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

Monetary policy normalization remained throughout 2023 as many central banks continued to increase their key policy interest rates to offset global inflationary pressures. For the first half of 2023, financial stability risks remained elevated with continued monetary policy tightening leading to the rapid rate hikes to counter the rising inflationary pressures which are not expected to return inflation to target until 2025. The risk lays in higher debt service burdens of households, firms, and governments and the effect on the demand for new credit. Moreover, a longer high interest rate environment has the risk of impacting the residential and commercial real estate sectors which can spillover and pose a significant risk to the financial sector.

March 2023 witnessed some foreign banks failures in USA & Switzerland. Nevertheless, such failures remained contained as regulators swift responses prevented potential global contagion. These events raised financial stability concerns related to liquidity and interest rate risks. At the same time, the global economy continued its slow recovery from the effects of the pandemic, Russia-Ukraine conflict, and high commodity prices.

Maintaining strong, sustainable growth will require policymakers to continue to stay agile and ready to contain financial market strains to minimize risks and address challenges posed by the interaction between tighter monetary conditions and any built-up vulnerabilities.

Locally, the Central Bank of Bahrain (CBB) continued to raise interest rates in line with rising rates globally. CBB raised its policy interest rates four additional times throughout 2023 to maintain financial and monetary stability.

The Bahrain economy in in H1 2023 continued its growth despite the geopolitical environment, inflationary pressures, and higher interest rates. The financial system, that has a major role in supporting the Bahraini economy, remained resilient showing strong performance across key metrics amidst a strong domestic macroeconomic environment. The banking system maintained adequate capital adequacy and liquidity buffers during 2023 and remained resilient due to strong pre-pandemic capital and liquidity positions with credit growth in the banking sector remains instrumental in supporting the private sector.

Moving forward, the CBB remains committed to addressing any potential vulnerabilities and remains alert to possible risks from any global developments and focused on monitoring asset quality. The CBB has also continued commitment to digital transformation, climate related risks to the financial sector, AML/CFT compliance and increased cyber risks.

Looking further ahead, the CBB also is continuing its development of best practices related to Environmental, Social and Governance (ESG) risk with a focus on climate-related financial risks to transition to a sustainable economy.

FINANCIAL STABILITY REPORT COVERAGE

A key objective of 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 to fostering the soundness and stability of financial institutions and markets. CBB recognizes that financial stability is critical to contribute to growth, employment, and development in Bahrain.

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 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 FSR primarily examines the performance of the key components of the Bahraini financial system up to end of June 2023. The Baking sector analysis covers the sector on a consolidated basis (including subsidiaries and branches abroad).

This edition of the FSR contains 9 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 capital markets.
- Part IV: Developments in the payments and settlement systems, fintech, and cyber security:
  - Chapter 8: Performance of payment and settlement systems, point of sale, and digital wallets.
  - Chapter 9: FinTech developments and financial inclusion.

FINANCIAL STABILITY

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.

EXECUTIVE SUMMARY

Global Macro Financial Environment Overview

Global economic recovery has been slow throughout the first half of the year 2023 amid high inflation, monetary tightening, and the geopolitical environment which have affected the global outlook. Monetary policy tightening remains with the US and other advanced economies in efforts to lower inflation.

Global economic economy growth is expected to fall from an estimated 3.5% in 2022 to 3.0% in 2023 with 1.5% for advanced economies and 4.0% for emerging markets and developing economics. Across major economies, the US expected growth for 2023 is 2.1%, China 5.0%, and the Euro Area 0.7%.

Financial Sector Overview

The size of the assets of the banking sector in Bahrain was USD 226.0 billion as of June 2023. Retail banking total assets continued growing to reach BD 38.6 billion (USD 101.7 billion) in June 2023, wholesale banking sector showed an increase to USD 124.3 billion, and Islamic banking sector assets (which represent 16.7% of the total banking sector assets) increased to USD 37.7 billion.

The total amount of credit to the private sector (business and personal) by retail banks increased to BD 11.3 billion, a growth of 4.7% YoY. The deposit base also witnessed growth to BD 19.4 billion in June 2023 with 77.9% being domestic deposits that had a 5.2% YoY increase.

Banking Sector

The Bahraini banking system remained resilient during H1 2023, supported by strong macroeconomic conditions and adequate capital and liquidity positions. The capital adequacy ratio (CAR) for the banking sector stood at 19.3% in June 2023. The NPL ratio continued decreasing to 3.1% with a stable provision coverage level of provisioning of 61.8%.

Return-on-assets (ROA) remained stable at 0.7% and return-on-equity (ROE) increased to 5.3%, showing strong profitability. Liquidity positions remained strong as liquid assets as a proportion of total assets stood at 23.4% and the Loan Deposit Ratio (LDR) at 63.2%.

Conventional Banks

The CAR for conventional retail increased to 21.7% by June 2023. Asset quality improved as NPL ratio stood at 3.6% in June 2023 with coverage at 66.7%. The profitability of retail banks remained positive as ROA increased to 0.9% and ROE to 7.1%. Liquidity position decreased to 30.9% in June 2023 and LDR at 71.4%.

As for wholesale banks, capital adequacy stood at 17.0% in June 2023. The NPL ratio dropped to 2.1% while specific provisions witnessed a decrease to 61.1%. Profitability was positive as ROA for the conventional wholesale banking remained stable at 0.9% and ROE at 3.2% in December 2022. Liquid assets for wholesale banks as a proportion of total assets decreased to 19.9% and LDR at 62.1% in June 2023.

Islamic Banks

The CAR of Islamic retail banks stood at 21.4% in June 2023. Asset quality is stable as non-performing facilities (NPF) ratio reached 5.0% while specific provisioning decreased to 49.6%. ROA for Islamic retail remained positive at 0.4% and ROE at 4.9%. Liquidity position to Islamic retail banks remained stable as liquid assets available to Islamic retail banks was 19.1% and LDR was 63.0%.

On the other hand, capital adequacy Islamic wholesale banks increased to 17.2% in June 2023. The NPF ratio for Islamic wholesale banks was 5.3% with provisioning for NPFs increasing to 81.5%. Islamic wholesale banks registered positive profitability with ROA reaching 0.7% and ROE at 5.8% in June 2023. Liquid assets decreased for Islamic wholesale to 20.2% of total assets while LDR increased to 32.3%.

Insurance Sector

Overall, the insurance sector in Bahrain remained sound and experienced sustained business growth. The insurance sector in Bahrain holds promise for growth, as demonstrated by the industry's performance for the period ended June 2023. The sector is expected to continue to grow due to the increase in the public awareness on the importance of the insurance products as well as due to the soundness of regulatory and supervisory framework of the insurance sector in Bahrain.

The Insurance sector in Bahrain is made up of two main segments: conventional and takaful. As of June 2023, total assets of the Insurance sector reached BD 2,287.4 million with a decrease of 1.9% YoY. Total assets of conventional insurance firms were BD 2,080.8 million, a YoY decrease of 2.6%. Takaful firms' assets increased by 6.2% YoY to reach BD 206.6 million.

Total gross premiums registered BD 151.5 million as of June 2023 with medical records having the highest concentration in Gross Premiums (34.5%) and Gross Claims (35.2%). Conventional local firms accounted for the largest segment of total gross premiums (54.9%) followed by Takaful (30.8%) and conventional overseas branches (14.3%).

Capital markets

As of 30th June 2023, Bahrain Bourse recorded a total listing of 42 Companies, 3 Mutual funds and 18 Bonds and Sukuk. Bahrain All Share Index increased by 3.3% during first half of 2023 reaching 1,957.87 points, while the Bahrain Islamic Index decreased by 12.0% reaching 746.98 points. As of end-June 2023, market capitalization of the Bahrain Bourse stood at BD 7.7 billion.

Most of the value shares traded in H1 2023 was in the materials sector representing 42.3%. As for the volume of shares traded, the majority came from the financials sector (72.1%). Most of the number of transactions in H1 2023 was attained by the financial sector representing 44.1% of total transactions.

Payments and Settlement Systems and Point of Sale and E-Commerce

The CBB's payment system remained robust during 2023 as CBB continues to further enhance its steps towards digital transformation. The demand for online transactions continues its upward trend based on the performance of the Electronic Fund Transfer System (EFTS) that enables electronic fund transfers within Bahrain with three services: Fawri+ Fawri, and Fawateer.

Daily average volume of Fawri+ transactions increased by 43.7% s in H1 2023 compared to H1 2022. The daily average value of Fawri+ transfers increased by 21.2% in H1 2023 compared to H1 2022.The daily average volume and value of ATM transactions for H1 2023 continued to decrease by 8.3% and 7.6% respectively compared to H1 2022 indicating a continued trend of declining cash withdrawals.

Point of Sale (POS) and E-commerce transactions volume and value increased in H1 2023 by 13.9% and 8.1% YoY respectively. Contactless POS payments continue to show an increasing trend reaching 78.6% and 52.3% of the volume and value of transactions respectively.

FinTech, Innovation, and Financial Inclusion

Bahrain continues its efforts in repositioning itself as a 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 end of June 2023, 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
3.0%	2.1%	0.7%
MENA Growth	**Advanced Economies Growth**	**Emerging Market Growth**
2.5%	1.5%	4.0%

- The World economy is continued to witness a slowed recovering but still facing headwinds amid high inflation, and heightened uncertainty.
- Russia-Ukraine war and geopolitical tensions continue to pose risks and remain a principal source of financial and economic instability.
- The rise in inflationary pressures has triggered an almost universal tightening in monetary policy.
- In the first half of 2023, the US Federal Reserve has lifted rates by 500 basis points from 2022 and the European Central Bank has raised rates by 400 bps.
- The rise in central bank policy rates to fight inflation continues to weigh on economic activity.
- Financial conditions are tightening, borrowing costs are rising.
- Equity markets in Europe and the US have been volatile.

1.1 Overview

The global economy has shown resilience and signs of recovery in the first half of 2023, but the outlook remains weak. The global recovery from the COVID-19 pandemic and Russia's invasion of Ukraine remains slow and uneven as economic activity still falls short of its pre-pandemic path. Risks for 2023 are more stable than they are earlier this year, but the outlook is still uncertain due to factors such as the ongoing conflict between Russia and Ukraine and the increasing probability of a global economic slowdown.

According to the recent update of the IMF's World Economic Outlook (WEO) in October 2023, global growth was 3.5% in 2022 with a projection of 3.0% in 2023 and 2.9% in 2024. Advanced Economies are projected to grow by 1.5% in 2023 and Emerging Market and Developing Economies by 4.0%. Regarding the world largest three economies, the IMF has projected 2023 USA growth to reach 2.1%, the Euro Area growth to reach 0.7%, and China at 5.0%.

Global headline inflation is expected to reach 6.9% in 2023 after being 8.7% in 2022 and continue to decline to 5.8% in 2024 on the back of lower commodity prices. The IMF expects that its unlikely for Inflation to return to targets before 2025.

Monetary policy actions remain important to keep inflation expectations anchored with returning inflation to targets. The successful calibration of monetary policy, and the course of global developments will determine the course of recovery of the global economy.

As for financial stability, concerns still remain as high global interest rates are also affecting the cost of financing, especially in emerging markets and developing economies. Prolonged high interest rates will put strains on borrowers to meet debt payments and also affect the repayment capacity of corporate and household borrowers as defaults are rising, especially in the real estate markets.

In the following sections, recent trends in the global economy are highlighted and the major financial and economic indicators during the first half of 2023.

1.2 Global Macro-financial Environment

Global economic recovery has been slow throughout the first half of the year 2023 amid high inflation, aggressive monetary tightening, and political instability. 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.

In its October 2023 WEO update, the IMF forecasted the global economy to fall from an estimated 3.5% in 2022 to 3.0% in 2023 and 2.9% 2024.

1.2.1 Economic Performance

The global economy continues to recover slowly from the blows of the pandemic, Russia's invasion of Ukraine, and the cost-of-living crisis. Despite the Russia-Ukraine war, the overall economic performance in Europe continues to show resilience in the face of the impressive shocks it has experienced in recent years, but it has lost momentum. Economic activity in the EU was very subdued in the first half of 2023. Uncertainty and geopolitical tensions have put additional downward pressure on the financial sector in Europe which in turn amplified volatility and raised new concerns in the global financial markets. According to the IMF regional economic outlook, Europe faces the difficult task of simultaneously bringing down inflation, sustaining economic growth, and preserving financial stability.

Inflation in Europe remains higher than expected. Prices growth is now expected to average 5.6% across the eurozone in 2023 and 3.3% in 2024 due to persisting core price pressures. The ECB has indicated that it will increase interest rates for the eurozone by at least 0.5 percentage points to almost 3.75% on its main deposit rate to reduce the pressure on prices.

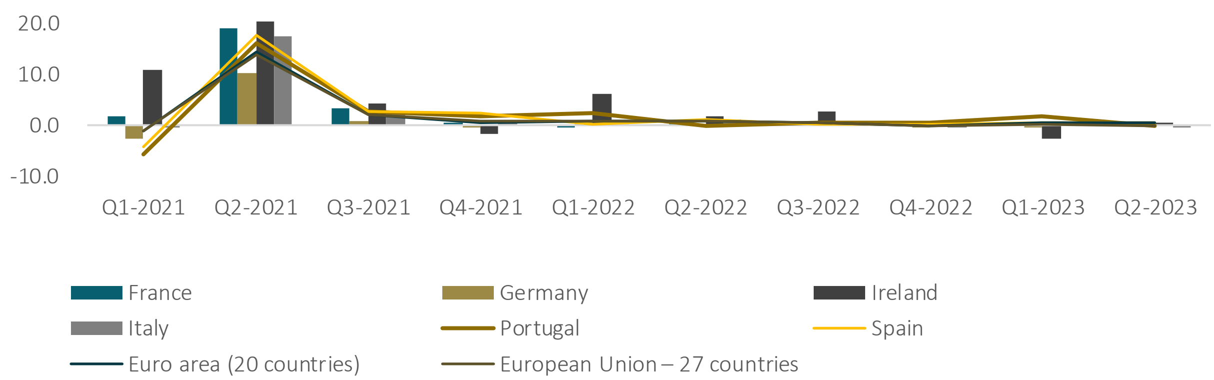
As Chart 1.1 shows, most European economies experienced slow growth. In its October WEO update, the IMF indicated Italy and Spain's forecasts by 0.7 % and 2.5% respectively. Ireland's growth of 3.3%, the largest in the eurozone, distorts the overall picture.

Regarding the two largest economies in the Eurozone, their performances decelerated in the first half of the year 2023 compared to what they achieved in 2022. Germany's economy was hit by sanctions on Russian gas since the third quarter of 2022. German economy is more dependent on heavy manufacturing exports than the other European countries, is currently facing an uncertain global trade environment and worker shortages. The IMF expects German economic growth to experience a recession by 0.5 %in 2023 and then to realize a modest growth by 0.9% in 2024 owing to elevated energy import prices and weak consumer confidence. As for France, tourism, demand for services and luxury goods are fueling the country's economic resilience. According to the IMF WEO, France's growth rate will accelerate from 1.0% in 2023 to 1.3% in 2024.

Turning to the Euro Area (20 countries) and the European Union (EU) (27 countries) their economies have also experienced weak performance in 2023. 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 to be 0.7% in 2023, lower from the 3.3% achieved in 2022. 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 5.7%, respectively.

According to the European Central Bank, the weaker growth momentum in the EU is expected to extend to 2024, and the impact of tight monetary policy is set to continue restraining economic activity. As the outlook for global growth and trade remains broadly unchanged compared to spring, the EU economy cannot count on strong support from external demand. However, a mild rebound in growth is still projected next year, as inflation keeps easing, the labor market remains robust and real incomes gradually recover.

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



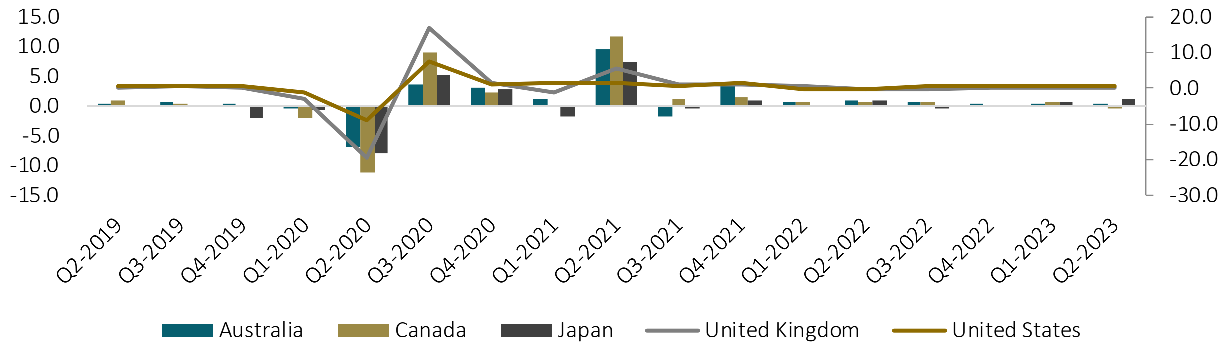
**Growth rate compared to the same quarter of previous year, seasonally adjusted.*
Source: OECD Quarterly National Accounts.

In the United Kingdom, after the economic activity returned to its pre-pandemic level in the beginning of 2023, new shocks hit the UK economy. The IMF forecast UK economic growth to reach 0.5% in 2023 and 0.6% in 2024, lower from the 4.1% realized in 2022.

The economic outlook for the United States has deteriorated amid soaring energy and commodity prices, tighter labor market conditions and aggressive monetary tightening by the Federal Reserve. GDP growth is expected to grow by 2.1% in 2023 similar to 2022 and by 1.5% in 2024.

Japan's economy returns to pre-pandemic levels. According to the IMF's world Economic Outlook, Japan is anticipated to see a steady growth by 2.0% for 2023 and then will slow to reach 1.0% in 2024.

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



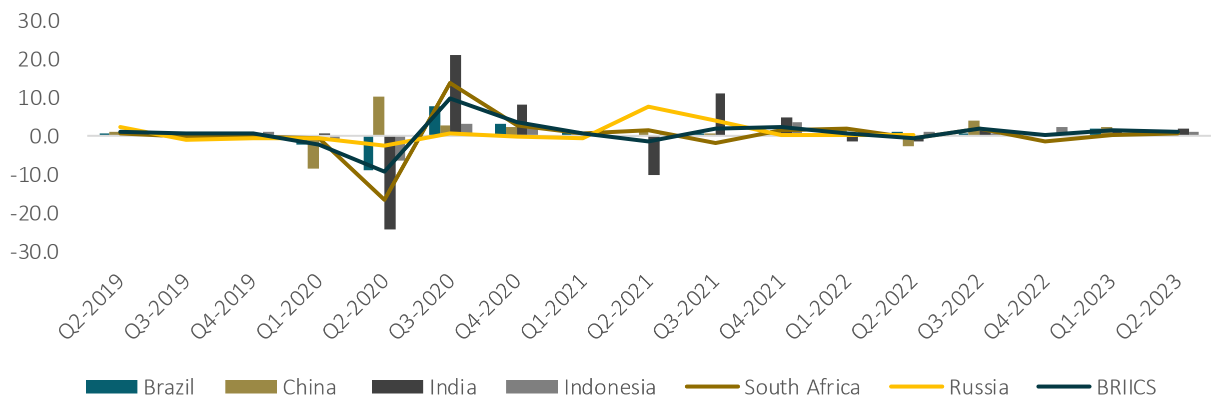
** Growth rate compared to the same quarter of previous year, seasonally adjusted*
Source: OECD Quarterly National Accounts.

As for emerging economies (Chart 1.3), the BRIICS countries' growth was weaker than expected as it reached the level of 1.0% in Q2/2023 from 1.5% achieved in Q1/2023. Recent data shows that China's GDP growth reduced to 0.8% in Q2 from 2.2% in Q1, showing a slowdown in the domestic economic recovery. The government has issued guidelines on boosting confidence in the private sector, and a new round of property easing measures to revive growth. The IMF recent update has maintained China's GDP growth forecast to 5.0% in 2023 compared to 3.0% in 2022 and expect the economy grow by 4.2% in 2024.

Similarly for India, after rapid economic growth of 7.2% achieved in 2022, economic momentum has remained strong in the first half of 2023. The IMF recent update has revised up India's GDP growth forecast to 6.3 for 2023 and 2024.Recent economic indicators for India during the first half of 2023 continue to signal expansionary economic conditions driven by domestic demand.

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 3.1% and 0.9% respectively in 2023 and achieve growth rates of 1.5% and 1.9% in 2024.

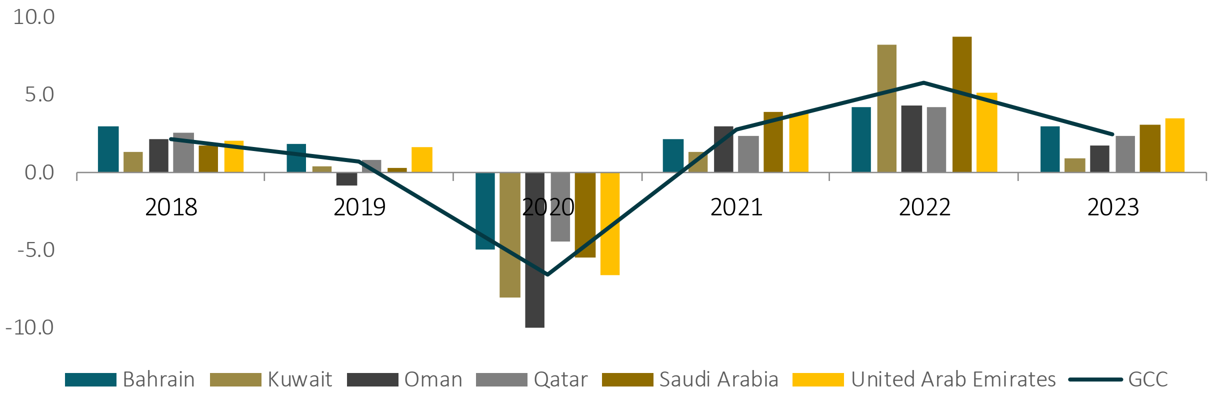
Chart 1.3: Quaterly Real GDP Growth in BRIICS (Quaterly %) *



**Growth rate compared to the same quarter of previous year, seasonally adjusted.*
Data on Russia growth in not available since Q1/2022.
Source: OECD Quarterly National Accounts.

Regionally, 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. WEO for October 2024 projects UAE's real GDP to grow by 3.5%, Saudi Arabia by 0.8%, Qatar by 2.4%, Oman by 1.2%, and Kuwait by -0.6%.

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

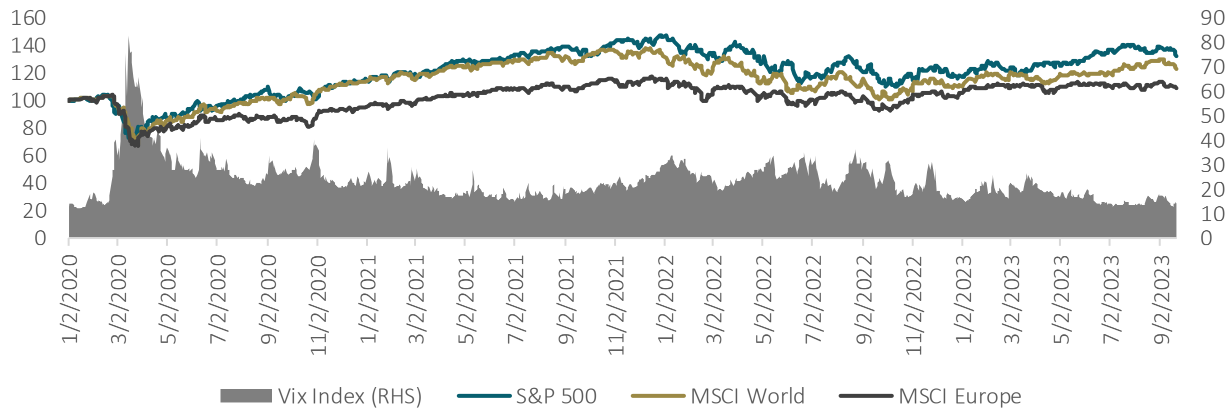


**Forecasts. Source: IMF Regional Economic Outlook, October 2023.*

1.2.2 Financial Markets

Overall financial market sentiment has remained positive on balance given the expected global recovery. However, the increasing number of concerns such as the Russia/Ukraine war, persistence of inflation and central-bank tightening have triggered mixed feeling in the equity market. Despite the relative strength of the US economy S&P 500 companies reported their third consecutive quarter of negative year-over-year earnings growth in the second quarter of 2023. S&P 500 earnings dropped 5.2% year-over-year in the second quarter, the largest earnings decline for the market since the third quarter of 2020. As for The MSCI Europe index, it dropped by 2.2% in August, dragged down by the banking sector after the Italian government announced a tax on banks' "excess" profits.

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



Source: Bloomberg.

2 DEVELOPMENTS IN THE FINANCIAL AND NON-FINANCIAL SECTORS

HIGHLIGHTS

As at end-June 2023

Financial Sector % of GDP	Number of Licenses	Banking Sector Assets
17.3%	363	USD 226.0 bn ▲ 0.3% YoY

Retail Banking Assets	Wholesale Banking Assets	Islamic Banking Assets
USD 101.7 bn ▲ 0.1% YoY	USD 124.3 bn ▲ 0.7% YoY	USD 37.7 bn ▲ 6.8% YoY

M2	Personal Credit	Business Credit
BD 14.5 bn ▲ 4.7% YoY	BD 5.9 bn ▲ 5.0% YoY	BD 5.1bn ▼ 0.3% YoY

- The size of the assets of the banking sector in Bahrain continued to grow reaching USD 226.0 billion as of June 2023.
- The retail banking sector assets increased to USD 101.7 billion and wholesale banking sector assets increased to USD 124.3 billion representing 45.0% and 55.0% respectively.
- The volume of credit increased by 3.6% to BD 11.3 billion in December 2022
- Household debt ratio witnesses an increase while business debt decreases.
- As of end of June 2023, outstanding Loans to SMEs represented 9.4% of total business lending and 4.1% of total lending.

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 on the their customers (households and business enterprises) and their vulnerabilities to changes in the economic environment. Not only are they sources of deposits, they represent major sources of demand for financial sector products and services.

2.2 Financial Sector Developments

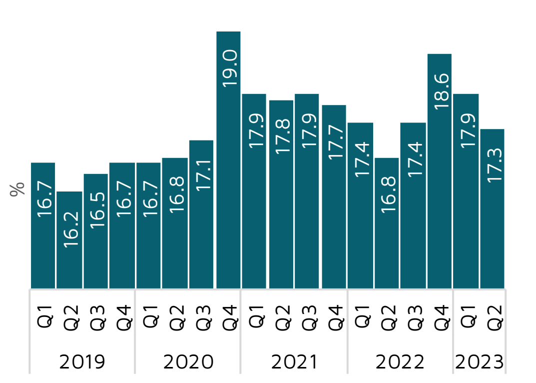
Bahrain's position as a regional financial center is essential to the development of its economy where the financial sector plays a significant role in economic activity and employment creation. The financial sector is the largest non-oil contributor to GDP representing 17.3% of real GDP in Q2 2023 (compared to 17.5% in 2022, 17.7% in 2021, 17.1% in 2020). As of end of June 2023 there were 363 licenses issued by CBB (bank and non-bank financial institutions). The banking sector in Bahrain was made up of 86 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: 55 wholesale banks that include 47 conventional (12 locally incorporated and 35 branches) and 8 Islamic wholesale banks.

The 271 non-banking financial institutions operating in Bahrain include investment business firms, insurance companies (including Takaful and Re-Takaful firms), representative offices and specialized licenses.

