



Kingdom of

Bahrain

Bahrain Monetary Agency

2004

Annual Report



His Highness
Shaikh Khalifa Bin Salman Al Khalifa
The Prime Minister



His Majesty
King Hamad Bin Isa Al Khalifa
King of Bahrain



His Highness
Shaikh Salman Bin Hamad Al Khalifa
The Crown Prince
Commander-in-Chief
of the Bahrain Defence Force

Board of Directors



His Highness
Shaikh Khalifa Bin Salman Al Khalifa

The Prime Minister
Chairman



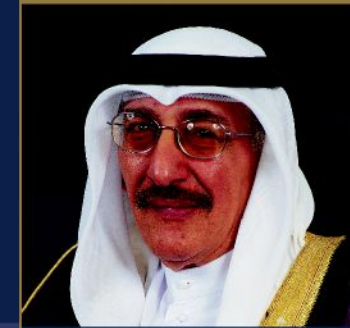
His Excellency
Shaikh Ahmed Bin Mohammed
Al Khalifa

Minister of Finance
Deputy Chairman



His Excellency
Rasheed Mohammed Al Maraj

Governor



Mr. Khalid Mohammed Kanoo

Chairman of Bahrain Chamber of
Commerce & Industry



Mr. Khalid Hussain Al Maskati

Businessman

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Foreword

I am pleased to present the 31st Annual Report of the Bahrain Monetary Agency. This report reviews the economic events of 2004 and the impact of these events on Bahrain and our financial sector. The report also summarises the main policy initiatives undertaken by the BMA during the year and presents our audited financial accounts for the fiscal year ending on December 31, 2004.

The international economy enjoyed one of its best years ever in 2004. After growing strongly in 2003, world economic output increased by 5.1% in 2004. While the advanced economies did well (growing at 3.4%, led by the United States at 4.4%), the strongest growth was in Asia (up 8.2%, led by China at 9.5%). The Middle East area, while not matching the Asian performance, also did well, growing at 5.5% in 2004. Inflation remained relatively subdued over the year, in spite of the strong growth, averaging 2% in the advanced economies and 5.7% in the emerging market economies. Commodity prices were strong; the price for oil averaged \$37.76 a barrel over the year (compared to \$29.00 in 2003) and was generally on an upward trend during the year. Oil prices have remained strong in 2005.

The Bahrain economy also had a good year. GDP at current prices grew by 13.5% and GDP at constant prices grew by 5.4% in 2004. The fiscal account recorded a net surplus of BD 60 million in 2004 or 1.4% of GDP. Bahrain's trade balance remained in surplus during 2004 for the sixth consecutive year. The current account surplus increased from BD 75.5 million in 2003 to BD 156.1 million in 2004. Bahrain's overall balance of payments was in surplus by BD 59.4 million for the year. Netting out the changes in total assets and total liabilities, Bahrain's net international asset position rose by 5% in 2004, to BD 2,100 million.

As part of its policy to liberalise the economy, Bahrain announced in June 2004 that the telecommunications market would be fully open to competition, commencing immediately. This gives Bahrain the first fully liberalised telecommunications market in the region.

A number of important investment projects were also completed in 2004 and several more

were initiated. Among the completed projects were the Shaikh Khalifa Bin Salman Causeway, the second phase of the Hidd power & water station, some of the major electrical transmission and substations and the upgrade of the taxiway to an emergency runway at Bahrain International Airport. A new industrial area was also established in Hidd and the reclamation works for Shaikh Khalifa Bin Salman Port were also finished. During 2004, the Bahrain private sector commenced work on a number of major long-term investment projects, including the Bahrain Financial Harbour, the Amwaj Islands and Durrat al Bahrain, and a major expansion of the Sheraton Towers.

The international credit rating agencies of Standard & Poors and Fitch, both of which visited Bahrain in late 2004, reaffirmed Bahrain's A- (investment-grade) credit rating for foreign currency debt. S&P gave Bahrain a "positive" outlook, while Fitch gave a "stable" outlook.

The 2004 IMF Article IV Consultation noted that Bahrain has "one of the most advanced economies in the region, with liberal exchange rate, trade and investment regimes". The IMF report also said that the Bahrain authorities have "done a commendable job in managing the economy".

