FINANCIAL STABILITY REPORT

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مصرف البحرين المركزي

Central Bank of Bahrain

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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 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 maintain monetary and financial stability in the Kingdom of Bahrain. As the single regulator for the financial system, CBB attaches utmost importance in fostering the soundness and stability of financial institutions and markets. 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 to growth, employment and development in Bahrain.

CBB defines financial stability as follows:

A situation where the financial system is able to function prudently, efficiently and uninterrupted, though providing financial services continuously even in the face of adverse shocks.

In pursuit of its objective of promoting financial stability, 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 Directorate (FSD) conducts regular surveillance of the financial system to identify areas of concern and undertakes research and analysis on issues relating to financial stability.

The Financial Stability Report (FSR) is one of the key components of CBB's financial sector surveillance framework. The principal purpose of this report is macro-prudential surveillance, assessing the safety and soundness of the financial system (intermediaries, markets, and payments/settlement systems), identifying potential risks to financial stability and mitigate them before they develop into systemic financial turbulence.

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

- Part I: International and national 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:
    - Chapter 6: Performance of the insurance sector.
    - Chapter 7: Performance of the non-banking financial sector.
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- Part IV: Developments in the payments and settlement systems, fintech, and cyber security:
    - Chapter 9: Performance of payment and settlement systems, point of sale, and digital wallets.
    - Chapter 10: FinTech developments and financial inclusion.

EXECUTIVE SUMMARY

Global Macro Financial Environment Overview

The global economy remains experiencing several challenges. High Inflation, high interest rates due to tightening monetary policy, the geopolitical climate, all have affected the global outlook. In its recent World Economic Outlook (WEO), the International Monetary Fund (IMF) forecasted 3.2% growth in 2022 compared to the 6.0% growth realized last year. Monetary policy tightening remains with the US and other advanced economies raising interest rates to control inflation.

Across major advanced economies, the US economic growth decreased to -0.1% in Q2/2022. The Euro Area (19 countries) and the European Union (EU) (27 countries) experienced growths of 0.8% and 0.7% in Q2/2022. The UK's GDP growth decelerated from 5.6% in Q2/2021 to -0.1% in Q2/2022. BRIICS countries' growth was weaker than expected as it reached the level of -0.5% in Q2/2022.

Financial Sector Overview

The size of the assets of the banking sector in Bahrain was USD 225.1 billion as of June 2022 (5.8 times of GDP). Retail banking total assets continued growing to reach BD 38.2 billion (USD 101.6 billion) in June 2022, wholesale banking sector showed an increase to USD 123.5 billion, and Islamic banking sector assets (which represent 15.7% of the total banking sector assets) increased to USD 35.3 billion.

The total amount of credit given to the private sector (business and personal) by retail banks witnessed a boost with a 5.8% YoY increase moving from BD 10.7 billion to 11.3. The deposit base also witnessed growth to BD 19.9 billion in June 2022 with 56.3% being domestic deposits that had a 1.3% YoY increase. Personal loans and business loans recorded 6.4% and 17.4% YoY growth respectively.

Banking Sector

The banking sector was able to weather challenges brought in by the COVID-19 pandemic with CBB policy and government support which helped maintain the stability in the sector. The capital adequacy ratio (CAR) for the banking sector stood at 19.1% in June 2022. The NPL ratio decreased to 3.3% in June 2022.
Return-on-assets (ROA) remained stable at 0.6% between June 2021 and June 2022, return-on-equity (ROE) increased to 4.6% from 3.9% over the same period. Liquidity positions remained strong as liquid assets as a proportion of total assets stood at 25.7%.

Conventional Banks

The CAR for conventional retail remained stable at 20.4% in June 2022. Asset quality improved as NPL ratio decreased to 3.8% in June 2022 while specific provisions increased to 73.2%. Profitability or retail banks remained positive with ROA increased to 0.8% and ROE to 6.6%. Liquidity position remained at the same level 34.1% in June 2022.

As for wholesale banks the CAR stood at to 17.7% in June 2022. The NPL ratio dropped to 2.5% in June 2022 while specific provisions witnessed a decrease to 69.6%. Profitability was positive as ROA for the conventional wholesale banking remained stable at 0.6% in June 2022 and ROE increased to 2.3%. Liquid assets for wholesale banks as a proportion of total assets decreased to 21.9% in June 2022.

Islamic Banks

The CAR of Islamic retail banks stood at to 21.0% in June 2022. Asset quality improved as non-performing facilities (NPF) ratio decreased by 1.0% to 4.5% in June 2022 while specific provisioning increased to 59.3%. ROA for Islamic retail banks increased to 0.4% in June 2022 and ROE to 5.5%. Liquidity position to Islamic retail banks decreased as liquid assets available to Islamic retail banks decreased from 19.2% of total assets in June 2021 to 19.0% in June 2022.

On the other hand, the CAR for Islamic wholesale banks decreased to 15.3% in June 2022. The NPF ratio for Islamic wholesale banks increased to 6.3% with provisioning for NPFs increasing to 86.7%. Islamic wholesale banks registered positive profitability ROA has reached 0.6% in June 2022 and ROE similarly increased from 3.6% to 5.5%. Liquidity assets decreased for Islamic wholesale to 17.4% of total assets.

Insurance Sector

The Insurance sector in Bahrain is made up of two main segments: conventional and takaful. Total gross premiums registered BD 146.9 million as of June 2022. As of June 2022, total assets of conventional insurance firms were BD 2,136 million, a YoY decrease of 3.6%. Takaful firms' assets was stable at BD 194.6 million.

Viewing the concertation of the overall insurance industry, medical records the highest concentration in Gross Premiums (31.8%) and Gross Claims (36.7%). Conventional local firms accounted for the largest segment of total gross premiums (55.3%), followed by Takaful (28.1%) and conventional overseas branches (16.6%).

For conventional insurance, medical insurance has the highest concentration for Gross Premiums (29.0%) and Gross Claims (33.7%), while motor has the highest concentration in, Net Premiums Written (37.8%) and Net Claims (40.9%). Takaful insurance companies have very high concentration on the medical and motor Insurance business lines as gross Premiums for both sectors represented (65.1%), Net Premiums Written (86.3%), Gross Claims (84.0%), and Net Claims (94.8%).

Capital markets

As of 30th June 2022, Bahrain Bourse recorded a total listing of 42 Companies, 3 Mutual funds and 20 Bonds and Sukuk. During the first half of 2022, there were 20 companies that closed higher and 16 closed lower and 6 remained unchanged. Bahrain All Share Index increased by 2.4% for the year reaching 1,839.6 points, while the Bahrain Islamic Index decreased by 11.2% reaching 667.8 points. As of end-June of 2022, market capitalization of the Bahrain Bourse stood at BD 11.1 billion.

Most of the value and the volume of shares traded in H1 2022 was in the Financials representing 49.3% and 80.0% respectively. Most of the number of transactions in H1 2022 (10,835 transactions) was attained by the Financials sector representing 49.0% of total transactions. As of December 2021, there was 30 private offerings with a total value of USD 2.555 billion.

Payments and Settlement Systems

The RTGS System provides for Payment and Settlement of Customer transactions as a value addition. The daily average volume of Bank transfers for H1 2022 increased to 175 transfers compared to 174 transfers for H1 2021.

The daily average volume of cheques for H1 2022 decreased compared to H1 2021 from 8,679 cheques to 8,524 cheques. The daily average value of cheques increased in the first half of 2022 by 4.9% when compared to the first half of 2021 from BD28.6 million to BD30.0 million. The daily average volume of ATM transactions for H1 2022 decreased by 6.7% compared to H1 2021 to 42,305 per day while the daily average value of ATM transactions increased by 4.8% to reach 4.3 million.

Point of Sale (POS) transactions reached 77.9 million in terms of volume and BD 1,879.6 million in terms of value with a 45.6% and 37.5% increase respectively for 2022 compared to 2021. There is a growing trend in using contactless cards during 2020 and 2022 as contactless transactions reached 75.0% of volume and 47.9% of value in June 2022.

FinTech, Innovation, and Financial Inclusion

Bahrain is repositioning itself to be a Financial Technology (FinTech) hub in the region combining conventional and Shariah compliant FinTech solutions. CBB established a dedicated Fintech Unit on the 22nd of October 2017 to ensure the best services provided to individual and corporate customers in the financial sector. CBB continues its Fintech initiatives as part of its digital transformation strategy to further facilitate a more efficient provision of banking services to customers. As of June 2022, CBB's regulatory sandbox includes 18 companies.

PART I:

DEVELOPMENTS IN THE INTERNATIONAL AND DOMESTIC FINANCIAL MARKETS

1 DEVELOPMENTS IN INTERNATIONAL FINANCIAL MARKET

HIGHLIGHTS

Global Growth	USA Growth	Euro Area Growth
3.2%	1.6%	3.1%
MENA Growth	Advanced Economies Growth	Emerging Market Growth
5.0%	2.4%	3.7%

- The global economy has been recovering from the COVID-19 pandemic, although the bounce-back has been uneven across countries.
- The Russia-Ukraine war has triggered sizable side-effects on the global commodity markets and global value chains are adding uncertainty.
- The lockdowns in China have added pressure on commodity prices while keeping supply chains under strain.
- The rise in inflationary pressures has triggered an almost universal tightening in monetary policy
- Many Central Banks have been raising interest rates in order to put inflation under control and anchor inflation expectations.
- Financial conditions are tightening, borrowing costs are rising and liquidity is shrinking.
- Stock markets indices worsened in the first half of 2022 and Equity markets in Europe have been volatile.

1.1 Overview

The global economy remains experiencing several challenges. High Inflation, tightening monetary policy in most regions, the geopolitical climate with Russia's invasion of Ukraine, and the COVID-19 pandemic all have affected the outlook. As a result, food, energy and commodity prices are still high, affecting household's income and generating a global cost-of-living crisis, especially in low-income countries. The global economic activity deteriorated amid high inflation, aggressive monetary tightening, and uncertainties from the war and the persistence of China "Zero Covid" strategy.

Global economic activity is experiencing a slowdown with inflation levels that were not seen in decades with countries continuing towards monetary and fiscal policy normalization with the aim to lower inflation. The successful calibration of monetary policy, the course of the war in Ukraine, and the possibility of further pandemic-related supply-side disruptions will determine the course of recovery of the global economy.

According to the recent update of the IMF's World Economic Outlook (WEO) in October 2022, global growth was revised to 3.2% in 2022 and 2.7% in 2023 (compared to the 3.6% in 2022 and 3.6% in 2023 in the April 2022 WEO). Advanced Economies are projected to grow by 2.4% in 2022 and Emerging Market and Developing Economies by 3.7% (revised down from the 3.3% and 3.8% projected in the April 2022 WEO). Regarding the world largest three economies, the the IMF revised down the projected

2022 USA growth by 2.1% to reach 1.6%, revised the projected 2022 Euro Area growth upward by 0.3% to reach 3.1%, and revised down the 2022 projected China growth by 1.2% to reach 3.2%.

Global inflation is expected to remain elevated for longer than previously expected reaching 8.8% by 2022. The war induced commodity price and broadening price pressures have let inflation projections of 7.2% in advanced economies and 9.9% in emerging market and developing economies; 1.5% and 1.2% higher than projected in in the April 2022 forecast.

Inflation has proven to be higher and more persistent than expected and remains a global challenge as consumers are feeling the high inflation in decades due to a rise in food and energy prices putting further pressure on household budgets. Inflation was significantly above targets in most advanced economies and emerging markets coupled with a faster than expected reopening fueling a surge in consumer spending with inventories suffering from supply chain disruption.

Several drivers contributed to the current inflation surge. Continued lockdowns and mobility restrictions leading to severe disruptions in various supply chains, causing short-term supply shortages. Another factor is the geopolitical situation due to Russia's invasion of Ukraine that has changed the outlook for the global economy by causing a surge in energy and food prices that affected consumers and businesses. Both Russia and Ukraine are exporters of major commodities, and the disruptions from the war and sanctions have caused global prices to soar.

Predictions are that inflation is to persist longer than previously expected. Impact will likely be bigger for low-income countries and emerging markets, where food and energy are a larger share of consumption. Central banks have a dilemma on how to tackle rising prices and stagflation concerns without slowing off economic recovery from the pandemic. To contain inflation, the Federal Reserve raised the interest rates aggressively in 2022. The rise in US interest rates is driven by worries on the effect on emerging markets with spillovers on economies with macroeconomic vulnerabilities (i.e., have not fully recovered from the pandemic) that are sensitive to the rise in U.S. interest rates.

The duration of the current inflation levels will depend on (1) the relationship between the labor market tightness and supply chain bottlenecks and the central bank response and (2) the duration of the geopolitical tensions and its impact on energy prices, food prices, and global growth.

GCC economies experienced recovery with hydrocarbon prices picking up and relaxation of social distancing measures and increased spending in some countries. Liquidity and fiscal support were above emerging economies. GCC are not insulated from global price developments but the effect remains contained and direct spillovers on the GCC economies from the war in Ukraine have been small.

As for financial stability, concerns show up in price volatility in markets that are leading to higher lending costs. Global financial systems have functioned well throughout the pandemic; however, the current geopolitical climate is amplifying existing risks. Rising inflation and interest rates will make it difficult for some borrowers to meet debt payments. Large falls in property or financial asset prices would be disruptive for financial markets and the economy.

In the following sections, recent trends in the global economy are highlighted and the major financial and economic indicators during the first half of 2022.

1.2 Global Macro-financial Environment

The global economic and financial conditions have deteriorated remarkably during the first half of 2022. The Russia-Ukraine war has weighted on the world economy as It is disrupting trade, leading to shortages of materials and contributing to soaring energy and commodity prices. Therefore, after a long period of price stability, inflation has returned in developing and developed countries affecting household's purchasing power and generating a worldwide cost-of-living crisis.

In its October 2022 World Economic Outlook update, the IMF forecasted the global economy to slow from 6.0 % last year to 3.2 % in 2022.

1.2.1 Economic Performance

Despite the Russia-Ukraine war, the economic performance in Europe was robust during the first semester of 2022 thanks to the relaxation of COVID-19 restrictions, and to the back to normal economic activity. However, uncertainty and geopolitical tensions have put additional downward pressure on financial sector in Europe which in turn amplified volatility and raised new concerns in the global financial markets. Particularly, the risk of a potential cut of Russia gas toward Europe during next Winter could generate potential challenges.

As Chart 1.1 shows, after witnessing negative growth in 2020, most European economies were performing better all over 2021 because most European countries moved toward normalization of economic activities as vaccine rollout proceeds and governments additional fiscal support reflecting tighter restrictions in the second semester of the year. As a result, European countries recovered faster than expected in 2021. However, a slowdown of economic activities has been recorded during the first semester of 2022. For example, growth rate in Spain moved from 2.2% in Q4/2021 to 0.2% in Q1/2022. Similarly, Italy, GDP moved from 2.7% in Q4/2021 to 0.1% in Q1/2022. As for Portugal, growth rate increased from 1.7% in Q4/2021 to 2.5% in Q1/2022.

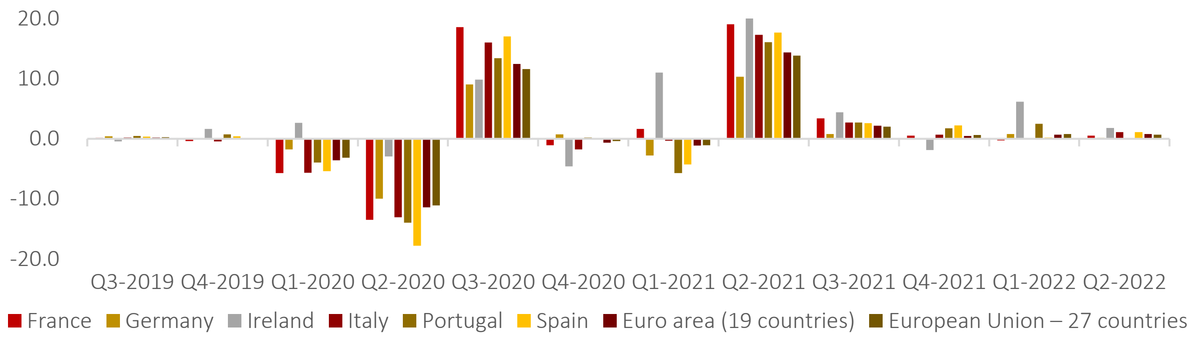
Regarding the two largest economies in the Eurozone, their performances improved in the second half of 2021 but slowed down in the beginning of the year 2022. Germany economic recovery took a temporary pause despite the recovery from the waves of the COVID-19 pandemic. High inflation, the Russia-Ukraine war and continued bottlenecks are the main results of the slowdown of the German economy. During the first semester of 2022, inflation reached 6.8%, the highest level since 1974. The IMF expects German economic growth to slow sharply to 1.2 percent in 2022 owing to elevated energy import prices and weak consumer confidence.

France after the end of the pandemic-related lockdowns, tensions gradually emerged in commodity prices, combined with increasing supply disruptions. These difficulties intensified significantly at the start of 2022 with the outbreak of the Ukraine conflict and the reintroduction of lockdown measures in some areas of China.

In the first quarter of 2022, GDP dropped by 0.2% (QoQ), reflecting a marked 1.5% decline in household consumption and weaker than expected exports. In the second quarter, GDP growth increased by 0.5% thanks to the recovery of tourism and also to some services sectors that are benefiting from the lifting of the last pandemic-related restrictions. France is currently facing stronger inflationary pressures on energy and food prices which in turn will affect household's purchasing power, consumption, production and growth.

Turning to the Euro Area (19 countries) and the European Union (EU) (27 countries) their economies have also experienced a better-than-expected recovery in 2021 with growth rates reached of 5.4% and 5.1% respectively. This performance is due to the gradual normalization of economic activity of many European countries that supported the recovery. However, the Russia-Ukraine war continues to negatively affect the EU economy, setting it on a path of lower growth and higher inflation. Growth in the euro area is expected at 2.6% in 2022, moderating to 1.4% in 2023. Annual average inflation is projected to peak at historical highs in 2022, at 7.6% in the euro area and 8.3% in the EU, before easing in 2023 to 4.0% and 4.6%, respectively.

Chart 1.1: Real GDP Growth in Selected Europeans Countries (Quaterly %) Seasonally Adjusted*



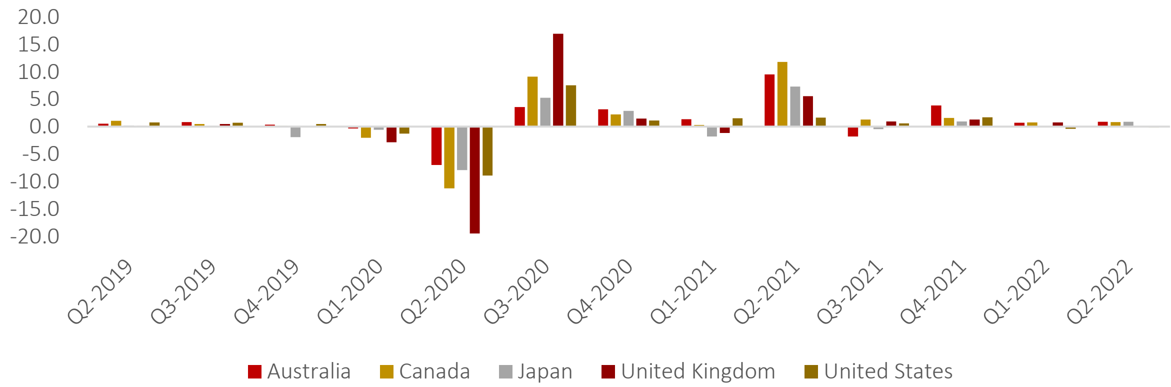
**Growth rate compared to the same quarter of previous year, seasonally adjusted.*
Source: OECD Quarterly National Accounts.

In the United Kingdom, after the economic activity returned to its pre-pandemic level in the beginning of 2022, new shocks hit the UK economy. The Russia-Ukraine war has negatively impacted the UK economy triggering a cost-of-living crisis. In fact, inflation reached 9.1% in May, its highest rate since March 1982. Furthermore, the rising tax burden has led to a fall in consumer confidence which is set to drag on discretionary spending. All these issues could lead to a significant deceleration in economic growth and potentially to a mild recession.

The economic outlook for the United States has deteriorated considerably amid soaring energy and commodity prices, tighter labor market conditions and aggressive monetary tightening by the Federal Reserve. After expanding by 5.7% in 2021, GDP contracted in the first and second quarter of 2022.

Japan's economy returns to pre-pandemic levels but may slow down again. Gross domestic product grew by 0.5% in the second quarter of 2022, but inflation is beginning to weigh on household consumption and economic activity. According to the IMF's world Economic Outlook, Japan is anticipated to see a steady growth by 1.7% for 2022 and 2023.

Chart 1.2: Real GDP Growth in Advanced Economies (Quaterly %) *



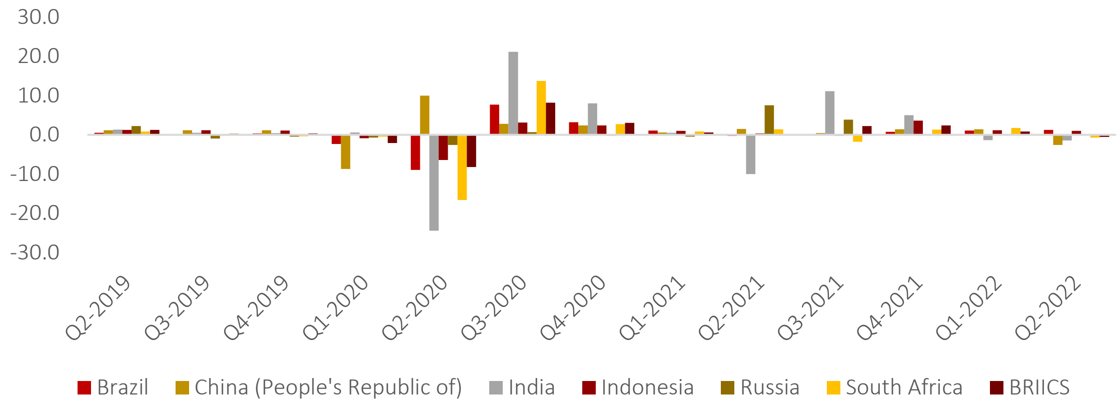
** Growth rate compared to the same quarter of previous year, seasonally adjusted*
Source: OECD Quarterly National Accounts.

As for emerging economies (Chart 1.3), the BRIICS countries' growth was weaker than expected as it reached the level of 4.7% in Q3/2021 from 12.2% achieved in Q2/2021.

Recent data shows that China economy is projected to slow to about 4% in 2022 due to the new waves of COVID-19 infections, the multiple lockdowns and the rising geopolitical risks. In Q2/2022, GDP growth fell to a two-year low of 0.4% as China's zero-tolerance COVID-19 measures were introduced to control the rise of the Omicron Variant of COVID-19. The growth is expected to gain momentum in the second half od 2022 and into 2023.

Similarly, India is expected to reach a growth rate by 7.4% in 2022, lower than the 9.1% achieved in 2021. Recently, the Reserve Bank of India has revised up its benchmark repo rate by 140 basis points, including 50 basis points in August, while warning about the impact of a global slowdown on domestic growth prospects. Turning now to Brazil and South Africa, they are looking to rebuild fiscal buffers and have also begun normalizing monetary policy to head off upward price pressures. The IMF expected Brazil and South Africa to achieve growth rates by 1.7 and 2.3% respectively in 2022.

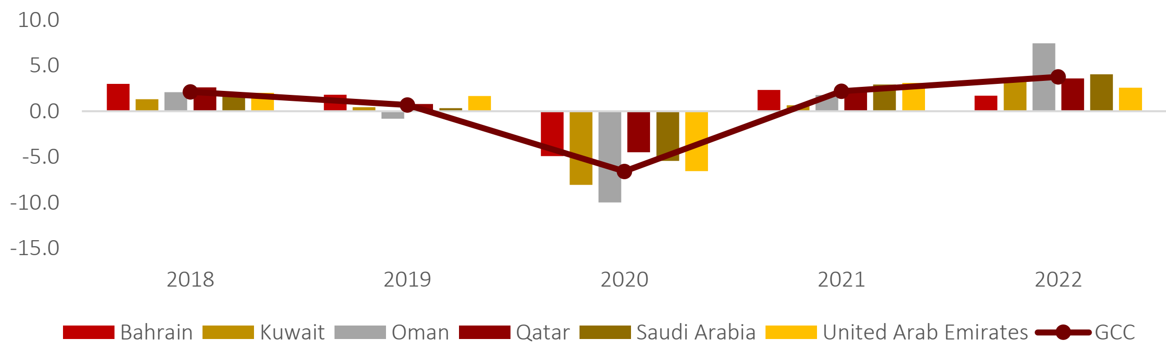
Chart 1.3: Quaterly Real GDP Growth in BRIICS (Quaterly %) *



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

Regionally, the COVID-19 pandemic hit the economic activities of all GCC countries in 2021. Moreover, the drop of oil prices since have added pressure on GCC public finance condition and caused a sharp deterioration of external and fiscal balances. Since the beginning of 2022, the pandemic was under control and economic activity went back to normal thanks to the release of the uncountable various restrictions imposed by the governments. The rise in oil and energy prices have helped GCC country to build buffers and to improve their fiscal unbalances that the GCC countries have witnessed during the past few years. As a result, the economies of the Gulf Cooperation Council (GCC) are projected to expand by 5.9% overall in 2022, with this recovery likely to continue in the medium-term, driven by the hydrocarbon and non-hydrocarbon sectors.

Chart 1.4: Real GDP Growth in GCC Countries (Annual percent change)

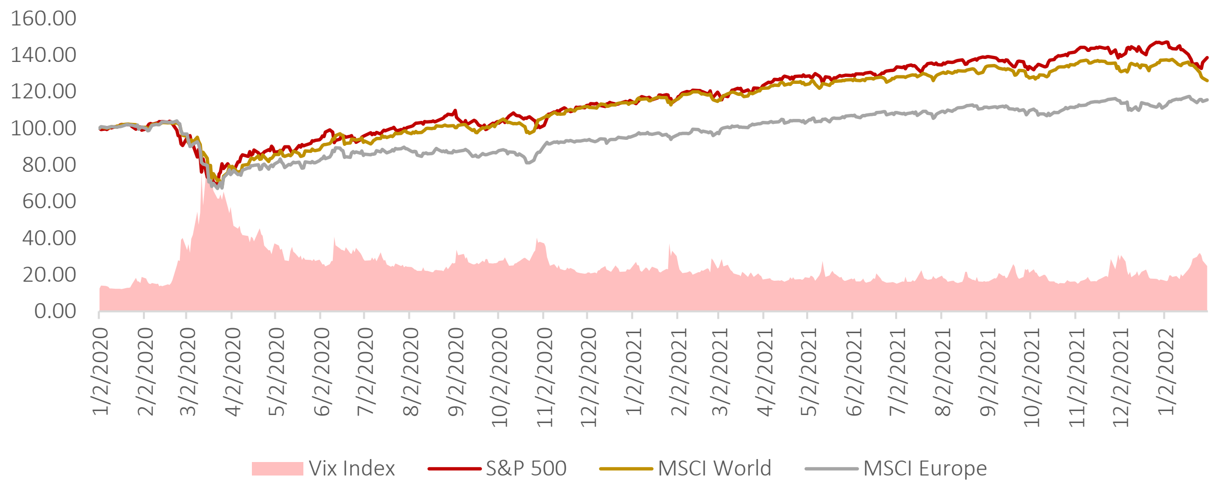


**Forecasts. Source: IMF Regional Economic Outlook, April 2021.*

1.2.2 Financial Markets

Despite all the pandemic challenges, financial conditions have remained supportive in the first and second quarter of 2021. Financial market sentiment has remained positive on balance given the expected global recovery. However, the increasing number of concerns such as the new COVID-19 lockdowns in early 2022, the economic slowdown in China, the Russia/Ukraine war, surging inflation and central-bank tightening have triggered a chaos in the equity market. In fact, all three major U.S. stock indexes finished the second quarter of 2022 in negative territory, with the S&P 500 notching its steepest first-half percentage drop since 1970, down 20.6%. The MSCI global stock index notched its biggest first-half of a year percentage drop on record on June 2022.

Chart 1.5: Global Equity Market Indices (Re-indexed to January 2020)



Source: Bloomberg.

2 DEVELOPMENTS IN THE FINANCIAL AND NON-FINANCIAL SECTORS

HIGHLIGHTS

Financial Sector % of GDP	Number of Licenses	Banking Sector Assets
17.4% Q1 2022	362 June 2022	USD 225.1 bn ▲ 5.6% YoY
Retail Banking Assets	**Wholesale Banking Assets**	**Islamic Banking Assets**
USD 101.6 bn ▲ 4.5% YoY	USD 123.5 bn ▲ 6.5% YoY	USD 35.3 bn ▲ 8.1% YoY
M2	**Personal Credit**	**Business Credit**
BD 13.8bn ▲ 2.5% YoY	BD 5.6 bn ▲ 17.4% YoY	BD 5.1 bn ▼ 6.4% YoY

- The size of the assets of the banking sector in Bahrain was USD 225.1 billion as of June 2022
- The retail banking sector assets increased to USD 101.6 billion and wholesale banking sector assets increased to USD 123.5 billion as of end-June 2022 representing 45.1% and 54.9% respectively.
- The volume of credit increased by 5.8% to BD 11,345.7 million in June 2022.
- Household debt ratio witnesses an increase while business debt decreases.

2.1 Overview

This chapter assesses the recent developments of the Bahraini financial and non-financial sectors. 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. 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 Financial Sector Developments

Bahrain's 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 financial sector is currently the largest non-oil contributor to GDP representing 17.3% of real GDP in 2020 showing an increase from the 16.1% in 2019 and 16.9% in 2018. In Q4 of 2021, the financial sector represented 17.7% of real GDP. In Q1 2022, the financial sector represented 17.4% of real GDP.

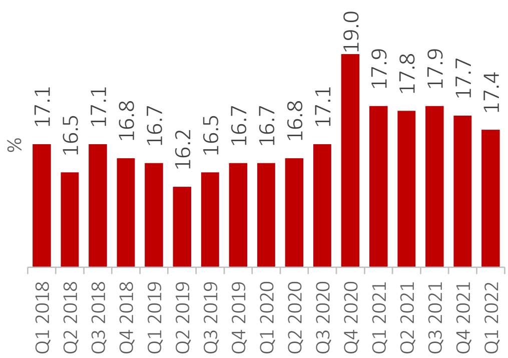
As of end of June 2022, there were 362 licenses issued by CBB (bank and non-bank financial institutions). The banking sector in Bahrain was made up of 87 banks, categorized as follows:

- Retail banks: 30 retail banks that include 24 conventional (7 locally incorporated and 17 branches) and 6 Islamic retail banks.
- Wholesale banks: 57 wholesale banks that include 49 conventional (13 locally incorporated and 36 branches) and 8 Islamic wholesale banks.

The 267 non-banking financial institutions operating in Bahrain includes investment business firms, insurance companies (including Takaful and Re-Takaful firms), representative offices and specialized licenses.

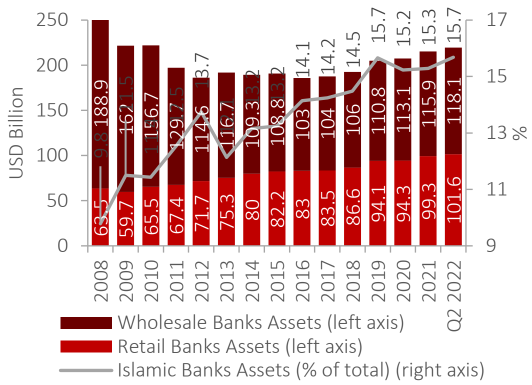
The size of the assets of the banking sector in Bahrain was USD 225.1 billion as of June 2022 (5.6% YoY increase). Table 2.1 shows the change of the size of the various banking segments to GDP. Retail banking continued to grow over the years reaching USD 101.6 billion by Q2 2022 along with the growth of size to GDP. The size of the wholesale banking sector declined between 2014 and 2017 then started to increase with an annual increase of 2.0% in 2018, 4.5% in 2019 and 2.0% in 2020. In June 2022, the size of the wholesale banking sector reached USD 123.5 billion increasing 6.5% YoY. As for the Islamic banking sector, it grew steadily over the same period to reach USD 35.3 billion in June 2022 representing 15.7% of the size of the banking sector.

Chart 1.6: Size of the Financial Sector to Real GDP



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

Chart 1.7: Banking Sector Asset Composition



Source: CBB Monthly Statistical Bulletin.

Table 1.1: Evolution of the size of the Banking sector in Bahrain

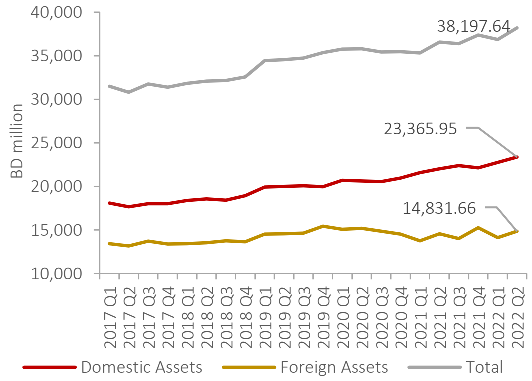
Indicator	2015	2016	2017	2018	2019	2020	2021*	Q2 2022*
Banking Sector (USD billion)	191.0	186.1	187.4	192.6	204.9	207.4	217.5	225.1
times GDP	6.1	5.8	5.3	5.1	5.3	5.4	6.1	5.8
Retail Sector (USD billion)	82.2	83.0	83.5	86.6	94.1	94.3	99.4	101.6
times of GDP	2.6	2.6	2.4	2.3	2.4	2.5	2.8	2.6
Wholesale Sector (USD billion)	108.8	103.0	104.0	106.0	110.8	113.1	118.1	123.5
times of GDP	3.5	3.2	2.9	2.8	2.9	2.9	3.3	3.2
Islamic Sector (USD billion)	25.3	26.3	26.7	27.9	32.1	31.6	34.6	35.3
times of GDP	0.8	0.8	0.8	0.7	0.8	0.8	1.0	0.9

** Using provisional current GDP data.*
Source: CBB Monthly Statistical Bulletin.

2.2.1 The Retail Banking Sector

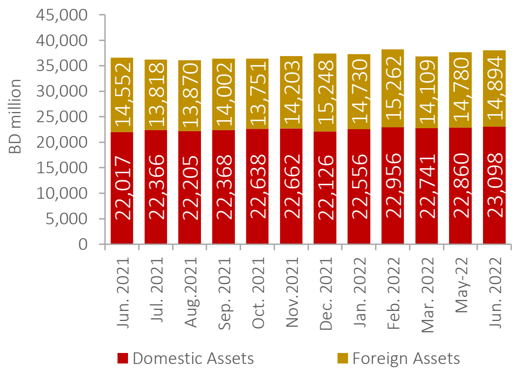
Retail banking assets continued growing to reach BD 38.2 billion (USD 101.6 billion) in June 2022 with a 4.5% year-on-year (YoY) increase (see Chart 2.3). As of June 2022, domestic assets comprised 61.2% of total assets with YoY growth of 6.1% while foreign assets comprised 38.8% of total assets with a YoY growth of 1.9%.

Chart 1.8: Retail Banks' Assets



Source: CBB Monthly Statistical Bulletin.

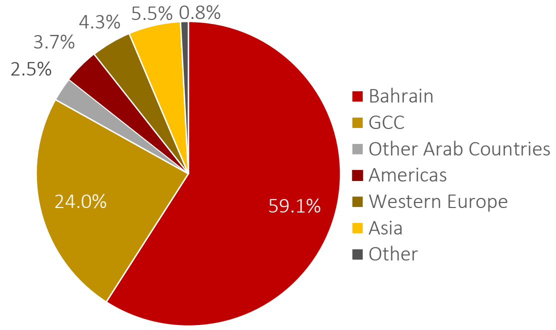
Chart 1.9: Categorization of Retail Banks' Assets



Source: CBB Monthly Statistical Bulletin.

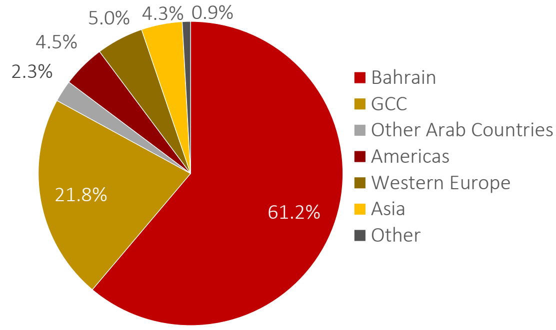
Retail-banking sector in Bahrain is relatively exposed to foreign risk regionally from GCC countries and lightly exposed to foreign risk from Europe and U.S as the share of GCC assets of total retail banking assets was 21.8% and European and the Americas contribution was 9.5%.

