 and Chart 4-8). The top 2 sectors (Financial and Other) jointly represented 50.8% in March 2018, an increase of 9.3% from the September 2017. Real estate/construction exposure increased from 27.6% in September 2017 to 30.0 in March 2018.

Table 4-14: Overseas CW Bank's Lending Distribution by Sector (% Total Loans)

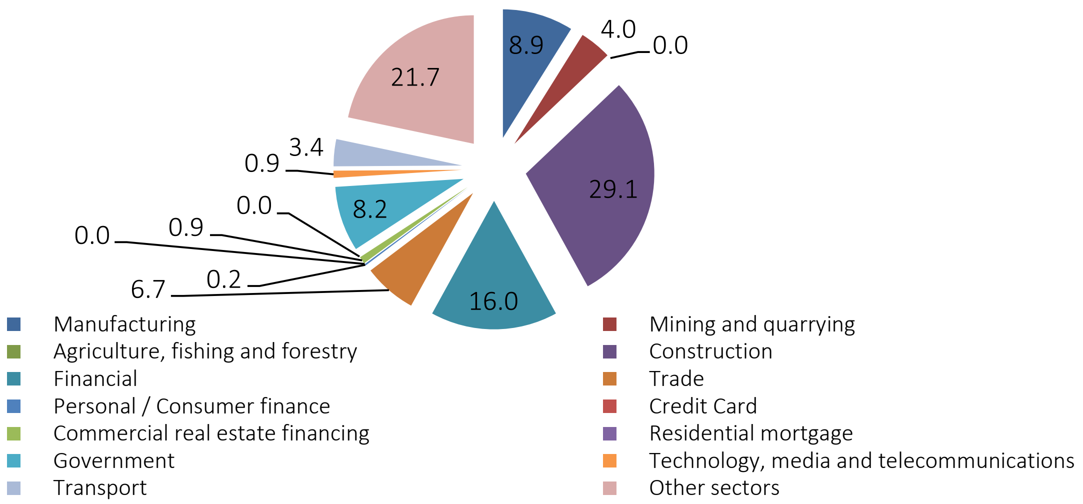
	Sep. 2017	Mar. 2018	Change
Manufacturing	8.3	8.9	0.6
Mining and quarrying	4.2	4.0	(0.2)
Agriculture, fishing and forestry	0.1	0.0	(0.1)
Construction	25.7	29.1	3.4
Financial	15.9	16.0	0.1
Trade	7.6	6.7	(0.9)
Personal / Consumer finance	0.3	0.2	(0.1)
Credit Card	0.0	0.0	0.0
Commercial real estate financing	1.9	0.9	(1.0)
Residential mortgage	0.0	0.0	0.0
Government	8.7	8.2	(0.5)
Technology, media and telecommunications	1.6	0.9	(0.7)
Transport	10.0	3.4	(6.6)
Other sectors	15.8	21.7	5.9
Top Two Sectors (%)	**41.5**	**50.8**	**9.3**
Real Estate/ Construction Exposure (%) **	**27.6**	**30.0**	**2.4**

** Figures may not add to a hundred due to rounding.*

*** Real Estate/Construction exposure is calculated as the share of the construction, commercial real estate financing, and residential mortgages sectors of total lending*

Source: CBB.

Chart 4-7: Overseas CW Bank's Lending Distribution by Sector (% Total Loans)



Source: CBB.

Stable earnings for wholesale banks

ROA for the conventional wholesale banking sector remained at 0.3% in March 2018. The ROA for both *local wholesale banks* also remained at 0.3, while *overseas wholesale banks* slightly decreased from 0.4% to 0.3%.

ROE for *local wholesale banks* increased from 1.9% to 2.1%. Net interest income as a proportion of total income decreased from 46.1% in March 2017 to 40.5% in March 2018. Operating expenses as a proportion of total income showed an increase from 52.2% in March 2017 to 57.9% in March 2018.

Table 4-15: CW Bank's Profitability

	Mar. 2017	Mar. 2018
ROA (%) *	0.3	0.3
ROA Locally Incorporated Banks (%)	0.3	0.3
ROA Overseas Banks (%)	0.4	0.3
ROE (%) **	1.9	2.1
Net Interest Income (% Total Income)	46.1	40.5
Operating Expenses (% Total Income)	52.2	57.9

** ROA = ratio of net income to assets.*

*** ROE = ratio of net income to tier 1 capital (for Locally Incorporated Banks only).*

Source: CBB.

Liquidity position increases

As at end-March 2018, the overall loan-deposit ratio for conventional wholesale banks stood at 69.2%, an increase from the 63.4% in September 2017. The loan deposit ratio for *local wholesale banks* increased to 67.9% in March 2018 from 61.2% in September 2017. Over the same period, the loan deposit ratio for *overseas wholesale* bank increased from 66.0% to 70.6%.

Liquid assets for wholesale banks as a proportion of total assets increased to 23.2% in March 2018 from 21.9% in September 2017. *Locally incorporated wholesale banks* decreased in liquidity over this period where their liquid asset ratio decreasing slightly to 27.0% from 27.6%. *Overseas wholesale banks* contributed mainly to the increased in liquid assets ratios as their liquidity increased from 15.1% to 19.0% in March 2018.

The liquid assets as a proportion of short-term liabilities decreased from 33.5% to 28.9% in March 2018. Finally, the deposits from non-bank sources as a proportion of total deposits stood at 52.8%, an increase from the 47.1% level achieved in September 2017, while bank deposits decreased from 52.9% in September 2017 to 47.2% in March 2018.

Table 4-16: CW Bank's Liquidity

	Sep. 2017	Mar. 2018
Liquid Asset Ratio (%)	21.9	23.2
Loan-Deposit Ratio (%)	63.4	69.2
Non-Bank Deposits (% of Total Deposits)	47.1	52.8

Source: CBB.

4.4 Overall Assessment of the Conventional Banking Sector

The financial soundness indicators show that conventional banks witnessed a slight decrease in capital adequacy ratios. Capital adequacy ratios for conventional retail banks decreased to 19.6% in March 2018. Capital adequacy ratio for conventional wholesale banks decreased to 18.6% over the same period. Non-performing loans have shown a slight increase between the periods of September 2017 to March 2018 from 5.8% to 5.9%, for conventional retail banks. As for conventional wholesale banks, loans classified as non-performing decreased from 5.6% in September 2017 to 5.3% in March 2018. Loan concentration remains high for conventional retail and for wholesale banks.

As at end-March 2018, return-on-assets (ROA) increased to 0.4% for conventional retail banks and remained at 0.3% for conventional wholesale banks. Return-on-equity (ROE) for *local retail banks* increased from 3.8% in March 2017 to 4.1% in March 2018. ROE for *local wholesale banks* increased from 1.9% to 2.1% over the same period. For conventional retail banks, liquid assets as a proportion of total assets slightly decreased over the period of September 2017 to March 2018 to reach 33.6% due to a decrease in liquid assets of conventional retail banks that are locally incorporated. Liquid assets for wholesale banks as a proportion of total assets increased from 21.9% in September 2017 to 23.2% in March 2018.

5. Islamic Banks

Chapter 5

Key Points

- Capital positions for Islamic retail and wholesale banks decreased slightly.
- Increase in non-performing facilities (NPF's) for Islamic retail banks and decrease in wholesale banks.
- Concentration of facilities for both Islamic retail banks and Islamic wholesale Banks continues.
- Earnings remained positive for Islamic retail and Islamic wholesale banks.
- Liquidity positions increased for Islamic retail banks while it decreased for Islamic wholesale banks.

5.1 Overview

This chapter analyzes the banking sector under the following categories: Islamic retail banks (section 5.2) and Islamic wholesale banks (section 5.3). Section 5.4 provides an overall assessment of the Islamic banking industry. Unless specified otherwise, the analysis in this chapter is based on consolidated financial data (Bahraini and non-Bahraini operations), as at end-March 2018 and compared with end-September 2017. This chapter offers macroprudential analysis of the Islamic banking sector based on a set of selected Financial Soundess Indicators (FSIs).[9]

5.2 Islamic Retail Banks

Decrease in capital positions

The CAR of Islamic retail banks decreased from 18.2% in September 2017 to 18.0% in March 2018. Tier 1 capital also decreased to 14.8% in March 2018 from 15.3% in September 2017.

Table 5-1: IR Capital Provisions Ratios

Indicator	Sep. 2017	Mar. 2018
CAR (%)	18.2	18.0
Tier 1 CAR (%)	15.3	14.8
NPF's Net of Provisions to Capital (%)	26.1	32.1

Source: CBB.

[9] This chapter does not contain a section on stress testing. Stress Testing exercises are performed separately in an internal report to obtain information on the potential quantitative impact of hypothetical scenarios on selected Bahraini Systemically-Important Banks (SIB's).

The ratio of non-performing facilities (NPF's) net of provisions to capital increased from 26.1% to 32.1% for the same period.

Increase in non-performing facilities

Non-performing facilities (NPF) ratio increased to 10.0% in March 2018, compared to 9.0% in September 2017. Specific Provisoining decreased from 44.1% in September 2017 to 41.3% in March 2018.

Table5-2: IR NPF Ratios

Indicator	Sep. 2017	Mar. 2018
NPF's (% Gross Facilities)	9.0	10.0
Specific Provisions (% of NPF's)	44.1	41.3

Source: CBB.

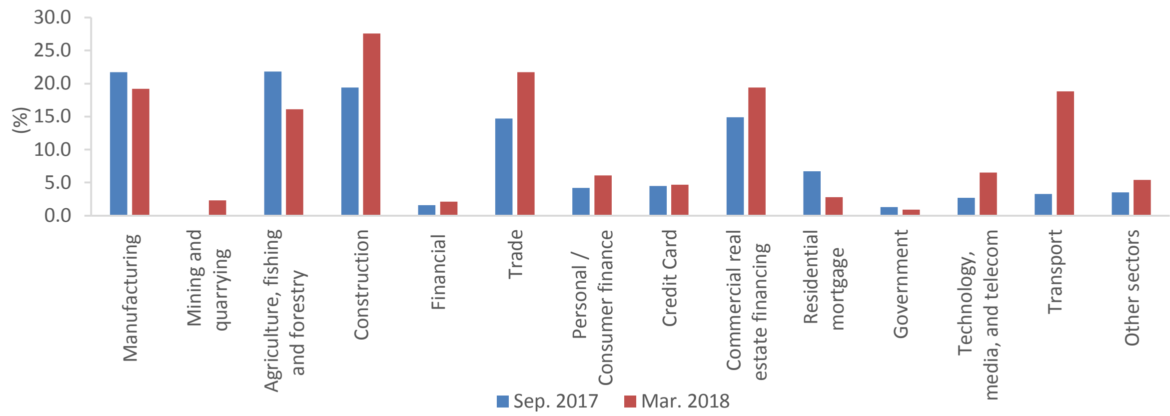
A look at the non-performing facilities by sector indicates that the "Construction" sector had the highest impairment of 27.6% in March 2018 followed by "Trade" and "Commercial real estate financing" with 21.7% and 19.4% respectively. The biggest declines in NPF's by sector was in the "Agriculture, fishing and forestry" Sector with a 5.7% decrease in NPF's from September 2017 to March 2018. The biggest increase in NPF's was the "Transport" sector with an increase of 15.5%.

Table 5-3: IR NPF Ratios by Sector (%)

	Sep. 2017	Mar. 2018	Change
Manufacturing	21.7	19.2	(2.5)
Mining and quarrying	0.1	2.3	2.2
Agriculture, fishing and forestry	21.8	16.1	(5.7)
Construction	19.4	27.6	8.2
Financial	1.6	2.1	0.5
Trade	14.7	21.7	7.0
Personal / Consumer finance	4.2	6.1	1.9
Credit Card	4.5	4.7	0.2
Commercial real estate financing	14.9	19.4	4.5
Residential mortgage	6.7	2.8	(3.9)
Government	1.3	0.9	(0.4)
Technology, media and telecommunications	2.7	6.5	3.8
Transport	3.3	18.8	15.5
Other sectors	3.5	5.4	1.9

Source: CBB.

Chart 5-1: IR NPF Ratios by Sector (%)



Source: CBB.

Diversification in asset concentration (loan portfolio)

There have been a diversification in the asset concentration among most of the sectors. At the end of March 2018, the top recipient of financing was "Personal / Consumer finance" at 19.8% down from 22.3% in September 2017. The top two recipients of financing ("Personal / Consumer finance" and "Financial") accounted for 35.8% of total facilities extended compared to 37.6% for the top two sectors in September 2017. Moreover, the share of the "Manufacturing" sector declined from 13.0% in September 2017 to 12.1% in March 2018.

"Real Estate/ Construction" exposure increased from 24.0% in September 2017 to 26.2% in March 2018.

Table 5-4: IR Lending Distribution by Sector (%Total Facilities)*

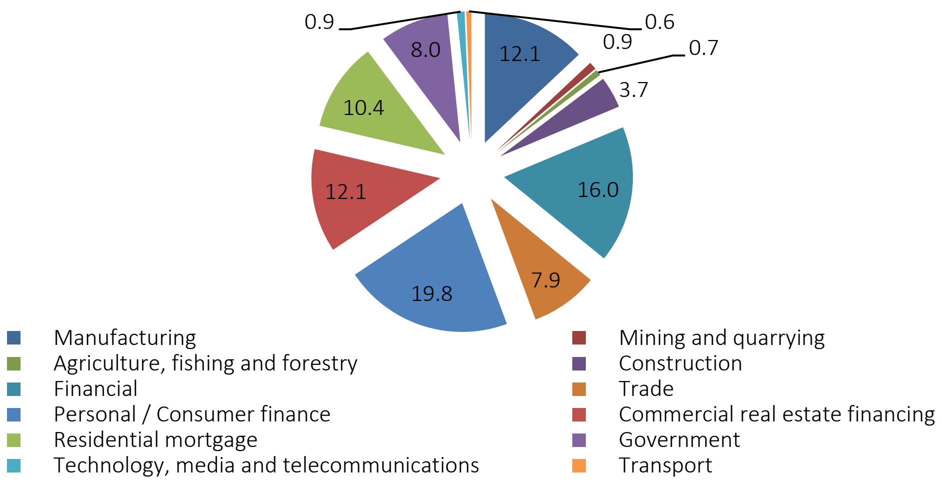
	Sep. 2017	Mar. 2018	Change
Manufacturing	13.0	12.1	(0.9)
Mining and quarrying	0.8	0.9	0.1
Agriculture, fishing and forestry	0.7	0.7	0.0
Construction	4.8	3.7	(1.1)
Financial	15.3	16.0	0.7
Trade	8.6	7.9	(0.7)
Personal / Consumer finance	22.3	19.8	(2.5)
Credit Card	0.8	0.8	0.0
Commercial real estate financing	11.4	12.1	0.7
Residential mortgage	7.8	10.4	2.6
Government	5.7	8.0	2.3
Technology, media and telecommunications	0.9	0.9	0.0
Transport	0.8	0.6	(0.2)
Other sectors	7.1	5.9	(1.2)
Top Two Sectors (%)	**37.6**	**35.8**	**(1.8)**
Real Estate/ Construction Exposure (%) **	**24.0**	**26.2**	**2.2**

** Figures may not add to a hundred due to rounding.*

*** Real Estate/Construction exposure is calculated as the share of the construction, commercial real estate financing and residential mortgages sectors of total lending.*

Source: CBB.

Chart 5-2: IR Lending Distribution by Sector (% Total Facilities)



Source: CBB.

Lending distribution by Islamic instrument remained nearly unchanged over the past quarter. At the end of March 2018, the top recipient of finance was "Murabaha" at 63.1% down from 63.8% in September 2017. This was followed by "Ijarah", which slightly increased from 21.5% to 21.7% for the same period.

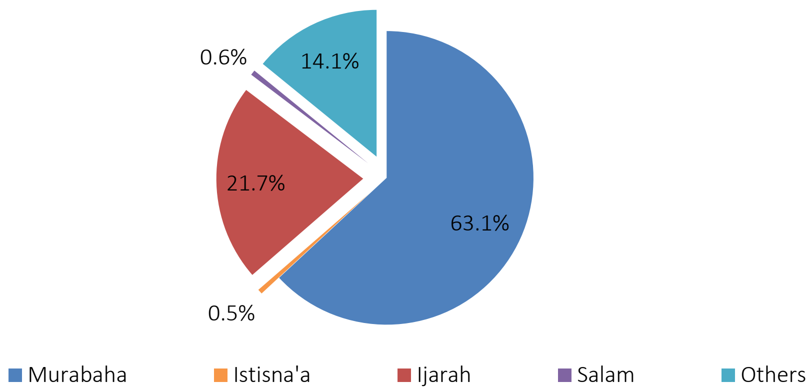
Table 5-5: IR Lending Distribution by Islamic Instrument (%Total Facilities)*

	Sep. 2017	Mar. 2018	Change
Murabaha	63.8	63.1	(0.7)
Istisna'a	0.5	0.5	0.0
Ijarah	21.5	21.7	0.2
Salam	0.6	0.6	0.0
Others	13.5	14.1	0.6

** Figures may not add to a hundred due to rounding.*

Source: CBB.

Chart 5-3: IR Lending Distribution by Islamic Instrument (%Total Facilities)



Source: CBB.

Slight growth in earnings

The return on assets (ROA) for Islamic retail banks increased to reach 0.2% in March 2018 compared to 0.1% in March 2017. Return on equity (ROE) also increased from 1.1% to 1.5% for the same period. In contrast, operating expenses decreased from 77.8% in March 2017 to 74.0% in March 2018.

Table 5-6: IR Profitability

	Mar. 2017	Mar. 2018
ROA (%) *	0.1	0.2
ROE (%) **	1.1	1.5
Operating expenses (% Total Income)	77.8	74.0

** ROA = ratio of net income to assets.*

*** ROE = ratio of net income to tier 1 capital.*

Source: CBB.

Increase in liquidity

The volume of liquid assets available to Islamic retail banks increased from 11.5% of total assets in September 2017 to 14.5% in March 2018. The ratio of total facilities to deposits increased from 89.1% in September 2017 to 94.4% in March 2018.

Table 5-7: IR Liquidity

Indicator	Sep. 2017	Mar. 2018
Liquid Assets (% of Total Assets)	11.5	14.5
Facility-Deposit Ratio (%)	89.1	94.4

Source: CBB.

5.3 Islamic Wholesale Banks

Decline in capital positions

As at end-March 2018, the CAR for Islamic wholesale banks decreased to 18.5% from 18.8% in September 2017. Tier1 capital also dropped from 18.3% to 17.4% over the same period. The ratio of NPF's net of provisions to capital increased from 0.3% to 1.0%.

Table 5-8: IW Capital Provisions Ratios

Indicator	Sep. 2017	Mar. 2018
CAR (%)	18.8	18.5
Tier 1 CAR (%)	18.3	17.4
NPF's net of Provisions to Capital (%)	0.3	1.0

Source: CBB.

Decreasing non-performing facilities (NPF's)

As of end-March 2018, NPF ratio for Islamic wholesale banks decreased to 1.4%. Provisioning for NPF's decreased from 95.8% to 75.7% over the same period.

Table 5-9: IW NPF Ratios

Indicator	Sep. 2017	Mar. 2018
NPF's (% Total Facilities)	2.4	1.4
Specific Provisioning (% of NPF's)	95.8	75.7

Source: CBB.

The sector with the highest impairment was the "Technology, media and telecommunications" sector with 79.8% in March 2018, up from the 48.5% in September 2017. This was followed by the "Mining and quarrying" and "Commercial real estate financing" sectors.

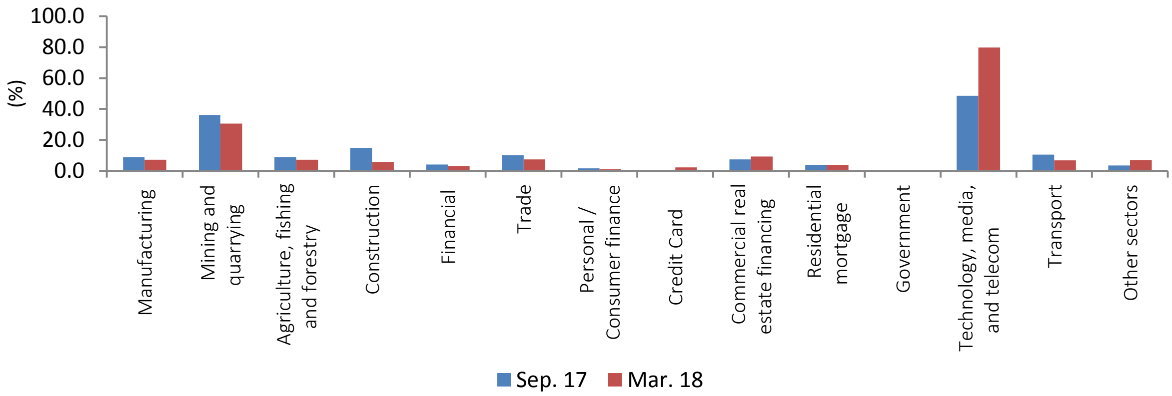
Table 5-10: IW NPF Ratios by Sector (%)

	Sep. 2017	Mar. 2018	Change
Manufacturing	8.8	7.2	(1.6)
Mining and quarrying	36.2	30.5	(5.7)
Agriculture, fishing and forestry	9.0	7.2	(1.8)
Construction	14.8	5.8	(9.0)
Financial	4.1	3.1	(1.0)
Trade	10.2	7.4	(2.8)
Personal / Consumer finance	1.6	1.1	(0.5)
Credit Card	0.0	2.3	2.3
Commercial real estate financing	7.5	9.3	1.8
Residential mortgage	3.9	4.0	0.1
Government	0.0	0.0	0.0
Technology, media and telecommunications	48.5	79.8	31.3
Transport	10.6	6.9	(3.7)
Other sectors	3.6	7.1	3.5

Source: CBB.

Available data on the sectoral breakdown of non-performing facilities shows that the biggest increase was in the "Technology, media and telecommunications" sector with an increase of 31.3%. The biggest drop was in the "Construction" with a decrease of 9.0% from 14.8% in September 2017 to 5.8% in March 2018.

Chart 5-4: IW NPF Ratios by Sector (%)



Source: CBB.

Decreases in asset concentration (loan portfolio)

At end-March 2018, the "Manufacturing" sector was the top recipient of financing from Islamic wholesale banks, at 22.6%, despite a 2.7% drop. The "Personal / Consumer finance" sector increased from 7.6% in September 2017 to 11.9% in March 2018.

Table 5-11: IW Lending Distribution by Sector (%Total Facilities)*

	Sep. 2017	Mar. 2018	Change
Manufacturing	25.3	22.6	(2.7)
Mining and quarrying	1.2	1.1	(0.1)
Agriculture, fishing and forestry	1.0	0.9	(0.1)
Construction	13.9	11.9	(2.0)
Financial	13.4	10.8	(2.6)
Trade	9.3	10.9	1.6
Personal / Consumer finance	7.6	11.9	4.3
Credit Card	0.0	0.4	0.4
Commercial real estate financing	1.9	1.7	(0.2)
Residential mortgage	3.3	3.6	0.3
Government	6.4	5.9	(0.5)
Technology, media and telecommunications	0.2	0.1	(0.1)
Transport	1.7	1.4	(0.3)
Other sectors	14.8	16.8	2.0
Top Two Sectors (%)	40.1	39.4	(0.7)
Real Estate/ Construction Exposure (%) **	19.1	17.2	(1.9)

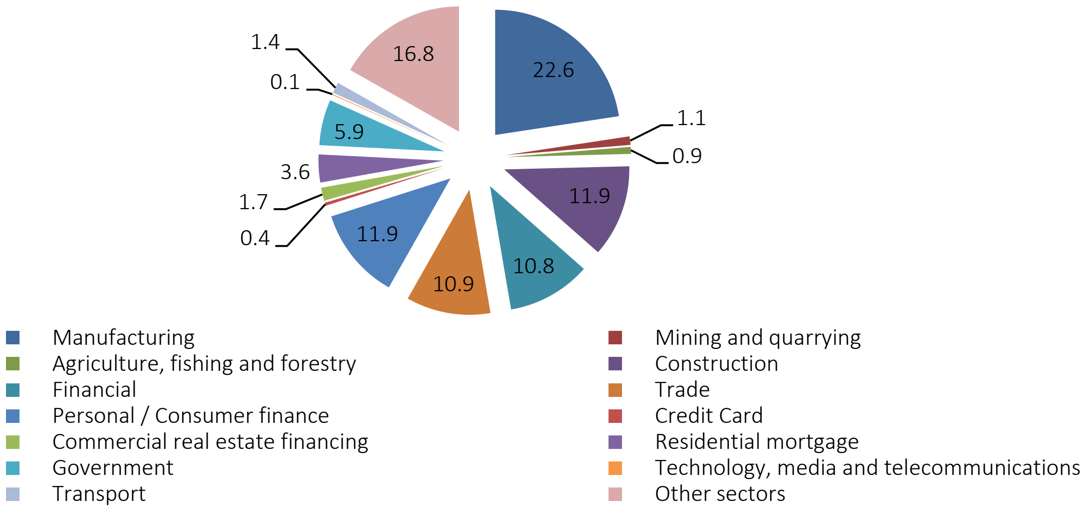
** Figures may not add to a hundred due to rounding.*

*** Real Estate/Construction exposure is calculated as the share of the construction, commercial real estate financing, and residential mortgages sectors of total lending.*

Source: CBB.

The top two recipient sectors in March 2018 (“Manufacturing” and “Construction”) jointly represented 39.4% of total financing, down from 40.1% in September 2017. Real estate/ construction exposure decreased to 17.2% in March 2018 from 19.1% in September 2017.

Chart 5-5: IW Lending Distribution by Sector (% Total Facilities)



Source: CBB.