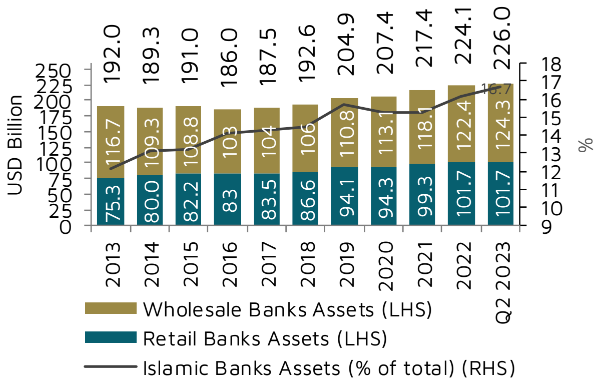
The size of the assets of the banking sector in Bahrain was USD 226.0 billion as of June 2023 (0.4% YoY increase). Growth in Retail and Wholesale banking continued in 2022 with YoY growth of 0.1% and 0.7% respectively. As for the Islamic banking sector, it grew steadily with a 6.8% YoY growth and represented 16.7% of the size of the banking sector.

Chart 2.1: Size of the Financial Sector to Real GDP



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

Chart 2.2: Banking Sector Asset Composition

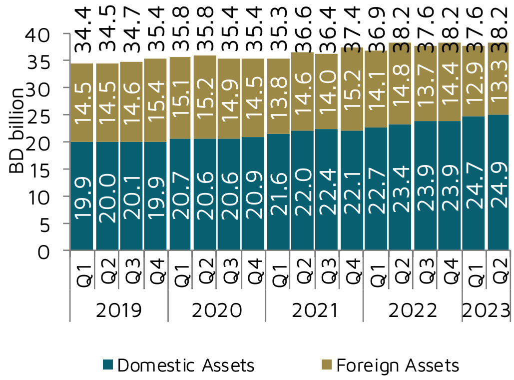


Source: CBB Monthly Statistical Bulletin.

2.2.1 The Retail Banking Sector

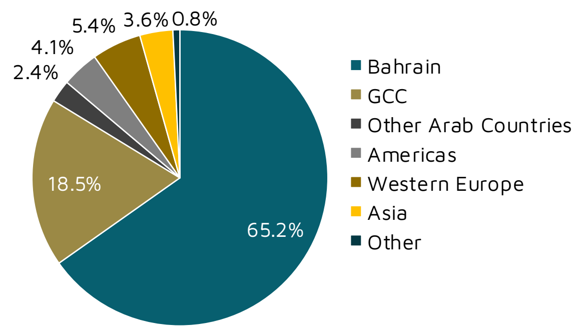
Retail banking assets continued to grow reaching BD 38.2 billion (USD 101.7 billion) in June 2023 with a 0.1% year-on-year (YoY) increase (see Chart 2.3). As of June 2023, domestic assets comprised 65.2% of total assets with a YoY growth of 6.7% while foreign assets comprised 34.8% of total assets with a YoY decline of 10.4%.

Chart 2.3: Retail Banks' Assets



Source: CBB Monthly Statistical Bulletin.

Chart 2.4: Retail Banks' Assets (%) by Geographical Classification (June 2023) *



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

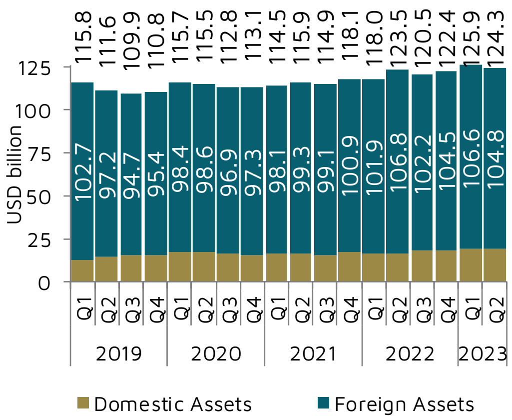
According to the geographical classification of the retail banking sector in Bahrain, the sector is exposed to foreign risk regionally from GCC countries and lightly exposed to Western Europe and U.S as the share of GCC assets of total retail banking assets was 18.5% and European and the Americas contribution was 9.5%.

2.2.2 The Wholesale Banking Sector

The size of the wholesale banking sector increased to USD 124.3 billion in June 2023 with a YoY growth of 0.7%. As of June 2023, domestic assets represented 15.7% of total assets and witnessed a YoY growth of 17.0% while foreign assets made 84.3% of total assets with a 1.8% YoY decrease in assets. (See Charts 2.5).

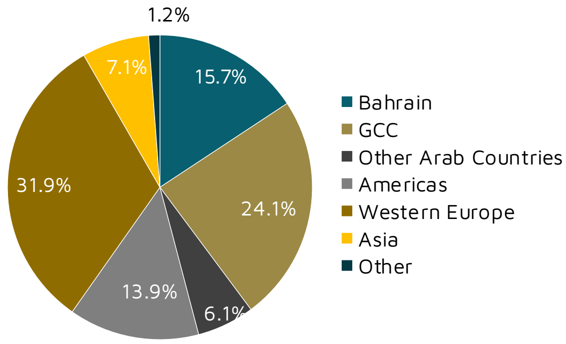
According to the geographical classification of wholesale banks' assets, wholesale banks are exposed to foreign risk from Western Europe and GCC countries. The share of GCC assets decreased to 27.3% in December 2022, which used to represent the larger portion of wholesale bank assets. The share of Western Europe's total assets increased to 31.9%, making it the largest portion of wholesale bank assets. The share of America's total assets increased to 13.9% and Asian assets increased to 7.1% in June 2023.

Chart 2.5: Wholesale Banks' Assets



Source: CBB Monthly Statistical Bulletin.

Chart 2.6: Wholesale Banks' Assets by Geographical Classification (June 2022) *

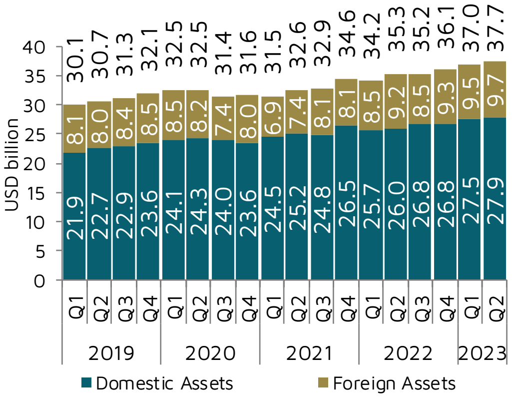


** For conventional and Islamic wholesale banks.*
Source: CBB Monthly Statistical Bulletin.

2.2.3 The Islamic Banking Sector

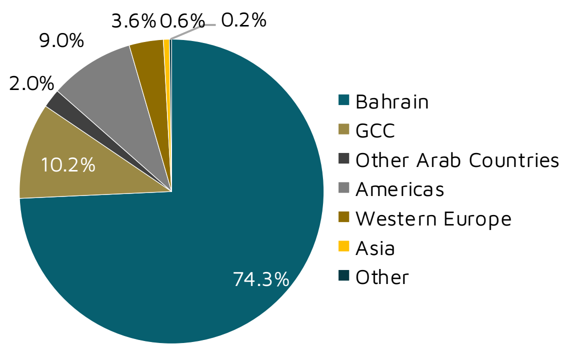
The size of the Islamic banking sector increased to USD 37.7 billion as of June 2023 indicating a 6.8% YoY increase. Domestic assets represented 74.2% of total Islamic banking assets in the sector (7.4% YoY increase) while foreign assets represented 25.8% of total Islamic banking assets (14.8% YoY increase). Islamic banks continue to be majorly exposed to domestic risks as the share of Bahrain's total assets decreased to 74.3% in December 2022 followed by the GCC (10.2%).

Chart 2.7: Islamic Banks' Assets



Source: CBB Monthly Statistical Bulletin.

Chart 2.8: Islamic Banks' Assets by Geographical Classification (June 2023)



Source: CBB Monthly Statistical Bulletin.

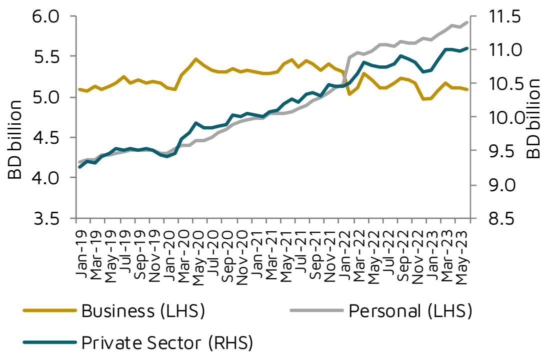
2.2.4 Islamic Windows

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 Sharia-compliant banking. As of June 2023, there were 5 Islamic windows operating by conventional retail licenses in Bahrain with total assets of BHD 4.6 billion (12.0% of retail banking assets). As of June 2023, 36.1% of total assets were domestic (48.9% YoY increase) while 63.9% were foreign (525.8% YoY increase).

2.3 Credit Developments

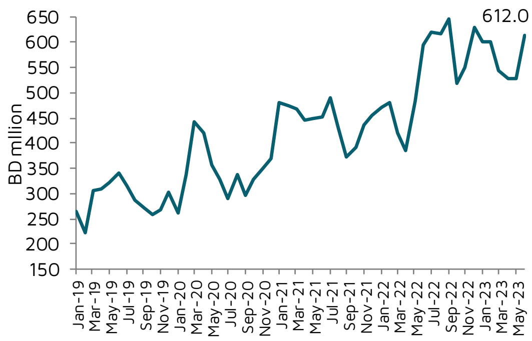
Domestic credit by retail banks increased from BD 11.3 billion in June 2022 to BD 11.6 billion in June 2023 with 2.5% YoY increase. Credit given to the private sector (business and personal) witnessed a YoY increase of 2.5% moving from BD 10.8 billion in June 2022 to BD 11.0 billion in June 2023 (Chart 2.9). Business lending contributed 43.8% of total lending and personal lending contributed 51.0%. The personal sector was the main driver of the growth in credit financing in 2022 led mainly by mortgage lending. Regarding retail banks' lending to the general government, there was an increase of BD 18.9 million (3.2% YoY increase) at end-June 2023 reaching BD 612.0 million (Chart 2.10).

Chart 2.9: Loans to the Private Sector*



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

Chart 2.10: Loans to General Government*

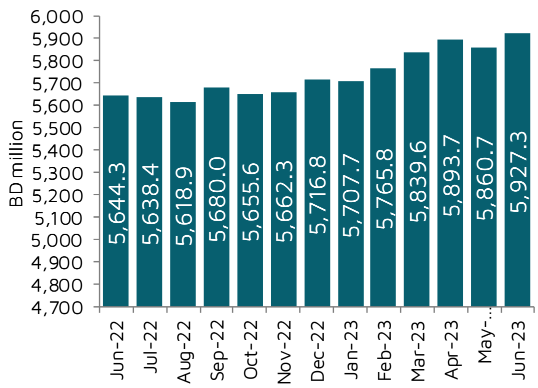


Source: CBB Monthly Statistical Bulletin.
** Excluding securities.*

2.3.1 The Households/Personal Sector

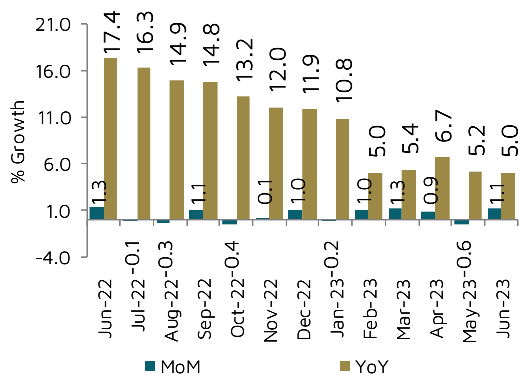
The household/personal sector in Bahrain plays an important role in financial stability and the overall economy. Outstanding personal loans, used as a proxy for household borrowing, shows an increase of 5.0% in 2022 reaching BD 5.9 bilion (Chart 2.11). Personal loans as a percentage of GDP decreased to 35.5% by June 2023.

Chart 2.11: Personal Loans



**Using 2022 forecasted GDP.*
Source: CBB Monthly Statistical Bulletin.

Chart 2.12: Growth Rates of Total Personal Loans and Advances (%)



Source: CBB Monthly Statistical Bulletin

The monthly growth rate in total personal loans and advances fluctuated in 2022 and the first half of 2023. It rose to reach its highest level for the year of 1.3% in March 2023 and later fell to reach -0.6% in May 2023. On a yearly basis, the biggest YoY increase was in June 2022 where the personal loans and advances were at 17.4% which then dropped to 5.0 in June 2023.

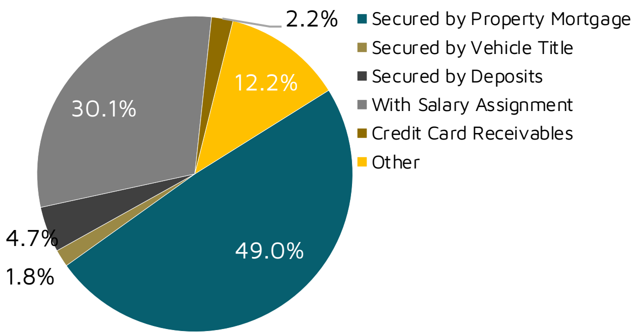
The two main contributors to personal loans remain to be personal loans secured by property mortgages which made up 49.0% of the total personal loans followed by personal loans secured with salary assignments at 30.1% of total personal loans.

Table 2.1: Personal Loans Breakdown

BD million	2019	2020	2021	2022	Q2 2023	% YoY
Total	**4,296.2**	**4,717.3**	**5,110.7**	**5,716.8**	**5,927.3**	**5.0**
Secured by Property Mortgage	1,953.2	2,197.9	2,261.5	2,760.8	2,905.7	8.1
Secured by Vehicle Title	123.0	118.1	109.2	106.6	105.6	-3.5
Secured by Deposits	140.1	187.6	133.7	129.4	277.6	115.7
With Salary Assignment	1,577.4	1,700.4	1,933.0	1,915.0	1,783.7	-11.3
Credit Card Receivables	104.0	92.2	99.5	84.2	130.7	28.4
Other	398.5	421.1	573.8	720.8	724.0	19.7

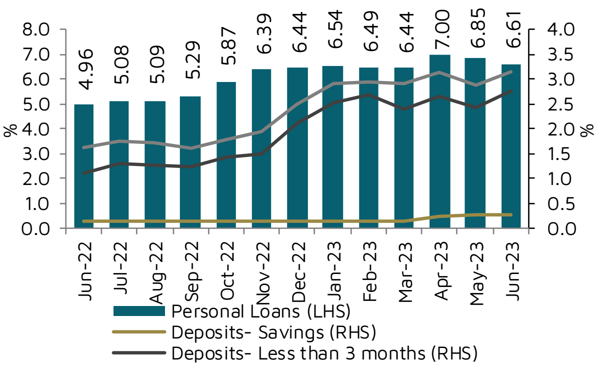
Source: CBB Monthly Statistical Bulletin.

Chart 2.13: Personal Loans Breakdown (June 2023)



Source: CBB Monthly Statistical Bulletin.

Chart 2.14: Retail Banks- Average Interest Rates on Personal Loans and Deposits (%)



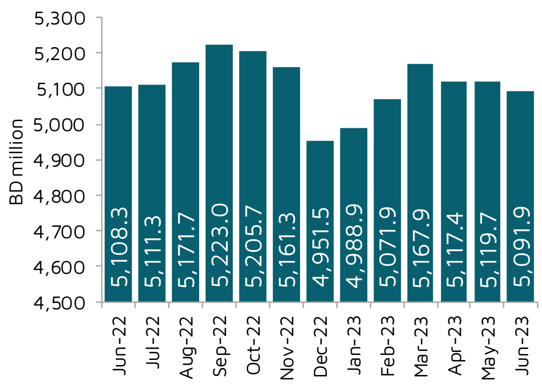
Source: CBB Monthly Statistical Bulletin.

Interest rates on personal loans started off at 4.96% in June 2022 and increased to 6.44% in December 2022 (Chart 2.17). 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. The increase in rates is a reflection the CBB raising its key policy interest rate multiple times throughout 2022.

2.3.2 The Bahraini Corporate/Business Sector

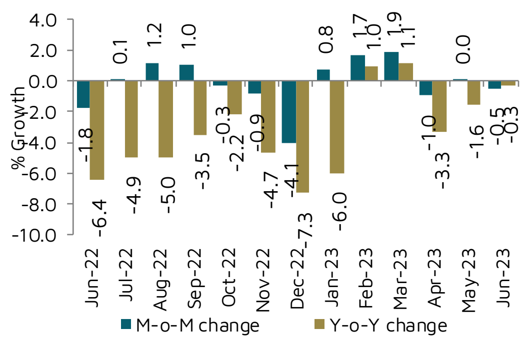
Business loans and advances contracted by 0.3% between June 2022 and June 2023 from BD million 5,108.3 in June 2022 to BD million 5,091.9 (Chart 2.18). Outstanding business loans as a percentage of GDP decreased to 30.5% in June 2023.

Chart 2.15: Business Loans



Source: CBB Monthly Statistical Bulletin.

Chart 2.16: 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 2022 and June 2023. Initially -1.8% in June 2022 it increased to reach its highest level for the year 1.9% in March 2023 before falling to -0.5% in June 2023. The highest YoY growth was March 2023 (1.1%).

The biggest contributors to business loans in December 2022 were the construction and real estate sector (31.4%) followed by manufacturing (23.5%), and then trade (15.5%) (Chart 2.20).

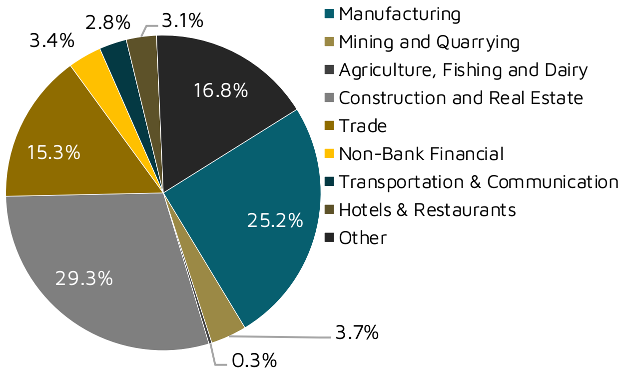
Table 2.2: Business Loans by Sector

BD million	2019	2020	2021	2022	Q2 2023	% YoY
Total	**5,138.6**	**5,326.9**	**5,341.2**	**4,951.5**	**5,091.9**	**-0.3**
Manufacturing	1,068.1	1,173.8	1,292.3	1,221.3	1,364.8	10.2
Mining and Quarrying	86.7	150.8	74.7	145.1	199.5	61.5
Agriculture, Fishing and Dairy	6.7	12.1	13.2	16.6	16.3	8.6
Construction and Real Estate	1,841.4	1,932.0	2,009.6	1,651.7	1,587.7	-6.0
Trade	1,071.0	934.4	903.9	814.0	828.2	-8.0
Non-Bank Financial	251.8	227.5	169.5	169.2	186.2	14.3
Transportation & Communication	127.2	209.0	147.5	144.7	152.3	-2.9
Hotels & Restaurants	151.6	188.1	196.1	161.4	167.5	-2.0
Other Sectors	534.1	499.2	534.4	627.5	909.2	-7.0

Source: CBB Monthly Statistical Bulletin.

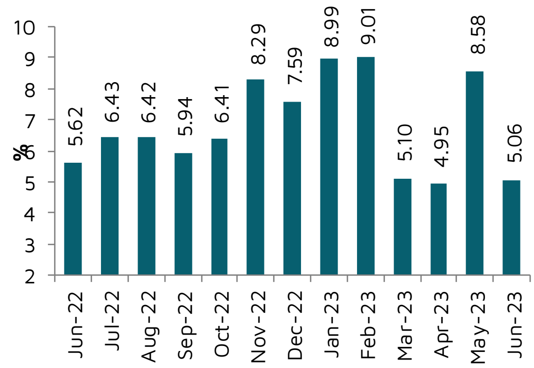
Average interest rates on business loans fluctuated throughout the first half of 2023, but had an overall decreasing trend. It was at its peak in February 2023 at 9.01% and reached 5.06% in June 2023 (Chart 2.21).

Chart 2.17: Business Loans by Sector (June 2023)



Source: CBB Monthly Statistical Bulletin.

Chart 2.18: Retail Banks' Average Interest Rates on Business Loans



Source: CBB Monthly Statistical Bulletin.

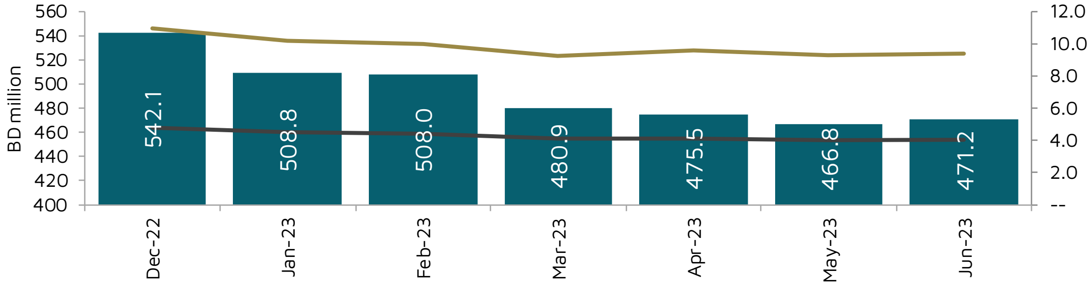
2.3.3 SMEs

The Kingdom of Bahrain has been able to establish a number of institutional frameworks to create an ecosystem conducive for start-ups and for the growth of small- and medium-sized enterprises (SMEs). CBB regonizes the role that SME's play in the economic growth in Bahrain and the importance of funding requiremed to help the sector

Within the Financial Sector Development Strategy 2022-2026, the CBB has indicated its efforts in strengthening of financing mechanisms available SMEs. CBB continues its efforts with the banking sector to help to make SME financing more accessible and affordable by encouraging banks to lend more to SMEs to help boost further the growth of the SME sector, which is a vital part of the Bahraini economy.

As of end of June 2023, outstanding Loans to SMEs were BD 471.2 million representing 9.4% of total business lending and 4.1% of total lending.

Chart 2.19: SME Loans



Source: CBB Monthly Statistical Bulletin.

2.4 Monetary Indictors

Money supply continued to grow in 2022. M2 stood at BD 14,456.3 million in June 2023, 4.7% higher than its value of June 2022. M3 was at BD 15,718.0 million in June 2023, 3.0% higher than in June 2023 (Table 2.1). Table 2.3 sets out an analysis of Bahrain's M1, M2 and M3 money supply as at the dates indicated.

Table 2.3: Money Supply Composoition

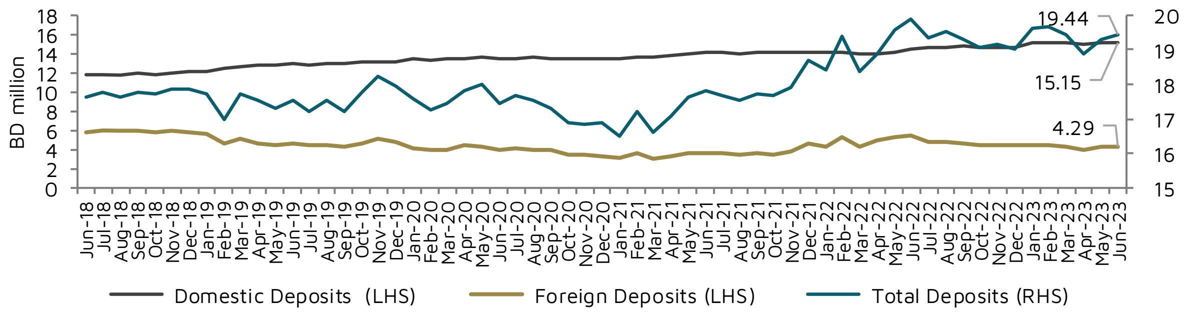
BD million	2019	2020	2021	2022	Q2 2023	% YoY
Currency Outside Banks	535.1	593.0	558.0	506.5	563.5	(0.1)
Demand Deposits	2978.5	3.288.0	3,952.0	3,398.5	2,989.1	(30.5)
M1	**3,513.6**	**3,880.9**	**4,510.0**	**4,214.0**	**4,142.1**	**(14.1)**
Time & savings deposits	8,538.6	8,959.0	8,955.4	10,079.7	10,903.7	22.0
M2	**12,052.2**	**12,840.0**	**13,465.4**	**13,984.8**	**14,456.3**	**4.7**
General Government Deposits	1,619.7	1,311.3	1,418.8	1,150.6	1,261.7	(13.7)
M3	**13,671.9**	**14,151.3**	**14,884.2**	**15,135.4**	**15,718.0**	**3.0**

Source: CBB Monthly Statistical Bulletin.

As of June 2023, growth in money supply was stimulated by a growth in savings deposits. Time and savings deposits increased by 22.0% from BD 10,079.7 million in December 2022 to BD 10,903.7 million in June 2023, while demand deposits decreased below December 2021 levels.

Total deposits reached BD 19.4 billion in June 2023 with a 2.3% YoY decrease (where domestic deposits represent 77.9% of total deposits and had a YoY increase of 5.2% During 2022, savings were boosted with increases in time deposits as customers were benefiting from the higher interest rates on deposits. Deposits continued a gradual upwards trajectory in line with the growth of the economy.

Chart 2.20: Total Deposits (BD billion)



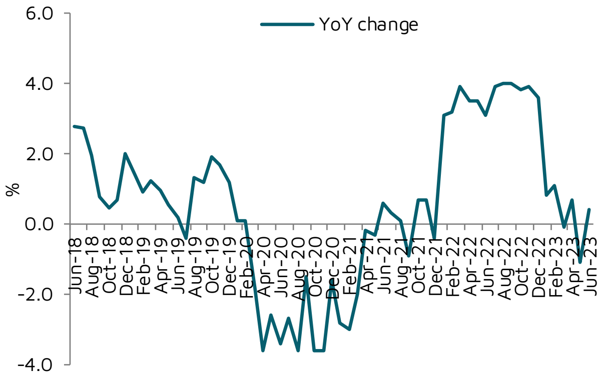
Source: CBB Monthly Statistical Bulletin.

2.5 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]

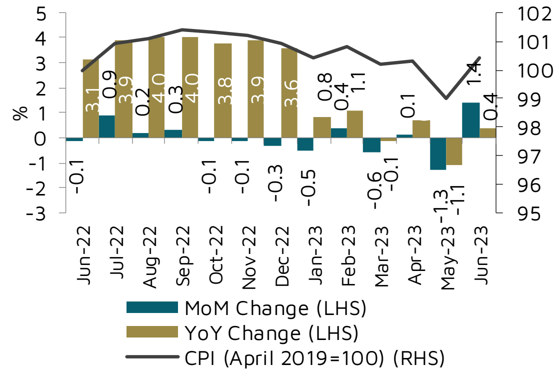
As of June 2023, the Consumer Price Index (CPI) increased to 100.4 points. The annual average rate of inflation in 2022 was 3.6% (compared to a decrease of 0.6% for 2021). The largest year-on-year price increase was recorded in January 2023 when prices increased by 0.8% January 2022.

Chart 2.21: CPI Change (Jun. 2019 – Jun. 2023)



Source: IGA.

Chart 2.22: Monthly Inflation Rate (Jun. 2022 –Jun. 2023)



Source: IGA.

The divisions which made the largest upward contribution to the CPI in June 2023 were the food and non-alcoholic beverages group and alcoholic beverages and tobacco. The increase in food and beverages is reflection of how supply chain disruptions due to the geopolitical events impacted the price of imported goods.

[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.

Box 1: CBB Key Interest Rates

Central banks around the world have continued increasing their key policy interest rates in 2023, in order to continue offseting the global inflationary pressures. In line with global rising rates the CBB raised the key policy interest rate 1-week deposit facility four times in 2023 as seen below.