Chart 1.10: Retail Banks' Assets (%) by Geographical Classification (December 2021)*



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

Chart 1.11: Retail Banks' Assets (%) by Geographical Classification (June 2022)*



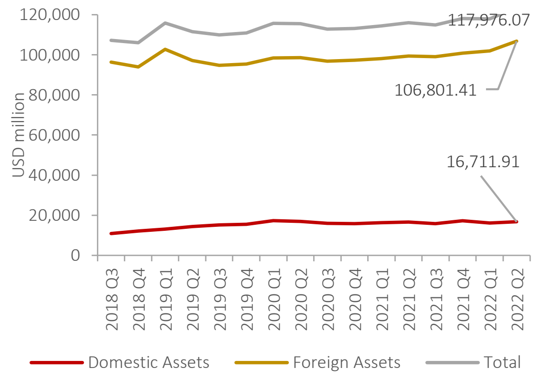
** For conventional and Islamic retail banks.*
Source: CBB Monthly Statistical Bulletin.

2.2.2 The Wholesale Banking Sector

The wholesale banking sector increased to USD 123.5 billion in June 2022 with a YoY growth of 6.5%. As of June 2022, domestic assets, representing 13.5 % of total assets, witnessed a YoY growth of 0.6% while foreign assets made 86.5% of total assets with a 7.5% YoY increase (See Charts 2.7 and 2.8).

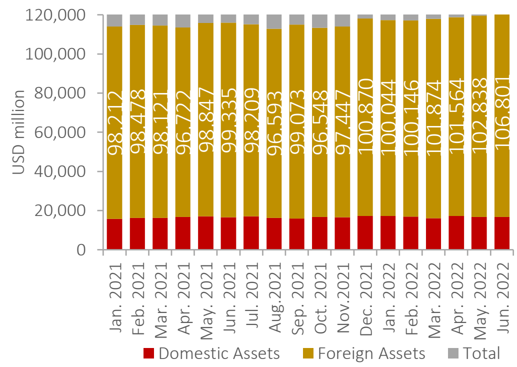
According to the geographical classification of wholesale banks' assets, wholesale banks are exposed to foreign risk from Western Europe and GCC countries. The share of GCC assets increased to 31.0% in June 2022, which represents the larger portion of wholesale bank assets compared to Europe. The share of Europe's total assets decreased to 29.0%, making it the second largest portion of wholesale bank assets. The share of America's total assets increased from 11.1% in December 2021 to 12.2% in June 2022. Asian assets remained at 7.3% in June 2022.

Chart 1.12: Wholesale Banks' Assets



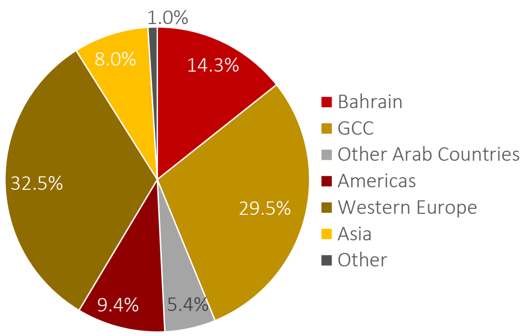
Source: CBB Monthly Statistical Bulletin.

Chart 1.13: Categorization of Wholesale Banks' Assets



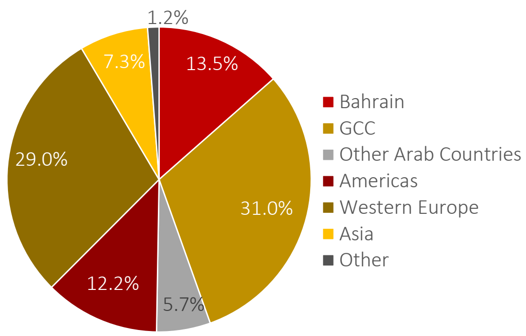
Source: CBB Monthly Statistical Bulletin.

Chart 1.14: Wholesale Banks' Assets by Geographical Classification (June 2021) *



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

Chart 1.15: Wholesale Banks' Assets by Geographical Classification (June 2022) *

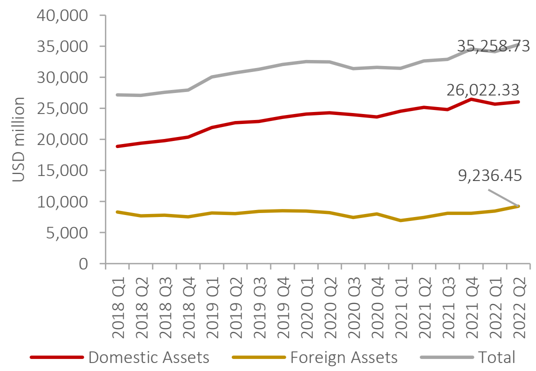


** For conventional and Islamic wholesale banks.*
Source: CBB Monthly Statistical Bulletin.

2.2.3 The Islamic Banking Sector

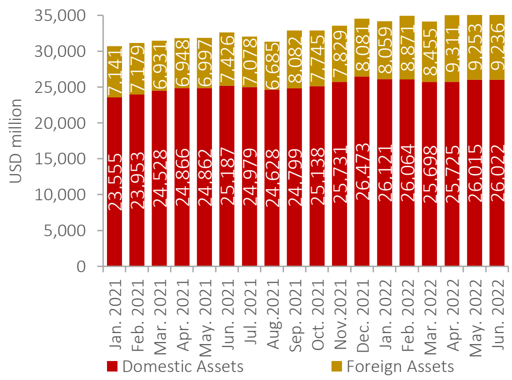
The Islamic banking sector increased to USD 35.3 billion as of June 2022 indicating a 8.1% YoY increase. Domestic assets represented 73.8% of total Islamic banking assets in the sector (3.3% YoY increase) while foreign assets represented 26.2% of total Islamic banking assets (24.1% YoY increase).

Chart 1.16: Islamic Banks' Assets



Source: CBB Monthly Statistical Bulletin.

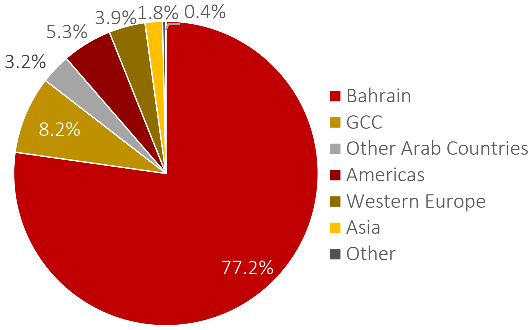
Chart 1.17: Categorization of Islamic Banks' Assets



Source: CBB Monthly Statistical Bulletin

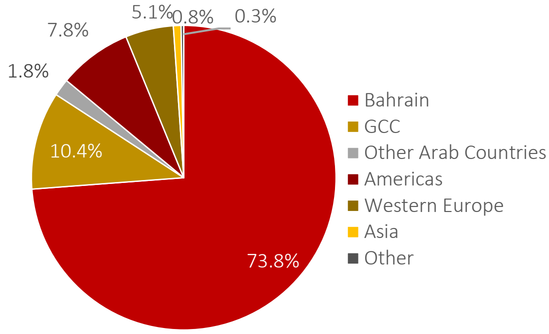
Islamic banks continue to be majorly exposed to domestic risks as the share of Bahrain's total assets decreased to 73.8% in June 2022 while GCC total assets was 10.4%.

Chart 1.18: Islamic Banks' Assets by Geographical Classification (June 2021)



Source: CBB Monthly Statistical Bulletin.

Chart 1.19: Islamic Banks' Assets by Geographical Classification (June 2022)

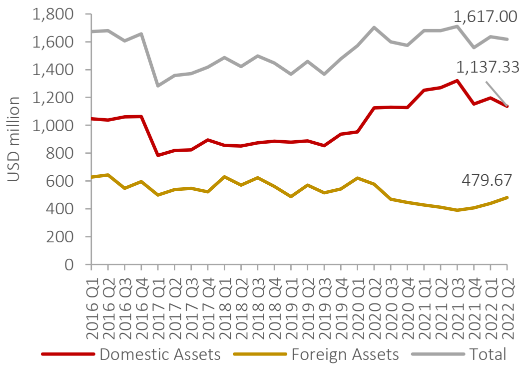


Source: CBB Monthly Statistical Bulletin.

2.2.4 Islamic Windows

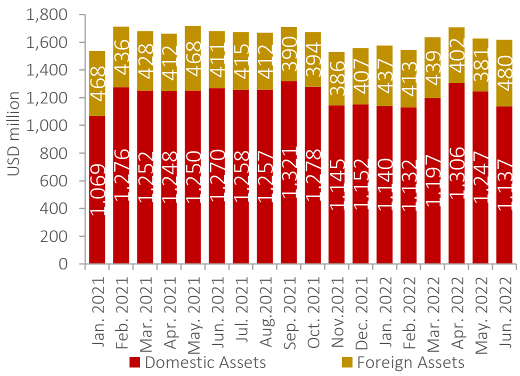
There are a number of conventional retail banks in Bahrain that maintain Islamic windows offering Islamic banking services/products to clients who are interested in completing their banking transactions in a Sharia-compliant system. As of June 2022, there were 5 Islamic windows operating by conventional retail licenses in Bahrain with total assets of BHD 1.6 billion (4.3% of retail banking assets). As of December 2021, 73.9% of total assets were domestic (2.2% YoY increase) while 26.1% were foreign (9.9% YoY decrease).

Chart 1.20: Islamic Windows' Assets



Source: CBB Monthly Statistical Bulletin.

Chart 1.21: Categorization of Islamic Windows' Assets

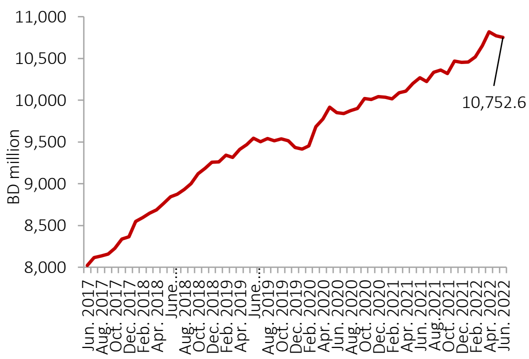


Source: CBB Monthly Statistical Bulletin.

2.2.5 Credit Developments

Credit given to the private sector (business and personal) by retail banks witnessed a YoY increase of 4.7% moving from BD 10.3 billion in June 2021 to BD 10.8 billion in June 2022 (Chart 2.17). Regarding retail banks' lending to the general government, there was an increase of BD 142.9 million at end-June 2022, from BD 450.2 million at end-June 2021 (Chart 2.18).

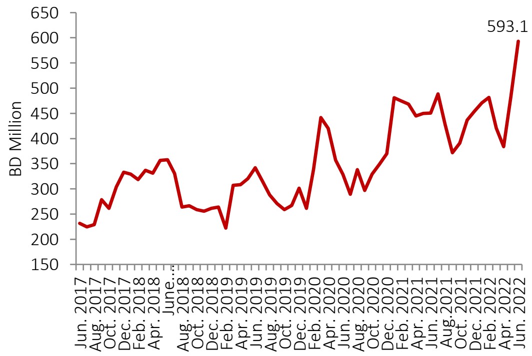
Chart 1.22: Loans to the Private Sector *



Source: CBB Monthly Statistical Bulletin.

*** Excluding securities.*

Chart 1.23: Loans to General Government *



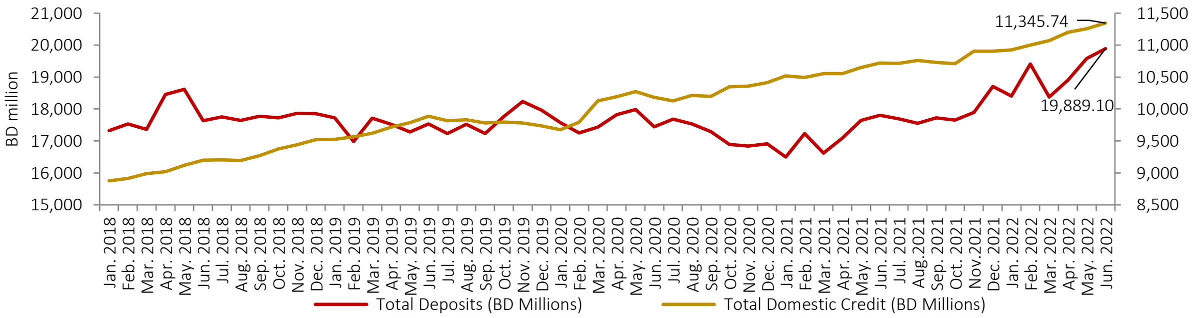
Source: CBB Monthly Statistical Bulletin.

*** Excluding securities.*

Despite a challenging economic environment during the pandemic, banks were active in lending activities driven mainly by some sectors such as mortgage lending and lower interest rates.

Total deposits reached BD 19.9 billion in June 2022 with a 11.7% YoY growth (where domestic deposits represent 56.3% of total deposits and had a YoY increase of 1.3%). Households boosted their savings amounts as a precautionary measure with extra savings due to the loan deferrals that was flowing into bank deposits. Domestic credit increased from BD 10,719.0 in June 2021 to 11,345.7 in June 2022 with a 5.8% YoY increase (Chart 2.19).

Chart 1.24: Total Deposits and Total Domestic Credit (BD Million)



Source: CBB Monthly Statistical Bulletin.

2.2.6 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. The NFA position by banking segment, as of June 2022, is negative (net borrowers) for retail banks, both conventional and Islamic, and conventional wholesale banks. As of June 2022, the NFA position for retail banks was *negative* USD 6,671.1 million and for wholesale banks, the NFA position was *negative* USD 520.8 million.

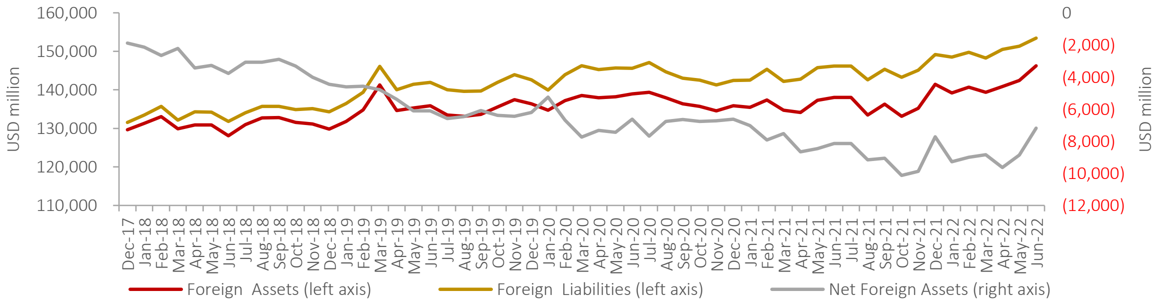
Table 1.2: Net Foreign Assets Postion by Banking Segment (June 2022)

Banking Segment (USD million)	Foreign Assets	Foreign Liabilities	Net Foreign Assets
Total Banking Segments	**146,247.3**	**153,439.2**	**(7,191.9)**
Retail (Conventional and Islamic)	**39,445.9**	**46,117.0**	**(6,671.1)**
Conventional Retail	36,790.6	40,317.1	(3,526.3)
Islamic Retail	2,655.3	5,714.1	(3,058.8)
Wholesale (Conventional and Islamic)	**106,801.4**	**107,322.2**	**(520.8)**
Conventional Wholesale	100,220.2	101,658.3	(1,438.1)
Islamic Wholesale	6,581.2	5,663.9	917.3

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 negative NFA position. Looking at the NFA position for the overall banking sector, data shows that there was an upward trend starting October 2021 as seen in the chart below.

Chart 1.25: Net Foreign Assets of the Overall Banking Sector

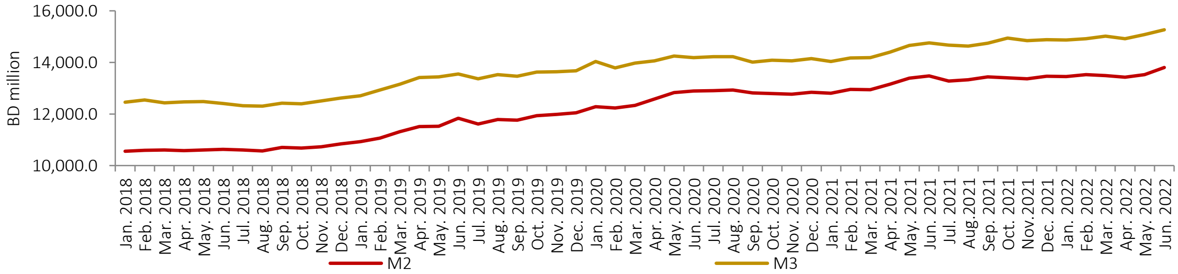


Source: CBB.

2.3 Monetary Indictors

Money supply continued to grow. M2 stood at BD 13,802.4 million in June 2022, 2.5% higher than its value of December 2021. M3 was at BD 15,265.1 million in end-June 2022, 2.6% higher than in December 2021 (Chart 2-22).

Chart 1.26: Money Supply (BD million)



Source: CBB Monthly Statistical Bulletin.

Table 2.3 sets out an analysis of Bahrain's M1, M2 and M3 money supply as at the dates indicated.

Table 1.3: Money Supply Composoition

	2019		2020		2021		June 2022	
	BD million	% Change	BD million	% Change	BD million	% Change	BD million	% Change
Currency Outside Banks	535.1	1.3	593.0	10.8	558.0	-5.9	562.8	0.9
Demand Deposits	2978.5	2.9	3.288.0	10.4	3,952.0	20.2	4,300.6	8.8
M1	**3,513.6**	**2.7**	**3,880.9**	**10.5**	**4,510.0**	**16.2**	**4,863.4**	**7.8**
Time and savings deposits	8,538.6	15.0	8,959.0	4.9	8,955.4	0.0	8,939.0	(0.2)
M2	**12,052.2**	**11.1**	**12,840.0**	**6.5**	**13,465.4**	**4.9**	**13,802.4**	**2.5**
General Government Deposits	1,619.7	-8.8	1,311.3	-10.0	1,418.8	8.2	1,462.7	3.1
M3	**13,671.9**	**8.3**	**14,151.3**	**3.5**	**14,884.2**	**5.2**	**15,265.1**	**2.6**

Source: CBB Monthly Statistical Bulletin.

As of June 2022, growth in money supply was stimulated by a growth in demand deposits. In particular, demand deposits increased by 8.8% from BD 3,952.0 million in December 2021 to BD 4,300.6 million in June 2022, while time and savings deposits remained decreased slightly below December 2021 levels.

2.4 Inflation

CBB maintains the Bahraini Dinar's peg against the U.S. Dollar, which has provided price stability over the years and as a result managed to keep inflation relatively stable. Bahrain's inflation is measured by its Consumer Price Index (CPI) and includes 12 broad categories of consumer goods that are representative of consumption patterns in the economy.[1] Since 2014, there was a reversal of the deflationary trend seen over the preceding three years and consumer prices increased moderately.

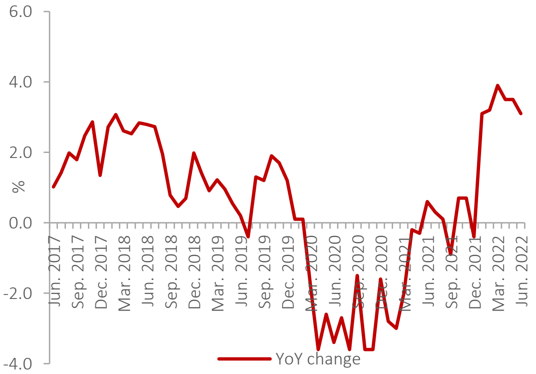
As of June 2022, the Consumer Price Index (CPI) stood at 100.0 points. Monthly inflation stayed at -0.1%. The division which caused the largest upward contribution to the CPI in the year were food and non-alcoholic beverages group (+7.3) and hotel and restaurants (+14.5). However, the divisions which caused the largest downward contribution to the CPI in the year were transport and housing, water, electricity, gas and other fuels (-1.4).

The CPI in June 2022 was 3.1% higher than a year earlier which shows price level recovery following the deflation that happened due to the effects of the COVID-19 pandemic and to the economic stimulus

[1] The index has been rebased to April 2019=100, with effect from May 2019, which resulted in certain methodological changes which include updating the expenditure weight, revising the sample of goods and services and improving the methods of price collection. Components are: food and non-alcoholic beverages; alcoholic beverages, tobacco and narcotics; clothing and footwear; housing, water, electricity, gas and other fuels; furnishing, household equipment and routine household maintenance; health; transport; communication; recreation and culture; education; restaurants and hotels; and miscellaneous goods and services.

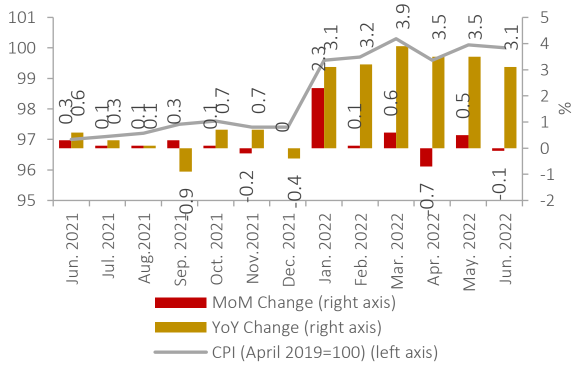
package released by the government to support households and businesses and in line with the global inflation increases.

Chart 1.27: CPI Change (Jun. 2017 – Jun. 2022)



Source: IGA.

Chart 1.28: Monthly Inflation Rate (June 2020 –June 2022)



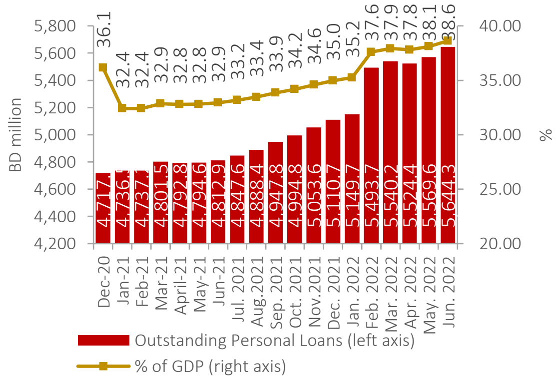
Source: IGA.

2.5 The Households/Personal 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.

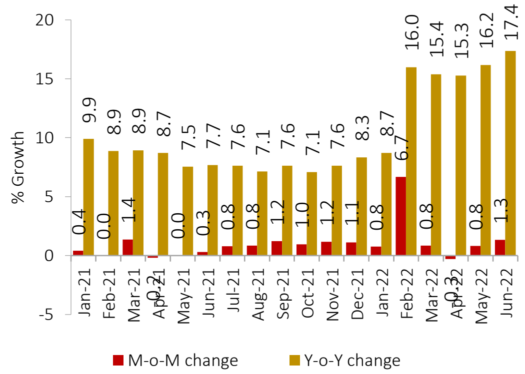
Outstanding personal loans, used as a proxy for household borrowing, shows an increase in personal credit between June 2021 and June 2022 (Chart 2.24).

Chart 1.29: Personal Loans and Advances (Volume and % of GDP)



**Using 2020 GDP.*
Source: CBB Monthly Statistical Bulletin.

Chart 1.30: Growth Rates of Total Personal Loans and Advances (%)



Source: CBB Monthly Statistical Bulletin.

Personal loans as a percentage of GDP increased to 38.6% by June 2022 (BD 5,644.3 milllon). There was a 10.1% increase in outstanding personal loans between December 2021 and June 2022 (YoY increase was 17.4%).

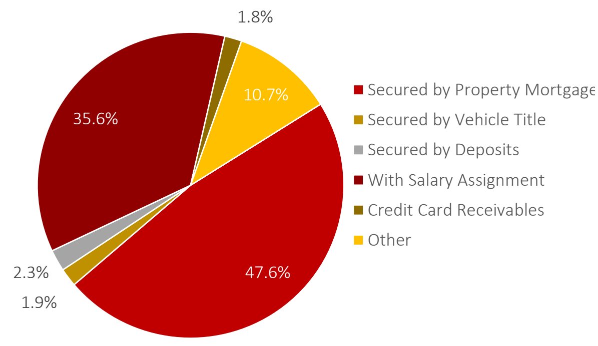
The monthly growth rate in total personal loans and advances fluctuated between December 2021 to June 2022. Initially at 0.8% in June 2021, it rose to reach its highest level for the year of 6.7% in Febuary 2022 and later fell to reach 1.3% in June 2022. On a yearly basis, the biggest YoY increase was in June 2022 where the personal loans and advances were at 17.4%, the two main contributors to personal loans as seen in chart 2.26 were personal loans secured by property mortgages which made up 47.6% of the total personal loans followed by personal loans secured with salary assignments at 35.6% of total personal loans.

Table 1.4: Personal Loans Breakdown

BD million	Dec. 2021	Jan. 2022	Feb. 2022	Mar. 2022	Apr. 2022	May 2022	Jun. 2022
Total	5,110.7	5,149.7	5,493.7	5,540.2	5,524.4	5,569.6	5,644.3
Secured by Property Mortgage	2,261.5	2,259.8	2,607.7	2,644.9	2,645.5	2,648.2	2,688.1
Secured by Vehicle Title	109.2	107.7	105.4	104.6	106.5	109.3	109.4
Secured by Deposits	133.7	127.0	128.9	133.3	133.1	131.6	128.7
With Salary Assignment	1,933.0	1,947.8	1,962.2	1,966.9	1,975.3	1,994.3	2,011.6
Credit Card Receivables	99.5	96.6	96.9	98.3	98.0	103.5	101.8
Other	573.8	610.8	592.6	592.2	566.0	582.7	604.7

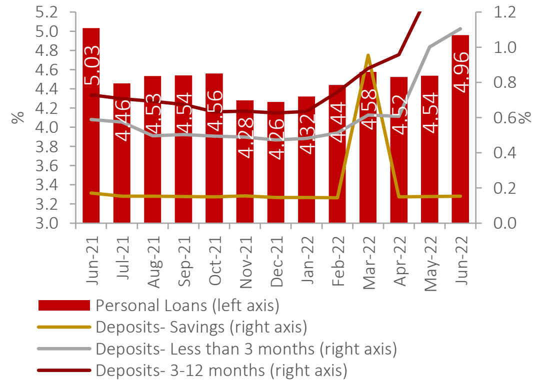
Source: CBB Monthly Statistical Bulletin.

Chart 1.31: Personal Loans Breakdown (June 2022)



Source: CBB Monthly Statistical Bulletin.

Chart 1.32: Retail Banks- Average Interest Rates on Personal Loans and Deposits (%)



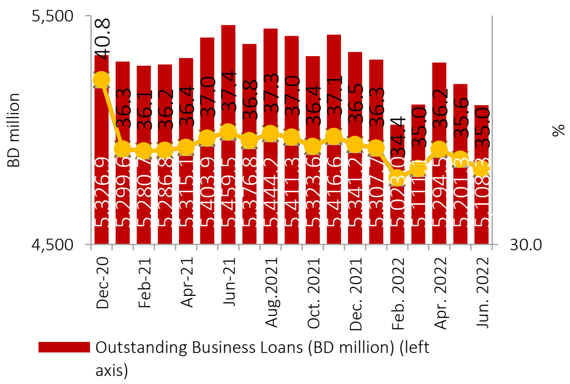
Source: CBB Monthly Statistical Bulletin

Interest rates on personal loans started off at 5.03% in June 2021 and decreased to 4.96% in June 2022 (Chart 2.27). 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.

2.6 The Bahraini Corporate/Business Sector

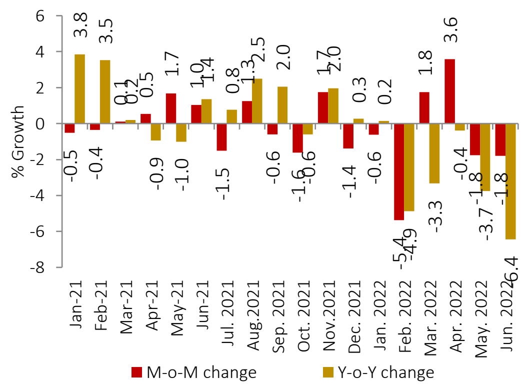
Business loans and advances contracted by 4.4% between December 2021 and June 2022 from BD million 5,341.2 in December 2021 to BD million 5,108.3 in June 2022 (Chart 2.28). As of June 2022, YoY growth for business loans contracted 6.4%. Outstanding business loans as a percentage of GDP decreased to 35.0% in June 2022.

Chart 1.33: Business Loans and Advances (Volume and % of GDP)



Source: CBB Monthly Statistical Bulletin.

Chart 1.34: Growth Rates of Total Business Loans and Advances (%)



Source: CBB Monthly Statistical Bulletin.

The monthly growth rate in total personal loans and advances fluctuated between June 2021 and June 2022. Initially at 1.0% in June 2021, it increased to reach its highest level for the year of 1.7% in November 2021 before falling to -6.4% in June 2022. The highest YoY growth was January 2022 (0.2%).

For the past six months, the main contributor to the business loans was the loans to the construction and real estate sector. The biggest contributors to business loans in June 2022 were the construction and real estate sector (33.1%) followed by manufacturing (24.3%), and then trade (17.6%) (Chart 2.30).

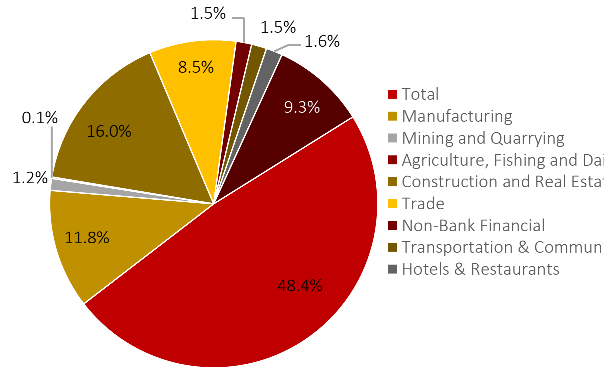
Average interest rates on business loans fluctuated throughout the period from June 2021 to June 2022. It was at its peak in June 2022 at 5.62% (Chart 2.31).

Table 1.5: Business Loans by Sector

BD million	Dec.2021	Jan. 2022	Feb. 2022	Mar. 2022	Apr. 2022	May 2022	Jun. 2022
Total	**5,341.2**	**5,307.7**	**5,023.0**	**5,111.1**	**5,294.5**	**5,201.3**	**5,108.3**
Manufacturing	1,292.3	1,287.4	1,262.0	1,272.9	1,355.5	1,293.8	1,239.0
Mining and Quarrying	74.7	77.1	77.3	78.0	122.0	122.4	123.5
Agriculture, Fishing and Dairy	13.2	13.5	13.2	14.0	14.4	14.5	15.0
Construction and Real Estate	2,009.6	2,020.4	1,720.4	1,744.7	1,735.8	1,697.7	1,689.4
Trade	903.9	890.6	886.1	914.4	942.5	907.9	900.4
Non-Bank Financial	169.5	164.9	170.3	171.8	166.7	170.4	162.9
Transportation & Communication	147.5	149.1	156.9	157.9	173.6	172.8	156.8
Hotels & Restaurants	196.1	173.7	173.6	172.5	172.7	171.4	171.0
Other Sectors	878.0	853.8	893.7	915.3	957.6	994.6	978.1

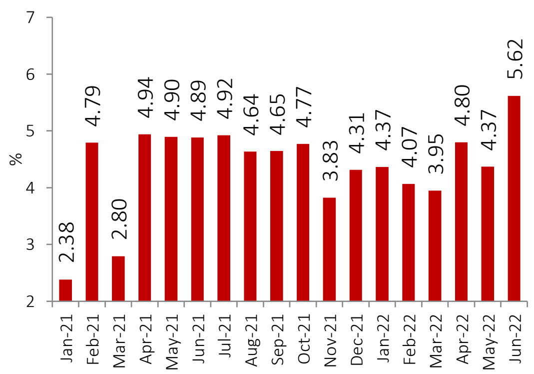
Source: CBB Monthly Statistical Bulletin.

Chart 1.35: Business Loans by Sector (June 2022)



Source: CBB Monthly Statistical Bulletin.

Chart 1.36: Retail Banks' Average Interest Rates on Business Loans



Source: CBB Monthly Statistical Bulletin.

PART II:

DEVELOPMENTS IN THE BANKING SECTOR

3 PERFORMANCE OF THE BANKING SECTOR

HIGHLIGHTS

CAR	19.1%	▲ 0.4% YoY
Tier 1 CAR	17.7%	▲ 0.2% YoY
Assets-to-Capital	8.7	▲ 0.4 YoY
NPL	3.3%	▼ 0.5% YoY
Specific Provisions	69.9%	▲ 0.8% YoY
ROA	0.6%	0.0% YoY
ROE	4.6%	▲ 0.7% YoY
Liquidity	25.7%	▼ 0.7% YoY
Loan/Deposit	65.7%	▼ 4.5% YoY

- Increase in capital positions.
- Non-performing loans continue to decrease.
- Loan portfolios remain concentrated in some sectors with no significant change from previous quarter.
- Stability in earnings for banks.
- Liquidity position remains resilient.

3.1 Overview

This chapter offers an assessment of the banking sector in Bahrain.[2] Macro-prudential analysis of the entire banking sector is performed based on a set of selected Financial Soundness Indicators (FSIs). The banking sector in Bahrain is divided into four segments: conventional retail (CR), conventional wholesale (CW), Islamic Retail (IR), and Islamic wholesale (IW). The performances of conventional and Islamic banking segments are analyzed separately in in Chapters 4 and 5.[3] Annex 1 presents selected FSIs for the different banking segments. Annex 2 presents selected graphs showing the development of selected FSIs over time.

Amidst the implications of COVID-19 on the banking sector and given that businesses have increasingly become vulnerable to financial losses, it has become important for CBB to understand and assess the financial impact the pandemic on banks. Having considered the implications of the instalment deferrals, CBB directed banks to apply a number of requirements keeping in view principles of consistent treatment across the industry, level playing field, prudence, and consumer and investor protection. As a result, capital and liquid positions remained strong during the peak of COVID-19 related volatility and Bahraini banks' profitability outlook is set to improve.

[2] Chapters 3, 4, and 5 cover the period between Q2 2021 and Q2 2022, unless otherwise indicated.

[3] Chapters 3, 4, and 5 do not contain any sections on stress testing. Stress testing exercises are performed separately in an internal report on selected Bahraini banks including Domestically Systemically-Important Banks (DSIB's).

3.2 Overall Banking Sector Performance

3.2.1 Capital Adequacy

Strong capital position with an increasing trend

The capital adequacy ratio[4] (CAR) for the banking sector stood at 19.1% in June 2022 increasing by 0.4% compared to June 2021. The core capital ratio (ratio of Tier 1 capital to risk-weighted assets) showed an increase from 17.5% in June 2021 to 17.7% in June 2022. Whereas the leverage ratio (ratio of assets over capital) increased to 8.7% during the same period.

Table 3.1: Capital Provision Ratios

Indicator*	Q2 2021	Q4 2021	Q2 2022	YoY Change
CAR (%)	18.7	18.7	19.1	0.4
Tier 1 CAR (%)	17.5	17.2	17.7	0.2
Assets/Capital (Times)	8.3	8.7	8.7	0.4

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

3.2.2 Asset Quality

Continued improvement in asset quality with decreasing NPL and increasing provisions

The non-performing loans (NPLs) ratio continued its decrease reaching 3.3% in June 2022 from 3.8% in June 2021. The CBB monitored the impact of the pandemic on NPL ratios as pressures on asset quality continued due to the global pandemic and after a contraction in economic activity in 2021. CBB's loan deferments managed to prevent defaults by individuals and business that suffered temporary cash-flow concerns preventing any deterioration in asset quality.

With the expected economic recovery to continue, banks need to remain prudent in monitoring any deteriorations in lending portfolios once the loan deferral program ends due to concerns of a lagged effect on NPLs.

The specific provisions as a proportion of NPLs continued to grow increasing to 69.9% in June 2022 from 69.0% in June 2021. Licensees were required to make an assessment on credit exposures and requested to be more prudent in determining any additional provision required considering the economic and financial impact of COVID-19 on customers.