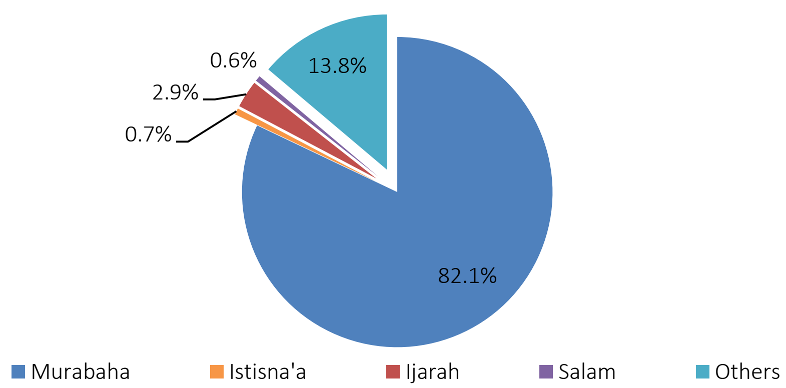
Lending distribution by Islamic instrument shows that at the end of March 2018, the top recipient of finance was “Murabaha” at 82.1%.

Table 5-12: IW Lending Distribution by Islamic Instrument (%Total Facilities)

	Sep. 2017	Mar. 2018	Change
Murabaha	90.1	82.1	(8.0)
Istisna'a	0.7	0.7	0.0
Ijarah	2.3	2.9	0.6
Salam	1.3	0.6	(0.7)
Others	5.6	13.8	8.2

**Figures may not add to a hundred due to rounding.*
Source: CBB.

Chart 5-6: IW Lending Distribution by Islamic Instrument (%Total Facilities)



Source: CBB.

Slight growth in earnings

The earnings performance of Islamic wholesale banks slightly improved over the period from March 2017 to March 2018. Return on assets (ROA) increased from 0.2% in March 2017 to 0.3% in March 2018. Return on equity (ROE) also increased from 1.4% to 2.0% in March 2018. Also, operating expenses (as % of total income) decreased from 73.0% in March 2017 to 64.8% in March 2018.

Table 5-13: IW Profitability

	Mar. 2017	Mar. 2018
ROA (%) *	0.2	0.3
ROE (%) **	1.4	2.0
Operating Expenses (% Total Income)	73.0	64.8

** ROA = ratio of net income to assets.*

*** ROE = ratio of net income to tier 1 capital.*

Source: CBB.

Liquidity position stable with no significant change

As of end-March 2018, liquid assets of Islamic wholesale banks represented 21.0% of total assets, 1.9% lower than the 22.9% registered in September 2017. Additionally, the facilities deposit ratio increased from 61.4% to 67.9% in March 2018.

Table 5-14: IW Liquidity

Indicator	Sep. 2017	Mar. 2018
Liquid Assets (% of Total Assets)	22.9	21.0
Facility-Deposit ratio (%)	61.4	67.9

Source: CBB.

5.4 Overall Assessment of the Islamic Banking Sector

The financial soundness indicators show that Islamic retail banks and wholesale banks capital positions decreased to 18.0% and 18.5% respectively during the period between September 2017 and March 2018. Non-performing facilities increased for Islamic retail and decreased for Islamic wholesale to reach 10.0% and 1.4% respectively. Facilities concentration has decreased in some sectors while increasing in others in retail Islamic banks and wholesale Islamic banks.

Earnings slightly improved for both Islamic retail and wholesale banks. Islamic retail banks' liquidity positions showed an increase in liquid assets and in facilities to deposit ratio. Islamic wholesale's experienced slight changes in its liquidity position as the facilities to deposits ratio increased while the liquid asset ratio decreased.

Part III:

Developments in the Non-Banking Financial Sector

6. Performance of the Insurance Sector

Key Points

- Conventional firms account for 73.9% of total insurance industry with BD 58.1 million in total gross premiums as of March 2018.
- General insurance contributes for 85.6% of total gross premiums.
- Takaful and Local Conventional insurance firms' performance is concentrated on Motor business line.
- Overseas insurance firms' performance is concentrated on Long-term (Life) and Engineering business line,

Chapter 6

6.1 Overview

This chapter highlights the overall performance of the insurance industry in Bahrain by looking at two main insurance segments: conventional and takaful, their different business lines, and classes. [10]

Chapter 6 of the report analyzes data covering the period between end-March 2017 and end-March 2018, unless otherwise indicated.

The insurance industry has been growing steadily in recent years, mirroring the growth of Bahrain's financial sector, the increased access to financial services and products has led to demand for insurance services. A notable development in recent years has been international insurers developing their regional operations, many of whom have chosen Bahrain as their regional base.

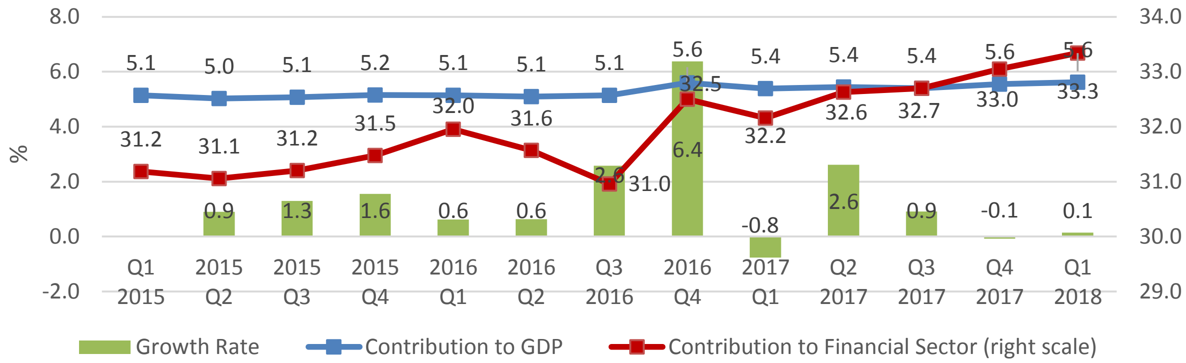
A significant number of insurance companies and organizations have established their presence in Bahrain. As of June 2018, there are a total of 143 insurance organizations licensed and registered in the Kingdom. There are 36 insurance companies: 16 conventional local 12 conventional overseas/foreign branches, and 7 takaful. From these companies, 2 companies are conventional re-insurance firms and 2 re-takaful firms. The remaining 108 other registered insurance licenses include:

- 32 Insurance Brokers,
- 4 Insurance Managers,
- 4 Insurance Consultants,
- 25 Insurance Firms, brokers and consultants restricted to business outside Bahrain,
- 29 Registered Actuaries,
- 12 Registered loss Adjusters, and
- 2 Insurance Pools and Syndicates.

[10] Takaful companies are companies conducting takaful business in line with Islamic principles. Overseas insurance companies are branches of foreign companies.

As of March 2018, the insurance sector represented 5.6% of the constant GDP, with an annual increase of 3.6% compared to March 2017. The contribution of the Insurance sector to the overall financial sector has increased representing 33.3% of the overall financial sector as of March 2018. Chart 6-1 shows the contribution of the Insurance sector to GDP since 2015, along with the quarterly growth rates, and the contribution of the insurance sector to the financial sector.

Chart 6-1: Insurance sector Contribution and Growth to GDP

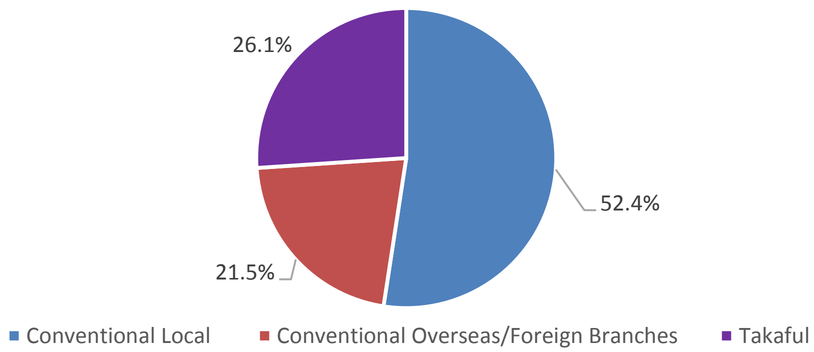


Source: IGA.

6.2 Performance of Overall Insurance Industry

The insurance sector in Bahrain is made up of two main segments: conventional and Takaful. The conventional sector is further divided into local and overseas/branches firms. As of March 2018, conventional insurance represented 73.9% of the total gross premiums accounting for BD 60.7 million. Local conventional and branches represented 52.4% and 21.5% of total gross premiums accounting for BD 43.0 million and BD 17.7 million respectively (Chart 6-2). Takaful firms accounted for BD 21.4 million which is 26.1% of gross premiums in the industry for the same period.

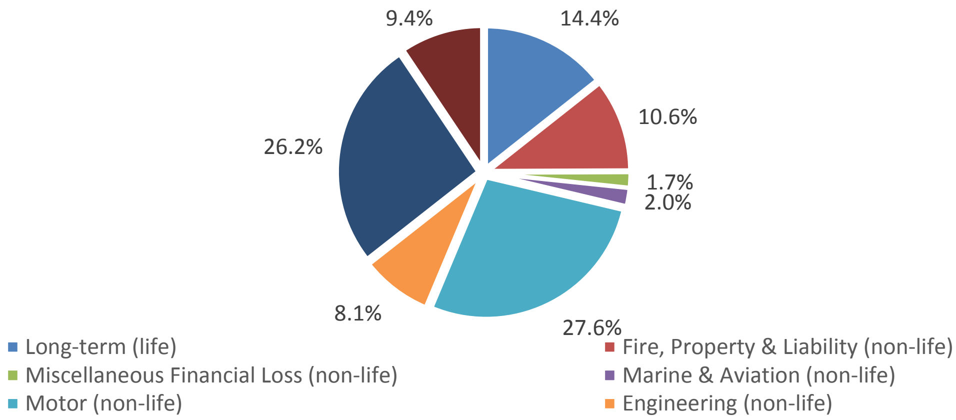
Chart 6-2: Gross Premiums of Insurance Sector by Segment (%)*



**Provisional Data*
Source: CBB.

The Insurance products and services in the Kingdom are delivered via two main insurance classes: Life and non-life insurance.[11] As of March 2018, life insurance represented 14.4% of gross premiums while non-life/general insurance represented 85.6% covering the various classes (Graph 6-3).

Chart 6-3: Market Share of Gross Premiums by Business Lines (%)*



**Provisional Data*

Source: CBB.

For non-life insurance, motor and medical insurance had the largest share in terms of their contribution to gross premiums accounting for 27.6% and 26.2% respectively. Fire, property, and liability made 11.0% of gross premiums. The top 3 business lines sectors represented 68.2% of total gross premiums. The high concentration within these sectors can be explained by:

- Banks imposing an obligatory requirement on the customers to have a life insurance prior to getting specific loans.
- Third party motor insurance being a mandatory requirement.
- Many institutions providing their employees with health insurance.

6.2 Performance of Insurance Sector by Insurance Segment

6.2.1 Conventional Insurance Firms

a. Assets: As of March 2018, total assets of the conventional insurance sector stood at BD 2,206.5 million increasing by 7% compared to the BD 2,061.5 million registered in the same quarter of 2017.
   i. Total assets of local insurance Firms were BD 1,920.5 million (80% of total assets) with a growth rate of 6.7 since March 2017.
   ii. Total assets of overseas foreign branches were BD 285.9 million (12% of total assets) recording a growth of 9.3%
b. Liabilities: As of March 2018, the liabilities of the conventional insurance sector registered at BD 1,652.9 million with a 10.6% increase from the BD 1,494.5 million in March 2017.

[11] Non-life or general insurance includes: Fire, Property & Liability, Miscellaneous Financial Loss, Marine & Aviation, Motor, Engineering, Medical and Others.

   i. The liabilities for local insurance firms registered at BD 1,394.2 million with an increase of 10.4%.
   ii. The liabilities of overseas foreign branches was BD 258.6 million in March 2018 with an increase of 11.4%.

c. Available Capital[12]: Total capital as of March 2018 was at BD 358.6 million increasing by 11.2% from the BD 322.4 million in the equivalent period of the preceding year.
   i. Total available capital for local insurance was BD 335.8 with a year to year decrease of 13.0%.
   ii. Total available capital for overseas foreign branches insurance dropped by 9.4%. The amount fell from BD 25.1 million in March 2017 to BD 22.7 million in March 2018.

6.2.2 Takaful Insurance Firms

a. Assets: Total assets in takaful firms in March 2018 experienced an annual growth of 16.4% reaching BD 184.0 million compared to BD 158.0 million in March 2017.
b. Liabilities: The liabilities increased by 16.5% from BD 105.8 million in March 2017 to BD 123.3 million in March 2018.
c. Available Capital: Total regulatory capital experienced an annual decline of 18.3% from BD 59.6 million in March 2017 to BD 48.7 million in March 2018.

6.3 Premiums and Claims Analysis by Class:

6.3.1 Overall Insurance

As of March 2018, the Gross Premiums for the overall insurance sector stood at BD 82.1 million, increasing by 9.2%. Looking at the performance by class, Others category experienced the greatest increase within the rest of the insurance business line, with an annual increase of 309.6%, followed by Miscellaneous Financial Loss and Engineering, both increasing by 10.9% and 9.4% respectively. On the other hand, Long-term insurance experienced an annual decline by 8.5% during the same period.

As of March 2018 Net Premiums Written increased compared to the previous period registering a value of BD 54.1 million, which is a 10.6% year-on-year increase from the BD 48.9 million in March 2017. The Others class showed the biggest increase in terms of growth over the period increasing by 1,754%, from BD 180 thousand in March 2017 to BD 3.3 million in March 2018. On the other hand, the biggest decline was derived from Fire, Property & Liability class, decreasing from BD 2.8 million in March 2017 to BD 2.3 million in March 2018.

Gross Claims for the overall insurance industry recorded a great year-on-year increase of 46.6% from BD 56.5 million in March 2017 to BD 82.8 million in March 2018. The increase was mainly due to an increase of Engineering business line by 1,666.1% from BD 2.1 million in March 2017 to BD 37.5 million

[12] As per the CBB Rulebook, equity is a regulatory equity, which means encompasses Tier 1 Capital, Tier 2 Capital and deduction.

in March 2018, followed by Miscellaneous Financial Loss class, showing an annual increase of 387.2% reaching BD 2.3 million in March 2018.

However, Net Claims for the overall insurance industry show an increase of 35.6%, which was derived from an annual increase in Others business line by 475.9%. The greatest decline was experienced in Marine & Aviation, dropping by 253.7%

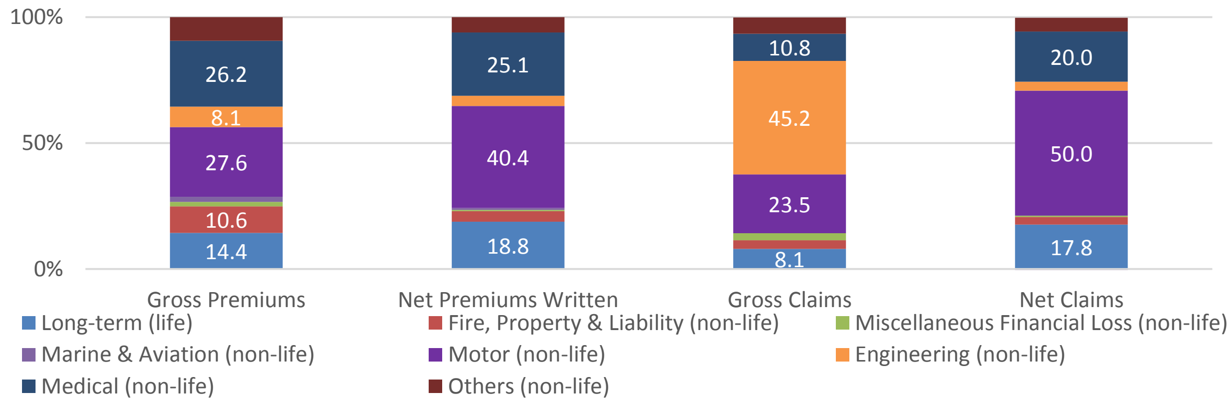
Table 6-1: Gross Premiums and Claims for all Insurance Firms by Class– Bahrain operations *

BD '000	Gross Premiums		Net Premiums Written		Gross Claims		Net Claims	
	Q1 2017	Q1 2018	Q1 2017	Q1 2018	Q1 2017	Q1 2018	Q1 2017	Q1 2018
Long-term (Life)	12,870	11,783	11,528	10,175	5,783	6,675	4,934	5,758
Fire, Property & Liability	8,749	8,676	2,798	2,269	21,257	2,880	810	999
Miscellaneous Financial Loss	1,277	1,417	93	293	467	2,277	118	157
Marine & Aviation	1,863	1,673	457	402	264	-171	74	-114
Motor	20,791	22,661	19,970	21,850	16,557	19,436	12,181	16,201
Engineering	6,064	6,633	2,321	2,213	2,121	37,458	718	1,145
Medical	21,612	21,490	11,558	13,566	8,721	8,929	4,761	6,489
Others	1,882	7,711	180	3,340	1,338	5,350	309	1,779
Total	**75,110**	**82,044**	**48,904**	**54,108**	**56,506**	**82,835**	**23,905**	**32,413**

**Provisional Data*
Source: CBB.

The concentrations of premuims and claims by class are viewed in Graph 6-5. For the overall insurance indusry, the exposure in Motor was the highest in Gross Premiums (27.6%), Net Premiums Written (40.4%), and Net Claims (50.0%). Whereas in Gross Claims, Engineering had the highest concentration (45.2%).

Chart 6-4: Concentrations of Gross Premiums and Claims for all Insurance Firms by Class – Bahrain Operations (Q1 2018)*



**Provisional Data*
Source: CBB.

6.3.2 Conventional Insurance

The Gross Premiums recorded for conventional insurance (Bahraini operations only) exhibited an increase by 4.4% based on a year-on-year comparison, where total gross premiums increased from BD 58.1 million in March 2017 to BD 60.7 million in March 2018 (Table 6-2). Where the greatest decline arrived from Medical business class by 16.1%. While the greatest annual increase was contributed by Others business line at 867.5%. In terms of concentration, Motor and Medical business classes represented 26.8% and 21.4% respectively of the total gross premiums.

Net Premiums Written reflected a modest annual increase by 6.2% compared to March 2017. Motor insurance remained the largest in terms of Net Premiums Written concentration as well, accounting for 39.1%, increasing from BD 15.6 million in March 2017 to BD 15.7 million in March 2017..

Gross Claims on the other hand, increased at an annual rate of 46.8% in March 2018 due to a substantial increase in Engineering, from merely being at BD 2.1 million in March 2017 accelerating to BD 37.4 million by March 2018. This insurance class furthermore accounted for the highest share in gross claims (50.9%), followed by Motor at 20.7%.

Net Claims experienced an annual increase of 30.9% from BD 19.1 million in March 2017, reaching BD 25.0 million in March 2018. Others business line increased by 710.4%. Nonetheless, the concentration falls heavily within the Motor insurance class, accounting for 51.5% of the total net claims.

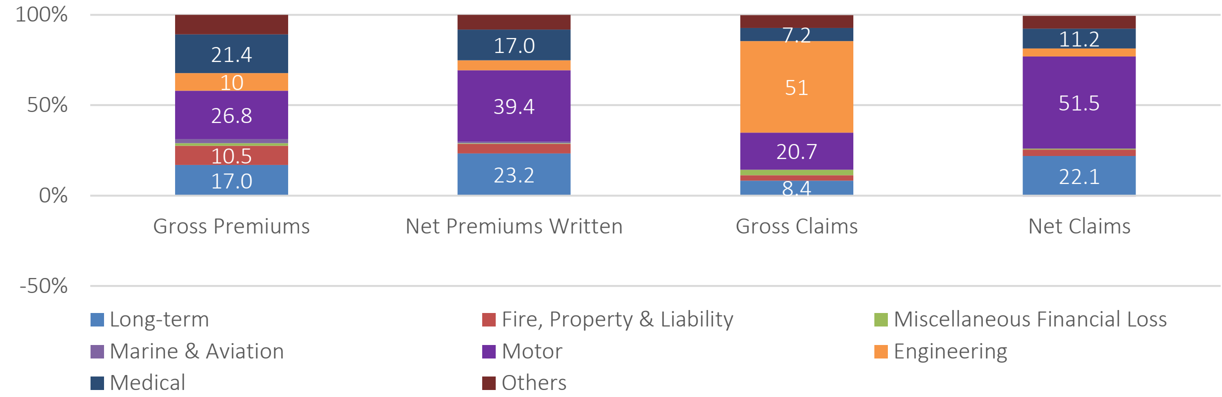
Table 6-2: Gross Premiums and Claims of Conventional Insurance by Class – Bahrain operations*

BD '000	Gross Premiums		Net Premiums Written		Gross Claims		Net Claims	
	Q1 2017	Q1 2018	Q1 2017	Q1 2018	Q1 2017	Q1 2018	Q1 2017	Q1 2018
Long-term (Life)	10,939	10,320	10,124	9,270	5,657	6,195	4,876	5,542
Fire, Property & Liability	6,387	6,356	2,583	2,138	20,995	2,177	778	886
Miscellaneous Financial Loss	1,021	938	41	171	499	2,223	115	156
Marine & Aviation	1,641	1,383	422	351	155	-226	55	-131
Motor	16,263	16,237	15,645	15,721	13,116	15,246	9,247	12,880
Engineering	5,715	5,888	2,280	2,174	2,046	37,447	705	1,113
Medical	15,465	12,968	6,419	6,781	7,089	5,300	3,125	2,795
Others	680	6,576	35	3,283	563	5,238	221	1,788
Total	**58,111**	**60,666**	**37,549**	**39,891**	**50,121**	**73,600**	**19,120**	**25,029**

**Provisional Data*
Source: CBB.

Motor insurance has the highest exposure in Gross Premiums (30%), Net Premiums Written (43.7%) and Net Claims (50.5%). In terms of Gross Claims, Fire, Property & Liability insurance line contributes by (36.4%), and Motor by (23.7%).

Chart 6-5: Concentrations of Gross Premiums and Claims for Conventional Insurance by Class - Bahrain Operations (Q1 2018)*



**Provisional Data*

Source: CBB.

Tables 6-3 below and Charts 6-6 and 6-7 shows a further division of the premiums and claims by class between Local and Overseas firms within the conventional insurance industry for Q3 2017. For local conventional insurance, Motor insurance has the highest concentration for Gross Premiums (29.8%) and Net Premiums Written (43.1%) and Net Claims (50.2%).

Table 6-3: Gross Premiums and Claims of for Conventional Local and Overseas Insurance by Class – Bahrain operations (Q1 2018)*

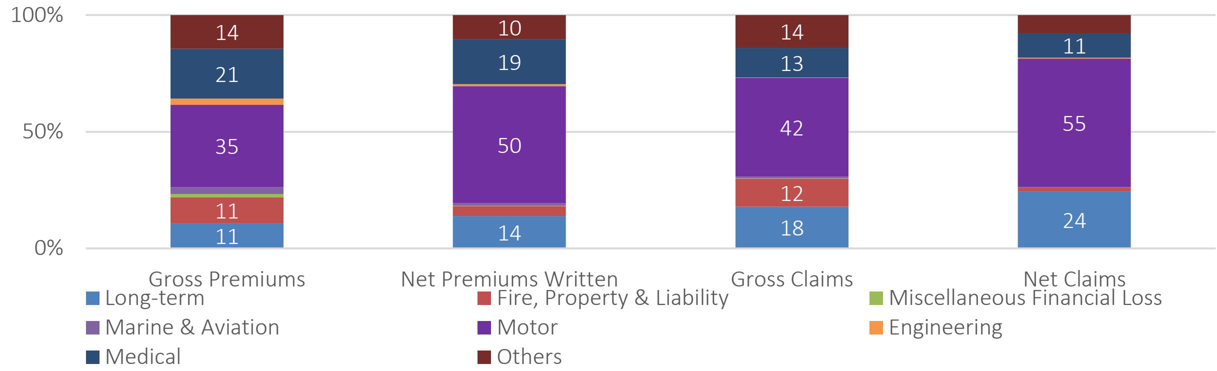
BD '000	Gross Premiums			Net Premiums Written			Gross Claims			Net Claims		
	Local	Overseas	Total	Local	Overseas	Total	Local	Overseas	Total	Local	Overseas	Total
Long-term (Life)	4,619	5,700	10,320	4,039	5,231	9,270	6,022	173	6,195	5,377	165	5,542
Fire, Property & Liability	4,775	1,581	6,356	1,265	873	2,138	4,088	(1,911)	2,177	345	540	886
Miscellaneous Financial Loss	656	282	938	48	124	172	5	2,218	2,223	6	151	156
Marine & Aviation	1,204	179	1,383	292	59	351	243	(469)	-226	70	(201)	-131
Motor	15,264	972	16,237	14,752	969	15,721	14,309	937	15,246	12,131	748	12,880
Engineering	1,082	4,807	5,888	222	1,952	2,174	71	37,376	37,447	75	1,038	1,113
Medical	9,208	3,760	12,968	5,662	1,120	6,782	4,279	1,021	5,300	2,347	449	2,795
Others	6,202	375	6,576	3,013	271	3,284	4,736	502	5,238	1,673	115	1,788
Total	43,010	17,656	60,666	29,293	10,599	39,892	33,753	39,847	73,600	22,024	3,005	25,029

**Provisional Data*

Source: CBB.

.

