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26th October 2015
Burgan Bank's Financial Strength Rating Upgraded – Outlook Revised to 'Stable' from 'Positive'

Capital Intelligence (CI), the international credit rating agency, announced today that it has raised Burgan Bank's (BB) Financial Strength Rating (FSR) to 'BBB+' from 'BBB'. The upgrade is supported by the Bank's improved asset quality in recent years coupled with strengthened cover for non-performing loans (NPLs), comfortable liquidity and large capital injections in 2014. The geographically diversified asset base and revenue streams are also supporting factors to some degree. The FSR is constrained by BB's high indirect exposure to non-investment grade sovereigns through subsidiary banks in Turkey and Jordan, the considerable exposure to related parties, and by customer concentrations in deposits and to a lesser extent in loans (although this is to an extent systemic). Also constraining the rating is the still modest net profitability (despite the recent rebound), and the ongoing challenging regional operating environment. Accordingly, the Outlook for the FSR is revised to 'Stable' from 'Positive'.

The Bank's Support Level of '2' is affirmed, reflecting the explicit government guarantee of customer deposits held with banks within Kuwait, which remains in force, as well as the high likelihood of official and shareholder financial support, in case of need. In view of this support, CI maintains the Bank's Long-Term Foreign Currency (FC) Rating at 'A-' and the Short-Term FC Rating at 'A2'. The Outlook on the FC ratings is maintained 'Stable'.

BB, currently Kuwait's second largest conventional commercial bank by consolidated assets, is majority owned by Kuwait Projects Company Holding (KSC) (KIPCO). KIPCO, one of the largest holding companies in the MENA region, has held an effective controlling interest in the Bank for nearly two decades. BB's risk asset profile was significantly modified over the recent past after it acquired (and integrated) four MENA regional banks from KIPCO group sister company United Gulf Bank. While BB has become one of the most regionally diversified Kuwaiti commercial banks with a clear focus on the MENA region, the takeover of the bank subsidiaries raised its risk exposure to low rated sovereigns (namely Jordan, Algeria, Iraq, Tunisia and, more recently, Turkey) from an earlier negligible level. The economy and operating environment in these countries remains challenging while the underlying credit and political risks have increased.

Although NPLs rose moderately in recent periods, following previous successive declines, the NPL to gross loans ratio remained at a very satisfactory level, while increased loan-reserves continued to provide more than full cover. This, together with a strong capital base means that the Effective Coverage Ratio is also strong. Liquidity, as measured by key indicators, remains good and among the best in the Kuwaiti market, reflecting BB's slightly lower share of loans in total assets, combined with its larger stock of liquid assets. However, CI notes that a significant proportion of this liquidity is at the subsidiary banks' level. The Bank's funding is sourced predominantly from customer deposits and these continue to grow at a healthy pace. On a positive note, concentrations in the customer deposit base have reduced, placing the Bank in good stead given the prospect of tightening liquidity conditions in the Kuwaiti market in the near to medium-term and the associated increase in funding risk.

BB's balance sheet is comfortably capitalised, following a Perpetual Tier 1 issue as well as the successful rights issue in 2014. This has helped maintain the capital adequacy ratio (CAR) at a satisfactory level, although the CAR declined as a result of Basel III implementation. Nonetheless, the Bank's leverage, as measured by the ratio of total capital to total assets, improved noticeably following the capital injection, and remained sound at the current mid-year. Internal capital generation recovered as a result of a rebound in net profitability and a significantly reduced dividend payout. However, while operating profitability has remained satisfactory, the return on average assets (ROAA) remains modest in part due to ongoing provision charges, including a significant level of general provisions. Gross income generation remains good nevertheless, reflecting multiple sources of revenue, while operating profitability at the current level provides the flexibility to step up provisioning if necessary.

BB commenced operations in 1977 as a government-owned bank. In 1997, the Bank was privatised with KIPCO obtaining control. During 2007, KIPCO increased its ownership in BB to 43.01%, cementing BB's status as the largest and core member of the KIPCO Group. The second largest shareholder is UGB (17.86%) in Bahrain. Through its domestic network of 27 branches, which is supplemented by

121 ATMs, the Bank provides corporate/commercial banking, as well as retail and private banking. As at end-June 2015, total assets rose to KWD7.98 billion (USD26.4 billion) and total capital reached KWD947mn (USD3.13 billion).

CREDIT RATINGS

Foreign Currency		Financial Strength	Support	Outlook	
LT	ST			FC	FSR
A-	A2	BBB+	2	Stable	Stable

Unquote.