Table 3.2: NPL Ratios (Q2 2022)

Indicator	Q2 2021	Q4 2021	Q2 2022	YoY Change
NPLs (% Total Loans)	3.8	3.2	3.3	-0.5
Specific provisions (% of NPLs) *	69.0	70.1	69.9	0.8

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

Data on NPLs by time segment (up to 1 year, 1 year to 3 years, and over 3 years) show that the majority of NPLs in the banking sector are for a period of over 3 years (51.2% of total NPLs). NPLs for over 3 years represented 1.7% of total gross loans. Specific provisioning for NPLs decrease as they are non-performing for longer periods of time. As seen in Table 3.3, NPLs for a period for more than 3 years are provisioned by 75.3%.

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

Table 3.3: NPL Ratios and Specific Provisions by Time Period (Q2 2022)

Indicator	Up to 1 year	1 up to 3 years	Over 3 years	Total
NPLs (% Total Loans)	0.8	0.8	1.7	3.3
Specific Provisions (% of NPLs)	53.7	74.7	75.6	69.9

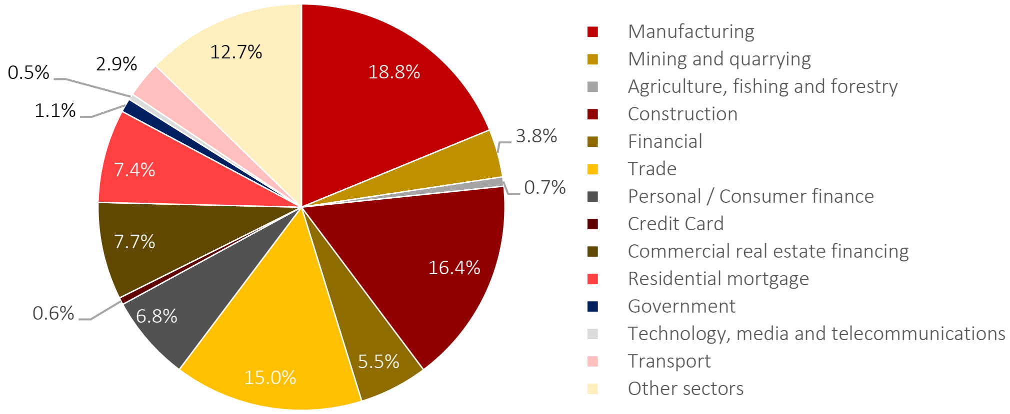
Source: CBB.

Chart 3.1: NPLs by Time Period (%)

Source: CBB.

Data on the concentration of NPLs by sector shows that the majority of NPLs come from manufacturing (18.8%), construction (16.4%), and trade (15.0%) as indicated in chart 3.2. [5]

Chart 3.2: NPLs Concentration by Sector (Q2 2022)



Source: CBB.

Data on the sectoral breakdown of NPLs ratios (NPLs per sector as a percentage of gross loans in each sector) shows increase in impairment in some sectors, while some experience a decrease and others remaining unchanged (Table 3.4). The highest increase was in mining and quarrying by 3.0%. The highest decrease was in the Technology, media and telecommunications sector which was 1.6%.

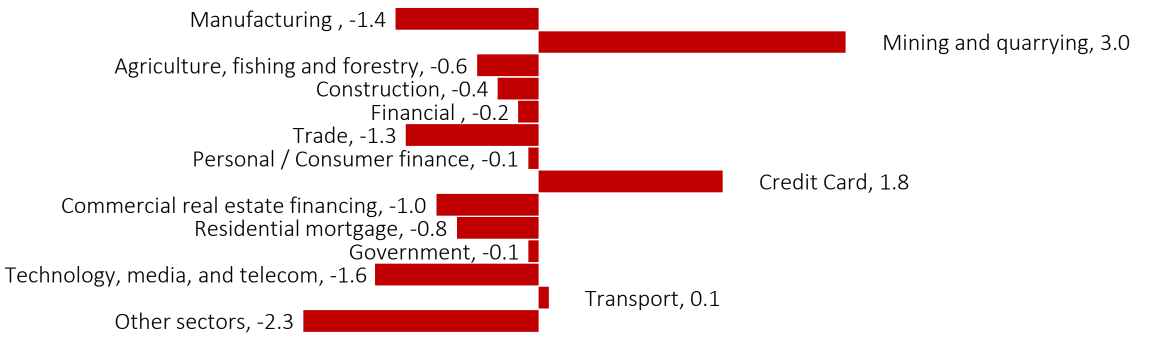
Table 3.4: NPL Ratios by Sector (%)

Sector	Q2 2021	Q4 2021	Q2 2022	YoY Change
Manufacturing	6.3	5.6	4.9	-1.4
Mining and quarrying	8.7	12.4	11.7	3.0
Agriculture, fishing and forestry	2.2	2.0	1.6	-0.6
Construction	6.0	5.3	5.6	-0.4
Financial	1.5	1.3	1.3	-0.2
Trade	9.1	7.7	7.8	-1.3
Personal / Consumer finance	2.5	2.2	2.4	-0.1
Credit Card	3.3	2.9	5.1	1.8
Commercial real estate financing	3.8	3.1	2.8	-1.0
Residential mortgage	5.1	4.4	4.3	-0.8
Government	0.7	0.6	0.6	-0.1
Technology, media and telecommunications	2.5	1.5	0.9	-1.6
Transport	3.1	3.1	3.2	0.1
Other sectors	5.0	4.2	2.7	-2.3

Source: CBB.

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

Chart 3.3: NPL by Sector- YoY Change (%)



Source: CBB.

Loan portfolios faces slight fluctuations and remain concentrated in some sectors

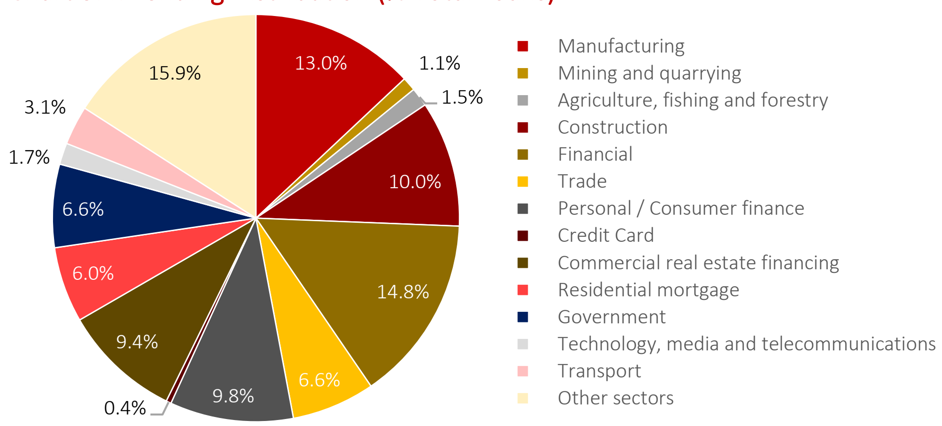
The loan portfolio of the banking system remains concentrated with no sector exceeding 20% of total loans. Financial and other sectors represented the highest exposure with 14.8% of total loans in June 2022. Manufacturing and Construction followed with 13.1% and 10.0% respectively. Personal/consumer finance stood at 9.8% of total loans. The sector with the largest decline was manufacturing dropping 2.1%.

Table 3.5: Lending Distribution (% Total Loans)

Sector	Q2 2021*	Q4 2021*	Q2 2022*	YoY Change
Manufacturing	15.1	15.0	13.1	-2.1
Mining and quarrying	0.9	0.8	1.1	0.2
Agriculture, fishing and forestry	1.3	1.2	1.5	0.2
Construction	11.0	10.4	10.0	-1.0
Financial	14.9	15.1	14.8	-0.1
Trade	7.4	6.8	6.6	-0.8
Personal / Consumer finance	9.4	10.1	9.8	0.4
Credit Card	0.4	0.4	0.4	0.0
Commercial real estate financing	8.7	9.0	9.4	0.7
Residential mortgage	6.2	5.8	6.0	-0.2
Government	5.3	5.6	6.6	1.3
Technology, media and telecommunications	1.1	1.3	1.7	0.6
Transport	3.5	3.2	3.1	-0.4
Other sectors	14.9	15.1	15.9	1.0
Top Two Sectors (%)	30.0	30.1	30.8	0.8
Real Estate/ Construction Exposure (%) **	25.9	25.2	25.4	-0.5

** 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 3.4: Lending Distribution (% Total Loans)



Source: CBB.

The top two recipient sectors, financial and other sectors, jointly represented 30.8% of loans in June 2022, increasing from 30.0% in June 2021. Exposure to real estate/construction was 25.4% of total lending in June 2022, a slight decrease from 25.9% registered in June 2021.

SME lending remains low

Credit extension to Small and Medium Enterprises (SMEs) remained unchanged between June 2021 and June 2022. SME loans (as a % of total loans) at 2.1% in June 2022. SME NPLs decreased from 9.0% in June 2021 to 8.7% in June 2022. Provisioning levels recorded a decrease from 40.5% in June 2021 to 39.6% in June 2022.

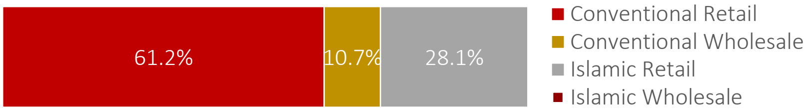
Table 3.6: SME Lending *

Indicator	Q2 2021	Q4 2021	Q2 2022	YoY Change
SME Loans (% of total Loans)	2.1	2.2	2.1	0.0
SME NPLs (% of total SME Loans)	9.0	9.0	8.7	-0.3
SME Provisioning (% of total SME NPLs)	40.5	40.2	39.9	-0.6

*For Bahrain Operations Only

Source: CBB.

Chart 3.5: SME Lending by Banking Segment (Q2 2022)



Source: CBB.

3.2.3 Profitability

Profitability remains positive

The overall banking sector's profitability indicators have been stable between June 2021 to June 2022 and remain robust. Return-on-assets (ROA) remained unchanged at 0.6% in June 2021 and in June 2022. As of End-June 2022, return-on-equity (ROE) increased to 4.6% from 3.9% in June 2021.

Table 3.7: Profitability

Indicator	Q2 2021	Q2 2022	YoY Change
ROA (%) *	0.6	0.6	0.0
ROE (%) **	3.9	4.6	0.7
Net Interest Income (% Total Income) ***	72.5	68.6	-3.9
Operating Expenses (% Total Income)	51.2	46.1	-5.1

** ROA = ratio of net income to assets.*
*** ROE = ratio of net profit to tier 1 capital (for Locally Incorporated Banks only).*
**** For Conventional Banks.*
Source: CBB.

Net interest income (as a % of total income) stood at 68.6% in June 2021. In addition, operating expenses as a proportion of total income was 46.1% in June 2022, a decrease from the 51.2% registered in June 2021.

3.2.4 Liquidity

Liquidity positions remain resilient

Between June 2021 and June 2022, the overall loan-deposit ratio decreased from 70.2% to 65.7%. Liquid assets as a proportion of total assets decreased from 26.4% to 25.7%, over the same period.

Table 3.8: Liquidity

	Q2 2021	Q4 2021	Q2 2022	YoY Change
Liquid Asset Ratio (%)	26.4	26.2	25.7	-0.7
Loan-Deposit Ratio (%)	70.2	69.8	65.7	-4.5

Source: CBB.

3.3 Developments in Regulation and Initiatives

The following section sheds light on the regulatory and policy initiatives that took place during 2022 for the banking and financial sector that are related to financial stability:

Table 3.9: Banking Sector Regulatory and Policy Developments

Item	Description
Amendments to Requirements on Promotion of Financial Products and Services	The CBB in January 2022, limited the requirement for independent verification and monitoring/witnessing by the bank's external auditors to draws of the raffle/lottery involving prizes of BD 10,000 or above in aggregate.
Amendments to Take-overs, Mergers and Acquisitions (TMA) Module	As part of the Central Bank of Bahrain's objectives to further enhance its regulatory framework and pursuant to the latest amendments to the Bahrain Commercial Companies Law, Decree Law No. 21 of 2001, on compulsory acquisition and sell-out rights, the CBB introduced certain amendments to the TMA Module in January 2022.
Amendments to the CBB Rulebook Volume 5 (Type 3: Financing Companies)	The CBB in February 2022, issued amendments to financing company regulations to cater to financing companies with limited scope of short-term instalment credit activities such as Buy Now Pay Later (BNPL). The amendments eased the authorization, capital adequacy and controller requirements, among others.
Requirements to Enhance Representation of Payment Transactions	The CBB in February 2022, required financing companies and payment service providers providing acquiring services to include Merchant Category Codes (MCC) consistent with ISO 18245, in the customer transaction data to be shared with the issuers.
Amendments to Module GR of the CBB Rulebook Volumes 1 and 2	As part of the CBB's objective to ensure better transparency with regards to payments transactions and customer account activities which is necessary for proper implementation of open banking, the CBB issued amendments to the General Requirements Module (Module GR) within CBB Rulebook Volumes 1 and 2 mandating access and sharing of the Merchant Category Code (MCC), consistent with ISO 18245, relevant to customer account activity/transactions in February 2022.
Climate-Related Risks	Further to CBB's circular dated 8th November 2021, the CBB issued to all licensees a guidance note on climate-related risks in March 2022 with the objective of ensuring that the licensees regulated and supervised by the CBB are kept abreast of the developments and practices in the area of climate-related risks management as it will shape business models in years to come.
Issuance of new Collective Investment Undertakings Module	Further to the consultation issued on 17th January 2022, the CBB issued in March 2022 a new CIU Module that replaced all existing CIU regulations in Volume 7. The new regulations intended to rationalize and simplify the CBB's CIU regime.
Amendments to Requirements on Reporting Cyber Security Incidents	As part of CBB's initiative to enhance its regulatory framework, the CBB updated the cyber security incident reporting requirements in March 2022, by introducing a one-hour deadline to report a cyber incident by phone and a two-hour deadline to report essential details by email.
Caps on Fees and Charges for Standard Services applicable to Microfinance Institutions	Further to the CBB's consultation letter dated 11th January 2022, the CBB in March 2022, introduced new caps on fees and charges for certain standard services provided by microfinance institutions.

Amendments to the Authorization Module (Module AU) – Volume 5 Type 7: Ancillary Service Providers	The CBB in March 2022, increased the limit of the amount that can be held in any multi-purpose, electronic or otherwise, pre-paid card, from BD 1,000 to BD 2,500.
Issuance of new Crowdfunding Platform Operators' Regulations	Further to the CBB's consultation dated 23rd February 2022, the CBB issued a new consolidated Crowdfunding Platform Operators Module (Module CFP) in April 2022 replacing existing regulations for both financing-based and equity-based crowdfunding. The new rules rationalized and simplified the requirements for crowdfunding platforms.
Discrepancies in BCRB Reporting	The CBB required all retail banks, financing companies and micro-finance institutions in April 2022, to conduct a data cleansing exercise of its clients' data to ensure accurate reporting to BCRB including a quarterly comparison to verify core system data with BCRB.
Bahrain Open Banking Framework – Developer Portal	The CBB is May 2022, introduced a requirement for retail banks to extend access to their developer portals (testing facilities) to open banking service providers operating in the regulatory sandbox and AISPs/PISPs granted in-principle confirmation to proceed with the CBB's licensing process.
Amendments to the Financial Crime Module (Module FC)	The CBB in June 2022, allowed banks in Bahrain to open accounts for Bahraini nationals residing outside Bahrain through a digital onboarding process using the National E-KYC system.
Directive: Employment of In-house Bahraini Actuaries	The CBB in June 2022, required all insurance firms to establish an internal actuarial unit within their organization structure for which all insurance firms must appoint an in-house Bahraini Qualified Actuary (by 30th June 2029) and an in-house Bahraini Actuarial Analyst (by 30th June 2023).

4 PERFORMANCE OF CONVENTIONAL BANKS

HIGHLIGHTS

	Retail		Wholesale	
CAR	20.4%	0.0% YoY	17.7%	▲ 0.1% YoY
Tier 1 CAR	19.0%	▲ 0.1% YoY	16.2%	▼ 0.5% YoY
Assets-to-Capital	7.3	▲ 0.3 YoY	9.5	▲ 1.2 YoY
NPL	3.8%	▼ 0.5% YoY	2.5%	▼ 1.1% YoY
Specific Provisions	73.2%	▲ 3.6% YoY	69.6%	▼ 4.3% YoY
ROA	0.8%	▲ 0.1% YoY	0.6%	0.0% YoY
ROE	6.6%	▲ 0.8% YoY	2.3%	▲ 0.6% YoY
Liquidity	34.1%	0.0% YoY	21.9%	▼ 2.6% YoY
Loan/Deposit	68.1%	▲ 0.9% YoY	61.8%	▼ 7.6% YoY

- Capital position of conventional banks remain at a similar level.
- NPLs decreased for conventional banks.
- Loan portfolios in conventional retail and wholesale banks remain concentrated despite the decrease in some sectors.
- Stability in earnings for conventional retail banks and conventional wholesale banks.
- Liquidity declined for conventional wholesale banks.

4.1 Overview

Chapter 4 offers macro-prudential analysis of the conventional banking sector based on a set of selected FSIs. The Chapter analyses the following conventional banking segments (retail and wholesale): capital adequacy (section 4.2), asset quality (section 4.3), profitability (section 4.4), and liquidity (section 4.5). Unless specified otherwise, the analysis in this chapter is based on consolidated financial data (Bahraini and non-Bahraini operations).

4.2 Capital Adequacy

Capital adequacy for conventional banks remains at a comfortable level

The CAR for conventional retail remained at 20.4% from June 2021 to June 2022. The core capital ratio (ratio of Tier 1 capital to risk-weighted assets) showed a slight increase from 18.0% in June 2021 to 19.0% in June 2022. The leverage ratio (ratio of assets over capital) increased to 7.3% during the same period. The NPLs net provisions to capital decreased to 4.3% in June 2022 from 5.3% in June 2021.

As for wholesale banks, CAR slightly increased to 17.7% in June 2022 from the level of 17.6% it registered in June 2021. Tier 1 capital decreased to 16.2% in June 2022 from the level of 16.7 it recorded in June 2021. Furthermore, the leverage ratio (ratio of assets over capital) increased to 9.5% in June 2022. Finally, the ratio of NPLs net of provisions to capital decreased to 3.4% over the same period.

Table 4.1: Conventional Banks' Capital Provisions Ratios

Indicator *	Retail			Wholesale		
	Q2 2021	Q2 2022	Change	Q2 2021	Q2 2022	Change
CAR (%)	20.4	20.4	0.0	17.6	17.7	0.1
Tier 1 CAR (%)	18.9	19.0	0.1	16.7	16.2	-0.5
Assets/Capital (Times)	7.0	7.3	0.3	8.3	9.5	1.2
NPLs net of Provisions to Capital (%)	5.3	4.3	-1.0	4.4	3.4	-1.0

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

4.3 Asset Quality

4.3.1 Non-Performing Loans

Drop in NPLs for conventional banks with high provisioning position

The NPL ratio decreased to 3.8% in June 2022 from 4.3% in June 2021 for conventional retail banks. Specific provisions as a proportion of NPLs increased to 73.2% in June 2022. As for conventional wholesale banks, the NPL ratio decreased from 3.6% in June 2021 to 2.5% in June 2022. Specific provisions witnessed a decrease of 4.3% from 73.9% in June 2021 to 69.6% in June 2022.

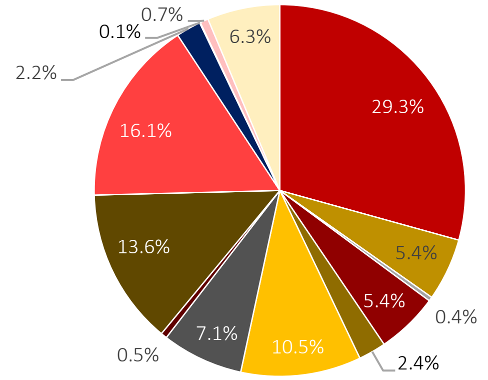
Table 4.2: Conventional Banks' NPL Ratios

Indicator *	Retail			Wholesale		
	Q2 2021	Q2 2022	Change	Q2 2021	Q2 2022	Change
NPLs (% Total Loans)	4.3	3.8	-0.5	3.6	2.5	-1.1
NPLs Local Banks (%)	4.3	3.7	-0.6	5.4	3.4	-2.0
NPLs Overseas Banks (%)	4.5	4.0	-0.5	2.1	1.9	-0.2
Specific Provisions (% of NPLs) *	69.6	73.2	3.6	73.9	69.6	-4.3

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

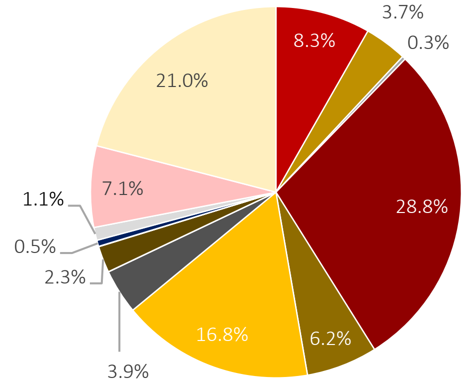
Data on the concentration of NPLs by sector for conventional retail banks shows that the majority of NPLs come from the manufacturing sector (29.3%), residential mortgage (16.1%), commercial real estate sector (13.6%) and trade (10.5%). On the other hand, the data on the concentration of NPLs by sector for wholesale banks indicates that that the majority of NPLs are concentrated and come from the construction sector (28.8%), trade (16.8%), and others (21.0%).

Chart 4.1: CR Banks' NPLs Concentration by Sector (June 2022)



Source: CBB.

Chart 4.2: CW Banks' NPLs Concentration by Sector (June 2022)



Source: CBB.

Available data on the sectoral breakdown of NPLs shows some sectors experiencing an increase in impairment, while most experience a decrease (Table 4.3). For conventional retail banks, the highest increase was in mining and quarrying by 25.4% while the largest decrease was in residential mortgage by 1.8%.

As for wholesale banks, sectoral breakdown of impaired loans demonstrates that impairment in trade was the highest between all sectors at 8.0%, followed by mining and quarrying with an impairment of 4.9%. The biggest decrease in impairment was found in the credit card sector with a decrease of 6.6%.

Table 4.3: Conventional Banks' NPL Ratios by Sector (%)

Sector	Retail			Wholesale		
	Q2 2021	Q2 2022	Change	Q2 2021	Q2 2022	Change
Manufacturing	9.0	8.2	-0.8	2.7	1.5	-1.2
Mining and quarrying	29.0	54.4	25.4	1.7	4.9	3.2
Agriculture, fishing and forestry	2.1	3.2	1.1	1.2	0.3	-0.9
Construction	6.6	5.5	-1.1	5.2	4.5	-0.7
Financial	1.3	1.1	-0.2	1.2	0.8	-0.4
Trade	4.5	4.5	0.0	11.6	8.0	-3.6
Personal / Consumer finance	1.8	1.8	0.0	4.4	4.0	-0.4
Credit Card	3.6	2.7	-0.9	8.4	1.8	-6.6
Commercial real estate financing	2.9	2.7	-0.2	4.0	3.1	-0.9
Residential mortgage	7.6	5.8	-1.8	1.3	0.8	-0.5
Government	3.1	2.2	-0.9	0.4	0.2	-0.2
Technology, media and telecommunications	0.8	0.1	-0.7	4.2	1.9	-2.3
Transport	1.7	1.4	-0.3	3.2	3.9	0.7
Other sectors	3.6	2.0	-1.6	3.9	2.6	-1.3

Source: CBB.

4.3.2 Loan Concentrations

Loan portfolios remain concentrated

The loan portfolio of retail banks remains concentrated with minimal changes in the composition of the loans. The top recipient of retail loans remains to be the commercial real estate financing sector accounting for 19.0% of total loans in June 2022 followed by personal/consumer finance representing 14.7%. Exposure to real estate/construction remained at 33.1% of total lending in June 2022. As for wholesale banks, lending remains concentrated in the financial sector and construction sector accounting for 20.3% and 16.3% respectively. Exposure to real estate/construction decreased to 18.3% of total lending in June 2022.

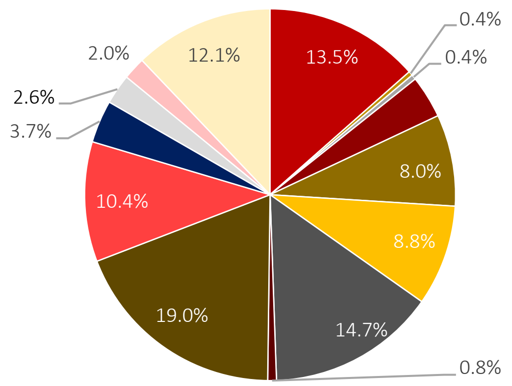
Table 4.4: Conventional Banks' Lending Distribution by Sector (% Total Loans)

Sector	Retail			Wholesale		
	Q2 2021	Q2 2022	Change	Q2 2021	Q2 2022	Change
Manufacturing	13.7	13.5	-0.2	14.8	13.9	-0.9
Mining and quarrying	0.4	0.4	0.0	1.4	1.9	0.5
Agriculture, fishing and forestry	0.4	0.4	0.0	2.5	2.7	0.2
Construction	3.8	3.7	-0.1	19.4	16.3	-3.1
Financial	7.6	8.0	0.4	19.6	20.3	0.7
Trade	9.8	8.8	-1.0	5.8	5.3	-0.5
Personal / Consumer finance	15.1	14.7	-0.4	1.8	2.5	0.7
Credit Card	0.7	0.8	0.1	0.0	0.0	0.0
Commercial real estate financing	19.1	19.0	-0.1	2.1	1.9	-0.2
Residential mortgage	10.3	10.4	0.1	0.1	0.1	0.0
Government	2.8	3.7	0.9	5.3	8.2	2.9
Technology, media and telecommunications	1.9	2.6	0.7	1.0	1.5	0.5
Transport	2.3	2.0	-0.3	5.8	4.6	-1.2
Other sectors	12.2	12.1	-0.1	20.3	20.9	0.6
Top Two Sectors (%)	34.2	33.7	-0.5	39.9	41.2	1.3
Real Estate/ Construction Exposure (%) **	33.1	33.1	0.0	21.6	18.3	-3.3

** 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.

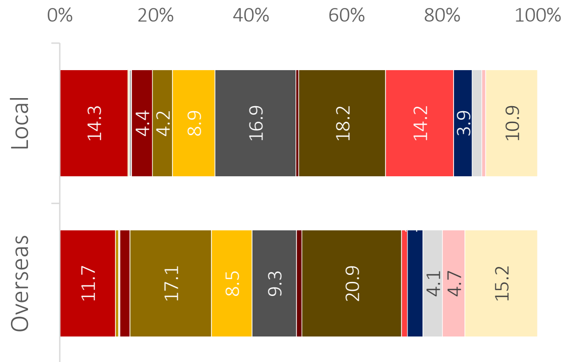
Available data on local and overseas banks, shows that loan portfolio of locally incorporated retail banks remains concentrated with the top recipient of loans being the commercial real estate financing sector (18.2%). Real estate/construction exposure decreased to 36.8% of total lending in June 2022. Similarly, the numbers as of end-June 2022 continue to show high concentration for overseas retail banks. The top recipient of loans was the commercial real estate financing sector (20.9%). And exposure to real estate/ construction was 24.2% of total lending in June 2022.

Chart 4.3: CR Banks' Lending Distribution by Sector (% Total Loans)



Source: CBB.

Chart 4.4: Local and Overseas CR Banks' Lending Distribution by Sector (% Total Loans)

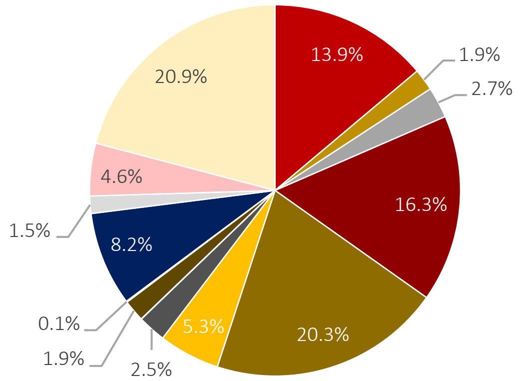


Source: CBB.

Manufacturing
Mining and quarrying
Agriculture, fishing and forestry
Construction
Financial
Trade
Personal / Consumer finance
Credit Card
Commercial real estate financing
Residential mortgage
Government
Technology, media and telecommunications
Transport
Other sectors

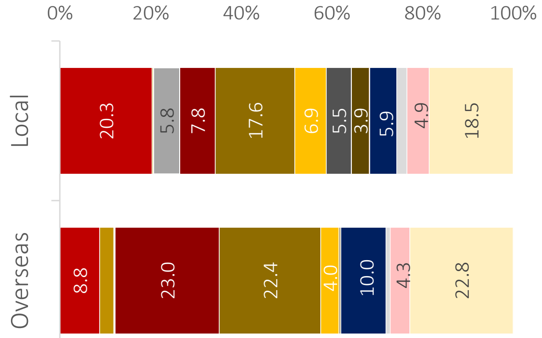
As for locally-incorporated wholesale banks, the top recipient of loans is the manufacturing sector (20.3%) and the real estate/ construction exposure was 11.8% for the same period. For overseas wholesale banks, the top recipient of loans in June 2022 was the construction sector (23.0%) and real estate/construction exposure decreased from 29.5% in June 2021 to 23.3% in June 2022.

Chart 4.5: CW Banks' Lending Distribution by Sector (% Total Loans)



Source: CBB.

Chart 4.6: Local and Overseas CW Banks' Lending Distribution by Sector (% Total Loans)



Source: CBB.

4.4 Profitability

Banks' profitability remains at the same level

Profitability for conventional retail banks was positive, and, as at end-June 2022, ROA slightly increased to 0.8%. ROA for locally incorporated banks remained at 0.8% in June 2022. For overseas banks, ROA remained at 0.6% in June 2022. ROE for locally incorporated banks increased to 6.6% from 5.8% during the same period. Net interest income (as a % of total income) decreased from 77.7% to 74.5% during the same period as well. Operating expenses as a proportion of total income decreased from 44.8% in June 2021 to 42.1% in June 2022.

Table 4.5: Conventional Banks' Profitability

Indicator	Retail			Wholesale		
	Q2 2021	Q2 2022	Change	Q2 2021	Q2 2022	Change
ROA (%) *	0.7	0.8	0.1	0.6	0.6	0.0
ROA Locally Incorporated Banks (%)	0.8	0.8	0.0	0.2	0.2	0.0
ROA Overseas Banks (%)	0.6	0.6	0.0	0.9	1.0	0.1
ROE (%) **	5.8	6.6	0.8	1.7	2.3	0.6
Net Interest Income (% Total Income)	77.7	74.5	-3.2	67.6	63.5	-4.1
Operating Expenses (% Total Income)	44.8	42.1	-2.7	44.3	44.1	-0.2

** ROA = ratio of net income to assets.*
*** ROE = ratio of net income to tier 1 capital (for Locally Incorporated Banks only).*
Source: CBB.

As for conventional wholesale banking sector, ROA remained at 0.6% in June 2022. The ROA for local wholesale banks remained at 0.2%, while overseas wholesale banks slightly increased from 0.9% to 1.0%. ROE for local wholesale banks increased from 1.7% to 2.3%. Net interest income as a proportion of total income decreased from 67.6% in June 2021 to 63.5% in June 2022. Operating expenses as a proportion of total income showed a slight decrease from 44.3% in June 2021 to 44.1% in June 2022.

4.5 Liquidity

Liquidity position is strong but declines for conventional wholesale banks

Between June 2021 and June 2022, non-bank deposits increased by 6.2% for conventional retail banks. The overall loan-deposit ratio for the segment increased to 68.1% in June 2022 from 67.2% in June 2021. Liquid assets as a proportion of total assets remained at 34.1% in June 2022. Liquid assets as a proportion of the short-term liabilities also remained at the same level of 42.7% over this period.

As at end-June 2022, the overall loan-deposit ratio for conventional wholesale banks stood at 61.8%, a decrease from the 69.4% recorded in June 2021. Liquid assets for wholesale banks as a proportion of total assets decreased to 21.9% in June 2022 from 24.5% in June 2021. The liquid assets as a proportion of short-term liabilities increased by 3.2% to be 30.0 % in June 2022. Non-bank deposits as a proportion of total deposits stood at 52.3%, an increase from the 49.3% level achieved in June 2021, while bank deposits decreased from 50.7% in June 2021 to 47.7% in June 2022.

Table 4.6: Conventional Bank's Liquidity

Indicator	Retail			Wholesale		
	Q2 2021	Q2 2022	Change	Q2 2021	Q2 2022	Change
Liquid Asset Ratio (%)	34.1	34.1	0.0	24.5	21.9	-2.6
Loan-Deposit Ratio (%)	67.2	68.1	0.9	69.4	61.8	-7.6
Non-Bank Deposits (% of Total Deposits)	70.4	76.6	6.2	49.3	52.3	3.0

Source: CBB.

5 PERFORMANCE OF ISLAMIC BANKS

HIGHLIGHTS

	Retail		Wholesale	
CAR	21.0%	▼ 0.6% YoY	15.3%	▼ 0.8% YoY
Tier 1 CAR	19.9%	▲ 0.3% YoY	14.7%	▼ 0.3% YoY
Assets-to-Capital	11.4	▲ 1.0 YoY	8.6	▼ 1.6 YoY
NPL	4.4%	▼ 1.1% YoY	6.3%	▲ 4.6% YoY
Specific Provisions	59.0%	▲ 7.2% YoY	86.7%	▲ 7.3% YoY
ROA	0.4%	▲ 0.1% YoY	0.6%	▲ 0.2% YoY
ROE	5.4%	▲ 1.8% YoY	5.0%	▲ 0.7% YoY
Liquidity	18.9%	▼ 0.3% YoY	17.4%	▼ 1.6% YoY
Loan/Deposit	73.5%	▼ 2.7% YoY	35.2%	▼ 29.7%

- Capital positions decreased for both Islamic retail and Islamic wholesale banks.
- Non-performing facilities (NPFs) decreased for Islamic retail banks but increased for wholesale.
- Concentration of facilities for Islamic banks continues in specific sectors.
- Earnings for Islamic banks slightly increased.
- Liquidity positions decreased for retail and wholesale banks.

5.1 Overview

Chapter 5 offers macro-prudential analysis of the Islamic banking sector based on a set of selected FSIs. The Chapter analyses the following conventional banking segments (retail and wholesale): capital adequacy (section 5.2), asset quality (section 5.3), profitability (section 5.4), and liquidity (section 5.5). Unless specified otherwise, the analysis in this chapter is based on consolidated financial data (Bahraini and non-Bahraini operations).

5.2 Capital Adequacy

Capital positions increase for Islamic retail and declines for Islamic wholesale

The CAR of Islamic retail banks slightly decreased from 21.6% in June 2021 to 21.0% in June 2022. Tier 1 capital decreased from 19.6% to 19.9% during this period. As at end- June 2022, the CAR for Islamic wholesale banks decreased to 15.3% from 16.1% in June 2021. Tier 1 capital also decreased from 15.0% to 14.7% over the same period. The ratio of NPFs net of provisions to capital decreased to 1.5% in June 2022.

Table 5.1: Islamic Banks' Banks' Capital Provisions Ratios

Indicator *	Retail			Wholesale		
	Q2 2021	Q2 2022	Change	Q2 2021	Q2 2022	Change
CAR (%)	21.6	21.0	-0.6	16.1	15.3	-0.8
Tier 1 CAR (%)	19.6	19.9	0.3	15.0	14.7	-0.3
Assets/Capital (Times)	10.4	11.4	1.0	10.2	8.6	-1.6
NPLs net of Provisions to Capital (%)	16.0	12.0	-4.0	1.8	1.5	-0.3

Source: CBB.

5.3 Asset Quality

5.3.1 Non-Performing Facilities

Decrease in retail NPFs for Islamic retail and slight increase for Islamic wholesale

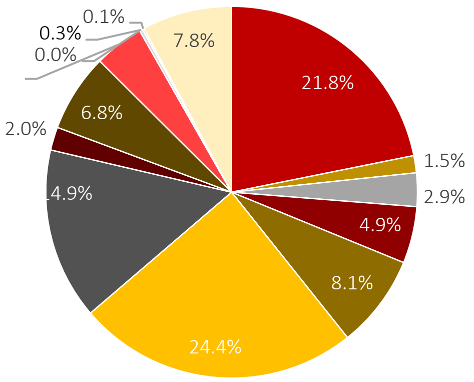
Non-performing facilities (NPF) ratio for Islamic retail banks decreased to 4.4% in June 2022. Specific provisoining increased to 59.0% in June 2022 from 51.8% in June 2021. As of end- June 2022, NPF ratio for Islamic wholesale banks increased to 6.3%. Provisioning for NPFs increased to 86.7% over the same period.

