مجلس التنمية الاقتصادية
البحرين
BAHRAIN
ECONOMIC DEVELOPMENT BOARD

Bahrain Economic Quarterly

June 2015



SUMMARY

BAHRAINI NON-OIL SECTOR REMAINS ROBUST

The performance of the Bahraini non-oil economy remained strong in Q1 of the year. This reflected the general resilience of the GCC economies at a time of renewed doubts about the global recovery. In particular, emerging economies seem to be transitioning to slower growth, whereas the Greek crisis has once again cast a shadow over the Eurozone.

- **Bahrain's non-oil growth came in clearly above our projection**. The non-oil sector grew by annual 5% in Q1, reflecting in part the continued strong build-up in infrastructure project activity. The fastest growing parts of the economy included private education and health care along with construction and transportation and communications.
- **Growth in the oil sector was held back by seasonal maintenance**. This translated into a 5.7% YoY decline in the sector. However, onshore production held up well. We expect a rebound during subsequent quarters as the Abu Sa'afah oil field reverts to capacity.
- **Steps toward higher interest rates in the US have continued to be delayed**. Although gradual tightening starting in the autumn is still seen as likely, the Federal Reserve has vowed to proceed cautiously. By contrast, the performance of the emerging economies has generally fallen short of expectations, highlighting the importance of renewed structural reforms.
- **Oil prices seem to be recovering, albeit gradually**. Oil prices have rebounded by close to 50% from their lows, and there has been a significant drop in investments in the sector. Key OPEC producers seem firmly committed to defending their market share, which is likely to contain the upward momentum.

Bahrain economic outlook

	2013	2014	2015f	2016f
Real GDP growth, %	5.3%	4.5%	3.6%	3.3%
Non-hydrocarbons sector	3.0%	4.9%	4.5%	4.0%
Hydrocarbons sector	15.3%	3.0%	0.0%	0.4%
Nominal GDP growth, %	8.3%	3.0%	-1.5%	9.8%
Inflation (CPI %)	3.3%	2.8%	3.5%	3.0%
Current account (% of GDP)	7.8%	7.7%f	1.7%	4.4%
Fiscal balance (% of GDP)	-3.3%	-3.6%	-5.6%	-2.0%
Crude Oil Arabian Medium (USD)	106.4	96.0	65.0	80.0

Source: Bahrain Economic Development Board

GLOBAL ECONOMY

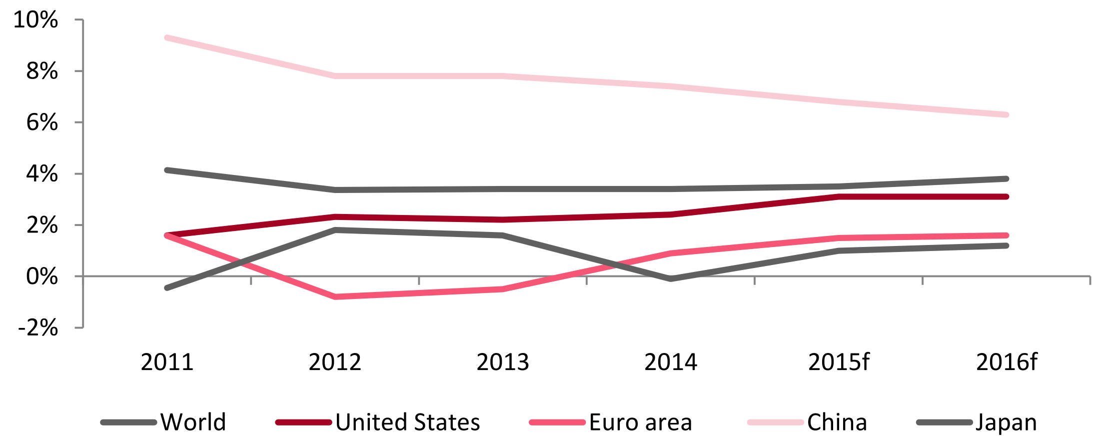
HESITANT PROGRESS

The pace of global growth in the first half of the year fell short of expectations

While the global economic recovery is continuing to make headway, the progress remains uneven and in many areas more tentative than expected. In general, the pace of growth in the advanced economies seems to be gradually strengthening, although the continuing wrangling around efforts to restructure Greece's foreign obligations has cast a long shadow on the Eurozone. While last year's deflation fears have significantly dissipated, this has also once again raised prospect of monetary tightening by the US with potentially significant implications for global capital flows.

By contrast, the emerging economies are struggling to maintain their recent momentum and there are disturbing signs of a deceleration in global trade volumes. In reflection of these uncertainties, the Organisation for Economic Co-operation and Development recently cut its 2015 global growth forecast from 3.7% to 3.1%. The International Monetary Fund (IMF) projects growth of 3.5% this year, which would represent a marginal improvement from an estimated 3.4% in 2014. The International Institute of Finance expects 2.8% growth this year to match its estimate of last year's growth. In general, growth is expected to strengthen next year.

Real GDP growth and forecasts, selected countries



Source: IMF World Economic Outlook, April 2015

Edging toward higher rates

While expectations of US monetary tightening persist, actual steps in this direction have been repeatedly delayed

One of the central indicators and determinants of the global recovery is connected to the direction of US monetary policy. The expectations of tighter policy were countered earlier in the year by an unexpected GDP contraction by 0.7% YoY in Q1, a figure that was, however, recently revised up to -0.2%. While some of this was attributed to seasonal weather-related factors, as well as a ports strike, it was also linked to a sharp Dollar appreciation, itself the consequence of tightening expectations. This highlights one the central challenges facing the US Federal Reserve in the face of an anaemic global recovery. Any speculation about rate increases tends to immediately translate into Dollar appreciation and tighter monetary conditions. This, in turn, has in the past delayed the perceived urgency and desirability of rate hikes. It has now been nine years since US rates were last increased.

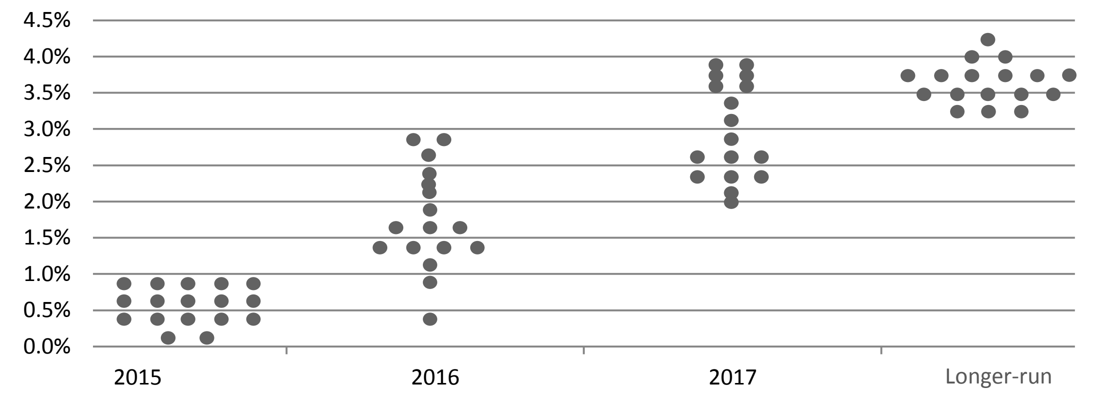
While continued caution by the Fed has helped counter some of the Dollar appreciation seen in Q1, an apparent rebound in economic activity has brought the tightening debate back to the fore. The US labor market exceeded expectations with 280,000 new jobs in May. Similarly, retail sales rebounded in May at an annual pace of 2.7% and especially car sales rose strongly (8.1%). New home sales rose by 2.2% MoM to a seven-year peak of 546,000. The reversal in Dollar appreciation also benefited from recent comments by the Bank of Japan Governor Haruhiko Kuroda, who indicated that the Yen was weak and unlikely to fall further.

The improving data has nevertheless not resulted in an abrupt change in the Fed's rhetoric. While a rate increase is widely viewed as likely after the summer, Chairwoman Janet Yellen has continued to emphasize her determination to proceed with caution. This is partly due to mixed data. The most recent Fed review of regional economic activity revealed that five of the 12 districts around the country had experienced export weakness and lower investment in sectors with significant overseas exposure. The Fed expects the US economy to expand by 1.8-2.0% this year, before accelerating to 2.4-2.7% next year.

The IMF recently urged the Fed to delay rate hikes past the new year

Moreover, even as the IMF projects US growth of 2.5% this year, it recently cautioned the Fed against a rate rise before the end of the year. The view was partly caused by caution about the lacklustre global recovery, but also the disruptions potentially caused of reversals in global capital flows that changing interest rate differentials would likely trigger.

Fed Funds rate projections (17 participants): Midpoint of target range or target level



Source: FOMC Economic Projections, June 2015

The Greek crisis continues to dominate the economic policy debate in Europe with recurrent bound of market volatility

Also the European economy has seen some improvement in its performance, not least due to the recent period of Euro weakness. The European Central Bank (ECB) now expects growth of 1.5% this year and 1.9% in 2016. Nonetheless, the mounting challenges around resolving Greece's fiscal challenges continue to test market confidence. Coming in connection with looser monetary policy by the ECB and diminishing fears about deflation, this has resulted in increased bond market volatility at a time when market liquidity is also a growing concern.

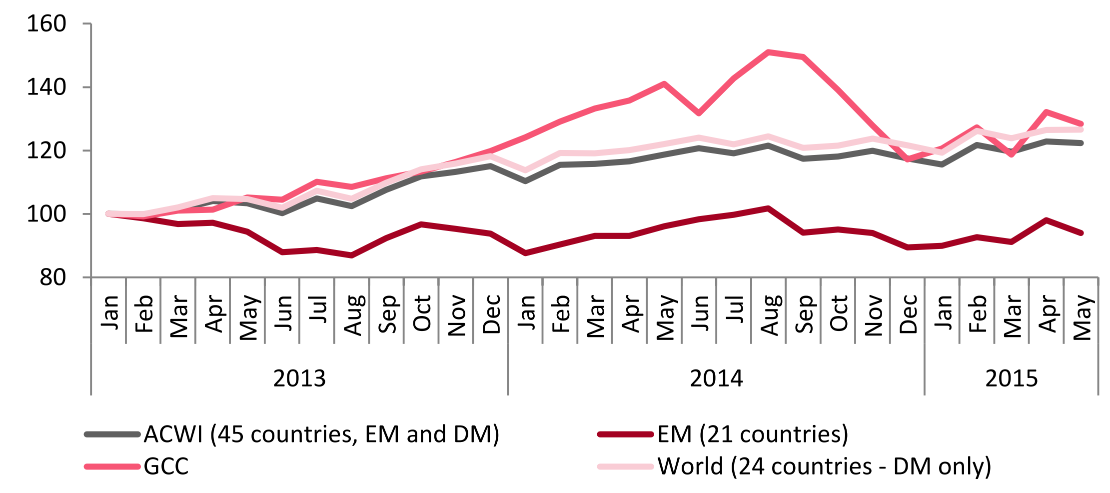
Efforts to strike a deal between the Greek government, the European Union, and the IMF have resulted in several rounds of inconclusive negotiations with mounting speculation that Greece might leave the single currency zone altogether. Without additional funding, Greece is likely to default on a EUR1.5bn repayment to the IMF by the end of June. The lack of certainty about the outcome has, in turn, led to record withdrawals from the Greek banking system, which is now critically reliant on liquidity support by the ECB. During a day of extreme market volatility, the government on 29 June imposed capital controls and announced a referendum on the bailout terms offered by Greece's creditors. The uncertainty around Greece has also revived fears about possible contagion to other heavily indebted peripheral Eurozone member states. This has resulted in bouts of increased bond yields.

Emerging trouble?

Emerging markets have generally performed less well than earlier during the crisis with growing signs of structural weaknesses

Having come to be seen as stalwarts of the global economy during the crisis years, emerging markets have generally lost much of their momentum over the past year. According to recent IMF estimates, the growth of emerging economies has decelerated from an annual pace of 7.2% in the decade leading up to the crisis to 6.5% since 2008. This is expected to fall further to 5.2% over the coming five years. At the moment, emerging market growth is estimated to be running at its lowest level since the downturn – approximately 3.5%. Among the largest emerging economies, Russia and Brazil are in downright recession. The gap in growth rates between emerging economies and the advanced markets has shrunk to its lowest in 15 years.