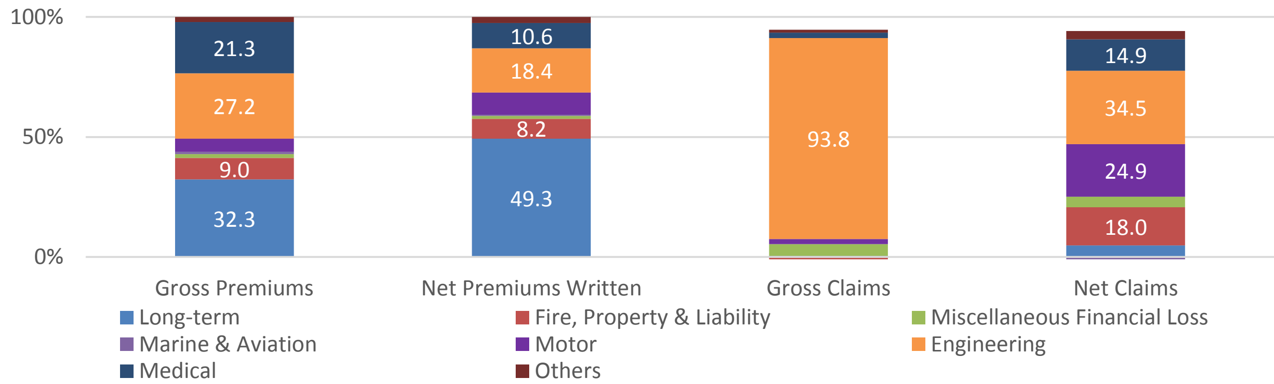
Chart 6-6: Concentrations of Gross Premiums and Claims for Conventional Local Insurance by Class - Bahrain Operations (Q1 2018)*



**Provisional Data*

Source: CBB.

Chart 6-7: Concentrations of Gross Premiums and Claims for Conventiaonal Overseas Insurance by Class - Bahrain Operations (Q1 2018)*



**Provisional Data*

Source: CBB.

Only two foreign overseas branches operations focus more on life insurance and contribute towards the concentration in Gross Premiums (32.3%) and Net Premiums written (49.3%). As For Gross Claims, Engineering business line had the highest share (68.2%).

6.3.3 Takaful

The Gross Premiums for Takaful companies increased on a year-on-year basis by 25.8%, from BD 16.9 million at Q1 2017 reaching BD 21.4 million in 2018, where the highest increase was attributed by Engineering insurance line, followed by Miscellaneous Financial Loss. Medical Insurance line however recorded the highest contributor towards total Takaful gross premiums, accounting for 39.7% of the total.

Net Premiums Written increased by 15.1% from March 2017 to September 2017, reaching BD 14.2 million. Miscellaneous Financial Loss Insurance increased on an annual basis by 139.2%, whereas 'Others' decreased by 60.7%. Medical Insurance is the largest in terms of net premiums written, representing around 47.7% of the total.

Gross Claims increased by 44.6% compared to March 2017, with Life insurance registering the highest increase within the same period. Motor and Medical insurance accounted for the largest components in terms of gross claims, representing 45.4% and 39.3% of the total gross claims.

Net Claims increased at a higher percentage compared to gross claims, recording an annual increase of 54.4% at March 2018, with Life insurance increasing at the highest rate amongst the other classes. However, it equates to the gross claims in terms of having Medical and Motor representing the largest components of net claims, accounting for 50.0% and 45.0% from the total respectively.

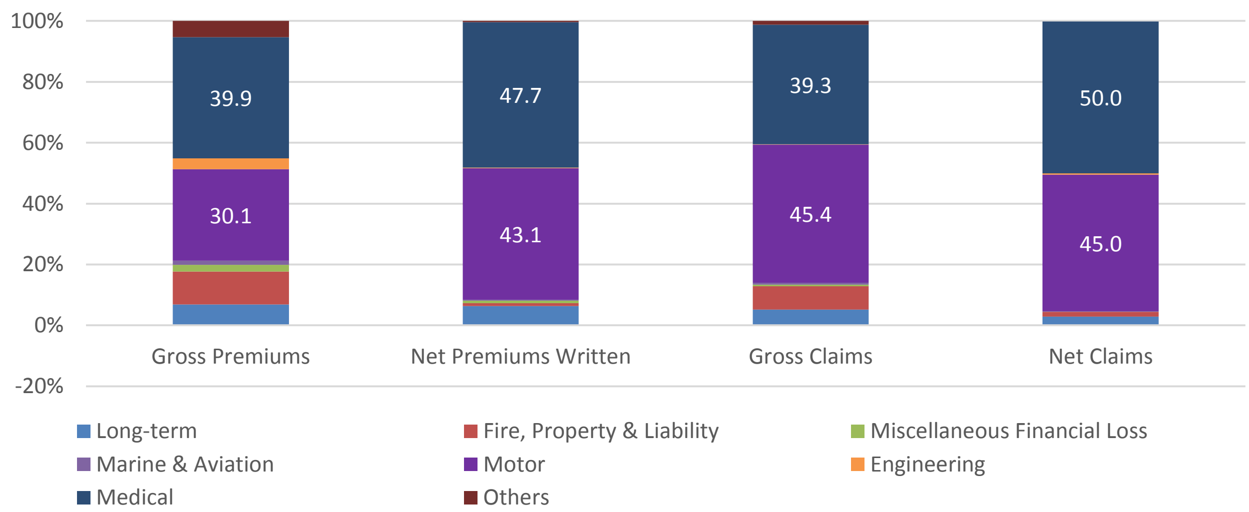
Table 6-4: Gross Premiums and Claims of Takaful Insurance Firms by Class – Bahrain operations*

BD '000	Gross Premiums		Net Premiums Written		Gross Claims		Net Claims	
	Q1 2017	Q1 2018	Q1 2017	Q1 2018	Q1 2017	Q1 2018	Q1 2017	Q1 2018
Long-term (Life)	1,931	1,463	1,404	904	126	480	58	216
Fire, Property & Liability	2,362	2,320	216	131	262	703	32	113
Miscellaneous Financial Loss	256	479	51	122	(32)	54	3	0
Marine & Aviation	223	289	35	50	109	55	19	17
Motor	4,527	6,424	4,325	6,129	3,441	4,190	2,934	3,321
Engineering	349	745	41	39	75	11	14	32
Medical	6,148	8,522	5,138	6,784	1,632	3,629	1,636	3,694
Others	1,203	1,134	145	57	775	112	88	(9)
Total	**16,998**	**21,377**	**11,355**	**14,216**	**6,386**	**9,234**	**4,784**	**7,384**

**Provisional Data*

Source: CBB.

Chart 6-8: Concentrations of Gross Premiums and Claims for Takaful Insurance Firms by Class - Bahrain Operations (Q1 2018)*



**Provisional Data*

Source: CBB.

Takaful insurance companies have very high concentration on the Medical and Motor Insurance business lines. Gross Premiums for both sectors combined represents 69.9%, Net Premiums Written (90.8%), Gross Claims (84.7%), and Net Claims (95.0%).

6.3.4 Retention Ratio and Loss Ratio (By Class)

Life insurance business line registered a retention ratio of 89.7% in March 2018. Observing the non-life insurance, Motor and Medical, accounted for 27.6% and 26.2% of the total Gross Premiums in March 2018 respectively, registered retention ratios of 96.4% for Motor and 63.1% for Medical. Nevertheless, retention ratios were significantly lower for other business lines such as Miscellaneous Financial Loss and Marine & Aviation, registering 20.7% and 24.0% respectively.

Table 6-5: Retention and Loss Ratios of Overall Insurance Sector*

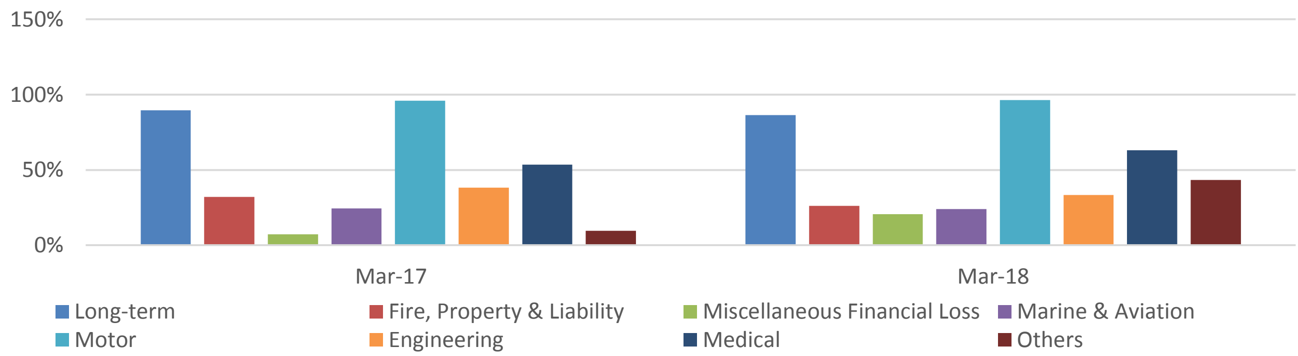
	Retention Ratio 1		Loss Ratio 2	
%	Mar-2017	Mar-2018	Mar-2017	Mar-2018
Long-term	89.6	86.4	43.5	55.3
Fire, Property & Liability	32.0	26.2	41.2	53.9
Miscellaneous Financial Loss	7.2	20.7	89.3	91.5
Marine & Aviation	24.5	24.0	20.2	-32.6
Motor	96.1	96.4	65.6	79.1
Engineering	38.3	33.4	33.5	129.1
Medical	53.3	63.1	60.1	70.1
Others	9.6	43.3	128.9	52.4

1. Net Premiums Written / Gross Premiums
2. Net Claims Incurred/Net Premiums Earned

Provisional Data

Source: CBB.

Chart 6-9: Retention and Loss Ratios of Insurance Sector*



Provisional Data

Source: CBB.

6.4 Insurance Profitability:

Net income decreased across all different categories, as conventional insurance firms' net income decreased from BD 11.4 million in March 2017 to BD 8.1 million in March 2018, whereas Takaful companies showed a slight drop of -5.6%.

Table 6-6: Profitability Indicators of Insurance Sector*

BD'000	Net Income after taxes *		Total Assets*		Capital Available * As per CBB requirements	
	March -17	March-18	March -17	March -18	March -17	March -18
Conventional	11,378	8,058	2,061,496	2,206,473	322,377	358,566
Local	10,177	5,797	1,920,543	1,799,904	297,256	335,811
Overseas	1,201	2,262	285,930	261,592	25,122	22,755
Takaful	1,135	1,071	184,034	158,043	59,654	48,722
All Insurance	12,513	9,130	2,390,507	2,219,539	382,031	407,288

*including results of Shareholders and Participants Funds.

**Provisional Data*

Source: CBB.

Conventional insurance firms' total assets increased by 7%, from BD 2,061.5 million March 2017 to BD 2,206.5 million March 2018. However, takaful companies' total assets dropped from BD 184.1 million March 2017 to BD 158.1 million in March 2018. Therefore, total assets dropped slightly for the entire insurance industry to BD 2,219.6 million. The capital available however experienced an increase for the entire industry, increasing from BD 382.1 million to BD 407.3 million.

6.5 Regulatory Changes, Market trends and Risks.

As part of the efforts towards enhancement and improvement of the regulatory framework, the CBB introduced its revised and enhanced Operational and Solvency framework for the Takaful and Retakaful industry in 2014 after undergoing deliberations and consultations with the industry and all the stakeholders.

The problem was that many Takaful firms incurred regulatory deficits in the participants funds for many years despite the fact that CBB gave Takaful and Retakaful firms a transition period of 5 years to assist participants funds in building their own capital. The regulatory deficit arises from the fact that the required capital of the participants' funds usually exceeds the available capital of the participants fund especially in the early years of the funds.

The solution to the problem was to combine both the capital of the shareholders and the capital of the participants in the calculation of the capital available and then compare it with the required capital of the funds. Accordingly, the CBB has amended its rules and regulation to give the effect of such in order to achieve the following main objectives:

- Enhance the competitiveness of the Takaful industry in Bahrain;
- Enhance the public's confidence in Takaful;

- Reduce the burden on Takaful firms in relation to the calculation of available capital and therefore, enabling Takaful firms to be in a level playing field with conventional insurance firms in relation to solvency assessment;
- Eliminate the need for Qard Hassan to address any regulatory deficit and replace it with capital injection from shareholders;
- Increase the probability of surplus distribution to participants;
- Provide more flexibility to participants funds to invest its funds rather than merely concentrating on meeting the solvency requirements; and
- Address gaps associated with the application of a Takaful model such as the availability of liquid assets in the shareholders fund to cover any deficit in participants' funds, standardization of Wakalah fee components and the impairment of Qard Hassan.
-

It is worth to mention that the CBB continue reviewing and analyzing the updated Takaful Returns submitted by the Takaful Firms to monitor the effect of the new rules which actually show positive financial results in recent years.

7. Performance of Capital Markets

Chapter 7

Key Points

- Decrease in the Bahrain All Share & Islamic Indices.
- Year-on-year increase in market capitalization.
- Increase in corporate profitability and decrease in leverage.
- GCC equities remain sluggish.

7.1 Overview

This chapter provides an overview of the capital markets sector in the Kingdom of Bahrain. Furthermore, this chapter will provide statistical insights as to the performance of the mainboard market operated by Bahrain Bourse as a Self-Regulatory Organization ("SRO") as well as relevant data on the issuance of securities and activities pertaining to takeovers, mergers and acquisitions in Bahrain.

In 2002 Bahrain expanded and centralized the scope of the financial sector regulatory supervision to encompass capital markets under the CBB's Capital Markets Supervision Directorate ("CMSD") supervisory umbrella. Henceforth, with the inception of the integrated regulator approach referred to as the "Single Regulatory Model", the CBB became responsible for Bahrain's capital markets with a combination of rule and principle based regulatory framework.

As at June 2018, Bahrain Bourse recorded a total listing of 43 Companies, 18 Mutual funds and 15 Bonds and Sukuks. "Commercial Banks" sector represents the highest value in traded shares by scoring 32.4% of total shares. Nevertheless, the largest 5 companies in terms of Market Capitalization are AUB, ALBH, NBB, GFH, and BBK which account for 56.5% of the total market.

7.2 Bahrain Bourse

Decrease in market index

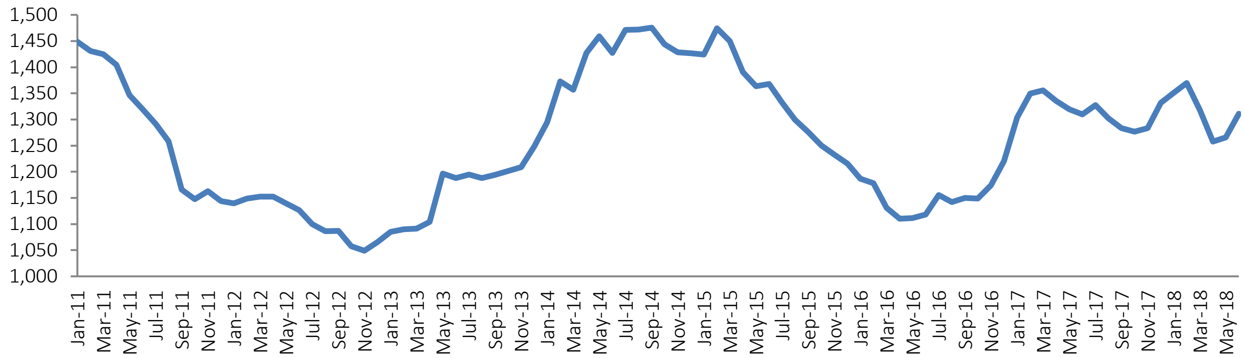
Year-on-year data demonstrates that the Bahrain All Share Index increased by 0.95 points (0.1%) between June 2017 and June 2018 (Table 7-1). Observing this period, the index was at its highest with 1,369.9 points in February 2018, where the index began to drop until May 2018 where the index scored the lowest point at 1,257.9. Subsequently, the index started to increase reaching 1,311.0 by June 2018 (Chart 7-1). When comparing on a month on month basis, the index increased from 1,265.8 in May 2018 to 1,310.9 in June 2018 (3.6%).

Table 7-1: Key Indicators of Bahrain Bourse

	2012	2013	2014	2015	2016	2017	H1 2018
All Share Index	1,065.6	1,248.9	1,426.6	1,215.9	1,220.5	1,331.7	1,311.0
Highest	1,152.8	1,248.9	1,476.0	1,474.8	1,220.5	1,356.0	1,369.9
Lowest	1,048.8	1,085.9	1,294.3	1,215.9	1,110.5	1,276.7	1,257.9
Market Cap (BD, mil)	5,855.6	6,963.0	8,327.1	7,199.9	7,248.2	8,146.3	8,037.5
Total Value (BD, mil)	110.2	225.9	269.1	110.0	124.5	211.3	127.9
Total Volume (mil)	627.7	1,867.8	1,126.1	515.6	734.4	1,129.8	684.4
No. of Transactions	10,168	14,197	16,211	11,248	10,592	19,440	9,359
No. of Companies Listed	47	47	47	46	44	43	43

Source: Bahrain Bourse.

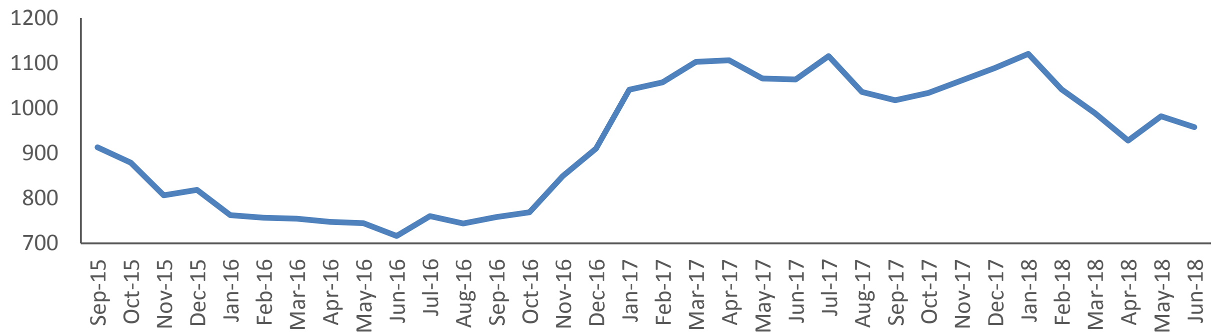
Chart 7-1: Bahrain All-Share Index, Jan 2012-June 2018



Source: Bahrain Bourse.

In September 2015, Bahrain Bourse launched the Bahrain Islamic Index. It was the first Islamic finance index in the region, and 17 Shari'ah compliant companies are included within the index. Since its inception, most movements in Bahrain Islamic Index have mirrored that of the Bahrain All-Share Index albeit with different volatilities. Year-on-year data demonstrates that the Bahrain Islamic Index decreased by 105.8 points (9.9%) between June 2017 and June 2018 reaching 958.1 points (Chart 7-2).

Chart 7-2: Bahrain Islamic Index, Sep 2015-Jun 2018



Source: Bahrain Bourse.

Decrease in market capitalization

As at end-June 2018, market capitalization of the Bahrain Bourse stood at BD 8.04 billion (Table 7-2). This level of market capitalization is 1.3% lower than the level attained in December 2017 and 3.4% higher year-on-year.

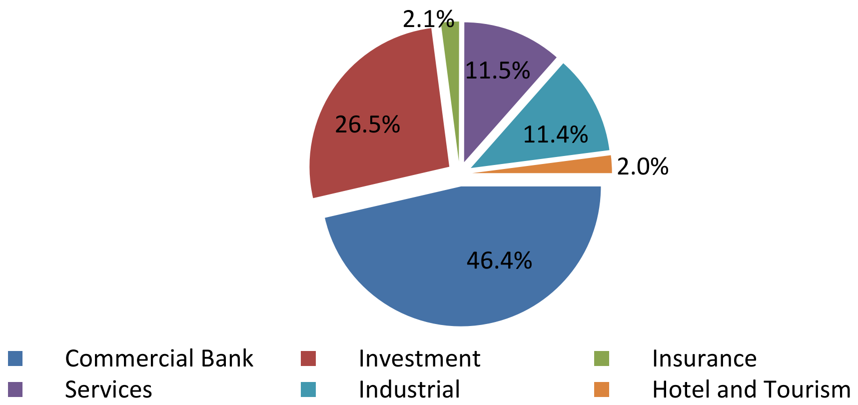
Table 7-2: Market Capitalization on the Bahrain Bourse

Sector BD	Jun. 2017	Dec. 2017	Jun. 2018	Dec. 2017-Jun. 2018 (% Change)	Jun. 2017-Jun. 2018 (% Change)
Commercial Banks	3,838,055,221	3,938,944,714	3,729,239,933	(5.3)	(2.8)
Investment	2,004,042,161	2,124,858,983	2,133,404,982	0.4	6.5
Insurance	148,489,778	157,250,245	167,672,100	6.6	12.9
Services	952,755,246	869,030,783	923,341,428	6.3	(3.1)
Industrial	667,092,314	891,787,040	919,378,298	3.1	37.8
Hotel and Tourism	166,504,926	164,461,880	164,461,880	0.0	(1.2)
Total	**7,776,939,646**	**8,146,333,645**	**8,037,498,621**	**(1.3)**	**3.4**

Source: Bahrain Bourse.

A breakdown of market capitalization by sector indicates that "Industrial" sector recorded the highest year-on-year increase in market capitalization (37.8%) followed by "Insurance" (12.9%) and "Investment" (6.5%). "Industrial" scored the highest decline among other market capitalization sectors with a 3.1% decrease.

Chart 7-3: Market Capitalization by Sector, June 2018



Source: Bahrain Bourse.

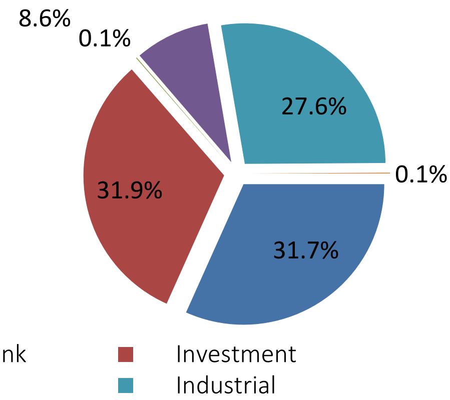
The bulk of the value of shares traded in June 2018 was the "Investment" sector whose traded shares (by value) represented 31.9% of total shares, which is a significant increase to what was attained in June 2017. The "Commercial Banks" sector represents the second greatest level at 31.7% of the total value of shares traded in June 2018, which remained close to the levels recorded in June 2017. Investors interest in "Hotel and Tourism" and "Insurance" sectors were the least during June 2018 whose traded shares by value represented only 0.2% of total traded shares (Table 7-3).

Table 7-3: Sectoral Distribution of Shares Traded by Value (% of all shares traded)

Sector	Jun. 2017	Dec. 2017	Jun. 2018
Commercial banks	31.6	54.8	31.7
Investment	14.6	15.3	31.9
Insurance	2.6	0.1	0.1
Services	20.4	16.0	8.6
Industrial	30.6	13.7	27.6
Hotel and Tourism	0.4	0.1	0.1

**Figures may not add to a hundred due to rounding.*
Source: Bahrain Bourse.

Chart 7-4: Sectoral Distribution of Shares Traded by Value (% of all shares traded) in June 2018



Source: Bahrain Bourse.

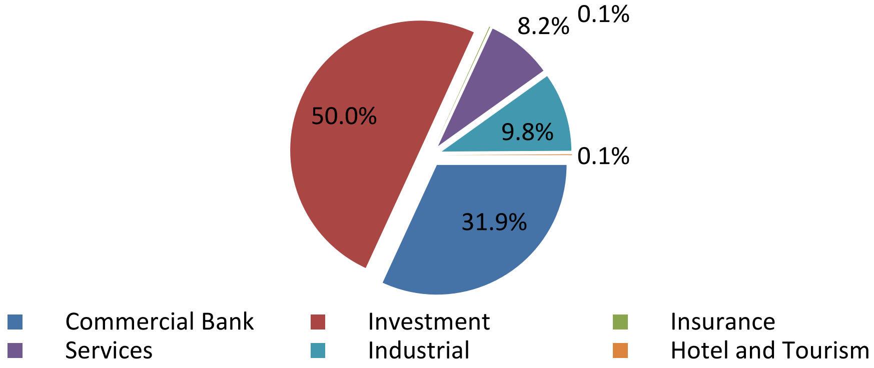
The bulk of the volume of shares traded in June 2018 was the "Investment" sector representing 50.0% of the total volume of shares traded, followed by the "Commercial Banks" sector at 31.9%. The lowest level was attained by the "Hotel and Tourism" and "Insurance" sectors at 0.1% each (Table 7-4).

Table 7-4: Sectoral Distribution of Shares Traded by Volume (% of all shares traded)

Sector	Jun. 2017	Dec. 2017	Jun. 2018
Commercial banks	41.0	71.4	31.9
Investment	24.2	15.7	50.0
Insurance	6.0	0.1	0.1
Services	11.8	9.1	8.2
Industrial	16.9	3.7	9.8
Hotel and Tourism	0.2	0.1	0.1

**Figures may not add to a hundred due to rounding.*
Source: Bahrain Bourse.

Chart 7-5: Sectoral Distribution of Shares Traded by Volume (% of all shares traded) –June 2018



Source: Bahrain Bourse.

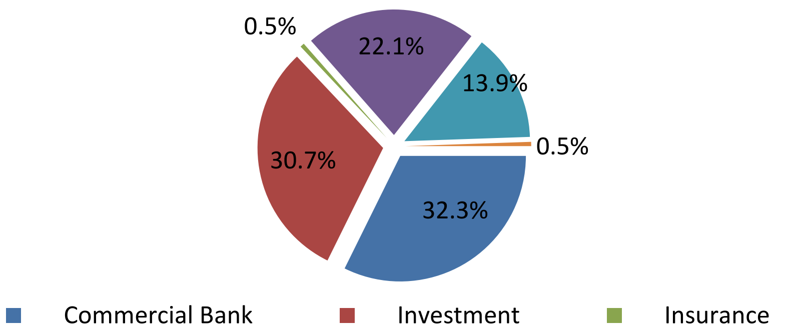
The majority of the number of transactions in June 2018 (1,104 transactions and a 38.2% decrease compared to December 2017) was attained by the "Commercial Banks" sector at 356 transactions (32.2% of all transactions), followed by the "Investment" sector at 338 transactions (30.7%), and the "Services" sector at 243 transactions (22.0%) (Table 7-5).