Table 5.2: Islamic Banks' NPF Ratios

Indicator *	Retail			Wholesale		
	Q2 2021	Q2 2022	Change	Q2 2021	Q2 2022	Change
NPFs (% Gross Facilities)	5.5	4.4	-1.1	1.7	6.3	4.6
Specific Provisions (% of NPFs)	51.8	59.0	7.2	79.4	86.7	7.3

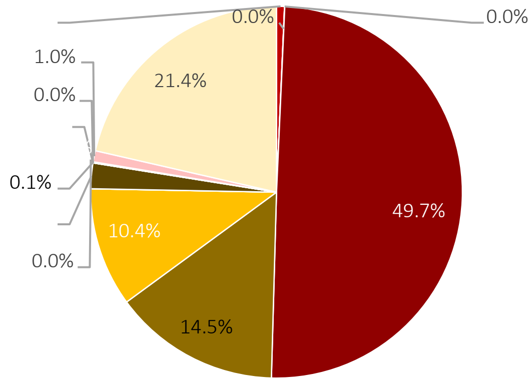
Source: CBB.

Chart 5.1: IR Banks' NPLs Concentration by Sector (June 2022)



Source: CBB.

Chart 5.2: IW Banks' NPLs Concentration by Sector (June 2022)



Source: CBB.

- Manufacturing
- Agriculture, fishing and forestry
- Financial
- Personal / Consumer finance
- Commercial real estate financing
- Government
- Transport
- Mining and quarrying
- Construction
- Trade
- Credit Card
- Residential mortgage
- Technology, media and telecommunications
- Other sectors

Looking at the data on the concentration of NPFs for Islamic retail banks by sector indicates that the majority of NPLs are concentrated and come from the trade sector (24.4%), manufacturing (21.8%), personal/consumer finance (14.9%) as indicated in chart 5.1. As for Islamic wholesale banks, the majority of NPFs are concentrated and come from construction (49.7%), financial (14.5%), and other sectors (21.4%) as indicated in chart 5.2.

A look at the non-performing facilities by sector for Islamic retail banks indicates that the trade sector had the highest impairment (19.3%) in June 2022 followed by agriculture, fishing and forestry and credit card with 17.1% and 14.3% respectively. The biggest declines in NPFs by sector was in the agriculture, fishing and forestry sector which went down by 19.3%. The biggest increase in NPFs was in credit card sector with an increase of 11.8% as indicated in table 5.3.

Table 5.3: Islamic Banks' NPF Ratios by Sector (%)

Sector	Retail			Wholesale		
	Q2 2021	Q2 2022	Change	Q2 2021	Q2 2022	Change
Manufacturing	13.0	10.8	-2.2	7.3	0.8	-6.5
Mining and quarrying	4.0	11.5	7.5	22.1	0.0	-22.1
Agriculture, fishing and forestry	36.4	17.1	-19.3	5.2	2.3	-2.9
Construction	4.3	6.9	2.6	10.6	24.1	13.5
Financial	4.5	3.1	-1.4	1.0	4.6	3.6
Trade	19.0	19.3	0.3	10.5	47.4	36.9
Personal / Consumer finance	4.1	2.7	-1.4	1.9	0.0	-1.9
Credit Card	2.5	14.3	11.8	2.6	0.0	-2.6
Commercial real estate financing	4.3	3.0	-1.3	21.8	15.2	-6.6
Residential mortgage	2.0	1.2	-0.8	2.0	0.0	-2.0
Government	0.0	0.0	0.0	0.0	0.0	0.0
Technology, media and telecommunications	3.7	11.3	7.6	36.2	100.0	63.8
Transport	5.5	1.2	-4.3	5.3	3.0	-2.3
Other sectors	6.0	4.1	-1.9	16.9	14.3	-2.6

Source: CBB.

On the other hand, the sector with the highest impairment for Islamic wholesale banks was the technology, media and telecommunications sector with 100.0% in June 2022. This was followed by the trade and construction sectors with 47.4% and 24.1% respectively. Available data on the sectoral breakdown of non-performing facilities shows that the biggest increase was in the mining and quarrying sector with an increase of 22.1%. The biggest drop was in the technology, media and telecommunications and trade sectors equally with a decrease of 63.8% and 36.9%. The mining and quarrying sector went down from 22.1% in June 2021 to 0.0% in June 2022. Whereas the technology, media, and telecommunications went up from the 36.2% recorded in June 2021 to 100.0 in June 2022.

5.3.2 Facilities Concentrations

Loan portfolios remain concentrated

There has been some diversification in the asset concentration among most of the sectors in Islamic retail banks. At the end of June 2022, the top recipient of financing was personal/consumer finance (24.2%), an increase from 18.4% recorded in June 2021. The top two recipients of financing (personal/consumer finance and residential mortgage) accounted for 39.8% of total facilities extended, compared to 34.9% for the top two sectors in June 2021. Real estate/construction exposure decreased to 28.8% in June 2022.

At End- June 2022, the financial sector was the top recipient of financing from Islamic wholesale banks, at 36.9%, increasing by 16.5% from June 2021. The manufacturing sector saw the largest decrease from 23.7% in June 2021 to 10.3% in June 2022. Real estate/ construction exposure increased from 17.5% in June 2021 to 25.9% in June 2022.

Table 5.4: Islamic Banks' Lending Distribution by Sector (% Total Facilities)

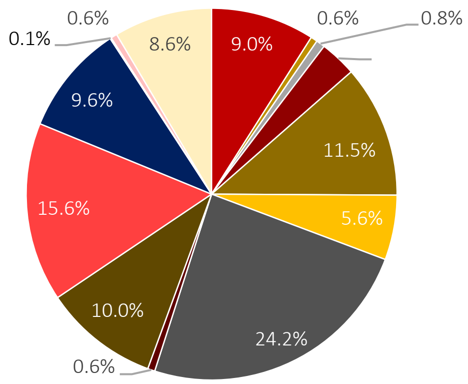
Sector	Retail			Wholesale		
	Q2 2021	Q2 2022	Change	Q2 2021	Q2 2022	Change
Manufacturing	9.8	9.0	-0.8	23.7	10.3	-13.4
Mining and quarrying	0.5	0.6	0.1	1.0	0.0	-1.0
Agriculture, fishing and forestry	0.2	0.8	0.6	0.7	0.1	-0.6
Construction	3.6	3.2	-0.4	9.5	24.2	14.7
Financial	11.6	11.5	-0.1	20.4	36.9	16.5
Trade	6.8	5.6	-1.2	7.1	2.6	-4.5
Personal / Consumer finance	18.4	24.2	5.8	11.2	0.0	-11.2
Credit Card	0.8	0.6	-0.2	0.3	0.0	-0.3
Commercial real estate financing	11.3	10.0	-1.3	2.0	1.7	-0.3
Residential mortgage	16.5	15.6	-0.9	6.1	0.0	-6.1
Government	10.1	9.6	-0.5	7.4	2.9	-4.5
Technology, media and telecommunications	0.5	0.1	-0.4	0.1	0.0	-0.1
Transport	0.5	0.6	0.1	1.4	3.7	2.3
Other sectors	9.4	8.6	-0.8	9.0	17.5	8.5
Top two recipient sectors	34.9	39.8	4.9	44.1	61.1	17.0
Real Estate/ Construction Exposure**	31.4	28.8	-2.6	17.5	25.9	8.4

Source: CBB.

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

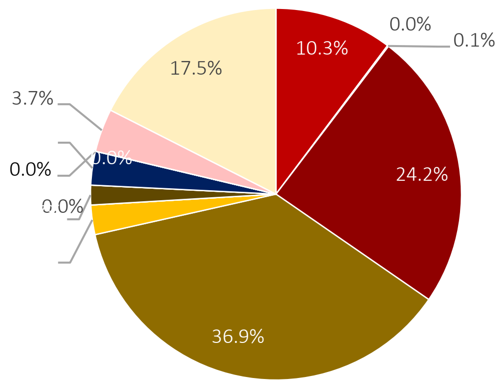
*** Real Estate/ Construction exposure is calculated as the share of the Construction, Commercial real estate financing and Residential Mortgages sectors of total lending.*

Chart 5.3: IR Banks' Lending Distribution by Sector (% of Total Facilities)



Source: CBB.

Chart 5.4: IW Banks' Lending Distribution by Sector (% of Total Facilities)



Source: CBB.

- Manufacturing
- Mining and quarrying
- Agriculture, fishing and forestry
- Construction
- Financial
- Trade
- Personal / Consumer finance
- Credit Card
- Commercial real estate financing
- Residential mortgage
- Government
- Technology, media and telecommunications
- Transport
- Other sectors

The concentration of lending distribution by Islamic instrument remained the same over the past. At the end of June 2022, the top recipient of finance for Islamic retail banks was Murabaha at 38.1% followed by Ijarah 32.8%. As for wholesale banks, the top recipient of finance was Murabaha at 92.2%.

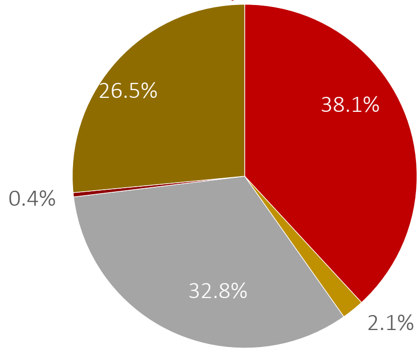
Table 5.5: Islamic Banks' Lending Distribution by Islamic Instrument (% of Total Facilities)

Instrument	Retail			Wholesale		
	Q2 2021	Q2 2022	Change	Q2 2021	Q2 2022	Change
Murabaha	39.7	38.1	-1.6	67.7	92.2	24.5
Istisna'a	2.8	2.1	-0.7	1.1	0.0	-1.1
Ijarah	31.0	32.8	1.8	0.9	7.8	6.9
Salam	0.8	0.4	-0.4	1.3	0.0	-1.3
Others	25.7	26.5	0.8	29.0	0.0	-29

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

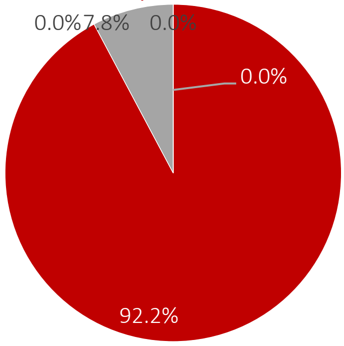
Source: CBB.

Chart 5.5: IR Banks' Lending Distribution by Islamic Instrument (% of Total Facilities)



Source: CBB.

Chart 5.6: IW Banks' Lending Distribution by Islamic Instrument (% of Total Facilities)



Source: CBB.

■ Murabaha ■ Istisna'a ■ Ijarah ■ Salam ■ Others

5.4 Profitability

Improvement in earnings for Islamic banks

ROA for Islamic retail banks increased to 0.4% in June 2022 compared to 0.3% in June 2021. ROE also increased from 3.6% to 5.5% for the same period. Furthermore, operating expenses decreased from 73.2% in June 2021 to 64.5% in June 2022. As for Islamic wholesale banks, ROA increased from 0.4% in June 2021 to 0.6% in June 2022. ROE also increased from 4.3% to 5.0% in the same period. Furthermore, operating expenses (as % of total income) decreased from 65.5% in June 2021 to 50.8% in June 2022.

Table 5.6: Islamic Banks' Profitability (%)

Indicator	Retail			Wholesale		
	Q2 2021	Q2 2022	Change	Q2 2021	Q2 2022	Change
ROA*	0.3	0.4	0.1	0.4	0.6	0.2
ROE**	3.6	5.4	1.8	4.3	5.0	0.7
Operating expenses (% total operating income)	73.2	64.5	-8.7	65.5	50.8	-14.7

Source: CBB.
** ROA = ratio of net income to assets.*
***ROE = ratio of net income to tier 1 capital.*

5.5 Liquidity

Liquidity remains remain stable for Islamic retail and wholesale banks

The volume of liquid assets available to Islamic retail banks decreased from 19.2% of total assets in June 2021 to 18.9% in June 2022. The ratio of total facilities to deposits decreased from 76.2% in June 2021 to 73.5% in June 2022.

As of end- June 2022, liquid assets of Islamic wholesale banks represented 17.4% of total assets, 1.6% lower than the 19.0% registered in June 2021. Additionally, the facilities deposit ratio decreased from 64.9% in June 2021 to 35.2% in June 2022.

Table 5.7: Islamic Banks' Liquidity (%)

Indicator	Retail			Wholesale		
	Q2 2021	Q2 2022	Change	Q2 2021	Q2 2022	Change
Liquid Assets (% of total assets)	19.2	18.9	-0.3	19.0	17.4	-1.6
Facilities – deposits ratio (%)	76.2	73.5	-2.7	64.9	35.2	-29.7

Source: CBB.

Part III:

DEVELOPMENT IN THE NON-BANKING FINANCING SECTOR

6 PERFORMANCE OF THE INSURANCE SECTOR

HIGHLIGHTS

Insurance Licenses	Contribution to GDP	Contribution to Financial Sector
130	5.3%	32.3%
Asset of Conv. Insurance	**Assets of Takaful Insurance**	**Gross Premiums**
BD 2,136 mn	BD 194.6 mn	BD 146.9 mn

- Conventional firms account for 91.5% of total insurance industry with BD 2,196 million in total gross premiums as of June 2022. General insurance contributes 79.1% of total gross premiums.
- Local Conventional insurance firms' performance is concentrated on Motor and Long-term (Life) business lines, and Takaful is concentrated in Motor and Medical business lines.
- Overseas insurance firms' performance is concentrated on Medical and Long-term (Life) business lines.

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.[6] The conventional sector is further divided into local and overseas/branch firms.[7]

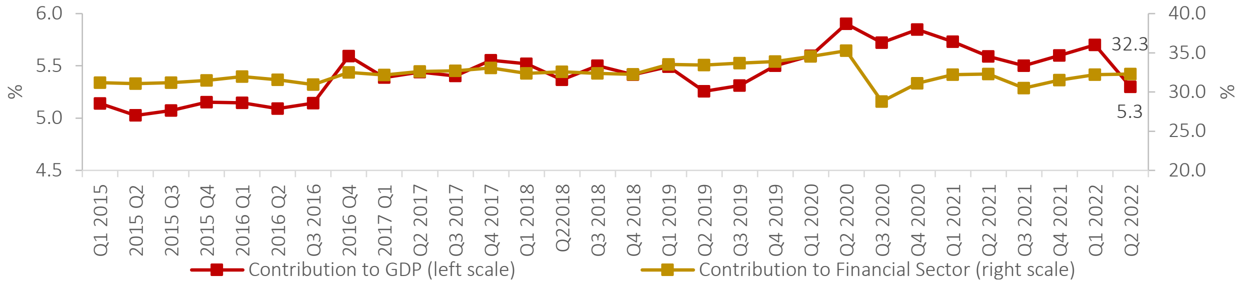
A significant number of insurance companies and organizations have established their presence in Bahrain. As of August 2022, there are a total of 130 insurance organizations licensed and registered in the Kingdom. There are 31 insurance companies: 16 conventional local, 10 conventional overseas/foreign branches, and 5 takaful. From these companies, 2 companies are conventional re-insurance firms and 2 re-takaful firms. These institutions offer all basic and modern insurance services such as medical and health insurance and long-term insurance (life and savings products). The remaining 99 other registered insurance licenses include 32 Insurance Brokers, 3 Insurance Managers, 3 Insurance Consultants, 16 Insurance Firms, brokers and consultants restricted to business outside Bahrain, 30 Registered Actuaries, 13 Registered loss Adjusters, and 2 Insurance Pools and Syndicates.

The insurance industry continued to grow during the past few years. 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. Insurance contribution increased to 5.4% of GDP by end of 2017, 5.5% by end of 2018, 5.4% by end of 2019, 5.8% by end of 2020, 5.6% by end of 2021. For Q2 2022, the insurance sector represented 5.3% of the real GDP and the contribution of the Insurance sector to the

[6] Takaful companies are companies conducting takaful business in line with Islamic principles. Overseas insurance companies are branches of foreign companies.
7 Chapter 6 covers the period between Q2 2021 and Q2 2022, unless otherwise indicated.

overall financial sector has increased representing 32.3%. Chart 6.1 shows the quarterly contribution of the Insurance sector to GDP along with the contribution of the insurance sector to the financial sector.

Chart 6.1: Insurance Sector Contribution and Quarterly Growth to GDP (%)



Source: IGA.

6.2 Financial Position and Profitability of Insurance Sector

As of June 2022, total assets of the Insurance sector reached BD 2,331.3 million with a decrease of 3.7% compared to BD 2,421.6 million in June 2021. Total liabilities had a decrease of 3.5% over the same period reaching BD 1,662.1 million.

Table 6.1: Total Assets, Liabilities, Capital, and Profitability of Insurance Sector by Segment

BD'000	Total Assets*		Total Liabilities*		Capital Available*		Net Profit*	
	Q2 2021	Q2 2022	Q2 2021	Q2 2022	Q2 2021	Q2 2022	Q2 2021	Q2 2022
Conventional	**2,217,185**	**2,136,742**	**1,592,791**	**1,531,120**	**379,382**	**363,531**	**20,356**	**1,299**
Local	1,987,508	1,942,680	1,399,694	1,369,323	345,625	332,739	17,566	(1,310)
Overseas	229,677	194,062	193,097	161,797	33,757	30,792	2,790	2,609
Takaful	**204,372**	**194,571**	**128,995**	**130,975**	**53,670**	**40,724**	**2,644**	**2,374**
All Insurance	**2,421,557**	**2,331,314**	**1,721,787**	**1,662,095**	**433,052**	**404,254**	**20,355**	**1,299**

**For takaful it only includes Shareholder figures.*
Source: CBB.

Total available capital[8] decreased from 433.1 BD million in June 2021 to 404.3 BD million in June 2022. Profitability on the other hand, decreased significantly between June 2021 and June 2022 reaching BD 1.3 million.

6.2.1 Conventional Insurance Firms

As of June 2022, total assets of the conventional insurance sector stood at BD 2,136.7 million decreasing by 3.6% compared to the BD 2,217.2 million registered in June 2021. Total assets of local insurance firms were BD 1,942.7 million (90.9% of total assets) with a negative growth rate of 2.3% since June 2021. Total assets of overseas foreign branches were BD 194.1 million (9.1% of total assets) recording a decline of 15.5%.

The liabilities of the conventional insurance sector registered at BD 1,531.1 million with a 3.9% decrease from the BD 1,592.8 million in June 2021. Liabilities for local insurance firms registered at BD 1,369.3 million decreasing by 2.2%. Liabilities of overseas foreign branches were BD 161.8 million in June 2022 with a decrease of 16.2%.

Available Capital: Total capital as of June 2022 was at BD 363.5 million decreasing by 4.2% from the BD 379.4 million in the equivalent period of the previous year. Total available capital for local insurance was BD 332.7 with a YoY decrease of 3.7%. Total available capital for overseas foreign branches decreased by 8.8% from BD 33.8 million in June 2021 to BD 30.8 million in June 2022.

Net profit decreased for conventional insurance firms from BD 20.4 million in June 2021 to a profit of BD 1.3 million in June 2022. Net loss for local insurance was BD 1.3 million with a YoY decrease of 107.5%. Net profit for overseas insurance was BD 2.6 with a year-to-year decrease of 6.8%.

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

6.2.2 Takaful Insurance Firms

Total assets in Takaful firms in June 2022 decreased by 4.8% to BD 194.6 million. The liabilities increased by 1.5% from BD 129 million in June 2021 to BD 131 million in June 2022. Total regulatory capital experienced an annual decrease of 24.1% from BD 53.7 million in June 2021 to BD 40.7 million in June 2022. As for net profits, Takaful companies showed a 10.2% decline in profits between June 2021 and June 2022 recording BD 2.4 million.

6.3 Insurance Premiums and Claims Analysis

The Insurance products and services in the Kingdom are delivered via two main insurance classes: Life and non-life insurance.[9]

Gross Premiums for the insurance sector stood at BD 146.9 million, increasing by 2.3% YoY. Conventional insurance represented 86.3% of total gross premiums (local and branches represented 39.7% and 46.3% respectively) while takaful accounted for 13.7% of gross premiums. As of June 2022, life insurance represented 15.9% of gross premiums while non-life/general insurance represented 84.1% covering the various classes (Graph 6.2).

Looking at the performance by class, Long-term (Life) category experienced the only decline within the rest of the insurance business line, with an annual decrease of 23.3%. On the other hand, the Miscellaneous Financial Loss business line and Engineering insurance experienced an annual increase by 38.6% and 32.1% during the same period. The top 3 business lines sectors represented 72.3% of total gross premiums. High concentration within these sectors can be explained by Banks imposing an obligatory requirement on customers to have a life insurance prior to getting specific loans, third party motor insurance being mandatory, and many institutions providing their employees with health insurance.

As of June 2022, Net Premiums Written decreased compared to the previous period registering a value of BD 90.3 million. Miscellaneous Financial Loss class showed the biggest increase over the period increasing by 224.6%, from BD 118 million in June 2021 to BD 385 million in June 2022. On the other hand, the biggest decline was derived from Long-term (Life) class, decreasing from BD 26.7 million in June 2021 to BD 18.8 million in June 2022.

However, Gross Claims for the overall insurance industry recorded a YoY decrease of 1.6% from BD 69.7 million in June 2021 to BD 68.6 million in June 2022. The decrease was mainly due to a decrease in the Long-term (Life) class by 35.9% from BD 19,227 million in June 2021 to BD 12,330 million in June 2022.

Net Claims for the overall insurance industry show an increase of 3.1%, which was derived from an annual increase Motor by BD 4,556 million (26.9%). The largest drop was recorded in Long-term (Life) by BD 4,882 million (33.7%).

Table 6.2: Premiums and Claims for all Insurance Firms by Class– Bahrain Operations

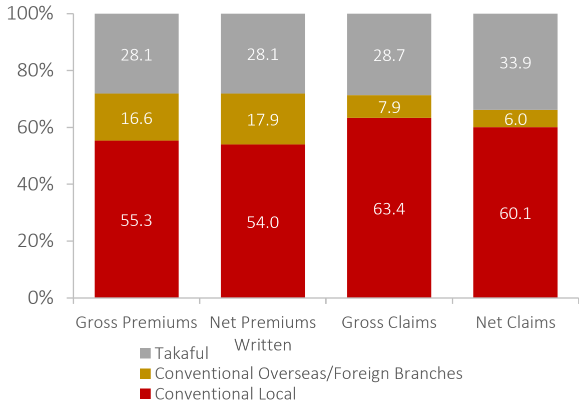
BD '000	Gross Premiums		Net Premiums Written		Gross Claims		Net Claims	
	Q2 2021	Q2 2022	Q2 2021	Q2 2022	Q2 2021	Q2 2022	Q2 2021	Q2 2022
Long-term (Life)	30,386	23,316	26,695	18,821	19,227	12,330	14,479	9,597
Fire, Property & Liability	18,164	21,356	2,575	3,267	5,876	4,911	372	1,180
Miscellaneous Financial Loss	3,050	4,228	118	385	254	227	84	(140)
Marine & Aviation	2,731	3,155	786	897	314	-66	222	24
Motor	34,477	36,060	33,201	34,781	19,406	24,060	16,914	21,470
Engineering	3,880	5,126	825	704	-518	183	148	-79
Medical	45,676	46,775	30,276	29,489	23,029	25,155	16,541	17,999
Others	5,250	6,847	1,470	1,911	2,161	1,801	500	755
Total	**143,615**	**146,862**	**95,948**	**90,255**	**69,749**	**68,601**	**49,261**	**50,808**

Source: CBB.

The concentrations of premuims and claims by class are viewed in Graph 6.3:

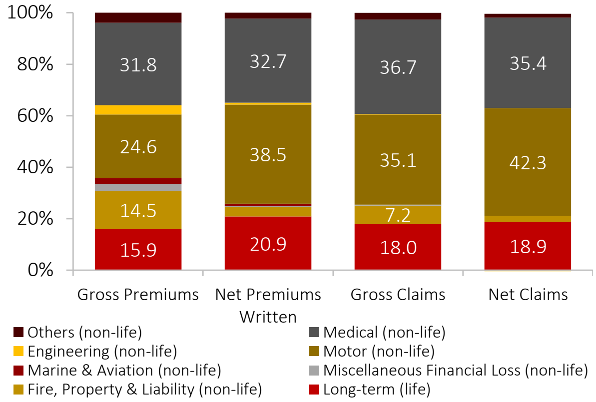
[9] Non-life or general insurance includes: Fire, Property & Liability, Miscellaneous Financial Loss, Marine & Aviation, Motor, Engineering, Medical and Others.

Chart 6.2: Premiums and Clais of Insurance Sector by Segment (%)



Source: CBB.

Chart 6.3: Concentrations of Premiums and Claims for Insurance Firms by Class (Q2 2022)



Source: CBB.

6.3.1 Conventional Insurance Firms

The Gross Premiums recorded for conventional insurance showed a YoY increase by BD 5.7 million (5.7%), where total gross premiums increased from BD 99.9 million in June 2021 to BD 105.6 million in June 2022 (Table 6.3). The greatest increases were from the Miscellaneous Financial Loss business class by around BD 500 million (56.3%). The largest YoY decline was by Long-term (Life) business classes with BD 6.9 million (25.5%). In terms of concentration, Long-term (life), Medical and Motor business classes represented 19.1%, 29.0% and 24.0% respectively of the total gross premiums.

Net Premiums Written reflected an annual decrease by 3.4% compared to June 2021. The greatest increase was from Others business class by around BD 351 million. Motor and Medical insurance remained the largest in terms of Net Premiums Written concentration as well, accounting for 37.8% and 27.6%.

Gross Claims decreased by 4.2% YoY in June 2022 due to a decrease in Marine and Aviation business class from BD 209 million in June 2021 to BD -142 million by June 2022. The highest share in gross claims was Medical 33.7 %, followed by Motor at 33.1%.

Net Claims on the other hand, experienced an annual increase of 0.6% from BD 33.4 million in June 2021, reaching BD 33.6 million in June 2022. Fire, Property and Liability business line increased by 363.7%. Nonetheless, the concentration falls heavily within the Motor insurance class, accounting for 40.9% of the total net claims.

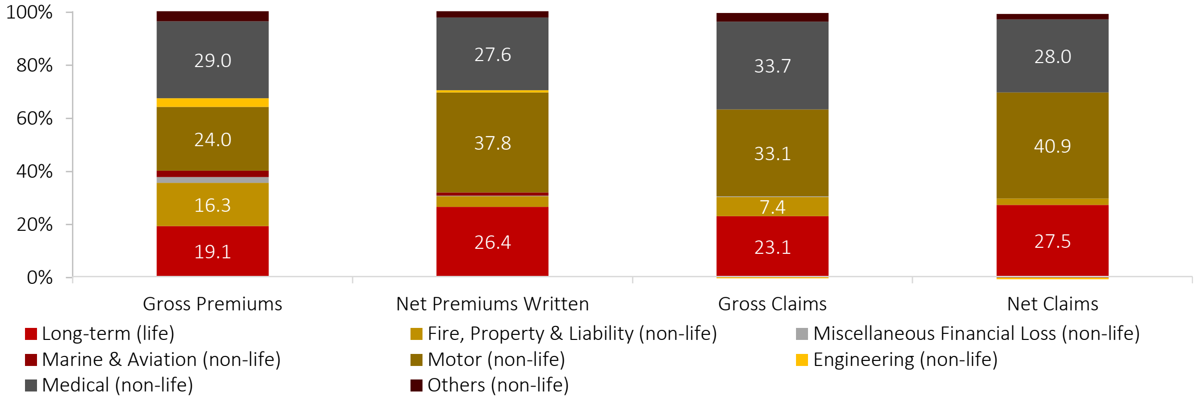
Table 6.3: Premiums and Claims for Conventional Insurance by Class

BD '000	Gross Premiums		Net Premiums Written		Gross Claims		Net Claims	
	Q2 2021	Q2 2022	Q2 2021	Q2 2022	Q2 2021	Q2 2022	Q2 2021	Q2 2022
Long-term (Life)	27,013	20,118	24,613	17,107	17,679	11,288	14,172	9,245
Fire, Property & Liability	13,477	17,179	2,023	2,581	5,660	3,602	179	830
Miscellaneous Financial Loss	1,420	2,220	(4)	183	144	142	23	(115)
Marine & Aviation	2,306	2,575	712	790	209	(142)	128	(44)
Motor	22,826	25,377	22,047	24,511	12,378	16,210	10,328	13,736
Engineering	2,258	3,401	718	560	(669)	(213)	88	(190)
Medical	27,467	30,572	16,181	17,892	14,514	16,469	8,182	9,415
Others	3,088	4,119	944	1,295	1,128	1,568	297	720
Total	**99,855**	**105,561**	**67,236**	**64,919**	**51,043**	**48,924**	**33,397**	**33,598**

Source: CBB.

Motor insurance had the highest exposure in Net Premiums Written (37.8%) and Net Claims (40.9%). Whereas, Medical had the highest exposure in Gross Premiums (29.0%) and Gross Claims (33.7%).

Chart 6.4: Concentrations of Premiums and Claims for Conventional Insurance by Class (Q2 2022)



Source: CBB.

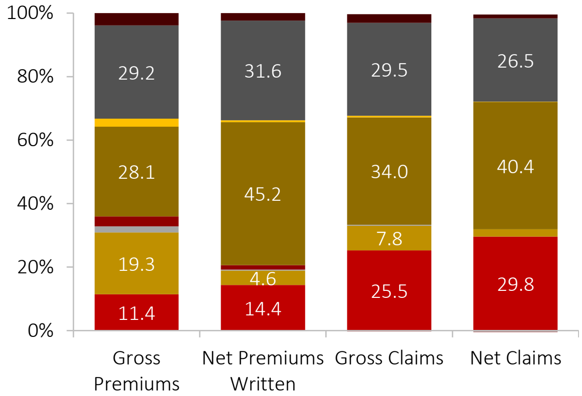
Table 6.4 below and Charts 6.6 and 6.7 shows a further division of the premiums and claims by class between Local and Overseas firms within the conventional insurance industry for June 2022. For local conventional insurance, Medical insurance has the highest concentration for Gross Premiums (29.2%), Motor has the highest concentration in Net Premiums Written (45.2%), Gross Claims (34.0%), and Net Claims (40.4%).

Table 6.4: Premiums and Claims for Conventional Local and Overseas Insurance by Class (Q2 2022)

BD '000	Gross Premiums		Net Premiums Written		Gross Claims		Net Claims	
	Local	Overseas	Local	Overseas	Local	Overseas	Local	Overseas
Long-term (Life)	9,248	10,869	7,027	10,080	11,077	211	9,114	131
Fire, Property & Liability	15,719	1,459	2,221	360	3,394	208	739	90
Miscellaneous Financial Loss	1,545	675	156	27	143	(1)	(114)	(1)
Marine & Aviation	2,484	91	715	75	(134)	(8)	(33)	(11)
Motor	22,828	2,549	22,031	2,480	14,792	1,419	12,334	1,402
Engineering	2,034	1,367	260	299	186	(399)	44	(234)
Medical	23,690	6,883	15,396	2,497	12,825	3,644	8,085	1,330
Others	3,705	413	945	350	1,218	350	370	350
Total	**81,254**	**24,307**	**48,750**	**16,168**	**43,500**	**5,423**	**30,540**	**3,058**

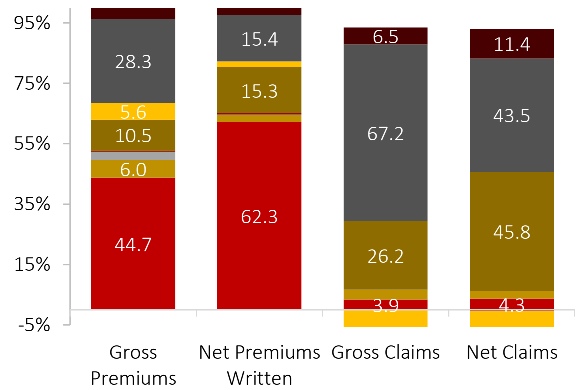
Source: CBB.

Chart 6.5: Concentrations of Premiums and Claims by Class for Local Insurance (Q2 2022)



Source: CBB.

Chart 6.6: Concentrations of Premiums and Claims by Class for Overseas Insurance (Q2 2022)



Source: CBB.

6.3.2 Takaful Insurance Firms

The Gross Premiums for Takaful companies decreased on a YoY basis by 5.6%, from BD 43.8 million at June 2021 reaching BD 41.3 million in June 2022. The largest increase was attributed to Marine and Aviation increasing by BD 155 million (36.5%). Medical Insurance line recorded the highest contributor towards total Takaful gross premiums, accounting for 39.2% of the total.
Net Premiums Written decreased by 11.8% from June 2021 to June 2022, reaching BD 25.3 million. Medical insurance accounted for the largest components in terms of gross claims, representing 45.8% of the total net premiums written.

Gross Claims increased by 5.2% compared from June 2021 to June 2022, with Fire, Property & Liability registering the largest increase (BD 1.1 million) within the same period. Medical and Motor insurance accounted for the largest components in terms of gross claims, representing 44.1% and 39.9% of the total gross claims.

Net Claims recorded an annual increase of 8.5% at June 2022, with Motor having the largest increase recorded at 17.4%. Furthermore, Medical and Motor represent the largest components of net claims, accounting for 49.9% and 44.9% from the total respectively.

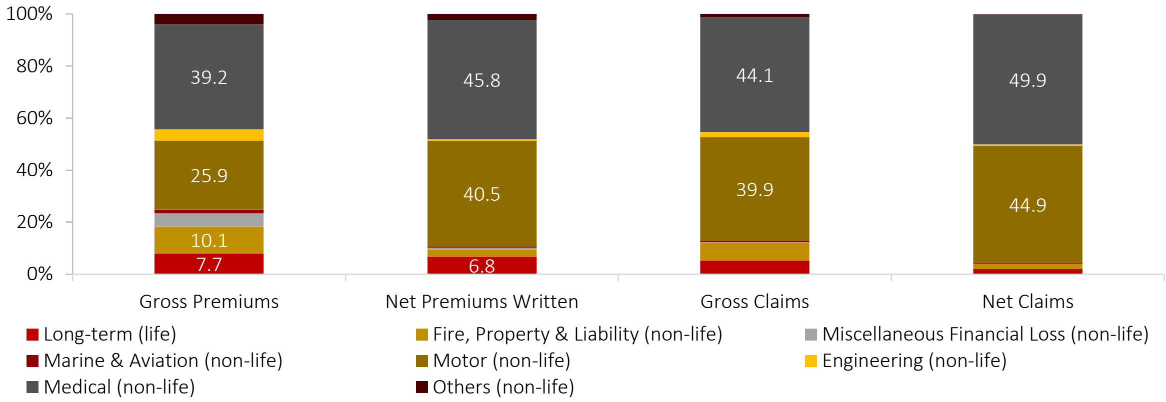
Table 6.5: Premiums and Claims by Class for Takaful Insurance Firms

BD '000	Gross Premiums		Net Premiums Written		Gross Claims		Net Claims	
	Q2 2021	Q2 2022	Q2 2021	Q2 2022	Q2 2021	Q2 2022	Q2 2021	Q2 2022
Long-term (Life)	3,374	3,198	2,082	1,715	1,548	1,041	306	352
Fire, Property & Liability	4,687	4,177	552	686	216	1,309	193	351
Miscellaneous Financial Loss	1,630	2,008	122	202	110	85	61	(25)
Marine & Aviation	425	580	74	107	105	76	94	68
Motor	11,651	10,682	11,155	10,270	7,029	7,850	6,587	7,734
Engineering	1,622	1,725	107	144	151	396	60	111
Medical	18,209	16,203	14,095	11,597	8,515	8,687	8,359	8,584
Others	2,162	2,728	526	615	1,033	233	204	35
Total	**43,760**	**41,301**	**28,712**	**25,336**	**18,707**	**19,677**	**15,864**	**17,210**

Source: CBB.

Takaful insurance companies have very high concentration on the Medical and Motor Insurance business lines. Gross Premiums for both sectors combined represent (65.1%), Net Premiums Written (86.3%), Gross Claims (84.0%), and Net Claims (94.8%).