MSCI regional indices (Base Jan 2013=100)



Source: MSCI

While some loss of momentum is due to one-off and cyclical factors, it also appears increasingly clear that the structural growth drivers in many emerging economies have weakened. Two areas in particular stand out as both symptoms and causes of the deceleration:

- The momentum of international trade has weakened. In Q1, emerging market trade volumes posted an unusual fall due to weaker imports. This has significant global implications as emerging economies now account for close to 50% of international trade.
- Most estimates of productivity in emerging economies point to weaker gains and even actual declines. This highlights the fact that the appetite for structural reforms significantly weakened during the commodities bull market and the permissive monetary policy.

The weaker growth prospects have gone hand in hand with expectations of US tightening. Largely in response, growing amounts of capital have been repatriated by Western investors. An estimated

USD9.3bn left emerging market funds in the last week of May, the highest monthly outflow since 2008. This year, the IIF expects capital flows into emerging markets to reach their lowest level since 2009. Total inflows are projected to fall from USD1,048bn in 2014 to USD981bn this year. The UNCTAD World Investment Report 2015 reports a 16% fall in global foreign direct investment to USD1.23trn in 2014. This is significant, as cheap capital has been an important growth driver in recent years for many emerging economies with a significant build-up in debt issuance, much of it foreign-funded. According to the Bank for International Settlements, leading emerging economies have seen their international loans double during the crisis. Recent experiences have highlighted the vulnerability of especially economies with external deficits to prospects of monetary tightening in the West.

Even as uncertainties abound, a number of factors suggest that the contribution of the emerging markets to global growth will likely begin to increase:

- Some countries are resorting to renewed stimulus measures. For instance, China has been loosening monetary policy by lowering its high bank reserve ratios closer to pre-crisis levels and removing its 75% loan-to-deposit cap. In a bid to tackle the large volume of borrowing by sub-national governments, Beijing recently authorized local governments to issue bonds to refinance some USD3.5trn worth of off-balance sheet debt issued by them. India has reduced interest rates, most recently in June, in response to lower inflation.
- Structural reforms are being undertaken by some emerging economies. For instance, new governments in Indonesia and India are trying to engage in government restructuring and deregulatory reform in a bid to stimulate growth.
- While further Dollar appreciation cannot be ruled out, the possibility of rebalancing in capital flows may be drawing nearer, especially if the pace of US tightening is measured as expected. A stop in Dollar appreciation should also be supportive of commodity prices.

Oil continues to edge up

Oil prices have continued to recover even with OPEC firmly committed to defending its market share

Despite continued volatility and persistent worries about a market glut, oil prices have remained on a fairly consistent upward trajectory since the turn of the year. Recent weeks have seen Brent benchmark prices hover around USD65 per barrel, some 45% above their recent trough. This recovery has coincided with signs of a potentially significant regrouping on the supply side. In particular, the OPEC producers have maintained record output levels, whereas new investment in especially North American shale oil has declined. In total, an estimated USD130bn worth of projects globally have been deferred or cancelled by oil companies in response to the lower price environment. While this can serve as a market stabilizer in the short term, it can also risk triggering tighter market conditions in the future. This importance of new investment is highlighted by the fact that an estimated 5-6 mbd of oil output is lost each year to the natural depletion of fields. An estimated 80% of the investment in the sector goes on compensating for these declines.

Most current projections point to relatively healthy growth in the global demand for oil this year, partly in response to lower prices. OPEC expects global oil demand to rise from 91.3 mbd in 2014 to 92.5 mbd this year. This would translate into a 29.3 mbd “call on OPEC” – some 700,000 b/d below the organization's current target. The International Energy Agency (IEA) expects global oil demand to rise by 1.5 mbd to 94 mbd, an increase of 320,000 b/d since its previous forecast. The demand for OPEC crude is expected to be 30.2 mbd. Non-OPEC production is expected to rise by 1 mbd to 58 mbd in 2015. The Energy Information Administration (EIA) of the US Department of Energy projects global production at 95.24 mbd as compared to projected demand of 93.3 mbd.

The oil price dynamics of recent months have been seen by key OPEC members as a validation of their strategy, which seeks to protect the market share of low-cost producers. In spite of its official commitment to a 30 mbd production target, OPEC members have in recent months boosted their output above this level. For instance, OPEC production was estimated at 31.58 mbd in May. In spite of this, the positive price dynamic is increasingly expected to continue, with many OPEC producers recently describing USD75-80 as a reasonable price. The EIA expects WTI to average 55.35 per barrel this year while the Brent price is seen at USD60.53, figures that now appear below the emerging market consensus.

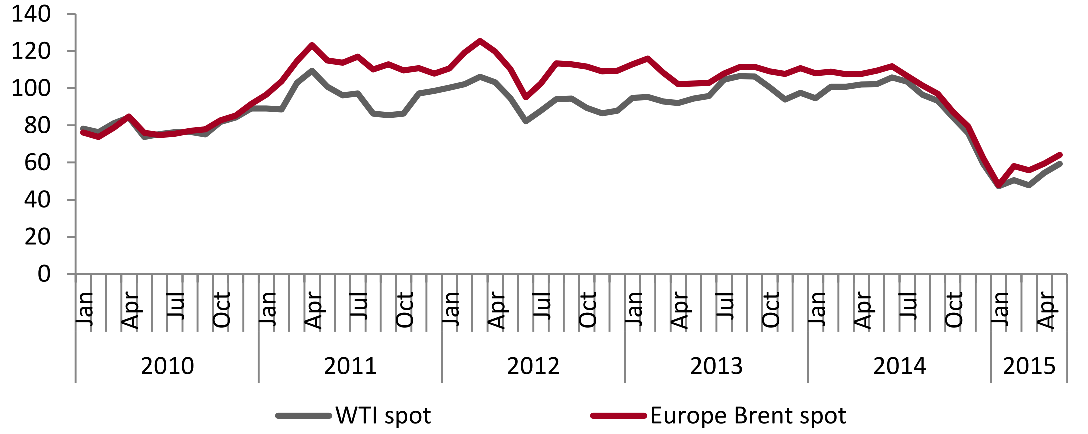
In spite of the generally positive price dynamics, there are important potential uncertainties linked to the near-term outlook:

- Key producers are boosting their output and have unveiled ambitious plans to continue. For instance, Russian production averaged 10.71 mbd in May. Iraq has boosted its output by a 430,000 b/d MoM increase, taking the total to a 35-year high of 3.68 mbd in March and some 3.85 mbd in April. Iraq has indicated that it would be able to export 3.3 mbd by the end of the year and has set an output target of 6 mbd by 2020. Angola reportedly plans to raise its output to 2 mbd by 2017.

- The prospect of a deal between Iran and the Western powers may result in the removal of sanctions and create the basis for increased oil exports by Iran. The country's recent production levels of some 2.8 mbd compare to around 4 mbd about a decade ago. Iran has indicated that it is able to boost production by 400,000 b/d within a month of the sanctions being lifted and by 1 mbd within 6-7 months. Iranian crude exports of 1.1-1.25 mbd this year compare to 2.5 mbd in 2011. However, many analysts suggest that the impact will be much more gradual. Some private sector estimates suggest that a lack of investment has reduced Iran's 2010 capacity of 3.7 mbd by potentially more than 500,000 b/d.

- Many North American shale producers have responded to the new market realities by boosting efficiency and cutting costs. Hence, even though the number of active US rigs has fallen some 60% from its October peak of 1,609, US oil output rose to an all-time high of 9.586 mbd at the end of May. The US Energy Information Administration sees US production declining very gradually from 9.56 mbd in June to 9.3 mbd in December. This compares to production of 8.71 mbd in 2014.

Crude oil prices (USD/barrel)



Source: US Energy Information Administration

Global oil demand and supply dynamics (mbd)

	IEA	OPEC	EIA
2013 Global oil demand (mbd)	91.9	90.2	90.5
Advanced economies	46.1	46.0	46.1
Emerging economies		29.0	
China	*10.1*	*10.1*	*10.6*
2014 Global oil demand (mbd)	92.6	91.3	92.1
Advanced economies	45.6	45.8	45.7
Emerging economies		29.8	
China	*10.4*	*10.5*	*10.7*
2015 Global oil demand (mbd)	94.0	92.5	93.3
Advanced economies	46.0	45.9	46.1
Emerging economies		30.6	
China	*10.8*	*10.8*	*11.0*
2013 Global oil supply (mbd)	91.4	90.2	90.2
OPEC	30.5	30.3	30.0
Non-OPEC	54.6	54.2	54.1
2014 Global oil supply (mbd)	93.7	92.4	93.2
OPEC	30.3	30.1	36.4
Non-OPEC	57.0	56.5	56.8
2015 Global oil supply (mbd)			95.2
OPEC			37.0
Non-OPEC	58.0	57.2	58.2

Source: International Energy Agency, Organization of the Petroleum Exporting Countries, US Energy Information Administration

Implications for Bahrain

While the global economy continues to be characterized by exceptional risks, the near-term outlook for Bahrain looks fairly benign.

- Any movements in US interest rates are generally expected to be quite gradual. This should limit the impact on the cost of capital.

- Renewed efforts to accelerate growth in Asia should support Bahraini exports and may help bolster export prices.
- The gradual recovery in the oil price looks likely to continue even if periods of volatility remain a possibility.

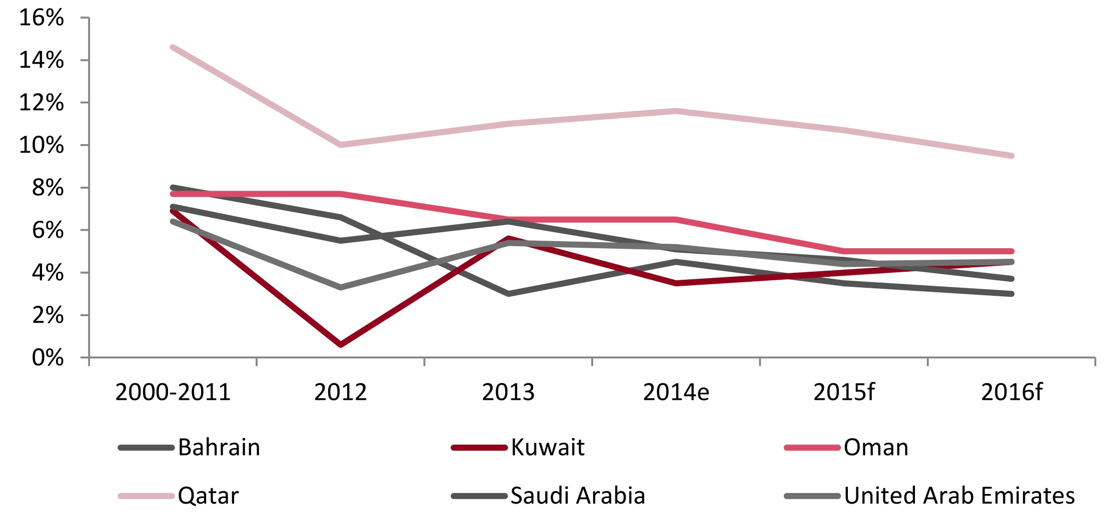
THE GCC REGION

REGIONAL BACKDROP REMAINS POSITIVE

The momentum of the regional non-oil economy remains robust in spite of the recent oil price volatility

The performance of the GCC economies has remained robust in the face of the recent oil market gyrations and global uncertainty. Both data on current activity and forward-looking indicators point to a high degree of continuity in the regional non-oil economy. This reflects the strength of the key structural growth drivers, as well as the firm commitment of regional governments and investors to long-term projects. Similarly, regional policymakers have, in many cases, mitigated the adverse impact of lower oil revenues through countercyclical fiscal policies, even if fiscal reform is on the agenda as never before. The IMF currently expects real growth in the region to decelerate only marginally from 3.6% in 2014 to 3.4% this year. This is currently projected to be followed by a broadly comparable 3.2% in 2016. Most of the deceleration is linked to what are expected to be modest production gains in the oil sector. Non-hydrocarbons sector growth is likely to be much faster than headline growth, yet expected to moderate somewhat from an estimated 6.2% in 2014 to 5.4% in 2015 and 5.0% in 2016.