Table 7-5: Number of Transactions by Sector

	Jun. 2017	Dec. 2017	Jun. 2018
Commercial Banks	290	931	356
Investment	146	231	338
Insurance	42	12	6
Services	257	507	243
Industrial	176	99	153
Hotels and Tourism	15	6	8
Total	**926**	**1,786**	**1,104**

Source: Bahrain Bourse.

Chart 7-6: Sectoral Distribution of Number of Transactions Traded (% of all transactions traded) in June 2018



Source: Bahrain Bourse.

GCC Indices remain sluggish

The GCC equity markets was sluggish during 2018 due to a combination of geopolitical factors and some unforeseen events. As a result, some GCC indices recorded negative rates compared to December 2017.

Despite this, the highest increase was recorded by the Tadawul All Share Index (12.0%) when compared to June 2017, followed by the Kuwait Market Index with an increase of 4.5%.

Table 7-6: Stock Market Indices in GCC counties

Index	Jun. 2017	Dec. 2017	Jun.2018*	Dec. 2017 - Jun 2018 (%)	Jun. 2017 – Jun. 2018 (%)
Bahrain All Share Index	1310.0	1331.7	1311.0	(1.6)	0.1
Tadawul All Share Index	7425.7	7226.3	8314.2	15.1	12.0
Kuwait Market Index	5205.4	5244.3	5438.7	3.7	4.5
Qatar Exchange Index	9030.4	8523.4	9024.0	5.9	(0.1)
Dubai Financial Market Index	3537.4	3370.1	2821.0	(16.3)	(20.3)
Abu Dhabi Exchange General Index	4425.4	4398.4	4560.0	3.7	3.0
Muscat Securities Market Index 30	5118.3	5099.3	4571.8	(10.4)	(10.7)

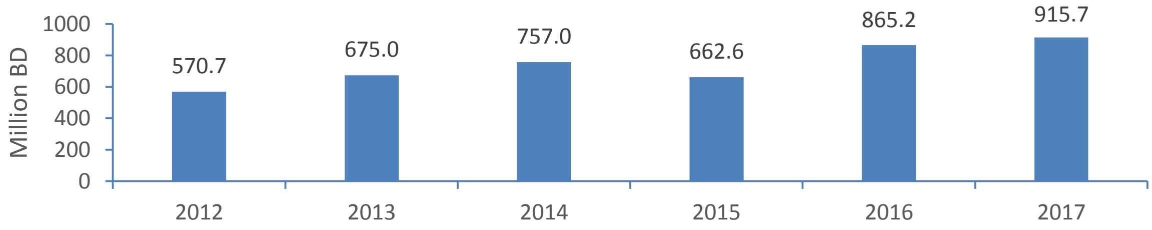
*June 30th, or latest available.
Sources: Bahrain Bourse, Saudi Stock Exchange (Tadawul), Boursa Kuwait, Qatar Stock Exchange, Dubai Financial Market, Abu Dhabi Exchange, and Muscat Securities Market.

7.3 Market Resilience

Increase in corporate profitability

The overall profitability of the Bahraini stock market increased by 5.8% to BD 915.7 million in 2017 from BD 865.2 million in 2016. Return on assets increased to 1.6% in 2017 compared to 1.5% in 2016, while return on equity rose to 9.5% in 2017 compared to 9.1% in 2016.

Chart 7-7: Stock Market Net Income



Source: Bahrain Bourse.

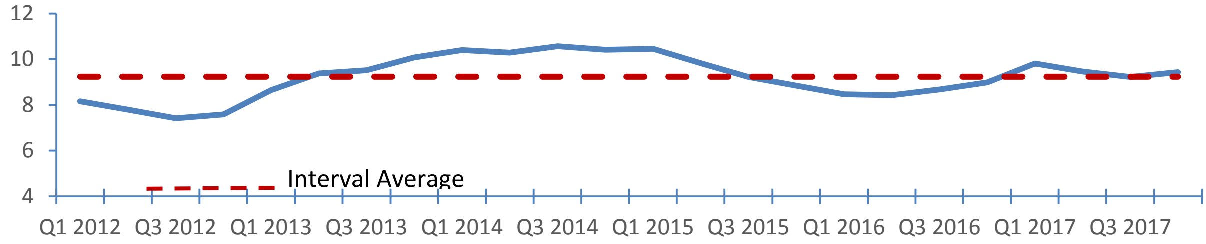
As at June 2018, all sectors experienced progress in their P/E ratio compared to December 2016 except for the Commercial Banks and Industrial sectors that dropped by 13.0% and 47.8% respectively. The total market P/E ratio in the fourth quarter of 2017 was at 9.4, a bit higher than the 6 year average and remains at the same level recording 9.5 in June 2018 (Chart 7-8) (Table 7-7).

Table 7-7: Price-Earnings Multiples

Sector	Jun. 2017	Dec. 2017	Jun. 2018
Commercial banks	10.5	10.8	9.4
Investment	6.8	5.6	8.5
Insurance	13.4	14.2	21.5
Services	11.4	10.4	11.7
Industrial	13.3	17.8	9.3
Hotel and Tourism	7.6	7.7	10.7
Total Market	9.5	9.4	9.5

Source: Bahrain Bourse.

Chart 7-8: Total Market Price-Earnings Multiples

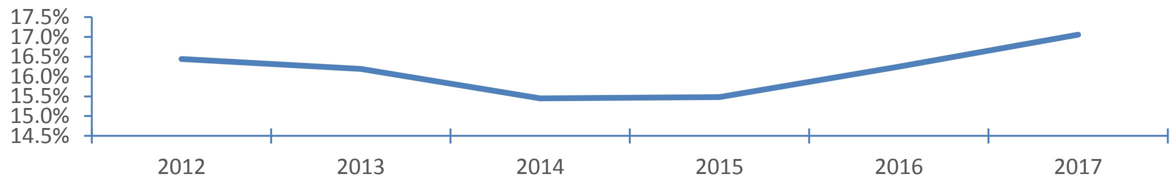


Source: Bahrain Bourse.

Corporate leverage decreased

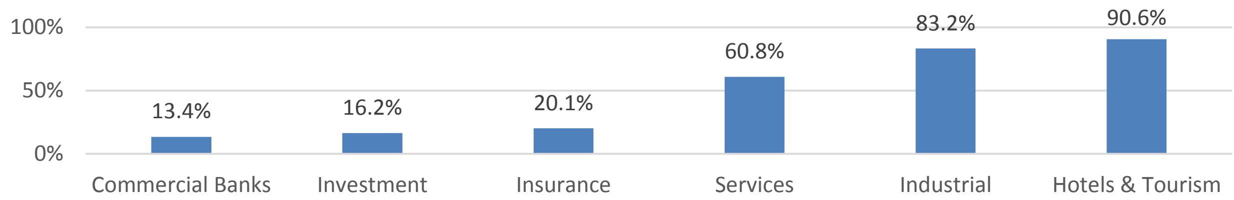
The overall equity-to-assets ratio increased by 3.6% to 17.1% in 2017. Most sectors contributed to the increase with the Hotel and Tourism sector having the highest increase (10%). The Commercial Banks and Investment sectors have the lowest equity/assets ratio due to the high leverage nature of the sectors (Chart 7-9 & 7-10).

Chart 7-9: Total Equity to Total Assets (%)



Source: Bahrain Bourse.

Chart 7-10: Total Equity/Total Assets by Sector

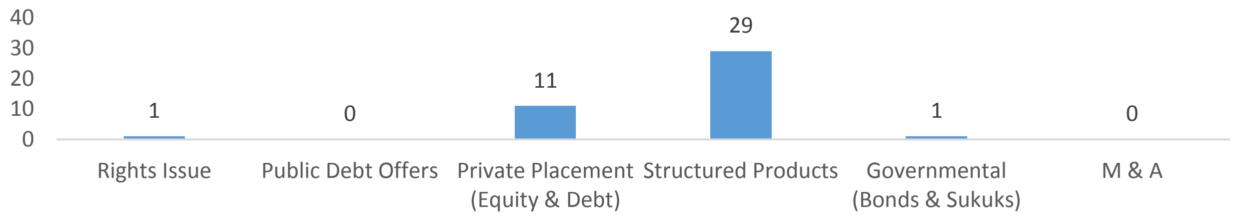


Source: Bahrain Bourse.

7.4 Capital Market Activities

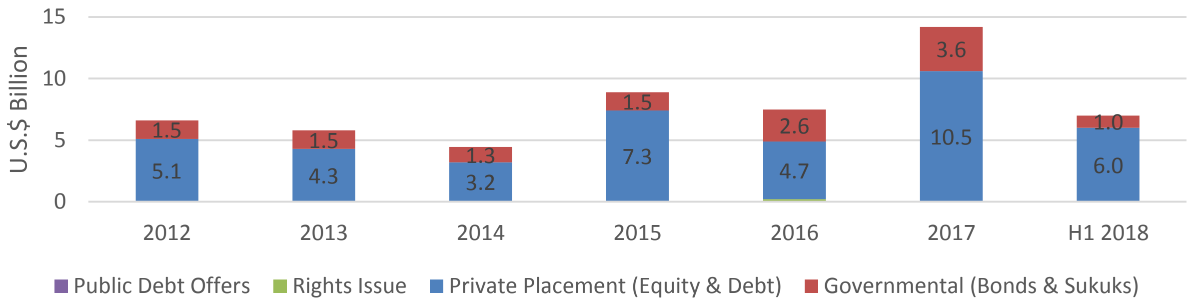
As of June 2018, the CBB issued its no objection to the issuance of 42 public and private offering documents after ensuring the completeness of all the information and details as per the CBB Law, Rules and Regulations. The total value of issuances reached USD 6.1 billion. (Chart 7-11 & 7-12).

Chart 7-11: Number of Capital Market Activities



Source: CBB.

Chart 7-12: Total Issuance Value

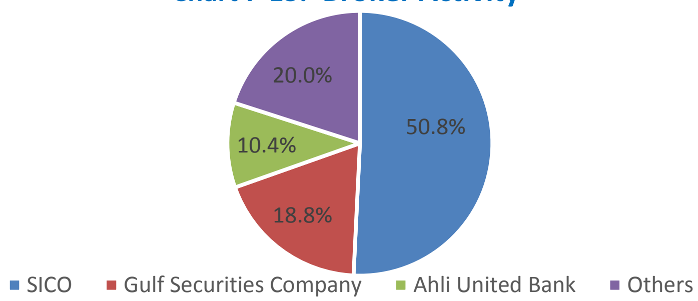


Source: CBB.

7.5 Performance of Brokers

For 2018, Bahrain Bourse had 13 active brokers conducting trades in the market. Securities and Investment Co. (SICO) was the top broker in terms of total value of shares traded with more than 50% of the total market value in 2018, while the top three made up 80.0% of the total market.

Chart 7-13: Broker Activity



Source: Bahrain Bourse.

7.6 Mutual Funds

Bahrain Bourse adopts simple listing requirements for mutual funds interested in listing, which positions Bahrain as a safe haven to a thriving mutual funds industry. As at June 2018, there are 18 Open-End mutual funds listed by the Bahrain Bourse with an average net asset value (N.A.V) of USD 77.8. The Khaleej Equity Fund has the highest N.A.V listed at USD 273.7.

7.7 Risks & Challenges in Capital Markets

The significance of cybersecurity risk on capital markets cannot be overlooked, given the developing landscape of the global markets, which decrees that regulators and capital market service providers must remain prudent, progressive, and vigilant to minimize such risks. In this regard, the CBB; through the requirements stipulated under Module of CBB Rulebook Volume 6 requires Licensees to have in place a well-designed Disaster Recovery Plan. It must also maintain at all times a plan of action (referred to as a business continuity plan) that sets out the procedures and establishes the systems necessary to restore fair, orderly and transparent operations, in the event of any disruption to the operations of the market.

Moreover, the regulatory framework for capital markets recognizes the significance of cybersecurity in the area of operating an equity crowdfunding platform and requires such operators to ensure that cyber-security includes the conduct of an IT security penetration test semi-annually by an independent consultant (discussed in part III of the report). In addition, Capital markets licensees are mandated to maintain relevant systems in place for mitigating and managing operational and other risks.

Among the shared goals of the CBB and the Bahrain Bourse at the moment is to increase liquidity and the number of investors in the market. Such an increase would mean a greater amount of due diligence and responsibility for the CBB as it aims to ensure that all stakeholders involved are aware and adhering to the rules and regulations. Meanwhile, listed companies are also aiming to increase liquidity and trading in their own shares by cross listing in multiple exchanges. Consequently, such initiatives bring about their own set of regulatory risks that the CBB tackles.

The FinTech solution are increasingly affecting the Capital Markets, these changes are being reflected on different areas including: the core infrastructure that connects investors/clients with the intermediaries through blockchain technologies, post-trade and settlement digitization and innovative technology driven business models. These FinTech driven changes will lead to reduction in overall risks due to further transparency and reduction of systematic risk. In order to effectively reduce risks related to use of FinTech solutions, the CBB is working towards further entertaining the regulatory framework pertaining to data security, legal framework of data usage, creating robust compliance and regulatory reporting and increasing partnership between financial institutions, FinTech services providers and the regulator. Another key area of focus for the CBB is Regulatory Technology (RegTech) which could be used to regulate the FinTech in the Capital Markets.

7.8 Developments in Regulation and Initiatives

In addition to the participation in joint work meetings of the GCC that aim to harmonize the rules and regulations for the Capital markets in the GCC. During the year 2017, the CBB's CMSD endeavoured to develop and complete the capital markets regulatory and legal frameworks, including Volume 6 of the CBB Rulebook, its main objectives being to enhance transparency, develop the capital markets, and protect investors. The following section will shed light on the activities that took place in the areas of policy, regulation and market infrastructure in 2017:

7.8.1 Policy and Regulatory Developments

- **Amendments of the Offering of Securities ("OFS") Module of CBB Rulebook Volume 6 :** In line with CMSD circular CMS/L373/17 dated 4th December 2017, all listed companies are required to comply with Paragraph OFS-2.6.7 of the OFS Module in relation to the Employee Stock Option Plan ("ESOP") which stipulates that all listed companies securities held on behalf of the employees under an employee stock option plan or employee share benefit plan, must be held in trust by a trustee subject to the prior written approval of the CBB. The same has been successfully effected during the first quarter of the year 2018.
- **Bahrain Bourse ("BHB") Listing Rules:** The BHB has completed the final draft of Listing Rules in consultation with the CBB and the industry. Along with the Listing Rules, BHB in consultation with the CBB will release the Listing Guidelines which sets further guidelines for listing.

- **Clearing, Settlement and Central Depository Rules:** Bahrain Clear (BHC) Clearing, Settlement and Central Depository Rules are being finalised in cooperation with consultants and the CBB.

- **Resolution No. 11 of 2018:** The CBB issued Resolution No. (11) of 2018 in respect of "Procedures and Rules for the implementation of the Self-Regulatory Organization (SRO) model of the Exchanges licensed by the Central Bank of Bahrain in relevance to the listing of securities and financial instruments post its initial public offering in the Official Gazette No. 3355 dated 1st March 2018. The resolution provides a legal and regulatory framework in relation to the initial listing of securities and financial instruments. The CMSD will continue to review public offering and listing requests concurrently with the licensed exchange, and to approve the registration of the prospectus, providing guidance and support to interested parties and persons in coordination with the relevant exchange.

7.8.2 The Capital Markets Supervision Directorate's Upcoming Initiatives

- **Short Selling and Giving Securities on Loan:** With the aim to further enhance the regulatory framework for the capital markets sector and in accordance with the requirements of the CBB Law in general and Article (92) in particular, the CBB has issued a draft regulation for short selling & giving securities on loan. The draft regulation was issued for industry consultation and the CBB is looking to finalize the same after accounting for the feedback received.

- **Financial and Administrative Sanctions:** The CMSD's regulatory mandate is to set and enforce high quality capital market industry standards, protect investors and strengthen market integrity while supporting a stimulating capital markets' ecosystem. The Investigation and Enforcement ("IE") team within the CMSD assumes responsibility to ensure effective enforcement of the CBB regulatory requirements with an objective to achieve fairness, transparency, investor protection and safeguard public interests in the Kingdom of Bahrain. In line with the CMSD's objective to develop a transparent regulatory environment, the CMSD produced the second issue of its Compliance & Enforcement Annual Report covering the year 2017; which provides a comparative overview of CMSD's efforts in 2015-2017 to identify and address non-compliances, negligence or misconduct, by accounting for all market participants in order to enact the word of the law, safeguard the interests of all stakeholders and ensure a stimulating environment within which the needs of members, investors and the regulator are met.

- **Press Release Pertaining to Financial Statements of listed companies:** The CMSD has proposed new requirements for the publication of press releases that cover financial results of public listed shareholding companies. A template was drafted to standardize the content of press releases amongst listed companies, and ensure that companies report to their shareholders in an objective and unbiased perspective. The template requirements include material information that reflect the main outcomes of the financial statement. The proposed requirements were open for consultation, as the template was shared with the listed shareholding companies for their feedback. The remarks have been collected and replied to, and CMSD is in the finalizing stage.

- **Market Maker Rules:** The market maker, in general, adds to the stability, liquidity and transparency of the capital markets and is therefore a desirable participant. They also are participants in quote-driven financial instruments trading environment that fulfil the function of generating bids and offers. Accordingly, the CMSD will be introducing new rules for market makers within the CBB Rulebook Volume 6, Market & Exchange Module, and Market

Intermediaries and Representatives Module, to ensure these participants operate with higher efficiency, fairness and transparency.

- **Tick Size:** A letter has been issued to the Bahrain Bourse approving the implementation of new tick sizes for a trial period starting on the 2nd September 2018 to 2nd December 2018. During the period, the effects of the changes in tick sizes will be studied and analysed to measure its effect on the stock exchange (whether positive or negative).

- **Islamic Securities Resolution** The objective of the CMSD is to continue to ensure investor protection and to further enhance the regulatory framework for the capital markets sector in the Kingdom of Bahrain. Therefore, the CMSD is in the process of drafting a resolution outlining the necessary requirements for the offering and issuance of Islamic securities, including ongoing reporting and disclosure obligations.

- **Treasury Shares Resolution:** Further to Article (93) of the Central Bank of Bahrain and Financial Institutions Law, the CMSD is currently in the process of introducing a resolution to regulate the purchase and sale of listed companies' treasury shares and the permitted uses for these shares.

Part IV:

Developments in the Payment Systems, FinTech, and Cyber Security

8. Payment and Settlement Systems

Chapter

8

Key Points

- The Payment and Settlement Systems in the Kingdom of Bahrain continue to function safely and efficiently.
- Oversight on Payment and Settlement Systems is of the primal tools that ensures stability of the financial system and efficiency of payment transactions.
- Payment and Settlement Systems have undergone crucial changes from the standpoint of products complexity and a range of payment products offered in recent years.
- FinTech challenges to Payment and Settlement Systems.

8.1 Overview

Payment and Settlement Systems are central to the smooth operations of the financial sector and the efficient functioning of the overall economy. Therefore, the safety and soundness of Payment and Settlement Systems is important for the evaluation of risks to financial stability.

Payment and settlement systems are a crucial part of the financial infrastructure of a country. Bahrain's Payment and Settlement Framework continues to function safely, securely and efficiently. The current Payments and Settlement infrastructure in the Kingdom of Bahrain comprises of five main components: i) the Real Time Gross Settlement System (RTGS); ii) the Scripless Securities Settlement System (SSSS); iii) the ATM Clearing System (ATM); iv) the Bahrain Cheque Truncation System (BCTS) and v) the Electronic Fund Transfer System (EFTS) including the Electronic Bill Presentment and Payment (EBPP) System.

Since the launch of the EFTS in 2015 by the Benefit Company, which has been overseen by the CBB, there has been increasing numbers of EFTS service providers reaching a total of twenty-six (26) participants as of 2018. The CBB assess the EFTS in terms of compliance with the requirements set by the Principles for Financial Market Infrastructures (PFMI) and CBB's Directives.

Bahrain's position in the financial services sector will enable it to become a strategic leader in international financial technology as it provides many of the features that will support the development of a supportive environment for financial technology, including a CBB regulator, innovative human capital, and an advanced ICT infrastructure. The CBB operates and manages the national payment and settlement systems in the Kingdom of Bahrain.

This chapter describes recent trends in the Payment and Settlement Systems.

8.2 Real Time Gross Settlement System (RTGS)

The CBB operates a Real Time Gross Settlement (RTGS) System where all inter-Bank payments are processed and settled in real time on-line mode which went live on the 14th of June, 2007. The RTGS System provides for Payment and Settlement of Customer transactions as a value addition.

The RTGS System enables the Banks to have real time information on, for example, account balances, used and available intra-day credit, queue status, transaction status etc. The RTGS System is multi-currency capable and based on Straight Through Processing (STP). The number of direct participants in the RTGS are twenty-nine (29) participants including the CBB (CBB).

The daily average volume of Bank transfers from 1st January, 2018 to 30th June, 2018 (first half of 2018) have increased by 1.1% to 176 transfers compared to 174 transfers for the period from 1st July, 2017 to 31st December, 2017 (second half of 2017). Furthermore, the daily average volume of Bank transfers for 1st January, 2018 to 30th June, 2018 decreased by 7.4% from 190 transfers to 176 transfers when compared to 1st January, 2017 to 30th June, 2017 (first half of 2017).

As the daily average volume of Bank transfers through the RTGS are decreasing, the value of those transfers have also decreased in the first half of 2018 by 0.1% when compared to the second half of 2017 from BD318.7 million to BD318.4 million. Moreover, the daily average value of Bank transfers for the first half of 2018 increased by 18.4% from BD268.9 million to BD318.4 million when compared to the first half of 2017.

Table 8-1: RTGS Bank Transfers Daily Average Volume and Value

RTGS	Daily Average Volume	Daily Average Value (BD million)
1st July, 2015 to 31st December, 2015	408	202.2
1st January, 2016 to 30th June, 2016	288	226.2
1st July, 2016 to 31st December, 2016	227	259.3
1st January, 2017 to 30th June, 2017	190	268.9
1st July, 2017 to 31st December, 2017	174	318.7
1st January, 2018 to 30th June, 2018	176	318.4

Source: CBB.

8.3 Scripless Securities Settlement System (SSSS)

The CBB operates and oversees Scripless Securities Settlement System (SSSS) that provides the Depository and Settlement Services for holdings and transactions in Government Securities including Treasury Bills (T-Bills), Governments Bonds and Islamic Securities (Sukuk). Moreover, the SSSS went live on the 14th of June, 2007 along with the RTGS System.

The number of direct participants are twenty-nine (29) participants and indirect participants are thirty-five (35) members in the SSSS.

The volume of issues for 1st January, 2018 to 30th June, 2018 decreased compared to 1st July, 2017 to 31st December, 2017 by 7.8% from 51 issues to 47 issues. Moreover, the volume of issues has increased in the first half of 2018 by 23.7% compared to the first half of 2017 from 38 issues to 47 issues.

The aggregate value of issues for the first half of 2018 decreased by 19.9% from BD4.43 billion in second half of 2017 to BD3.55 billion. Additionally, the aggregate value of issues for the first half of 2018 increased when compared to the first half of 2017 by 45.5% from BD2.44 billion to BD3.55 billion.

Table 8-2: SSSS Aggregate Volume and Value

SSSS	Aggregate Volume	Aggregate Value (BD billion)
1st July, 2015 to 31st December, 2015	45	3.04
1st January, 2016 to 30th June, 2016	41	2.65
1st July, 2016 to 31st December, 2016	43	3.06
1st January, 2017 to 30th June, 2017	38	2.44
1st July, 2017 to 31st December, 2017	51	4.43
1st January, 2018 to 30th June, 2018	47	3.55

Source: CBB.

The volume of issues did not pose problems to the System's processing capacity and the risk of significant participant's failure is minimised due to executing and settling in Real Time Gross Settlement System (RTGS).

The SSSS continued to operate smoothly and efficiently for the period from 1st January, 2018 to 30th June, 2018.

8.4 ATM Clearing System (ATM)

ATM clearing is based on a Deferred Net Settlement (DNS) system. The Benefit Company (BENEFIT) in Bahrain receives and processes all the ATM transactions. The GCC net, a leased line network across the GCC countries, provides for the communication backbone for the transmission of all the ATM transactions and settlement related electronic messages (source: BENEFIT website).

The daily average volume of ATM transactions for the 1st January, 2018 to 30th June, 2018, increased by 11.6% to 51,948 transactions per day compared to 46,549 transactions per day for 1st July, 2017 to 31st December 2017. In addition, the daily average volume of ATM transaction increased by 15.6% when comparing the two periods 1st January, 2018 to 30th June, 2018 with 1st January, 2017 to 30th June, 2017.

The daily average value of ATM transactions for the first half of 2018 increased by 13.6% from BD4.4 million in the second half of 2017 to 5.0 million. Furthermore, the daily average value of ATM transactions for the first half of 2017 also increased by 13.6% compared to the first half of 2017.