During 2004, the IMF reviewed the financial sector performance of countries in the Middle East and North Africa. The review looked at financial sector development, openness and quality of management. Bahrain earned the highest overall score, the only country in the region to receive a "very high" rating.

The financial sector in Bahrain had a good year in 2004. The gross domestic output of the financial sector grew by 35.0% and contributed to 24.2% of total GDP at constant prices. Based on preliminary non-audited results, net profits of the banking sector more than doubled from the previous year. The consolidated balance sheet increased almost 18% in 2004, to reach US\$ 118.9 billion. The consolidated balance sheet of the full commercial banks grew the fastest during the year, up by almost 20%. By the end of 2004 there were 24 Islamic banks, with consolidated assets of US\$ 5.4 billion.

There were 23 new licenses issued during the year; 3 to full commercial banks, 5 to offshore banking units, 1 to an investment bank, 6 to insurance companies and 8 to other financial institutions.

With the Bahrain economy growing strongly, the currency in circulation rose by 11.5% over the year, to BD 17.9 million. In line with this increase, the higher monetary aggregates also grew, with M3 (currency in circulation, plus demand, savings and government deposits) up by 8.1%. This rise is in line with the monetary expansion necessary to accommodate Bahrain's economic performance.

Interest rates on dinar loans were largely unchanged during 2004, falling by only a few basis points. The average interest rate on business loans declined by 7 basis points to 5.27% during the year. Similarly, the average interest rate on personal loans fell 16 basis points to 7.73%. With international interest rates trending upwards near the end of 2004, the rate on fixed term deposits (3-12 months) had increased by 128 basis points by the end of 2004.

In September 2004, Bahrain and the USA signed the Bahrain-USA Free Trade Agreement, the first in the Gulf region. The Agreement now awaits ratification in the American Congress and the Bahrain Parliament. The BMA took a leading role in negotiating the financial services section of the Agreement. The resulting increase in investment by American financial institutions will reinforce Bahrain's position as the premier financial centre in the Middle East.

Since becoming the single regulator in 2002, the BMA has pursued a multi-year programme to integrate the regulation of the financial sectors. New regulations were issued in 2004 to prevent money laundering and insider trading in capital markets. New guidelines were issued covering the issuing of debt securities. Resolutions were issued for special purpose vehicles to register mutual funds, asset backed securities, Sukuks and captive insurance companies. Volume 1 of the BMA Rulebook, containing regulations applicable to conventional banks, was issued in October. When completed, the Rulebook project will consolidate all of the BMA's regulations.

During 2004, consultation papers were issued on securities and exchange regulation, updated risk management and financial crime regulations for the banking sector, as well as five consultation papers covering a proposed new insurance regulatory framework.

In 2004, the BMA also consulted on the proposed single license framework. When in place, the single framework will change the licensing of financial institutions in Bahrain, emphasising the activities the firm undertakes, rather than the nature of the institution. This will be consistent with best global regulatory practices.

The success that the BMA has achieved in 2004 would not have been possible without the strong support of others. I would particularly like to thank His Majesty, King Hamad Bin Isa Al Khalifa; His Highness the Prime Minister, Shaikh Khalifa Bin Salman Al Khalifa; and His Highness the Crown Prince and Commander-in-Chief of the Bahrain Defence Force, Shaikh Salman Bin Hamad Al Khalifa, for their continued guidance and support of the Bahrain Monetary Agency.

In addition, I would like to thank my predecessor, H.E. Shaikh Ahmed Bin Mohammed Al-Khalifa Minister of Finance, for his dedication to strengthening the Bahrain Monetary Agency and to raising the profile of Bahrain as a major financial sector.

I also extend my sincere appreciation to all the Government Ministries and Agencies that the BMA works with, for their continued cooperation. The leaders of Bahrain's financial firms have also played a major part in the BMA's success over the last year. They are our partners in ensuring the health and future of Bahrain's financial sector, and their help and cooperation is essential to our success. Finally, I would like to recognise the contribution that the personnel of the Agency have made in ensuring that the BMA can carry out its responsibilities efficiently and effectively.