GCC non-oil real GDP growth, %



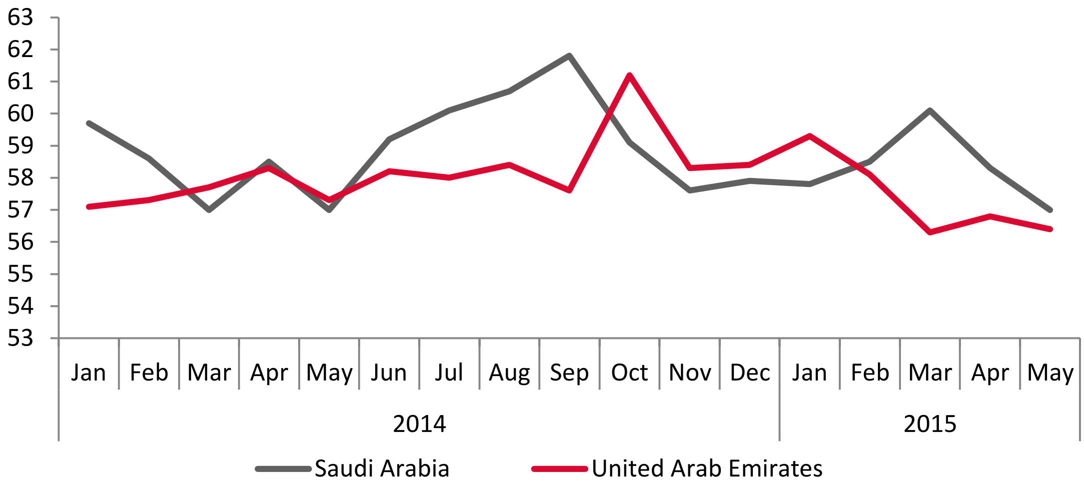
Source: International Monetary Fund, World Economic Outlook Database, April 2015

Key indicators of economic activity remain favorable

Key indicators of economic activity in the largest regional economies point to continued strong expansion

In spite of some erosion in the main forward-looking economic indicators, the GCC economy appears to remain firmly in an expansionary mode. In Saudi Arabia, the SABB/Market Purchasing Managers' Index (PMI) declined to its lowest level in two years in May. Nonetheless, the 57.0 reading suggested continued strong growth, both by historical and by global standards. It compared to a reading of 58.3 in April. The UAE PMI in May stood at 56.4, only marginally down on the 56.8 figure posted in April.

HSBC/Markit Purchasing Managers' Index



Source: HSBC, SABB

National accounts data, along with other indicators of economic activity across the region, further underscore the high degree of continuity in economic performance. The Saudi economy is estimated to have expanded by 3.5% in 2014 led by a 5.6% gain in the non-oil private sector. While some key indicators have displayed month-to-month volatility, they almost constantly echo the positive messages of the PMI. As of April, indicators of consumer spending were up by an annual 7.7%, while cement sales grew by an almost comparable 7.1%. Imports in March rose by an annual 2.8%. The IMF expects Saudi Arabian growth to reach 3.5% this year – in line with 2014.

Growth prospects remain favorable across the GCC with at best minimal moderation expected in non-oil growth

The UAE reportedly posted 4.6% growth in 2014 in a slight deceleration from 5.2% in 2013. The economy is expected to continue to expand strongly this year as well, although slower public spending and the strong Dollar may reduce the pace of growth to some 3.6%, according to the IIF. The housing market in the UAE has seen some continued slowdown in recent months with market estimates for May pointing to YoY declines of just over 10% in spite of rising transaction volumes.

The Qatari economy is estimated to have grown 6.2% in 2014, largely in line with the year before, in spite of a slight contraction in the oil sector. Growth in 4Q14 reached 6.7% and this pace is likely to be sustained this year due to project spending and continued immigration. The annual pace of population growth reached 9.2% in May. Like the UAE, Qatar has also seen some slowdown in real estate inflation, although prices are still rising strongly.

The IMF expects the Kuwaiti economy to expand by 1.7% this year and by 1.8% in 2016. By contrast, the pace of growth in Oman is projected to moderate somewhat from a brisk 4.6% this year to 3.1% in 2016.

Reflecting the strong underlying momentum, corporate earnings of the 658 listed companies in the GCC rose from USD61.7mn to USD68bn in 2014, thereby surpassing the previous peak of USD63.2bn which was achieved in 2007. According to estimates by the Kuwait Financial Centre (Markaz), UAE companies led the gains with a 32% YoY increase, followed by Bahraini companies at 11% and Kuwaiti companies at 8%.

Promising FDI outlook despite slowdown

The GCC region continued to attract strong foreign direct investment inflows in 2014

According to the United Nations Conference of Trade and Development's (UNCTAD) World Investment Report 2015, the GCC region has continued to attract significant inflows of foreign direct investment in spite of some decline in line with lower volumes globally. In 2014, inward FDI in the region declined by 4% (USD22bn) in 2014. Flows into the UAE and Saudi Arabia registered slight declines to USD10bn and USD8bn, respectively. However, as regional governments continue to pursue infrastructure and development projects, FDI volumes are generally expected to rebound.

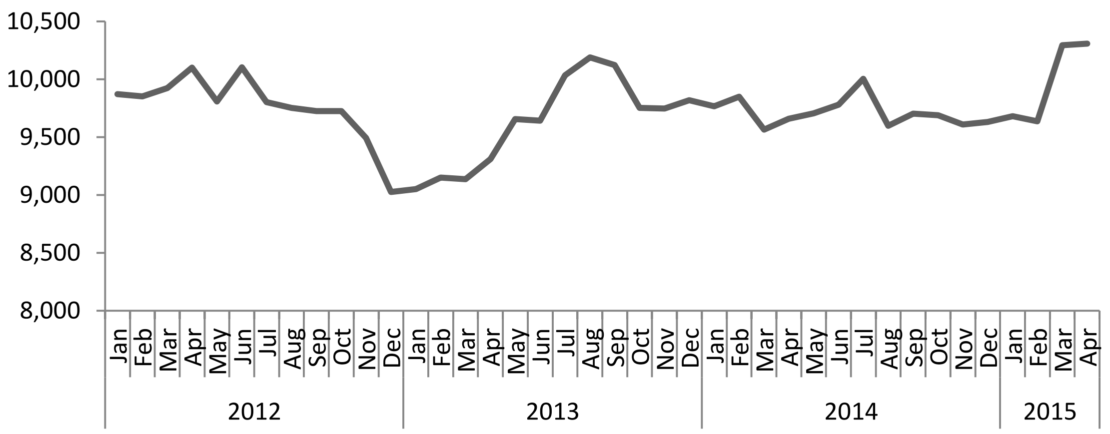
Regional producers defend their market share

In line with OPEC's policy of producing at or even slightly above its quota, Saudi Arabia has seen record production in recent months. The monthly average output climbed over 10 mbd in March to 10.3 mbd, the highest level since the early 1980s. Production of 10.33 mbd was reported in May, marginally up on 10.31 mbd in April.

The region has seen unexpectedly strong momentum in the oil sector, both upstream and downstream

Part of the growing output is going to serve the needs of the domestic economy at a time of a major build-up of downstream capacity and increasing power generation needs. Saudi domestic consumption reached 3.1 mbd, or some 27% of total production, in 2013. Domestic consumption has recently been growing at an annual pace of 6%. Saudi refineries increased production by 18.3% last year due to the ramp-up at the new Satorp facility. The average Saudi refinery output reached 2.18 mbd and the total refinery capcity in the Kingdom now stands at 2.9 mbd. The new Satorp and Yasref refineries process heavy crude from the offshore Manifa field. Saudi Arabia is working to boost its power generation capacity by 40% through fifteen new plants by 2018. The combined capacity at the end of 2014 stood at 61.87 GW.

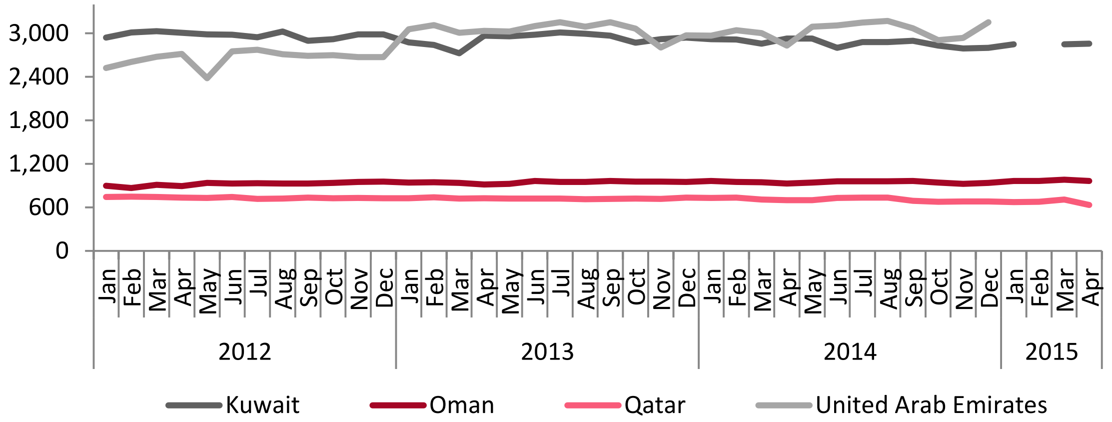
Monthly oil production by Saudi Arabia ('000 b/d)



Source: Joint Organisations Data Initiative

Other regional producers have also maintained their output levels. According to the Joint Organisations Data Initiative, Kuwaiti oil production reached 2.85 mbd in March and 2.86 mbd in April.

Monthly oil production by other GCC producers ('000 b/d)



Source: Joint Organisations Data Initiative

Consumer prices dynamics in the region remain generally stable although a clear divergence has opened up

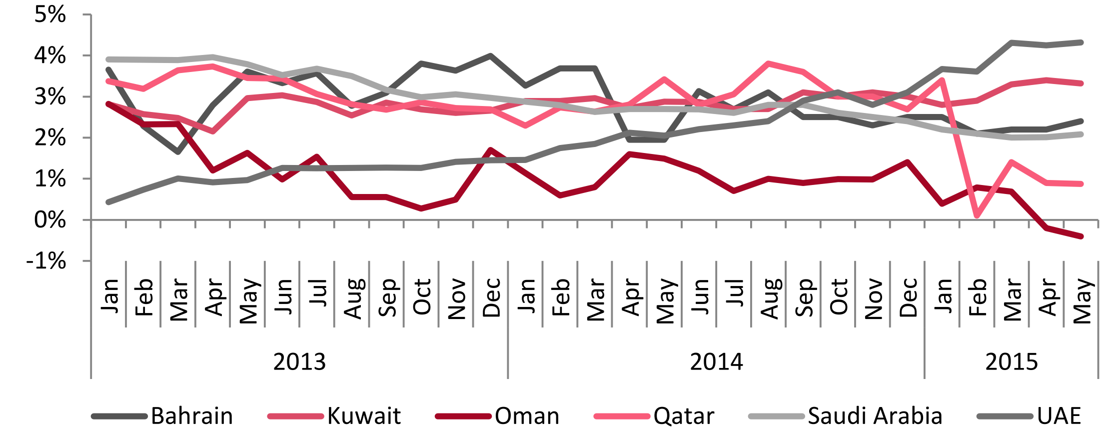
Regional price pressures generally stable

Consumer price inflation across the GCC region has been generally stable, although a clear divergence has emerged in recent months between Saudi Arabia, Qatar and Oman on the one hand, and the rest of the region on the other. The UAE recently registered the highest inflation rate in the region with consumer prices rising by 4.32% in May. Dubai's CPI increased by 4.6%, its highest level since 2009, mainly due to the increase in housing and utility costs. Kuwait's CPI increased by 3.4%.

Qatar has experienced a sharp deceleration in its headline inflation rate since September 2014. Having peaked at close to 4%, consumer price rises decelerated to 0.87% as of May. The slowdown is largely attributed to lower food and rent inflation. Price pressures are generally expected to begin to build up in the coming months due to continued rapid population growth.

Also headline inflation in Saudi Arabia has been trending down fairly consistently for the past two years from the neighborhood of 4% to 2.1% in May, which marked a small acceleration from 2% in April. This was the first increase since September. The reversal was mainly due to an acceleration in housing inflation. Oman's CPI, unusually for the region, registered a 0.4% decline in May.