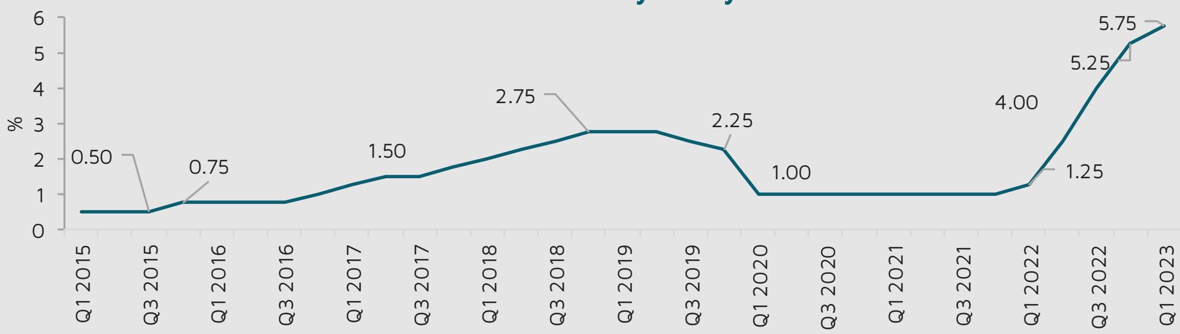
Box 1 Table 1- CBB Policy Rates

	1- Night	1- week	4- weeks	Lending Rate
Mar. 16,2022	1.00%	1.25%	1.75%	2.50%
May 4, 2022	1.50%	1.75%	2.50%	3.00%
Jun. 15 2022	2.25%	2.50%	3.25%	3.75%
Jul. 27 2022	3.00%	3.25%	4.00%	4.50%
Sep. 21, 2022	3.75%	4.00%	4.75%	5.25%
Nov. 2, 2022	4.50%	4.75%	5.50%	6.00%
Dec. 14, 2022	5.00%	5.25%	6.00%	6.50%
Feb. 1, 2023	5.25%	5.50%	6.25%	6.75%
Mar. 22, 2023	5.50%	5.75%	6.50%	6.75%
May 3, 2023	5.75%	6.00%	6.75%	7.00%
Jul. 26, 2023	6.00%	6.25%	6.75%	7.00%

Source: CBB.

The move by the Bahrain was to maintain their currency's pegs to the US dollar. The exchange rate peg provides an anchor for monetary policy, which contributes to controlling inflation and protecting the external value of the currency.

Box 1 Chart 1- CBB Key Policy Rates



Source: CBB.

By raising the benchmark interest rate that banks use in lending money to each other, tighter monetary policy makes consumer and business loans more expensive and harder to get. Lowers demand for credit-financed goods and services, and in time also lowers inflation. Looking forward, unsustainable trends, such as the continued expansion in retail lending, is expected to reverse as we enter into an era of higher interest rates and costlier borrowing.

CBB continues to monitor how the high-rate environment might impact borrowers' creditworthiness and their ability to repay. Banking system is well capitalized with stable non-performing facilities.

PART II:
DEVELOPMENTS IN THE BANKING SECTOR

3 PERFORMANCE OF THE BANKING SECTOR

HIGHLIGHTS

Q2 2023

CAR	Tier 1 CAR	Assets-to-Capital
19.3%	17.8%	9.0
▲ 0.2% YoY	▲ 0.1% YoY	▲ 0.3 YoY

NPL Ratio	Specific Provisions Ratio	ROA
3.1%	61.8%	0.7%
▼ 0.2% YoY	▼ 8.1% YoY	▲ 0.1% YoY

ROE	Liquid Asset Ratio	Loan/Deposit Ratio
5.3%	23.4%	63.2%
▲ 0.5% YoY	▼ 2.3% YoY	▼ 2.5% YoY

- Increase in capital positions. Capital positions remain strong.
- Improvement in asset quality with continued decreasing trend in NPL ratio.
- Loan portfolios remain concentrated in some sectors with no significant change from the previous quarter.
- Stabile positive 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. Annex 1 and Annex 2 presents selected FSIs for the different banking segments. [3]

[2] Chapters 3, 4, and 5 cover the period between Q4 2021 and Q4 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).

Despite recent global macroeconomic developments in regard to inflationary pressures and monetary tightening, there was no impact on the Bahraini banking sector. Capital and liquid positions remained strong during the peak of COVID-19 related volatility and Bahraini banks' profitability continued to improve post-COVID. FSIs continued to show ample levels of capital and liquidity, low levels of defaults and adequate levels of provisions coverage.

CBB conducted liquidity stress tests of Bahraini retail banks that showed overall banking sector stability. The tests assessed the resilience of the banks against the backdrop of market uncertainty and the banking sector crisis in March 2023. Results indicated that the overall banking system can withstand these hypothetical adverse scenarios.

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 19.3% in June 2023 increasing by 0.2% compared to June 2022. The core capital ratio (ratio of Tier 1 capital to risk-weighted assets) showed an increase from 17.7% June 2022 to 17.8% in June 2023. Whereas the leverage ratio (ratio of assets over capital) increased to 9.0 times during the same period.

Table 3.1: Capital Provision Ratios

Indicator*	Q2 2022	Q4 2022	Q2 2023	YoY Change
CAR (%)	19.1	19.5	19.3	0.2
Tier 1 CAR (%)	17.7	18.1	17.8	0.1
Assets/Capital (Times)	8.7	8.2	9.0	0.3

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

3.2.2 Asset Quality

Continued improvement in asset quality with decreasing NPL and strong provisions

The non-performing loans (NPLs) ratio continued its decrease reaching 3.1% in June 2023 from 3.3% in June 2022. The CBB continues to monitor 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 businesses that suffered temporary cash-flow concerns, preventing any deterioration in asset quality. There has been no major effect of the lifting of the loan deferments on the asset quality and CBB has been monitoring the NPL ratios of retail Banks and financing companies since the end of the loan deferral program.

The specific provisions as a proportion of NPLs continued to fall, decreasing to 61.8% in June 2023 from 69.9% in June 2022. Faced with an increase in credit risk, licensees took larger provisions as they were required to assess credit exposures. The CBB requested them to be more prudent in determining any additional provision during the pandemic that resulted in an increase in provisioning. Banks have been gradually reducing their provisions to pre-pandemic levels as the economic outlook and business activity improved.

Table 3.2: NPL Ratios (Q4 2022)

Indicator	Q2 2022	Q4 2022	Q2 2023	YoY Change
NPLs (% Total Loans)	3.3	3.0	3.1	-0.2
Specific provisions (% of NPLs)*	69.9	68.5	61.8	-8.1

Source: CBB.

[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.

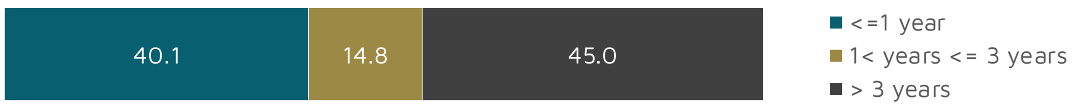
Data on NPLs by time segment (up to 1 year, 1 year to 3 years, and over 3 years) show that the majority of NPLs in the banking sector are for a period of over 3 years (55.2% of total NPLs). NPLs for over 3 years represented 1.4% of total gross loans. Specific provisioning for NPLs decreases as they are non-performing for longer periods of time. As seen in Table 3.3, NPLs for a period of more than 3 years are provisioned by 71.6%.

Table 3.3: NPL Ratios and Specific Provisions by Time Period (Q2 2023)

Indicator	Up to 1 year	1 up to 3 years	Over 3 years	Total
NPLs (% Total Loans)	1.2	0.5	1.4	3.1
Specific Provisions (% of NPLs)	47.1	71.9	71.6	61.8

Source: CBB.

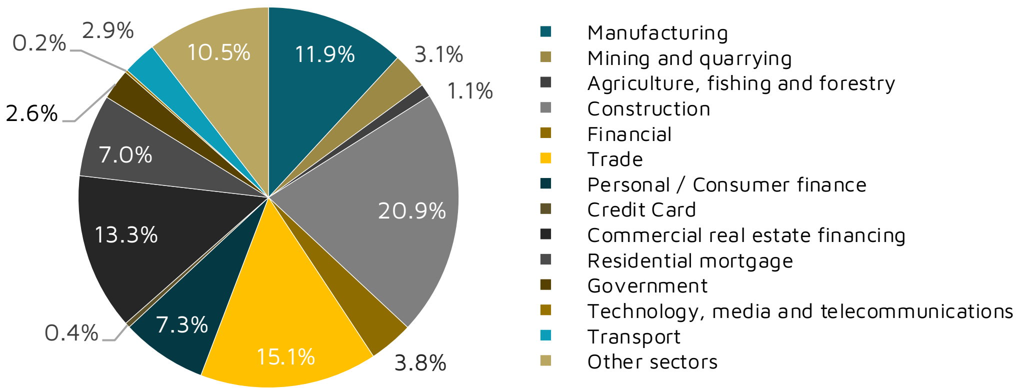
Chart 3.1: NPLs by Time Period (%)



Source: CBB.

The NPLs were concentrated in construction (20.9%), trade (15.1%) and commercial real estate financing (13.3%) as indicated in chart 3.2. [5]

Chart 3.2: NPLs Concentration by Sector (Q2 2023)



Source: CBB.

Data on the sectoral breakdown of NPLs ratios (NPLs per sector as a percentage of gross loans in each sector) shows an increase in impairment in some sectors, while some experience a decrease and others remain unchanged (Table 3.4). The highest increase was in commercial real estate financing by 1.8%. The highest decrease was in the mining and quarrying sector which was 6.9%.

Table 3.4: NPL Ratios by Sector (%)

Sector	Q2 2022	Q4 2022	Q2 2023	YoY Change
Manufacturing	4.9	3.8	2.8	-2.1
Mining and quarrying	11.7	5.9	4.8	-6.9
Agriculture, fishing and forestry	1.6	2.0	2.4	0.8
Construction	5.6	7.0	6.8	1.2
Financial	1.3	0.7	0.7	-0.6
Trade	7.8	6.6	6.2	-1.6
Personal / Consumer finance	2.4	2.2	2.3	-0.1
Credit Card	5.1	2.6	2.9	-2.2
Commercial real estate financing	2.8	2.7	4.6	1.8
Residential mortgage	4.3	3.5	3.8	-0.5
Government	0.6	0.4	1.2	0.6
Technology, media and telecommunications	0.9	1.1	0.4	-0.5
Transport	3.2	3.5	3.1	-0.1
Other sectors	2.7	2.6	2.3	-0.4

Source: CBB.

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

Loan portfolios faces slight fluctuations and remain concentrated in some sectors

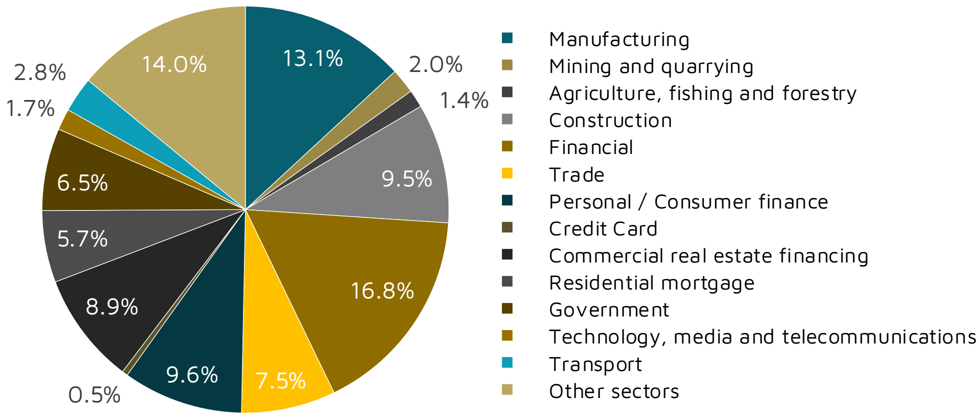
The loan portfolio of the banking system remains concentrated in some sectors yet no sector exceeding 20% of total loans. Financial represented the highest exposure with 16.8% of total loans in June 2023. Manufacturing followed with 13.1% and personal/consumer finance stood at 9.6% of total loans.

Table 3.5: Lending Distribution (% Total Loans)

Sector	Q2 2022*	Q4 2022*	Q2 2023*	YoY Change
Manufacturing	13.1	12.4	13.1	0.0
Mining and quarrying	1.1	1.6	2.0	0.9
Agriculture, fishing and forestry	1.5	1.4	1.4	-0.1
Construction	10.0	10.1	9.5	-0.5
Financial	14.8	15.0	16.8	2.0
Trade	6.6	6.5	7.5	0.9
Personal / Consumer finance	9.8	9.7	9.6	-0.2
Credit Card	0.4	0.5	0.5	0.1
Commercial real estate financing	9.4	9.2	8.9	-0.5
Residential mortgage	6.0	6.2	5.7	-0.3
Government	6.6	7.3	6.5	-0.1
Technology, media and telecommunications	1.7	1.8	1.7	0.0
Transport	3.1	2.9	2.8	-0.3
Other sectors	15.9	15.3	14.0	-1.9
Top Two Sectors (%)	30.8	30.3	30.8	0.0
Real Estate/ Construction Exposure (%) **	25.4	25.6	24.1	-1.3

** 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.

Chart 3.3: Lending Distribution (% Total Loans)



Source: CBB.

The top two recipient sectors, financial and other sectors, jointly represented 30.8% of loans in June 2023, a slight increase from the 30.8% in June 2022. Exposure to real estate/construction was 24.1% of total lending in June 2023, a moderate decrease from 25.4% registered in June 2022.

3.2.3 Profitability

Profitability remains positive

The overall banking sector's profitability indicators have been stable between June 2022 to June 2023 and remain robust. Return-on-assets (ROA) increased to 0.7% in June 2023 from 0.6% in June 2022. As of June 2023, return-on-equity (ROE) increased to 5.3% from 4.8% in June 2022. Net interest income (as a % of total income) stood at 66.9% in June 2023. In addition, operating expenses as a proportion of total income was 44.4% in June 2023, a decrease from the 46.1% registered in June 2022.

Table 3.6: Profitability

Indicator	Q2 2022	Q2 2023	YoY Change
ROA (%) *	0.6	0.7	0.1
ROE (%) **	4.8	5.3	0.5
Net Interest Income (% Total Income) ***	68.6	66.9	-2.0
Operating Expenses (% Total Income)	46.1	44.4	-1.7

** 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.

3.2.4 Liquidity

Liquidity positions remain comfortable.

Between June 2022 and June 2023, the overall loan-deposit ratio decreased from 65.7% to 63.9%. Liquid assets as a proportion of total assets remain stable at 23.7% over the same period.

Table 3.7: Liquidity

Indicator	Q2 2022	Q4 2022	Q2 2023	YoY Change
Liquid Asset Ratio (%)	25.7	25.3	23.4	-2.3
Loan-Deposit Ratio (%)	65.7	68.5	63.2	-2.5

Source: CBB.

Liquidity indicators such as liquidity coverage ratio (LCR) and net stable funding ratio (NSFR) remained above CBB's requirements and guidelines. LCR for locally incorporated retail banks (conventional and Islamic) was 369.9% and NSFR was 144.8%.

3.3 Developments in Regulation and Initiatives

The following section sheds light on the regulatory and policy initiatives that took place in 2023 for the banking and financial sector:

Table 3.8: Key Banking Sector Regulatory and Policy Developments 2023

Item	Description
Amendments to the Credit Risk Management Module (Module CM)	The CBB in January 2023, amended Module CM requiring banks to calculate Expected Credit Loss using the methodology under IFRS 9 for exposures to sovereigns which were previously subject to impairment loss assessments using the sovereign debt matrix.
Amendments to the Financial Crime and AML Modules (Module FC & AML)	The CBB in January 2023, introduced amendments to Module FC and AML for all licensees, requiring them to report to CBB any assets frozen or actions taken in compliance with the prohibition requirements of the relevant UNSCRs, including attempted transactions.
Guidance Paper – Trade-Based Money Laundering	The CBB in February 2023, issued a guidance paper to all licensees to assist financial institutions in understanding trade-based money laundering and the means of identifying suspicious activities associated with it.
Amendments to the Capital Adequacy Module (Module CA)	The CBB in February 2023, amended Module CA reducing the minimum capital requirement for category 3 investment firms to BD 25k and requiring them to maintain adequate liquid funds to cover its operating expenses.
Amendments to the Credit Risk Management Module (Module CM)	The CBB in February 2023, issued amendments to Module CM for all retail banks and financing companies which included classifying purchased or originated credit impaired (POCI) facilities as part of non-performing exposures and amendments to the criteria for re-categorisation of non-performing exposures to performing.
Revised High Level Controls Module (Module HC)	The CBB in March 2023, issued a revised Module HC for all banks, which is in line with the Basel Committee on Banking Supervision Paper "Principles of Corporate Governance". The CBB in June 2023, also issued revised Module HC for all investment firms.
Amendments to Crypto-asset Module (Module CRA)	The CBB in March 2023, issued amendments to Module CRA which included a new Chapter on digital token offerings, revisions to the

	definitions of crypto-assets and enhancements to the cyber security requirements.
Amendments to General Requirements Module (Module GR) and	The CBB in March 2023, issued amendments to Module GR applicable to all banks on the requirement to submit additional information for CBB's prior approval of proposed cash or stock dividends.
Amendments to General Requirements Module (Module GR)	The CBB issued in June 2023 revised "Appointed Representatives Requirements" in Module GR of CBB Rulebook Volume 3 for all insurance firms. The amendments require greater accountability for overseeing and managing their appointed representatives.

Box 2: ESG Disclosure Guidelines

The ESG reporting landscape is in a state of constant change, as companies now face mounting pressure from investors, regulators, and other stakeholders to disclose information relating to their stance on climate change, social issues, and governance factors. This heightened interest has led to a surge in sustainable investments such as ESG funds and Green Bonds, as more and more investors recognize the significance of taking into account the financial and economic ramifications of ESG issues when making investment decisions.

As part of CBB's objective to maintain disclosure transparency and high corporate governance standards, in addition to its commitment to social and climate related goals, the CBB developed Environmental, Social, and Governance ("ESG") disclosure guidelines to assist companies with ESG integration and reporting against a broad range of environmental, social, and corporate governance factors.

Based on CBB's consultation dated 17th August 2023 and the industry feedback, the CBB is issuing the Environmental, Social and Governance Requirements Module (Module ESG) including ESG reporting requirements. The requirements apply for listed companies, all banks, all insurance firms, all financing companies, and all category 1 and 2 investment firms. The ESG reporting requirements are important for effective adoption of ESG frameworks which contributes to the Kingdom of Bahrain's commitment to Sustainable Development Goals.

The CBB views that ESG reporting is an effective tool for stakeholders to better examine a company's efficiency, sustainability, and risk exposure. The objective of issuing ESG reporting requirements is to establish a uniform framework for listed companies and licensees to disclose their ESG performance and sustainability efforts.

The CBB is aware that many companies are at different stages on their sustainability journey, and the goal is to provide information on important aspects of ESG reporting and offer a thorough approach to ESG reporting and are to be viewed in conjunction with relevant international best practices, frameworks, and guidelines.

Companies are needed to take steps to report the Key Performance Indicators (KPIs) using alternative methods or simplified reporting mechanisms where such disclosure would remain fair, clear and not misleading.

Under the newly issued ESG Module, listed companies and licensees must submit an ESG report to the CBB on an annual basis. The ESG report must incorporate the ESG KPIs. Branches of foreign financial institutions must either submit the ESG Report of their respective head offices or provide a separate report. Similarly, companies operating under a group governance framework must either submit the consolidated group ESG Report or provide a separate report.

The requirements are effective from year ending 31st December 2024 with the first report for the year ending 31st December 2024 is due in the year 2025.

4 PERFORMANCE OF CONVENTIONAL BANKS

HIGHLIGHTS

Q2 2023

	Retail		Wholesale	
CAR	21.7%	▲ 1.3% YoY	17.0%	▼ 0.7% YoY
Tier 1 CAR	20.3%	▲ 1.3% YoY	15.3%	▼ 0.9% YoY
Assets-to-Capital	6.8	▼ 0.5 YoY	10.3	▲ 0.8 YoY
NPL	3.6%	▼ 0.2% YoY	2.1%	▼ 0.4% YoY
Specific Provisions	66.7%	▼ 6.5% YoY	61.1%	▼ 8.5% YoY
ROA	0.9%	▲ 0.1% YoY	0.7%	▼ 0.1% YoY
ROE	7.1%	▲ 0.5% YoY	3.2%	▲ 0.9% YoY
Liquidity	30.9%	▼ 3.2% YoY	19.9%	▼ 2.0% YoY
Loan/Deposit	71.4%	▲ 1.3% YoY	62.1%	▼ 0.8% YoY

- Capital position of conventional retail slightly improves but deteriorates for conventional wholesale.
- Asset quality of conventional banks improves with decreasing NPLs.
- Loan portfolios in conventional retail and wholesale banks remain concentrated despite the decrease in some sectors.
- Slight increase in earnings for conventional retail banks and conventional wholesale banks.
- Liquidity declined for conventional banks, but they continue to have ample liquidity levels.

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, asset quality, profitability and liquidity. Unless specified otherwise, the analysis in this chapter is based on consolidated financial data (Bahraini and non-Bahraini operations).

4.2 Capital Adequacy

Conventional banks remain well capitalized.

The CAR for conventional retail increased from 20.4% in June 2022 to 21.7% in June 2023. The core capital ratio (ratio of Tier 1 capital to risk-weighted assets) also increased from

19.0% in June 2022 to 20.3% in June 2023. Assets over capital decreased by 0.5 during the same period to reach 6.8 times. The NPLs net provisions to capital decreased to 4.0% in June 2023 from 4.3% in June 2022.

As for wholesale banks, CAR decreased to 17.0% in June 2023 from the level of 17.7% it registered in June 2022. Tier 1 capital decreased to 15.3% in June 2023 from the level of 16.2% it recorded in June 2022. Furthermore, the leverage ratio (ratio of assets over capital) increased to 10.3 times in June 2023. Finally, the ratio of NPLs net of provisions to capital slightly decreased to 2.1% over the same period.

Table 4.1: Conventional Banks' Capital Provisions Ratios

Indicator *	Retail			Wholesale		
	Q2 2022	Q2 2023	Change	Q2 2022	Q2 2023	Change
CAR (%)	20.4	21.7	1.3	17.7	17.0	-0.7
Tier 1 CAR (%)	19.0	20.3	1.3	16.2	15.3	-0.3
Assets/Capital (Times)	7.3	6.8	-0.5	9.5	10.3	0.8
NPLs net of Provisions to Capital (%)	4.3	4.0	-0.2	2.5	2.1	-0.4

** 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 for retail banks

The NPL ratio decreased to 3.6% in June 2023 from 3.8% in June 2022 for conventional retail banks. Specific provisions as a proportion of NPLs decreased to 66.7% in June 2023. As for conventional wholesale banks, the NPL ratio decreased from 2.5% in June 2022 to 2.1% in June 2023. Specific provisions witnessed a decrease of 8.5% from 69.6% in June 2022 to 61.1% in June 2023.

Table 4.2: Conventional Banks' NPL Ratios

Indicator *	Retail			Wholesale		
	Q2 2022	Q2 2023	Change	Q2 2022	Q2 2023	Change
NPLs (% Total Loans)	3.8	3.6	-0.2	2.5	2.1	-0.4
NPLs Local Banks (%)	3.7	3.2	-0.5	3.4	2.4	-1.0
NPLs Overseas Banks (%)	4.0	4.7	0.7	1.9	1.8	-0.1
Specific Provisions (% of NPLs) *	73.2	66.7	-6.5	69.6	61.1	-8.5

Source: CBB.

Available data on the sectoral breakdown of NPLs shows most sectors experiencing an increase in impairment, while some experience a decrease (Table 4.3). For conventional retail banks, the highest increase was in mining and quarrying by 10.3% while the largest decrease was in manufacturing by 4.7%.

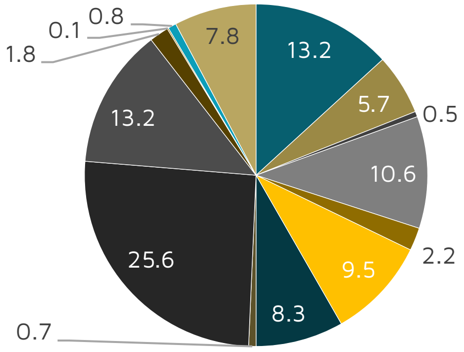
Table 4.3: Conventional Banks' NPL Ratios by Sector (%)

Sector	Retail			Wholesale		
	Q2 2022	Q2 2023	Change	Q2 2022	Q2 2023	Change
Manufacturing	8.2	3.5	-4.7	1.5	1.6	0.1
Mining and quarrying	54.4	64.7	10.3	4.9	0.7	-4.2
Agriculture, fishing and forestry	3.2	4.5	1.3	0.3	1.4	1.1
Construction	5.5	12.1	6.6	4.5	4.7	0.2
Financial	1.1	1.0	-0.1	0.8	0.5	-0.3
Trade	4.5	3.6	-0.9	8.0	4.6	-3.4
Personal / Consumer finance	1.8	2.1	0.3	4.0	3.6	-0.4
Credit Card	2.7	3.0	0.3	1.8	0.5	-1.3
Commercial real estate financing	2.7	4.9	2.2	3.1	2.9	-0.2
Residential mortgage	5.8	4.4	-1.4	0.8	0.5	-0.3
Government	2.2	1.4	-0.8	0.2	1.8	1.6
Technology, media and telecommunications	0.1	0.2	0.1	1.9	0.5	-1.4
Transport	1.4	2.1	0.7	3.9	3.2	-0.7
Other sectors	2.0	2.6	0.6	2.6	1.7	-0.9

Source: CBB.

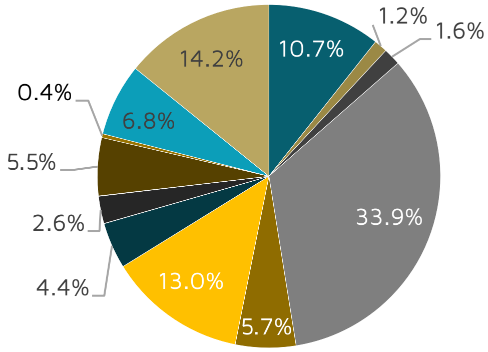
As for wholesale banks, sectoral breakdown of impaired loans demonstrates that impairment in construction loans was the highest between all sectors at 4.7%, followed by trade with an impairment of 4.6%. The biggest decrease in impairment was found in mining and quarrying with a decrease of 4.2%. Data on the concentration of NPLs by sector for conventional retail banks shows that the majority of NPLs come from the commercial real estate sector (25.6%), residential mortgage (13.2%), manufacturing (13.2%) and construction (10.6%). 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 (33.9%), others (14.2%), and trade (13.0%).

Chart 4.1: CR Banks' NPLs Concentration by Sector (June 2023)



Source: CBB.

Chart 4.2: CW Banks' NPLs Concentration by Sector (June 2023)



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

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 19.1% of total loans in June 2023 followed by personal/consumer finance representing 14.2%. Exposure to real estate/construction increased to 33.3% of total lending in June 2023. As for wholesale banks, lending remains concentrated in the financial sector and construction sector accounting for 24.1% and 15.1% respectively. Exposure to real estate/construction decreased to 17.0% of total lending in June 2023.