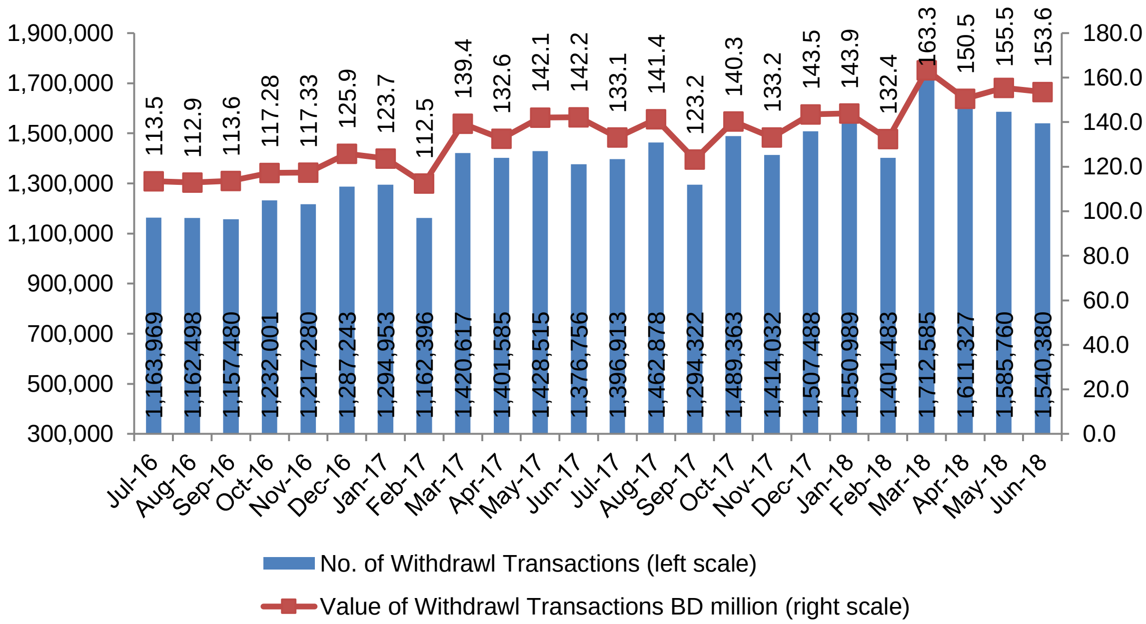
Table 8-3: ATM Transactions Daily Average and Volume

ATM Transitions	Daily Average Volume	Daily Average Value (BD million)
1st July, 2016 to 31st December, 2016	39,242	3.8
1st January, 2017 to 30th June, 2017	44,951	4.4
1st July, 2017 to 31st December, 2017	46,549	4.4
1st January, 2018 to 30th June, 2018	**51,948**	5.0

Source: BENEFIT.

Overall, there is an upward trend in both the value and the volume between June 2017 and June 2018 despite a number of decreases. For the first half of 2018, the highest value of withdrawals was witnessed in March 2018 at BD 163.3 million and the lowest value of withdrawals was in February 2018 at BD 132.4 million. The highest volume of transactions over the past six months was in April 2018 with 1,611,327 transaction. February 2018 also had the lowest volume of transactions over the past six months with 1,401,483.

Chart 8-1: Number and Value of ATM Transactions, July 2016- June 2018



Source: BENEFIT.

8.5 Bahrain Cheque Truncation System (BCTS)

Cheques are seen as one of the most popular instruments in use among Retail Customers and Corporate Customers. As part of the CBB vision to replace the paper based Automated Cheque Clearing System operated by the CBB, the Bahrain Cheque Truncation System (BCTS) commenced its operations in co-operation with the BENEFIT Company (BENEFIT) on the 13th May, 2012. The launch of the BCTS was a milestone to the Bahraini financial sector which raised efficiency and Customer satisfaction. Under the BCTS, cheques presented for payment will be scanned at the Bank where the Customer deposits his/her cheque(s) and the electronic images and payment information, instead of the physical cheque, will be transmitted to the BCTS Clearing House.

The main feature of the BCTS is the increasing efficiency and speed of the cheque clearing as it facilitates Bank Customers to have their cheques cleared and obtain their funds on the same day or maximum by the next working day in addition to providing Customers with a more secure and convenient service. The BCTS is operated by BENEFIT and overseen by CBB (CBB).

The number of participants in the BCTS are twenty eight (28) participants. The daily average volume of cheques for the first half of 2018 decreased by 3.5% when compared to the second half of 2017 from 13,294 cheques to 12,827 cheques. In addition, the daily average volume of cheques decreased by 3.7% from 13,326 cheques to 12,827 cheques compared to the first half of 2017.

Furthermore, the daily average value of cheques decreased in the first half of 2018 by 2.5% when compared to the second half of 2017 from BD40.0 million to BD39.0 million. Moreover, the daily average value of cheques for the first half of 2018 decreased by 5.1% from BD41.1 million to BD39.0 million compared to the first half of 2017.

Table 8-4: BCTS Daily Average Volume and Value

BCTS	Daily Average Volume	Daily Average Value (BD million)
1st July, 2015 to 31st December, 2015	13,162	40.4
1st January, 2016 to 30th June, 2016	13,320	41.6
1st July, 2016 to 31st December, 2016	13,432	40.0
1st January, 2017 to 30th June, 2017	13,326	41.1
1st July, 2017 to 31st December, 2017	13,294	40.0
1st January, 2018 to 30th June, 2018	12,827	39.0

Source: BENEFIT.

The BCTS continued to operate smoothly and efficiently for the period from 1st January, 2018 to 30th June, 2018.

8.6 Electronic Fund Transfer System (EFTS) including Electronic Bill Presentment and Payment (EBPP) System

With the introduction of International Bank Account Number (IBAN) in January, 2012, transfers were easier and less time consuming for both Customers and Banks nevertheless, secured and more convenient. It was perceived that further uses of the IBAN can be utilised. Therefore, the Electronic Fund Transfer System (EFTS) was launched on the 5th of November, 2015, whereas Electronic Bill Presentment and Payment (EBPP) System was launched on the 3rd of October, 2016, operated by the Benefit Company (BENEFIT) and overseen by the CBB.

The EFTS including EBPP is an electronic system that interconnects all Retail Banks in Bahrain with each other and major billers in the Kingdom of Bahrain in order to enhance the efficiency of fund transfers and bill payments promoting a more proactive and forward-thinking banking sector.

The Kingdom of Bahrain took a step forward in line with the global trend of going cashless by introducing the EFTS that enabled electronic fund transfers within Bahrain with three options: Fawri+ Fawri, and Fawateer. Fawri+, Fawri and Fawateer provide fund transfers and real-time bill payments offering the public easier access, faster processes and virtually no mistakes. The number of participants offering outward EFTS Services has reached twenty-six (26) participants.

The daily average volume of Fawri+ transfers for the first half of 2018 increased by 60.9% when compared to the second half of 2017 from 1,187 transfers to 1,910 transfers. Furthermore, the daily average volume of Fawri+ transfers for 1st January, 2018 to 30th June, 2018 increased significantly by 126.6% from 843 transfers to 1,910 transfers when compared to 1st January, 2017 to 30th June, 2017 (second half of 2017).

In addition, the daily average value of Fawri+ transfers increased by 47.4% from BD269,330 to BD396,930 for this period when compared to 1st July, 2017 to 31st December, 2017. Moreover, the daily average value of Fawri+ transfers for 1st January, 2018 to 30th June, 2018 increased by 89.4% from BD209,600 to BD396,930 when compared to 1st January, 2017 to 30th June, 2017.

Table 8-5: EFTS Fawri+ Daily Average Volume and Value

EFTS: Fawri+	Daily Average Volume	Daily Average Value (BD)
1st January, 2016 to 30th June, 2016	229	67,100
1st July, 2016 to 31st December, 2016	476	121,400
1st January, 2017 to 30th June, 2017	843	209,600
1st July, 2017 to 31st December, 2017	1,187	269,330
1st January, 2018 to 30th June, 2018	1,910	396,930

Source: BENEFIT.

The daily average volume of Fawri transfers for the first half of 2018 decreased by 26.1% when compared to the second half of 2017 from 20,960 transfers to 15,484 transfers. Moreover, the daily average volume of Fawri transfers for 1st January, 2018 to 30th June, 2018 decreased by 13.6% from 17,925 transfers to 15,484 transfers when compared to 1st January, 2017 to 30th June, 2017.

Table 8-6: EFTS Fawri Daily Average Volume and Value

EFTS: Fawri	Daily Average Volume	Daily Average Value (BD million)
1st January, 2016 to 30th June, 2016	8,590	25.1
1st July, 2016 to 31st December, 2016	12,540	33.2
1st January, 2017 to 30th June, 2017	17,925	36.2
1st July, 2017 to 31st December, 2017	20,960	40.8
1st January, 2018 to 30th June, 2018	15,484	30.0

Source: BENEFIT.

In addition, the daily average value of Fawri transfers decreased by 26.5% from BD40.8 million to BD30.0 when compared to 1st July, 2017 to 31st December, 2017. Furthermore, the daily average value of Fawri transfers for 1st January, 2018 to 30th June, 2018 decreased by 17.1% from BD36.2 million to BD30.0 million when compared to 1st January, 2017 to 30th June, 2017 (first half of 2017).

Table 8-7: EBPP Fawateer Daily Average Volume and Value

EBPP: Fawateer	Daily Average Volume	Daily Average Value (BD)
1st July, 2016 to 31st December, 2016[13]	358	38,000
1st January, 2017 to 30th June, 2017	4,460	164,000
1st July, 2017 to 31st December, 2017	5,379	261,000
1st January, 2018 to 30th June, 2018	4,427	339,000

Source: BENEFIT.

The daily average volume of Fawateer transfers for the first half of 2018 decreased by 17.7% when compared to the second half of 2017 from 5,379 transfers to 4,427 transfers. Moreover, the daily average volume of Fawateer transfers for 1st January, 2018 to 30th June, 2018 decreased by 0.7% from 4,460 transfers to 4,427 transfers when compared to 1st January, 2017 to 30th June, 2017.

In addition, the daily average value of Fawateer transfers increased by 29.9% from BD261,000 to BD339,000 when compared to 1st July, 2017 to 31st December, 2017. Furthermore, the daily average value of Fawateer transfers for 1st January, 2018 to 30th June, 2018 increased by 106.7% from BD164,000 to BD339,000 when compared to 1st January, 2017 to 30th June, 2017 (first half of 2017).

The EFTS including EBPP continued to operate smoothly and efficiently from 1st January, 2018 to 30th June, 2018. The CBB (CBB) continued to assess the EFTS including EBPP in terms of compliance with the requirements set by the Principles for Financial Market Infrastructures (PFMI) and CBB's Directives.

[13] Fawateer went live on 6th October, 2016.

9. FinTech and Financial Inclusion

Key Points

Chapter

9

- Bahrain's established financial services industry, its role as a leading Islamic finance hub, and the national drive for financial inclusion are supporting the growth of FinTech.
- CBB's FinTech is responsible for the approval process to participate in the Regulatory Sandbox and monitoring technical and regulatory developments in the FinTech field.
- Continues Fintech developments and within the Kingdom and the launch of a number of digital wallets were over the last year.
- The FSD conducted a financial Inclusion Survey was conducted to analyze customer appetite for retail deposit accounts in Bahrain along with payments statistics.

9.1 Overview

The Kingdom of Bahrain is an established financial hub in the Gulf Cooperation Council (GCC) and Middle East region. The Kingdom is repositioning itself to be a Financial Technology (FinTech) hub of the region combining conventional and Shari'ah compliant FinTech solutions. Offering low cost, convenient and instant payments, FinTech has been of great interest to the regulators that were posed with the challenges of regulating, overseeing and ensuring safety and efficiency of those new payment methods.

The Kingdom is repositioning itself to be a FinTech hub of the region by embracing and encouraging digital transformation and the adoption of innovative technology, ultimately adding value and creating a more efficient financial services sector and achieving higher financial inclusion. The higher degree of financial inclusion enabled through FinTech provides countless benefits to the economy and plays a crucial role in the country's economic and social development.The CBB seeks to make the Kingdom of Bahrain a key player in FinTech through the availability of (1) innovative financial solutions, (2) highly qualified national talent in finance and banking, and (3) access to supportive policies.

The aim of the chapter is to show the recent trends and developments in the FinTech Industry and Financial Inclusion within the Kingdom and highlight initiatives taken Central Bank and other industry players in in this field.

9.2 FinTech Developments

The CBB has issued a series of measures to strengthen its position as a regional financial centre; including guidelines on the regulatory environment to ease the implementation of FinTech's solutions.

Innovation and regulatory sandboxes play a vital role in harnessing the advancement of financial technology solutions to support financial inclusion. The CBB has announced a series of measures towards consolidating its position as a regional financial hub and facilitating a number of FinTech initiatives.

The Kingdom of Bahrain achieved remarkable progress towards financial inclusion by putting in place a facilitating regulatory and policy environment through its financial regulator. Additionally it stimulated competition in the financial sector by allowing banks and non-banks to innovate and expand access to financial services, which created an advanced and competitive space that has been accompanied with regulations to ensure responsible provision of financial services.

As part of the CBB's ongoing initiatives towards financial digital transformation and developments in digital financial services, the CBB announced the establishment of a dedicated FinTech & Innovation Unit on the 22nd of October 2017 to ensure an adequate regulatory framework is in place to adapt FinTech, which in turn will enhance the services provided to individual and corporate customers in the financial sector.

The proposed FinTech Unit will be responsible for the approval process to participate in the Regulatory Sandbox, supervision of the activities and operations of the authorized Regulatory Sandbox companies' and monitoring technical and regulatory developments in the FinTech field which will allow industry players to apply innovative products while maintaining the overall safety and soundness of the financial system. This step in the development of the current ecosystem in place is to encourage growth in the FinTech industry and to attract more local, regional, and international FinTech firms to the Kingdom.

The sections below cover the latest FinTech developments and initiatives within the Kingdom.

9.2.1 Regulatory Sandbox

The CBB has launched a regulatory sandbox in June 2017 that enables both local and international emerging businesses, financial technology companies as well as existing CBB licensees, to test their innovative ideas and create pioneering solutions for the financial services sector.[14] This initiative aims to attract FinTech companies from around the world to develop and expand their business in the Arabian Gulf and MENA Region, which will strengthen Bahrain's position as a centre of FinTech and financial innovation in the region.

The newly launched sandbox, which includes 12 companies to date, will provide such authorized companies with the opportunity to test and experiment their innovative financial solutions freely. Additionally, the sandbox is also open to CBB licensed companies to help develop ideas until they are commercially viable. The period allowed for this arrangement will be nine months and may be extended if need be by an additional three months. The Sandbox focuses on three criteria items that include:

[14] A Regulatory Sandbox (Sandbox) is a framework and process that facilitates the development of the FinTech industry in a calculated way. It is defined as a safe space in which businesses can test innovative products, services, business models and delivery mechanisms without immediately incurring all the normal regulatory and financial consequences of engaging in the activity in question.

1. Innovation: The solution should be truly innovative or significantly different from existing offerings, or offer a new use for existing technologies.
2. Customer benefit: The solution should offer identifiable direct or indirect benefits to customers.
3. Technical testing for existing solutions: In case of existing solutions, results of the technical testing must be made available to the CBB.

9.2.2 Crowdfunding

The CBB has also issued regulations for both equity and financing based crowdfunding activities, whereby the regulations accommodate for conventional as well as Shariah compliant crowdfunding transactions. For the first time, small and medium-sized companies in Bahrain and the region will be able to raise conventional financing or Shariah-compliant financing through crowdfunding platforms. Companies operating an electronic equity/financing based crowdfunding platform must be licensed in Bahrain under the instructions depicted in Volume V of the CBB Rulebook. CBB anticipates that entrepreneurs will benefit from the global trend in crowdfunding, which provides a feasible alternative to bank financing. The CBB is particularly keen to ensure that the Kingdom has a leading spot in the crowdfunding market.

It is expected that Bahraini entrepreneurs will benefit from the global crowdfunding trend, which provides a viable alternative to bank financing. In particular, the CBB is keen to see Bahrain dominate the Shari'a compliant financing-based crowdfunding market in the region. The demand for Shari'a compliant financing is already high and is expected to see it reflected in the crowdfunding market.
Some of the key highlights of the crowdfunding regulations by CBB are as follows:

- Minimum capital requirement for crowdfunding platform operators is BD 50,000.
- Only Person to Business (P2B) lending / financing is permitted.
- SMEs with paid up capital not exceeding BD 250,000 can raise funds through crowdfunding platforms.
- These SMEs may be based in Bahrain or outside; however, in case of foreign SMEs the platform operators have to clearly mention the cross-border and jurisdictional risk financiers have to take.
- It is the responsibility of the lenders/financiers to perform their own creditworthiness assessment on borrowers/fundraisers.
- Crowdfunding platform operators have to comply with the CBB rules on Anti Money Laundering, Combating Financing of Terrorism (AML/CFT), and consumer protection.

9.2.3 Benefit

The Bahrain Credit Reference Bureau (known as BENEFIT) stores, analyzes and categorizes credit information. It also provides innovative payment capabilities, information management solutions, and business process outsourcing services that add value to the financial sector and other stakeholders to manage their business effectively. The BENEFIT Company positions itself in being at the forefront of developing powerful tools for the banking and financial services sector to increase productivity, profitability and customer satisfaction.

The Central Bank also uses BENEFIT's credit data for statistical purposes and performs studies related to financial inclusion to support policy development. The Central Bank is also examining ways to further develop indicators related to financial inclusion, and strongly urges the strengthening of public-private cooperation to create a reinforcing environment for financial inclusion. The services that Benefit offers include:

- Automated Teller Machine (ATM)
- Point of Sale (POS):
- Bahrain Credit Reference Bureau
- Bahrain Cheque Truncation System
- Electronic Fund Transfer System (EFTS)
- Payment Gateway
- Internet Banking Shared Platform
- GCCNet Dispute Management System
- Direct Debit
- Tele Bill Payment through Mobile Phones
- Benefit FinTech Lab

9.2.4 Small and Medium Enterprises Support

In addition to the microfinance institutions, the government continues to support micro, small and medium enterprise financing options through its support initiatives; Bahrain Development Bank, and Tamkeen, which constantly develops ways SMEs can obtain formal financing options suitable to the nature of the enterprises, in addition to providing various means of support. Formalizing SME funding through suitable funding channels in the financial system enables higher financial inclusion, and facilitates higher financial coverage. The crowdfunding initiatives taking place in the Kingdom will help SMEs and start-ups fill gaps in lending and move ahead with developing products and solution which is seen as a vital way both to encourage innovation and support our thriving ecosystem.

9.2.5 FinTech Bay

Bahrain FinTech Bay (BFB) is a FinTech ecosystem launched in February 2018 by The Bahrain Economic Development Board (EDB) and Singapore-based FinTech Consortium (FTC). BFB is dedicated to further develop and accelerate FinTech firms and drive innovation in Bahrain by bringing industry leaders and new entrants to (1) drive innovation, (2) create opportunities for growth and (3) foster the interaction between players in the financial sector, investors, entrepreneurs, and government bodies. BFB provides co-working spaces and other shared infrastructure to attract FinTech start-ups to base themselves within the Kingdom.

9.2.6 E-Wallets

Bahrain's appetite for digital wallets is growing where significant steps have been made in realizing the nation's vision to become a technology pioneer. A number of digital wallets were launched in the Kingdom that allows users to make instant payments via smart phones and also facilitate the collection of payments electronically through debit and credit cards.

Table 9-1: Digital Wallets and Features in the Kingdom

Wallet	Launch	Description	Features
b-wallet	January 2018	Bahrain's digital services provider, partnered with Arab Financial Services (AFS), to introduce a digital mobile wallet and payment solution for customers in the Kingdom. The digital mobile wallet app enables quick and secure payments through a smartphone app. The user can scan the QR Code available at different merchants to make payment.	• Add money into a user's account using any debit card issued in Bahrain • Send and receive money between b-wallet accounts • Request money from another b-wallet account, and • Make payments to merchants • Pay with your smartphone using QR code. • Available Offers
BenefitPay	May 2017	BenefitPay is an app that works using QR code scanning Technology by allowing users to make safe and secure payments. The service provides a one-time step to add a card and then enables the customer to scan a QR code from the merchant app and enters proper authentication to complete the transaction.	• Make Payments to Merchants • Payments using Credit cards • Through the mobile App payments or websites • P2P transfers through Fawri+ • Bill payments through Fawateer • Pay with your smartphone using QR code. • Available Offers
Max Wallet	July 2017	MaxWallet is a virtual wallet allowing customers to pay for their purchases using their mobile device without presenting their physical credit cards and paying with a smartphone using QR code. The payment solutions have been launched via a collaboration between BBK and CrediMax to focus on providing more services and payment options.	• Transferring money and sharing payments with friends and family. • Make purchase payments to merchants • Pay with your smartphone using QR code. • Available Offers
Viva Cash	March 2018	Viva Bahrain launched Viva Cash, a new application offering consumers secure and convenient a digital mobile wallet for payments. Viva partnered with Sadad Bahrain, licensed and regulated by the CBB. VIVA Cash is a mobile wallet that can be used to pay your day to day expenses.	• Add money to VIVA Cash account • Send Money to friends and Family • Pay post-paid bills & recharge prepaid Lines • Send money internationally • Shop at participating merchants • Pay with your smartphone using QR code • Make purchase payments to merchants • Available Offers

Source: www.batelco.com, www.credimax.com, www.benefit.bh, and https://www.viva.com.bh.

9.2.7 Other Initiatives and Remarks

The financial services sector provides services to various categories of the Bahraini population. All payments made by the government, whether in the form of salaries, wages, social benefits or payments to service providers to government agencies, are through formal bank accounts. Women and young adults face no obstacles or any form of barrier preventing access from the financial sector. The government is also currently working on the development of a system that will formalize the wage distribution of foreign workers employed in the private sector. All private institutions will be obliged to pay salaries to their foreign employees through banks, with control of the payment mechanism to ensure that there is no breach of the obligations of companies towards workers.

Efforts have been made by the CBB to prioritize financial inclusion in terms of adopting and implementing a viable national strategy, improving women's, SME, and young people's access to financial services, promoting the protection of consumers of financial services, improving and providing financial coverage data and statistics to support policy development, and promoting awareness and financial education.

The CBB is also currently undertaking efforts to enhance financial coverage and provide financial services through:

1. Conducting a study within the CBB to examine the Wage Protection System.
2. Granting licenses to two microfinance institutions, namely the Ebdaa Bank and the Family Bank (Microfinance Institutions).

9.3 Financial Inclusion

Financial inclusion refers to individuals, irrespective of income level, and businesses having access to useful and affordable financial products and services to meet their needs (through transactions, payments, savings, credit and insurance). These products and services have to be delivered in a responsible and sustainable way.

In the recent years, policy-makers and regulators around the world have shown a strong interest in Financial Inclusion. The interest arises from the substantial importance of Financial Inclusion in facilitating access to financial services, creating jobs, and improving the standards of living and economic growth.

Financial inclusion efforts in Bahrain aim to ensure that all businesses and households, have access to and can efficiently use the suitable financial services they need to engage in day-to-day transactions. The CBB closely monitors developments in the areas of financial inclusion and their impact on domestic, regional and global levels and gathers relevant financial inclusion data. The CBB is taking a number of initiatives to further develop indicators related to financial inclusion by expanding (1) the scope of the data and (2) its frequency. The figures in Table 9-2 confirm Bahrain’s continued efforts to achieve a higher level of financial inclusion within its financial sector by providing easy access to financial services.

From 2011 to 2017, figures shows that access to finance measured by the number of Branches and ATM machines per 100,000 people within the Kingdom is large. In terms of bank branches per 100,000 people, Bahrain stands at 11.4 for 2017. As for the number of ATM machines per 100,000, Bahrain records 31.7 ATMs per 100,000 in population for 2017.

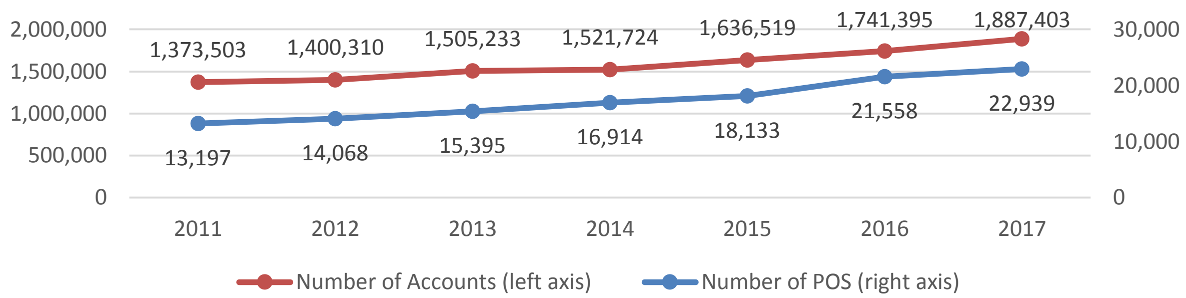
Table 9-2 : Financial Inclusion Figures for the Kingdom of Bahrain*

	2011	2012	2013	2014	2015	2016	2017
Number of Banks	29	28	27	27	27	27	26
Number of Branches	136	147	163	167	171	172	171
Number of Branches per 100,000 in population	*11.4*	*12.2*	*13*	*12.7*	*12.5*	*12.1*	*11.4*
Number of ATMs	450	462	471	452	458	*461*	*476*
Number of ATMs per 100,000 in population	*37.7*	*38.2*	*37.6*	*34.4*	*33.4*	*32.4*	*31.7*
Number of POS	13,197	14,068	15,395	16,914	18,133	*21,558*	*22,939*
Number of POS per 100,000 in population	*1,104.3*	*1,163.6*	*1,228.5*	*1,286.7*	*1,323.3*	*1,514.2*	*1,528.1*
Number of Accounts **	1,373,503	1,400,310	1,505,233	1,521,724	1,636,519	1,741,395	1,887,403
Number of Accounts per 1,000 in population	*1,149*	*1,158*	*1,201*	*1,158*	*1,194*	*1,223*	*1,257*
Number of internet/PC linked accounts	286,188	313,783	352,982	471,535	468,746	544,111	534,033
ATM Cards (thousands)	1,082.6	1,157.2	1,199.7	1,229.6	1,352.6	1407.7	
Debit Cards (thousands)	898.1	976.4	1,002.2	1,010.0	1,097.2	1111.2	
Credit Cards (thousands)	189.6	187.7	202.3	222	253.3	290.3	
Population	1,195,020	1,208,964	1,253,191	1,314,562	1,370,322	1,423,726	1,501,116

**Retail Banks only (Conventional and Islamic).*
***Includes saving deposits as they are used for payments in Bahrain.*
Source: CBB and IGA.

The number of bank accounts within retail banks increased over the last 6 years from 1,373,503 in 2011 to 1,887,403 in 2017 demonstrating an increase of 34.7% (The 2017 increase in the number of retail bank accounts was 10.6%). The number of POS's over the last 6 years also witnessed a significant increase from 13,197 in 2011 to 22,939 in 2017, demonstrating a significant increase of 73.9% (The 2017 increase in POS's was 6.4%).