Consumer price inflation in GCC countries (% YoY)



Source: National statistical offices

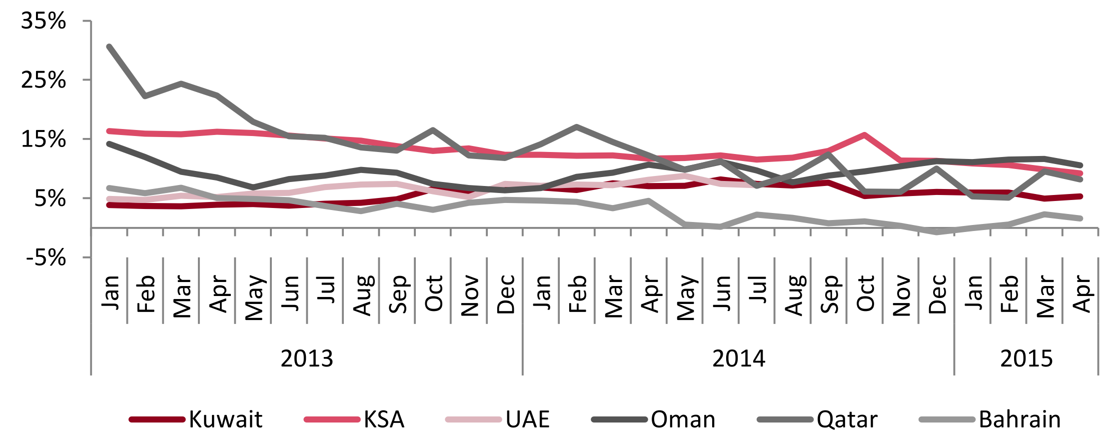
Resilience in the face of slower deposits and loan growth

Bank lending growth in the region remains robust with healthy institutions. This is serving as an important source of continuity in the face of oil price volatility

There is some concern, voiced among others by the IMF, that liquidity in the GCC region could tighten in the coming months due to the decline in oil-related bank deposits, while non-performing loans could increase. However, the regional banking sector appears to rest on strong foundations in view of its current financial position.

In actual fact, credit growth in the GCC region has generally picked up recently, most notably in the UAE, Oman and Kuwait. Only Qatar witnessed a slight decline. YoY lending growth in Saudi Arabia reached 9.52% in April, the slowest since October 2011, while the UAE's bank lending rose by 8.4%. Bank loans in Kuwait registered 5% growth. Oman has gained a strong momentum in the banking sector activity with lending growth reaching 11.6% in March. On the other hand, Qatar experienced a MoM decline of 0.5%. However, Qatari banking sector's loans-to-deposits ratio reached 108% in March, and the Qatar Central Bank projects bank lending to grow by 9% in 2015.

YoY growth of domestic bank credit (%)



Source: National central banks

GCC equity market performance generally resilient

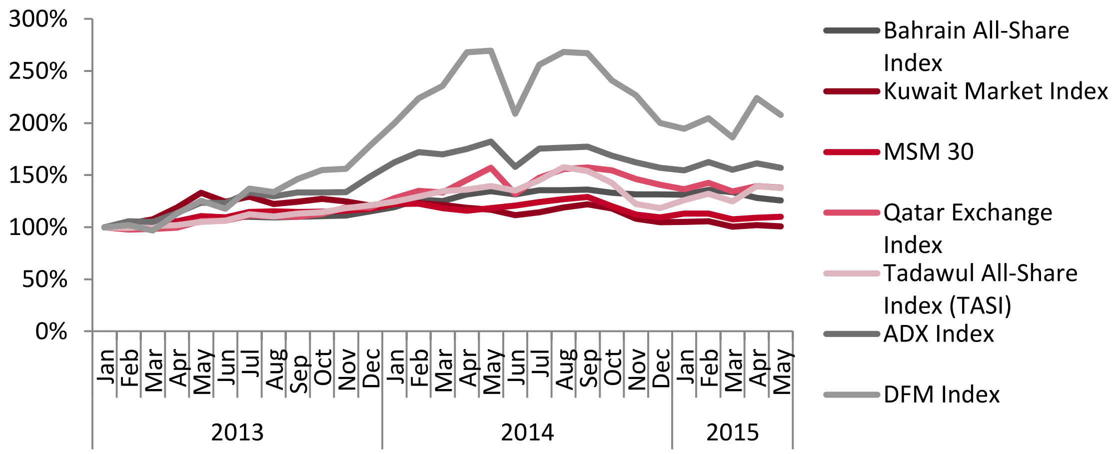
The performance of the regional bourses has been fairly uneven in recent months

The GCC capital markets have reflected much of the resilience inherent in the performance of the non-oil economy. However, recent months have continued to see some volatility in response to oil price volatility, as well as to developments in other parts of the Middle East. During the first two quarters of the year, Saudi Arabia had the best performing regional bourse with a 9.0% YTD gain. It was followed by Dubai and Abu Dhabi with 8.3% and 4.3% gains, respectively. Oman was the only other GCC exchange to post an increase in the first half of the year – by 1.3%. Qatar Exchange saw a small 0.7% decline, whereas the Kuwait Stock Exchange shed 5.1%.

In an important development for the regional markets, the Capital Market Authority of Saudi Arabia this year issued regulations to permit direct foreign ownership of Saudi equities for the first time. The regulations became effective as of mid-June. Such investments are permitted for so-called Qualified Foreign Investors only. As a rule, these have to be legal entities with a track of record of at least five years and assets under management of at least SAR18.75bn. The expected increase in institutional investment is expected to reduce the volatility of the Saudi market, where individuals typically account for close to 90% of trading volumes. Overall foreign ownership is capped at 20% of individual companies and 10% of Tadawul's total capitalization. Foreigners currently own some 7.7% of the Saudi market. In a further impetus to the market, the new Saudi Council of Economic and Development Affairs is looking at ways to accelerate privatizations.

In the effort to improve market liquidity, the UAE's new Commercial Companies Law reduces the minimum free float requirement in an IPO, in addition to introducing a book building mechanism with regards to pricing newly issued IPO shares. The introduction of this new law is expected to further encourage listings.

GCC equity market indices (Jan 2013=100)



Source: Bahrain Bourse, Kuwait Stock Exchange, Muscat Securities Market, Qatar Exchange, Tadawul, Abu Dhabi Securities Exchange, Dubai Financial Market

Fixed income markets experience a cautious rebound

The regional bond and sukuk markets are showing signs of renewed growth after they lost some of their momentum in the second half of last year. Despite a slow start in the beginning of the year, the GCC bond market has seen some renewed growth. In May, bond issuances in the GCC

Q4 was characterized by a clear slowdown in issuance activity in both conventional and Shariah-compliant fixed income

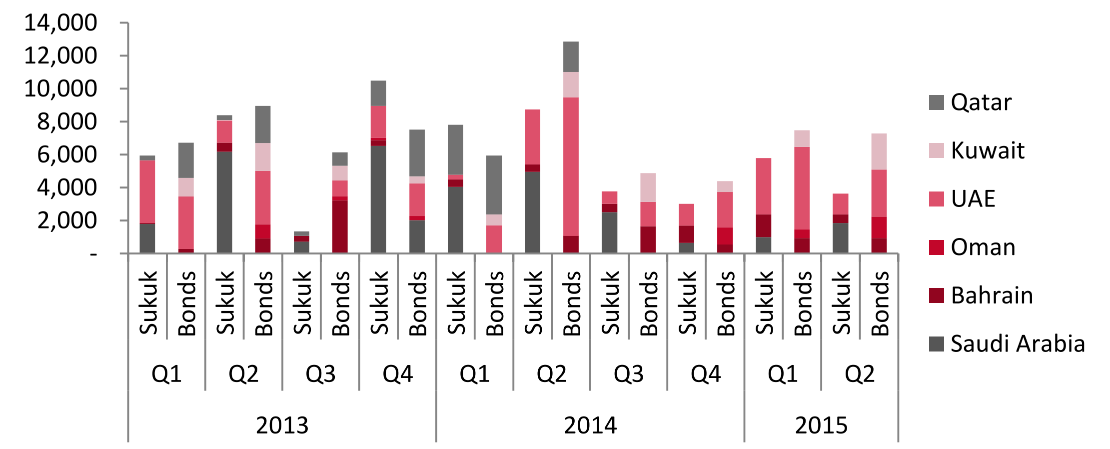
rose 8% by value, issuing 10 issuances with a total value of USD3.4bn. In spite of the rebound, the sukuk market activity remains clearly below last year's levels. In May, sukuk issuance by value declined by 46% year on year to USD7bn. This was due to the sharp decline in sovereign issuances (down 40% year on year), corporate issuances (down 48%), and quasi-sovereign issuances (down 55%). Bahrain was the largest issuer of sukuk by number of issuances (12) in GCC for YTD May 2015, followed by UAE (5) and Saudi Arabia (4).

Overall, the region saw 26 primary sukuk offerings worth USD9.56bn during the first half of the year. This compared to 31 sukuk worth USD16.55bn a year earlier. Primary sukuk issuance during the first two quarters of the year was unusually limited to only three regional economies — Saudi Arabia, the UAE and Bahrain.

The conventional market saw more continuity, partly because of ongoing issuance by some regional sovereigns. Overall, 44 primary bond offerings took place in the region during the first half of the year. Their aggregate value reached USD15.55bn. This compared to 30 bonds worth USD17.23bn during the corresponding period in 2014.

Among regional landmark deals, Emirates Airlines in June listed a USD913mn sukuk on Nasdaq Dubai. In May, Dubai Islamic Bank priced a USD750mn five-year sukuk carrying a profit rate of 2.921%. Noor Islamic Bank raised USD500mn. In Saudi Arabia, Riyad bank placed a USD1.066bn, 10-year sukuk. Saudi Arabia's National Commercial Bank at the end of June announced a plan for a SAR1bn privately placed perpetual sukuk. Corporate issuers of landmark conventional bonds in Q2 included National Bank of Abu Dhabi, Bank of Sharjah, Industrial and Commercial Bank of China (Middle East), DP World, Oman Electricity Transmission Co., and National Bank of Kuwait.

GCC bond and sukuk issuance (USD mn)



Source: Zawya

Implications for Bahrain

The pace of economic activity in the GCC is set to remain brisk, which will provide a favorable backdrop for Bahrain as the most regionally integrated economy.

- Regional tourism flows are likely to be characterized by continued growth.
- Investment activity in regional corporates and real estate looks likely to remain resilient in the face of fairly low cost of capital. The large pipeline of infrastructure projects in Bahrain should act as a further magnet.

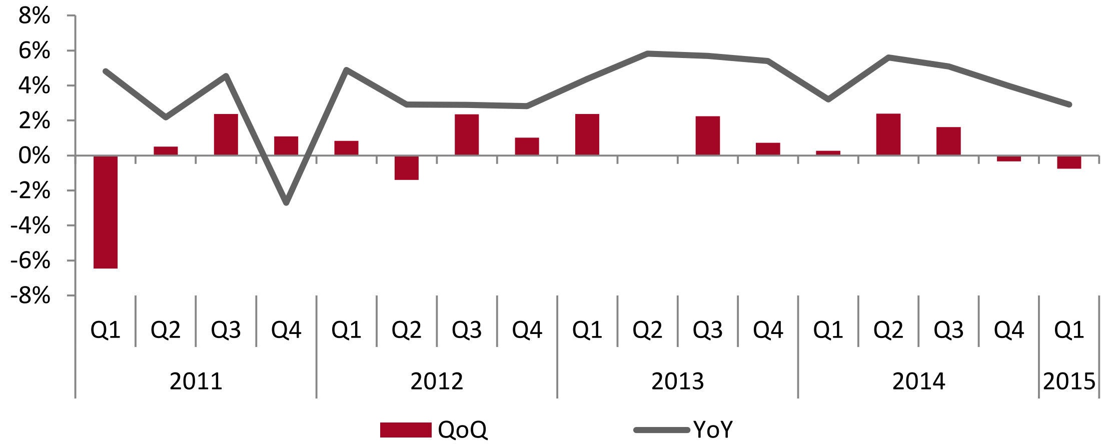
BAHRAIN

NON-OIL SECTOR MOMENTUM REMAINS ROBUST

Non-oil growth has held up very well in the face of oil price volatility and expanded by an annual 5.0% in Q1

In line with our expectations, growth momentum in Bahrain's non-oil economy has remained brisk into the opening months of the year, even as the hydrocarbons sector experienced a 5.6% YoY decline due to seasonal maintenance. As a result, Bahrain's headline real GDP expanded 2.9% on an annual basis during Q1. Growth in the non-oil economy, which constitutes more than 80% of the Kingdom's GDP, reached a healthy 5.0%.