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

Sector	Retail			Wholesale		
	Q2 2022	Q2 2023	Change	Q2 2022	Q2 2023	Change
Manufacturing	13.5	13.7	0.2	13.9	14.1	0.2
Mining and quarrying	0.4	0.3	-0.1	1.9	3.6	1.7
Agriculture, fishing and forestry	0.4	0.4	0.0	2.7	2.4	-0.3
Construction	3.7	3.2	-0.5	16.3	15.1	-1.2
Financial	8.0	8.2	0.2	20.3	24.1	3.8
Trade	8.8	9.6	0.8	5.3	5.9	0.6
Personal / Consumer finance	14.7	14.2	-0.5	2.5	2.5	0.0
Credit Card	0.8	0.8	0.0	0.0	0.1	0.1
Commercial real estate financing	19.0	19.1	0.1	1.9	1.9	0.0
Residential mortgage	10.4	11.0	0.6	0.1	0.1	0.0
Government	3.7	4.7	1.0	8.2	6.5	-1.7
Technology, media and telecommunications	2.6	2.4	-0.2	1.5	1.6	0.1
Transport	2.0	1.3	-0.7	4.6	4.5	-0.1
Other sectors	12.1	11.0	-1.1	20.9	17.6	-3.3
Top Two Sectors (%)	33.7	33.3	-0.4	41.2	41.7	0.5
Real Estate/ Construction Exposure (%) **	33.1	33.3	0.2	18.3	17.0	-1.3

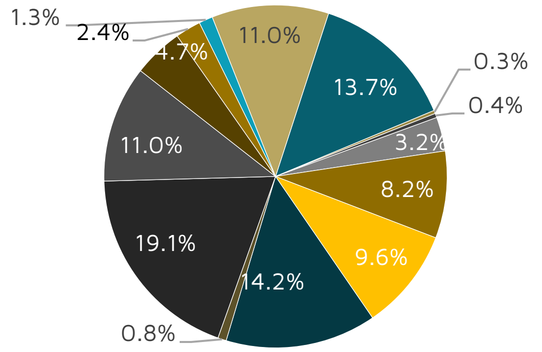
** Figures may not add to a hundred due to rounding.*

*** 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.

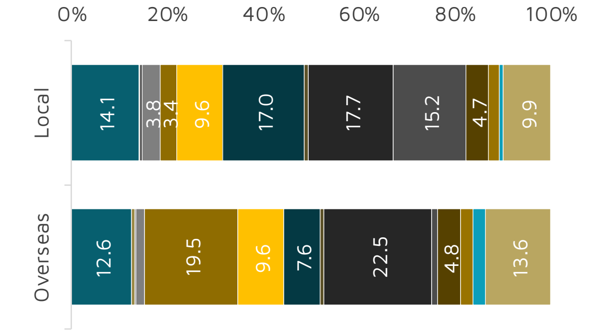
The loan portfolio of locally incorporated retail banks remains concentrated in some sector with the top recipient of loans being the commercial real estate financing sector (17.7%). Real estate/construction exposure decreased to 36.6%. Similarly, the overseas retail banks loan portfolio shows commercial real estate financing sector as the top sector (22.5%) and the exposure to real estate/ construction was 25.5% of total lending in June 2023.

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)

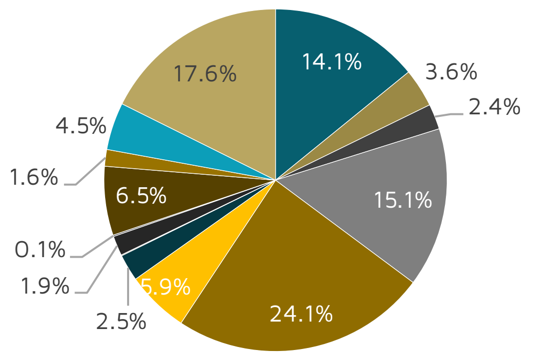


Source: CBB.

- Manufacturing
- 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

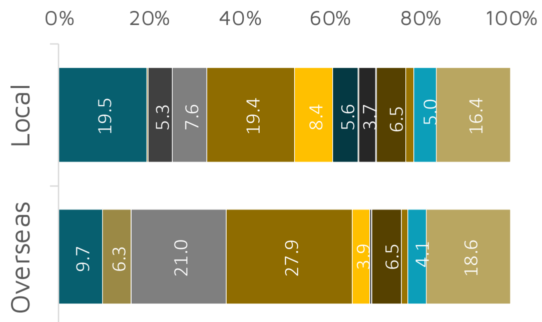
As for locally-incorporated wholesale banks, the top recipient of loans is the manufacturing sector (19.5%) and the real estate/ construction exposure was 11.6% for the same period. For overseas wholesale banks, the top recipient of loans in June 2023 was the financial sector (27.9%) and real estate/construction exposure decreased from 23.3% in June 2022 to 21.5% in June 2023.

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.

- 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

4.4 Profitability

Banks' profitability remains positive and at similar levels as last year

Profitability for conventional retail banks was positive, and, as at end-June 2023, ROA slightly increased to 0.9%. ROA for locally incorporated banks increased to 7.1% in June 2023. For overseas banks, ROA increased to 0.8% in June 2023. ROE for locally incorporated banks increased to 7.1% from 6.6% during the same period. Net interest income (as a % of total income) increased from 74.5% to 77.8% during the same period as well. Operating expenses as a proportion of total income decreased from 42.1% in June 2022 to 39.5% in June 2023.

Table 4.5: Conventional Banks' Profitability

Indicator	Retail			Wholesale		
	Q2 2022	Q2 2023	Change	Q2 2022	Q2 2023	Change
ROA (%) *	0.8	0.9	0.1	0.6	0.7	0.1
ROA Locally Incorporated Banks (%)	0.8	1.0	0.2	0.2	0.3	0.1
ROA Overseas Banks (%)	0.6	0.8	0.2	1.0	1.2	0.2
ROE (%) **	6.6	7.1	0.5	2.3	3.2	0.9
Net Interest Income (% Total Income)	74.5	77.8	3.3	63.5	58.2	-5.3
Operating Expenses (% Total Income)	42.1	39.5	-2.6	44.1	41.5	-2.6

** 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 slightly increased to 0.7% in June 2023 from 0.6% in June 2022. The ROA for local wholesale banks increased slightly to 0.3 %, while overseas wholesale banks increased from 1.0% to 1.2%. ROE for wholesale banks increased from 2.3% to 3.2%. Net interest income as a proportion of total income decreased from 63.5% in June 2022 to 58.2% in June 2023. Operating expenses as a proportion of total income showed a decrease from 44.1% in June 2022 to 41.5% in June 2023.

4.5 Liquidity

Liquidity position is strong but declines for conventional banks.

Between June 2022 and June 2023, non-bank deposits decreased by 0.6% for conventional retail banks. The overall loan-deposit ratio for the segment increased to 71.4% in June 2023 from 70.1% in June 2022. Liquid assets as a proportion of total assets decreased to 30.9% in June 2023. Liquid assets as a proportion of the short-term liabilities also decreased to 39.6% over this period.

As of June 2023, the overall loan-deposit ratio for conventional wholesale banks stood at 62.1%, a decrease from the 63.0% recorded in June 2022. Liquid assets for wholesale banks as a proportion of total assets decreased to 19.9% in June 2023 from 21.9% in June 2023. The liquid assets as a proportion of short-term liabilities decreased by 1.7% to 25.1% in June 2023. Non-bank deposits as a proportion of total deposits stood at 47.6%, a decrease from the 52.4% level achieved in June 2022, while bank deposits increased from 23.4% in June 2022 to 24% in June 2023.

Table 4.6: Conventional Bank's Liquidity

Indicator	Retail			Wholesale		
	Q2 2022	Q2 2023	Change	Q2 2022	Q2 2023	Change
Liquid Asset Ratio (%)	34.1	30.9	-3.2	21.9	19.9	-2.0
Loan-Deposit Ratio (%)	70.1	71.4	1.3	63.0	62.1	-0.9
Non-Bank Deposits (% of Total Deposits)	76.6	76.0	-0.6	52.4	47.6	-4.8

Source: CBB.

5 PERFORMANCE OF ISLAMIC BANKS

HIGHLIGHTS

Q2 2023

	Retail		Wholesale	
CAR	21.4%	▼ 0.2% YoY	17.2%	▲ 1.8% YoY
Tier 1 CAR	19.5%	▼ 0.4% YoY	16.3%	▲ 1.6% YoY
Assets-to-Capital	12.5	▲ 1.1 YoY	9.0	▲ 1.2 YoY
NPL	5.0%	▲ 0.6% YoY	5.3%	▼ 1.0% YoY
Specific Provisions	49.6%	▼ 9.4% YoY	81.5%	▲ 5.2% YoY
ROA	0.4%	0.0% YoY	0.7%	▲ 0.1% YoY
ROE	4.9%	▼ 0.5% YoY	5.8%	▲ 1.2% YoY
Liquidity	19.1%	▲ 0.2% YoY	20.2%	▼ 4.2% YoY
Loan/Deposit	63.0%	▼ 3.2% YoY	24.8%	▲ 2.2% YoY

- Sector remains well capitalized despite decrease in capital position for Islamic retail and increased for Islamic wholesale banks.
- Non-performing facilities (NPFs) slightly increased for Islamic retail banks and decreased for wholesale.
- Concentration of facilities for Islamic banks continues in specific sectors.
- Earnings for retail Islamic banks slightly decreased but for increased for wholesale.
- Liquidity positions slightly increased for retail Islamic banks but decreased for 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, asset quality, profitability, and liquidity . Unless specified otherwise, the analysis in this chapter is based on consolidated financial data (Bahraini and non-Bahraini operations).

5.2 Capital Adequacy

Islamic retail and wholesale banks remain well-capitalized despite slight decrease in retail

The CAR of Islamic retail banks slightly decreased from 21.5% in June 2022 to 21.4% in June 2023. Tier 1 capital decreased from 19.9% to 19.5% during this period. As at end- June

2023, the CAR for Islamic wholesale banks increased to 17.2% in June 2023 from 15.3% in June 2022. Tier 1 capital also increased from 14.7% to 16.3% over the same period. The ratio of NPFs net of provisions to capital increased to 2.0% in June 2023.

Table 5.1: Islamic Banks' Banks' Capital Provisions Ratios

Indicator	Retail			Wholesale		
	Q2 2022	Q2 2023	Change	Q2 2022	Q2 2023	Change
CAR (%)	21.5	21.4	-0.1	15.3	17.2	1.8
Tier 1 CAR (%)	19.9	19.5	-0.4	14.7	16.3	1.6
Assets/Capital (Times)	11.4	12.5	1.1	7.8	9.0	1.2
NPFs Net Provisions to Capital (%)	12.0	17.1	5.1	1.5	2.0	0.5

Source: CBB.

5.3 Asset Quality

5.3.1 Non-Performing Facilities

Increase in retail NPFs for Islamic retail banks

Non-performing facilities (NPF) ratio for Islamic retail banks increased to 5.0% in June 2023. Specific provisoining decreased to 49.6% in June 2023 from 59.0% in June 2022. As of end- June 2023, NPF ratio for Islamic wholesale banks decreased to 5.3%. Provisioning for NPFs decreased to 81.5% over the same period.

Table 5.2: Islamic Banks' NPF Ratios

Indicator	Retail			Wholesale		
	Q2 2022	Q2 2023	Change	Q2 2022	Q2 2023	Change
NPFs (% Gross Facilities)	4.4	5.0	0.6	6.3	5.3	-1.0
Specific Provisions (% of NPFs)	59.0	49.6	-9.4	86.7	81.5	-5.2

Source: CBB.

A look at the non-performing facilities by sector for Islamic retail banks indicates that the trade sector had the highest impairment (18.2%) in June 2023 followed by construction and agriculture, fishing and forestry with 17.0% and 14.0% respectively. The biggest declines in NPFs by sector was in the credit card sector which went down by 10.8%. The biggest increase in NPFs was in construction, with an increase of 10.2% as indicated in table 5.3.

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

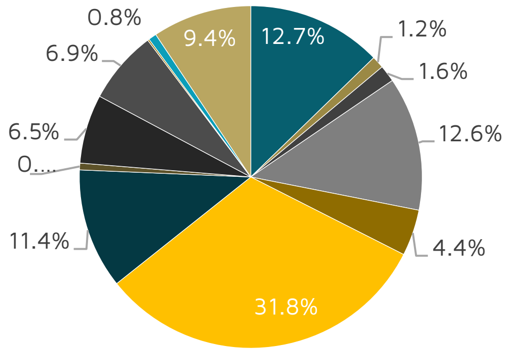
Sector	Retail			Wholesale		
	Q2 2022	Q2 2023	Change	Q2 2022	Q2 2023	Change
Manufacturing	10.8	7.3	-3.4	0.8	1.6	0.8
Mining and quarrying	11.7	11.3	-0.4	0.0	0.0	0.0
Agriculture, fishing and forestry	17.1	14.0	-3.1	2.3	100.0	97.7
Construction	6.9	17.0	10.2	24.1	16.9	-7.2
Financial	3.1	2.7	-0.4	4.6	0.1	-4.5
Trade	19.3	18.2	-1.1	47.4	10.8	-36.6
Personal / Consumer finance	2.7	2.2	-0.6	0.0	0.0	0.0
Credit Card	14.3	3.5	-10.8	0.0	0.0	0.0
Commercial real estate financing	3.0	3.6	0.6	15.2	54.0	38.8
Residential mortgage	1.2	2.5	1.3	0.0	1.8	1.8
Government	0.0	0.0	0.0	0.0	0.0	0.0
Technology, media and telecommunications	11.3	1.7	-9.6	100.0	9.4	-90.5
Transport	1.2	9.0	7.8	3.0	4.7	1.7
Other sectors	3.9	6.3	2.4	14.3	3.4	-10.9

Source: CBB.

On the other hand, the sector with the highest impairment for Islamic wholesale banks was the agriculture, fishing, and forestry sector with 100.0% in June 2023. This was followed by commercial real estate financing and trade sectors with 54.0% and 10.8% respectively. Available data on the sectoral breakdown of non-performing facilities shows that the biggest increase was in the agriculture, fishing, and forestry sector with an increase of 97.7%. The biggest drop was in the technology, media, and telecommunications sector with a decrease of 90.5%. The trade sector went down from 47.4% in June 2022 to 10.8% in June 2023. Also, construction went down from the 24.1% recorded in June 2022 to 16.9% in June 2023.

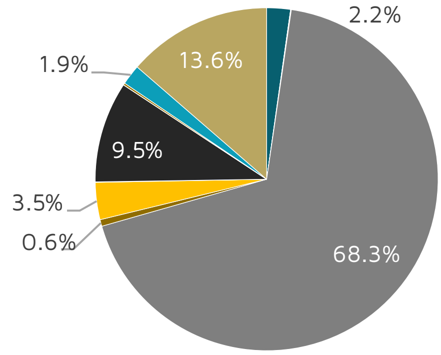
Looking at the data on the concentration of NPFs for Islamic retail banks by sector indicates that the majority of NPLs are concentrated and come from the trade sector (31.8%), construction (12.6%), personal/consumer finance (11.4%) as indicated in chart 5.1. As for Islamic wholesale banks, the majority of NPFs are concentrated and come from construction (68.3%), and other sectors (13.6%) as indicated in chart 5.2.

Chart 5.1: IR Banks' NPLs Concentration by Sector (June 2023)



Source: CBB.

Chart 5.2: IW Banks' NPLs Concentration by Sector (June 2023)



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

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 2023, the top recipient of financing was personal/consumer finance (25.7%), an increase from 24.3% recorded in June 2022. The top two recipients of financing (personal/consumer finance and residential mortgage) accounted for 39.4% of total facilities extended, compared to 39.8% for the top two sectors in June 2022. Real estate/construction exposure decreased to 26.3% in June 2023.

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

Sector	Retail			WWholesale		
	Q2 2022	Q2 2023	Change	Q2 2022	Q2 2023	Change
Manufacturing	9.0	8.6	-0.4	10.3	7.6	-2.7
Mining and quarrying	0.6	0.5	-0.1	0.0	0.0	0.0
Agriculture, fishing and forestry	0.8	0.6	-0.2	0.1	0.0	-0.1
Construction	3.2	3.7	0.5	24.2	21.3	-2.9
Financial	11.5	8.0	-3.5	36.9	42.3	5.4
Trade	5.6	8.7	3.1	2.6	1.7	-0.8
Personal / Consumer finance	24.3	25.7	1.4	0.0	0.0	0.0
Credit Card	0.6	0.9	0.3	0.0	0.0	0.0
Commercial real estate financing	10.0	9.0	-1.0	1.7	0.9	-0.8
Residential mortgage	15.6	13.6	-2.0	0.0	0.0	0.0
Government	9.6	12.4	2.8	2.9	3.0	0.1
Technology, media and telecommunications	0.1	0.4	0.3	0.0	0.1	0.1
Transport	0.6	0.4	-0.2	3.7	2.1	-1.6
Other sectors	8.6	7.4	-1.2	17.5	20.9	3.4
Top two recipient sectors	39.8	39.4	-0.4	61.1	63.6	2.5
Real Estate/ Construction Exposure**	28.8	26.3	-2.5	25.9	22.3	-3.6

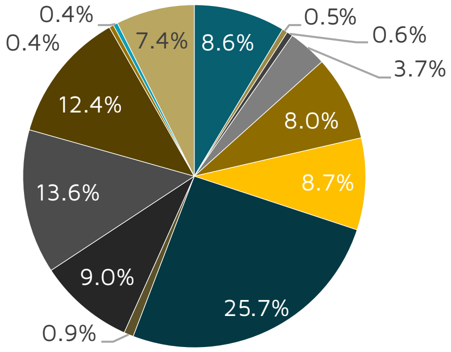
Source: CBB.

**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.*

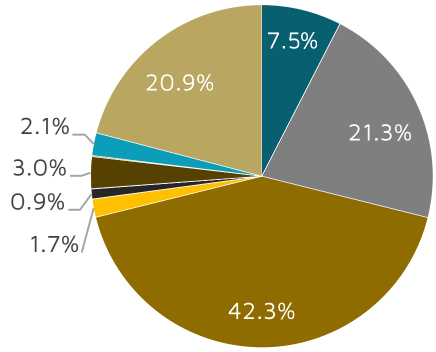
At End- June 2023, the financial sector was the top recipient of financing from Islamic wholesale banks, at 42.3%, increasing by 5.4% from June 2022. The construction sector saw the largest decrease from 24.2% in June 2023 to 21.3% in June 2022. Real estate/ construction exposure decreased from 25.9% in June 2022 to 22.3% in June 2023.

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
- 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

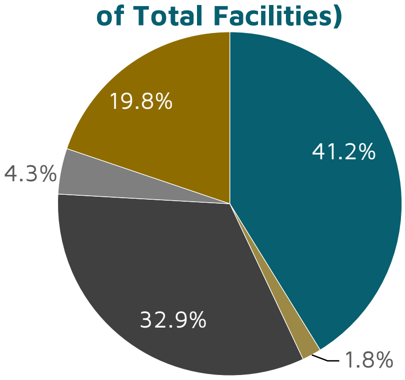
The concentration of lending distribution by Islamic instrument remained the same over the past. At the end of June 2023, the top recipient of finance for Islamic retail banks was Murabaha at 41.2% followed by Ijarah 32.9%. As for wholesale banks, the top recipient of finance was Murabaha at 52.4%.

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

Instrument	Retail			Wholesale		
	Q2 2022	Q2 2023	Change	Q2 2022	Q2 2023	Change
Murabaha	38.1	41.2	3.1	92.2	52.4	-39.8
Istisna'a	2.1	1.8	-0.3	0.0	13.3	13.3
Ijarah	32.8	32.9	0.1	7.8	2.9	-4.9
Salam	0.4	4.3	3.9	0.0	0.0	0.0
Others	26.5	19.8	-6.7	0.0	31.3	31.3

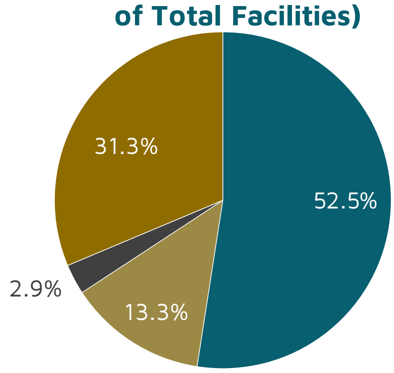
**Figures may not add to a hundred due to rounding.*
Source: CBB.

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 wholesale Islamic banks

ROA for Islamic retail banks remained the same for the period between June 2022 to June 2023. ROE decreased from 5.4% to 4.9% for the same period. Furthermore, operating expenses increased from 64.5% in June 2022 to 69.2% in June 2023. As for Islamic wholesale banks, ROA increased from 0.6% in June 2022 to 0.7% in June 2023. ROE also increased from 4.6% to 5.8% in the same period. Furthermore, operating expenses (as % of total income) increased from 50.8% in June 2022 to 52.1% in June 2023.

Table 5.6: Islamic Banks' Profitability (%)

Indicator	Retail			Wholesale		
	Q2 2022	Q2 2023	Change	Q2 2022	Q2 2023	Change
ROA*	0.4	0.4	0.0	0.6	0.7	0.1
ROE**	5.4	4.9	-0.5	4.6	5.8	1.2
Operating Expenses (% Total Operating Income)	64.5	69.2	4.7	50.8	52.1	1.3

Source: CBB.

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

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

5.5 Liquidity

Increased liquidity levels for Islamic retail and wholesale banks

The volume of liquid assets available to Islamic retail banks increased from 18.9% of total assets in June 2022 to 19.1% in June 2023. The ratio of total facilities to deposits decreased from 65.1% in June 2022 to 63.0% in June 2023. As of end- June 2023, liquid assets of Islamic wholesale banks represented 20.2% of total assets, 2.8% higher than the 17.4% registered in June 2022. Additionally, the facilities deposit ratio decreased slightly from 25.4% in June 2022 to 24.8% in June 2023.

Table 5.7: Islamic Banks' Liquidity (%)

Indicator	Retail			Wholesale		
	Q2 2022	Q2 2023	Change	Q2 2022	Q2 2023	Change
Liquid Assets (% of total assets)	18.9	19.1	0.2	17.4	20.2	2.8
Facilities – deposits ratio (%)	65.1	63.0	-2.1	25.4	24.8	-0.5

Source: CBB.

PART III:
DEVELOPMENT IN THE NON-BANKING FINANCING SECTOR

6 PERFORMANCE OF THE INSURANCE SECTOR

HIGHLIGHTS

Q2 2023

Insurance Licenses	Contribution to GDP	Contribution to Financial Sector
129	5.1%	29.6
Asset of Conv. Insurance	**Assets of Takaful Insurance**	**Gross Premiums**
BD 2,080.8 mn	BD 206.6 mn	BD 151.5 mn

- Conventional firms account for 69.2% of total insurance industry with BD 104.8 million in total gross premiums as of June 2023. General insurance contributes 87.4% 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 2023, there are a total of 129 insurance organizations licensed and registered in the Kingdom. There are 31 insurance companies: 16 conventional local, 10 conventional overseas/foreign branches, and 5 takaful. 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 98 other registered insurance licenses include Insurance Brokers, Insurance Managers, Insurance Consultants, Registered Actuaries, Registered loss Adjusters, and Insurance Pools and Syndicates.

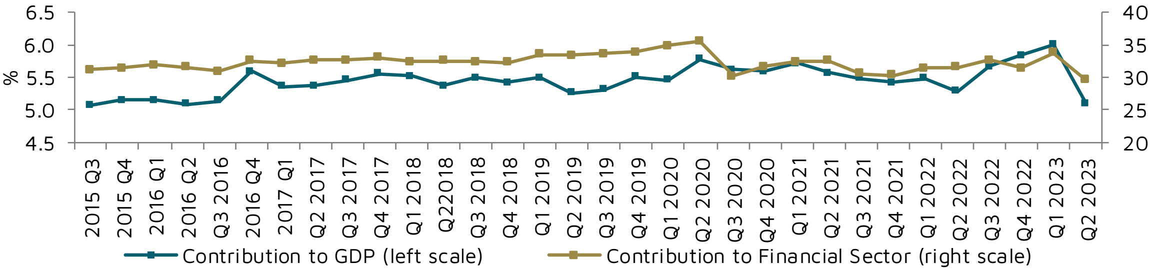
Insurance contribution reached 5.1% of GDP by end of Q2 2023 (compared to 5.6% by end of Q2 2021 and 5.3% by end of Q2 2022). The contribution of the Insurance sector to the overall financial sector reached 29.6% in Q2 2023. Chart 6.1 shows the quarterly

[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 2022 and Q2 2023, unless otherwise indicated.

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 Sectors

As of June 2023, total assets of the Insurance sector reached BD 2,287.4 million with a decrease of 1.9% compared to BD 2,331.3 million in June 2022. Total liabilities decreased by 2.9% over the same period reaching BD 1,614,042.

Total available capital[8] decreased from 404.3 BD million in June 2022 to 393.2 BD million in June 2023. Profitability, on the other hand, increased significantly between June 2022 and June 2023 reaching BD 28.2 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 2022	Q2 2023	Q2 2022	Q2 2023	Q2 2022	Q2 2023	Q2 2022	Q2 2023
Conventional	2,136,742	2,080,784	1,531,120	1,477,818	363,531	346,169	1,299	28,162
Local	1,942,680	1,881,505	1,369,323	1,310,243	332,739	318,801	(1,310)	26,760
Overseas	194,062	199,279	161,797	167,575	30.792	27,368	2,609	1,402
Takaful	194,571	206,604	130,975	136,224	40,724	47,000	-	-
All Insurance	**2,331,314**	**2,287,388**	**1,662,095**	**1,614,042**	**404,254**	**393,169**	**1,299**	**28,162**

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

6.2.1 Conventional Insurance Firms

As of June 2023, total assets of the conventional insurance sector stood at BD 2,080.8 million decreasing by 2.6% compared to the BD 2,136.7 million registered in June 2022. Assets of local insurance firms were BD 1,881.5 million (90.4% of total assets) with a negative growth rate of 3.1% since June 2022. Total assets of overseas foreign branches were BD 199.3 million (9.6% of total assets) recording an increase of 2.7%.

The liabilities of the conventional insurance sector registered at BD 1,477.8 million with a 3.5% decrease from BD 1,531.1 million in June 2022. Liabilities for local insurance firms registered at BD 1,310.2 million decreasing by 4.3%. Liabilities of overseas foreign branches were BD 167.5 million in June 2023 with an increase of 3.6%.

Total capital as of June 2023 was at BD 346.2 million decreasing by 4.8% from BD 363.5 million in the equivalent period of the previous year. Total available capital for local insurance was BD 318.8 with a YoY decrease of 4.2%. Total available capital for overseas foreign branches decreased by 11.1% from BD 30.7 million in June 2022 to BD 27.4 million in June 2023.

Net profit increased for conventional insurance firms from BD 1.3 million in June 2022 to a profit of BD 28.2 million in June 2023. Net profit for local insurance was BD 26.8 million with a YoY increase of 2,142.4%. Net profit for overseas insurance was BD 1.4 with a yoy decrease of 46.3%.

[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 2023 increased by 6.2% to BD 206.6 million. The liabilities increased by 4.0% from BD 131.0 million in June 2022 to BD 136.2 million in June 2023. Total regulatory capital experienced an annual increase of 15.2% from BD 40.7 million in June 2022 to BD 47.0 million in June 2023.

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 151.5 million, increasing by 3.1% YoY. Conventional insurance represented 69.2% of total gross premiums (local and branches represented 54.9% and 14.3% respectively) while takaful accounted for 30.8% of gross premiums. As of June 2023, life insurance represented 10.5% of gross premiums while non-life/general insurance was 89.5% covering the various classes.

Looking at the performance by class, Long-term (Life) category experienced an annual decrease of 31.8%. Marine and Aviation also decreased by 12.7%. On the other hand, Miscellaneous Financial Loss increased by 26.2% and Engineering increased by 24.7%. The top 3 business lines sectors represented 74.3% of total gross premiums.

As of June 2023, Net Premiums Written increased by 5.1% compared to the previous period registering a value of BD 94.8 million. Motor showed the biggest increase (8.5%) over the period increasing from BD 34.7 million in June 2022 to BD 37.7 million in June 2023. On the other hand, the biggest decline was derived from Long-term (Life) class, decreasing by 29.5% from BD 18.8 million in June 2022 to BD 13.3 million in June 2023.