Chart 6.7: Concentrations of Premiums and Claims by Class for Takaful Insurance Firms (Q2 2022)



Source: CBB.

6.3.3 Retention Ratio and Loss Ratio (By Class)

Life insurance business line registered a retention ratio of 80.7% in June 2022. Observing the non-life insurance, Medical and Motor, that accounted for 56.4% of the total Gross Premiums in June 2022 respectively, registered retention ratios of 96.5% for Motor and 63.0% for Medical. Nevertheless, retention ratios were significantly lower for other business lines such as Fire, Property and Liability and Miscellaneous Financial Loss, registering 15.3% and 9.1% respectively.

Table 6.6: Retention and Loss Ratios of Overall Insurance Sector

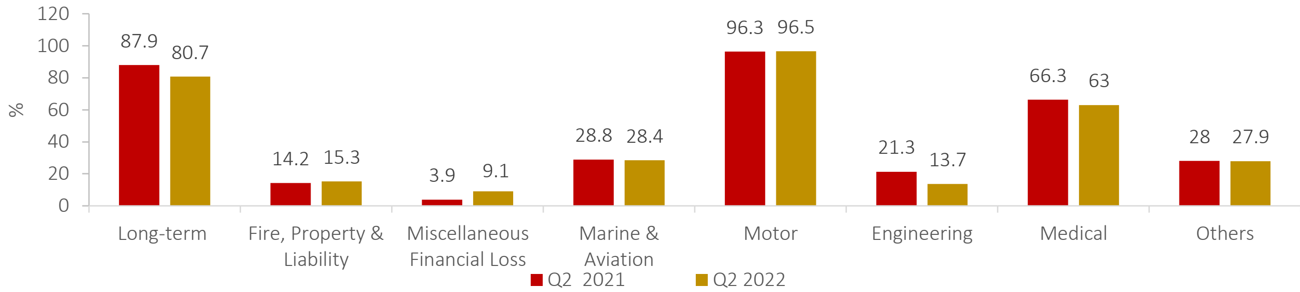
%	Retention Ratio [1]		Loss Ratio [2]	
	Q2 2021	Q2 2022	Q2 2021	Q2 2022
Long-term	87.9	80.7	58.6	57.6
Fire, Property & Liability	14.2	15.3	14.8	39.6
Miscellaneous Financial Loss	3.9	9.1	37.6	-72.0
Marine & Aviation	28.8	28.4	32.5	2.8
Motor	96.3	96.5	50.1	60.7
Engineering	21.3	13.7	36.6	-15.6
Medical	66.3	63.0	72.3	76.0
Others	28.0	27.9	41.0	52.0

1. *Net Premiums Written / Gross Premiums*

2. Net Claims Incurred / Net Premiums Earned

Source: CBB.

Chart 6.8: Retention Ratios of Insurance Sector



Source: CBB.

6.4 Regulatory Changes, Market trends and Risks.

The CBB has continued to take proactive approach towards achieving its mandated objectives towards the Insurance Sector with consideration of all stakeholders. The below demonstrates the list of initiatives taken to further develop the market for the benefit of all stakeholders:

- Reducing Outsourcing requirements to bolster business dealings and innovation;
- Strengthened Cybersecurity requirements, in light of recent cyber security risks;
- Proactively monitoring the implementation of IFRS 17;
- Amended CBB Reporting Requirement, in order to obtain timely prudential data;
- Employment of In-House Bahraini Actuaries, in order to anchor the important of the function & enhance local human capital wealth;
- Digitalizing Motor Insurance Process, in order to elevate people's experience;
- Digitalization of Medical Claim Process, in order to elevate people's experience;
- Proactively monitoring the implementation of Mutually Resolved Minor Accident to Insurance Firms, in order to elevate people's experience.

In addition, recently the CBB has been part of Bahrain's Economic Recovery Plan to increase insurance sector contribution to GDP to 8% by 2026.

7 PERFORMANCE OF CAPITAL MARKETS

HIGHLIGHTS

# of Companies	All Share Index	Islamic Index
42 June 2022	1,839.63 ▲ 2.36% YTD	667.76 ▼ 11.2% YTD
Market Capitalization	**Value of Transactions**	**Volume of Transactions**
BD 11.1 bn ▲ 2.4% YTD	BD 102 mn H1 2022	0.32 bn H1 2022

- Increase in Bahrain All Share & decrease in Bahrain Islamic Index.
- Bahrain Bourse's market capitalization stood at BHD 11.1 bn by the first half, increasing from BHD 10.8 bn in end of second half 2021, resulting in an increase of 2.4%.
- Financials Sector dominated the market trading activity as it had the highest value traded.
- Bahrainis represented 71% of the value of shares bought and 65% of value of shares sold during first half 2022.

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 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", CBB became responsible for Bahrain's capital markets with a combination of rule and principle based regulatory framework.

As of end of first half 2022, Bahrain Bourse recorded a total listing of 42 Companies, 3 Mutual Funds, 20 Bonds and Sukuk and one REIT. During second quarter of 2022, there were 20 companies that closed higher and 16 closed lower and 6 remained unchanged. Financials sector remains the dominant sector in Bahrain Bourse in terms of market capitalization and trading activity accounting for 49% of total value traded during first half 2022 and making up 70% of the total market capitalization. Bahrain Bourse remains a highly concentrated market in terms of market capitalization as the largest 5 companies in terms of market capitalization are AUB, NBB, ALBH BATELCO, and BBK represent 75.2% of the total market.

7.2 Bahrain Bourse

7.2.1 All Share Index and Islamic Index Overview

Increase in market index

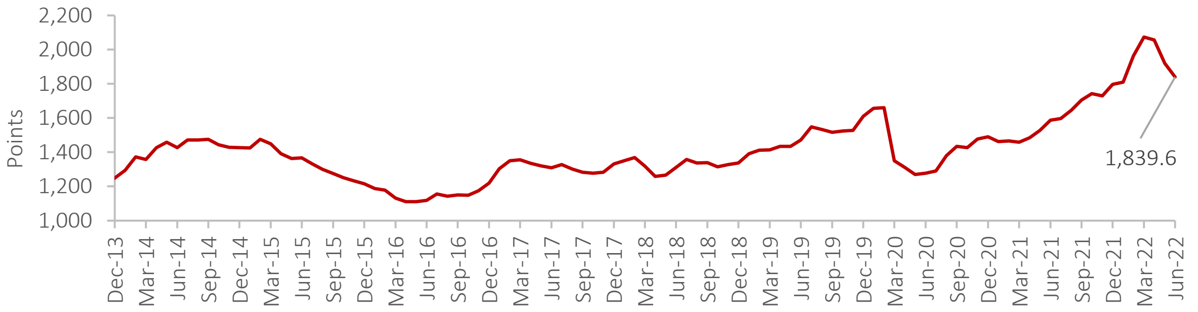
Bahrain All Share Index increased by 2.8% during second half 2022 year to date. The index kept increasing during the first half of the year with the lowest month-end close level recorded was in January, and the highest month end close was recorded in April.

Table 7.1: Key Indicators of Bahrain Bourse

Indicator	2014	2015	2016	2017	2018	2019	2020	2021	June 2022
All Share Index	1,426.6	1,215.9	1,220.5	1,331.7	1,337.3	1,610.2	1,489.8	1,797.3	1,839.6
Highest	1,476.0	1,474.8	1,220.5	1,356.0	1,369.9	1,610.2	1,668.7	1,797.3	2,122.5
Lowest	1,294.3	1,215.9	1,110.5	1,276.7	1,257.9	1,391.4	1,232.4	1,447.6	1,792.2
Market Cap (BD, million)	8,327.1	7,199.9	7,248.2	8,146.3	8,198.5	10,134.6	9,277.3	10,815.5	11,073.9
Total Value (BD million)	269.1	110.0	124.5	211.3	323.8	286.4	212.8	195.7	102.7
Total Volume (million)	1,126.1	515.6	734.4	1,129.8	1,441.1	1,157.3	1,209.3	1,018.3	328.2
No. of Transactions	16,211	11,248	10,592	19,440	19,225	20,712	19,309	21,001	10,835
No. of Companies Listed	47	47	46	44	43	44	44	42	42

Source: Bahrain Bourse.

Chart 7.1: Bahrain All-Share Index, Dec. 2013 – Jun. 2022



Source: Bahrain Bourse.

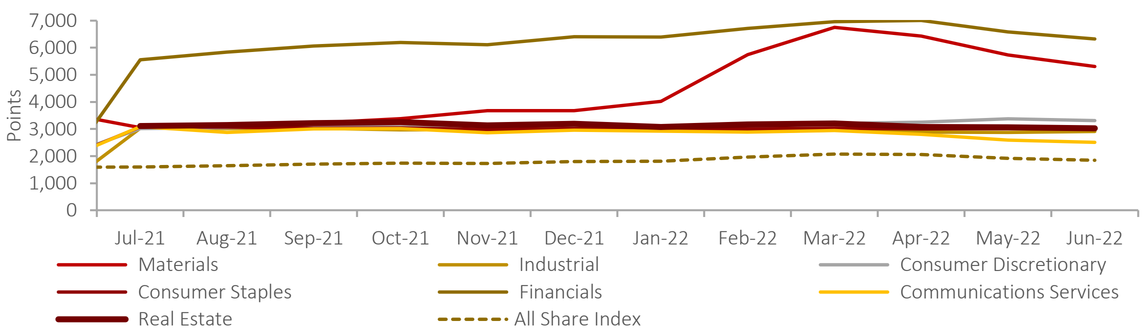
Bahrain Bourse's earlier sector industry classification had been in place since the establishment of Bahrain Bourse in 1987. The decision to reclassify current industrial sectors aims to enhance transparency and provide more reliable information on sector performance that is aligned to international best practices.

Table 7.2: Bahrain All Share Index by Sector

	2021	H1 2022
Materials	3,675.4	5,306.3
Industrials	3,042.2	2,908.5
Consumer Discretionary	3,035.8	3,312.8
Consumer Staples	3,010.6	3,003.1
Financials	6,402.5	6,329.9
Communications Services	2,957.9	2,507.1

Source: Bahrain Bourse.

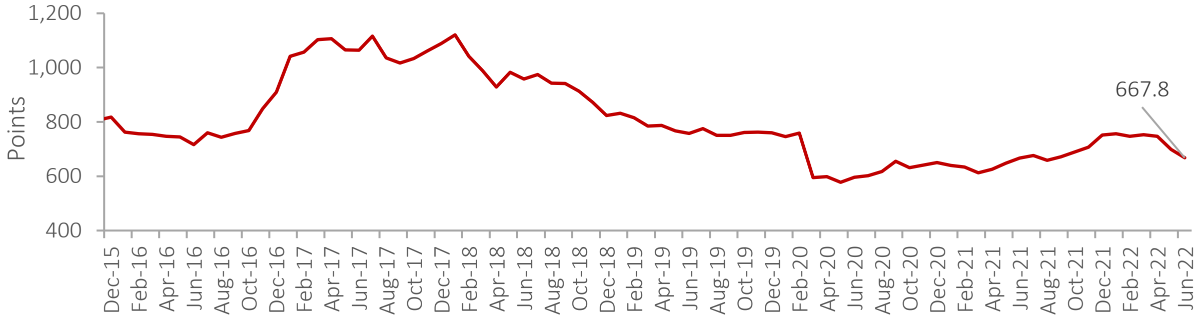
Chart 7.2: Sector Indices Levels & Returns, July. 2021 – Jun. 2022



Source: Bahrain Bourse.

In September 2015, Bahrain Bourse launched the Bahrain Islamic Index. It was the first Islamic finance index in the region, and 16 Shariah compliant companies are included within the index as of first half of 2022. YTD data demonstrates that the Bahrain Islamic Index decreased by 11.2% between January 2022 and June 2022 reaching 667.8 points.

Chart 7.3: Bahrain Islamic Index, Dec. 2015 – Jun. 2022



Source: Bahrain Bourse.

7.2.2 Bahrain Bourse Trading Statistics

Increase in market capitalization

As of first half of 2022, market capitalization of the Bahrain Bourse stood at BD 11.1 billion. This level of market capitalization is 2.4% higher from the second half of 2022.

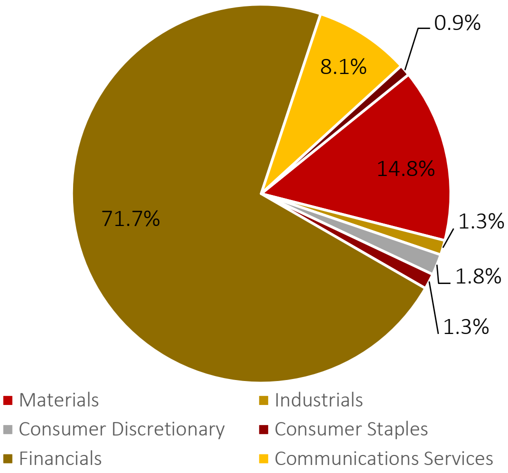
Table 7.3: Market Capitalization on the Bahrain Bourse

Sector (BD)	H2 2021	H1 2022	H2 2021–H1 2022 (% Change)
Materials	1,136,000,000	1,640,100,000	44.4
Industrials	145,265,000	138,880,000	-4.4
Consumer Discretionary	180,580,543	197,055,918	9.1
Consumer Staples	146,583,999	146,218,178	-0.2
Financials	8,032,611,119	7,945,112,635	-1.1
Communications Services	1,063,716,677	901,602,966	-15.2
Real Estate	110,693,971	104,975,971	-5.2
Total	**10,815,451,308**	**11,073,945,668**	**2.4**

Source: Bahrain Bourse.

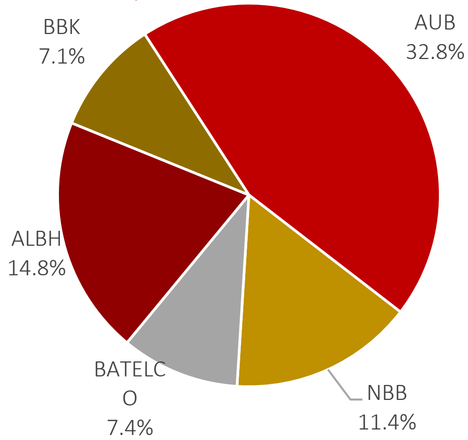
A breakdown of market capitalization by sector indicates that the Materials sector scored the highest increase in market capitalization (44.4%) during the first six months of 2022. The Communications Services sector recorded the highest percentage decrease in market capitalization with a 15.2% decrease during the first six months of 2022.

Chart 7.4: Market Capitalization by Sector (June 2022)



Source: Bahrain Bourse.

Chart 7.5: Largest 5 companies by Market Capitalization (June 2022)



Source: Bahrain Bourse.

Ahli United Bank is the largest company in terms of Market Capitalization and contributes 32.8% of the total market capitalization as of first half 2022. Aluminum Bahrain has the second largest share of Market Capitalization of 14.8% and it is followed by National Bank of Bahrain with 11.4%, Bahrain Telecommunication Company with 7.4% and Bank of Bahrain and Kuwait with 7.1%.

Table 7.4: Largest 5 Companies by Market Capitalization (Jun. 2022)

Company	Market Capitalization (BHD)	% from Total Market
Ahli United Bank (AUB)	3,635,396,188	32.8
National Bank of Bahrain (NBB)	1,266,941,965	11.4
Bahrain Telecommunication Company (BATELCO)	814,968,000	7.4
Aluminum Bahrain (ALBH)	1,640,100,000	14.8
Bank of Bahrain and Kuwait (BBK)	790,896,462	7.1
Total	**8,148,302,615**	**73.6**

Source: Bahrain Bourse.

Most of the value of shares traded during first half 2022 was in the Financial sector whose traded shares (by value) represented 49% of total value.

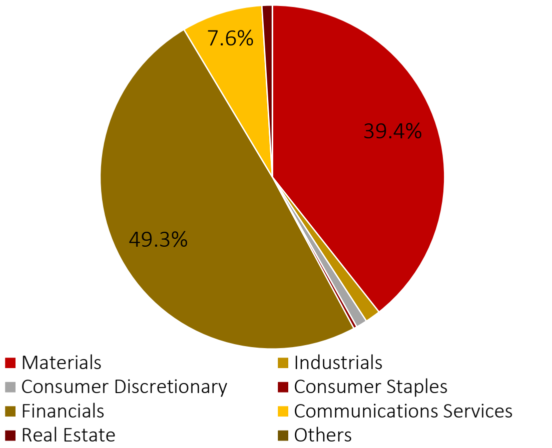
Table 7.5: Value of Shares Traded by Sector (% of Value of all shares traded)

Sector	H2 2021	H1 2022
Materials	22.2	39.4
Industrials	4.3	1.4
Consumer Discretionary	1.6	1.0
Consumer Staples	0.8	0.3
Financials	58.4	49.3
Communications Services	10.7	7.6
Real Estate	1.1	1.0

Source: Bahrain Bourse.

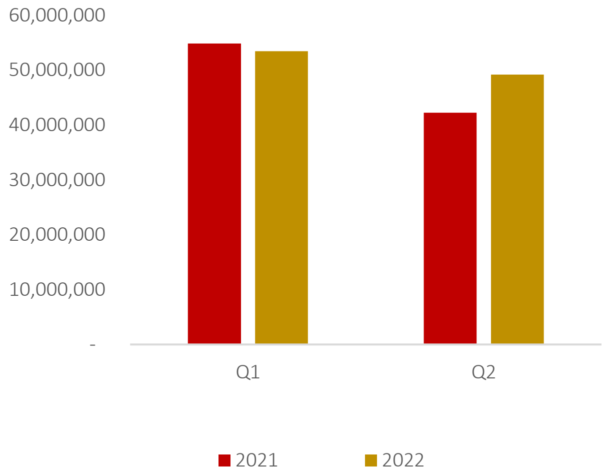
The Materials sector represents the second largest level at 39.4% of the total value of shares traded in first half 2022. Investors interest in Consumer Staples sector were the least during first half of 2022 whose traded shares by value represented only 0.3% each of the total value of traded shares. During first half 2022, the value of shares traded was highest in April and the lowest was in May, and the average value of shares traded during the year for a month was BD 17.1 million.

Chart 7.6: Value of Shares Traded by Sector (% of Value of all shares traded) (H2 2022) *



** Other sector includes Closed companies, Non-Bahraini and IPOs.*
Source: Bahrain Bourse.

Chart 7.7: Value of Shares Traded Comparison



Source: Bahrain Bourse.

The bulk of the volume of shares traded in first half 2022 was also in the Financial sector representing 80% of the total volume of shares traded, followed by the Materials sector at 10%. The lowest level was attained by the Consumer Staples sector at 0.2%.

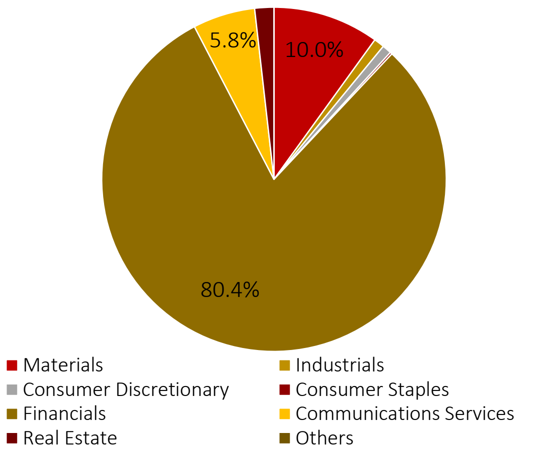
Table 7.6: Volume of Shares Traded by Sector (% of Volume of all shares traded)

Sector	H2 2021	H1 2022
Materials	6.8	10
Industrials	1.8	1
Consumer Discretionary	1.0	1
Consumer Staples	0.3	0.2
Financials	81.8	80
Communications Services	5.6	6
Real Estate	1.4	2
Closed	1.4	0

Source: Bahrain Bourse.

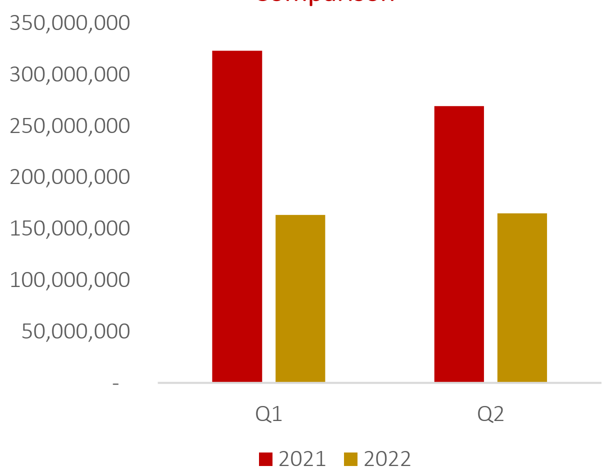
During first half of 2022, the volume traded was highest in April and the lowest was in January, and the average volume traded during the year for a month was 54.7 million shares.

Chart 7.8: Volume of Shares traded by Sector (% of Volume of all shares traded) (H2 2022) *



** Other sector includes Closed companies, Non-Bahraini and IPOs.*
Source: Bahrain Bourse.

Chart 7.9: Volume of Shares Traded Comparison



Source: Bahrain Bourse.

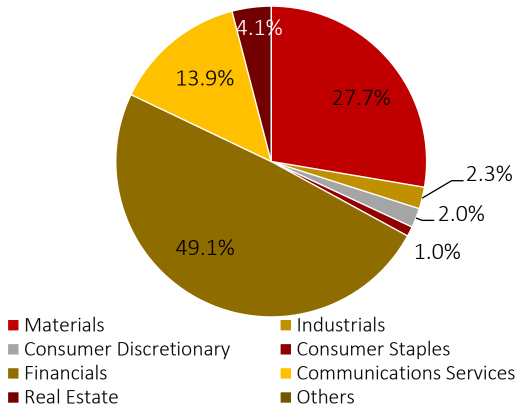
During the first half of 2022, the market executed 10,835 transactions. Most of the transactions were executed by the Financials sector at 5,323 transactions (49% of all transactions), followed by the Materials at 2,996 transactions (28%), and the Communications Services sector at 1,501 transactions (14%).

Table 7.7: Number of Transactions by Sector

Sector	H2 2021	H1 2022
Materials	1,408	2,996
Industrials	498	245
Consumer Discretionary	221	219
Consumer Staples	123	111
Financials	7,048	5,323
Communications Services	1,262	1,501
Real Estate	410	440
Closed	1	0
Total Market	10,971	10,835

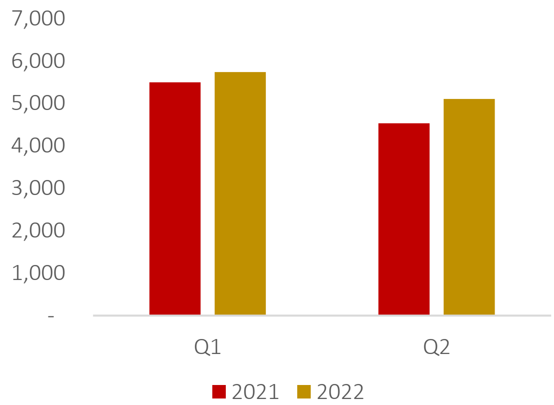
Source: Bahrain Bourse.

Chart 7.10: Number of Transactions (% of all transactions) (H1 2022) *



**Other sector includes Closed companies and IPOs.*
Source: Bahrain Bourse.

Chart 7.11: Number of Transactions Comparison



Source: Bahrain Bourse.

Trading by Nationality

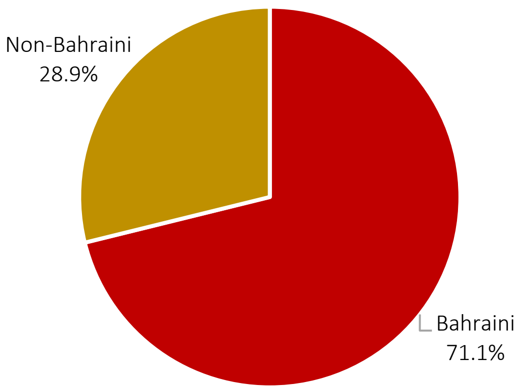
As of first half 2022, Non-Bahraini nationals contributed to 29% of the value of shares bought while Bahraini nationals contributed the remaining 71% of the value of shares bought. As for sell-side of the transactions, Non-Bahraini nationals contributed to 35% of the value of shares sold while Bahraini nationals contributed to 65% of the remaining value of shares sold.

Table 7.8: Value of Transactions by Nationality (BD)

	H2 2021		H1 2022	
	Bahraini	Non-Bahraini	Bahraini	Non-Bahraini
Buy	67,728,614	25,310,642	73,036,154	29,617,297
Sell	70,727,345	22,311,912	66,520,795	36,132,655

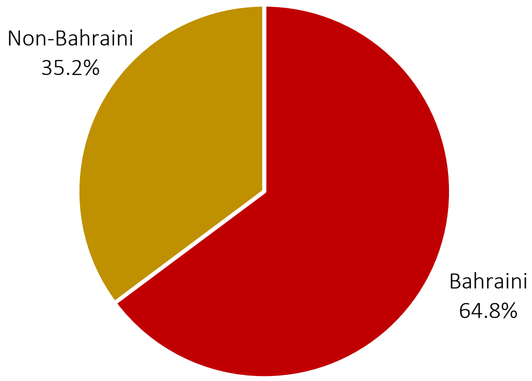
Source: Bahrain Bourse.

Chart 7.12: Share of Trading Value of Buy transactions by nationality (H1 2022)



Source: Bahrain Bourse.

Chart 7.13: Share of Trading Value of Sell transactions by nationality (H1 2022)



Source: Bahrain Bourse.

GCC Indices recover

All the GCC major equity markets indices with the exception of Muscat Securities Market Index 30 recorded positive returns during first half 2022 compared to end of year 2021. The largest increase was recorded by Abu Dhabi Exchange General Index at 10%, followed by Kuwait All Share Index with an increase of 5.4%.

Table 7.9: Stock Market Indices in GCC counties

Index	2021	H1 2022	2021 – H1 2022 (% Change)
Bahrain All Share Index	1,797	1,839	2.3
Kuwait All Share Index	7,043	7,423	5.4
Dubai Financial Market General Index	3,196	3,223	0.8
Tadawul All Share Index	11,282	11,523	2.1
Abu Dhabi Exchange General Index	8,488	9,378	10.5
Qatar Exchange Index	11,626	12,194	4.9
Muscat Securities Market Index 30	4,130	4,122	-0.2

Sources: Bahrain Bourse, Saudi Stock Exchange (Tadawul), Boursa Kuwait, Qatar Stock Exchange, Dubai Financial Market, Abu Dhabi Securities Exchange and Muscat Securities Market.

7.2.3 Economic Recovery Plan and Capital Markets Development Strategy

In December 2021, the Government of Bahrain has initiated the economic recovery plan, part of which aims to greatly contribute in making Bahrain Bourse a regional financial market. With the support of the Central Bank of Bahrain, Bahrain Bourse continues to develop its operations in order to develop the financial services sector, benefit the national economy, provide more quality job opportunities, and attract investments.

The Central Bank of Bahrain is working with Bahrain Bourse to implement a set of priorities and initiatives in partnership with the relevant parties, specifically in areas that will develop the performance of the financial market sector. The initiatives include encouraging initial public offerings and listing of companies, including government-owned companies, and enhancing ways for coordination of dual listing with other GCC countries. Efforts are also focused on encouraging small and medium-sized companies to list in the Bahrain Investment Market (BIM), where the main performance indicator specified for this initiative is the listing of 5 new companies on the BIM during the next five years.

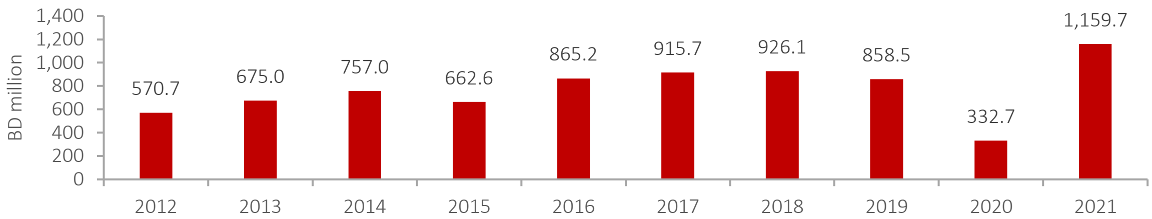
The strategy also aims to develop the financial market by supporting Bahrain in joining the emerging markets index, which would stimulate investment and support intermediaries in a way that contributes to expanding the number of investors and improving liquidity levels. It is also worth noting that the Central Bank of Bahrain is currently working with Bahrain Clear to enhance ways of coordinating and linking clearing, settlement and central depository systems regionally and internationally, which aims to facilitate and enable investors to access the market of both parties by removing borders as much as possible. Further, Bahrain Bourse and Bahrain Clear are currently working on various areas to automate the services provided to investors, including the application of the digital onboarding mechanism to attract investors and facilitate the trading process and its related services.

7.3 Market Resilience

Boost in corporate profitability

The overall profitability of the Bahraini Bourse increased by 249% to BD 1,159.7 million in 2021 from BD 332.7 million in 2020. Return on assets increased to 1.7% in 2021, while return on equity increased to 11.2% in 2021 compared to 3.4% in 2020.

Chart 7.14: Stock Market Net Income



Source: Bahrain Bourse.

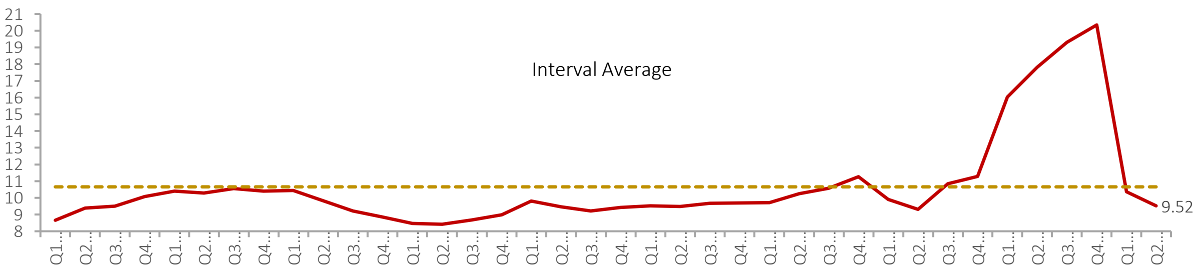
As at December 2021, the total market P/E ratio increased to 20.35 from 16.40 in 2020.

Table 7.10: Price-Earnings Multiples

Sector	2020	2021
Materials	N/A	2.51
Industrials	N/A	-57.97
Consumer Discretionary	N/A	27.79
Consumer Staples	N/A	12.98
Financials	N/A	14.36
Communications Services	N/A	13.38
Real Estate	N/A	20.32
Total Market	16.40	20.35

Source: Bahrain Bourse.

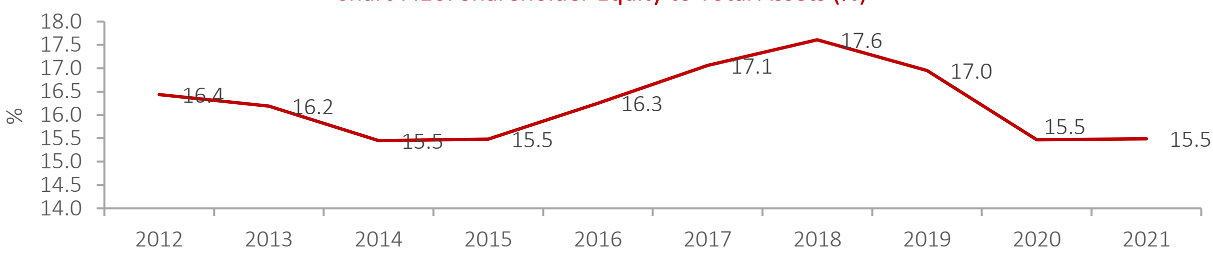
Chart 7.15: Total Market Price-Earnings Multiples



Source: Bahrain Bourse.

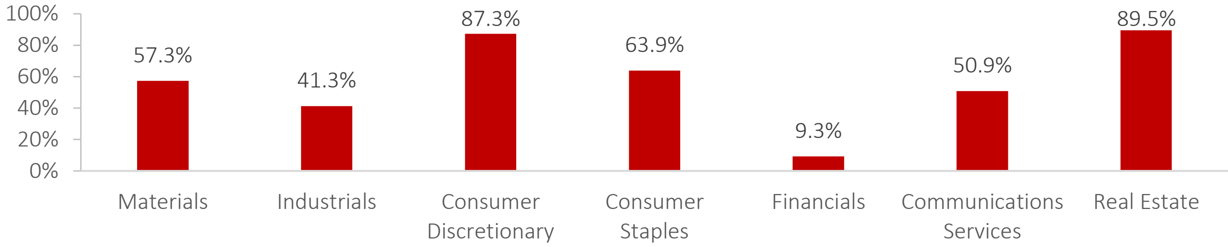
The overall equity-to-assets ratio remained at 15.5% in 2021. The Financials sector has the lowest equity/assets ratio due to the high leverage nature of the sector (Chart 7.17 & 7.18).

Chart 7.16: Shareholder Equity to Total Assets (%)



Source: Bahrain Bourse.

Chart 7.17: Shareholder Equity/Total Assets by Sector (2021)



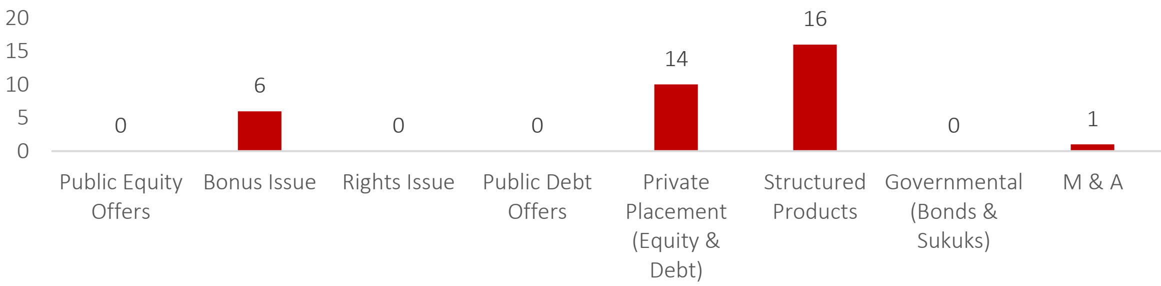
Source: Bahrain Bourse.

7.4 Capital Market Activities

7.4.1 Offering of Securities

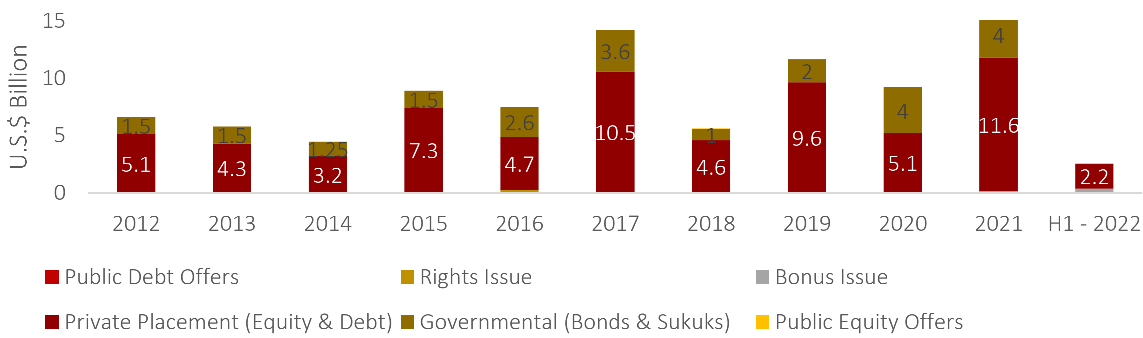
As at June 2022, CBB issued its no objection to the issuance of 30 private offering documents after ensuring the completeness of all the information and details as per CBB Law, Rules and Regulations. The total value of issuances reached USD 2.555 billion. (Chart 8.19 & 8.20).

Chart 7.18: Number of Capital Market Activities



Source: CBB.

Chart 7.19: Total Issuance Value



Source: CBB.

7.4.2 Kuwait Finance House ("KFH") offer to acquire 100% of Ahli United Bank B.S.C.'s ("AUB") issued and paid-up capital

KFH announced on 25th July 2022 its firm intention to make an offer to acquire up to 100% of the issued and paid-up ordinary shares of AUB, by way of a share exchange at a ratio of 2.695 AUB shares for each KFH share. KFH also published its offer document on the same date.