Chart 9-1: Number Accounts and POS



Source: CBB.

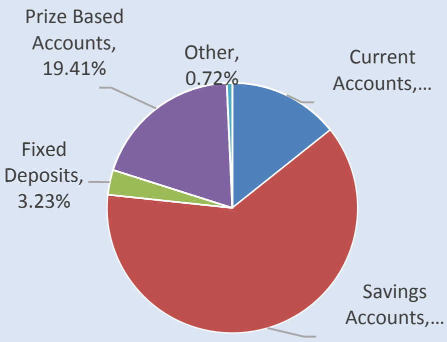
Box 2: FSD Payments and Financial Inclusion Survey

As a step towards establishing a financial inclusion and payments statistics database within the CBB, a survey was conducted by the FSD in January 2018 to analyze customer appetite for retail deposit accounts in Bahrain along with payments statistics. The survey was distributed for the second time to all retail banks in Bahrain in July 2018 and the survey response rate reached 100%.

I. Retail Deposit Accounts.

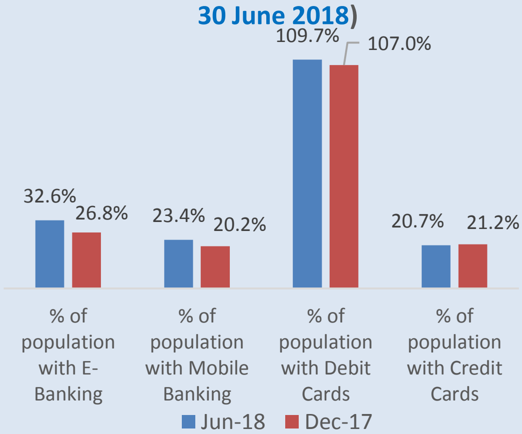
The survey results indicated that as of June 2018, more than 62% of retail bank customers in Bahrain held Savings Accounts, increasing by more than 13% from December 2017. Prize Based Accounts came in the second category with almost 19%. The number of customers holding current accounts reached 14% of and nearly 3% for fixed deposits (as seen in Chart 1). This shows that retail customers have a high appetite for Savings Accounts due to the different features offered by this account type such as providing easy access to funds through debit cards and other payment channels. The statistics also indicate that Retail Customers in Bahrain have a high appetite for Prize Based Schemes which increased by almost 3% from December 2017.

Box 2 Chart 1: Percentage of Retail Customers by deposit account type *(as of 30 June 2018)*



Source: FSD Payments Survey.

Box 2 Chart 2: Payments Statistics (as of 30 June 2018)



Source: FSD Payments Survey, IGA Population figures 2017.

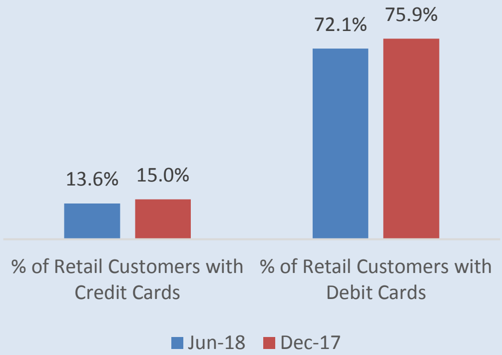
The survey results also showed that the number of Retail Banking customers in Bahrain as of 30th June 2018 exceeds the 2017 population figures for the age group (20-69) by almost 1.5 times. This indicates that Retail Banking Customers tend to hold deposit accounts in several retail banks but also reflects the ease of access that the population has to financial services in Bahrain. This is also mirrored in the percentage of the population with debit cards, which reached over 100% of the adult population in 2017 (shown in Chart 2).

II. Debit and Credit Card Transactions

The survey results indicated that retail banking customers in Bahrain own more Debit Cards than Credit Cards despite the fact that the average number of different credit cards offered by retail banks exceeds the number of Debit Cards (as seen in Chart 3). Almost 72% of retail bank customers own debit cards as of June 2018 and only 13.6% own Credit Cards. Retail banks in Bahrain offer an average of 4 different types of credit cards with the highest number being 13 cards, whereas the average number of different debit card types offered is 2 cards with the highest being 3 cards. The percentage of Retail Customers with Credit Cards remains very low at 13.6% compared to Debit Cards, which reached 72.1% in June 2018 (as seen in Chart 3).

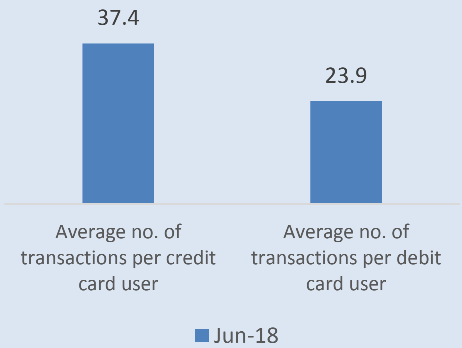
However, the number of transactions made by credit card users of retail banks exceeded that of debit cards (as seen in Chart 4). The average number of credit card transactions per credit card user in the period between 01 Jan-30 June 2018 totalled 37 transactions while the number of debit card transactions made per debit card user reached 24 transactions

Box 2 Chart 3: Percentage of Retail Customers with Credit Cards and Debit Cards (As of 30 June 2018)



Source: FSD Payments Survey.

Box 2 Chart 4: Count of Credit and Debit Card Transactions for the first half of 2018

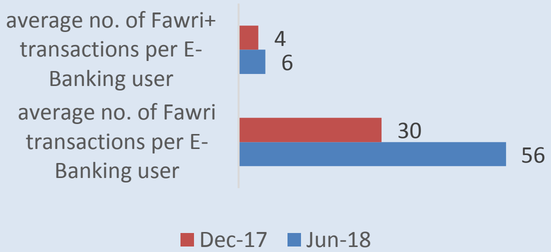


Source: FSD Payments Survey.

III. E-Banking and Mobile Banking Account Users

The survey results revealed that almost 33% of the population own E-Banking accounts, while 23% own Mobile Banking accounts (shown in Chart 2 above). This statistic was used to identify the usage of the Electronic Fund Transfer Systems (EFTS), Fawri and Fawri+ payment options. Since the inception of the EFTS, the average number of Fawri+ transactions conducted per E-Banking user totalled 6 transactions and as for Fawri, the average number of transactions totalled a count of 56.

Box 2 Chart 6: Count of Fawri and Fawri+ Transactions (since inception to 30th June 2018)



Source: FSD Payments Survey.

10. Cyber Security

Chapter

10

Key Points

- Cyber risk is a threat to financial stability with increase attacks on financial institution and central banks.
- Cyber-attacks on banks account for the majority of the attacks targeted at financial institutions.
- The FSD issued a survey in July 2018 to all Retail Banks in Bahrain which served both microprudential and macroprudential objectives.
- The survey's scope covered: Governance & Leadership, Identification, Protection, Detection and Response & Recovery.

10.1 Overview

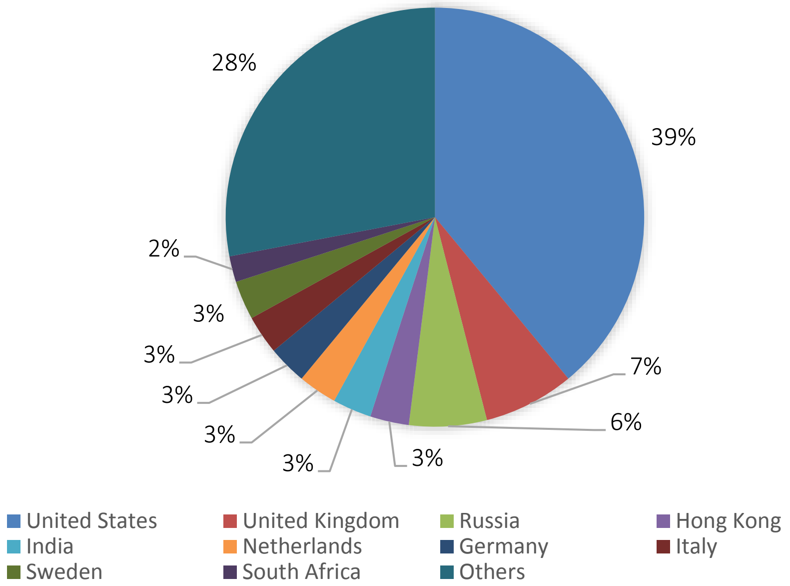
Cyber risk is steadily evolving into a main threat to all industries. Its impact however on the financial services industry is growing into an individually recognised risk by all financial institutions. Given the innovations in information technology (IT) and financial institutions' increased reliance on IT channels, cyber security is no longer regarded as a technical issue but a main threat to the industry.

The CBB will therefore be addressing developments in cyber risk as a recurrent chapter in its Financial Stability Report. The aim of the chapter is to Highlight the different initiatives of the Central Bank and actively spread awareness about Cyber Risk by warning the financial industry of the large operational, financial and security risks involved with cyber security.

10.2 A Global Overview of Cyber Threats Targeted at Financial Institutions

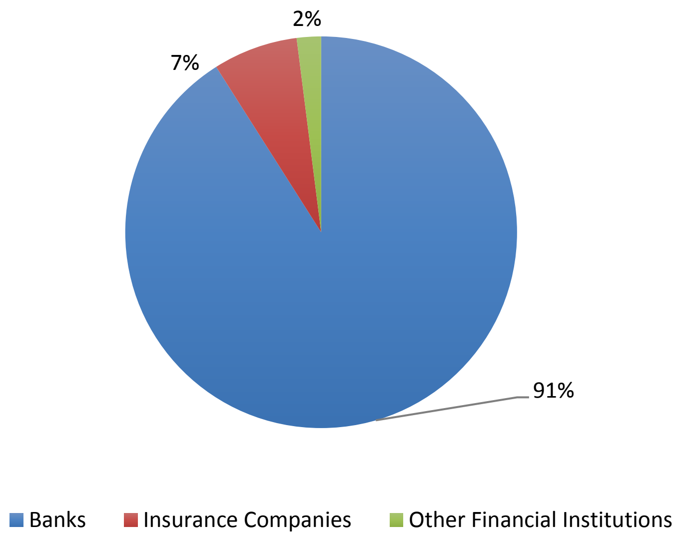
Cyber risk has become a serious threat to financial stability over the past five years, which has resulted in recent attacks on financial institutions and central banks. An IMF working paper published in June 2018 presented cyber risk threats around the world for financial institutions by analysing the different types of cyber incidents (data breaches, fraud and business disruption) and identifying patterns. Chart10- 1 below presents the percentage of cyber-attacks on financial institutions by country. The statistics show that almost 40% of cyber-attacks on financial institutions occurred in the US. According to the IMF study, cyber-attacks on banks accounted for the majority of the attacks targeted at financial institutions by almost 91 percent of the attacks as shown in Figure 2. Of the cyber-attacks targeted at banks, retail banking activities accounted for the majority of the attacks by almost 39% and credit card services came in second at 25%.

Chart 10-1: Cyber Attacks Financial Institutions by Country



Source: ORX News; IMF staff calculations.

Chart 10-2: Most Targeted Financial Institutions by Cyber Attacks



Source: ORX News, IMF Working Paper, WP/18/143.

10.3 A Global Overview of Cyber Threats targeted at Central Banks

Table 10-1 below shows recent cyber-attacks on Central Banks since 2010. The trend shows that with time, the financial losses linked to cyber-attacks are on an increasing trajectory. Central banks in Advanced Economies and Emerging Markets have also been the victims of cyber-attacks. According to the IMF study, the US and Italy were both victims of data breaches, while Norway and Sweden were victims of business disruptions. In Emerging Markets, the majority of the attacks took the form of fraud, which resulted in losses of approximately USD 117 million.

Table 10-1: Recent cyber-attacks on central banks

Institution	Year	Type of attack	Details
Federal Reserve Bank of Cleveland	2010	Data breach	Theft of 122,000 credit cards
Federal Reserve Bank of New York	2012	Data breach	Theft of proprietary software code worth USD 9.5 Million
Sveriges Riksbank	2012	Business Disruption	Distributed Denial of Service (DDoS) attack left the website offline for 5 hours
Banco Central del Ecuador	2013	Fraud	USD 13.3 Million stolen from the account of the city of Riobamba at the central bank
Federal Reserve Bank of Saint Louis	2013	Data breach	Publication of credentials of 4,000 US bank executives by Anonymous
Central Bank of Swaziland	2014	Fraud	Theft of USD 688,000
ECB	2014	Data breach	20,000 email addresses and contact information compromised
Norges Bank	2014	Business Disruption	DDoS attack on seven large financial institutions, resulting in suspended services during a day.
Central Bank of Azerbaijan	2015	Data breach	Theft of thousands of bank customers' information
Bangladesh Bank	2016	Fraud	The SWIFT credentials of the Bangladesh central bank were used to transfer USD 81 Million from its account at the FRBNY. Hackers tried to steal USD 951 Million.
Bank of Russia	2016	Fraud	21 Cyber-attacks aimed at stealing USD 50 Million from correspondent bank accounts at the central bank, resulted in a loss of USD 22 Million.
Bank of Italy	2017	Data Breach	Hack of email accounts of two former executives.

Source: IMF Working Paper WP/18/143.

10.4 CBB Cybersecurity Initiatives

A. TRMST Committee Updates

The TRMST (Technology Risk Management Security Team) is currently working on the "Development of a single Information Technology Module for all CBB licensees". This project is in now being studied by the Regulatory Policy Unit, and a best and most efficient solution for compiling the IT related Rulebook requirements will be decided upon.

The team has also participated in reviewing the "Open Banking" initiative studied by the FinTech and Innovation Unit.

B. CBB Cyber Security Survey

I- Survey Scope & Objectives

As part of the CBB's continuous effort to track and assess the resilience of Bahrain's Financial Sector to cyber threats, the FSD issued a survey in July 2018 to all Retail Banks in Bahrain which served both microprudential and macroprudential objectives. The survey was replicated from the Bank of England's Cyber Resilience Questionnaire with the aim of establishing a good practice and serving as a self-assessment process for supervisors and executive management at banks to evaluate their readiness to cyber related risks. The aim of the survey is to assess which cyber threats constitute the most serious of threats to Bahrain's Retail Banking system.The questionnaire compares how well banks' risk management policies and procedures are aligned to their capabilities and whether or not they are adequate for the types of operational risk incidents and threats that they face.

The survey was divided into five parts: Governance & Leadership, Identification, Protection, Detection and Response & Recovery.

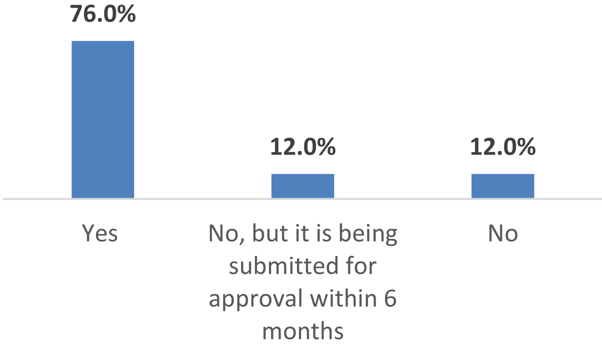
II- Key Survey Findings:

The survey response rate was at 100% and the survey results drew upon some major findings that included the following:

1- 76% of banks reported that their cyber-security strategy has been approved by their Board of Directors and 12% reported that their strategy is not board-approved.
2- 72% of banks report all cyber threats to their Board of Directors while 28% group cyber security incidents into total operational risk incidents.
3- 84% of banks reported that cyber security roles within the organization are aligned with the strategy.
4- 88% of banks measure the effectiveness of the implementation of risk management practices while only 8% do not.
5- 80% of banks have a process to identify critical internal functions, which are annually verified, while 20% of banks do not undertake this exercise on a repeatable basis.
6- 92% of banks reported that they conduct cyber security training to their staff and information which this regard is collected, while 8% of banks only conduct training on an ad-hoc basis.
7- 40% of banks provide additional cyber security training to higher risk staff while 48% of banks do not.
8- Regarding data loss prevention strategy, 44% of banks have a full and documented process and strategy while 52% of banks have a partial data loss prevention strategy which is only aligned to critical systems and data.
9- Only 12% of banks protect and store encrypted data at rest while 64% of banks only encrypt and store critical information/data at rest.
10- 68% of banks back-up all data in multiple formats while 32% of banks only back-up critical data.
11- 56% of banks purchase cyber-specific insurance, while for 20% of banks this is included in their general property and liability insurance.

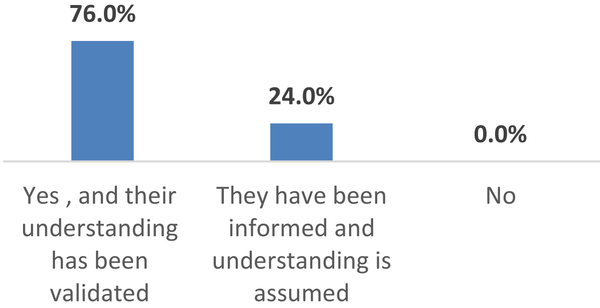
Chart 10-3: CBB Cyber Security Survey Results July 2018

1- Governance & Leadership : Has your cyber security strategy been approved by the board?



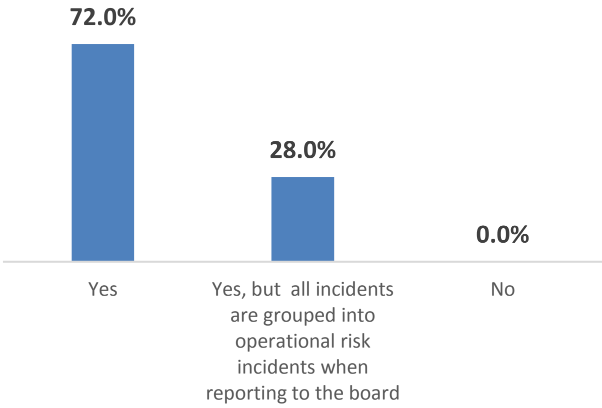
Source: CBB Cyber Security Survey (July 2018).

2- Governance & Leadership : Do senior executives understand their roles and responsibilities with regards to cyber security?



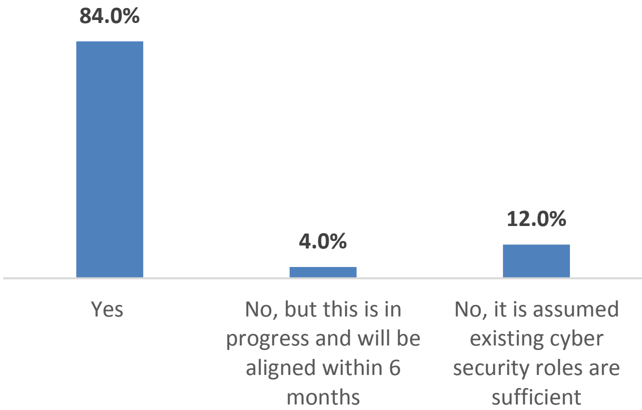
Source: CBB Cyber Security Survey (July 2018).

3- Governance & Leadership : Do you report all operational risk incidents and cyber related incidents to your Board?



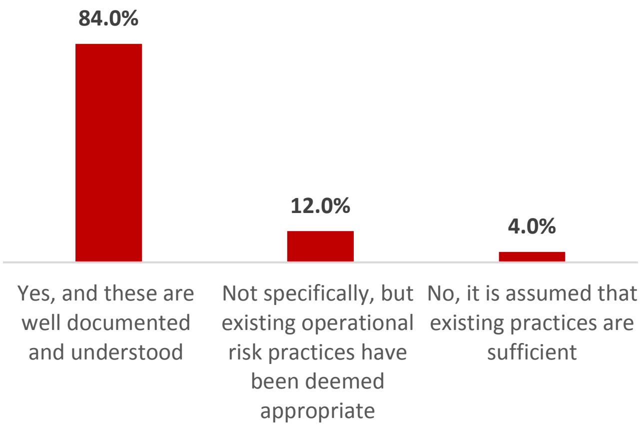
Source: CBB Cyber Security Survey (July 2018).

4- Governance & Leadership : Have cyber security roles within the organisation been aligned to the strategy?



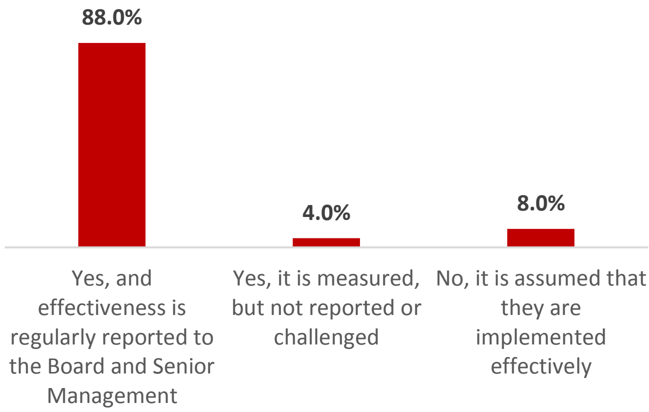
Source: CBB Cyber Security Survey (July 2018).

5- Identification: Are effective risk management practices in place to address cyber security risks?



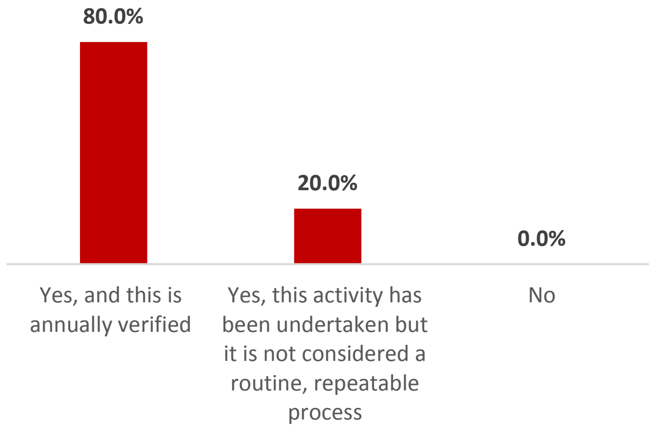
Source: CBB Cyber Security Survey (July 2018).

6-Identification: Do you measure the effectiveness of the implementation of risk management practices?



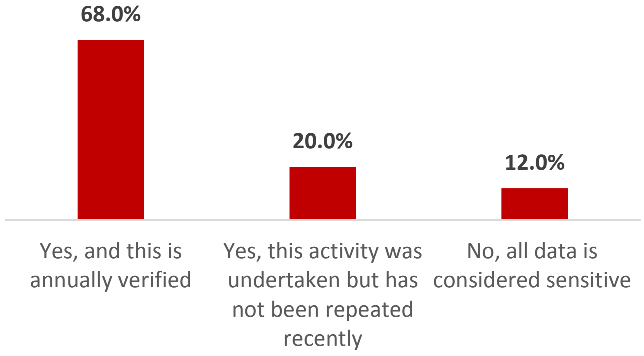
Source: CBB Cyber Security Survey (July 2018).

7- Identification: Do you have a process to identify your critical internal functions?



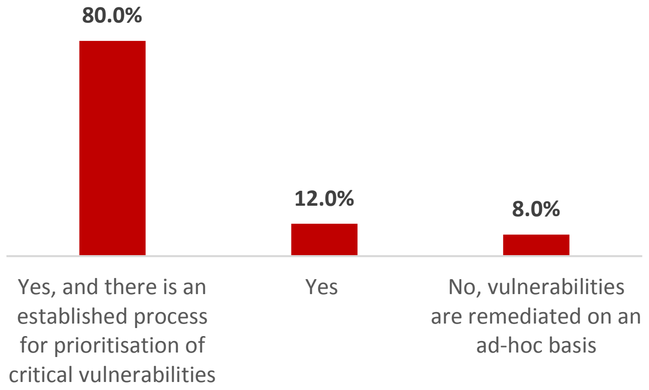
Source: CBB Cyber Security Survey (July 2018).

8- Identification: Has the sensitivity and integrity of your data security controls, required for the delivery of critical internal functions, been assessed?



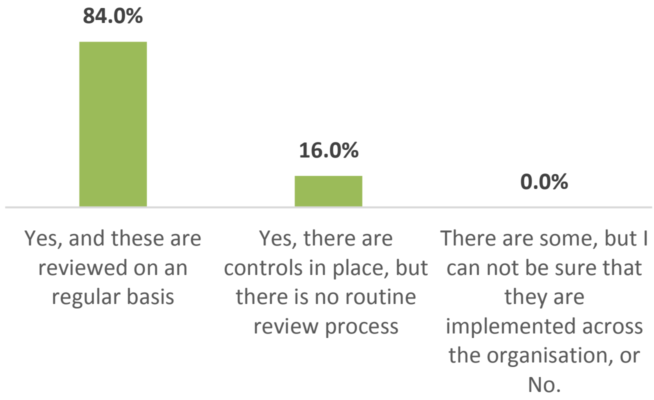
Source: CBB Cyber Security Survey (July 2018).

9-Identification: Are hardware and software vulnerabilities identified, documented and remediated?



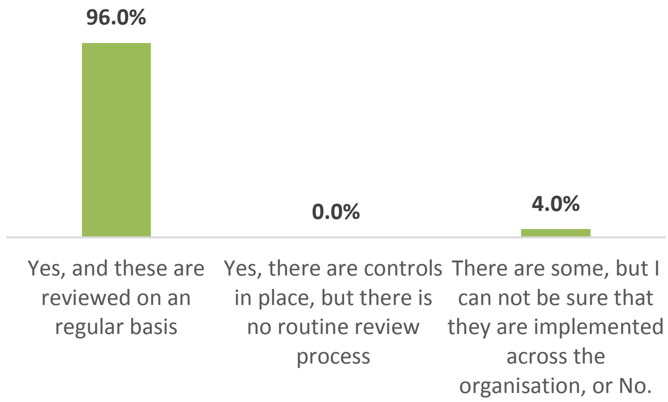
Source: CBB Cyber Security Survey (July 2018).