Gross Claims for the insurance industry recorded a YoY increase of 25.4% from BD 68.6 million in June 2022 to BD 86.0 million in June 2023. The increase was mainly in the Fire, Property and Liability class increasing by 104.0% from BD 4.9 million in June 2022 to BD 10.0 million in June 2023 and Medical by 20.2% from BD 25.1 million to BD 30.2 million.

Net Claims for the insurance industry show an increase of 9.1%, which was derived from an annual increase in Medical (19.7%) and Long-term (Life) (6.8%).

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

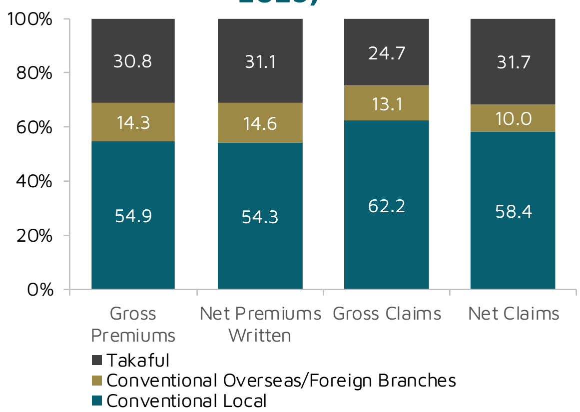
BD 000	Gross Premiums		Net Premiums Written		Gross Claims		Net Claims	
	Q2 2022	Q2 2023	Q2 2022	Q2 2023	Q2 2022	Q2 2023	Q2 2022	Q2 2023
Long-term (Life)	23,316	15,902	18,821	13,268	12,330	11,911	9,597	10,253
Fire, Property & Liability	21,356	21,421	3,267	4,362	4,911	10,019	1,180	1,127
Miscellaneous Financial Loss	4,228	5,337	385	1,099	227	238	(140)	75
Marine & Aviation	3,155	2,755	897	700	(66)	312	24	203
Motor	36,060	38,890	34,781	37,727	24,060	26,585	21,470	22,048
Engineering	5,126	6,390	704	514	183	2,879	(79)	(197)
Medical	46,775	52,312	29,489	34,333	25,155	30,248	17,999	21,540
Others	6,847	8,479	1,911	2,834	1,801	3,843	755	373
Total	**146,862**	**151,486**	**90,255**	**94,836**	**68,601**	**86,035**	**50,808**	**55,423**

Source: CBB.

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

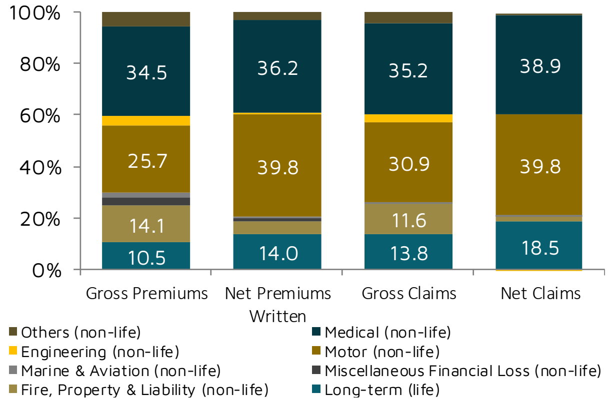
[9] Non-life or general insurance includes: Fire, Property & Liability, Miscellaneous Financial Loss, Marine & Aviation, Motor, Engineering, Medical and Others.

Chart 6.2: Premiums and Claims of Insurance Sector by Segment (%) (Q2 2023)



Source: CBB.

Chart 6.3: Concentrations of Premiums and Claims for Insurance Firms by Class (Q2 2023)



Source: CBB.

6.3.1 Conventional Insurance Firms

Gross Premiums for conventional insurance recorded a YoY slight decrease by BD 0.7 million (0.7%) decreasing from BD 105.6 million in June 2022 to BD 104.8 million in June 2022 (Table 6.3). The greatest increase was from Engineering insurance by around BD 1.2 million (34.5%). The largest YoY decline was from Long-term (Life) by BD 6.9 million (34.3%). In terms of concentration, Medical, Motor, Fire Property & Liability business classes represented 30.0%, 26.0% and 13.1% respectively of the total gross premiums.

Net Premiums Written reflected a YoY decrease by 0.7%. The Motor class had an increase of BD 2.0 million (8.3%). On the other hand, Long term (Life) net premiums written decreased by BD 5.1 million (29.9%). Long-term (Life), Motor and Medical insurance remained the largest in terms of Net Premiums Written concentration, accounting for 11.4%, 25.3% and 18.6%.

Gross Claims increased by 32.4% YoY in June 2023 due to a an increase in Fire, Property, and Liability from BD 3.6 million to BD 8.7 million (142.1). The highest share in gross claims was Motor 18.3%, followed by Medical at 19.4%.

Net Claims experienced an annual increase of 12.7% from BD 33.6 million in June 2022, reaching BD 37.9 million in June 2023. Net claims for Medical insurance increased by BD 2.5 million (26.7%) and by BD 1.2 million (8.5%) for Motor insurance. The concentration falls heavily within the Motor insurance class, accounting for 14.2% of the total net claims.

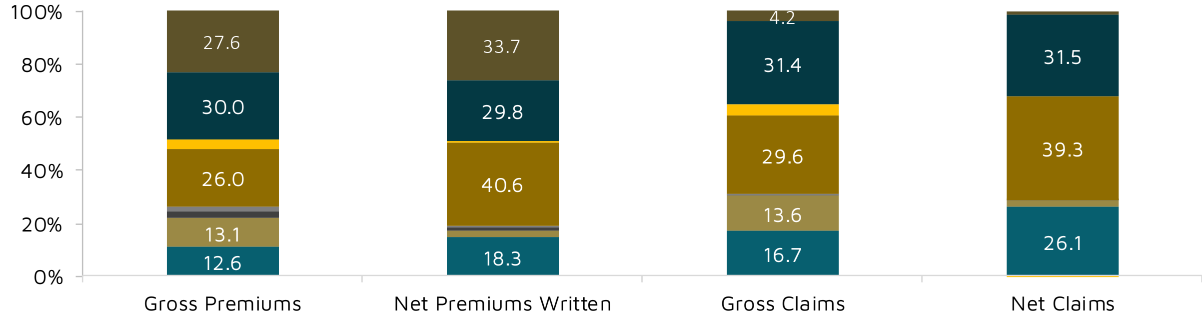
Table 6.3: Premiums and Claims for Conventional Insurance by Class

BD 000	Gross Premiums		Net Premiums Written		Gross Claims		Net Claims	
	Q2 2022	Q2 2023	Q2 2022	Q2 2023	Q2 2022	Q2 2023	Q2 2022	Q2 2023
Long-term (Life)	20,118	13,212	17,107	11,984	11,288	10,825	9,245	9,894
Fire, Property & Liability	17,179	16,951	2,581	3,661	3,602	8,721	830	901
Miscellaneous Financial Loss	2,220	3,176	183	875	142	167	(115)	55
Marine & Aviation	2,575	2,336	790	629	(142)	190	(44)	108
Motor	25,377	27,301	24,511	26,549	16,210	19,191	13,736	14,898
Engineering	3,401	4,575	560	325	(213)	2,601	(190)	(237)
Medical	30,572	31,473	17,892	19,485	16,469	20,344	9,415	11,929
Others	4,119	5,611	1,295	1,839	1,568	2,740	720	331
Total	**105,561**	**104,818**	**64,919**	**65,347**	**48,924**	**64,780**	**33,598**	**37,878**

Source: CBB.

Medical had the highest exposure in Gross Premiums (26.8%). Whereas Motor insurance had the highest exposure in Net Premiums Written (25.7%), Gross Claims (32.6%) and Net Claims (41.6%).

Chart 6.4: Concentrations of Premiums and Claims for Conventional Insurance by Class (Q2 2023)



Source: CBB.

Table 6.4 below and Charts 6.5 and 6.6 shows a further division of the premiums and claims by class between Local and Overseas firms within the conventional insurance industry for June 2023.

Table 6.4: Premiums and Claims for Conventional Local and Overseas Insurance by Class (Q2 2023)

BD '000	Gross Premiums		Net Premiums Written		Gross Claims		Net Claims	
	Local	Overseas	Local	Overseas	Local	Overseas	Local	Overseas
Long-term (Life)	4,958	8,255	4,458	7,526	9,480	1,346	8,998	896
Fire, Property & Liability	15,126	1,825	3,344	317	7,706	1,015	337	559
Miscellaneous Financial Loss	2,348	829	844	30	167	-	55	-
Marine & Aviation	2,100	236	557	73	147	43	65	43
Motor	24,600	2,701	23,931	2,618	16,790	2,400	12,637	2,262
Engineering	4,449	171	233	92	1,143	1,459	(226)	(12)
Medical	24,296	7,176	16,620	2,866	15,451	4,893	9,978	1,951
Others	5,224	387	1,526	313	2,644	96	497	(166)
Total	83,101	21,717	51,513	13,834	53,528	11,251	32,341	5,537

Source: CBB.

Chart 6.5: Concentrations of Premiums and Claims by Class for Local Insurance (Q2 2023)

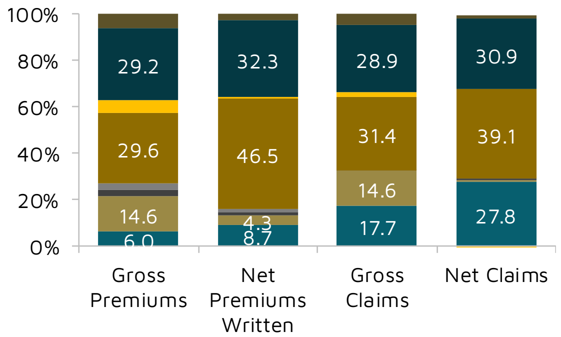
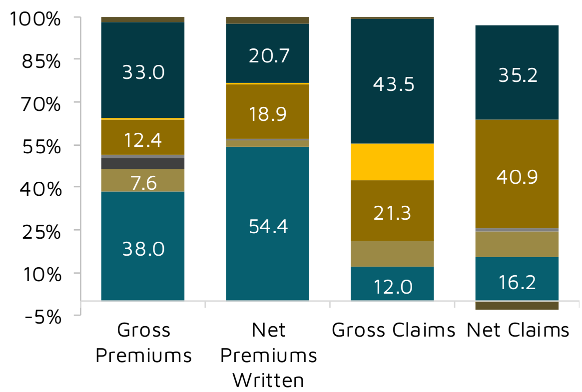


Chart 6.6: Concentrations of Premiums and Claims by Class for Overseas Insurance (Q2 2023)



Source: CBB.

Long-term (life)
Fire, Property & Liability (non-life)
Miscellaneous Financial Loss (non-life)
Marine & Aviation (non-life)
Motor (non-life)
Engineering (non-life)
Medical (non-life)
Others (non-life)

6.3.2 Takaful Insurance Firms

The Gross Premiums for Takaful companies decreased on a YoY basis by 13.0%, from BD 41.3 million at June 2022 reaching BD 46.6 million in June 2023. The largest increase was attributed to Medical increasing by BD 4.6 million (28.6%). Fire, Property & Liability had a decline of BD 0.6 million (13.4%). Medical insurance line was the highest contributor towards Takaful gross premiums, accounting for 44.7% of gross premiums.

Net Premiums Written increased by 16.4% from June 2022 to June 2023, reaching BD 29.5 million. Motor and Medical insurance accounted for the largest components in terms of gross claims, representing 24.0% and 31.8% of the total net premiums written.

Gross Claims increased by 8.0% compared from June 2022 to June 2023, with Medical registering the largest increase (BD 1.2 million) within the same period. Medical and Motor insurance accounted for the largest components in terms of gross claims, representing 15.8% and 21.2% of the total gross claims.

Net Claims recorded an annual increase of 1.9% in June 2022, with Medical insurance having the an increase recorded at 12.0%. Furthermore, Medical and Motor represent the largest components of net claims, accounting for 20.6% and 15.3% of the total respectively.

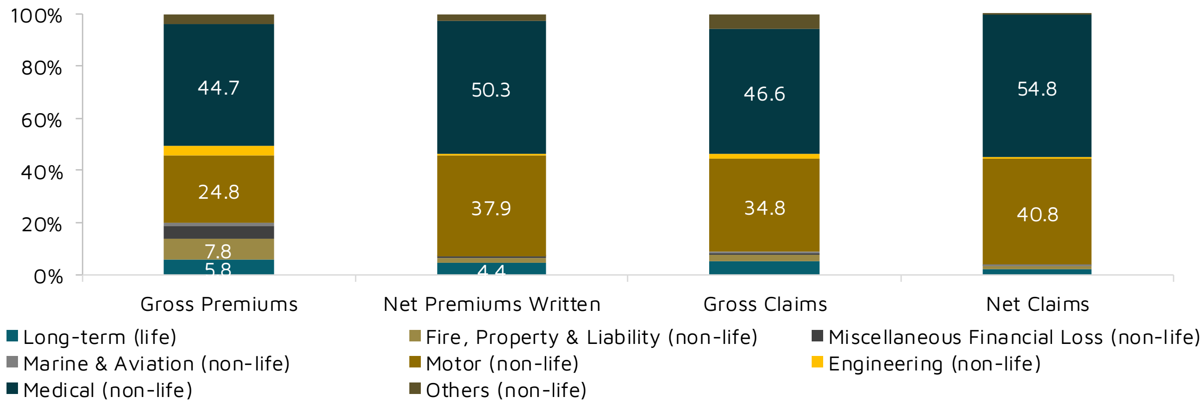
Table 6.5: Premiums and Claims by Class for Takaful Insurance Firms

BD '000	Gross Premiums		Net Premiums Written		Gross Claims		Net Claims	
	Q2 2022	Q2 2023	Q2 2022	Q2 2023	Q2 2022	Q2 2023	Q2 2022	Q2 2023
Long-term (Life)	3,198	2,689	1,715	1,284	1,041	1,085	352	360
Fire, Property & Liability	4,177	4,469	686	701	1,309	1,298	351	227
Miscellaneous Financial Loss	2,008	2,161	202	224	85	71	(25)	20
Marine & Aviation	580	418	107	71	76	122	68	95
Motor	10,682	11,589	10,270	11,179	7,850	7,394	7,734	7,150
Engineering	1,725	1,633	144	188	396	278	111	40
Medical	16,203	20,839	11,597	14,847	8,687	9,905	8,584	9,611
Others	2,728	2,868	615	995	233	1,103	35	43
Total	41,301	46,668	25,336	29,489	19,677	21,256	17,210	17,545

Source: CBB.

Takaful insurance companies have very high concentration on the Medical and Motor Insurance business lines. Gross Premiums for both sectors combined represent (69.5%), Net Premiums Written (88.3%), Gross Claims (81.4%), and Net Claims (95.5%).

Chart 6.7: Concentrations of Premiums and Claims by Class for Takaful Insurance Firms (Q2 2023)



Source: CBB.

6.3.3 Retention Ratio and Loss Ratio (By Class)

Life insurance business line registered a retention ratio of 83.4% in June 2023. Observing the non-life insurance, Medical and Motor, that accounted for 60.2% of the total Gross

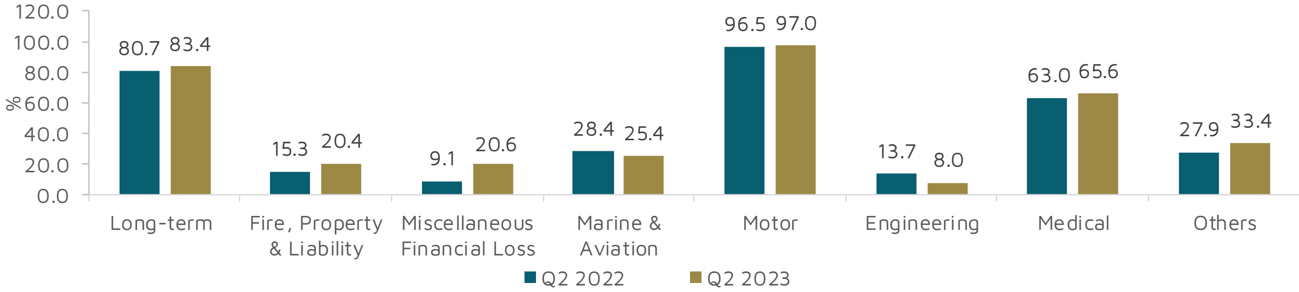
Premiums in June 2023 respectively, registered retention ratios of 97.0% for Motor and 65.6% for Medical. Nevertheless, retention ratios were significantly lower for other business lines such as Fire, Property & Liability and Engineering, registering 20.4% and 8.0% respectively.

Table 6.6: Retention and Loss Ratios of Overall Insurance Sector

%	Retention Ratio [1]		Loss Ratio [2]	
	Q2 2022	Q2 2023	Q2 2022	Q2 2023
Long-term	80.7	83.4	57.6	90.3
Fire, Property & Liability	15.3	20.4	39.6	41.2
Miscellaneous Financial Loss	9.1	20.6	-72.0	10.3
Marine & Aviation	28.4	25.4	2.8	29.3
Motor	96.5	97.0	60.7	58.8
Engineering	13.7	8.0	-15.6	-41.7
Medical	63.0	65.6	76.0	80.0
Others	27.9	33.4	52.0	19.5

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:

- 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:
- Proactively safeguarding policy holders rights by introducing new rules to protect and enhance the life insurance landscape in the kingdom;
- Reviewing and amending the prudential reports required to reflect the successful implementation of International Financial Reporting Standard (IFRS) 17;
- Revised the appointed Representative Requirements to enhance the market practice and protect the customers interest;
- Support implementation of the mandatory health insurance for expatriates led by the Supreme Council of Health;
- Actively promoted innovation and digital transformation through the issuance of directives to enhance motor and medical insurance services;
- Promote awareness of insurance needs in order to enhance insurance literacy within the Kingdom; and
- Ensuring CBB's commitments of having a fair and positive customer experience within the insurance industry, a directive has been issued to all insurance firms for enhancing the Compliance Function and Being Client Centric.

7 PERFORMANCE OF CAPITAL MARKETS

HIGHLIGHTS

# of Companies	All Share Index	Islamic Index
42	1,957.87 ▲ 3.3%	746.9 ▲12.6%

Market Capitalization	Value of Transactions	Volume of Transactions
BD 7.7 bn ▼ 30.6% YTD	BD 119.3 mn	441.8 mn

- Increase in Bahrain All Share & increase in Bahrain Islamic Index.
- Bahrain Bourse's market capitalization stood at BHD 7.7 billion in H1 2023, decreasing by 30.6%.
- The Materials Sector dominated the market trading activity as it had the highest value traded.
- Bahrainis represented 51% of the value of shares bought and 61% of value of shares sold during first half 2023.

7.1 Overview

This chapter provides an overview of the capital markets sector in the Kingdom of Bahrain and provide statistical insights of 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 2023, Bahrain Bourse recorded a total listing of 42 Companies (including 1 REIT), 3 Mutual Funds, 18 Bonds and Sukuk and one REIT. During the second quarter of 2023, there were 15 companies that closed higher and 23 closed lower and 4 remained unchanged. Financials sector remains the dominant sector in Bahrain Bourse in terms of market capitalization making up 61% 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 ALBH, NBB, BBK, BEYON, and UGH represent 68% of the total market.

7.2 Bahrain Bourse

7.2.1 All Share Index and Islamic Index Overview

Increase in market index

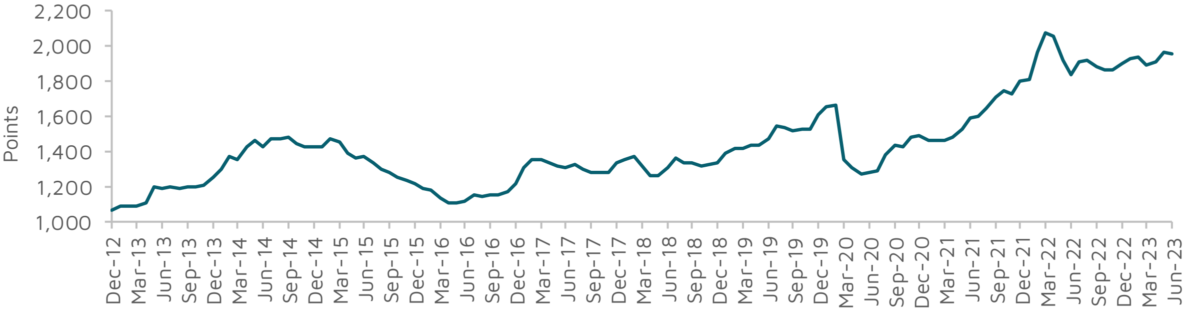
Bahrain All Share Index increased by 3.3% during first half 2023 year to date. The index increased during the first half of the year with the lowest month-end close level recorded being in March, and the highest month-end close was recorded in May.

Table 7.1: Key Indicators of Bahrain Bourse

Indicator	2018	2019	2020	2021	2022	H1 2023
All Share Index	**1,337.3**	**1,610.2**	**1,489.8**	**1,797.3**	**1,895.3**	**1,957.87**
Highest	1,369.9	1,610.2	1,668.7	1,797.3	1,918.0	1,963.51
Lowest	1,257.9	1,391.4	1,232.4	1,447.6	1,839.6	1,886.61
Market Capitalization (BD,	8,198.5	10,134.6	9,277.3	10,815.5	11,408.9	7,687.7
Total Value (BD million)	323.8	286.4	212.8	195.7	160.6	119.3
Total Volume (million)	1,441.1	1,157.3	1,209.3	1,018.3	517.3	441.8
No. of Transactions	19,225	20,712	19,309	21,001	17,190	9,853
No. of Companies Listed	43	44	44	42	42	42

Source: Bahrain Bourse.

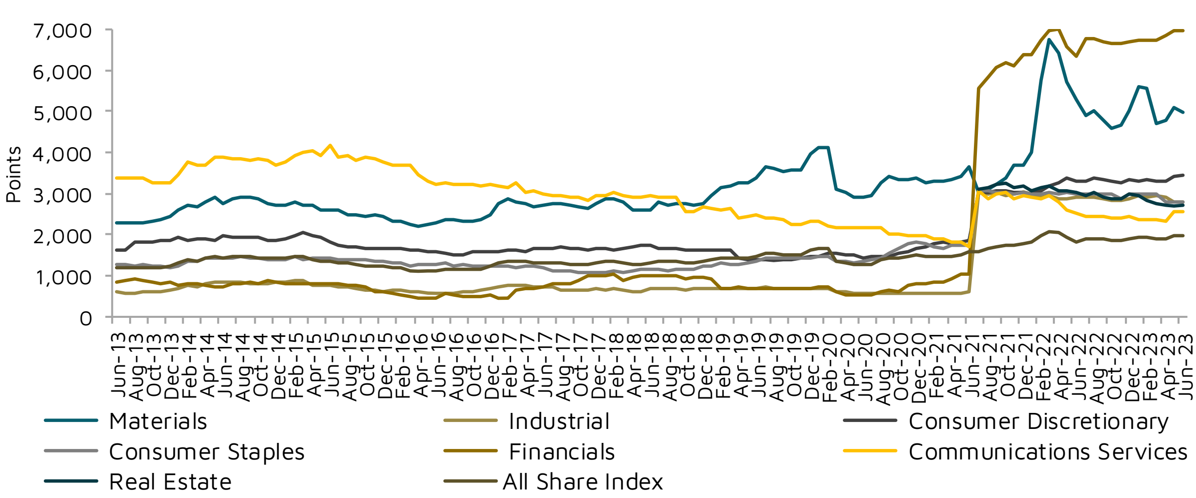
Chart 7.1: Bahrain All-Share Index, Dec. 2012 – Jun. 2023



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.

Chart 7.2: Sector Indices Levels & Returns, Jan. 2013 – Jun. 2023



Source: Bahrain Bourse.

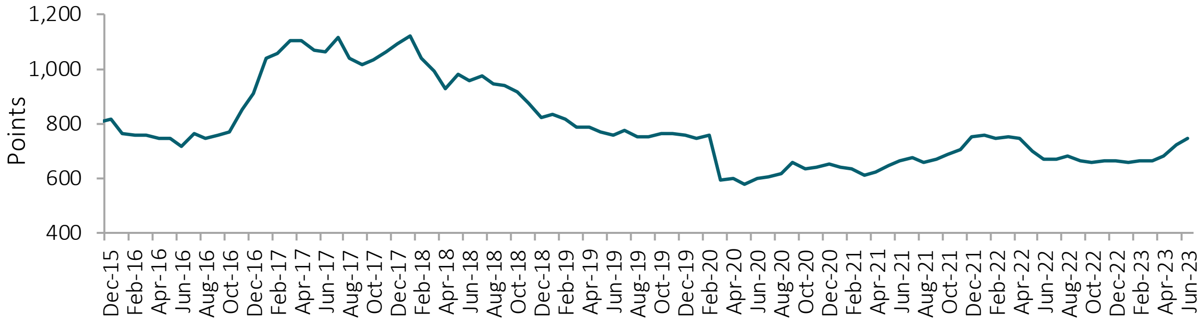
Table 7.2: Bahrain All Share Index by Sector

	2022	H1 2023
Materials	5,007.7	4,989.28
Industrials	2,871.2	2,786.47
Consumer Discretionary	3,333.0	3,448.62
Consumer Staples	3,003.9	2,794.28
Financials	6,691.2	6,971.34
Communications Services	2,437.1	2,578.22

Source: Bahrain Bourse.

In September 2015, Bahrain Bourse launched the Bahrain Islamic Index as the first Islamic finance index in the region. There were 14 Shariah compliant companies included within the index as of H1 2023. YTD data demonstrates that the Bahrain Islamic Index decreased by 12.0% between January 2023 and June 2023 reaching 746.98 points.

Chart 7.3: Bahrain Islamic Index, Dec. 2015 – Jun. 2023



Source: Bahrain Bourse.

7.2.2 Bahrain Bourse Trading Statistics

Market Capitalization

As of first half of 2023, market capitalization of the Bahrain Bourse stood at BD 7.7 billion. This level of market capitalization is 32.6% lower than the second half of 2022.

Table 7.3: Market Capitalization on the Bahrain Bourse

Sector (BD)	H2 2022	H1 2023	(% Change)
Materials	1,547,800,000	1,542,120,000	-0.4
Industrials	137,100,000	133,053,000	-3.0
Consumer Discretionary	198,256,972	205,135,534	3.5
Consumer Staples	146,255,232	136,049,424	-7.0
Financials	8,398,661,786	4,650,448,468	-44.6
Communications Services	876,430,856	927,188,952	5.8
Real Estate	104,381,971	93,725,185	-10.2
Total	**11,408,886,817**	**7,687,720,563**	**-32.6**

Source: Bahrain Bourse.

A breakdown of market capitalization by sector indicates that the Communications Services sector scored the highest increase in market capitalization (5.8%) during the first half of 2023. The Financials sector recorded the highest percentage decrease in market capitalization with a 44.6% decrease during the first half of 2023.

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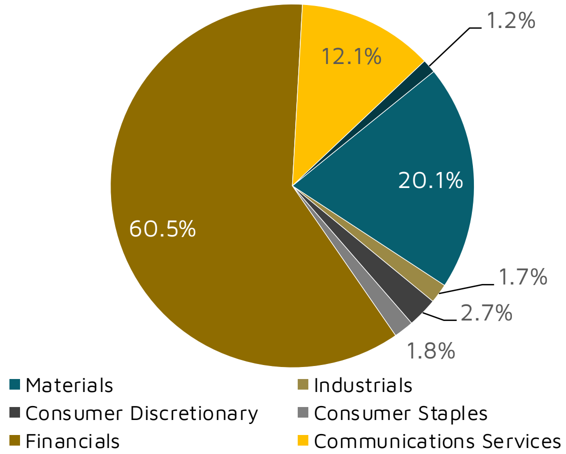
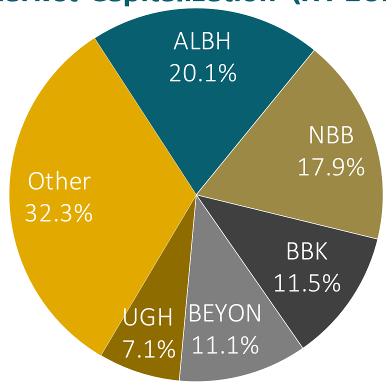
Chart 7.4: Market Capitalization by Sector (H1 2023)



Source: Bahrain Bourse.