Real GDP quarterly growth



Source: Central Informatics Organisation

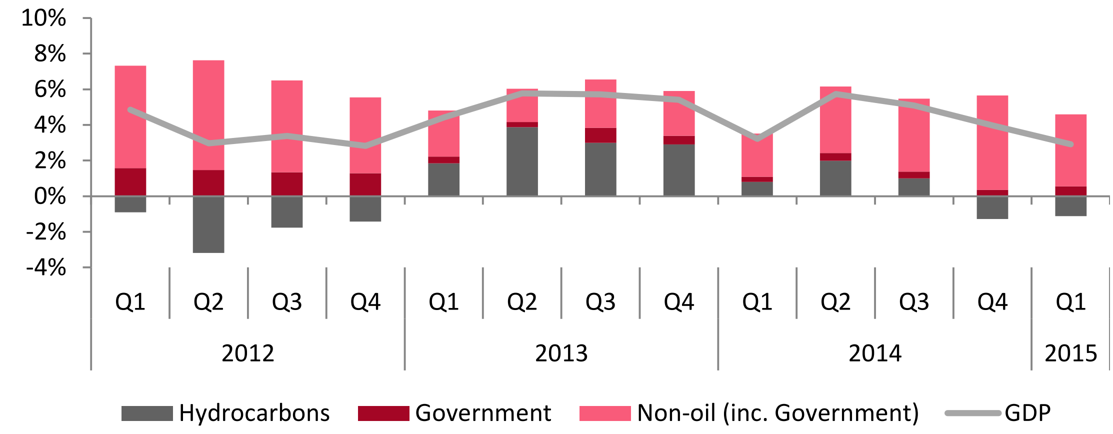
Non-oil drivers remain very strong

The positive performance of the Bahraini economy in 1Q15 was entirely driven by the non-hydrocarbon sector and continued the positive momentum that took shape in 2014. The contribution of the non-oil economy to YoY headline growth in Q1 was 4.0%, as opposed to -1.1% for the oil sector. Of the 4.0%, government services contributed 0.6 percentage points. This composition of growth, much in line with the pattern observed last year, highlights the role of the private sector in driving the economy forward.

Growth in the non-oil private sector has held up well and creates a strong basis for the year

In line with the pattern of recent years, growth in Bahrain was very broad-based in Q1. Social and personal services – mainly composed of private education and health care – overtook the hotels and restaurants sector as the fastest-growing sector, expanding at an annual pace of 8.3%. This highlights the dynamism of a sector that has been at the forefront of growth for more than a decade with double-digit expansion in most years. The construction sector, with 7.5% YoY growth, continued the strong momentum that became apparent in the second half of last year as project spending escalated. The transport and communications sector was the third-fastest growth sector with a 7.3% YoY expansion. Manufacturing posted strong growth as well, expanding 5.9% YoY during Q1.

Breakdown of quarterly growth (in real terms, YoY)



Source: Central Informatics Organisation

Important projects are underway to support the continued expansion of Bahrain's dynamic tourism sector

The hotels and restaurants sector experienced a slowdown in its annual pace of growth to 3.5% during Q1 as compared to previous quarters. This was likely caused in part by a base effect after a couple of years of brisk expansion. Nonetheless, going forward, the sector is poised to benefit from a number of a key hotel development projects in the coming years. Emaar Hospitality Group plans to bring to Bahrain its flagship hotel brands, The Address Hotel and Resort and Vida Hotel and Resort. Other luxury five-star hotels planning to establish a presence in Bahrain include the One & Only Royal Mirage, Shaza Hotels and Melia Hotels International, a Spanish hotel chain that is eyeing a strategic expansion plan into the GCC.

YoY real growth of key sectors, 2012-2014

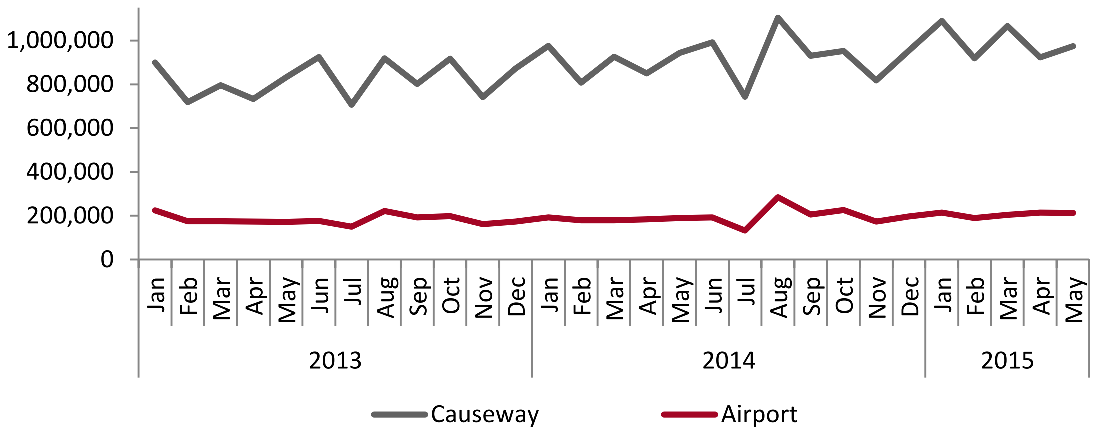
YoY growth	2012	2013	2014					2015
	Annual	Annual	Annual	Q1	Q2	Q3	Q4	Q1
Crude pet. & Gas	-8.5%	15.3%	3.0%	4.1%	9.3%	4.7%	-5.9%	-5.6%
Manufacturing	4.7%	3.2%	4.2%	0.8%	4.4%	4.1%	7.6%	5.9%
Construction	4.1%	2.7%	7.3%	1.4%	3.6%	12.3%	12.5%	7.5%
Retail	6.2%	2.0%	4.0%	3.9%	3.1%	4.4%	4.4%	2.6%
Hotel & rest.	11.2%	9.5%	9.9%	9.9%	10.3%	7.4%	11.9%	3.5%
Trans. & Comm.	4.5%	2.5%	6.2%	4.9%	6.4%	4.0%	9.4%	7.3%
Social & pers. Serv.	12.7%	6.5%	7.5%	6.6%	8.2%	6.6%	8.7%	8.3%
Real est. and Bus. Act.	3.6%	2.4%	4.7%	4.4%	4.5%	4.6%	5.3%	3.1%
Finance	4.0%	2.3%	3.4%	1.9%	3.9%	3.5%	4.1%	2.0%
Government	12.1%	2.1%	2.8%	2.3%	3.3%	3.0%	2.8%	4.3%
Other	11.2%	2.8%	9.0%	5.9%	6.3%	12.2%	11.6%	10.5%
GDP	**3.4%**	**5.3%**	4.5%	**3.1%**	**5.6%**	**5.1%**	4.0%	2.9%

Source: Central Informatics Organisation

The numerous new projects in the hotels and restaurants area reflect steady growth in visitors to the Kingdom. As of May, a total of 6.05mn visitors to Bahrain have been registered during 2015, an almost 11% increase on the total number of visitors recorded during the same period a year ago. Arrivals through the King Fahad Causeway were 973,167 in May and contributed to an accumulated figure of 4.97mn crossed during the year. This accounted for 82% of total arrivals during the 5-month period. The Bahrain International Airport also saw increased visitor traffic with

1.03mn passengers between January and May, a 12% growth compared to the same period in 2014.

Monthly tourist arrivals in Bahrain by port of entry, 2013-2015



Source: Ministry of Interior

While offshore oil extraction was affected by seasonal maintenance in Q2, onshore extraction has remained robust

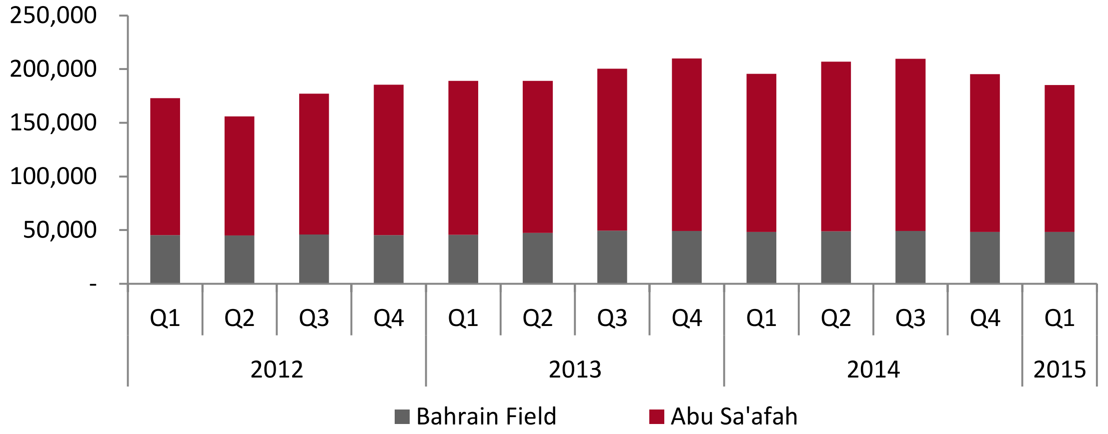
Seasonal volatility in the hydrocarbons sector

In contrast to the stronger-than-expected expansion in 2014, the hydrocarbons sector was held back by seasonal maintenance in the opening quarter of the year. The average production from the Bahraini share of the offshore Abu Sa'afah field amounted to 136,935 barrels per day (b/d), clearly short of the 150,000 b/d capacity. This represented a 7% decline in production in both QoQ and YoY terms. By contrast, production from the onshore Bahrain field was marked by continuity, averaging 48,242 b/d during Q1, only marginally below the 48,289 b/d and 48,352 b/d produced on average during the previous quarter and 1Q14, respectively. The budget bill projects Bahrain field average output of 47,000 b/d this year and 46,000 next year.

The Government has also approved plans to develop alternative energy in its efforts to diversify its sources for power generation. A 5MW solar plant has already been launched and another 5MW combined solar and wind facility is due to start in 2015. The Government is further planning to establish an independent National Renewable Energy Regulatory Authority.

Power consumption in Bahrain is expected to reach 3,350MW this summer, representing a 6% increase on the peak recorded last August. The total installed capacity currently stands at 3,934MW. The Government plans to expand its capacity through the second phase of the Al Dur power station, with the expansion starting next year and expected to be completed by 2019.

Quarterly oil output (barrels per day)



Source: National Oil and Gas Authority

Near-term outlook linked to non-oil drivers

Momentum in the non-oil economy looks likely to hold up well due to the build-up of infrastructure spending

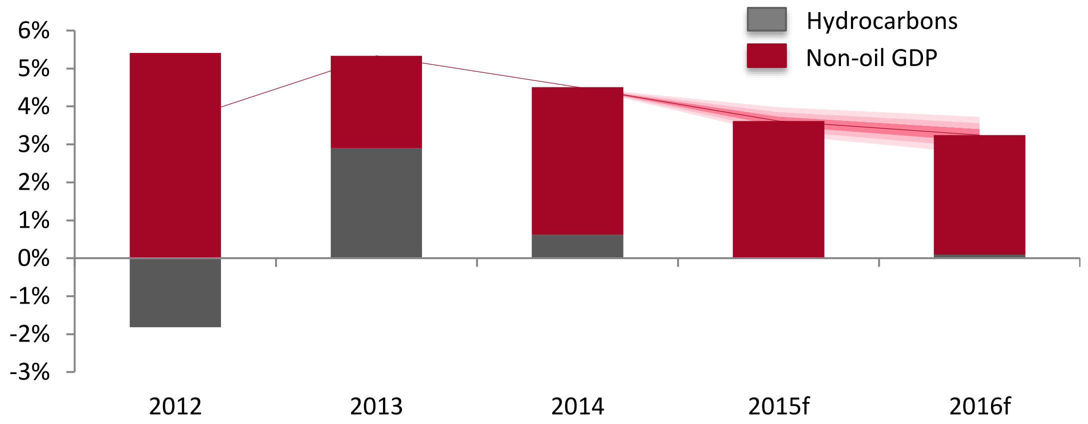
The near-term outlook for the Bahraini economy is very heavily linked to the non-hydrocarbons sector. While the period of low oil prices and the anticipated tightening of monetary policy by the US Federal Reserve later this year may constitute risk factors, we expect their effect to be countered by the resilient growth drivers in the Kingdom. The strength of the project pipeline will benefit other parts of the economy through historically strong backward and forward linkages.