Rasheed M. Al-Maraj
Governor

Our Vision

To strengthen the position of Bahrain as a major international financial centre through the application of sound monetary and financial policies consistent with international best practices.

Our Mission

To ensure monetary and financial stability in the Kingdom of Bahrain.

To regulate, develop and maintain confidence in the financial sector.

The BMA will carry out its mission through:

Providing central banking services to the government and the financial sector that are cost effective, reliable and that support national objectives and Bahrain's position as a leading financial centre,

Ensuring that the regulation and supervision of the financial sector of Bahrain meets the highest international standards, while maintaining Bahrain's reputation for market friendly regulation and encouraging ongoing investment by leading global firms in the Bahrain financial sector,

Ensuring the consistent application of regulatory standards in banking, insurance and capital markets, as well as encouraging an open and cooperative approach in dealing with financial institutions,

Working with international organisations such as the International Monetary Fund (IMF), the Bank for International Settlements (BIS), the International Organisations of Securities Commissions (IOSCO), the International Association of Insurance Supervisors (IAIS) and the Financial Action Task Force (FATF), in order to foster the stability of the global financial system,

Facilitating market innovation, including the development of Islamic banking and finance and encouraging the use of training and technology to ensure Bahrain's financial sector is globally competitive,

Promoting a culture of excellence within the BMA work environment that emphasises the highest standards of professionalism, integrity, prudence, teamwork and innovation.

Main Economic Indicators 2004

Total Population	707,160
Bahraini	438,209
Non-Bahraini	268,951
Growth Rate (%)	2.6
Total Employment	285,390
Private Sector	247,814
Public Sector	37,576
Gross Domestic Product (GDP)	
Current GDP (BD Millions)	4140.5
Growth Rate (%)	13.5
Non-oil GDP Growth Rate (%)	15.7
Constant GDP (BD Millions)	3237.6
Growth Rate (%)	5.4
Non-oil GDP Growth Rate (%)	8.6
GDP per Capita (BD)	5855.2
Public Finance (BD Millions)	
Total Revenue	1300.4
Oil Revenue	943.8
Non-oil Revenue	356.6
Total Expenditure	1104.6
Current Expenditure	864.0
Projects Expenditure	240.6
Surplus (Deficit)	60.0
As a % of GDP	1.4
Trade Balance	
Total Exports (BD Millions)	2,827.0
Total Imports (BD Millions)	2,438.2
Trade Balance (BD Millions)	388.8
Balance of Payments	
Current Account (BD Millions)	156.1
Overall Balance (BD Millions)	59.4

Monetary Aggregates	
Currency in Circulation (BD Millions)	173.7
M1 (BD Millions)	861.1
M2 (BD Millions)	2,879.6
M3 (BD Millions)	3,545.8
Banking System Total Assets/Liabilities (US\$ Billions)	118.9
Consolidated Balance Sheet of Commercial Banks (BD Millions)	5,498.3
Total Domestic Deposits (BD Millions)	3,326.6
Loans & Advances (BD Millions)	2,230.7
Interest Rates on Deposits	
Time (3-12 months)	1.96
Savings	0.35
Interest Rates on Loans	
Business	5.27
Personal	7.73
Consolidated Balance Sheet of Offshore Banking Units (US\$ Billions)	98.1
Consolidated Balance Sheet of Investment Banks (US\$ Billions)	6.2
Consolidated Balance Sheet of Islamic Banks (US\$ Billions)	5.4
Domestic Public Debt	
Total Outstanding (BD Millions)	585.5
Treasury Bills	130.0
Islamic Leasing Securities	427.3
Al Salam Islamic Securities	28.2
BD Exchange Rates Against Major Currencies	
US Dollar	0.376
Pound Sterling	0.723
Euro	0.512
Japanese Yen	3.620
Swiss Franc	0.332
Bahrain Stock Exchange (BSE)	
Bahrain All Share Index (Points)	1,733.7
Market Capitalisation (BD Billions)	5.1
Value of Shares Traded (BD Millions)	174.6
No. of Listed Companies	45
Insurance Sector	
No. of Policies Issued (Millions)	2.0
Gross Premiums (BD Millions)	90.1
Gross Claims (BD Millions)	37.5