The Offer Documents, which include the Offer Document issued by KFH, the Offeree Board Circular issued by AUB's Board of Directors, and the report of the independent professional advisor, were sent to AUB's shareholders and were published on the websites of AUB, KFH, Bahrain Bourse and Boursa Kuwait on 15th August 2022 in accordance with the requirements of the Takeovers, Mergers and Acquisitions (TMA) Module, Volume 6 of the CBB Rulebook.

The Offer opened for acceptances on 24th August 2022 for an initial offer period ending on 7th September 2022. KFH announced the Offer unconditional in all respects on 8th September 2022, having received acceptances representing 96.107% and that the offer will remain open for acceptances until 23rd September 2022 in accordance with the requirements of the Takeovers, Mergers and Acquisitions (TMA) Module, Volume 6 of the CBB Rulebook.

In addition, having received the abovementioned acceptances, KFH also announced that it intends to exercise its right of compulsory acquisition in accordance with Article 319 bis I of the CCL and TMA 3.4.4 of the TMA Module, and issued notices of compulsory acquisition to the dissenting shareholders on 14th September 2022.

7.5 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, CBB; through the requirements stipulated under Module of CBB Rulebook Volume 6 requires Licensees to have in place a well-designed Disaster Recovery Plan and 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 crypto-asset services. Crypto-asset service providers are required to test their IT infrastructures and core systems to verify the robustness of the security control measure that is in place to prevent security breaches, including penetration testing and vulnerability assessment undertaken by reputable third-party cyber security consultants to be conducted each year in June and December. In addition, Capital Markets licensees are mandated to maintain relevant systems in place for mitigating and managing operational and other risks.

FinTech solutions 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 block chain technologies, post-trade and settlement digitization and innovative technology driven business models. In order to effectively reduce risks related to use of FinTech solutions, 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.

Among the shared goals of CBB and the Bahrain Bourse presently 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 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 CBB tackles.

As of June 2022, 6 of the 42 listed companies on Bahrain Bourse were cross-listed outside of Bahrain, leading to challenges faced by CBB in maintaining the cross-listed companies' compliance with the capital market regulations of Bahrain. CBB is utilizing the IOSCO MMoU and the MoU between regulators of the financial markets in the Gulf Cooperation Council States in requesting assistance in relation to cross-listed companies.

It is important that the Buy-and-Hold/Passive Investment investor mentality is tackled, through the provision of tools which gives the investors a clear view of market activity. Bahrain Bourse is in collaboration with market information companies, such as Bloomberg, Thompson Reuters etc., to distribute data packages which include facilities relating to real-time market coverage, historical and end-of-day data, etc.

7.6 Developments in Regulation and Initiatives

The CBB's CMSD actively takes part in joint work meetings of the GCC Council's Capital Market Authorities (or their equivalent) that aim to harmonize the rules and regulations for the capital markets in the GCC and actively participates in the organization and management of a number of bilateral economic cooperation initiatives between the Kingdom of Bahrain and the Kingdom of Saudi Arabia as approved by the Saudi-Bahraini Coordination Council. In addition, the CMSD, on behalf of the CBB, manages its international cooperation within the capital markets' field, while making use of the best international experiences, among others. Therefore, the CMSD actively participates in the International Organization of Securities Commissions' ("IOSCO") Multilateral Memorandum of Understanding ("IOSCO MMoU"), which CBB is a signatory of, by contributing in all incoming and outgoing requests including surveys. Such international cooperation enables the CBB to better protect investors, promote investor confidence, maintain fair, efficient, and transparent markets and address systemic risks; by utilizing information exchange to cooperate in developing, implementing, and promoting adherence to internationally recognized and consistent standards of regulation, oversight, and enforcement.

Beyond this, during 2022, the CBB's CMSD endeavored to develop and complete the capital markets regulatory and legal frameworks, including Volume 6 of 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 during 2022:

7.6.1 Policy and Regulatory Developments

- **Amendments to CBB's Resolution No. (27) of 2012, and its amendment, with respect to the Review of Penalties and Administrative Measures the CBB may impose upon Licensees, Members of their Board of Directors and their Executive Management:** This Resolution pertains to the establishment of the Enforcement Decision Review Committee ("EDRC") for the purpose of taking enforcement decisions of material significance, on behalf of the CBB. The amendments have been issued on 17th March 2022 to include that the scope of the EDRC within the Resolution to be extended to account for enforcement decisions imposed upon listed companies in order to streamline the enforcement escalation process as a whole, seeing as the previous structure only covers the review of enforcement decisions related to licensees and their approved persons (inclusive of their board members and executive management).
- **Amendments to the Takeovers, Mergers and Acquisitions ("TMA") Module of Volume 6 of the CBB Rulebook**: The CBB issued a circular (Ref. OG/34/2022) dated 19 January 2022 addressed to all listed companies in relation to the amendments to the Takeovers, Mergers and Acquisitions (TMA) Module, Volume 6 of the CBB Rulebook. Such amendments are in relation to the

compulsory acquisition in accordance with the amendments to the Commercial Companies Law by Decree Law No. (28) of 2020 amending some provisions of the Commercial Companies Law promulgated by Decree Law No. (21) of 2001

- **The Anti-Money Laundering and Combating Financial Crime ("AML") Module of Volume 6 of the CBB Rulebook:** The AML Module has been amended in January 2022 to include updates pertaining to customer due diligence requirements, digital on-boarding, and risk-based approach, amongst other areas.
- **The Markets and Exchanges ("MAE") Module of Volume 6 of the CBB Rulebook**: Amendments have been issued to the MAE Module in April 2022 to reflect the shift in equity crowdfunding operators' requirements following the issuance the Crowdfunding Platform Operators (CPO) Module under Volume 5 of the CBB Rulebook.
- **Crypto-Asset ("CRA") Module of Volume 6 of the CBB Rulebook:** The CRA Module has been issued for consultation in August 2022 with amendments made to strengthen the regulatory framework in line with developments in the sector and international best practices, including the introduction of requirements relating to digital token offerings and amendments to crypto-asset listing requirements.

7.6.2 The Capital Markets Supervision Directorate's Upcoming Initiatives

- **Updates and Amendments to the Dispute Resolution, Arbitration & Disciplinary Proceedings Module:** Following the March 2020 revision of the DRA Module, the CMSD has currently proposed additional amendments mainly in relation to the structure and functioning of an SRO's Arbitration Committee, to ensure that regulatory responsibilities are discharged in an effective manner and in line with international best practices.
- **Offering of Securities ("OFS") Module Updates and Amendments:** The CMSD is currently drafting updates and amendments to the OFS Module of Volume 6 of CBB Rulebook, to be in line with international best practice regarding the offering and issuing of securities in and from the Kingdom of Bahrain. As a result of the witnessed growth and development in several capital market products including the wide range of Structured Products, the CMSD is currently studying the international best practices regarding appropriate regulatory tools concerning the behavior of issuers and intermediaries within the capital market and the extent of the regulator's involvement in pre-approving the products and setting products standards and disclosure requirements, in addition to the significant ramifications associated with offering and marketing the products.
- **Treasury Shares Resolution:** Further to Article (93) of the CBB 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.
- **Takeovers, Mergers and Acquisition Resolution:** Further to Article (93 bis) of CBB Law Amendment No. (14) of 2020, the CMSD is currently in the process of introducing a resolution to regulate the process and procedures of mergers and acquisitions of listed companies.
- **Securities Resolution:** Further to Article (83 (a)) of the CBB Law, the CMSD is currently in the process of introducing a resolution to specify the types of securities that may be issued, the methods of offering and dealing with them and the obligations of each issuing party.
- **Prohibition of Market Abuse and Manipulation ("MAM") Module Updates and Amendments:** The CMSD is currently reviewing suggested updates and amendments to the MAM Module of Volume 6 of CBB Rulebook, generally to be in line with international best practices in various areas of investigation and enforcement.
- **Women empowerment:** The CMSD is cooperating with the Supreme Council for Women (SCW) and the Ministry of Industry & Commerce (MOIC) to enhance governance standards in capital markets by proposing amendments to the High-Level Controls Module (HC Module) of the CBB Rulebook Volume 6, entailing requirements in relation to women's representation in the board of directors (BoD) of listed companies. Current proposals involve having no less than 5 BoD members from both genders and obligating companies to disclose the gender composition of its BoD in the annual governance report.

7.6.3 Investor Protection Initiatives

- The Capital Market Authorities in the GCC formed the investor awareness program 'Mulim', which was launched as long-term Gulf program to raise Capital Market awareness. The program commenced in February 2022 and aims to raise awareness of the culture of financial transactions and investment in the capital markets, through a number of awareness programs and events. One of the initiatives of the program was the Gulf investor week in March 2022, in which members of CMSD's Research and Investor Protection Department ("RIP") participated in during the event held in Expo 2020. Another initiative is the GCC Smart Investor Award, which opens the door for participation to citizens and residents of the GCC countries in order to establish creative ideas related to the culture of financial and investment transactions. There are three lanes to the award, with the categories being videography, drawing and photography. Members of the CMSD's RIP Department also contributed by multiple TV and newspaper interview to help promote the award.

PART IV:

DEVELOPMENTS IN PAYMENT SYSTEMS, FINTECH, AND CYBER SECURITY

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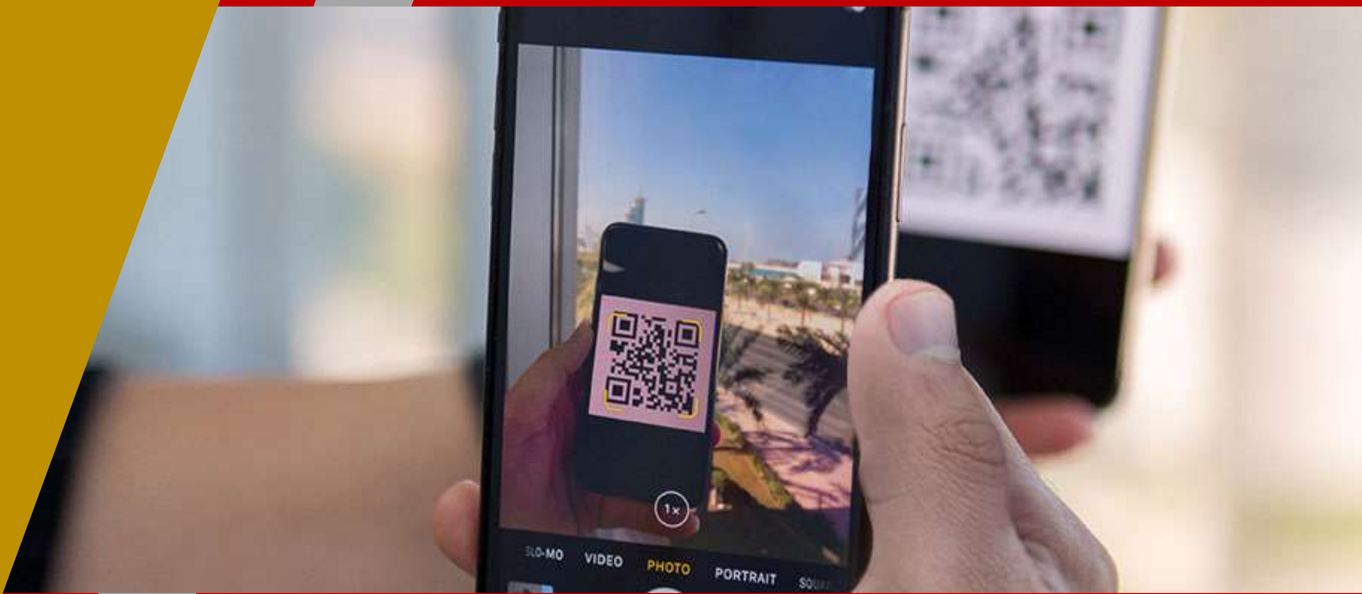


8 FINANCIAL MARKET INFRASTRUCTURES, PAYMENT AND SETTELEMENT SYSTEMS, POINT OF SALE, AND DIGITAL PAYMENTS

HIGHLIGHTS

RTGS Daily Average		SSSS Aggregate		ATM Daily Average	
175 Volume	BD 338.9 mn Value	45 Volume	BD 2.82 bn Value	42,305 Volume	BD 4.3 mn Value
BCTS Daily Average		**Fawri + Daily Average**		**Fawri Daily Average**	
8,524 Volume	BD 30.0 mn Value	608,427 Volume	BD 16.4 mn Value	43,086 Volume	BD 71.8 mn Value
Fawateer		**POS Transactions**			
45,448 Volume	BD 3.5 mn Value	77.9 mn Volume	BD 1.9 bn Value		

- Daily average (volume and value) of bank transfers increased in H1 2022 compared to H2 2021 while decreasing for ATM Transactions. Daily average volume and value of cheques decreased over same period.
- Daily average of volume and value of Fawri+ transactions increased by 31.33% and 21.01% respectively in H1 2022 compared to H2 2021. Daily average of volume and value of Fawri Transactions increased by 4.75% and 9.28% in H1 2022 compared to H1 2021.
- Daily average of volume and value of Fawateer Transactions increased by 66.47% and 71.64% respectively in H1 2022 compared to H1 2021.
- POS Transactions volume and value increased by 45.6% and 37.5% respectively in H1 2022 compared to H1 2021.

8.1 Overview

Financial Market Infrastructures (FMIs), Payment and Settlement Systems are central to the smooth operations of the financial sector and the efficient functioning of the overall economy. Therefore, the Oversight of FMIs and Payments improve the stability of Payments, markets and the wider financial system in addition to providing a valuable measure to evaluate risks to financial stability. FMIs, Payment and Settlement Systems are a crucial part of the financial infrastructure in the country.

The current FMIs 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. CBB operates, manages and oversees the national Payment and Settlement Systems in the Kingdom of Bahrain[10]. In addition, CBB assess the all FMIs, Payment and Settlement Systems in terms of compliance with the requirements set by the Principles for Financial Market Infrastructures (PFMI), CBB Law, CBB's

[10] CBB operates the Real Time Gross Settlement System (RTGS) and the Scripless Securities Settlement System (SSSS), whereas BENEFIT operates the ATM Clearing System (ATM), the Bahrain Cheque Truncation System (BCTS) and the Electronic Fund Transfer System (EFTS) including the Electronic Bill Presentment and Payment (EBPP) System on behalf of CBB.

Directives, etc. Bahrain's position in the financial services sector has enabled 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, along with CBB as a Regulator, innovative human capital, and an advanced ICT infrastructure.

The FMIs, Payment and Settlement Systems Framework continues to operate smoothly and function safely, efficiently, resiliently and reliably, assuring to maintain the financial stability during the first half of 2022 (from 1st January, 2022 to 30th June, 2022).

Point of Sale (POS) terminals and digital payments are other methods that enhance a customer's shopping experience by acknowledging their spending habits and preferences, in line with the Bank's efforts to remain closer to the needs of its customers. The POS System in Bahrain provides payment solutions that support international and domestic payment schemes and FinTech payment options such as contactless cards.

Several Digital Wallets were established in Bahrain's FinTech ecosystem that offer various payment solutions that come with value-added benefits such as acceptance of all major card schemes, easy payments to be made digitally without the use of cash or cards. While cash and card payments are still seen as dominant payment method, seamless contactless and digital payments transactions are projected to be the prominent payment methods in the future.

This chapter describes recent trends in the FMIs, Payment and Settlement Systems, POS, and digital wallet transactions.

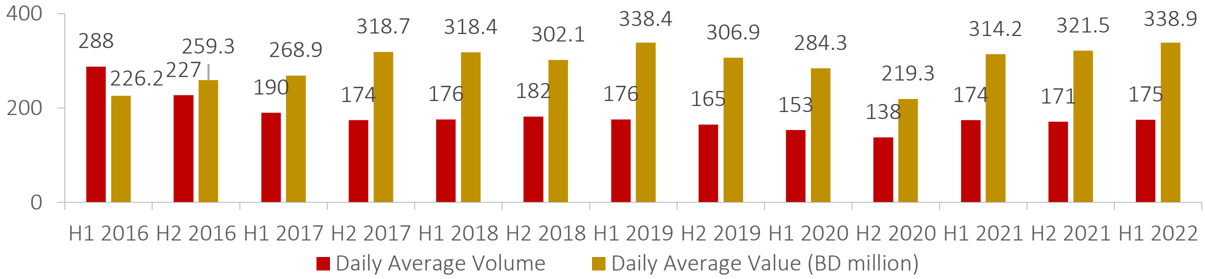
8.2 Real Time Gross Settlement System (RTGS)

CBB operates and oversees the 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 thirty-one (31) Participants including CBB. On Tuesday, 8th March, 2022, Central Bank of Kuwait (CBK) joined the RTGS System.

Chart 8.1: RTGS Bank Transfers Daily Average Volume and Value



Source: CBB.

The daily average volume of Bank Transfers for H1 2022 (first half of 2022) increased slightly by 2.34% to 175 Transfers compared to 171 Transfers for H2 2021 (second half of 2021).[11] Furthermore, the daily average volume of Bank Transfers for H1 2022 has increased by 0.57% from 174 to 175 Transfers when compared to H1 2021.

[11] H1 data is from 1st January until 30th June; H2 data is from 1st July to 31st December.

The value of those transfers has increased in H1 2022 by 5.41% when compared to H2 2021 from BD 321.5 million to BD 338.9 million. In addition, the daily average value of Bank Transfers for H1 2022 had increased by 7.86% from BD 314.2 million to BD 338.9 million when compared H1 2021.

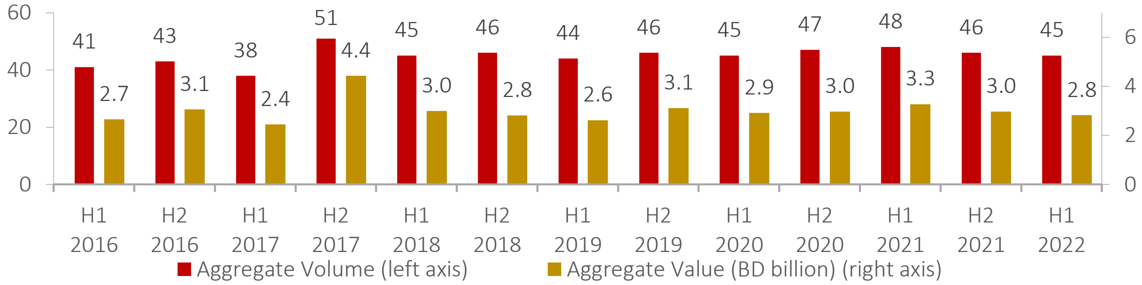
8.3 Scripless Securities Settlement System (SSSS)

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 June, 2007 along with the RTGS System. The number of direct participants is twenty-nine (29) participants where the indirect participants are thirty (30) members in the SSSS.

The volume of issues H1 2022 decreased slightly compared to H2 2021 by 2.17% from 46 issues to 45 issues. Moreover, the volume of issues also decreased in H1 2022 compared H1 2021 by 6.25% from 48 issues to 45 issues.

The aggregate value of issues in H1 2022 had a modest decrease by 6.67% to BD 2.8 billion from BD 3.0 billion in H2 2021 and comparing to H1 2021 value decreased by 15.15% from BD 3.3 billion.

Chart 8.2: SSSS Aggregate Volume and Value [12]



Source: CBB.

The volume of issues was within the normal range of issues which did not pose additional burden 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 during the period from 1st January 2022 to 30th June 2022.

8.4 ATM Clearing System (ATM)

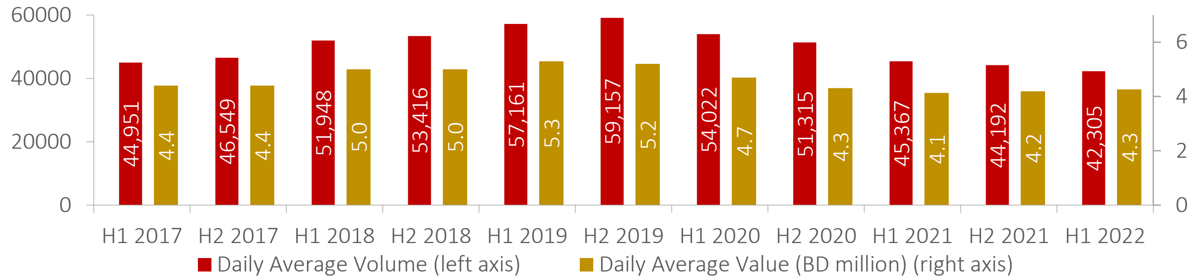
ATM clearing is based on a Deferred Net Settlement (DNS) system. The Benefit Company (BENEFIT) in Bahrain receives and processes all the ATM transactions. The GCC net, a leased line network across the GCC countries, provides for the communication backbone for the transmission of all the ATM Transactions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

The daily average volume of ATM Transactions for H1 2022 decreased by 4.3% to 42,305 per day compared to 44,192 transactions per day for H2 2021. In addition, the daily average volume of ATM transaction decreased by 6.7% in H1 2022 compared to H1 2021 (45,367 transactions per day).

The daily average value of ATM Transactions for the H1 2022 increased by 1.7% to reach BD 4.3 million when compared to the BD 4.2 million in H2 2021 and increased by 3.2% when compared H1 2021 (BD 4.1 million).

[12] Revised Figures as per the latest Report received from the Banking Services Directorate (BKS).

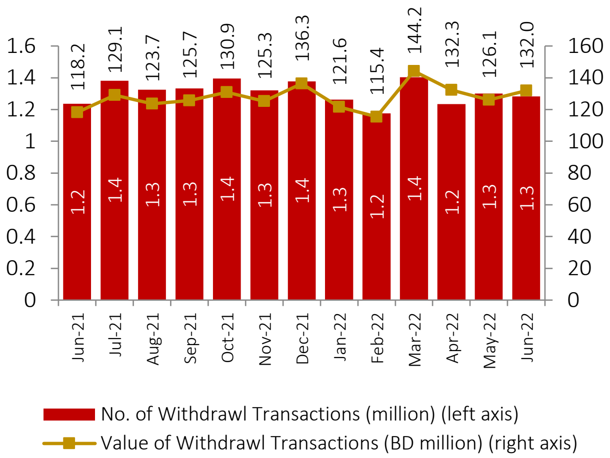
Chart 8.3: ATM Transactions Daily Average and Volume



Source: BENEFIT.

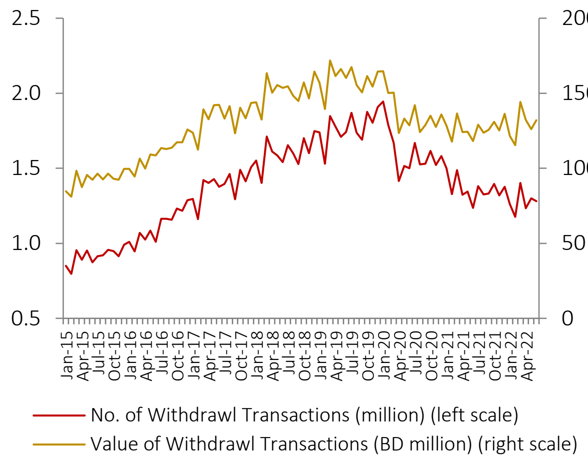
Overall, there was a downward trend in both the value and the volume of ATM transactions compared to 2020 (Chart 8.5). In H1 2022, monthly volume of ATM transactions ranged between 1.2 and 1.4 million transactions while the value of ATM transactions ranged between BD 115.4 million and BD 144.2 million.

Chart 8.4: Number and Value of ATM Transactions, June 2021 – June 2022



Source: BENEFIT.

Chart 8.5: Number and Value of ATM Transactions



Source: BENEFIT.

8.5 Bahrain Cheque Truncation System (BCTS)

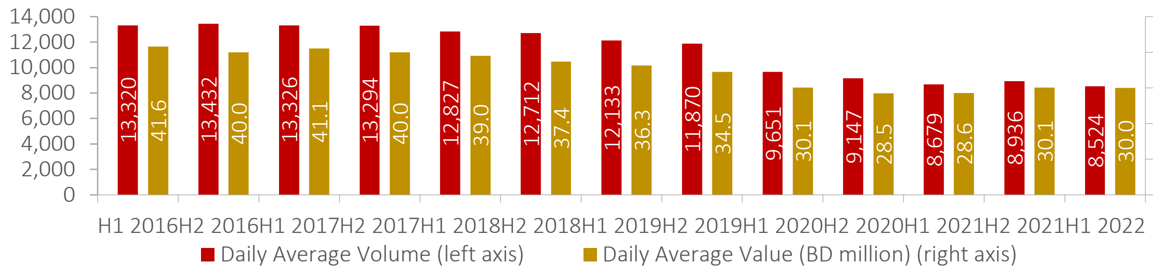
Cheques is one of the most popular instruments in use among Retail and Corporate Customers. As part of CBB vision to replace the paper based Automated Cheque Clearing System operated by CBB, the Bahrain Cheque Truncation System (BCTS) commenced its operations in co-operation with the BENEFIT Company (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.

The number of participants in the BCTS are thirty (30) participants. The daily average volume of cheques for H1 2022 decreased by 4.61% when compared to the H2 2021 from 8,936 cheques to 8,524 cheques. However, the daily average volume of cheques in H1 2022 decreased by 1.79% from 8,679 cheques in H1 2021.

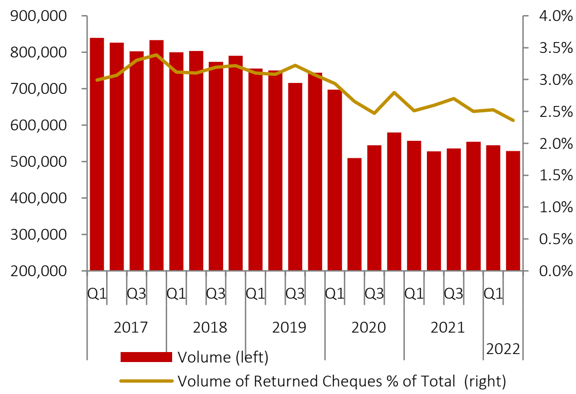
Furthermore, the daily average value of cheques decreased slightly in the first half of 2022 by 0.33% when compared to the second half of 2021 from BD 30.1 million to BD 30.0 million. In addition, the daily average value of cheques for the first half of 2022 increased by 4.90% from BD 28.6 million for the first half of 2021 to BD 30.0 million.

Chart 8.6: BCTS Daily Average Volume and Value



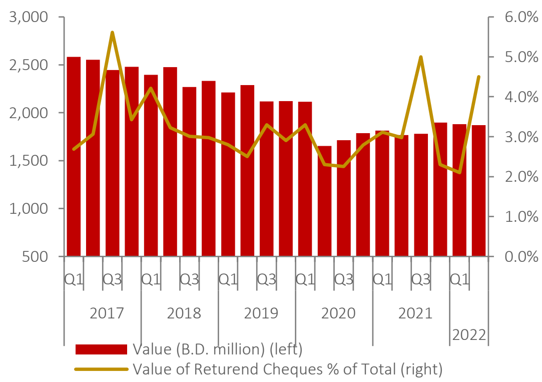
The BCTS continued to operate smoothly and efficiently for the period from 1st January 2022 to 30th June 2022. Charts 8.7 and 8.8 show the volume and value of cheques and the percentage returned cheques to the total volume and value. Between Q3 2021 and Q2 2022, returned cheques ranged between 2.4% to 2.7% as a percentage of total volume and 2.1% to 5.0% as a percentage of total value.

Chart 8.7: Volume of Issued Cheques and % of Returned Cheques



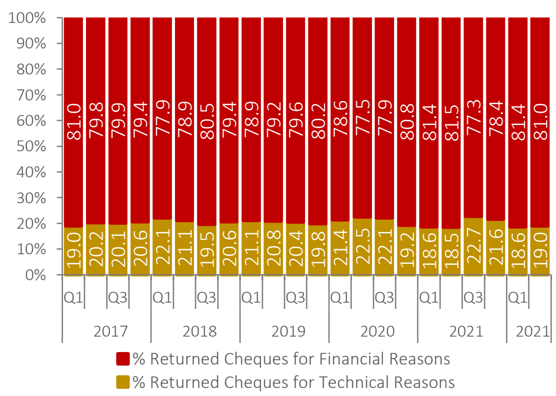
Source: BENEFIT.

Chart 8.8: Value of Issued Cheques and % of Returned Cheques (BD million)



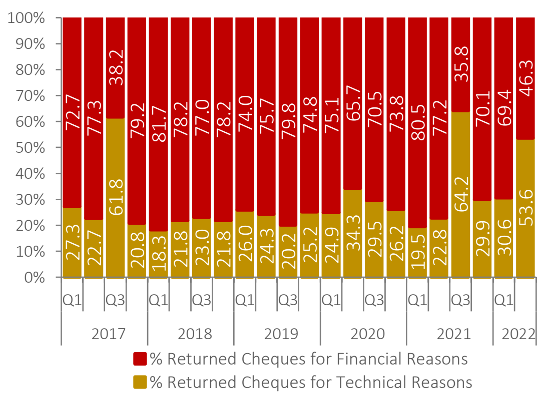
Source: BENEFIT.

Chart 8.9: Returned Cheques by Volume (% of Technical vs. Financial)



Source: BENEFIT.

Chart 8.10: Returned Cheques by Value (% of Technical vs. Financial)



Source: BENEFIT.

The majority of the cheques returned in terms of volume are returned due to financial reasons reaching 81.4% in Q1, 2022 and 81.0% of the total volume of cheques in Q2, 2022, where in terms on the value of returned cheques, financial reasons consumed majority of cheques returned in both quarters Q1 and Q2, 2022 with 70.1% and 69.4% respectively. (Charts 8.9 and 8.10).

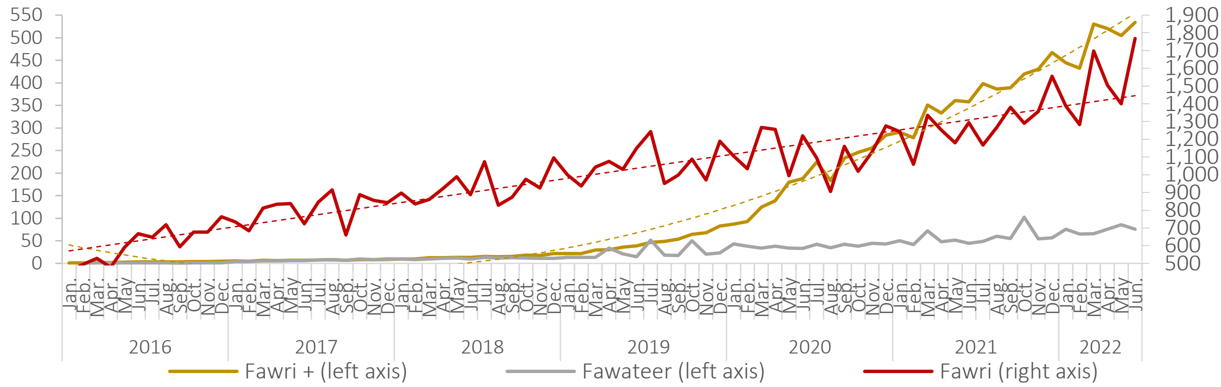
8.6 Electronic Fund Transfer System (EFTS) including Electronic Bill Presentment and Payment (EBPP) System

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 utilized. Therefore, the Electronic Fund Transfer System (EFTS) was launched on the 5th November 2015, whereas Electronic Bill Presentment and Payment (EBPP) System was launched on the 3rd October 2016, operated by the Benefit Company (BENEFIT) and overseen by 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 services: Fawri+ Fawri, and Fawateer. Fawri+ and Fawri provide fund transfers service to individuals and corporates, where Fawateer provides real-time bill payments offering the public easier access, faster processes and virtually no errors. The number of participants offering outward EFTS Services has reached twenty-six (26) participants.

Chart 8.11 shows an overall increasing trend in the monthly transfers in Fawri+, Fawri and Fawateer. The value of Fawri+ transfers increased by 19.04% from BD 2,491.1 million for H2 2021 to BD 2,965.3 million for H1 2022. The total value of Fawri transfers for H1 2022, increased by 12.77% from BD 8,017.05 million for H2 2021 to BD 9,041.41 million for H1 2022.

Chart 8.11: EFTS Fawri, Fawri+, and Fawateer Value (BD million)



Source: BENEFIT.

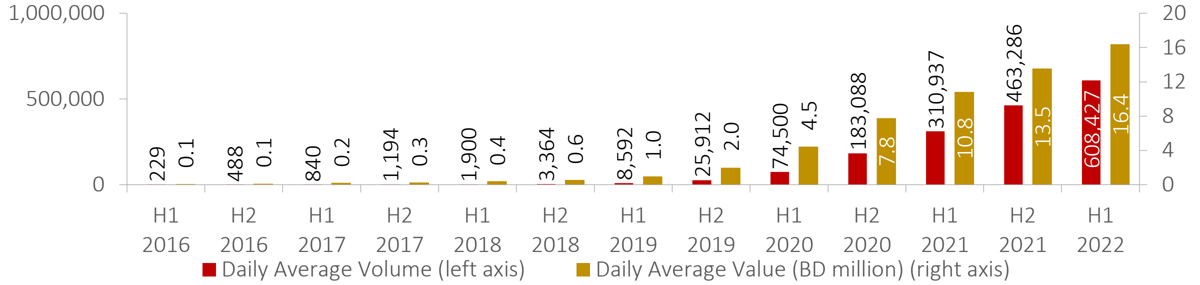
In addition, the value of Fawateer payments increased by 17.52% from BD 377.3 million in H2 2021 to BD 443.4 million in H1 2022. The Fawri+ transfers in addition to Fawateer payments in all electronic channels including internet banking, mobile banking and BenefitPay surged during 2020 and 2021 is due to the increasing popularity and convenience in going cashless during the COVID-19 pandemic.

The daily average volume of Fawri+ transfers for H1 2022 increased significantly by 31.33% when compared to H2 2021 from 463,286 transfers to 608,427 transfers. Furthermore, the daily average volume of Fawri+ transfers for H1 2022 increased by 95.68% from 310,937 transfers in H1 2021. The daily average value of Fawri+ transfers increased by 21.01% from BD 13,538,383.544 in H2 2021 to BD 16,382,622.259 in H1 2022. The daily average value also increased by 51.24% in H1 2022 when compared to the from BD 10,832,196.670 in H1 2021.

The daily average volume of Fawri transfers in H1 2022 increased by 4.75% when compared H2 2021 from 41,132 transfers to 43,086 transfers. Moreover, the daily average volume of Fawri transfers in H1

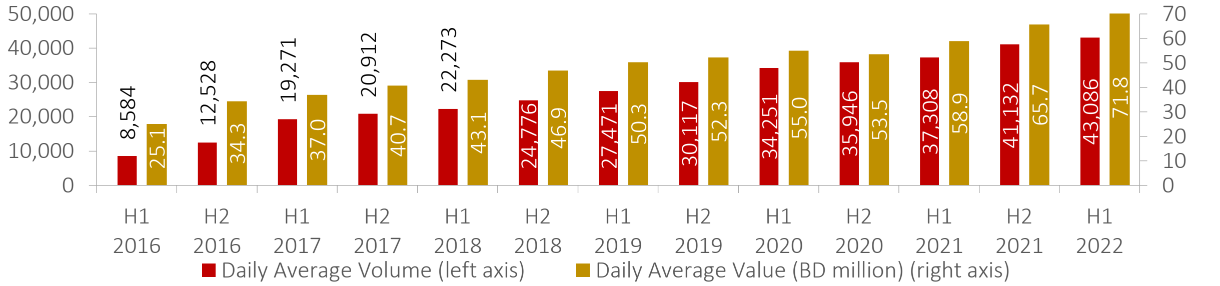
2022 increased by 15.49% from the 37,308 transfers in H1 2021. In addition, the daily average value of Fawri transfers increased by 9.28% from BD 65.7 million in H2 2021 to BD 71.8 million in H1 2022. Furthermore, the daily average value of Fawri transfers increased by 21.90% from BD 58.9 million in H1 2021.

Chart 8.12: EFTS Fawri+ Daily Average Volume and Value



Source: BENEFIT.