Chart 7.5: Largest 5 companies by Market Capitalization (H1 2023)



Source: Bahrain Bourse.

Aluminum Bahrain is the largest company in terms of Market Capitalization and contributes 20.1% of the total market capitalization as of first half 2023. National Bank of Bahrain has the second largest share of Market Capitalization of 17.9% and it is followed by Bank of Bahrain & Kuwait with 11.5%, Bahrain Telecommunication Company with 11.1% and United Gulf Holding Company with 7.1%.

Table 7.4: Largest 5 Companies by Market Capitalization (H1 2023)

Company	Market Capitalization (BHD)	% from Total Market
Aluminum Bahrain (ALBH)	1,542,120,000	20.1
National Bank of Bahrain (NBB)	1,377,773,636	17.9
Bank of Bahrain and Kuwait (BBK)	885,804,037	11.4
Bahrain Telecommunication Company (BEYON)	854,884,800	11.1
United Gulf Holding Company (UGH)	544,476,638	7.1
Total	**5,205,059,111**	**67.7**

Source: Bahrain Bourse.

Value of Shares Traded

Most of the value of shares traded during the first half of 2023 was in the Materials sector whose traded shares (by value) represented 42.3% of total value.

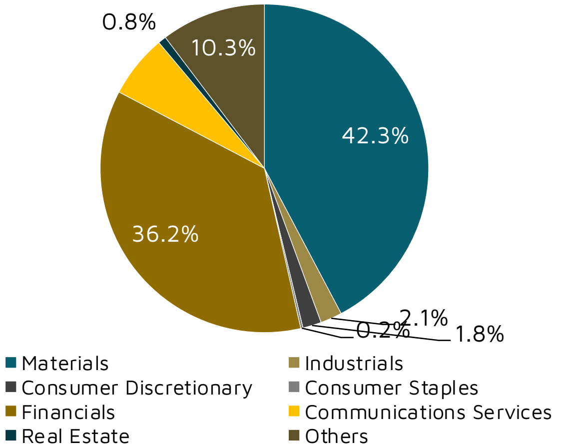
Table 7.5: Value of Shares Traded by Sector (% of Value of all shares traded)

Sector	H2 2022	H1 2023
Materials	33.6	42.3
Industrials	1.7	2.1
Consumer Discretionary	1.9	1.8
Consumer Staples	2.1	0.2
Financials	39.4	36.2
Communications Services	6.7	6.2
Real Estate	0.9	0.8

Source: Bahrain Bourse.

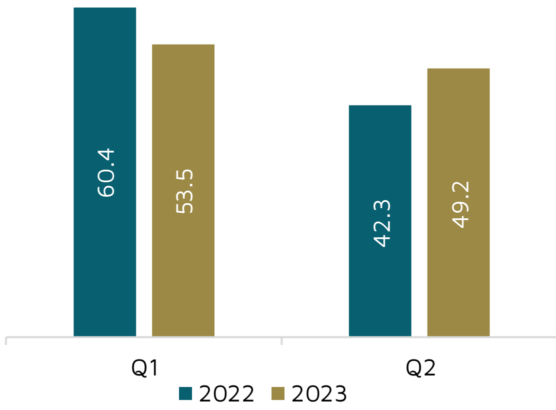
The Financials sector represents the second largest level at 36.2% of the total value of shares traded in the first half of 2023. Investors' interest in Consumer Staples sector was the least during this period with traded shares by value representing only 0.2% of the total value of traded shares. During the first half of 2023, the value of shares traded was highest in May and the lowest was in April, and the average value of shares traded during the first half for a month was BD 20 million.

Chart 7.6: Value of Shares Traded by Sector (% of Value of all shares traded) (H1 2023)*



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

Chart 7.7: Value of Shares Traded Comparison



Source: Bahrain Bourse.

Volume of Shares Traded

The bulk of the volume of shares traded in first half 2023 was in the Financial sector representing 72% 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%.

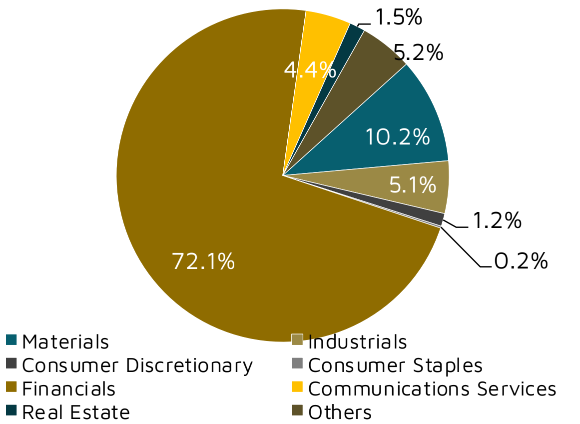
Table 7.6: Volume of Shares Traded by Sector (% of Volume of all shares traded)

Sector	H2 2022	H1 2023
Materials	11.2	10.2
Industrials	4.3	5.1
Consumer Discretionary	2.0	1.2
Consumer Staples	2.4	0.2
Financials	72.7	72.1
Communications Services	5.4	4.4
Real Estate	2.1	1.5

Source: Bahrain Bourse.

During the first half of 2023, the volume traded was highest in March and the lowest was in January, and the average volume traded during the year for a month was 73.6 million shares.

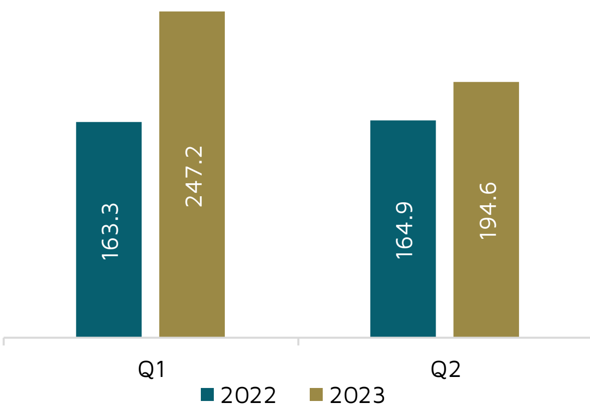
Chart 7.8: Volume of Shares traded by Sector (% of Volume of all shares traded) (H1 2023)*



** Other sector includes Closed companies, Non-Bahraini and IPOs.*

Source: Bahrain Bourse.

Chart 7.9: Volume of Shares Traded Comparison



Source: Bahrain Bourse.

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Number of Transactions

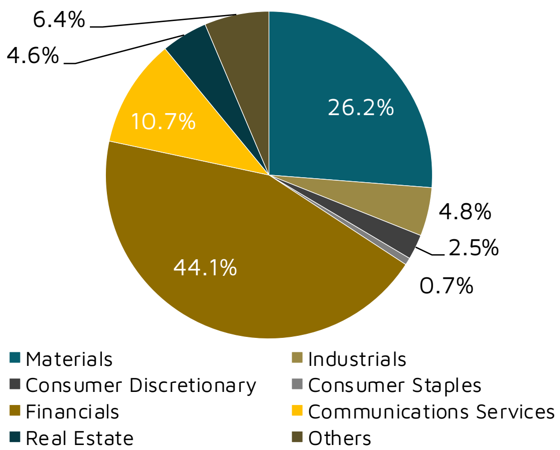
During the first half of 2023, the market executed 9,853 transactions. Most of the transactions were executed by the Financials sector at 4,347 transactions (44% of all transactions), followed by the Materials at 2,585 transactions (26%), and the Communications Services sector at 1,054 transactions (11%).

Table 7.7: Number of Transactions by Sector

Sector	H2 2022	H1 2023
Materials	1,586	2,585
Industrials	209	472
Consumer Discretionary	167	244
Consumer Staples	82	70
Financials	2,976	4,347
Communications Services	961	1,054
Real Estate	374	451
Total Market	**6,355**	**9,853**

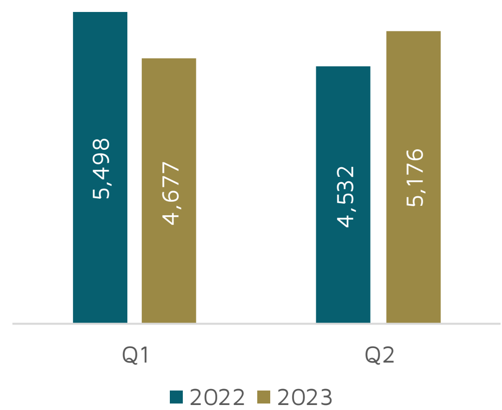
Source: Bahrain Bourse.

Chart 7.10: Number of Transactions (% of all transactions) (H1 2023) *



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

Chart 7.11: Number of Transactions Comparison



Source: Bahrain Bourse.

Trading by nationality

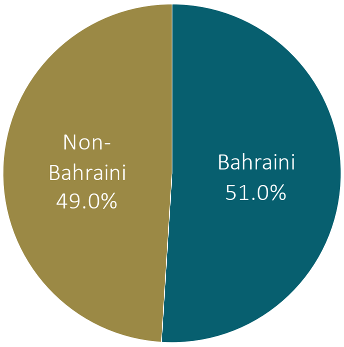
As of first half 2023, non-Bahraini nationals contributed to 35% of the value of shares bought while Bahraini nationals contributed the remaining 65% of the value of shares bought. As for sell-side of the transactions, Non-Bahraini nationals contributed to 33% of the value of shares sold while Bahraini nationals contributed to 67% of the remaining value of shares sold.

Table 7.8: Value of Transactions by Nationality (BD million)

	Q1 2023		Q2 2023	
	Bahraini	Non-Bahraini	Bahraini	Non-Bahraini
Buy	28.0	37.1	33.5	20.7
Sell	37.8	27.2	35.3	19.0

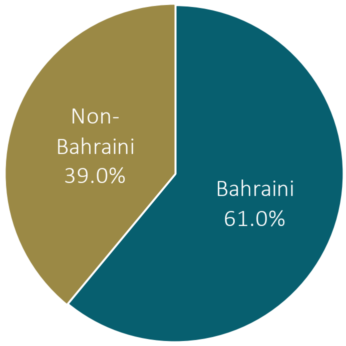
Source: Bahrain Bourse.

Chart 7.12: Share of Trading Value of Buy transactions by nationality (H1 2023)



Source: Bahrain Bourse.

Chart 7.13: Share of Trading Value of Sell transactions by nationality (H1 2023)



Source: Bahrain Bourse.

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 to making Bahrain Bourse a regional financial market. With the support of the CBB, 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 CBB continues to work 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).

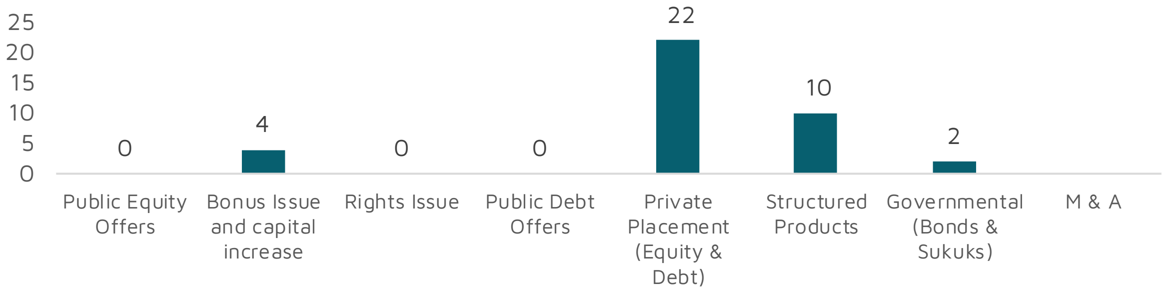
The strategy also aims to develop the financial market by supporting Bahrain in joining the emerging markets index, which would stimulate investment and support intermediaries in a way that contributes to expanding the number of investors and improving liquidity levels. It is also worth noting that the CBB 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 – this initiative has seen light by virtue of the launch of the TabadulHub Platform. 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 Capital Market Activities

7.3.1 Offering of Securities

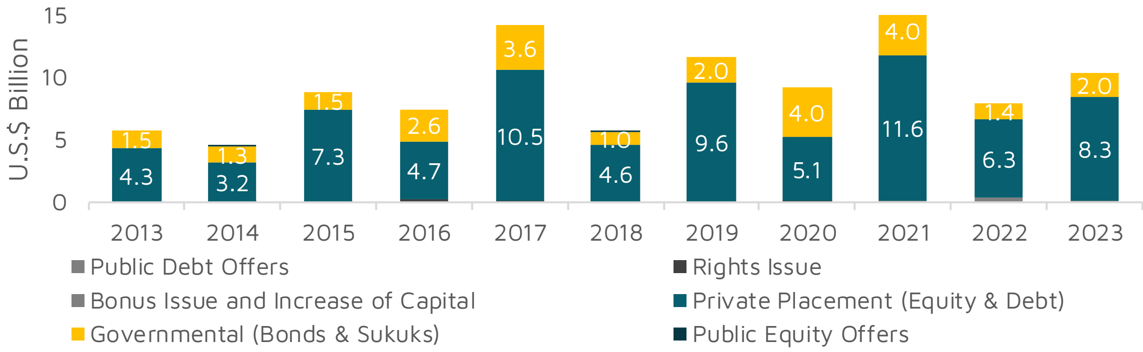
As at June 2023, CBB issued its no objection to the issuance of 38 offering documents. The total value of issuances reached USD 10.43 billion. (Chart 7.18 & 7.19).

Chart 7.14: Number of Capital Market Activities



Source: CBB.

Chart 7.15: Total Issuance Value



Source: CBB.

7.3.2 Esterad Investment Company B.S.S. ("Esterad") increase of capital and issuance of ordinary shares for the acquisition of 100% of Venture Capital Bank B.S.C. ("VCB")

On 8th June 2023, Esterad announced the establishment and registration of the Trust established for the settlement of the purchase consideration for VCB's shareholders.

On 19th June 2023, upon ensuring the satisfaction of all regulatory requirements, the CMSD provided its no objection to the increase of the issued and paid up capital of Esterad from BD 14,000,000 representing 140,000,000 shares to 14,706,316 representing 147,063,161 shares through the issuance of 7,063,161 new ordinary shares at a nominal value of BHD 0.100 based on the approved swap ratio of 0.245 ordinary shares of Esterad in exchange for 1 ordinary share in Venture Capital Bank.

7.4 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 2023, 5 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.

7.5 Developments in Regulation and Initiatives

The CBB 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 ("MMoU") and GCC 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.

During 2023, CBB 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 2023:

7.5.1 Policy and Regulatory Developments

- The Anti-Money Laundering and Combating Financial Crime ("AML") Module of Volume 6 of the CBB Rulebook: Amendments to the AML Module haven been issued for consultation in June 2023 to reflect new provisions relating to reliance on third parties for customer due diligence.
- Crypto-Asset ("CRA") Module of Volume 6 of the CBB Rulebook: As part of its initiatives to further enhance the regulatory framework, and in line with the developments in the sector and international best practices, the CBB issued amendments to the CRA Module in March 2023. In addition to a new chapter on digital token offerings, the new amendments enable crypto-asset licensees to provide additional activities subject to the CBB's prior approval on a case-by-case basis.
- The Central Bank of Bahrain issued a consultation paper on Environmental, Social, and Governance (ESG) disclosure guidelines on August 17, 2023, to all listed companies, banks, insurance firms, financing companies, and category 1 and 2 investment firms.

7.5.2 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 is in its second year with the aim of raising awareness on the culture of financial transactions and investment in the capital markets, through a number of awareness programs and events. Two of the initiatives of the program are the Gulf investor week and 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.

PART IV:

DEVELOPMENTS IN PAYMENT SYSTEMS, FINTECH, AND CYBER SECURITY

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

HIGHLIGHTS

H1 2023

RTGS Daily Average	
Volume	Value
191	BD 360.0 mn
▲ 9.1% YoY	▲ 6.2% YoY

SSSS Daily Average	
Volume	Value
869,441	BD 3.0 bn
▲ 9.1% YoY	▲ 6.2% YoY

ATM Daily Average	
Volume	Value
38,790	BD 3.9 mn
▼ 8.3% YoY	▼ 7.6% YoY

BCTS Daily Average	
Volume	Value
8,324	BD 29.2 mn
▼ 2.4% YoY	▼ 2.6% YoY

Fawri + Daily Average	
Volume	Value
869,441	BD 19.7 bn
▲43.7 % YoY	▲21.2% YoY

Fawri Daily Average	
Volume	Value
50,532	BD 82.6 mn
▲17.3% YoY	▲15.1% YoY

Fawateer Daily Average	
Volume	Value
50,721	BD 3.8 mn
▲ 11.6% YoY	▲ 7.6% YoY

POS Transactions	
Volume	Value
88.7 mn	BD 2.0 bn
▲ 13.9% YoY	▲ 8.1% YoY

- Daily average (volume and value) for ATM Transactions continued decreasing trend for cash transactions by 8.3% and 7.6% compared to H1 2022.
- The daily average volume and value of cheques decreased over the same period by 3.5% and 3.9% respectively.
- Daily average of volume and value of Fawri+ transactions increased by 43.7 and 21.2% respectively in H1 2023 in comparison to H1 2022. The daily average of volume and value of Fawri Transactions increased by 17.3% and 15.1% in H1 2023 in comparison to H1 2022.
- Daily average of volume and value of Fawateer Transactions increased by 11.6% and 7.6% respectively in H1 2023 in comparison to H1 2022.
- POS and Ecommerce transactions (volume and value) increased by 13.9% and 8.1% respectively in H1 2023 with contactless transactions representing 78.6% and 52.3% respectively.

8.1 Overview

The payment landscape has moved from traditional systems to digital alternatives. Technologies have been introduced that address consumer and market dynamics and support the drive towards greater autonomy and flexibility. As a regulator and facilitator, CBB has supported the introduction and structured development of advanced payment systems that have enabled the growing digitalization of the financial sector. In The Kingdom of Bahrain and around the world, the pandemic served as a catalyst to accelerate the rapid digitalization of the payments as consumer preferences began to shift towards contactless payment.

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 improves 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 all FMIs, Payment and Settlement Systems in terms of compliance with the requirements set by the Principles for Financial Market Infrastructures (PFMI), CBB Law, and CBB's Directives. 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 second half of 2022 (from 1st July 2022 to 31st December 2022).

Point of Sale (POS) terminals, E-Commence and digital payments are other methods that enhance a customer's payment experience in Bahrain by providing payment solutions that support international and domestic payment schemes. Several digital wallets are established in Bahrain's FinTech ecosystem that offer various payment solutions. Seamless contactless and digital payments transactions are projected to be the prominent payment methods in the future.

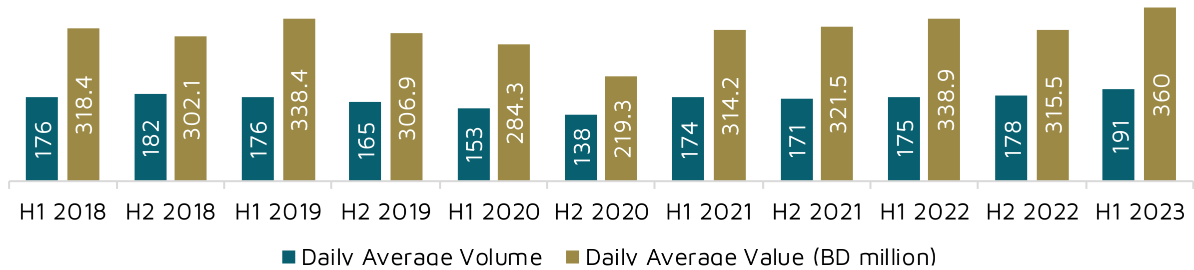
This chapter describes recent trends in FMIs, Payment and Settlement Systems, POS, and digital wallet transactions.

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 and 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-two (32) Participants including CBB. On Monday, 17th October 2022, Central Bank of UAE (CBUAE) joined the RTGS System as part of AFAQ.

[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.

Chart 0.1: RTGS Bank Transfers Daily Average Volume and Value



Source: CBB.

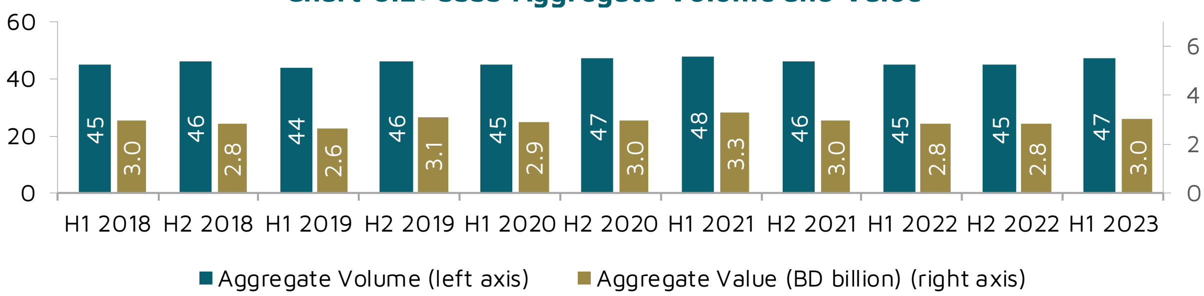
The daily average volume of Bank Transfers for H1 2023 increased by 9.1% from 175 to 191 Transfers when compared to H1 2022. [11] In addition, the daily average value of Bank Transfers for H1 2023 had increased by 6.2% from BD 338.9 million to BD 360.0 million when compared H1 2022.

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 14th June 2007 along with the RTGS System. The number of direct participants is thirty (30) participants whereas the indirect participants are twenty-nine (29) members in the SSSS.

The volume of issues in H1 2023 increased by 4.4% in comparison to H1 2022, from 45 issues to 47 issues in both halves. The aggregate value of issues in H1 2023 increased by 7.1% to BD 3.0 million from BD 2.8 billion in H1 2022.

Chart 0.2: SSSS Aggregate Volume and Value



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 2023 to 30th June 2023.

8.4 ATM Clearing System (ATM)

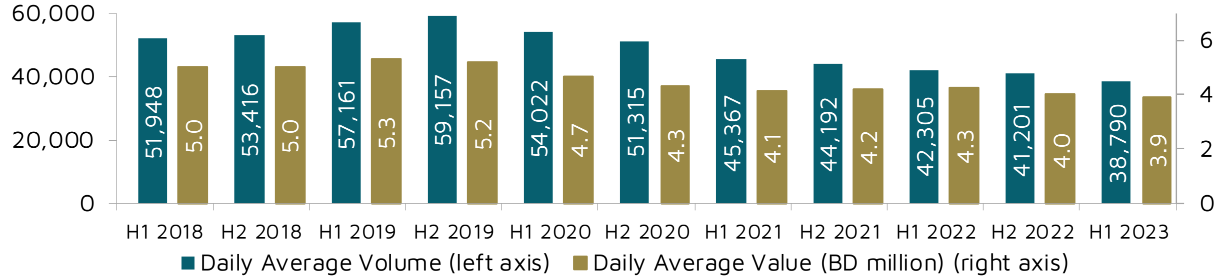
ATM clearing is based on a Deferred Net Settlement (DNS) system. The Benefit Company (BENEFIT) in Bahrain receives and processes all the ATM transactions. The GCC net, a leased line network across the GCC countries, provides for the communication backbone for the transmission of all the ATM Transactions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

The daily average volume of ATM Transactions for H1 2023 reached 38,790 transactions per day, an 8.3% decrease compared to 42,305 per day in H1 2022. The daily average

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

value of ATM Transactions for H1 2023 also decreased by 7.6% to reach BD 3.9 million when compared H2 2022 (BD 4.3 million).

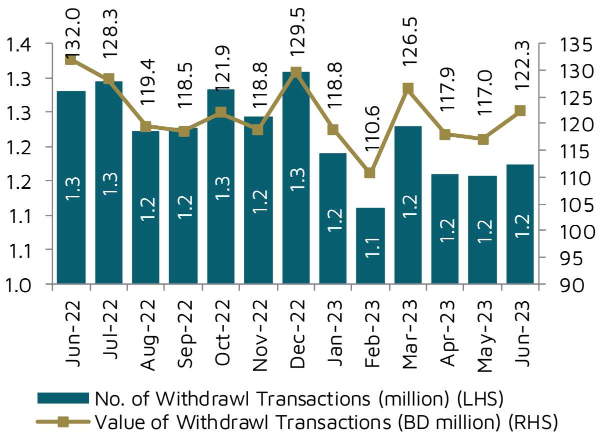
Chart 0.3: ATM Transactions Daily Average and Volume



Source: BENEFIT.

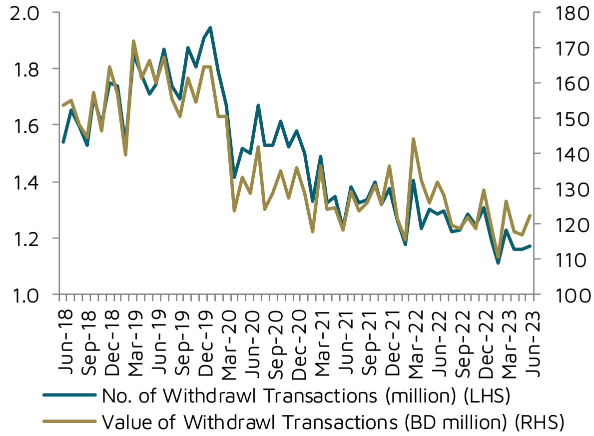
Overall, there is a continued downward trend in both the value and the volume of ATM transactions (Chart 8.5). In H1 2023, monthly volume of ATM transactions ranged between 1.1 and 1.3 million transactions while the value of ATM transactions ranged between BD 110.6 million and BD 126.5 million.

Chart 0.4: Number and Value of ATM Transactions, June 2022 – June 2023



Source: BENEFIT.

Chart 0.5: 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 BCTS is operated by BENEFIT and overseen by CBB.

The number of participants in the BCTS is 30 participants. The daily average volume of cheques for H1 2023 decreased in H1 2023 by 2.4% from 8,524 cheques in H1 2022 to 8,324 cheques. Furthermore, the daily average value of cheques decreased in H1 2023 by 2.6% from BD 30.0 million for H1 2022 to BD 29.2 million.

The BCTS continued to operate smoothly and efficiently for the period from 1st January 2023 to 30th June 2023. 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 Q1 2023 and Q2 2023, returned cheques declined from 2.9% to 2.8% as a percentage of total volume and the value increased from 3.4% to 4.5% as a percentage of total value.