We currently project real GDP growth of somewhat less than 4% for 2015 and 2016. We expect growth in the oil sector to remain subdued during this period. However, activity in the non-oil economy should remain robust, with an average of 4.5% for the year. It should be noted, however, this figure was already clearly exceeded in Q1 and faster implementation of the project pipeline could push the total up. We expect non-oil growth to come close to 4% next year as well as quite possibly exceed this figure with a continued build-up in the projects area.

Among other things, work is currently underway on 3,895 housing units in the Northern City and in East Hidd. The project is an important part of the 25,000 units the Government is planning to complete over the coming four-year period in five areas. Also, 1,985 units in the Northern City are being constructed under the auspices of a private-public partnership with Naseej. The private sector's involvement in social and affordable housing projects, through joint ventures or public-private partnerships (PPPs) has increased, which plays an important role in sustaining the growth momentum of the non-oil sector in the face of a slower hydrocarbons sector.

In an important development for the manufacturing sector, the Board of Directors of Alumnium Bahrain in June approved the sixth production line. The USD3.5bn project will boost production at Alba by 514,000 metric tonnes per annum to reach 1.45mn tonnes, positioning Alba as the world's largest single-site smelter. The project's construction phase will commence in 2016 and production is expected to begin by 2019.

Projected GDP growth



Source: Central Informatics Organisation, EDB estimates

2015-2016 budget presented

The government's budget bill seeks to rationalize spending while developing new revenue sources

Following a delay caused by the parliamentary elections at the end of last year, the Government presented its two-year budget for the 2015-2016 period in early May. Following the recent oil price correction, the draft foresees a significant increase in the fiscal deficit from a budgeted BHD914mn in 2014 to BHD1.47bn this year. The revenue projection of BHD2.10bn marks a 25% drop on last year's figure and is premised on an oil price assumption of USD60 per barrel. Overall budgeted expenditure stands at BHD3.57bn, which is 3.5% below the 2014 figure.

In total, the 2015-2016 budget foresees spending of BHD7.29bn and revenues of BHD4.26bn, with anticipated deficits of BHD1.47bn and BHD1.56bn in 2015 and 2016, respectively. The Government is likely to finance the deficits largely through additional borrowing, accommodated through the recent increase in the debt ceiling from BHD5.00bn to BHD7.00bn. The Government is also planning to spend BHD1.4bn on subsidies during 2015-2016. Nonetheless, the subsidy bill is set to decline from last year's BHD935mn to BHD754.1mn this year.

Government budget 2015-2016

	2015	2016
Revenue		
Net oil and gas	1,700,787,000	1,757,613,000
Non-oil revenue	368,342,000	371,721,000
Grants	28,200,000	28,200,000
Total Revenue	**2,097,329,000**	**2,157,534,000**
Expenditure		
Recurrent	2,381,815,000	2,483,085,000
Subsidies	754,171,000	652,889,000
Projects	435,000,000	585,000,000
Total expenditure	**3,570,986,000**	**3,720,974,000**
Budget deficit	**1,473,657,000**	**1,563,440,000**

Source: Ministry of Finance

The budget is expected to develop new revenue streams from government-related entities and enforce cost recovery on government services. A medium-term plan will control the growth of recurrent expenditures, and a number of measures were approved by the Cabinet in mid-May with a total projected savings of BHD386mn. As part of its review of the current subsidy programme, the Government is planning to differentiate and target subsidy changes. The Government has proposed to start making direct cash transfer payments to Bahraini citizens in August, as part of eliminating meat subsidies.

In spite of oil price volatility in the second half of last year, the actual fiscal performance of the country has remained strong. According to the 2014 consolidated final accounts, government revenues rose 11% to BHD3.09bn in 2014, expenditures declined 11% to BHD3.54bn and the budget deficit contracted by 62% to BHD455mn. This was just under one-half of the budgeted figure.

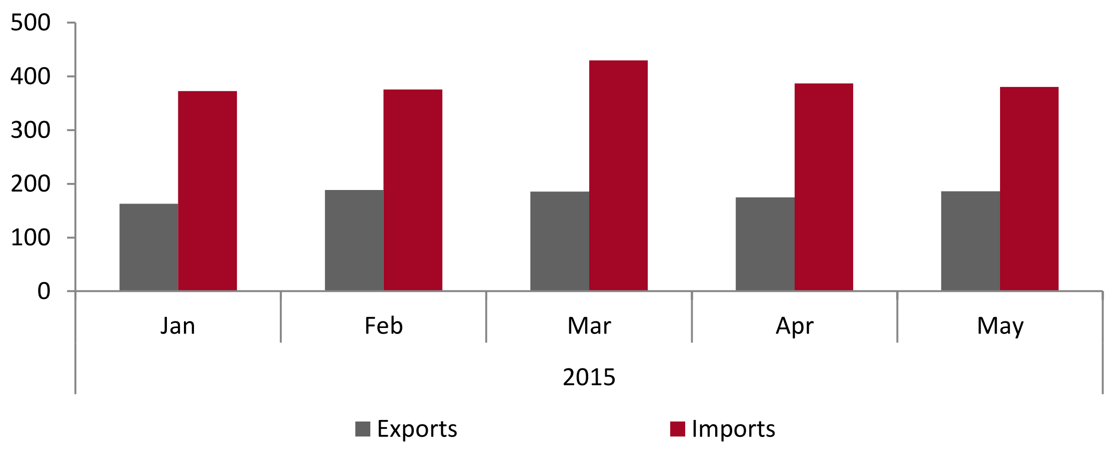
Foreign trade data reflects strong non-oil growth

Growth in trade volumes has reflected the strength of the non-oil economy

Total imports into Bahrain during the first five months of 2015 reached BHD1.95bn. China was the most important source of imports during the period at BHD254.97mn, followed by BHD186.60mn worth of goods from the UAE, and BHD156.86mn from the US. The leading non-oil imports as of May 2015 were mechanical and electrical equipment (BHD339.72mn), transportation vehicles and equipment (BHD337.76mn) and chemicals (BHD228.93mn). Taken together, these accounted for almost 47% of total imports.

Bahrain's non-oil exports were valued at BHD897.44mn for the period Jan-May. Saudi Arabia was the main destination, attracting BHD250.66mn worth of goods, followed by the UAE at BHD153.73mn and the US at BHD105.41mn. The leading non-oil exports were aluminium wires (BHD88.81mn), aluminium rods (BHD74.58mn) and iron ore (BHD66.98mn).

Non-oil goods exports and imports, 2015 (BHD mn)



Source: Ministry of Interior

FDI inflows resilient

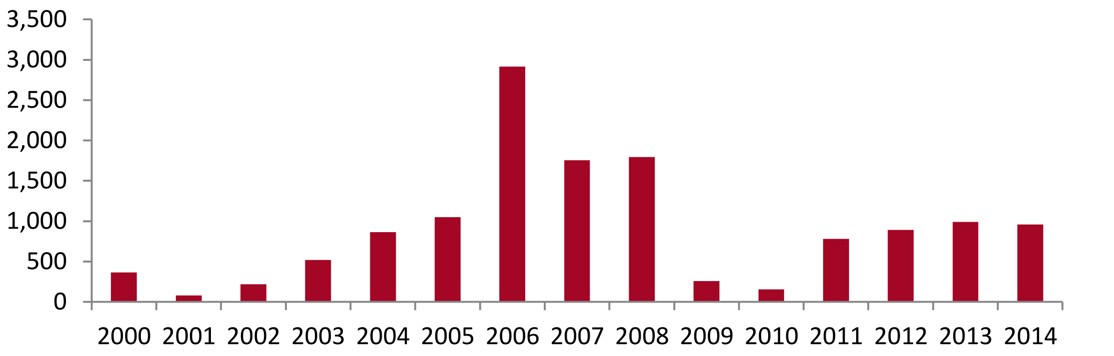
Despite a small YoY drop during 2014, inward foreign direct investment (FDI) into Bahrain remained in excess of the levels seen in 2009-2012. Mirroring a regional trend across the GCC, Bahrain's FDI inflows fell to USD957mn in 2014 from USD989mn in 2013. Nonetheless, this 3.2% decline was smaller than the 3.6% drop seen in the GCC region as a whole. This region-wide

Inward foreign direct investment has held up well in spite of declines globally

downward trend reflects the broader global dynamics linked to the global financial crisis. More recently, geopolitical tensions elsewhere in the broader Middle East have emerged as a factor.

The total inward FDI stock in Bahrain stood at USD18.8bn in 2014, an increase of 5.4% above the USD17.8bn recorded in 2013, and up 23.5% on the USD15.2bn stock in 2010. The economic importance of the Kingdom's inward FDI stock also exhibited relative growth, reaching 55.4% of GDP in 2014, up from 54.3% in the previous year.

Foreign direct investment inflows into Bahrain (USD mn)



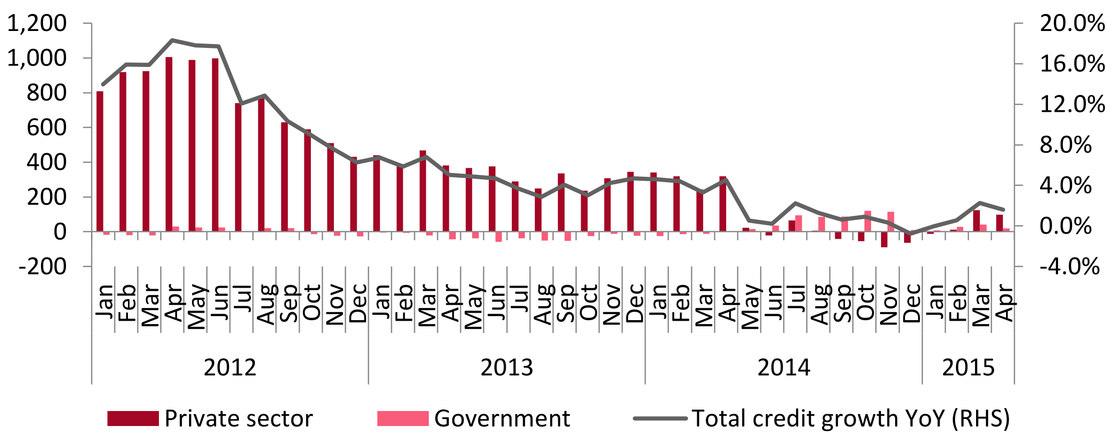
Source: United Nations Conference on Trade and Development

The banking sector remains strong

Bahraini banks remain in a strong position to boost lending

Building on strong annual results in 2014, Bahraini banks continued to post substantial increases in profitability during the first quarter of the year. Against this benign backdrop, credit growth in the Kingdom has strengthened since December as the build-up in infrastructure projects is beginning to be felt. The recent data on bank lending does not permit direct comparisons as some institutions have changed their licences from retail to other types. However, the data clearly shows that lending growth in recent months has risen, following a 0.8% contraction in December, to reach a high reading of 2.3% in March and a 1.6% growth pace in April of this year. Lending to the private sector has tended to be somewhat faster than the growth of credit to the Government in recent months.

Year-on-year credit growth to the private sector and government (BHD mn)



Source: Central Bank of Bahrain

Bank deposit growth has continued its steady upward climb to stand at BHD16.3bn in April and up 3.7% on BHD15.7bn a year earlier. Whereas banks' deposit liabilities to the Government have remained stable in recent years, some volatility notwithstanding, the stronger deposits base of retail banks has been driven by larger deposits from the private sector. In April, private sector deposits reached BHD9.6bn, which represented annual growth of 5.7%.

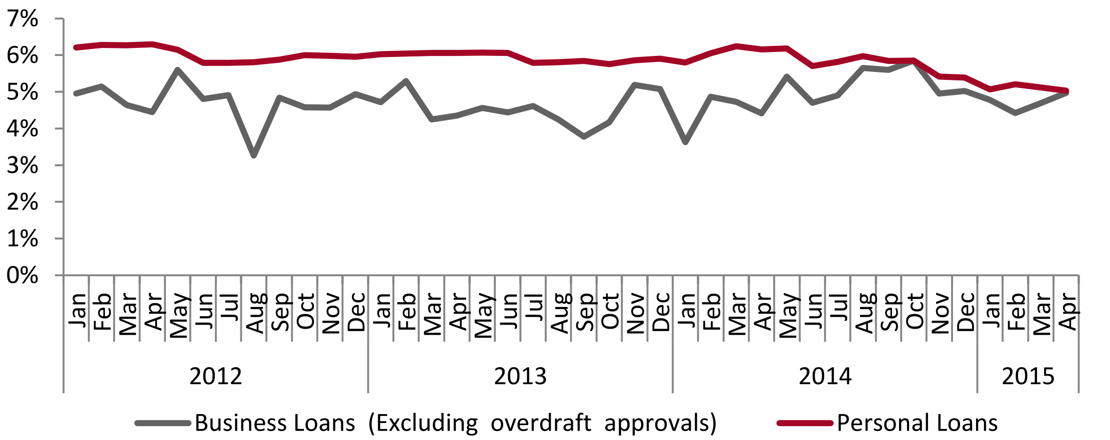
Deposit liabilities to non-banks (BHD mn)

Source: Central Bank of Bahrain

The cost of borrowing has remained low

In spite of recurrent worries about steps toward monetary tightening in the US, the cost of credit in Bahrain has trended down in recent months. The convergence of business and personal loan rates witnessed during the second half of 2014 showed some signs of renewed divergence during the opening months of this year. However, the average rate of interest on business loans rose in recent months to converge with the average interest rate on personal loans at 5.0% in April.