10- Protection: Are effective remote access controls implemented, maintained and monitored across your organisation's facilities?



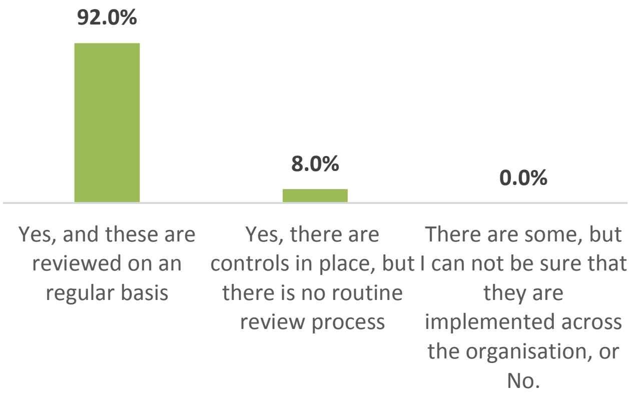
Source: CBB Cyber Security Survey (July 2018).

11- Protection: Are effective physical access controls implemented, maintained and monitored across your organisation's facilities?



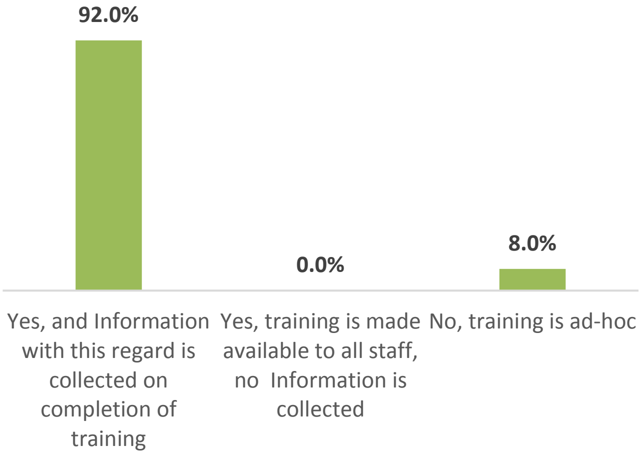
Source: CBB Cyber Security Survey (July 2018).

12- Protection: Are effective privileged user access rights implemented, maintained and monitored across your organisation's facilities?



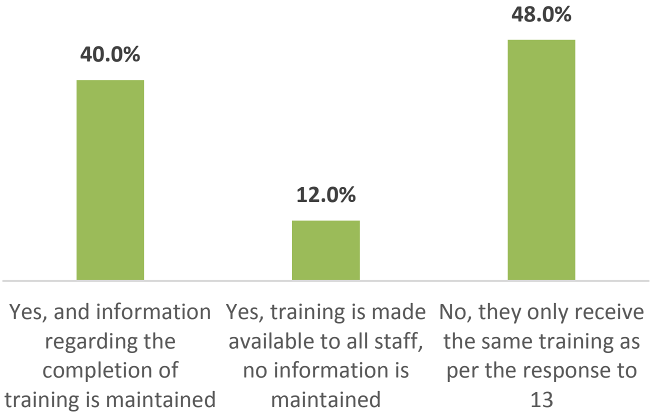
Source: CBB Cyber Security Survey (July 2018).

13- Protection: Are all staff provided with cyber security training?



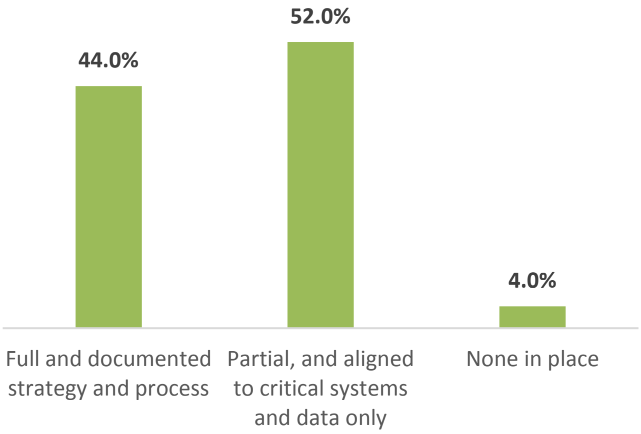
Source: CBB Cyber Security Survey (July 2018).

14-Protection: Is additional training provided to higher risk staff?



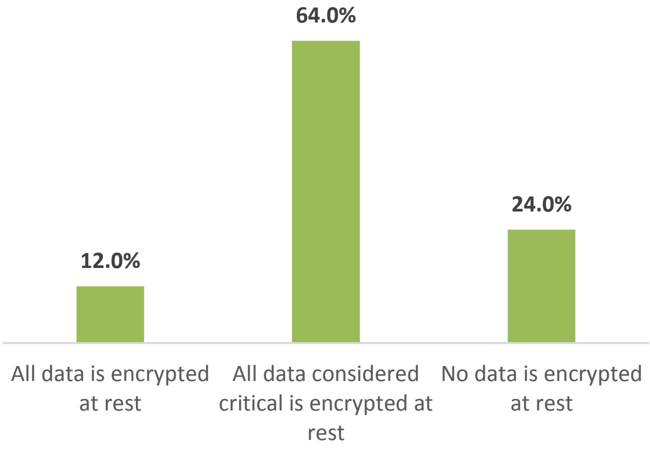
Source: CBB Cyber Security Survey (July 2018).

15- Protection: Which option best describes your data loss prevention strategy?



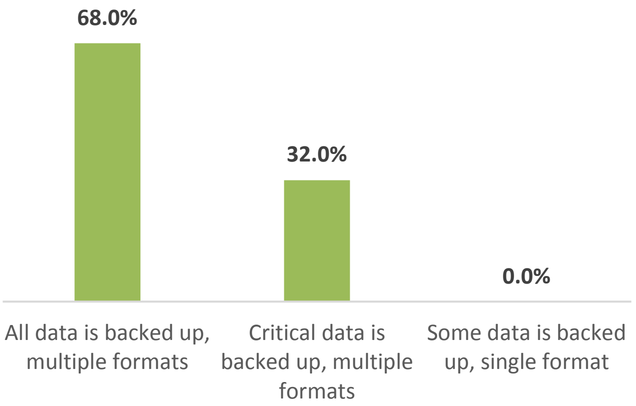
Source: CBB Cyber Security Survey (July 2018).

16- Protection: Which option best describes how data is stored?



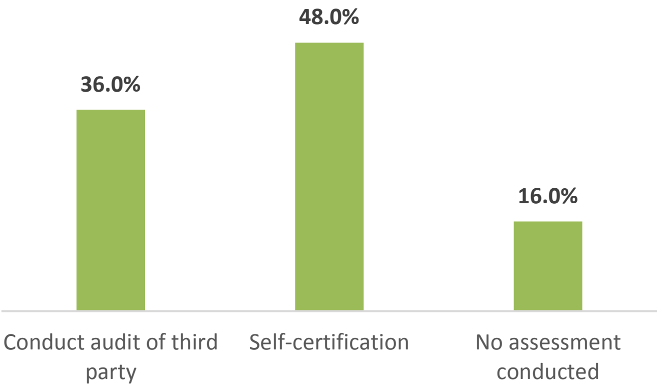
Source: CBB Cyber Security Survey (July 2018).

17- Protection: Which option best describes your data back-up process?



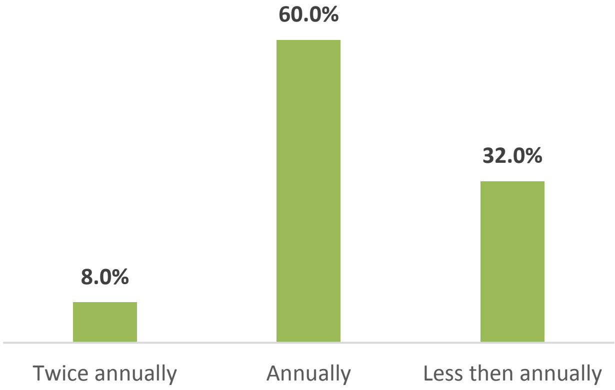
Source: CBB Cyber Security Survey (July 2018).

18- Protection: How do you assess third-party providers' security capabilities?



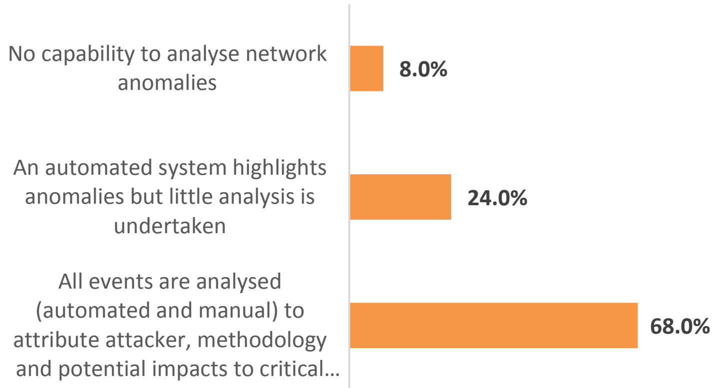
Source: CBB Cyber Security Survey (July 2018).

19- Protection: How often are third-party providers' security capability assessments carried out?



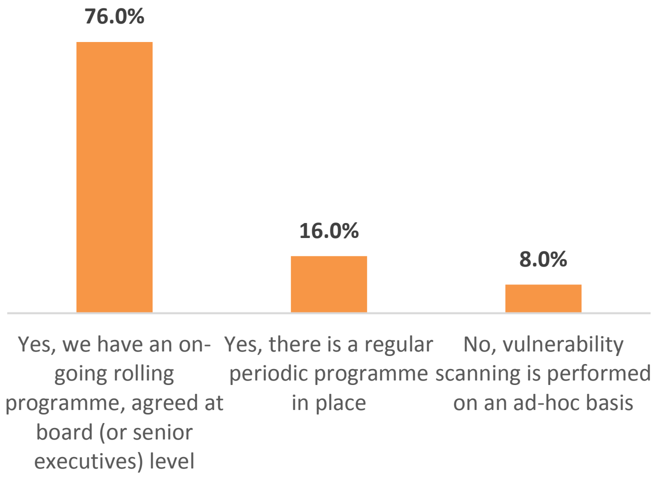
Source: CBB Cyber Security Survey (July 2018).

20-Detection: Which option best describes your network detection and monitoring processes and controls?



Source: CBB Cyber Security Survey (July 2018).

21-Detection: Do you perform regular vulnerability scanning?



Source: CBB Cyber Security Survey (July 2018).

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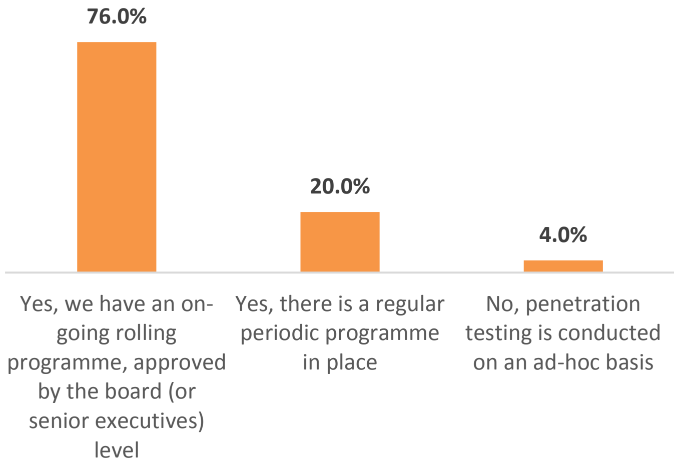
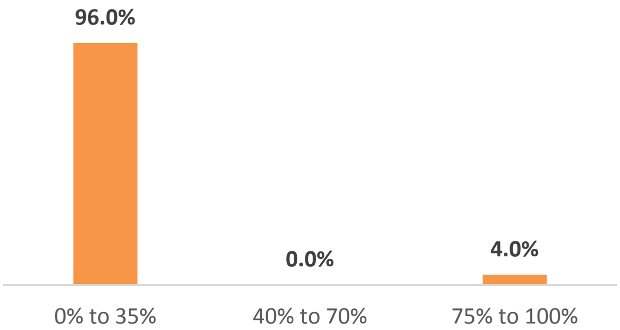
22-Detection: Do you perform regular penetration testing?



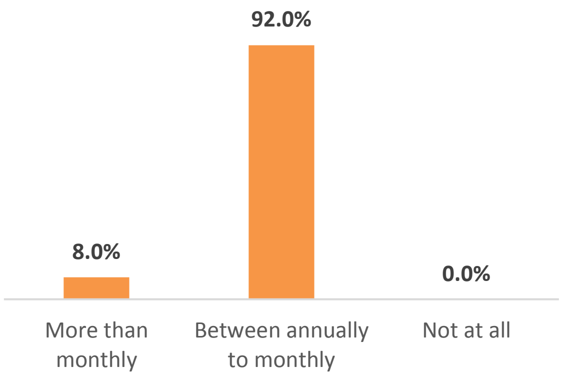
Source: CBB Cyber Security Survey (July 2018)

23- Detection: Approximately what proportion of your organisation's operational risk incidents were cyber security related over the past 6 months?



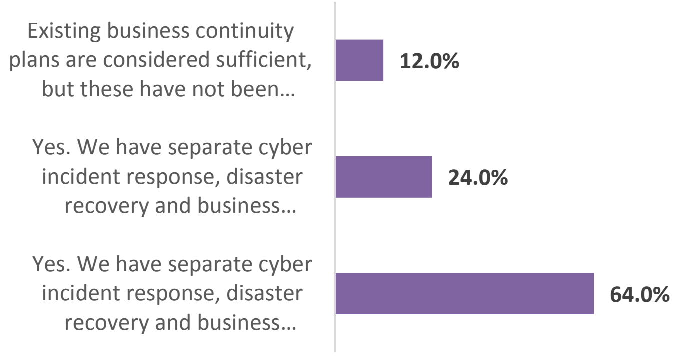
Source: CBB Cyber Security Survey (July 2018).

24- Detection: Describe how frequently you undertake vulnerability scanning and penetration testing and ensure that both are effective.



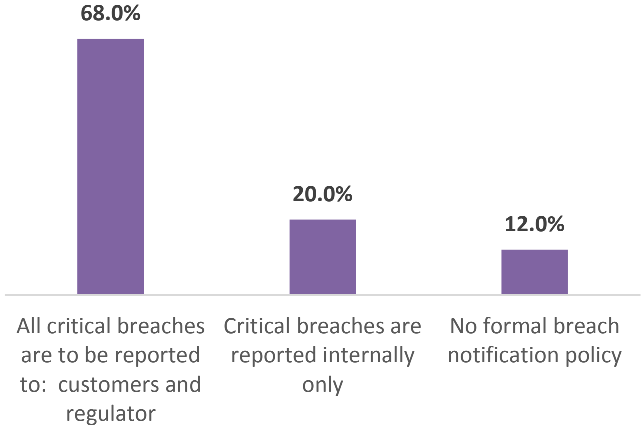
Source: CBB Cyber Security Survey (July 2018).

25- Response & Recovery: Do you have a documented and regularly tested response plan (business continuity, disaster recovery and/or cyber incident response)?



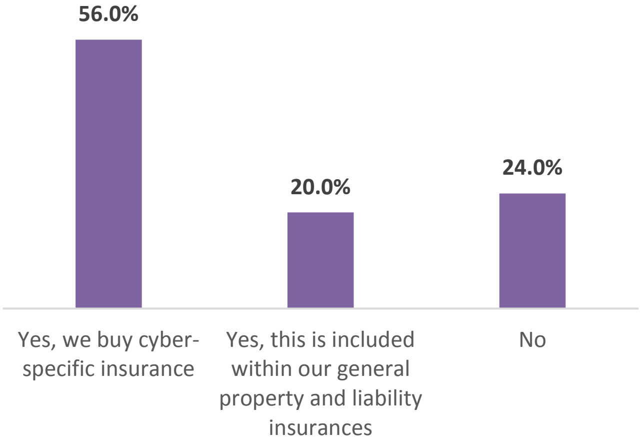
Source: CBB Cyber Security Survey (July 2018).

26- Response & Recovery: Describe your data breach notification policy?



Source: CBB Cyber Security Survey (July 2018).

27- Response & Recovery: Do you buy cyber insurance?



Source: CBB Cyber Security Survey (July 2018).

Annex:

Financial Soundness Indicators and Selected Graphs

Annex 1: Financial Soundness Indicators

Annex1 Table 1:
Selected Financial Soundness Indicators—Overall Banking System

(End of period)

	Mar-17	Sep-17	Mar-18
Capital Adequacy			
CAR (%) *	18.7	19.4	18.8
Tier 1 CAR (%) *	17.4	18.1	17.4
Leverage (Assets/Capital) (Times) *	6.8	6.9	6.9
Asset Quality			
NPL's (% of Total Loans)	5.9	5.7	5.5
Specific Provisions (% of NPL's)	57.3	57.0	52.1
Loan Concentration (Share of Top Two Sectors) (%)	30.1	29.4	30.0
Real Estate/ Construction Exposure (%) **	23.0	23.6	24.3
Earnings			
ROA (%)	0.3	0.9	0.3
ROE (%) ***	2.1	5.7	2.5
Net Interest Income (% of Total Income) ****	58.5	66.1	55.0
Net Fees & Commissions (% of Total Income) ****	23.6	16.1	22.9
Operating Expenses (% of Total Income)	65.0	53.4	57.5
Liquidity			
Liquid Assets (% of Total Assets)	24.3	25.6	25.5
Loan-Deposit Ratio (%)	68.3	67.9	72.7

** Locally-Incorporated Banks only.*
*** Real Estate/ Construction exposure is calculated as the share of the construction, commercial real estate financing, and residential mortgages sectors of total lending.*
****ROE is defined as net profit over Tier 1 Capital.*
***** Conventional Banks only.*
Source: CBB.

Annex1 Table 2:
Selected Financial Soundness Indicators—Conventional Retail Banks

(End of period)

	Mar-17	Sep-17	Mar-18
Capital Adequacy			
CAR (%) *	20.3	20.4	19.6
Tier 1 CAR (%) *	18.6	18.8	18.1
Leverage (assets/capital) (Times) *	6.6	6.5	6.7
Non-Performing Loans Net Provisions to Capital (%) *	6.0	6.6	7.0
Asset Quality			
NPL's (% of Total Loans)	5.7	5.8	5.9
Specific Provisions (% of NPL's)	50.0	49.5	47.8
Net NPL' (% of Net Loans)	3.0	3.1	3.2
Loan Concentration (Share of Top Two Sectors) (%)	34.7	35.2	33.8
Real Estate/ Construction Exposure (%) **	30.7	30.7	30.7
Earnings			
ROA (%)	0.2	1.2	0.4
ROA Local Banks (%)	0.5	1.5	0.6
ROA Overseas Banks (%)	-0.3	0.8	0.1
ROE (%) ***	3.8	10.3	4.1
Net Interest Income (% of Total Income)	72.4	74.5	73.6
Net Fees & Commissions (% of Total Income)	15.6	13.9	14.5
Operating Expenses (% of Total Income)	72.6	43.0	48.6
Liquidity			
Liquid Assets (% of Total Assets)	24.6	35.8	33.6
Liquid Assets (% of Short-Term Liabilities)	39.1	45.3	42.4
Loan-Deposit Ratio (%)	73.8	70.8	73.4
Non-Bank Deposits (% of Total Deposits)	77.6	78.3	80.2

** Locally-Incorporated Banks only.*
*** Real Estate/ Construction exposure is calculated as the share of the construction, commercial real estate financing, and residential mortgages sectors of total lending.*
**** ROE is defined as net profit over Tier 1 Capital (Locally-Incorporated Banks only).*
Source: CBB.

Annex1 Table 3:
Selected Financial Soundness Indicators—Conventional Wholesale Banks

(End of period)

	Mar-17	Sep-17	Mar-18
Capital Adequacy			
CAR (%) *	18.1	19.2	18.6
Tier 1 CAR (%) *	17.0	18.2	17.6
Leverage (assets/capital) (Times) *	6.8	7.0	6.8
NPL's Net Provisions to Capital (%) *	4.7	5.6	5.3
Asset Quality			
NPL's (% of Total Loans)	5.6	5.6	5.3
Specific Provisions (% of NPL's)	67.9	64.9	59.9
Net NPL' (% of Net Loans)	1.9	2.1	2.2
Loan Concentration (Share of Top Two Sectors) (%)	36.1	35.7	37.3
Real Estate/ Construction Exposure (%) **	16.5	18.7	20.6
Earnings			
ROA (%)	0.3	0.8	0.3
ROA Local Banks (%)	0.3	0.5	0.3
ROA Overseas Banks (%)	0.4	1.1	0.3
ROE (%) ***	1.9	3.4	2.1
Net Interest Income (% of Total Income)	46.1	57.6	40.5
Net Fees & Commissions (% of Total Income)	36.5	20.7	34.2
Operating Expenses (% of Total Income)	52.2	48.1	57.9
Liquidity			
Liquid Assets (% of Total Assets)	27.4	21.9	23.2
Liquid Assets (% of Short-Term Liabilities)	37.6	33.5	28.9
Loan-Deposit Ratio (%)	62.6	63.4	69.2
Non-Bank Deposits (% of Total Deposits)	46.2	47.1	52.8

** Locally-Incorporated Banks only.*
*** Real Estate/ Construction exposure is calculated as the share of the construction, commercial real estate financing, and residential mortgages sectors of total lending.*
**** ROE is defined as net profit over Tier 1 Capital (Locally-Incorporated Banks only).*
Source: CBB.

Annex1 Table 4:
Selected Financial Soundness Indicators—Islamic Retail Banks

(End of period)

	Mar-17	Sep-17	Mar-18
Capital Adequacy			
CAR (%)	17.1	18.2	18.0
Tier 1 CAR (%)	15.3	15.3	14.8
Leverage (Assets/Capital) (Times)	7.6	8.5	8.6
NPF's Net Provisions to Capital (%)	27.2	26.1	32.1
Asset Quality			
NPF's (% of Total Facilities)	10.1	9.0	10.0
Specific Provisions (% of NPF's)	39.9	44.1	41.3
Net NPF's (% of Net Facilities)	6.4	5.3	6.2
Facilities Concentration (Share of Top Two Sectors) (%)	37.1	37.6	35.8
Real Estate/ Construction Exposure (%) *	25.6	24.0	26.2
Earnings			
ROA (%)	0.1	0.4	0.2
ROE (%) **	1.1	4.5	1.5
Net Income from Own Funds, Current Accounts and Other Banking Activities (% of Operating Income)	62.6	62.9	60.1
Net income from Jointly Financed Accounts and Mudarib Fees (% of Operating Income)	36.8	36.1	38.6
Operating Expenses (% of Total Income)	77.8	78.2	74.0
Liquidity			
Liquid Assets (% of Total Assets)	12.4	11.5	14.5
Facility-Deposit Ratio (%)	86.3	89.1	94.4
Current Accounts from Non-Banks (% of Non-Capital Liabilities, excl. URIA)	29.2	29.3	28.3

** Real Estate/ Construction exposure is calculated as the share of the construction, commercial real estate financing, and residential mortgages sectors of total lending.*
*** ROE is defined as net profit over Tier 1 Capital.*
Source: CBB.

Annex1 Table 5:
Selected Financial Soundness Indicators—Islamic Wholesale Banks

(End of period)

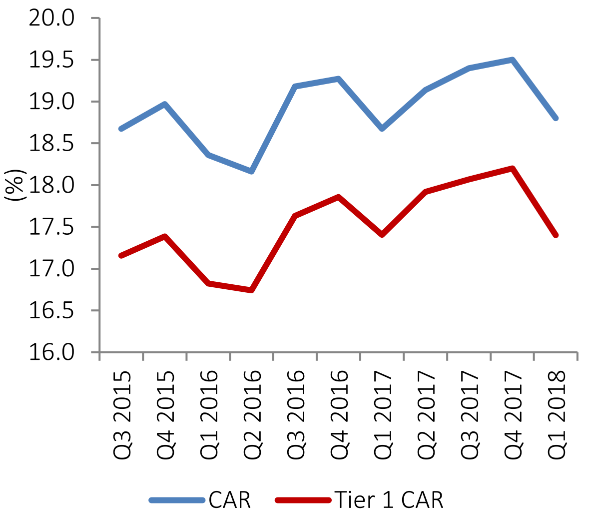
	Mar-17	**Sep-17**	**Mar-18**
Capital Adequacy			
CAR (%)	18.5	18.8	18.5
Tier 1 CAR (%)	17.8	18.3	17.4
Leverage (Assets/Capital) (Times)	6.7	6.5	6.7
NPF's Net Provisions to Capital (%)	0.5	0.2	1.0
Asset Quality			
NPF's (% of Total Facilities)	2.6	2.3	1.4
Specific Provisions (% of NPF's)	93.8	96.5	75.7
Net NPF's (% of Net Facilities)	0.2	0.1	0.4
Facilities Concentration (Share of Top Two Sectors) (%)	40.5	40.1	39.4
Real Estate/ Construction Exposure (%) **	19.9	19.1	17.2
Earnings			
ROA (%)	0.2	0.8	0.3
ROE (%) ***	1.4	5.0	2.0
Net income from own funds, current accounts and other banking activities (% of operating income)	54.8	58.8	59.6
Net income from jointly financed accounts and Mudarib fees (% of operating income)	44.5	40.3	38.9
Operating expenses (% of total income)	73.0	68.3	64.8
Liquidity			
Liquid Assets (% of Total Assets)	21.6	22.9	21.0
Facility-Deposit Ratio (%)	61.3	61.4	67.7
Current Accounts from Non-Banks (% of Non-Capital Liabilities, excl. URIA)	44.0	44.4	43.7

** Real Estate/ Construction exposure is calculated as the share of the construction, commercial real estate financing, and residential mortgages sectors of total lending.*
*** ROE is defined as net profit over Tier 1 Capital.*
Source: CBB.