Chart 0.6: BCTS Daily Average Volume and Value

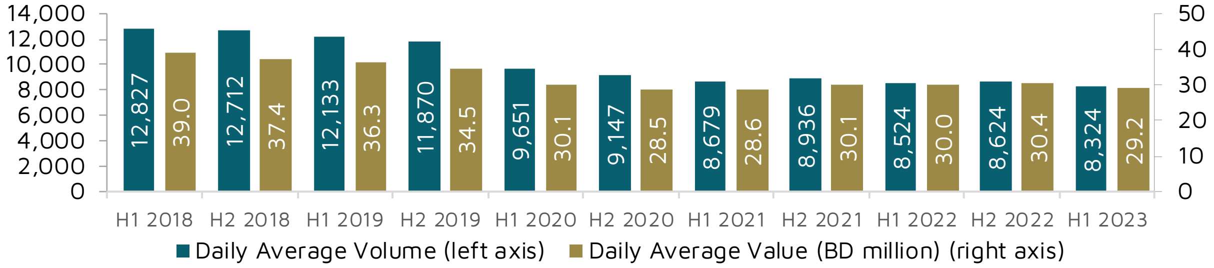
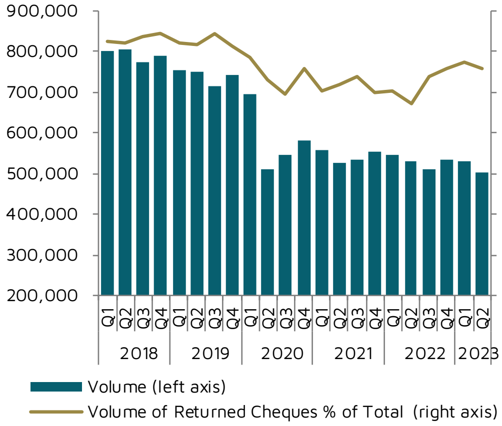
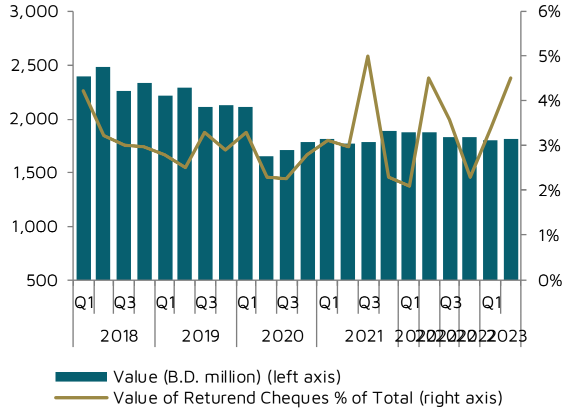


Chart 0.7: Volume of Issued Cheques and % of Returned Cheques



Source: *BENEFIT.*

Chart 0.8: Value of Issued Cheques and % of Returned Cheques (BD million)



Source: *BENEFIT.*

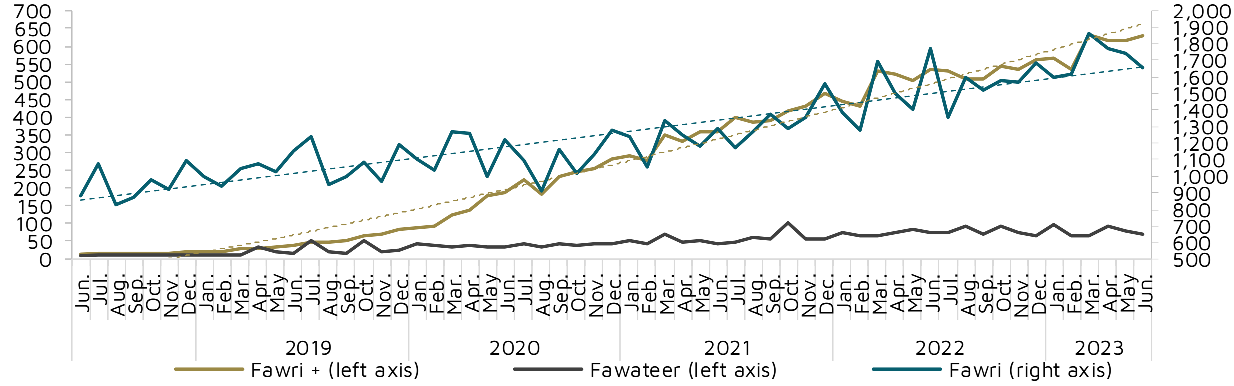
8.6 Electronic Fund Transfer System (EFTS) including Electronic Bill Presentment and Payment (EBPP) System

With the introduction of International Bank Account Number (IBAN) in January 2012, transfers became easier, less time consuming, and more secure for both customers and banks. The Electronic Fund Transfer System (EFTS) was launched on 5th November 2015 and the 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 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 and faster processes. The number of participants offering outward EFTS Services has reached twenty-six (26) participants.

Chart 8.9 shows an overall increasing trend in the monthly transfers in Fawri+, Fawri and Fawateer. The total value of Fawri+ transfers reached BD 3,593.3 million for H1 2023 increasing by 21.2% compared to H1 2022. Similarly, the total value of Fawri transfers increased by 13.3% for H1 2023 reaching BD 10,242.5 million. In addition, the value of Fawateer payments increased by 5.8% from to BD 469.6 million in H1 2023.

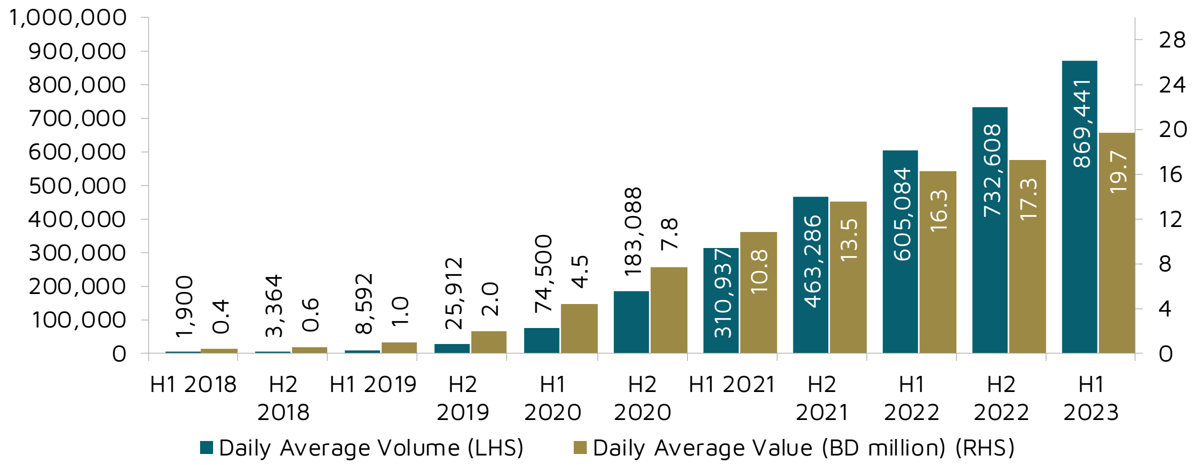
Chart 0.9: EFTS Fawri, Fawri+, and Fawateer Value (BD million)



Source: BENEFIT.

The daily average volume of Fawri+ transfers of H1 2023 when compared to H1 2022 increased by 43.7% from 605,084 transfers to 869,441 transfers. The daily average value of Fawri+ transfers increased by 21.2% in H1 2023 when compared to H1 2022 from BD 16.3 million to BD 19.7 million.

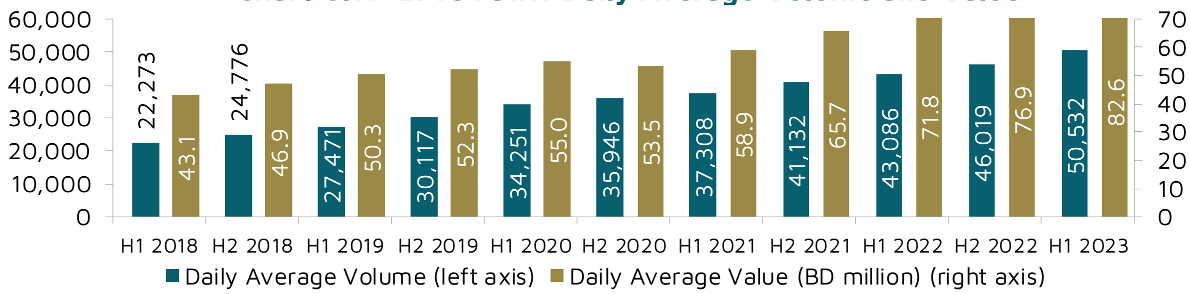
Chart 0.10: EFTS Fawri+ Daily Average Volume and Value



Source: BENEFIT.

The daily average volume of Fawri transfers in H1 2023 increased by 17.3% from the 43,086 transfers in H1 2022 to 50,532 transfers. In addition, the daily average value of Fawri transfers increasedby 15.1% in H1 2023, from BD 71.8 million in H1 2022 to BD 82.6 million in H1 2023.

Chart 0.11: EFTS Fawri Daily Average Volume and Value

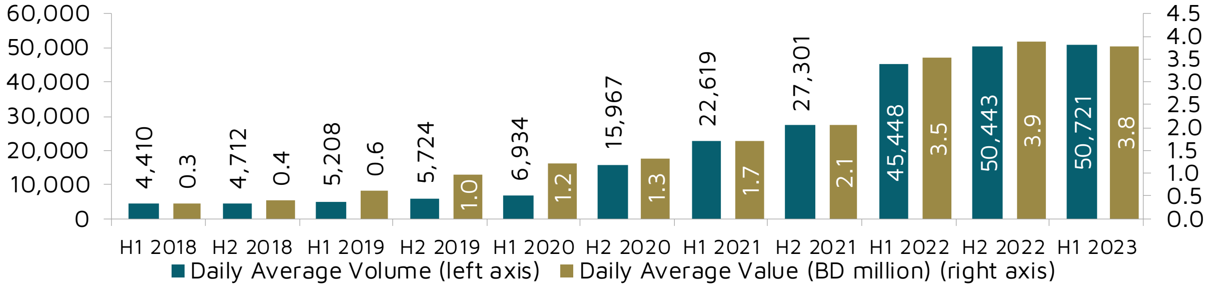


Source: BENEFIT.

The daily average volume of Fawateer Payments for the first half of 2023 increased slightly by 11.6% from the 45,448 payments in H1 2022. In addition, the daily average value of Fawateer reached BD 3.8 million in H1 2023 increasing by 7.6% compared to the BD 3.5 million in H1 2022.

The EFTS including EBPP continued to operate in a safe, efficient, resilient and reliable manner from 1st January 2023 to 30th June 2023. 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.

Chart 0.12: EBPP Fawateer Daily Average Volume and Value



Source: BENEFIT.

8.7 Point of Sale (POS) and E-Commerce

POS terminals are available at most business outlets in Bahrain to create a seamless payment experience for customers for effective digital transactions. The increase in POS terminals helps in achieving higher financial inclusion. POS transactions in Bahrain continue to show 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 2023 has reached 88.7 million transactions (13.9% increase compared to H1 2022). Similarly, the total value of transactions for 2022 increased to BD 2,032.8 million (8.1% increase compared to H1 2022). Both the volume and value of cards issues in Bahrain had increased by 11.4% and 6.5% respectively in H1 2023 when compared to H1 2022. The volume and value of transactions by cards issued outside Bahrain showed a significant increase of 25.6% and 15.5% respectively over the same period.

Table 0.1: Point of Sale (POS) and E-Commerce Transactions in Bahrain

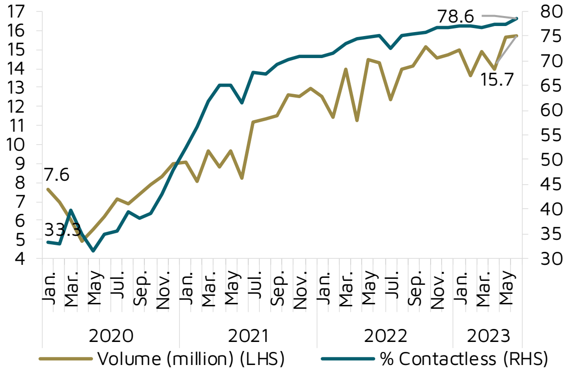
		Volume of transactions (million)			Value of transactions (BD million)		
		Cards issued in Bahrain	Cards issued outside Bahrain	Total	Cards issued in Bahrain	Cards issued outside Bahrain	Total
2018		49.0	15.4	**64.5**	1,524.1	453.2	**1,977.2**
2019		58.4	15.2	**73.7**	1,877.2	557.2	**2,434.4**
2020		77.3	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**
2022		132.1	30.7	**162.8**	3,090.8	753.8	**3,844.6**
2022	H1	64.3	13.6	**77.9**	1,534.8	344.8	**1,879.6**
	H2	67.8	17.1	**84.9**	1,555.9	409.0	**1,965.0**
2023	H1	71.6	17.1	**88.7**	1,634.6	398.3	**2,032.8**

Source: CBB.

Chart 8.13 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 H1 2023 shows the continued trend of people preferring to make direct payments to merchants through POS terminals instead of ATM/Cash withdrawals.

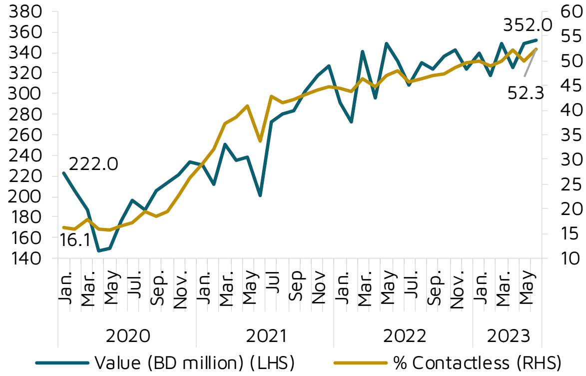
Contactless adoption continues to accelerate in the Kingdom due to the change in consumer spending habits. The percentage of contactless transactions in terms of volume increased from 33.3% in January 2020 to 78.6% in June 2023. Similarly, in terms of value, the percentage of contactless transactions increased from 16.1% in January 2020 to 52.3% in June 2023.

Chart 0.13: Volume of Monthly POS and E-Commerce Transactions (millions)



Source: CBB.

Chart 0.14: Value of Monthly POS and E-Commerce Transactions (BD million)

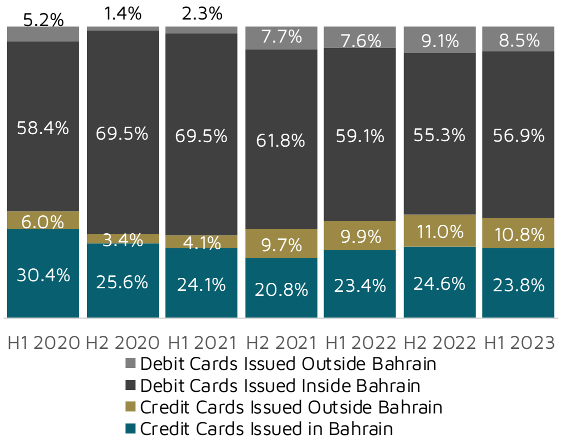


Source: CBB.

As of H1 2023, 80.7% of the volume of transactions and 80.4% of the value of transactions came from cards issued inside Bahrain (Chart 8.15 and Chart 8.17). 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.

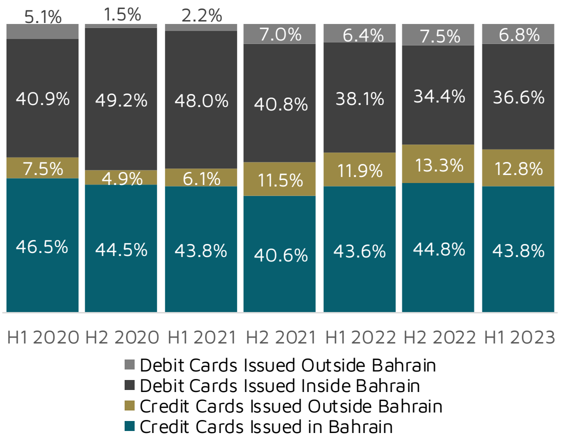
The volume of transactions remained to be from debit cards (representing 65.3% in H1 2023) while most of the value of transactions were from credit cards (representing 56.6% in H1 2023).

Chart 0.15: Volume of POS and E-Commerce Transactions (% by Card Type)



Source: CBB.

Chart 0.16: Value of POS and E-Commerce Transactions (% by Card Type)

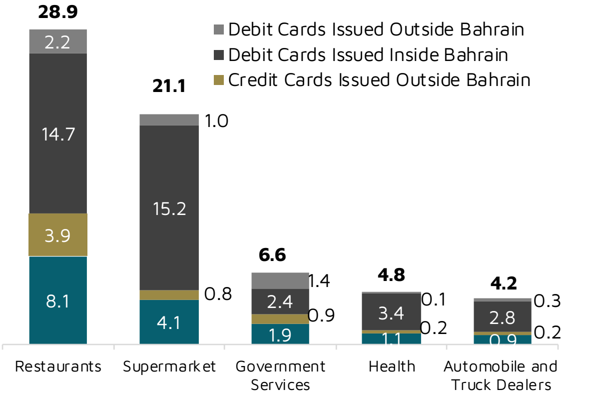


Source: CBB.

Charts 8.19 and 8.20 show the top 5 sectors in terms of volume and value of transactions for H1 2023. In terms of volume the top 5 sectors represented 74.0% of all the transactions for 2022 and were: restaurants (28.9 million), supermarkets (21.1 million), government services (6.6 million), health (4.8 million), and automobiles and truck dealers (4.2 million). The majority of the number of transactions for the restaurants, supermarket, government services, health, and department stores were made using debit cards issued inside Bahrain making 50.9%, 72.0%, 35.9%, 70.4% and 66.6% of the transactions respectively.

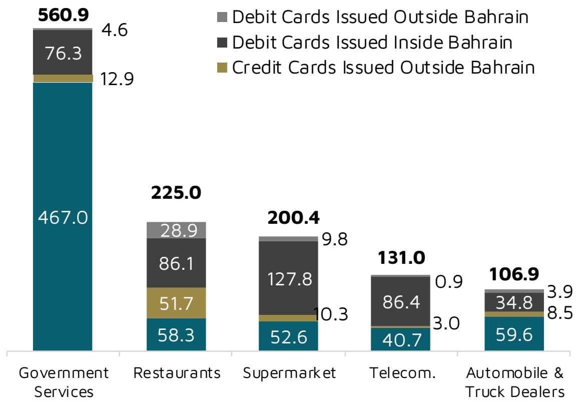
In terms of value, the top 5 sectors represented 60.2% of all transactions and were: government services (BD 560.9 million), restaurants (BD 225.0 million), supermarkets (BD 200.4 million), telecommunication (BD 131.0 million), automobile dealers (BD 106.9 million). For government services and automobile dealers, 83.3% and 55.8% of the value of transactions respectively were made by credit cards issued inside Bahrain. As for restaurants, supermarkets, and telecommunication 38.3%, 63.8%, and 65.9% of the value of transactions respectively were made by debit cards issued inside Bahrain.

Chart 0.17: Top 5 Sectors by Volume of POS and E-Commerce – H1 2023 (million)



Source: CBB.

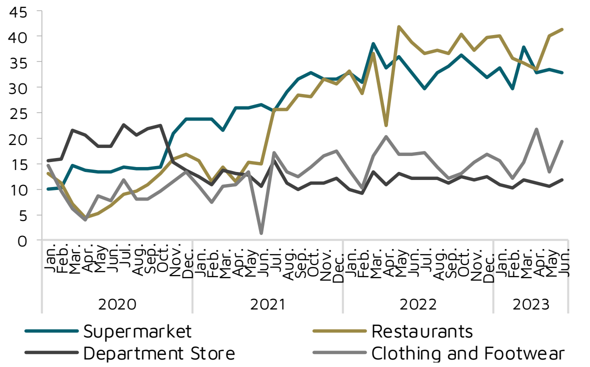
Chart 0.18: Top 5 Sectors by Value of POS and E-Commerce –H1 2023 (BD million)



Source: CBB.

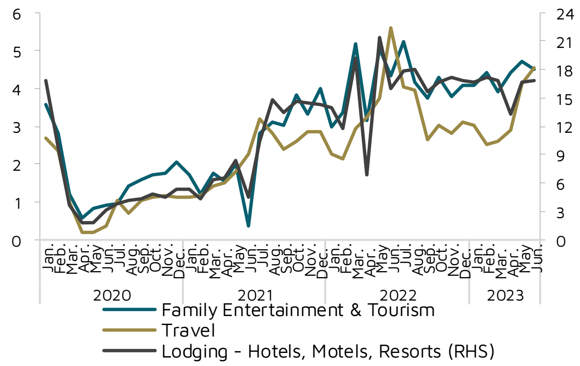
Charts 8.19 and 8.20 show the monthly value of POS transactions from January 2020 to June 2022 in selected sectors that have witnessed a change in consumer during the pandemic and sow continuous recovery and growth.

Chart 0.19: Monthly Value of POS and E-Commerce of Selected Indicators (BD million)



Source: CBB.

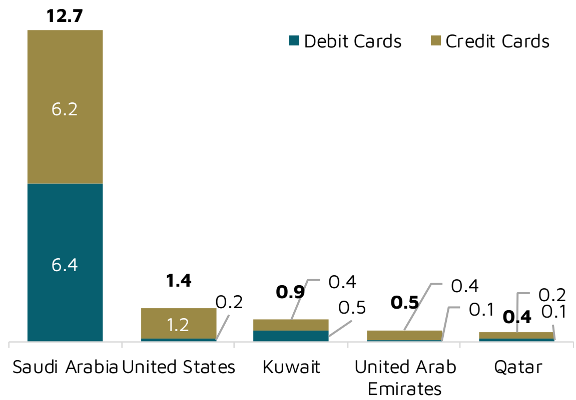
Chart 0.20: Monthly Value of POS and E-Commerce of Selected Indicators (BD million)



Source: CBB.

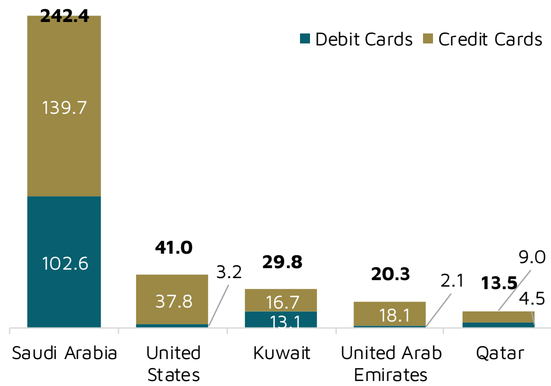
Charts 8.20 and 8.21 show the top 5 countries in terms of volume and value of foreign transactions for H1 2022. In terms of volume the top 5 countries represented 92.6% of total foreign transactions and were: Saudi Arabia (12.7 million), United States (1.4 million), Kuwait (0.9 million), United Arab Emirates (0.5 million), and Qatar (0.4 million).

Chart 0.21: Top 5 Nationalities by Volume of POS and E-Commerce – H1 2023 (million)



Source: CBB.

Chart 0.22: Top 5 Sectors by Value of POS and E-Commerce – H1 2023 (BD million)



Source: CBB.

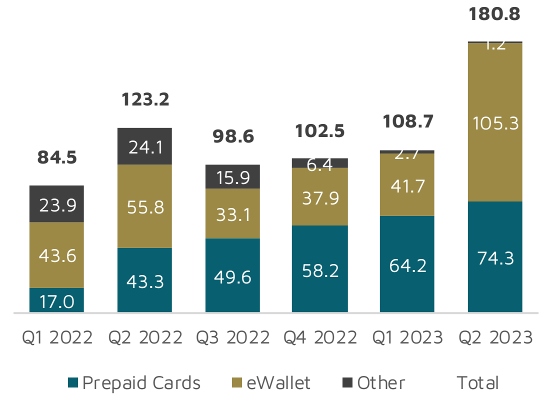
In terms of value, the top 5 countries represented 87.1% of the total value of foreign transaction and were: Saudi Arabia (BD 242.4 million), United States (BD 41.0 million), Kuwait (BD 29.8 million), United Arab Emirates (BD 20.3 million), and Qatar (BD 13.5 million).

8.8 Prepaid Cards and E-Wallets

Bahrain's appetite for digital payments is growing where significant steps have been made in realizing the nation's vision to become a technology pioneer. The Kingdom has been working towards a successful digital economy by building a proper ecosystem that provides a network of connected entities from CBB to banks, to telecommunication companies, to merchants and consumers.

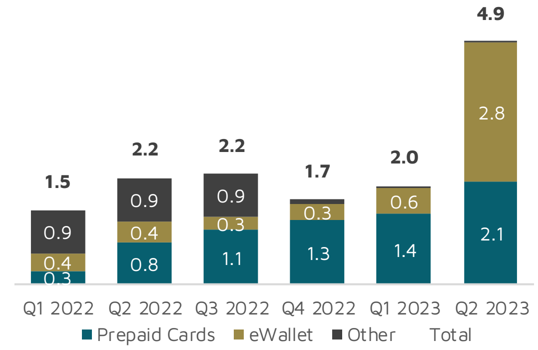
The volume and value of transactions through digital wallets (prepaid wallets and e-wallets) has been increasing significantly over the as provided in Charts 8.23 and 8.24, with an increasing trend in both the volume and value of transactions, indicating the continued success of adoption of these digital solutions.

Chart 0.23: Volume of Prepaid and E-Wallet Transactions (millions)



Source: CBB.

Chart 0.24: Value of Prepaid and E-Wallet Transactions (BD millions)



Source: CBB.

9 FINTECH, INNOVATION AND FINANCIAL INCLUSION

HIGHLIGHTS

Regulatory Sandbox	Bank Branches	ATMS
18	148	476
ATM Cards	**Debit Cards**	**Credit Cards**
2,121.0 thousand	1,822.6 thousand	272.0 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 in the region offering conventional and Shariah compliant FinTech solutions. The Kingdom is encouraging digital transformation and the adoption of innovative technology to create a more efficient financial services sector and achieve 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 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 within the Kingdom.

9.2 FinTech Developments

The CBB has developed its digital transformation strategy with a vision to develop projects that introduce the latest electronic payment and settlement products and FinTech projects facilitating more efficient provision of banking services. The digital transformation initiatives also focus on working with financial institutions to encourage and accelerate their transition with technological developments in line with international best practices to ultimately benefit the national economy. The CBB established a FinTech & Innovation Unit in October 2017, to ensure an adequate regulatory framework is in place to adapt FinTech solutions that will enhance services provided to individual and corporate customers.

9.2.1 Regulatory Sandbox

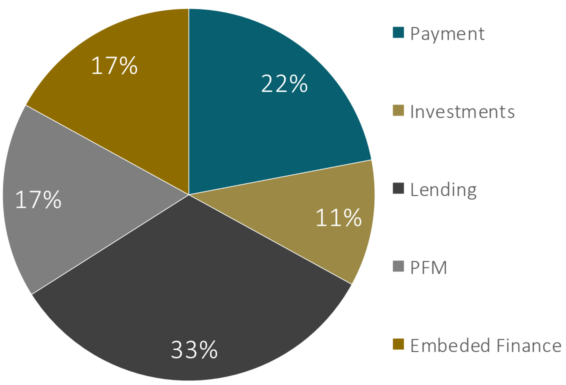
CBB launched a regulatory sandbox in June 2017 to attract both local and international emerging FinTech companies as well as existing CBB licensees to enable them to test their innovative ideas and expand their business in the region.[12] The sandbox provides authorized companies with the opportunity to test and experiment their innovative financial solutions freely until they are commercially viable. The Sandbox focuses on the following Innovation, Customer benefit, Identification of Major Risks, Compliance with CDD and AML/CFT Requirements, and Confidentiality Requirements.

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.

The CBB announced its new Regulatory Sandbox Framework in December 2021 to allow FinTech firms to test and experiment with 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 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, 2023, CBB had 18 companies testing their solutions within the Regulatory Sandbox with a wide range of solutions.

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



Payment	▪ Digitizing Payment Workflow ▪ Providing cashless and automated payments
Personal Finance Management	▪ Aggregates end-user's financial information into single interface ▪ Enhances finance management
Investments and Wealth Management	▪ Provides holistic financial advice. ▪ Aims to increase investments/returns
Lending	▪ Streamlines and automates lending process. ▪ Includes short-term financing.
Embedded Finance	▪ Provides financial services through non-financial products ▪ Offered by non-financial firms

Source: CBB.

Table 9.1: Regulatory Sandbox Statistics- Classification by Region

Region	No. of Sandbox Companies
MENA	16
Americas	1
Europe	1
Asia	0
Total	**18**

Source: CBB.