Average rate of interest on credit facilities (conventional retail banks)



Source: Central Bank of Bahrain

The Central Bank of Bahrain has introduced important new initiatives to support the development of Islamic finance in the Kingdom

The Central Bank of Bahrain has continued its established track record of regulatory and product innovation to support the development of Islamic finance:

- The CBB is taking steps to establish a national Shariah board of scholars. Embracing a national model is designed to reduce differences between Islamic products, thereby boosting investor confidence, as well as to speed the creation and launch of new product offerings.

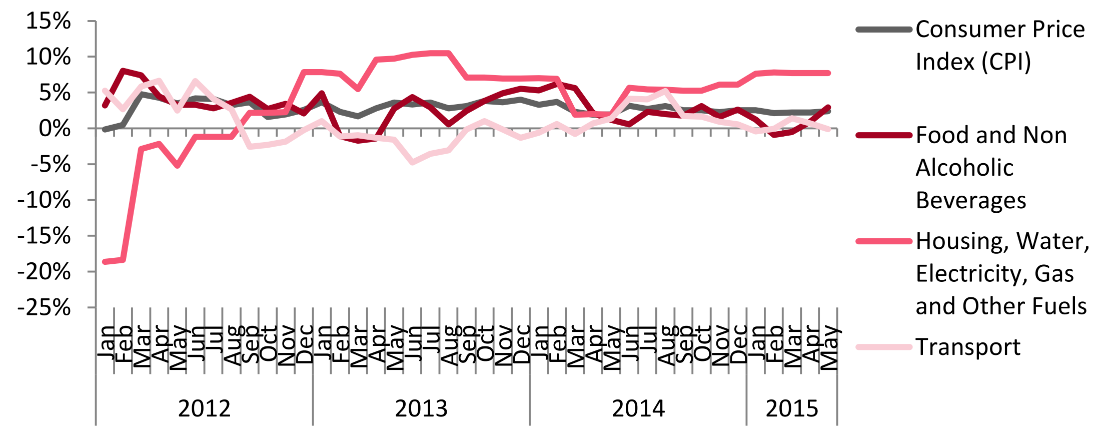
- The regulator introduced a new Islamic Sukuk Liquidity Instrument (ISLI) to manage liquidity at the Kingdom's Shariah-compliant banks. Islamic banks now have the opportunity to place excess liquidity in *wakala* deposits on a weekly basis, every Tuesday. The funds are then invested in a high-quality sukuk portfolio by the CBB on behalf of the banks. Previously, Islamic banks faced limited options and higher costs in managing their excess liquidity, as Shariah-compliant money markets lagged behind the conventional space. The most popular instruments included the CBB's monthly issues of 3- and 6-month sukuk. ISLI not only provides more efficient management of short-term liquidity, but it also enhances Islamic banks' readiness for Basel III high quality liquidity requirements.

Consumer price pressures remain moderate

New inflationary pressures have remained minimal

Headline consumer price inflation stood at 2.4% in May 2015, rising from an earlier moderated level of 2.20% in the past couple of months. Prices in the housing, water, electricity, gas and other fuels sector led the increase of the CPI index reading with a YoY advance of 7.7%, a figure that has remained constant since March. This reflects the ongoing recovery in the real estate market. The increase in the prices of food and non-alcoholic beverages rose to 2.9%. The transport sector witnessed a 0.1% decline in prices.

Sector-specific consumer price inflation indicators (YoY, %)

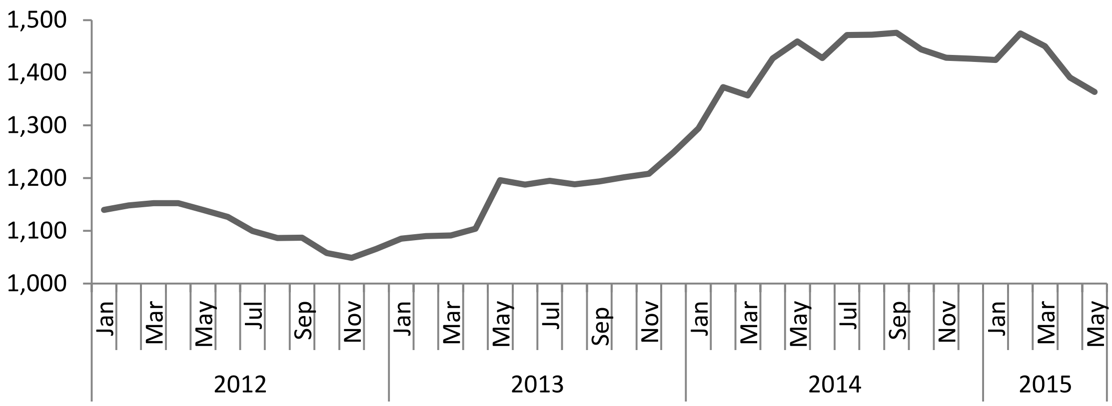


Source: Central Informatics Organisation

Capital market uncertainty

After emerging as one of the strongest regional stock markets during the opening months of 2015, Bahrain Bourse (BHB) experienced a small decline in its index during the first half of the year – by a total of 4.1%. This is in line with the general mixed sentiment felt across regional equity markets fuelled by the volatility in oil prices during the year so far. Nonetheless, the Bourse has continued its efforts to enhance trading activity and diversify its product and service offerings to investors and issuers.

Bahrain All-Share Index

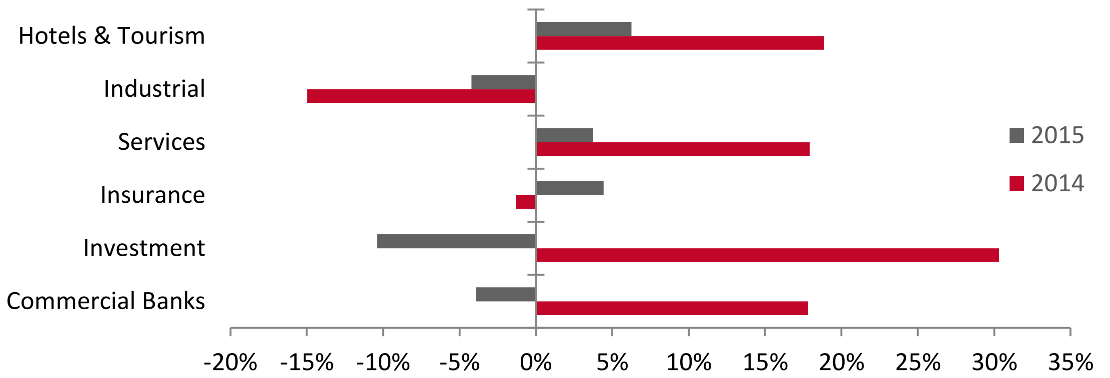


Source: Bahrain Bourse

Tourism and insurance were the strongest sectors on the Bourse during the first half of the year

The sectoral performance of the Bahrain All-Share Index paints a mixed picture so far during the year, with several sectors paring the gains realized in 2014 and turning into the red, while other sectors showing continued resilience since January 2015. The Hotels & Tourism sector, the third-strongest performing sector during 2014, led the Index in 2015, up by 6%. This was followed by the Insurance and Services sector, which posted 4% gains each.

Sectoral stock market indices, 2014-2015 YTD May



Source: Bahrain Bourse

Bahrain Bourse is expected to see the first listing of a real estate investment trust (REIT) this year. The Bourse approved in June the Trading Guidelines for REITs, following the approval of the Listing Guidelines of REITs which came into effect in May. REITs invest in income-generating properties, either through mortgages or direct property acquisitions. Since they are traded like equity, REITs offer investors a highly liquid opportunity of investing in real estate. BHB's rules allow for the listing of local and foreign REITs and require a minimum asset value of USD20mn. The securities must pay out a minimum of 90% of their realized income in dividends, and therefore would typically offer investors higher yields than other investments.

The fixed income market continues to see short-term (weekly, monthly, 3-month and 6-month) issuances of conventional treasury bills and Shariah-compliant sukuk by the Central Bank of Bahrain (CBB). Aside from the activity in short-term sovereign issuances, the CBB placed a 12-

month Treasury bill worth BHD200mn in the first week of June, with a coupon of 1.59%. The issue was oversubscribed at 220%. In a joint effort between Bahrain Bourse and the CBB, and for the first time regionally, both individual and institutional investors alike can participate in the primary market for CBB bond and sukuk issuances through BHB as of January.

Bahrain is expecting a clear revival in corporate capital market activity

Subsequent to the USD400mn, five-year conventional bond placed by BBK in March, the corporate bond market in Bahrain is set to see further activity later in the year, with players including Gulf Finance House and Al Baraka Banking Group having announced plans for sukuk issuances later in the year. During the second quarter of 2015, Ahli United Bank successfully priced its USD400mn Perpetual Additional Tier 1 bond, which will enhance its Tier 1 (core) capital base in order to meet stricter requirements under Basel III. The Bahraini-based lender was met with strong investor demand for its security, which offered a 6.875% coupon, following a successful roadshow across Singapore, Hong Kong, Abu Dhabi, Dubai, London, Zurich and Geneva. Another corporate issue was successfully placed in Q2 by Jawad Business Group, raising USD235mn to refinance existing debt through a combination of an amortized term loan (USD215mn) and a revolving facility (USD20mn).

Bahrain sovereign short-term bond and sukuk issuance

Issue Date	Issue	Value, BHD mn	Maturity, days	Average interest/ profit rate, %	Average price, %	Over-subscription, %
24 Jun 2015	Sukuk Al Salam No. 170	43	91	1.20		276
18 Jun 2015	Sukuk al ijarah No. 118	26	182	1.25		193
17 Jun 2015	Treasury bill No. 1552	70	91	1.21	99.696	211
10 Jun 2015	Treasury bills No. 1551	70	91	1.23	99.691	228
7 Jun 2015	Treasury bill No. 1550	35	182	1.25	99.372	372
4 Jun 2015	Treasury bill No. 25	200	12 months	1.59	98.416	220
3 Jun 2015	Treasury bill No. 1549	70	91	1.23	99.690	206
25 May 2015	Sukuk Al Salam No. 169	43	91	1.20		166
20 May 2015	Treasury bill No. 1548	70	91	1.23		
17 May 2015	Treasury bill No. 1547	35	182	1.25	99.372	178
13 May 2015	Treasury bill No. 1546	70	91			
12 May 2015	Sukuk al ijarah No. 117	26	182	1.25		100
6 May 2015	Treasury bill No. 1545	70	91	1.14	99.712	114
29 Apr 2015	Treasury bill No. 1544	70	91	0.99	99.751	100
20 Apr 2015	Sukuk al salam No. 168	43	91	0.92		100
15 Apr 2015	Treasury bill No. 1543	70	91	0.96	99.757	136
14 Apr 2015	Sukuk al ijarah No. 116	20	182	1.00		168
8 Apr 2015	Treasury bill No. 1542	70	91	0.92	99.767	110
5 Apr 2015	Treasury bill No. 1541	35	182	1.06	99.467	148.5
1 Apr 2015	Treasury bill No. 1540	70	91	0.81	99.783	180

Source: Central Bank of Bahrain

SME and entrepreneurship support infrastructure development

Through the Kingdom's diversification efforts over the past decade, economic growth has transitioned more towards service-oriented sectors and private sector industry. This has provided new opportunities for entrepreneurship and the development of small and medium-sized companies. This year has seen a number of initiatives to further develop the ecosystem of enterprise support in Bahrain:

- The Ministry of Industry and Commerce, in partnership with the International Finance

Corporation, has launched an online platform to provide advice and management support for SMEs in the areas of accounting, finance, human resources, legal and marketing. The Ministry will be working with Tamkeen, BDB and Bahrain Chamber of Commerce and Industry (BCCI) in promoting the portal.

