

Fitch Affirms the Bank of Kuwait and the Middle East at 'A-'; Outlook Stable

September 22, 2008

Fitch Ratings has today affirmed the Bank of Kuwait and the Middle East's (BKME) ratings at long-term issuer default (IDR) 'A-' (A minus) with stable outlook, short-term IDR 'F2', individual 'C' and support '1'.

The support rating floor is affirmed at 'A-' (A minus).

BKME's IDRs and support rating reflect the extremely high probability of support from the Kuwaiti authorities, in case of need. The individual rating reflects the bank's sound asset quality and improving profitability and cost efficiency, but also the bank's relatively modest franchise, declining capital adequacy ratios and reliance on a relatively small and undiversified economy. Upward potential to the individual rating may arise if the bank succeeds in growing its franchise. Downside risk could arise if the bank's profitability, funding and/or capital adequacy were to come under significant pressure.

BKME's operating profit increased 34.9% yoy in H108 and 11.9% in 2007, driven by growth in fee income, primarily from the bank's brokerage/investment management activities, and, notably in H108, significant gains on the sale of equity investments. However, net interest revenue has been under pressure as Kuwaiti banks compete for corporate deposits to comply with the 80% loan/deposit ratio imposed by the Central Bank of Kuwait (CBK).

The impaired loans/total loans ratio worsened slightly to 3.1% in H1 2008 but impairment reserve coverage was sound at 122%. Loan growth has slowed in 2008. There is some concentration in real-estate lending and share-financing, as well as by borrower, though this is not unusual in Kuwait. Market risk is limited and mainly relates to its portfolio of equity investments. Funding consists largely of customer deposits, where there is some concentration but they have proved stable. Liquidity is supported by a portfolio of Kuwaiti government bonds and interbank placements, as well as facilities with group entities and other banks. Regulatory capital ratios have declined in H1 2008, mainly due to regulatory changes. At end-June 2008, the bank's Tier 1 and total capital ratios were, nevertheless, adequate at 10.6% and 13.2%, respectively. The Fitch eligible capital ratio stood at 13.2%.

BKME is a medium-sized Kuwaiti commercial bank, providing a broad range of retail, corporate, treasury and investment management services. In August 2005 Bahrain-based Ahli United Bank (rated 'A-' (A minus)/Stable) increased its stake in BKME to 75% from 48%. BKME is fully integrated into the AUB Group. The Public Institution for Social Security in Kuwait is the largest shareholder in AUB (19.5%) and holds 11.9% of BKME. In June 2008 the CBK granted in-principle approval for BKME to convert to an Islamic bank within one year.

Source: AME Info