[12] 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.

9.2.2 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 cross-currency service allows its participants to transfer payments from one local currency to another local currency in real time within the business day schedule. The service was launched on 10th December 2020 with the CBB and Saudi Central Bank (SAMA) as its first participants, and in March 2022, the Central Bank of Kuwait joined the service. The CBB has successfully onboarded all its Retail Banks during the Year 2022, becoming the first central bank in the GCC to accomplish this milestone.

During 2023, the total number of outgoing retail transactions sent through AFAQ was 18,151 transactions with a total value of BHD 173.2 million (up to August 2023). On average the monthly outgoing retail payments volume is 2,270 transactions at an average value of BHD 21.6 million.

9.3 Financial Inclusion

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

Financial inclusion efforts in Bahrain aim to ensure that all businesses and households, have access the suitable financial services they need to engage in day-to-day transactions. CBB is taking a number of initiatives to further develop indicators related to financial inclusion. Figures show access to finance through a number of financial inclusion metrics (Table 9.2). The number of accounts within retail banks and the number of internet/PC linked accounts increased by 17.4% YoY and 24.5% YoY in 2022 respectively.

CBB is continuing its efforts to prioritize financial inclusion in terms of adopting and implementing a viable national strategy to 1) improving women's, SME, and young people's access to financial services 2) promoting the protection of consumers of financial services 3) improving and providing financial coverage data and statistics to support policy development, and 4) promoting awareness and financial education.

Table 9.2: Financial Inclusion Figures for the Kingdom of Bahrain

Indicator	2018	2019	2020	2021	2022*
Number of Banks **	29	29	29	29	29
Number of Branches	173	204	175	151	148
Number of Branches per 100,000 in population	*11.5*	*13.7*	11.9	10.1	9.7
Number of ATMs	*479*	515	505	461	476
Number of ATMs per 100,000 in population	*31.9*	*34.7*	34.3	30.6	31.2
Number of Accounts ***	1,907,307	2,108,637	2,026,890	2,457,448	2,885,562
Number of Accounts per 1,000 in population	*1,269*	*1,421*	1,376.8	1,633.6	1,892.6
Number of Internet/PC linked accounts	477,894	616,960	707,794	1,107,994	1,379,607
ATM Cards (thousands)	1,384.6	1,644.1	1,733.7	1,808.3	2,121.0
Debit Cards (thousands)	1,171.7	1,210.3	1,363.4	1,557.5	1,822.6
Credit Cards (thousands)	322.9	306.6	402.2	312.0	272.0
Population	1,503,091	1,483,756	1,472,204	1,504,365	1,524,693

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

9.4 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 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.

On 9th February 2023, the CBB organized a training workshop on cybersecurity for the banking sector, in the presence of CEOs, C-level executives and cybersecurity and technical staff. The event is part of the CBB's strategy to enhance cyber security practices and systems in the financial services sector, and its continuous efforts to maintain financial stability and ensure providing a safe environment for banking transactions.

The training workshop included an exercise in cyber resilience for the banking sector, with more than 80 participants from the CBB, participating local banks and The Benefit Company.

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 issued several amendments to Module CRA in March 2023 which included enhancements to cyber security requirements in line with other volumes after consulting the industry in August 2023.
2. The CBB issued new requirements for multi-factor authentication for money changers, financing companies, payment service providers and crowdfunding platforms in July 2023 after consulting with the industry in April 2023. Similar requirements were issued to crypto-asset licensees in September 2023.
3. The CBB also consulted on 'Proposed Financial Cybersecurity Controls' in November 2022 and on 'National Risk Management Framework for Information Security' in June 2023 which were both developed by National Cyber Security Centre (NCSC).

ANNEX:

FINANCIAL SOUNDESS INDICATORS AND SELECTED GRAPHS

ANNEX 1: SELECTED FINANCIAL SOUNDNESS INDICATORS (FSIs)

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

Indicator	Q2 2022	Q4 2022	Q2 2023
Capital Adequacy			
CAR (%) *	19.1	19.5	19.3
Tier 1 CAR (%) *	17.7	18.1	17.8
Assets-to-Capital (Times) *	8.7	8.2	9.0
Asset Quality			
NPLs (% of Total Loans)	3.3	3.0	3.1
Specific Provisions (% of NPLs)	69.9	68.5	61.8
Loan Concentration (Share of Top Two Sectors) (%)	30.8	30.3	30.8
Real Estate/ Construction Exposure (%)	25.4	25.6	24.1
Earnings			
ROA (%)	0.6		0.7
ROE (%) *	4.8		5.3
Net Interest Income (% of Total Income) **	68.6		66.9
Net Fees & Commissions (% of Total Income) **	13.3		10.8
Operating Expenses (% of Total Income)	46.1		44.4
Liquidity			
Liquid Assets (% of Total Assets)	25.7	25.3	23.4
Loan-Deposit Ratio (%)	63.9\	66.4	63.2

** 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 2022	Q4 2022	Q2 2023	Q2 2022	Q4 2022	Q2 2023
Capital Adequacy						
CAR (%) *	20.4	21.5	21.7	17.7	17.5	17.0
Tier 1 CAR (%) *	19.0	20.1	20.3	16.2	15.9	15.3
Assets-to-Capital (Times) *	7.3	6.8	6.8	9.5	8.8	10.3
NPLs Net Provisions to Capital (%) *	4.3	3.3	4.0	3.4	3.3	3.2
Asset Quality						
NPLs (% of Total Loans)	3.8	3.3	3.6	2.5	2.3	2.1
Specific Provisions (% of NPLs)	73.2	74.3	66.7	69.6	67.0	61.1
Net NPLs (% of Net Loans)	1.1	0.9	1.3	0.8	0.8	0.8
Loan Concentration (Share of Top Two Sectors) (%)	33.7	33.9	33.3	41.2	40.6	41.7
Real Estate/ Construction Exposure (%)	33.1	34.0	33.3	18.3	18.0	17.0
Earnings						
ROA (%)	0.8		0.9	0.6		0.7
ROA Local Banks (%)	0.8		1.0	0.2		0.3
ROA Overseas Banks (%)	0.6		0.8	1.0		1.2
ROE (%) *	6.6		7.1	2.3		3.2
Net Interest Income (% of Total Income)	74.5		77.8	63.5		58.2
Net Fees & Commissions (% of Total Income)	10.0		8.4	17.2		12.2
Operating Expenses (% of Total Income)	42.1		39.4	44.1		41.5
Liquidity						
Liquid Assets (% of Total Assets)	34.1	32.8	30.9	21.9	22.9	19.9
Liquid Assets (% of Short-Term Liabilities)	42.7	41.9	39.6	26.8	28.6	25.1
Loan-Deposit Ratio (%)	68.1	68.8	71.4	61.8	68.3	62.1
Non-Bank Deposits (% of Total Deposits)	76.6	76.0	76.0	52.3	54.1	47.6

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

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

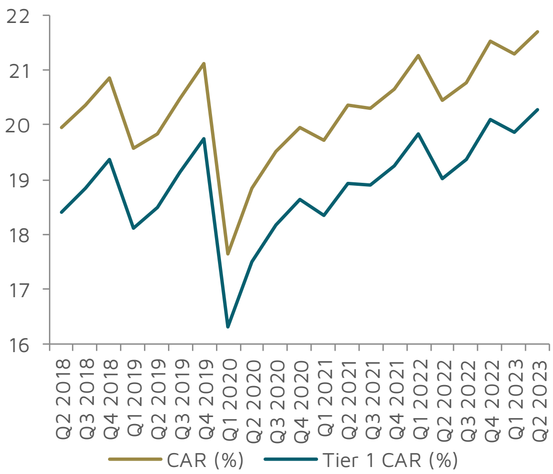
Indicator	Islamic Retail			Islamic Wholesale		
	Q2 2022	Q4 2022	Q2 2023	Q2 2022	Q4 2022	Q2 2023
Capital Adequacy						
CAR (%) *	21.5	21.2	21.4	15.3	16.9	17.2
Tier 1 CAR (%) *	19.9	19.7	19.5	14.7	16.2	16.3
Assets-to-Capital (Times) *	11.4	11.3	12.5	8.6	8.9	9.0
NPFs Net Provisions to Capital (%) *	12.0	13.2	17.1	1.5	0.5	2.0
Asset Quality						
NPFs (% of Total Facilities)	4.4	4.8	5.0	6.3	4.8	5.3
Specific Provisions (% of NPFs)	59.0	54.8	49.6	86.7	94.9	81.5
Net NPFs (% of Net Facilities)	2.0	2.3	2.6	0.7	0.6	1.0
Facilities Concentration (Share of Top Two Sectors) (%)	39.8	41.5	39.4	61.1	60.6	63.6
Real Estate/ Construction Exposure (%)	28.8	30.3	26.3	25.9	26.7	22.3
Earnings						
ROA (%)	0.4		0.4	0.6		0.7
ROE (%) *	5.4		4.9	5.0		5.8
Net Income from Own Funds, Current Accounts and Other Banking Activities (% of Operating Income)	28.0		51.5	44.3		63.4
Net income from Jointly Financed Accounts and Mudarib Fees (% of Operating Income)	70.9		41.9	48.0		28.0
Operating Expenses (% of Total Income)	64.5		69.2	50.8		52.1
Liquidity						
Liquid Assets (% of Total Assets)	18.9	17.0	19.1	17.4	13.8	20.2
Facility-Deposit Ratio (%)	65.1	62.1	63	35.2	33.5	24.8
Current Accounts from Non-Banks (% of Non-Capital Liabilities, excl. URIA)	42.2	36.5	38.3	5.8	3.5	5.0

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

ANNEX 2: SELECTED FSIs GRAPHS

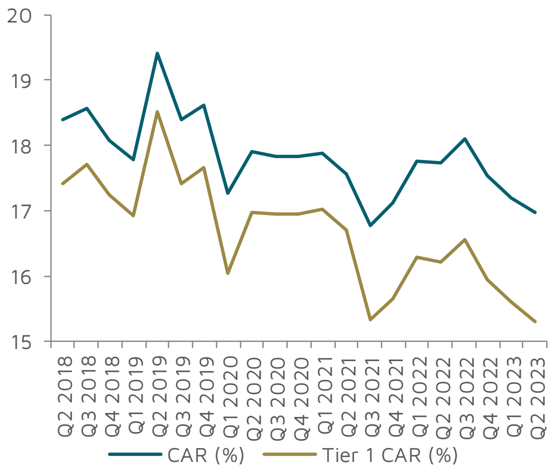
A. Capital Adequacy

Annex 2 Graph 1: Conventional Retail



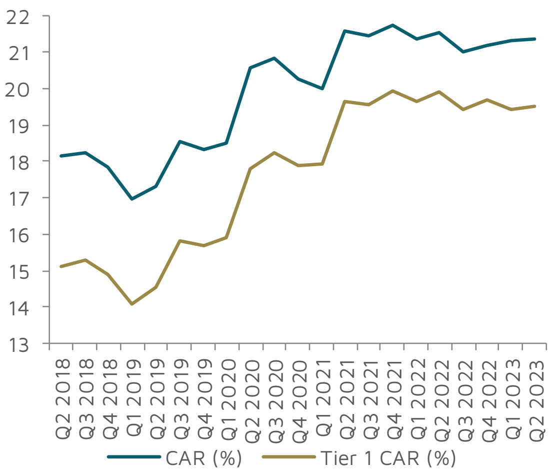
Source: CBB.

Annex 2 Graph 2 : Conventional Wholesale



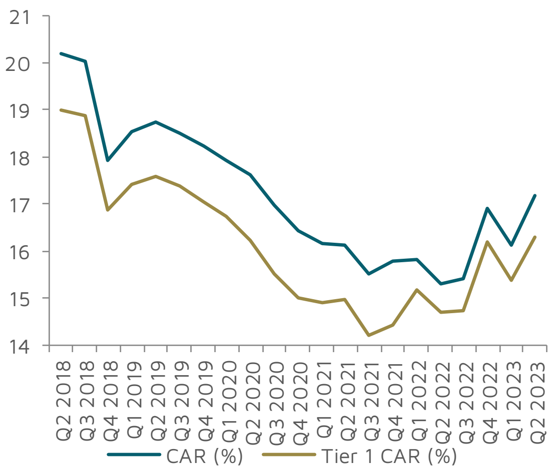
Source: CBB.

Annex 2 Graph 3: Islamic Retail



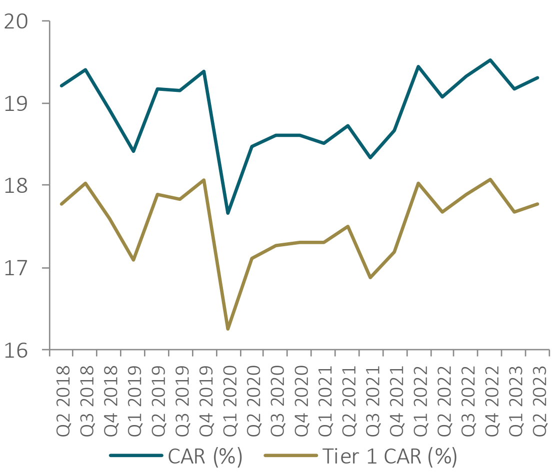
Source: CBB.

Annex 2 Graph 4: Islamic Wholesale



Source: CBB.

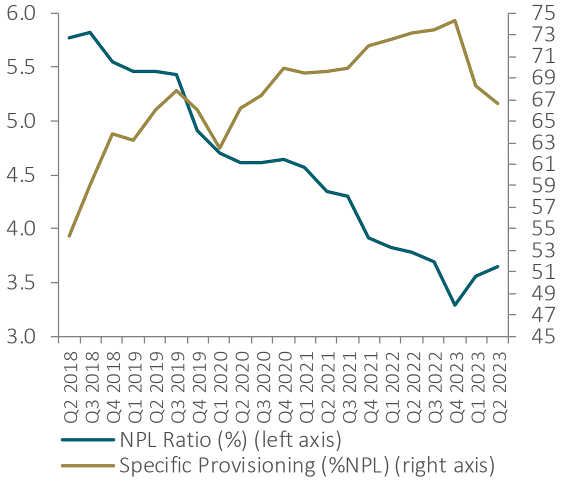
Annex 2 Graph 5: All Banking



Source: CBB.

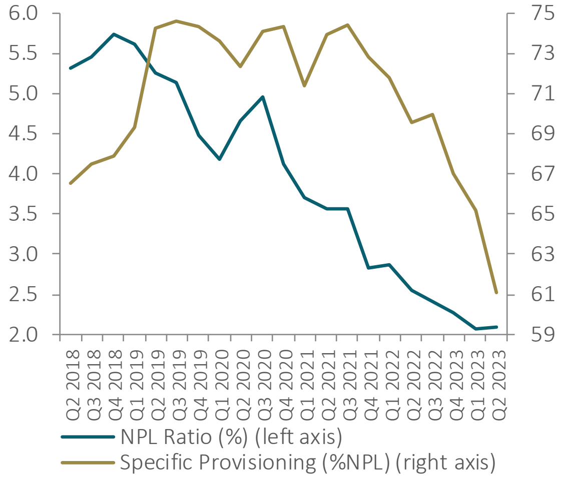
B. Asset Quality

Annex 2 Graph 6: Conventional Retail



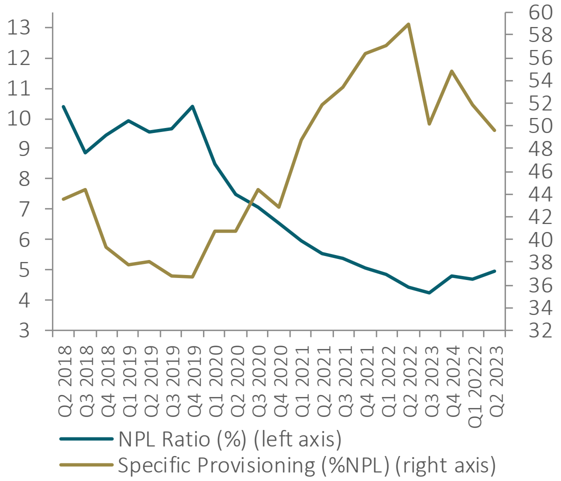
Source: CBB.

Annex 2 Graph 7: Conventional Wholesale



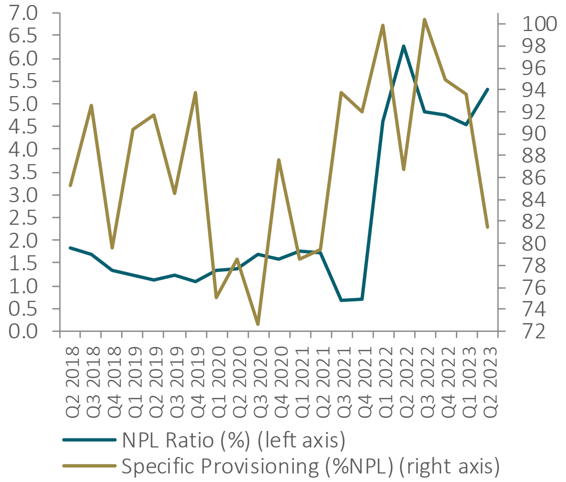
Source: CBB.

Annex 2 Graph 8: Islamic Retail



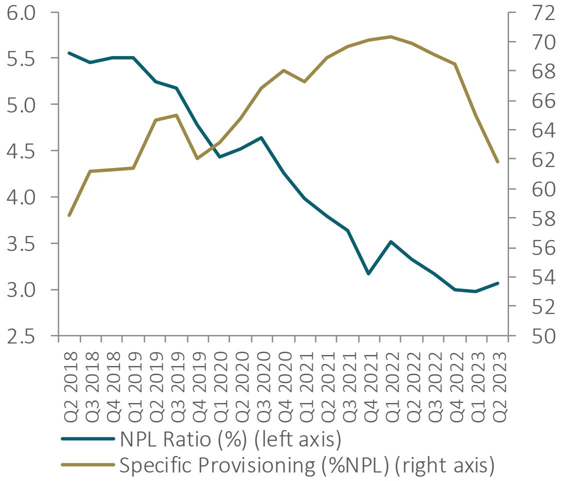
Source: CBB.

Annex 2 Graph 9: Islamic Wholesale



Source: CBB.

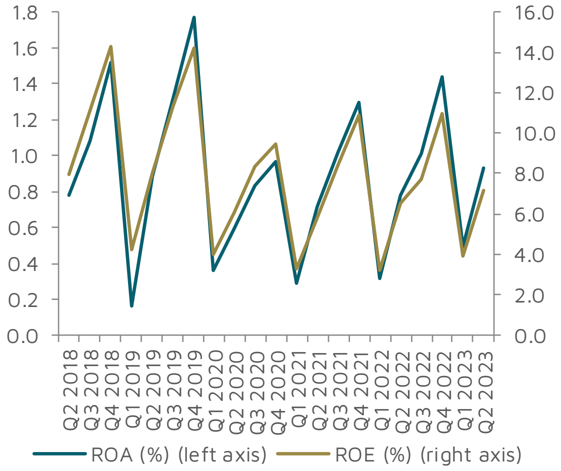
Annex 2 Graph 10: All Banking



Source: CBB.

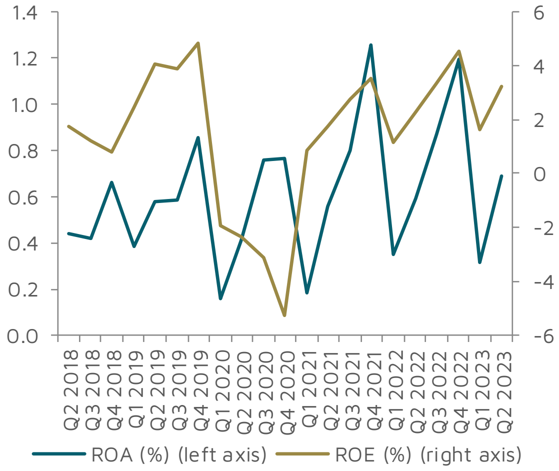
C. Profitability

Annex 2 Graph 11: Conventional Retail



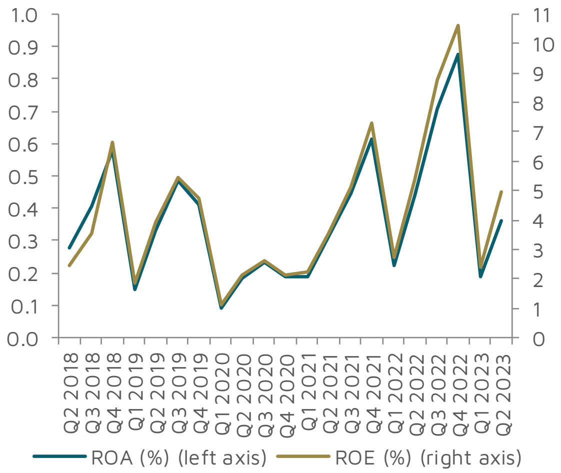
Source: CBB.

Annex 2 Graph 12: Conventional Wholesale



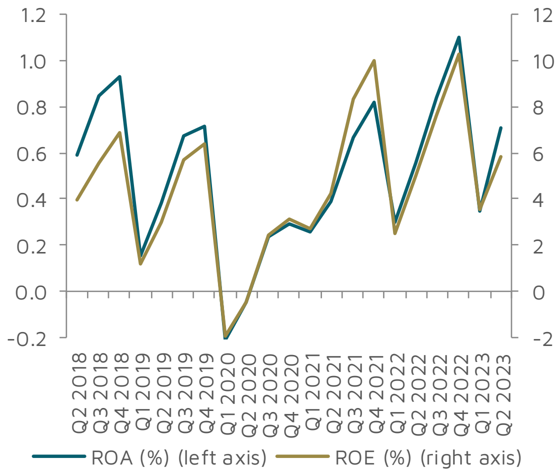
Source: CBB.

Annex 2 Graph 13: Islamic Retail



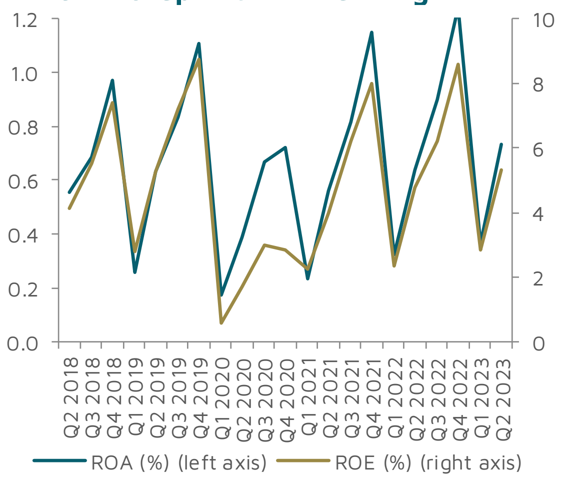
Source: CBB.

Annex 2 Graph 14: Islamic Wholesale



Source: CBB.

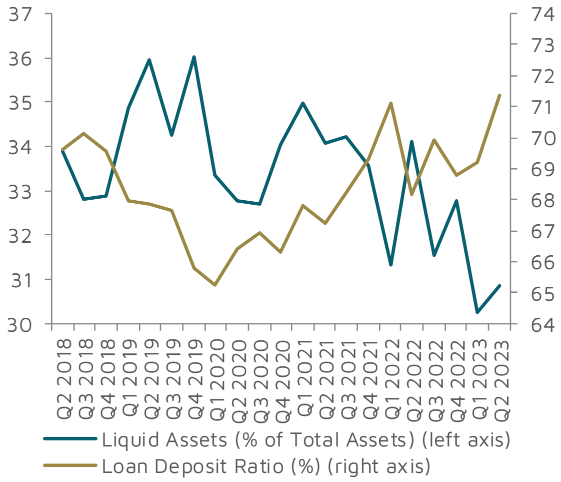
Annex 2 Graph 15: All Banking



Source: CBB.

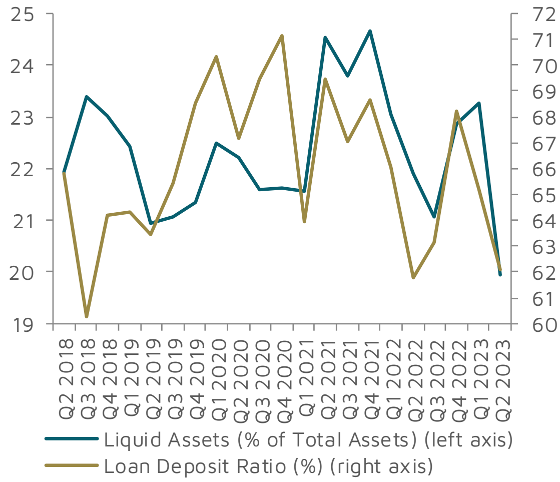
D. Liquidity

Annex 2 Graph 16: Conventional Retail



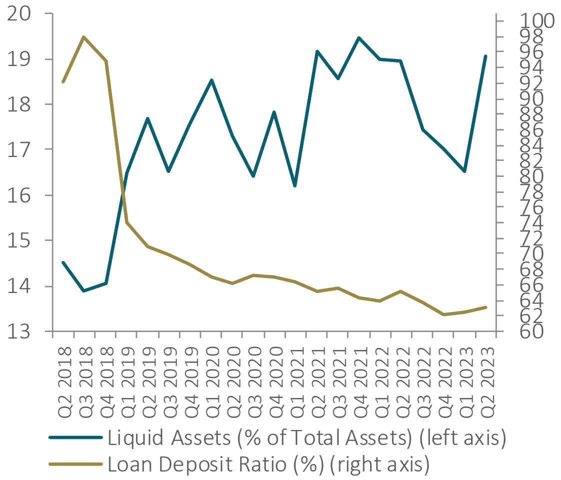
Source: CBB.

Annex 2 Graph 17: Conventional Wholesale



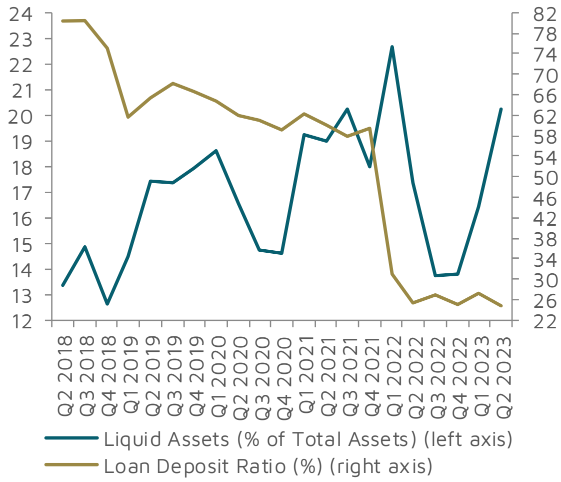
Source: CBB.

Annex 2 Graph 18: Islamic Retail



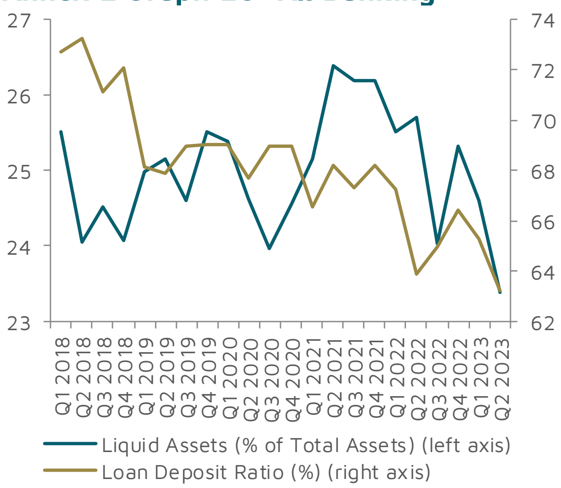
Source: CBB.

Annex 2 Graph 19: Islamic Wholesale



Source: CBB.

Annex 2 Graph 20: All Banking



Source: CBB.

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
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
WEO	World Economic Outlook