Annex 2: Selected Graphs

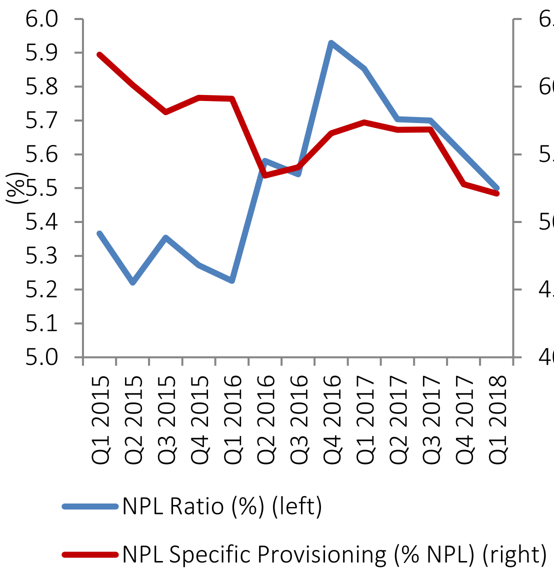
A. Overall Banking Sector

Annex 2 Graph 1: CAR



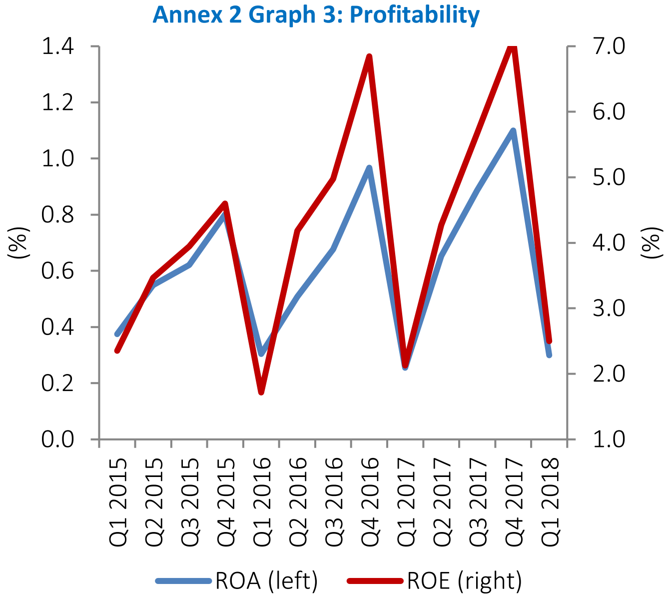
Source: CBB.

Annex 2 Graph 2: NPL's and Provisioning



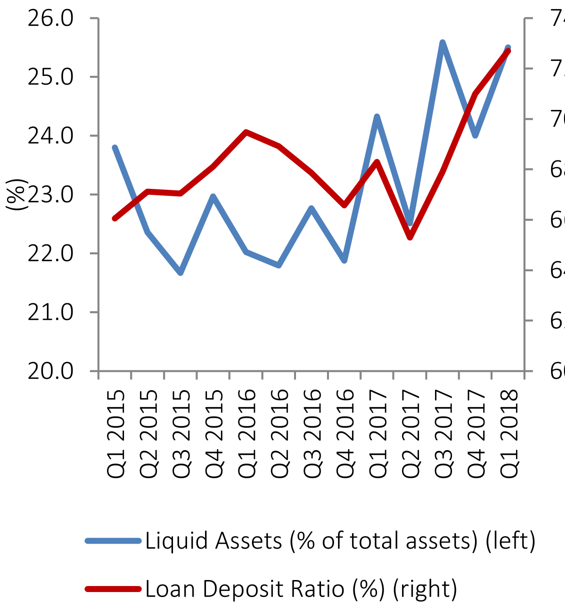
Source: CBB.

Annex 2 Graph 3: Profitability



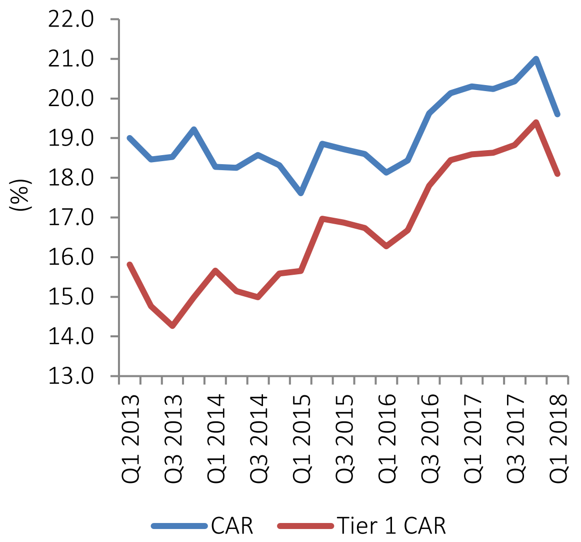
Source: CBB.

Annex 2 Graph 4: Liquidity



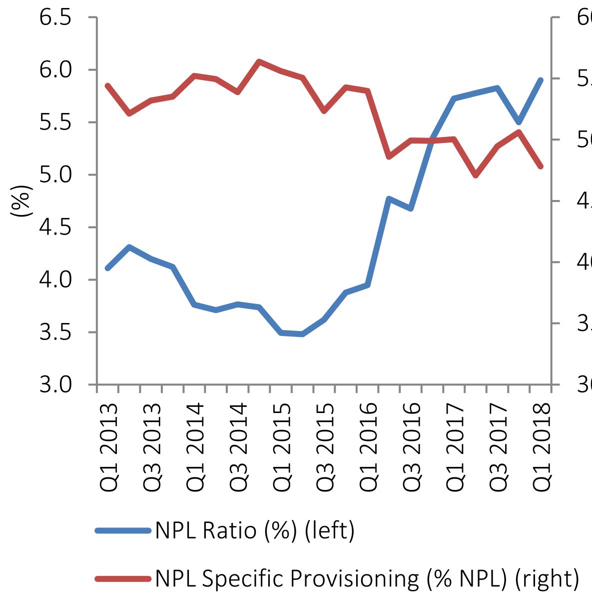
B. Conventional Retail

Annex 2 Graph 5: CAR



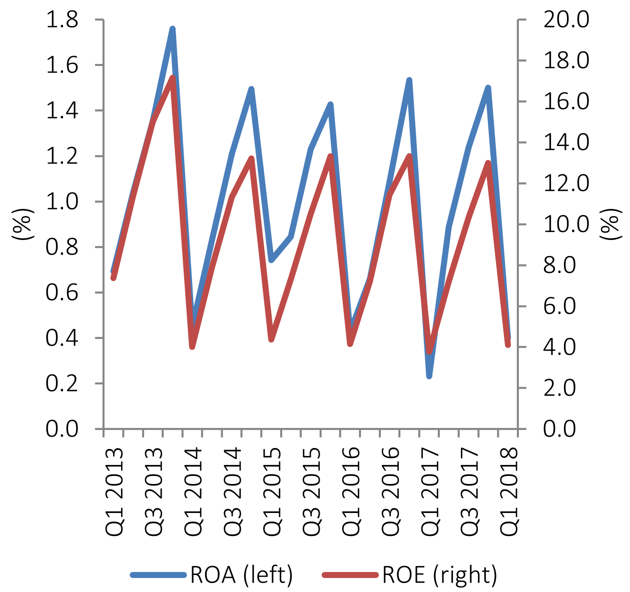
Source: CBB.

Annex 2 Graph 6: NPL's and Provisioning



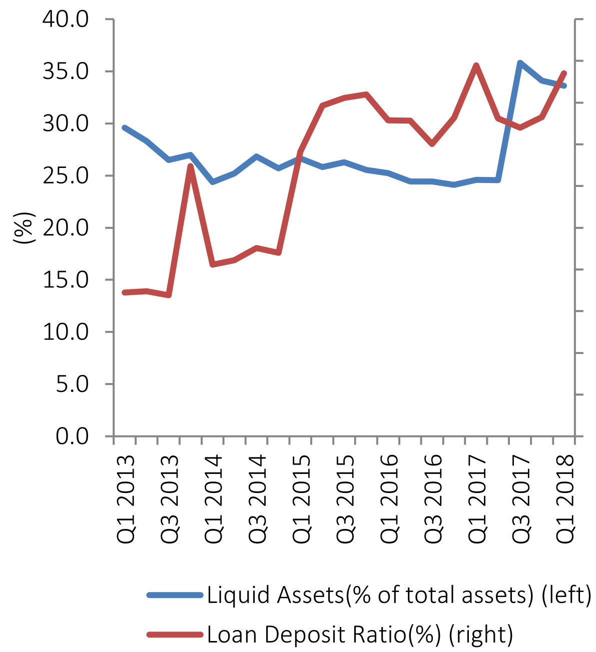
Source: CBB.

Annex 2 Graph 7: Profitability



Source: CBB.

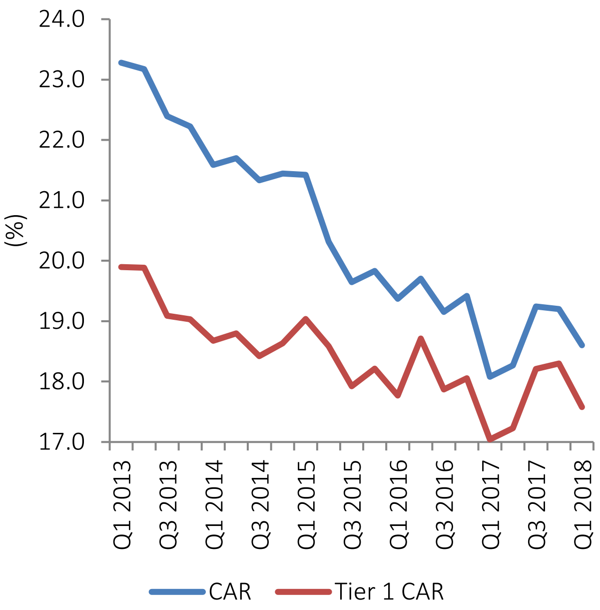
Annex 2 Graph 8: Liquidity



Source: CBB.

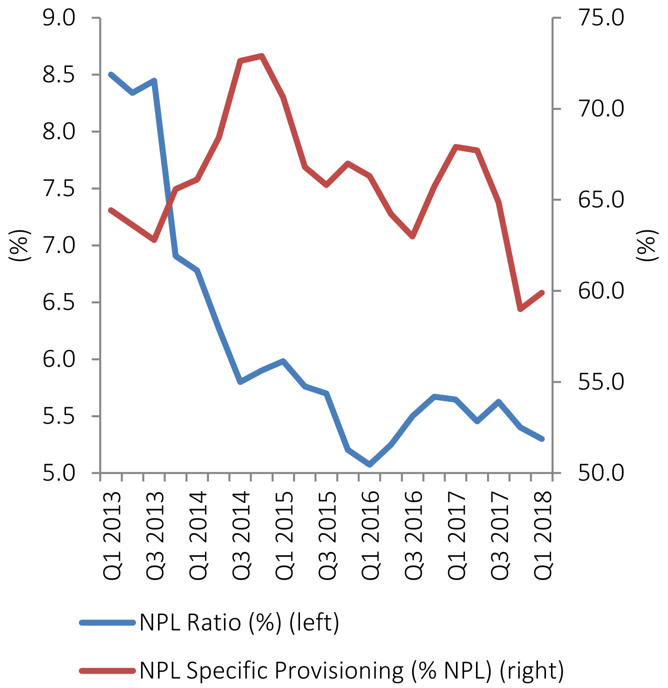
C. Conventional Wholesale

Annex 2 Graph 9: CAR



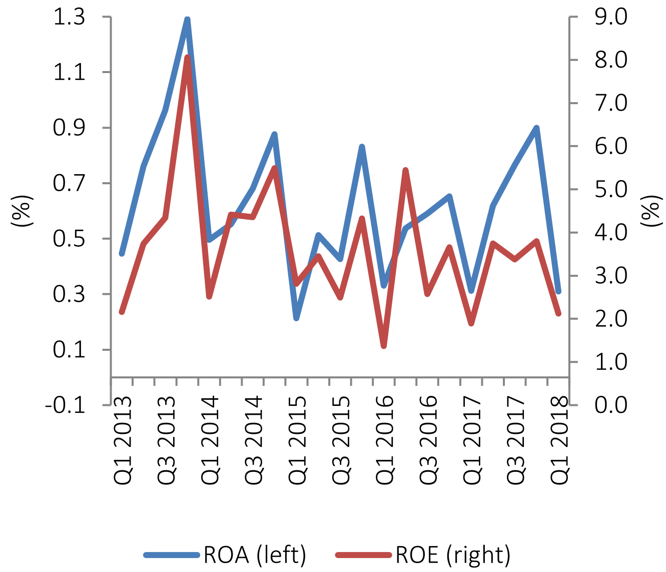
Source: CBB.

Annex 2 Graph 10: NPL's and Provisioning



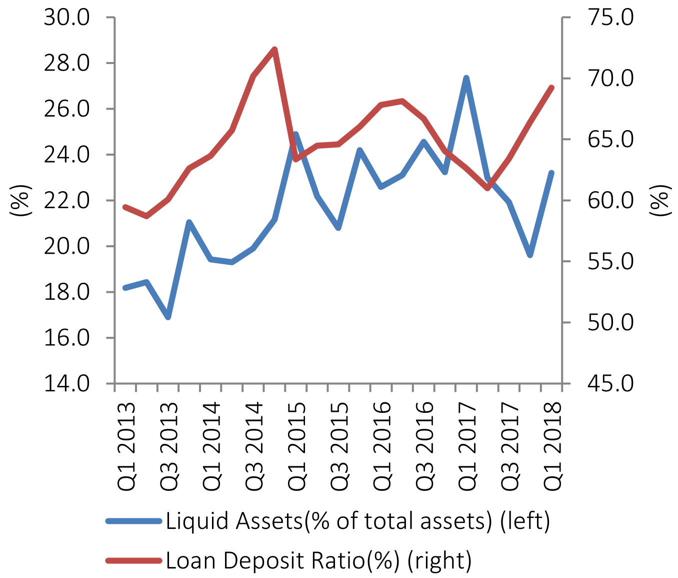
Source: CBB.

Annex 2 Graph 11: Profitability



Source: CBB.

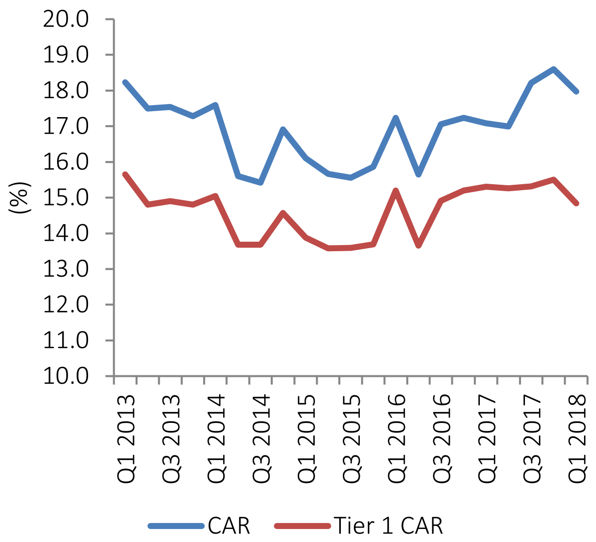
Annex 2 Graph 12: Liquidity



Source: CBB.

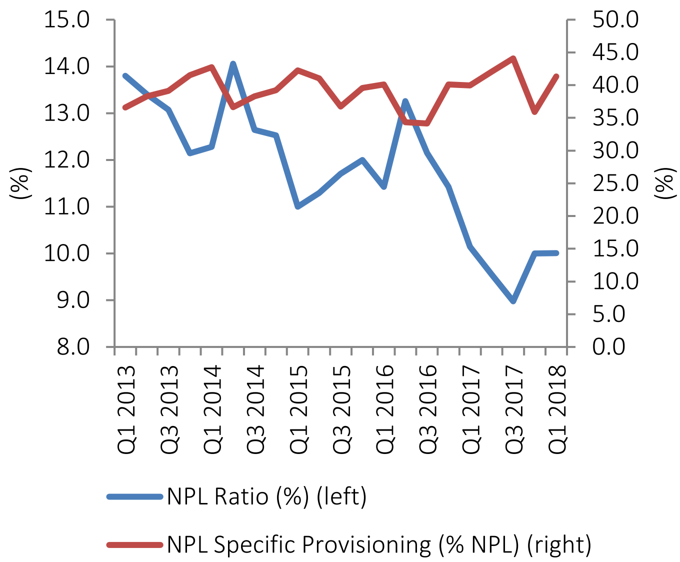
D. Islamic Retail

Annex 2 Graph 13: CAR



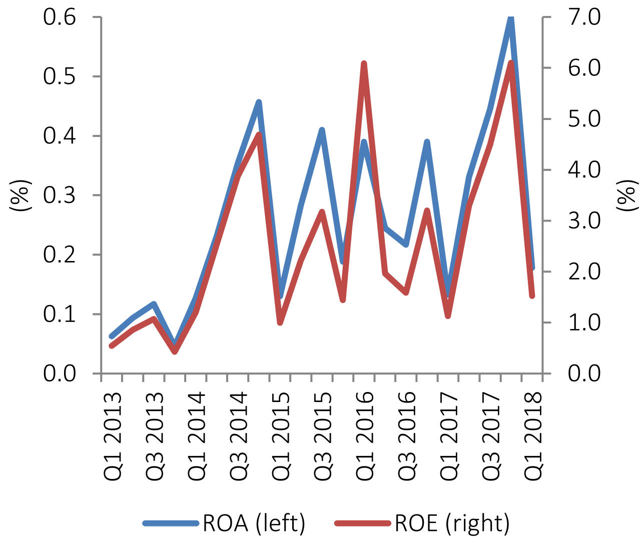
Source: CBB.

Annex 2 Graph 14: NPF's and Provisioning



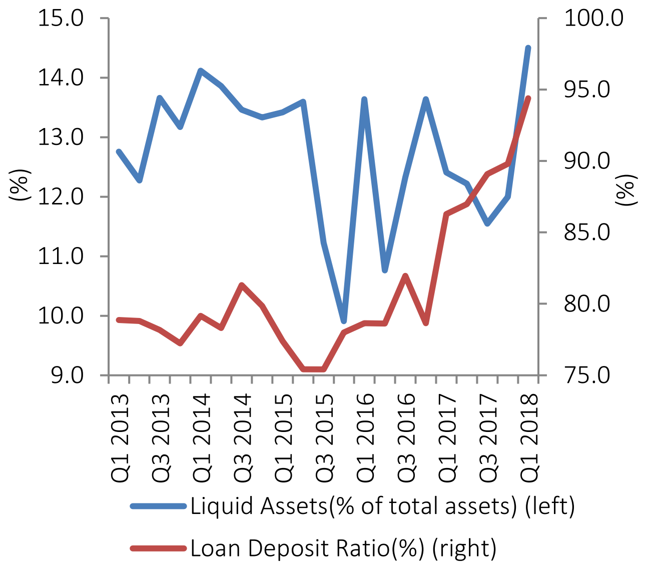
Source: CBB.

Annex 2 Graph 15: Profitability



Source: CBB.

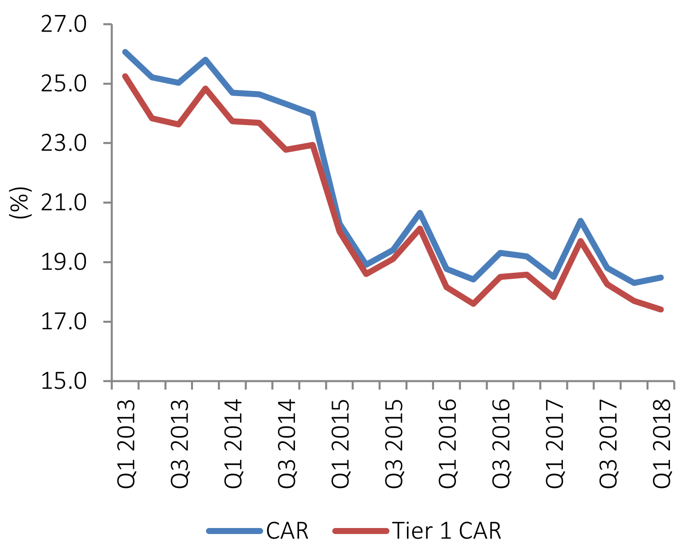
Annex 2 Graph 16: Liquidity



Source: CBB.

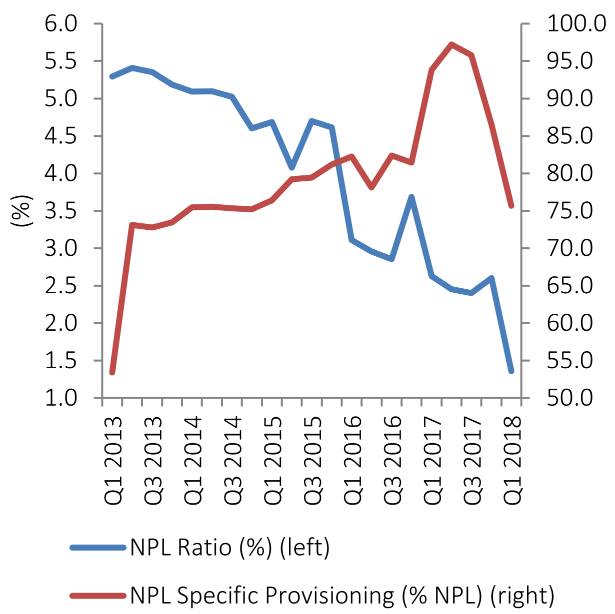
E. Islamic Wholesale

Annex 2 Graph 17: CAR



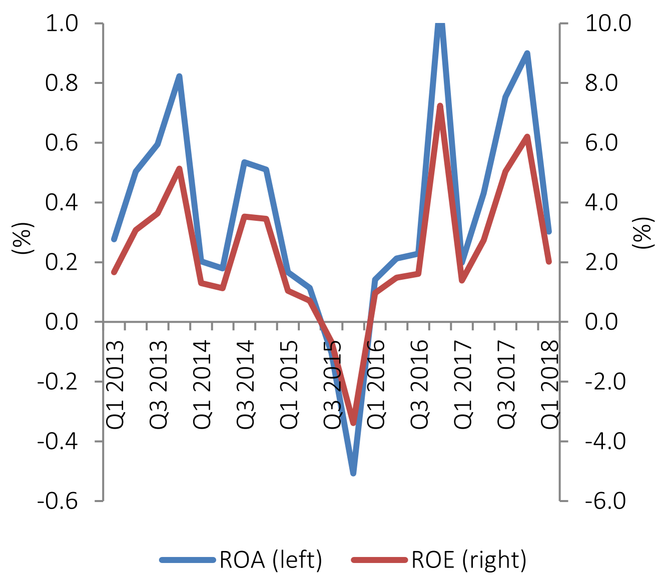
Source: CBB.

Annex 2 Graph 18: NPF's and Provisioning



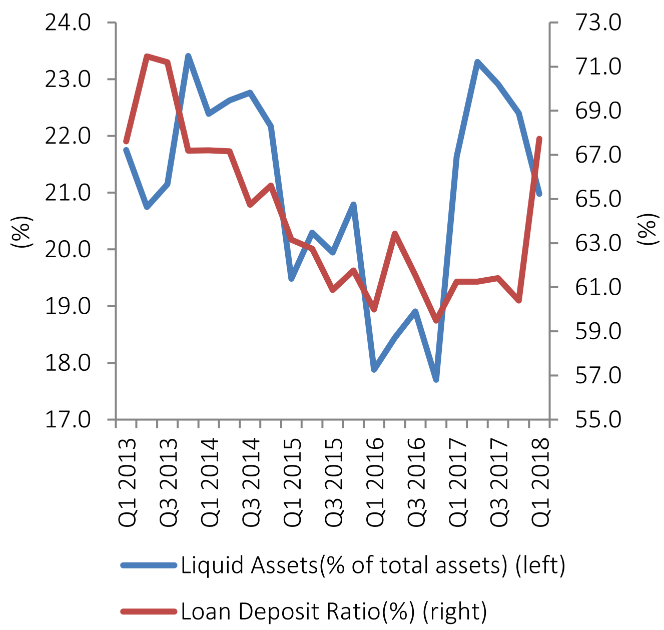
Source: CBB.

Annex 2 Graph 19: Profitability



Source: CBB.

Annex 2 Graph 20: Liquidity



Source: CBB.

List of Acronyms

Acronym	Description
ATM	ATM Clearing System
BCTS	Bahrain Cheque Truncation System
BENEFIT	The Benefit Company
BFB	Bahrain Fintech Bay
BSE	Bahrain Stock Exchange
CAR	Capital Adequacy Ratio
CBB	Central Bank of Bahrain
CMSD	Capital Markets Supervision Directorate
CRB	Conventional Retail Banks
CWB	Conventional Wholesale Banks
DSIBs	Domestically Systemically Important Banks
EBPP	Electronic Bill Presentment and Payment System
EFTS	Electronic Fund Transfer System
EU	European Union
FinTech	Financial Technology
FSC	Financial Stability Committee
FSD	Financial Stability Directorate
FSIs	Financial Soundness Indicators
FSR	Financial Stability Report
GCC	Gulf Cooperation Council
GDP	Gross Domestic Product
GP	Gross Premiums
IBAN	International Bank Account Number
IGA	Information and E-Government Authority
IMF	International Monetary Fund
IRB	Islamic Retail Banks
IWB	Islamic Wholesale Banks
JYP	Japanese Yen
LCR	Liquidity Coverage Ratio
NFA	Net Foreign Assets
NPW	Net Premiums Written
NPF	Non-performing Facilities
NPL	Non-performing Loans
NSFR	Net Stable Funding Ratio
P/E ratio	Price Earnings Ratio
PFMI	Principles for Financial Market Infrastructures
POS	Point of Sale
ROA	Return on Assets
ROE	Return on Equity
RTGS	Real Time Gross Settlement
RWA	Risk Weighted Assets
SMEs	Small Medium Enterprises
SSSS	Scripless Securities Settlement System
TRMST	Technology Risk Management Security Team