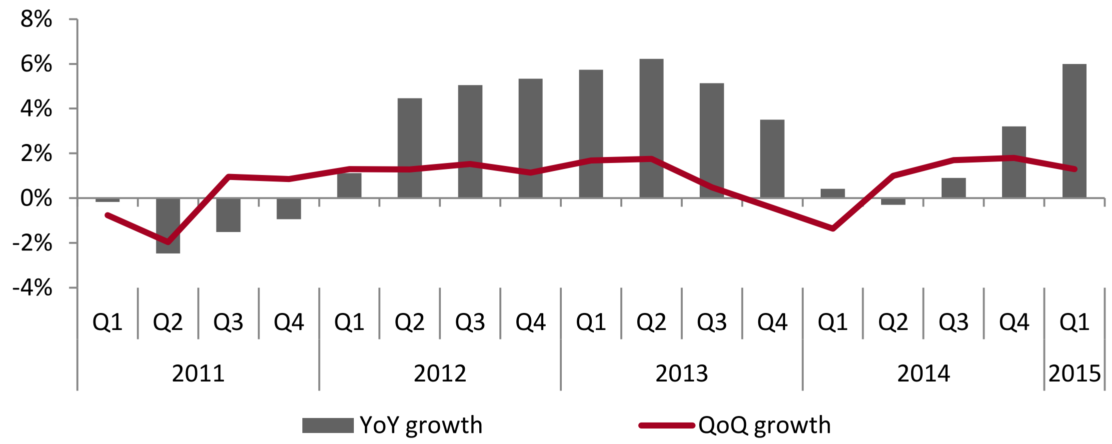
Important new initiatives are designed to support Bahrain's vibrant SME sector

- In recognition of the challenges faced by SMEs in securing financing through traditional channels, Bahrain Development Bank (BDB) has further enhanced its cooperation with Tamkeen to provide additional channels for SME funding through Tamkeen's Enterprise Finance Programme. In their most recent agreement, the two entities added BHD20mn to the programme in the form of Shariah-compliant facilities, to reach a total of BHD170mn in support.
- Tenmou, the first-of-its-kind angel investment company in the Kingdom, held the second MENA Angel Investors Summit 2015 in May. The event, which attracted over 200 angel investors and 45 growing start-ups from the region, led to the launch of the MENA Investor Network, the first network association of its kind in the region.
- The eighth roundtable discussion of the Waqf Fund, held at the Central Bank of Bahrain, focused on the development of Islamic venture capital. It emphasized the need for the development of favorable regulatory, accounting and legal environments to attract the participation of VC funding in start-ups and growth companies, along with appropriate exit routes.
- This year, Bahrain Bourse announced plans to launch the Bahrain Investment Market in 2015, an exchange designed for the listing and trading of local and regional SMEs.
- The establishment of BCMS, one of the world's leading advisors on the sale of private companies, in Bahrain during Q2 provides another exit channel to SMEs in Bahrain and other GCC states through BCMS's vast network and expertise within the M&A industry.

Labor market strength

According to the Ministry of Labour and the Labour Market Regulatory Authority, the labor market expanded markedly in the first quarter of 2015. Total employment stood at 694,909, up 5.0% over the same period in 2014, its quickest pace since 2Q13. This was mainly driven by the increase in expatriate labor as some of the long-term development projects have started to make headway. While Bahraini employment saw a modest increase of 1.9% YoY in Q1, expatriate labor grew 6.0% YoY. In the private sesctor, employment saw strong growth of 6.0% YoY during the quarter.

Total private sector employment growth (excl. domestic workers)



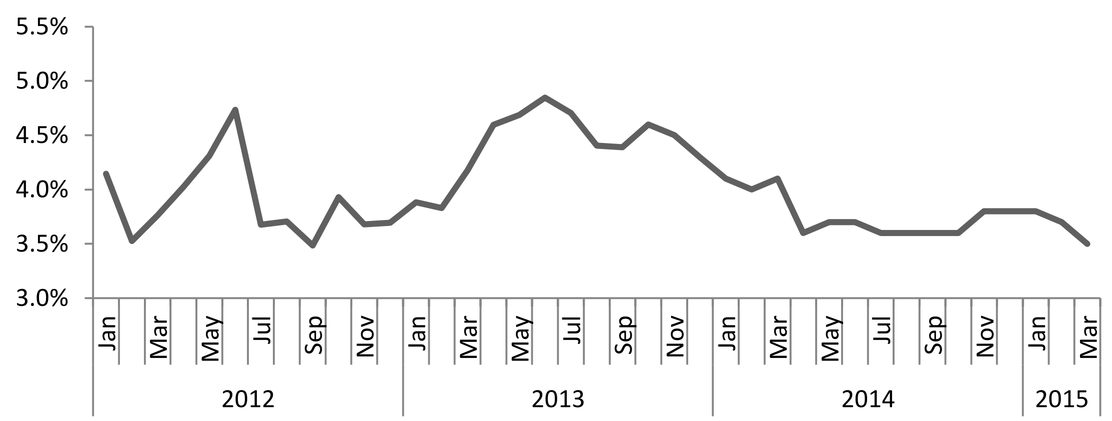
Source: Labour Market Regulatory Authority

The private sector continues to be at the forefront of employment growth in the Kingdom, representing 89% of the annual growth in total job creation during Q1. The number of private sector employees reached 518,921, an increase of 6,845 from 4Q14. In fact, private sector employment expanded 1.3% QoQ, completely absorbing the 1.1% QoQ growth in total employment along with a slight decline of 0.2% QoQ in public sector employment.

Unemployment has declined in recent months

The official unemployment rate fell during the first quarter of 2015, reaching 3.5% in March – a level last seen during 3Q12. This represented a significant improvement from the 3.8% reading in December 2014. Furthermore, the Ministry of Labour's vacancy bank reported 4,674 vacant positions in March, up 9% on January. A total of 2,854 individuals received training through the Ministry, representing a 61% increase on the number of trainees recorded in January.

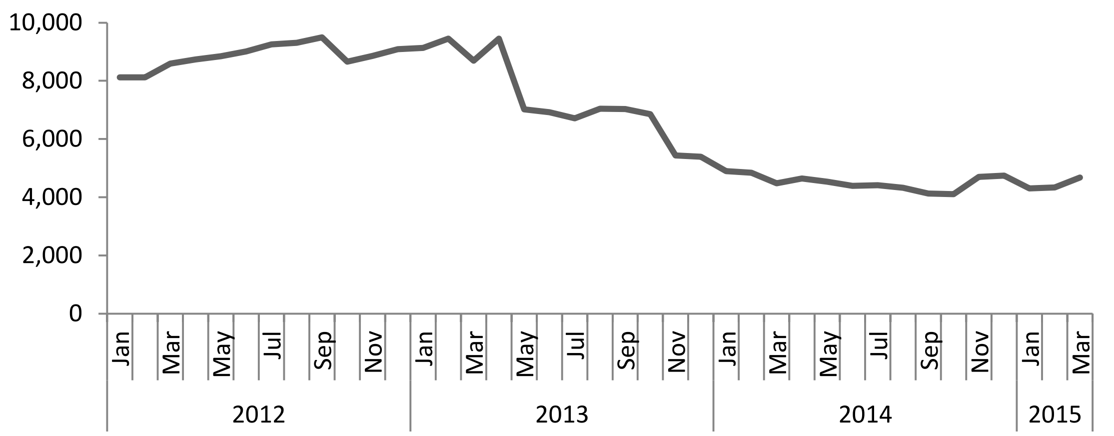
Unemployment rate (%)



Source: Ministry of Labour

In its most recent efforts to enable national employment within the private sector, Tamkeen signed an agreement with Citibank Bahrain in June to provide quality jobs for at least 70 Bahraini nationals. Tamkeen will support Citibank Bahrain in recruiting Bahraini graduates and training them for positions in the Citiphone call centre at the bank, with longer-term opportunities for growth and development in the bank. This agreement is the latest in a number of similar agreements that Tamkeen has signed in the past under its Employment Support Programme, which provides bespoke solutions to employers in meeting their human resource needs with qualified nationals. To date, the Programme has provided employment and training opportunities for 7,800 Bahrainis across many sectors.

Number of vacancies reported by the Ministry of Labour



Source: Ministry of Labour

External assessments

Bahrain's ICT credentials continue to compare favorably in the global context

The Kingdom of Bahrain has occupied the 30th position in the Networked Readiness Index covered in the Global Information Technology Report 2015. The report, published by the World Economic Forum in cooperation with INSEAD, provides an overview of the state of ICT readiness in 143 countries including ICT infrastructure, use of ICT among government and businesses, and social and economic impact of ICT. Bahrain maintained its score of 4.9 (out of 7) in the index, however its position has decreased slightly from the 29th place to the 30th. Nevertheless, Bahrain's ICT usage by individuals and government is strong, with 90% of the population using the Internet and some 93% of households being equipped with a computer (7th). The United Nations ranks it seventh for the quality of its online services offerings and 14th in the e-participation, which assesses the availability of online information and participatory tools and services to citizens. Additionally, the government consistently invests in advanced technologies (23rd).

The World Economic Forum has also published the Travel & Tourism Competitiveness Report 2015, which analyses the performance of 141 countries in tourism and related activities. The Travel & Tourism Competitiveness Index measures the set of factors and policies that enable the sustainable development of the sector including the enabling environment and policies and conditions. Bahrain's position has dropped 5 places to currently stand at 60th globally. Bahrain's current standing is attributed to the strong enabling business environment (11th), ICT readiness (15th), price competitiveness (18th), and ground and port infrastructure (11th).

The U.N. Sustainable Development Solutions Network published the Happiness Report 2015 which researches the controversial field of "happiness economics." The elements of happiness comprised life expectancy, freedom to make choices, perception of corruption, GDP per capita, social support (measured by having someone to count on in times of trouble) and generosity (measured by donations). The report surveyed a group of citizens in all 158 states between 2012 and 2014 using information from the global research company Gallup. Bahrain has had a significant jump in rank, moving 30 places upwards to rank 49th out of 158 countries in the 2015 Happiness Index.

Following the volatility of global oil prices, Fitch Ratings has revised Bahrain's sovereign credit ratings. Fitch has downgraded Bahrain's Long-term foreign currency Issuer Default Rating (IDR) to BBB- from BBB and Long-term local currency IDR to BBB from BBB+, with a stable outlook. Fitch has affirmed Bahrain's Country Ceiling at BBB+ and Short-term foreign currency IDR at F3. Moreover, Standard & Poor's has reaffirmed Bahrain's foreign and local currency sovereign credit ratings at BBB-/A-3.

Bahrain news

- Al Baraka Islamic Bank and Al Baraka Banking Group donated BHD5,000 to BIBF's Dealing Room, the first educational training facility of its kind in the region.
- Bahrain Mumtalakat Holding Company posted a strong 60% increase in operating income in Q1, and an 11% growth in profits, which reached BHD91.6mn.
- The Parliament in May approved a new law on international commercial arbitration, which is in line with the principles of the United Nations Commission on International Trade Law.
- Despite a decline in the price of LME aluminium, Alba exhibited an increase in its overall sales and throughput resulting in a positive Q1 result in 2015. Sales reached 228,307 mt, up 0.8% YoY, while production increased by 2.4% to 237,774 during the quarter.
- Desert Adventures, part of the Kuoni Destination Management Specialists division, has partnered up with Bahrain Mumtalakat Holding Company to establish the Kingdom's first destination management company. The company will capitalize on Bahrain's history as a tourism hub, its transport links and authentic culture to drive the potential in attracting more visitors and growing the tourism sector.
- Eagle Hills, a private real estate development company based in Dubai, showcased for the first time in Bahrain during the Gulf Property Show 2015 in May, its landmark project Marassi Al Bahrain. The 865,000 sqm waterfront destination will be located on the Northern shores of Diyar Al Muharraq, offering luxury hotels, residential apartments, restaurants, shopping and other leisure facilities.
- Manara Developments announced the launch of "Wahati" in Muharraq and the "Kenaz Al Bahrain" in the Northern Governorate, providing a total of 136 residential apartments. Kenaz Al Bahrain has reached 20% completion since it started in February, and is expected to complete in April 2016. Wahati is expected to be completed in 2 years.

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