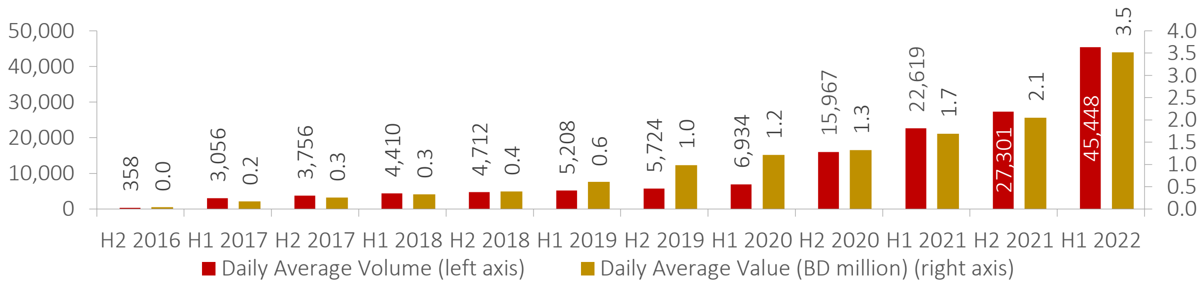
Chart 8.13: EFTS Fawri Daily Average Volume and Value



Source: BENEFIT.

The daily average volume of Fawateer Payments for the first half of 2022 increased significantly by 66.47% when compared to H2 2021 from 27,301 payments to 45,448 payments and increased by 100.93% from the 22,619 payments in H1 2021. In addition, the daily average value of Fawateer reached BD 3,519,374.361 in H1 2022 increasing by 71.64 % when compared to H2 2021 (BD 2,050,391.525) and by 107.85 % compared to H1 2021 (BD 1,693,214.598).

Chart 8.14: EBPP Fawateer Daily Average Volume and Value



Source: BENEFIT.

The EFTS including EBPP continued to operate in a safe, efficient, resilient and reliable manner from 1st January 2022 to 30th June 2022. CBB continues to assess the EFTS including EBPP in terms of compliance with the requirements set by the Principles for Financial Market Infrastructures (PFMI), CBB Law and CBB's Directives, etc.

8.7 Point of Sale (POS) and E-Commerce

The increase in POS terminals and their utilities, combined with mobile POS helps in achieving higher financial inclusion. POS Transactions in Bahrain have shown a steady increase in both in volume and value, an indicator of strong business and economic activity within the Kingdom.

The total number of transactions for H1 2022 reached 77.9 million (a 45.6% increase compared to 2021). Similarly, the total value of transactions for H1 2022 increased to BD 1,879.6 million (a 37.5%

increase compared to H1 2021). Both the volume and value of cards issues in Bahrain has increased in H1 2022 by 28.4% and 22.3% respectively when compared H1 2021. The volume and value of transactions by cards issued outside Bahrain showed a significant increase in H1 2022 compared to H1 2021 increasing by 297.0% and 206.3% respectively indicating a recovery as a result of the removal of travel restrictions due to COVID-19 pandemic.

Table 8.1: Point of Sale (POS) and E-Commerce Transactions in Bahrain

		Volume of transactions (million)			Value of transactions (BD million)		
		Cards issued in Bahrain	Cards issued outside Bahrain	Total	Cards issued in Bahrain	Cards issued outside Bahrain	Total
2018		49.0	15.4	**64.5**	1,524.1	453.2	**1,977.2**
2019		58.4	15.2	**73.7**	1,877.2	557.2	**2,434.4**
2020		77.3	6.4	**83.8**	2,124.9	217.0	**2,341.9**
2021		109.5	16.0	**125.5**	2,707.2	444.0	**3,151.2**
2020	Q1	17.2	3.4	**20.6**	502.3	111.8	**614.1**
	Q2	15.9	0.8	**16.6**	447.3	25.0	**472.3**
	Q3	20.5	0.9	**21.4**	554.9	33.2	**588.1**
	Q4	23.8	1.4	**25.1**	620.5	46.9	**667.4**
2021	Q1	25.2	1.6	**26.8**	639.4	53.6	**693.0**
	Q2	24.9	1.8	**26.7**	615.3	59.0	**674.3**
	Q3	29.1	4.9	**34.0**	698.4	138.4	**836.9**
	Q4	30.4	7.7	**38.0**	754.1	193.0	**947.0**
2022	Q1	31.2	6.7	**37.9**	734.8	169.3	**904.2**
	Q2	33.1	6.9	**40.0**	800.0	175.5	**975.4**

Source: CBB.

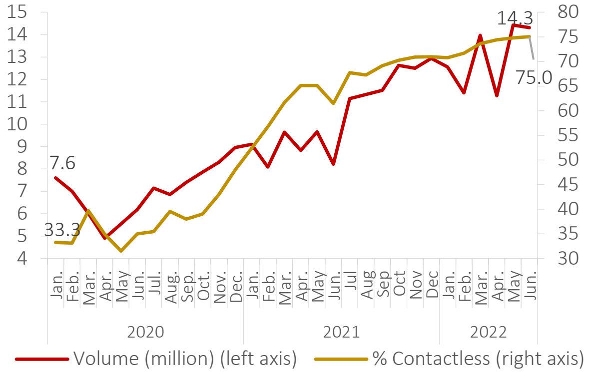
As of Q2 2022, the total number of transactions performed using POS machines in Bahrain was 40.0 million which is a 49.8% YoY increase from Q2 2021, and 5.4% increase from Q1 2022. As for the total value of transactions, the total value of transactions performed using POS machines in Bahrain in Q2 2022 was BD 975.4 million which is a 44.7% YoY increase from Q2 2021, and 16.7% increase from Q1 2022. The increase in spending in volume and value of POS transactions reflects the increase in consumer spending compared to the first two quarters of 2021 where there was still an impact of the COVID-19 pandemic on consumer spending.

Chart 8.15 shows the monthly of POS Transactions in terms of volume and value which can help identify any cyclicality in behavior over the long run. The continued increase in POS transactions in the first half of 2022 compared to the first half of 2021 and second half of 2021 shows the continued trend of people preferring to make direct payments to merchants through POS terminals instead of ATM/Cash withdrawals.

The COVID-19 health crisis impacted the nature of POS transactions shifting consumers towards contactless payments. As part of CBB's precautionary efforts to contain COVID-19, CBB increased the limit on contactless transactions without PIN transaction to BD 50 in March 2020. In September 2020 CBB requested that necessary measures are taken to finalize the issuance and distribution of contactless debit, credit, and prepaid and charge cards to customers by the end of 2020 at no charge to the customers.

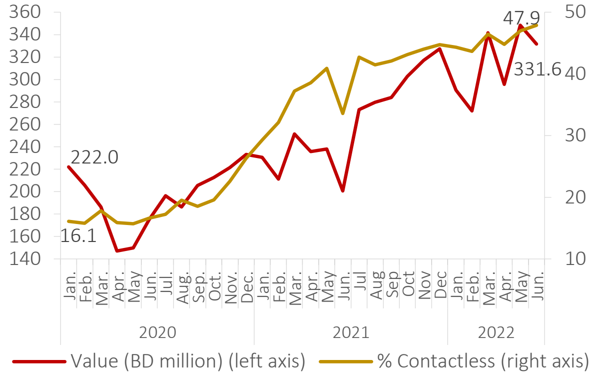
Contactless adoption has accelerated in the Kingdom and will continue to grow due to the change in consumer spending habits. Charts 8.15 and 8.16 show the increasing trend in using contactless cards. The percentage of contactless transactions in terms of volume increased from 33.3% in January 2020 to 75.0% in June 2022. Similarly, in terms of value, the percentage of contactless transactions increased from 16.1% in January 2020 to 47.9% in June 2022.

Chart 8.15: Volume of Monthly POS and E-Commerce Transactions (millions)



Source: CBB.

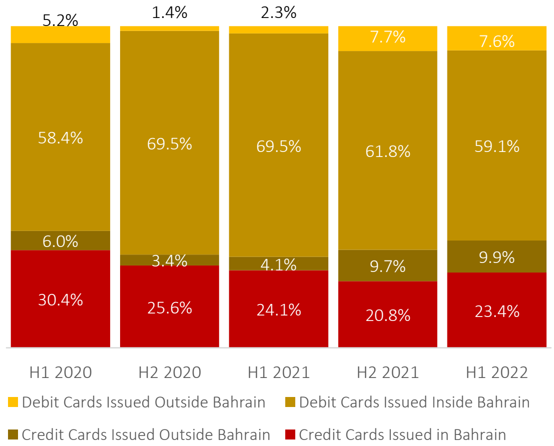
Chart 8.16: Value of Monthly POS and E-Commerce Transactions (BD million)



Source: CBB.

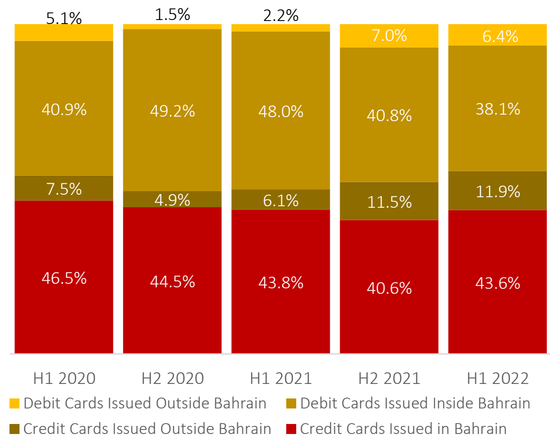
As H1 2022, 82.5% of the volume of transactions and 81.7% of the value of transactions came from cards issued inside Bahrain (Chart 8.17 and Chart 8.18). The increase in share of cards issued outside Bahrain which is noticeable from H2 2021 is due to increase in number of foreigners visiting Bahrain as restrictions are easing for vaccinated travelers and travel restrictions placed during the COVID-19 pandemic were gradually lifted. The share of cards issued outside Bahrain saw an increase starting Q3 2021.

Chart 8.17: Volume of POS and E-Commerce Transactions (% by Card Type)



Source: CBB.

Chart 8.18: Value of POS and E-Commerce Transactions (% by Card Type)



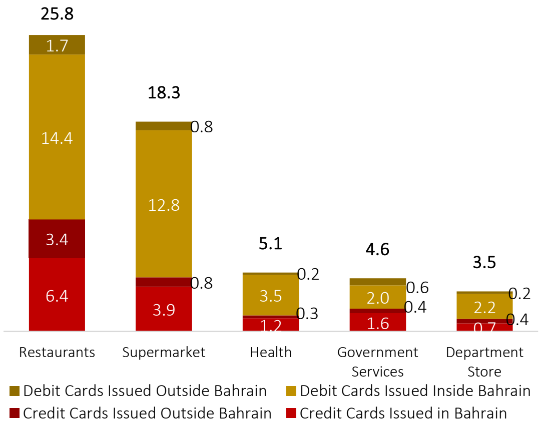
Source: CBB.

For H1 2022, most of the volume and of transactions were from debit cards (representing 66.7%) while most of the value of transactions were from credit cards (representing 55.5%). The share of transactions by credit cards increased H2 2021 due to an increase in the share of credit cards issued outside Bahrain.

Charts 8.19 and 8.20 show the top 5 sectors in terms of volume and value of transactions for H1 2022. In terms of volume the top 5 sectors represented 73.6% of all the transactions for 2021 and were: restaurants (25.8 million), supermarkets (18.3 million), health (5.1 million), government services (4.6 million), and department stores (3.5 million). The majority of the number of transactions for the restaurants, supermarket, health, government services, and department stores were done using debit cards issued inside Bahrain making 55.6%, 70.1%, 68.9%, 44.3%, and 62.3% of the transactions respectively.

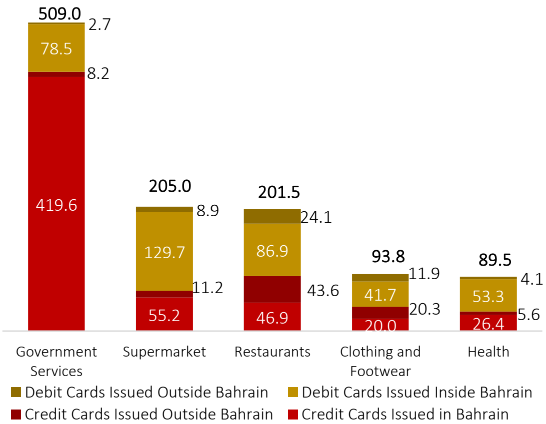
In terms of value, the top 5 sectors represented 58.5% of all transactions and were: government services (BD 509.0 million), supermarkets (BD 205.0 million), restaurants (BD 201.5 million), clothing and footwear (BD 93.8 million), and health (BD 89.5 million). For government services, 82.4% of the value of transactions were made by credit cards issued inside Bahrain. As for supermarkets, restaurants, clothing and footwear, and health 63.2%, 43.1%, 44.5% and 59.6% of the value of transactions respectively were made by debit cards issued inside Bahrain.

Chart 8.19: Top 5 Sectors by Volume of POS and E-Commerce – H1 2022 (million)



Source: CBB.

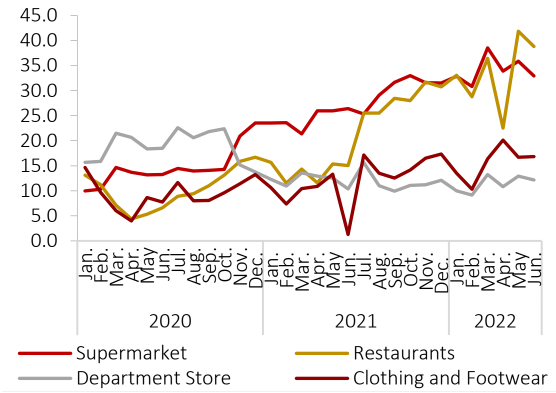
Chart 8.20: Top 5 Sectors by Value of POS and E-Commerce – H1 2022 (BD million)



Source: CBB.

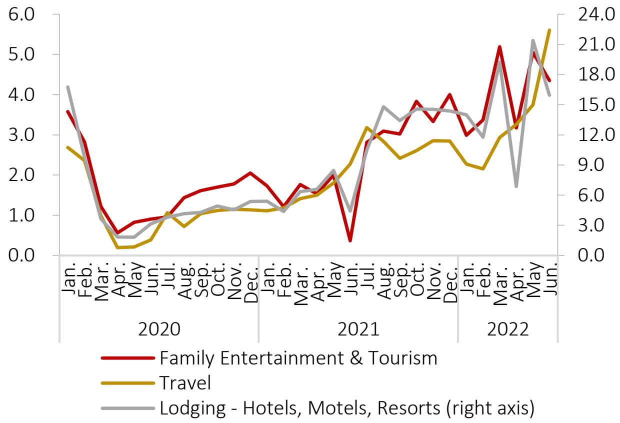
Charts 8.21 and 8.22 shows the monthly value of POS transactions for from January 2020 to June 2022 in selected sectors that have witnessed a change in consumer during the pandemic.

Chart 8.21: Monthly Value of POS and E-Commerce of Selected Indicators (BD million)



Source: CBB.

Chart 8.22: Monthly Value of POS and E-Commerce of Selected Indicators (BD million)

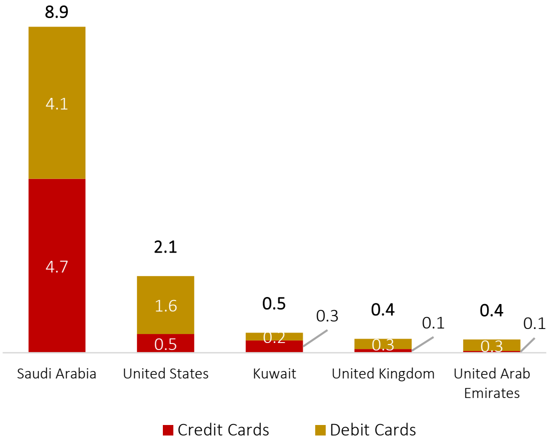


Source: CBB.

Charts 8.23 and 8.24 show the top 5 countries in terms of volume and value of foreign transactions for H1 2022. In terms of volume the top 5 countries represented 89.9% of total foreign transactions and were: Saudi Arabia (8.9 million), United States (2.1 million), Kuwait (0.5 million), United Kingdom (0.4 million), and United Arab Emirates (0.4 million).

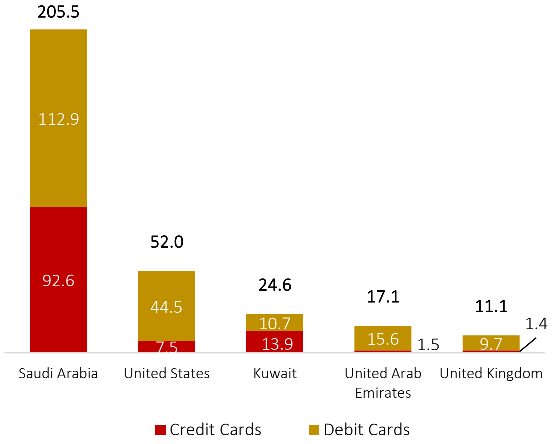
In terms of value, the top 5 countries represented 90.0% of the total value of foreign transaction and were: Saudi Arabia (BD 205.5 million), United States (BD 52.0 million), Kuwait (BD 24.6 million), United Arab Emirates (BD 17.1 million), and United Kingdom (BD 11.1 million).

Chart 8.23: Top 5 Nationalities by Volume of POS and E-Commerce – H1 2022 (million)



Source: CBB.

Chart 8.24: Top 5 Sectors by Value of POS and E-Commerce – H1 2022 (BD million)



Source: CBB.

9 FINTECH, INNOVATION AND FINANCIAL INCLUSION

HIGHLIGHTS

Regulatory Sandbox	Bank Branches	ATMS
18	204	515
ATM Cards	**Debit Cards**	**Credit Cards**
1,664.1 thousand	1,210.3 thousand	306.6 thousand

- 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 making recommendations on the necessary regulatory reforms to encourage innovation within the financial services sector via the use of FinTech solutions, supervising and overseeing the progress of companies participating in the Regulatory Sandbox and monitoring technical and regulatory developments within the FinTech field.
- Continued FinTech developments within the Kingdom in Open Banking, e-KYC, and contactless payments.

9.1 Overview

Bahrain is repositioning itself to be a Financial Technology (FinTech) hub of the region combining conventional and Shariah 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 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. 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 pandemic has accelerated the trend toward digitalization of retail financial services. While comprehensive data on the market shares of FinTechs and other retail digital financial services are scarce, proxies suggest they have further expanded their footprint in financial services. The COVID-19 pandemic has accelerated the adoption of innovative financial services. While the ability of digital innovation to improve market access, the range of product offerings, and convenience has been acknowledged for some time, pandemic-related responses and containment measures increased the importance of these factors in 2020-21. COVID-19 hastened several trends already underway, including the use of digital payments and changes in the way retail customers and vendors buy and sell goods.

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 by CBB and other industry players in in this field within the Kingdom.

9.2 FinTech Developments

The CBB has developed its digital transformation strategy with a vision to develop projects that introduce latest electronic payment and settlement products and FinTech projects to gradually shift to digital systems and reduce the use of cash in financial transactions facilitating a more efficient provision of banking services to individuals. The digital transformation initiatives also focus on working with financial institutions to encourage and accelerate their transition with technological developments to ultimately benefit the national economy and be in line with international best practices.

As part of its digital transformation strategy, CBB announced a series of measures towards consolidating its position as a regional financial hub and facilitating a number of FinTech initiatives. The CBB has established a Fintech and Innovation Unit, launched a Regulatory Sandbox for financial technology startups and existing financial institutions, and provided licenses for digital banks.

The CBB announced the establishment of a dedicated FinTech & Innovation Unit in 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 FinTech Unit is responsible for 1) the approval process to participate in the Regulatory Sandbox 2) supervision of the activities and operations of the authorized Regulatory Sandbox companies' and 3) 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 4) collaborate with other regulators and policy makers to exchange ideas, share experiences and learnings.

9.2.1 Regulatory Sandbox

CBB launched a regulatory sandbox in June 2017 to attract both local and international emerging FinTech companies as well as existing CBB licensees to enable them to test their innovative ideas and expand their business in the region.[13] The sandbox provides authorized companies with the opportunity to test and experiment their innovative financial solutions freely until they are commercially viable. The period allowed for this arrangement is nine months and may be extended if needed. The Sandbox focuses on three criteria items that include:
This section sets out the main eligibility criteria for participation in the Sandbox, which include the following:

1. Innovation: The service must be truly innovative, addresses a market gap or is sufficiently different from existing offerings, or offers a new use for existing technologies within financial services (as evidenced by market research and a comparison of the key features of the Applicant's technology or operating methodology against competitors).
2. Customer benefit: The service must offer identifiable direct or indirect benefits to customers (for e.g. based on customer research showing improved security, customer experience, efficiency, quality of product, lower prices or a combination of any of the above). These must be supported by quantifiable estimations or demonstrations, where possible.

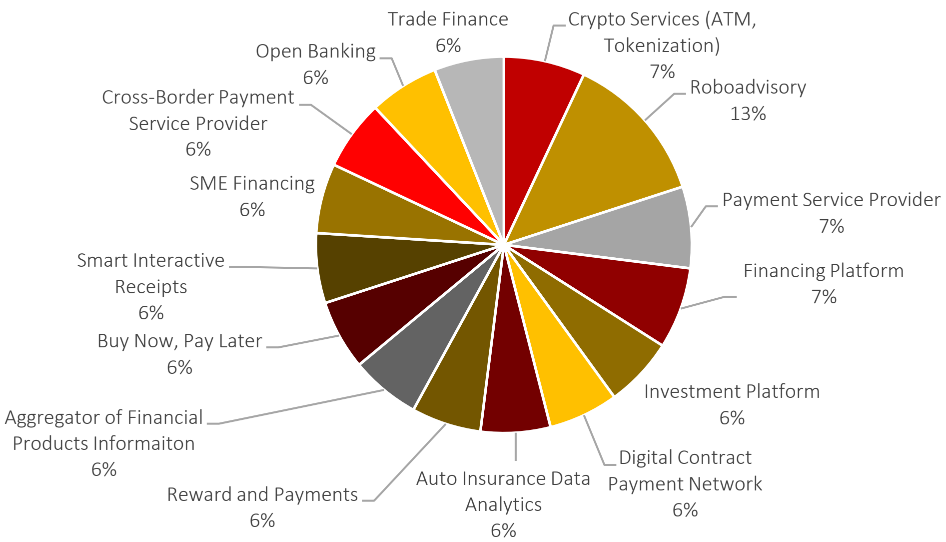
[13] A Regulatory Sandbox (Sandbox) is a framework and process that facilitates the development of the FinTech industry in a calculated way. It is defined as a safe space in which businesses can test innovative products, services, business models and delivery mechanisms without immediately incurring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

3. Identification of Major Risks: The Applicant must identify the major risks associated with the solution or service, as well as the measures to mitigate these, including business continuity and disaster recovery.
4. Compliance with CDD and AML/CFT Requirements: The Applicant must be able to comply with the Customer Due Diligence (CDD) and Anti-money Laundering/Combating the Financing of Terrorism (AML/CFT) Requirements set out in the CBB Rulebook.
5. Confidentiality Requirements: The Applicant must be able to maintain the confidentiality of customer information in accordance with the Central Bank of Bahrain and Financial Institutions Law No.64 of 2006, as amended ("CBB Law") and other applicable laws.

The Sandbox has gained significant interest from local, regional and global start-ups and a number of companies have successfully completed testing their solutions. As of June 30, 2022, CBB had 18 companies testing their solutions within the Regulatory Sandbox. The solutions being tested out in the sandbox range from digital financing solutions, crypto platforms, tokenization offerings, open-banking solutions, payment services providers, robo-advisory solutions, buy now pay later and many more.

As part of its efforts to further develop the FinTech ecosystem and enhance the competitiveness of the financial services sector, CBB announced its new Regulatory Sandbox Framework in December 2021 which will allow FinTech firms to test and experiment their ideas and solutions related to the sector in a more efficient and effective environment. The new Framework enhances the eligibility criteria for participation in the Regulatory Sandbox, as well as streamlines the entire Sandbox process to ensure a more phased and consistent approach to support testing. The revised framework serves as a continuation of the CBB's efforts to keep pace with technological developments to adopt modern banking services through FinTech solutions, promoting a culture of innovation in the financial sector and national economy.

Chart 9.1: Regulatory Sandbox Statistics- Company Types (%)



Source: CBB.

Table 9.1: Regulatory Sandbox Statistics- Classification by Region

Region	No. of Sandbox Companies
MENA	17
Americas	0
Europe	1
Asia	0
Africa	0

Source: CBB.

9.2.2 FinHub 973: CBB Digital Lab

In October 2020, CBB introduced FinHub 973, which aims to serve as a virtual FinTech platform for the MENA region. The platform has been launched with the help of the Economic Development Board, Bank ABC, ila Bank, BENEFIT, National Bank of Bahrain, and the Bahrain Islamic Bank.

FinHub 973 offers a virtual environment that includes an API for banking services, and it will also provide a way for Fintech firms to work cooperatively with new business partners. The platform also helps with create a collaborative environment for FinTechs based in the MENA region.

The goal is to connect FinTech entrepreneurs to financial institutions, consultants, tech companies, mentors and investors and develop an open innovation platform for the Kingdom of Bahrain to test and build products that solve real consumer problems.

In April 2021, CBB continued its collaboration with FinHub by announcing the launch of a series of nation-wide FinTech innovation challenges, named the 'Bahrain Supernova'. The challenges aimed at furthering the development of the FinTech industry in the Kingdom of Bahrain by presenting real market challenges faced by the financial institutions in the Kingdom, aiming to find customer-centric solutions using emerging technologies. The financial institutions along with the CBB announced several problem-statements, whereby start-ups and tech firms from Bahrain and the region were invited to submit their proposals via the FinHub973 digital platform.

In May 2022 the CBB launched the second edition of its FinTech challenges 'Bahrain Supernova 2022' which was hosted on FInHub973, in collaboration with Fintech Galaxy (our technical partner) and financial institutions. The challenges, which are aimed at furthering the development of the FinTech sector in the Kingdom of Bahrain, align with the CBB's digital strategy to boost collaboration and integration between financial institutions and startups utilizing open APIs. The Bahrain Supernova 2022 presented real market challenges related to financial services, aimed at finding customer-centric solutions revolving around Open Banking use cases.

9.2.3 Open Banking

In October 2020, CBB launched the Bahrain Open Banking Framework (BOBF) to ensure holistic implementation of Open Banking services by the industry. The framework includes detailed operational guidelines, cyber security standards and guidelines for adoption, customer experience guidelines, technical open Application Programming Interface (API) specifications and the overall governance framework needed to protect customer data. These standards follow the comprehensive rules on Open Banking which were previously issued in December 2018. The open banking regulations mandated the adoption of open banking by all retail banks in the Kingdom by 30 June 2019. With that, Bahrain became the first country in the Middle East to adopt open banking making access to financial information easier, faster, and tailored to the needs of customers.

Open Banking services entail the provision of two broad categories of services:

- The first is "account information service" which provides customers with access to all bank account information in an aggregated manner through a single platform.
- The second category is "payment initiation service" which allows licensed third parties to initiate payments on behalf of customers while allowing seamless transfers between different customer accounts through a mobile based application.

The OBF aims to improve the reach and quality of services offered by retail banks through digital online and mobile channels. The entrepreneurial and FinTech start-up ecosystem found in Bahrain, that encompasses accelerators, incubators, training programs and funding schemes, can play a major part in Open Banking that will foster foster competition and enhance efficiency of the financial system adapting to changing consumer trends.

Following the launch of the BOBF, CBB issued for consultation the amended CBB Rulebook Modules to be aligned to BOBF on 28th April 2021. CBB also issued a circular regarding the second phase of the OBF directing retail banks and financial institutions to implement the requirements for the second phase of the framework by 30 June 2022. The second phase of the framework includes guidelines and standards related to the following services:

- Sharing Open Data (publicly available data such as ATM locator, Branch Locator, etc.)
- Domestic Standing Orders
- International Standing Orders
- International Future Dated Payments
- Bulk/Batch Payment

9.2.4 The Arabian Gulf System for Financial Automated Quick Payment Transfer (AFAQ)

The Arabian Gulf System for financial Automated Quick Payment Transfer (AFAQ) is a Real Time Gross Settlement service for cross-currency cross-border payments between GCC countries. The system is operated by the Gulf payment Company (GPC) which is owned and funded by the GCC central Banks including the CBB. The AFAQ system allows its participants to transfer payments from one local currency to another local currency in real time within the business day schedule.

The AFAQ cross-currency service was launched on 10th December 2020 with the CBB and Saudi Central Bank (SAMA) as its first participants. The CBB is currently in the process of onboarding all Bahrain Banks into the system, representing the first batch, five banks were live on 19th April 2021 which are Ahli United Bank (AUB), Bahrain Islamic Bank (BISB), Bahrain and Kuwait Bank (BBK), Eskan Bank and National Bank of Bahrain (NBB). By the end of December 2021, the CBB has successfully managed to onboard a total of 9 banks, with a target of onboarding all Bahrain Banks during the Year 2022. With regards to the onboarding of other GCC Central Banks, the Central Bank of Kuwait has joined the system on 13th March 2022 whereas, other Central Banks onboarding is in progress.

9.3 Cyber Security Initiatives

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 recognized 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 has more than one role in addressing Cyber risk. Cyber Incidents are required to be reported to the CBB's Banking Supervision immediately upon such occurrence. The related rules are also being revised to seek details of remedial measures and action plans for addressing the weaknesses that led to the incident.

The CBB's Banking Supervision receives vulnerability and penetration testing reports from financial institutions on a regular basis. The Inspection Directorate conducts both on-site and off-site inspections on financial institutions information technology and cyber security infrastructure, recently multiple financial institutions have been inspected. Additionally, the Inspection Directorate covers the whole cybersecurity domains that ranges from physical security, security operation, risk assessment, governance, threat intelligence, user education, and framework and standards. The Economic Research Division at the FSD issued Cyber Risk Surveys to cover cyber risk relative to governance and leadership, identification, protection, detection, response and recovery.

The CBB continues to develop its regulations on cybersecurity in an effort to strengthen the cyber resilience of its financial institutions. The following developments can be highlighted:

1. The CBB introduced more stringent cyber incident reporting to the CBB in March 2022, by introducing a one-hour deadline to report a cyber incident by phone and a two-hour deadline to report essential details by email.
2. The CBB consulted the industry on the requirements related to email domains used to communicate with customers and URLs in messages sent to customers during May and June 2022. Subsequent to the consultation, amended requirements were issued in August 2022 enhancing the requirements and clarifying the exceptions.
3. While the CBB has issued cyber security requirements for banks, insurance licensees, investment business firms, money changers and ancillary service providers, the CBB is currently working on introducing cyber security requirements for other specialized licensees.

ANNEX:

FINANCIAL SOUNDESS INDICATORS AND SELECTED GRAPHS

ANNEX 1: SELECTED FINANCIAL SOUNDESS INDICATORS (FSIs)

Annex 1 Table 1: Selected Financial Soundness Indicators – All Banking System

Indicator	Q2 2021	Q4 2021	Q2 2022
Capital Adequacy			
CAR (%) *	18.7	18.7	19.1
Tier 1 CAR (%) *	17.5	17.2	17.7
Assets-to-Capital (Times) *	8.3	8.7	8.7
Asset Quality			
NPLs (% of Total Loans)	3.8	3.2	3.3
Specific Provisions (% of NPLs)	69.0	70.1	69.9
Loan Concentration (Share of Top Two Sectors) (%)	30.0	30.5	30.8
Real Estate/ Construction Exposure (%)	26.0	25.2	25.4
Earnings			
ROA (%)	0.6	1.1	0.6
ROE (%) *	3.9	7.8	4.6
Net Interest Income (% of Total Income) **	72.5	70.3	68.6
Net Fees & Commissions (% of Total Income) **	13.1	13.0	13.3
Operating Expenses (% of Total Income)	51.2	52.4	46.1
Liquidity			
Liquid Assets (% of Total Assets)	26.4	26.2	25.7
Loan-Deposit Ratio (%)	70.2	69.8	65.7

** Locally-Incorporated Banks only.*
***Conventional Banks only.*
Source: CBB.

Annex 1 Table 2: Selected Financial Soundness Indicators - Conventional Banks

Indicator	Conventional Retail			Conventional Wholesale		
	Q2 2021	Q4 2021	Q2 2022	Q2 2021	Q4 2021	Q2 2022
Capital Adequacy						
CAR (%) *	20.4	20.6	20.4	17.6	17.1	17.7
Tier 1 CAR (%) *	18.9	19.2	19.0	16.7	15.6	16.2
Assets-to-Capital (Times) *	7.0	6.9	7.3	8.3	9.0	9.5
NPLs Net Provisions to Capital (%) *	5.3	4.3	4.3	4.4	3.1	3.4
Asset Quality						
NPLs (% of Total Loans)	4.3	3.9	3.8	3.6	2.8	2.5
Specific Provisions (% of NPLs)	69.6	71.9	73.2	73.9	72.8	69.6
Net NPL' (% of Net Loans)	1.4	1.2	1.1	1.0	0.8	0.8
Loan Concentration (Share of Top Two Sectors)	34.2	34.2	33.7	39.9	41.9	41.2
Real Estate/ Construction Exposure (%)	33.1	33.4	33.1	21.6	19.4	18.3
Earnings						
ROA (%)	0.7	1.3	0.8	0.6	1.3	0.6
ROA Local Banks (%)	0.8	1.5	0.8	0.2	0.4	0.2
ROA Overseas Banks (%)	0.6	0.9	0.6	0.9	2.2	1.0
ROE (%) *	5.8	10.9	6.6	1.7	3.5	2.3
Net Interest Income (% of Total Income)	77.7	78.9	74.5	67.6	62.8	63.5
Net Fees & Commissions (% of Total Income)	9.9	10.2	10.0	16.1	15.2	17.2
Operating Expenses (% of Total Income)	44.8	49.4	42.1	44.3	42.7	44.1
Liquidity						
Liquid Assets (% of Total Assets)	34.1	33.6	34.1	24.5	24.7	21.9
Liquid Assets (% of Short-Term Liabilities)	42.8	42.4	42.7	30.0	30.8	26.8
Loan-Deposit Ratio (%)	67.2	69.3	68.1	69.4	68.7	61.8
Non-Bank Deposits (% of Total Deposits)	70.4	73.9	76.6	49.3	50.3	52.3

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

Annex 1 Table 3: Selected Financial Soundness Indicators - Islamic Banks

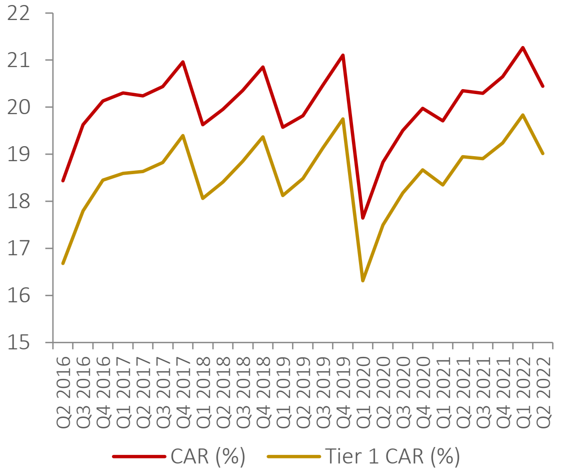
Indicator	Islamic Retail			Islamic Wholesale		
	Q2 2021	Q4 2021	Q2 2022	Q2 2021	Q4 2021	Q2 2022
Capital Adequacy						
CAR (%) *	21.6	21.7	21.5	16.1	15.8	15.3
Tier 1 CAR (%) *	19.6	19.9	19.9	15.0	14.4	14.7
Assets-to-Capital (Times) *	10.4	11.0	11.4	10.2	11.1	8.6
NPFs Net Provisions to Capital (%) *	16.0	13.7	12.0	1.8	0.3	1.5
Asset Quality						
NPFs (% of Total Facilities)	5.5	5.0	4.4	1.7	0.7	6.3
Specific Provisions (% of NPFs)	51.8	56.4	59.0	79.4	92.0	86.7
Net NPFs (% of Net Facilities)	2.8	2.6	2.0	0.4	0.1	0.7
Facilities Concentration (Share of Top Two	34.9	38.2	39.8	44.1	42.5	61.1
Real Estate/ Construction Exposure (%)	31.4	28.4	28.8	17.5	20.1	25.9
Earnings						
ROA (%)	0.3	0.6	0.4	0.4	0.8	0.6
ROE (%) *	3.6	7.3	5.4	4.3	10.0	5.0
Net Income from Own Funds, Current Accounts and Other Banking Activities (% of Operating Income)	39.3	38.5	28.0	39.8	41.8	44.3
Net income from Jointly Financed Accounts and Mudarib Fees (% of Operating Income)	59.6	60.6	70.9	58.2	56.0	48.0
Operating Expenses (% of Total Income)	73.2	73.9	64.5	65.5	67.6	50.8
Liquidity						
Liquid Assets (% of Total Assets)	19.2	19.5	18.9	19.0	18.0	17.4
Facility-Deposit Ratio (%)	76.2	73.3	73.5	64.9	63.0	35.2
Current Accounts from Non-Banks (% of Non-Capital Liabilities, excl. URIA)	36.0	37.2	42.2	46.7	46.8	5.8

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

ANNEX 2: SELECTED FSIs GRAPHS

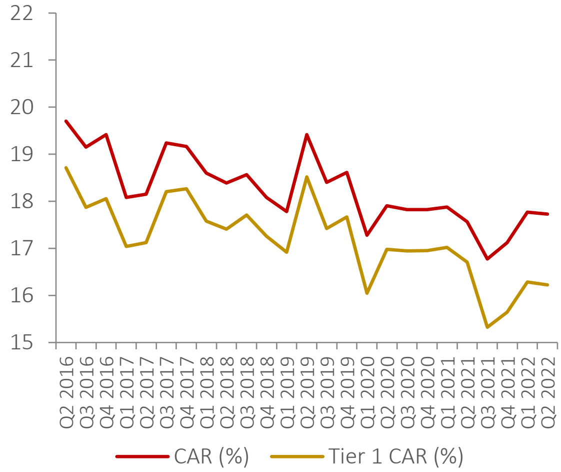
A. Capital Adequacy

Annex 2 Graph 1: Conventional Retail



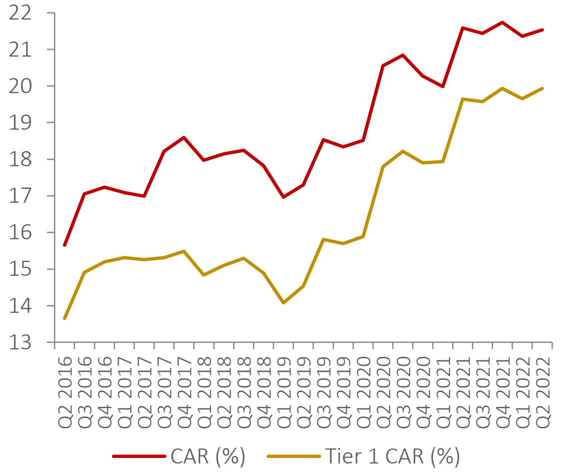
Source: CBB.

Annex 2 Graph 2 : Conventional Wholesale



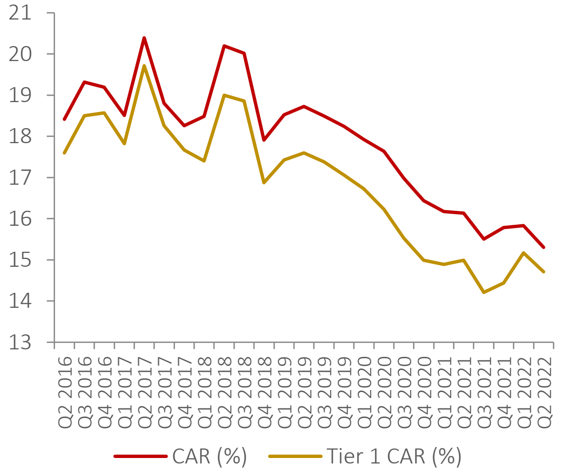
Source: CBB.

Annex 2 Graph 3: Islamic Retail



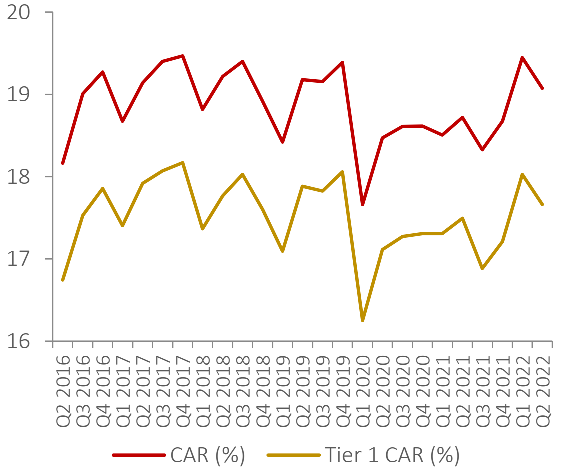
Source: CBB.

Annex 2 Graph 4: Islamic Wholesale



Source: CBB.

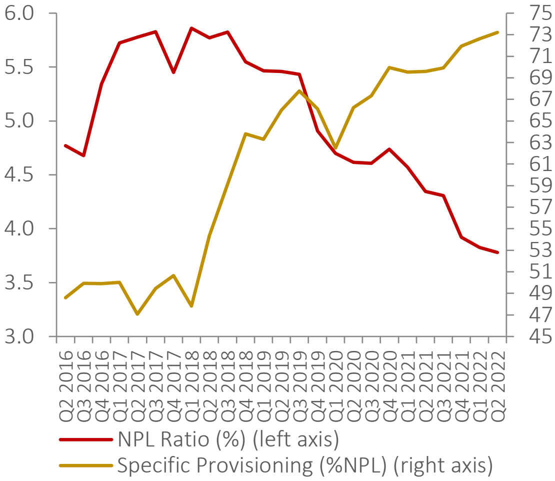
Annex 2 Graph 5: All Banking



Source: CBB.

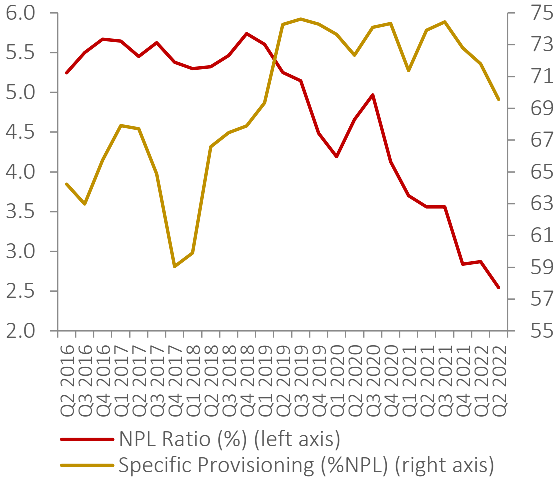
B. Asset Quality

Annex 2 Graph 6: Conventional Retail



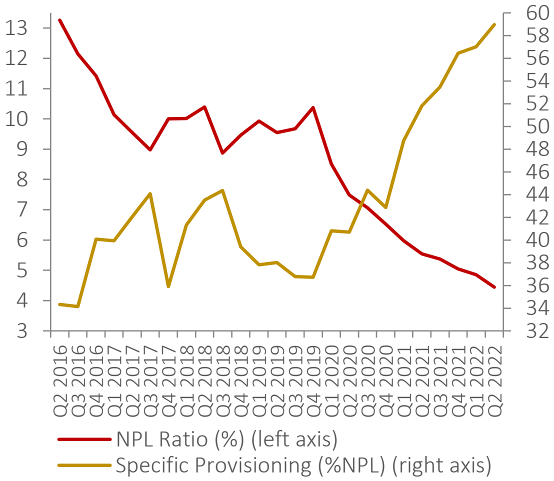
Source: CBB.

Annex 2 Graph 7: Conventional Wholesale



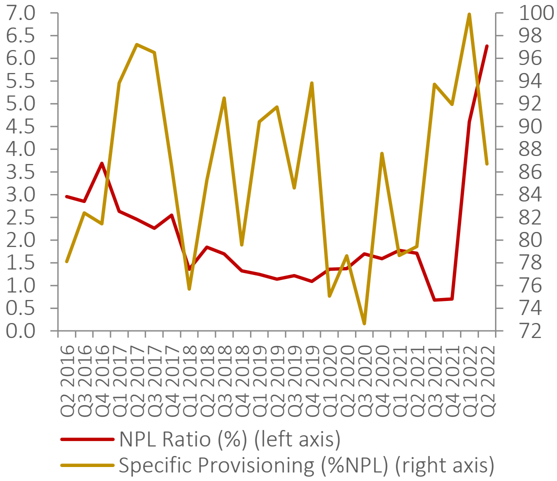
Source: CBB.

Annex 2 Graph 8: Islamic Retail



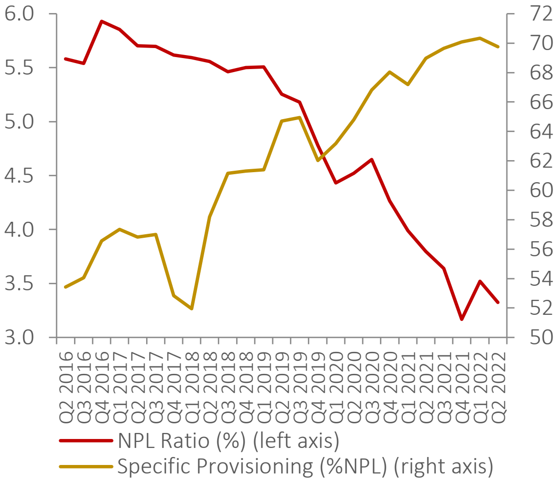
Source: CBB.

Annex 2 Graph 9: Islamic Wholesale



Source: CBB.

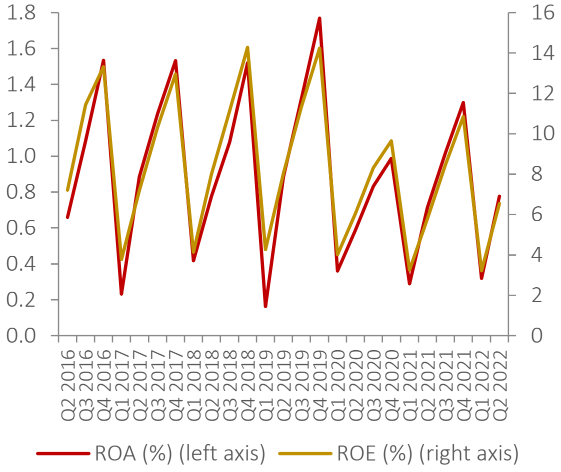
Annex 2 Graph 10: All Banking



Source: CBB.

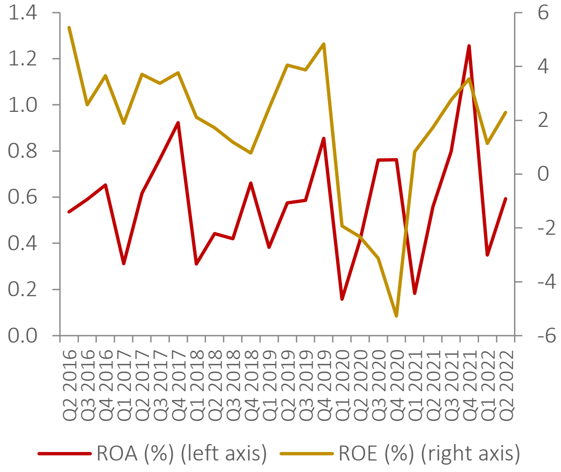
C. Profitability

Annex 2 Graph 11: Conventional Retail



Source: CBB.

Annex 2 Graph 12: Conventional Wholesale

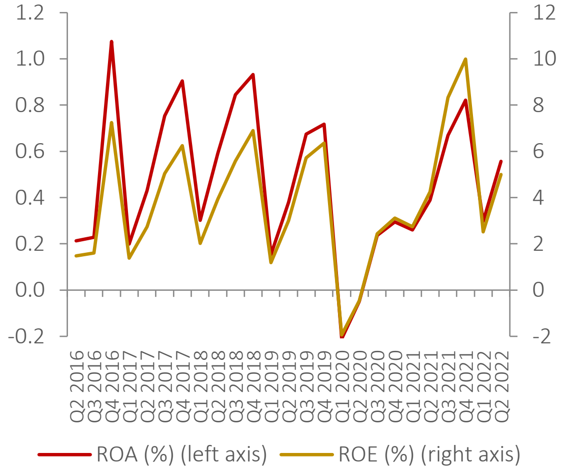


Source: CBB.

Annex 2 Graph 13: Islamic Retail

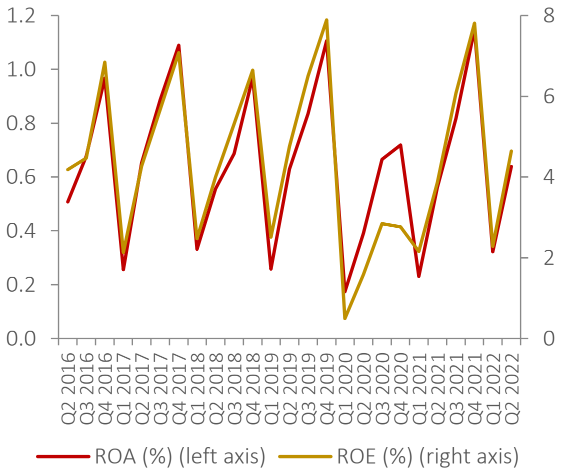
Source: CBB.

Annex 2 Graph 14: Islamic Wholesale



Source: CBB.

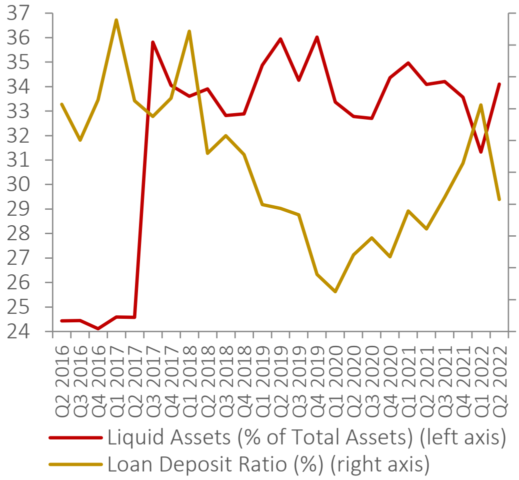
Annex 2 Graph 15: All Banking



Source: CBB.

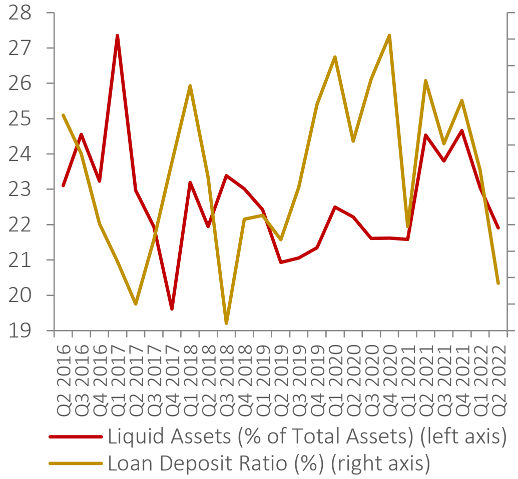
D. Liquidity

Annex 2 Graph 16: Conventional Retail



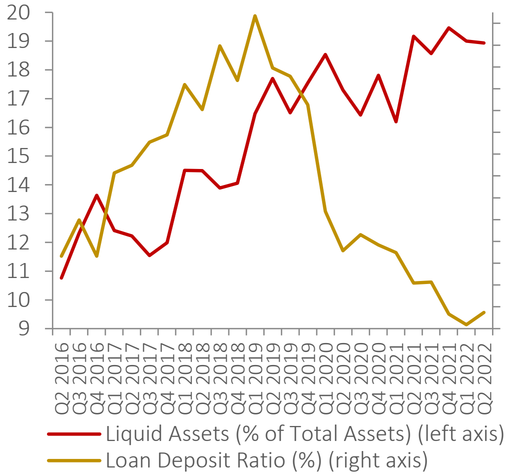
Source: CBB.

Annex 2 Graph 17: Conventional Wholesale



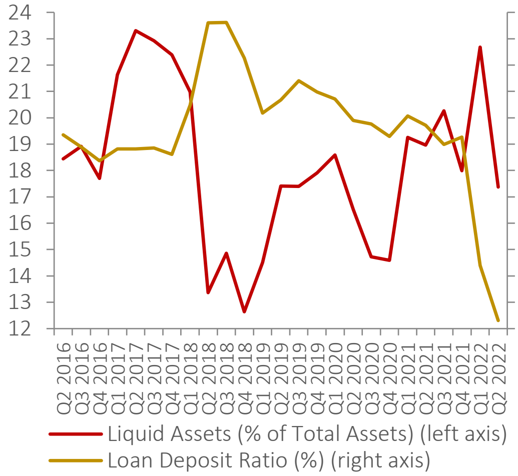
Source: CBB.

Annex 2 Graph 18: Islamic Retail



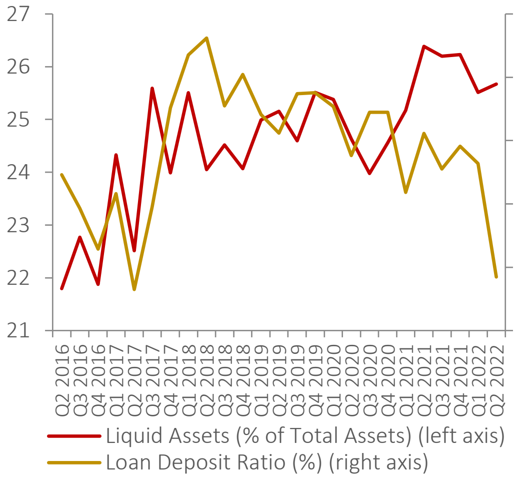
Source: CBB.

Annex 2 Graph 19: Islamic Wholesale



Source: CBB.

Annex 2 Graph 20: All Banking



Source: CBB

ANNEX 3: CBB MEASURES TO CONTAIN EFFECTS OF COVID-19 PANDEMIC

CBB Initiatives

The Bahraini financial system remained resilient through the challenges posed by the repercussions of the COVID-19 pandemic. CBB actively monitored the situation and implemented a series of policy decisions that have succeeded in mitigating any risks to capital, liquidity, and credit quality of the banking system. Key policy responses (including fiscal, monetary, and macro-financial) were issued to mitigate any implications on customers of financial services, financial institutions, and merchants affected by COVID-19, in addition to protecting the stability of the financial sector in the Kingdom. Measures were also taken to preserve the health and safety of customers and workers in the sector.

The evolving nature of the pandemic and the associated economic uncertainty led to a variety of policies by the CBB that fall under one of the categories as seen in figure 1. CBB continued to closely monitor economic and market developments in order to ensure financial stability.

Figure 1: Classication of Policy Measures Taken by the CBB During the COVID-19 Pandemic

Health, Security and Working Arrangements

- Hygiene protocols
- Safety measures
- Working arrangements

Lending and Funding Support

- Supporting access to credit for firms and households
- Increasing banks' lending capacity

Operations Risk and Business Continuity Measures

- Decision-making arrangements
- Internal and External Communication

Prudential Regulation and Reporting Requirements

- Efficient monitoring
- Date sensitive reporting requirements

Since the beginning of the global outbreak of COVID-19, CBB issued directives as part of the preventative measures to contain the virus. The figure below highlights some of the main directives introduced by CBB. A detailed list of the CBB directives, CBB circulars, and other government related measures in chronological order is available in Annex 3.

CBB Loan Deferments

Many central banks provided loan deferral schemes, enabling customers (business and households) to defer interest or principal payments for a period of time, with the deferral period reassessed periodically. One concessionary measure taken by the CBB was recurring loan deferment options announced in a number of CBB circulars issued to licensees.

CBB circulars specified in detail the licensees that will offer the deferment options, the customers that the option will be extended to, the length of the deferment, and what the extension of the tenor will take into account (i.e., what type of accounts will it cover, whether additional profit/interest will be charged). CBB issued five loan deferral options since the beginning of the pandemic:

- Phase 1: Announced in end of March 2020 for six months (March 2020 until August 2020).
- Phase 2: Announced in end of September 2020 for four months (September 2020 until December 2020) unless the borrower agrees to pay within a shorter period.
- Phase 3: Announced in end of December 20200 for six months (January 2021 until June 2021) unless the borrower agrees to pay within a shorter period.

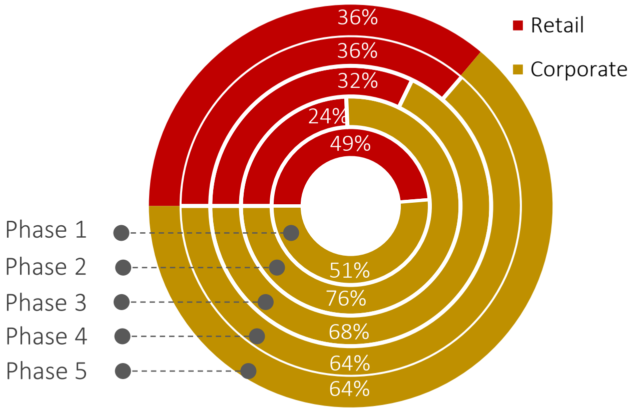
- Phase 4: Announced in end of May 2021 for six months (July 2021 until December 2021) unless the borrower agrees to pay within a shorter period.
- Phase 5: Announced in end of December 2021 for six months (January 2022 until June 2022) unless the borrower agrees to pay within a shorter period.

Figure 3: Summary of CBB's Loan Deferments

	Phase 1	Phase 2	Phase 3	Phase 4	Phase 5
Number of Customers who Applied Instalment Deferral					
Total	-	72,685	74,274	75,237	78,099
Retail	-	70,857	72,217	73,131	76,386
Corporate	-	1,828	2,057	2,106	1,713
% of Total Customers	-	24.5%	23.3%	24.4%	23.5%
Total Outstanding Loans for Customers who applied for deferment (BD' 000)					
Total	6,233,426	2,756,930	2,879,915	2,821,604	3,108,174
Retail	4,233,565	1,507,829	1,646,134	1,612,237	1,837,411
Corporate	1,999,861	1,249,100	1,233,781	1,209,367	1,270,763
% of Total Loan Portfolio	-	26.1%	27.0%	25.0%	26.3%
Deferred Installments Amounts (BD' 000)					
Total	1,079,388	255,601	343,582	382,771	388,503
Retail	525,888	62,227	110,660	138,906	140,381
Corporate	553,501	193,374	232,922	243,865	248,122
% of Total Deferred	17.3%	9.3%	11.9%	13.6%	12.5%

Source: CBB.

Chart 1: Insallment Deferrals (Retail vs. Corporate)



Source: CBB.

Figure 2: Timeline of Main CBB Policy Measures During the COVID-19 Pandemic

2020

16 MARCH

- CBB's cut key policy interest rate on the one-week deposit facility from 1.75% to 1.00%.
- CBB cut overnight deposit rate from 1.50% to 0.75%
- CBB cut one-month deposit rate from 2.20% to 1.45% and CBB lending rate from 2.45% to 1.70%.

18 MARCH

- All licensees to follow and implement sterilization instructions issued Ministry of Health.
- Increase limit of contactless (NFC) transactions on POS to BD 50 without a PIN.
- Cap of 0.8% set on merchant fees imposed on debit card transactions.
- Reduced cash reserve ratio for retail banks from 5% to 3%.
- Relax LTV for new residential mortgages.
- Provide retail banks repo arrangements up to 6 months at 0% on a case-by-case basis.
- Loan deferment Phase 1: Defer loan payments to customers for a period of 6 month (March 2020 until August 2020).

23MARCH

- Money changers to disinfect all incoming currency notes and wholesale imported notes.
- Money changers required to equip employees with Personal Protective Equipment (PPE).

22 SEPTEMBER

- Loan Deferment Phase 2: Defer loan payments to customers for 4 months (September 2020 until December 2020).

29 DECEMBER

- Loan Deferment Phase 3: Defer Loan payments to customers for 6 months (January 2021 until June 2021).

2021

27 MAY

- Loan Deferment Phase 4: Defer Loan payments to customers for 6 months (July 2021 until December 2021).

23 DECEMBER

- Loan Deferment Phase 5: Defer loan payments to customers for 6 months (January 2022 until June 2022).

CBB Measures

CBB's Regulatory Measures as Part of Precautionary Efforts to Contain COVID-19

Date	Measures
16th March 2020	▪ CBB cut key policy interest rate. ▪ CBB's key policy interest rate on the one-week deposit facility was cut from 1.75% to 1.00%. CBB also decided to cut the overnight deposit rate from 1.50% to 0.75%, the one-month deposit rate from 2.20% to 1.45%, and CBB lending rate from 2.45% to 1.70%.
18th March 2020	▪ CBB urged providers of POS devices to communicate with merchants to sterilize such devices regularly and to require customers to directly enter and remove their cards from the POS devices. ▪ CBB urged all licensees to follow and implement sterilization instructions issued by the Ministry of Health and submit a report on this. CBB also instructed licensees to communicate with the public by covering the measures taken to ensure the safety of their employees and customers in the press or through social media.

	▪ The volume limit of contactless (NFC) transactions on POS devices has been increased to BD50/- without the need to use a PIN code. CBB also instructed its licensees to adhere to the requirements of continuation of operations and services. ▪ A cap of 0.8% has also been set on merchant fees imposed by local banks and finance companies on debit card transactions to reduce merchant and company costs (0.35% to the acquirer, 025% to the issuer, 0.2% to the benefit company). ▪ CBB issued several regulatory measures for a period of six months to contain any financial repercussions on customers of the banking sector, which will be reviewed by CBB at the end of the period in consultation with the banking sector. These measures aim to provide more liquidity and flexibility to enable banks to continue providing financing to their customers. ▪ CBB required retail banks, financing companies and microfinance institutions to postpone instalments for any borrower or credit card holder affected by the economic repercussions of the Coronavirus without fees or interest on interest or increase in the percentage of profit / interest for a period of 6 months, unless the borrower agrees to pay within a shorter period. ▪ CBB provided retail banks concessionary repo arrangements with up to 6 months at zero percent on a case-by-case basis. ▪ CBB reduced cash reserve ratio for retail banks from 5% to 3%. ▪ CBB requested to relax the LTV for new residential mortgages or Bahrainis except Mazaya loans.
20th March 2020	▪ In light of the current situation faced by the Kingdom of Bahrain and to preserve the health and safety of citizens and residents, CBB Bahrain urged consumers to communicate through the National Suggestion & Complaint System "Tawasul" or through CBB website https://www.cbb.gov.bh/complaint-form/ or by calling 17547789/17547360, instead of personally visiting the Consumer Protection Office at CBB.
23rd March 2020	▪ CBB instructed Money Changers to disinfect all incoming currency notes and wholesale imported notes to limit the risk of exposure to the Coronavirus (COVID-19). ▪ Under the instructions, Money Changers are required to disinfect incoming currency and wholesale imported notes with Ultraviolet Germicidal Irradiation (UVGI) or by isolating notes for 72 hours. ▪ Money Changers Licensees are also required to equip employees with Personal Protective Equipment (PPE) as per recommendations outlined by the Ministry of Health.
20th September 2020	▪ CBB announced that banks will defer loan payments to their customers until the end of the current year in a manner that does not affect the banks' liquidity and financial solvency, provided that interest rates and fees prescribed by banks on these loans are calculated during the deferral period. ▪ CBB's announcement followed directives by the Cabinet in its weekly session to help offset the negative impact of Covid-19, without affecting banks' liquidity and financial solvency to contribute in providing liquidity in supporting citizens and various economic sectors to alleviate the economic effects of the pandemic.
22nd September 2020	▪ CBB has clarified that no fees, except insurance, can be charged by lenders on the four-month loan deferral for Bahrainis and local companies. ▪ No fees must be charged to customers for providing loan deferment option, except for additional insurance fees resulting from extension of the loan tenor.
29th December 2020	▪ CBB directed banks and financing companies to offer their customers six-month installments deferment option, starting from 1st January 2021. The option must entail extending the tenor to take into account the additional profit/interest, while keeping the installment amount unchanged. Moreover, licensees must not increase profit/interest rates; ▪ The following exposures are excluded from the deferment option: - Credit card exposures; - Financing instalments received through court unless arranged through court; - Credit syndication facilities to resident corporates involving non-resident participating lenders; and - Pre-export financing under letters of credit without recourse to the resident corporate (exporter). ▪ CBB will reassess the need to continue with such concessionary measures during June 2021 and advise licensees accordingly.

27th May 2021	▪ CBB has decided that the existing deferral agreement expiring on 30th June 2021 will be extended for another period of six months until 31st December 2021 for all Stage 1&2 resident retail, small and medium sized enterprises and other corporate customers. ▪ CBB will reassess for the need for any further deferral arrangement during December 2021 and shall advise the licensees accordingly.
23rd December 2021	▪ CBB has decided that the existing deferral arrangements expiring on 31st December 2021 will be extended for another period of six months until 30th June 2022 for all Stage 1 & 2 resident retail, SMEs and other corporate customers.
28th June 2022	▪ The CBB agrees with the recommendation of the Bahrain Association of Banks to discontinue the instalment deferral program by 30th June 2022. ▪ The CBB urges all licensees to assess customers' needs for either rescheduling or restructuring existing facilities.

Source: CBB.

CBB Circulars

CBB Circulars as Part of Precautionary Efforts to Contain COVID-19

Date/ Circular	Licenses	Subject
5th March 2020 EDBS/KH/C/21/2020	All Banks All Financing Companies All Micro-Finance Companies	Concessionary Measures to Mitigate the Impact of Coronavirus
8th March 2020 EDBS/KH/C/24/2020	Selected Retail Banks/Specialized Licenses/Ancillary Service Providers	Measures to Mitigate the Impact of Coronavirus
11th March 2020 EDBS/KH/C/25/2020	All Banks All Financing Companies All Micro-Finance Institutions All Ancillary Services All Representative Offices	Disinfection Instructions
11th March 2020 EDFIS/C/024/2020	Self-Regulatory Organizations (SRO) SRO Members Crypto-asset Licensees All listed Companies	Disinfection Instructions
12th March 2020 EDBS/KH/C/26/2020	All Retail Banks	Services Continuity Measures
16th March 2020 EDBS/KH/C/28/2020	All Banks All Financing Companies All Micro-Finance Institutions All Ancillary Services All Representative Offices	Disinfection Instructions
17th March 2020 OG/106/2020	All Banks All Financing Companies All Microfinance Companies All Ancillary Services Providers	Regulatory Measures to Contain the Financial Repercussions of the Covid-19
19th March 2020 OG/108/2020	All CBB Licensees All Listed Companies	Upcoming General Meetings
23rd March 2020 EDBS/KH/C/30/2020	All Retail Banks All Financing Companies All Microfinance Companies	Implementation Guidelines Regarding the 6th Months Deferral
24th March 2020 EDBS/KH/C/32/2020	All Retail Banks All Financing Companies All Microfinance Companies	Implementation Guidelines Regarding the 6th Months Deferral
24th March 2020 EDFIS/C/030/2020	All Insurance Licensees	Sub: Services Continuity Measures
26th March 2020 EDFIS/C/032/2020	Self-Regulatory Organizations (SRO) SRO Members Crypto-asset Licensees	Services Continuity Measures
30th March 2020 EDBS/KH/C/33/2020	All Banks	Deferral of Implementation of Announced Regulator Policy Requirements
30th March 2020 OG/124/2020	All listed Companies All locally incorporated banks	Exemption for First Quarter Financial Results Preparation and Publication
30th March 2020 CMS/C/010/20	SRO Members	Market Intermediaries responsibility Amid COVID-19

1st April 2020 EDBS/KH/C/34/2020	Ancillary Service Providers Financing Companies Microfinance Institutions	Agreed Upon Procedures for Financial Crime (FC) Module
1st April 2020 EDBS/KH/C/35/2020	All Banks	Agreed Upon Procedures for Financial Crime (FC) Module
1st April 2020 EDFIS/C/034/2020	All Insurance Licensees	Agreed Upon Procedures for Financial Crime (FC) Module
1st April 2020 EDFIS/C/035/2020	All Investment Firms	Agreed Upon Procedures for Financial Crime (FC) Module
1st April 2020 EDFIS/C/036/2020	All Money Changers All Non-Bank Representative Offices All Administrators/Registrars All Trust Services Providers Ancillary Services Providers- Third Party Administrators	Agreed Upon Procedures for Financial Crime (FC) Module
1st April 2020 EDFIS/C/037/2020	Self-Regulatory Organizations (SRO) SRO Members Crypto-asset Licensees	Agreed Upon Procedures for Anti-Money laundering and Combating of Financial Crimes (AML) Module
1st April 2020 CMS/C/011/2020	All Listed Companies	Market Fairness and Integrity Amid COVID-10 Developments
2nd April 2020 EDBS/KH/C/36/2020	All Banks	Date Sensitive Reporting Requirements Extensions/Exemptions Under Rulebooks (Volume 1 and 2)
2nd April 2020 EDBS/KH/C/37/2020	All Financing Companies All Microfinancing Companies	Date Sensitive Reporting Requirements Extensions/Exemptions Under Rulebooks (Volume5)
2nd April 2020 EDBS/KH/C/38/2020	All Banks	Date Sensitive Reporting Requirements Extensions/Exemptions Under Rulebooks (Volume 5)
8th April 2020 OG/148/2020	All Licensees	Additional COVID-19 Precautionary Measures
12th April 2020 OG/152/2020	All Retail Banks	Directive on Use of Salary Transfers to Bahrainis by the Government
26th April 2020 EDBS/C/41/2020	All Bank Licensees All Financing Companies All Microfinance Companies	Financial Impact Assessment of the Six Months Instalment Deferral
27th May 2020 EDFIS/C/052/2020	All Licensees	Money Laundering & Terrorist Financing Risks & Practices during COVID-19
21st June 2020 OG/226/2020	All Bahraini Bank Licensees All Financing Companies All Microfinance Institutions	Regulatory Concessionary Measures
1st July 2020 OG/249/2020	All Branches of Foreign Banks	Regulatory Concessionary Measures
14th July 2020 OG/259/2020	All Listed companies All Licensees	Reporting of Financial Impact of COVID-19
24th August 2020 EDBS/KH/C/54/2020	All Banks Al Financing Companies ALL Microfinance Companies	Exemptions from Submission of Agreed Upon Procedures on PIR/PIRI/PIRFM (Volumes 1, 2, and 5)
26th August 2020 OG/296/2020	All Banks Al Financing Companies ALL Microfinance Companies All Payment Services Providers All Cards Processing Services Providers	Status Update on COVID-19 Policy Measures
21st September 2020 OG/318/2020	All Retail Banks Financing Companies Micro-Finance Companies	Further Deferment of Loan Instalments
22st September 2020 OG/321/2020	All Retail Banks Financing Companies Micro-Finance Companies	Further Deferment of Loan Instalments
8th November 2020 EDBS/C/67/2020	All Retail Banks All Financing Companies All Micro-Finance Companies	Non-Charging of Interest/Profit on Deferral Period

29th December 2020 OG/431/2020	All Banks All Financing Companies All Micro-Finance Companies All Payment Service Providers	Update on COVID-19 Policies Measures
28th February 2021 EDFIS/C/015/2021	All Investment Firms	Agreed-Upon Procedures for The Financial Crime (FC) Module
28th February 2021 EDFIS/C/014/2021	All Insurance Licensees	Agreed-Upon Procedures for The Financial Crime (FC) Module
28th February 2021 EDFIS/C/017/2021	Self-Regulated Organizations (SROs) SRO Members Crypto-assets Licensees	Agreed-Upon Procedures of Anti-Money Laundering and Combating Financial Crime (AML) Module
3rd March 2021 EDBS/KH/C/07/2021	All Banks	Agreed-Upon Procedures for The Financial Crime (FC) Module
27th May 2021 OG/170/2021	All Retail Banks All Financing Companies	Extension of Credit Instalments Deferral
23rd December 2021 OG/417/2021	All Retail Banks All Financing Companies	Update on COVID-19 Regulatory Measures
9th May 2022 OG/187/2022	All Listed Companies All Licensees	Reporting Financial Impact of COVID-19
28th June 2022 ODG/27/2022	All Retail Banks All Financing Companies	Update on COVID-19 Policy Measures
28th June 2022 ODG/28/2022	All Retail Banks	Update on COVID-19 Policy Measures

Source: CBB.

LIST OF ABBREVIATIONS

Acronym	Description
ATM	ATM Clearing System
API	Application Programming Interface
BCTS	Bahrain Cheque Truncation System
BECS	Bahrain Electronic Cheque 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
CR	Conventional Retail
CW	Conventional Wholesale
DSIBs	Domestically Systemically Important Banks
EBPP	Electronic Bill Presentment and Payment System
EFTS	Electronic Fund Transfer System
EU	European Union
FinTech	Financial Technology
FMI	Financial Market Infrastructure
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
IR	Islamic Retail
IW	Islamic Wholesale
NFA	Net Foreign Assets
NPW	Net Premiums Written
NPF	Non-performing Facilities
NPL	Non-performing Loans
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