11- CAPITAL ADEQUACY RATIO

A) Circular No. (2/BS/184/2005) Regarding the Implementation of the Revised Capital Adequacy Ratio Basel (2).

B) Instructions No. (2/BS/28/97) on the conditions to be observed when evaluating fixed assets and long-term financial investments, and when determining the valuation provision which is allowed to be included within the components of subordinated capital for the purposes of measuring capital adequacy ratio.

C) Circular Dated 9/12/2001 requiring banks to calculate the ratios required under Central Bank of Kuwait's instructions (Maximum credit concentration limit, financing securities trading, liquidity… etc) on the basis of the capital in its broad concept as on the data submission date.

D) Instructions No. (2/BS/94/2002) requiring banks to report the fair value reserve resulting from Financial Investments Available for Sale, within the components of the subordinated capital when calculating capital adequacy ratio.

E) Circular No. (2/BS/217/2008) to all foreign banks branches operating in the Sate of Kuwait, concerning the amendment of the implementation of the instructions of Basel (2) Capital Adequacy Ratio.

F) Circular No. (2/BS/220/2008) concerning the amendment of the instructions of Basel (2) Capital Adequacy Ratio.

G) Circular No. (2/BS/225/2008) on considering real estate properties as one of the acceptable (eligible) collaterals for mitigating credit risk, when calculating the capital adequacy ratio.

H) Circular requesting to provide the Central Bank of Kuwait with the results of stress testing as per the financial position on 31/12/2008.

I) Circular stressing that banks should give due attention to stress testing, and to submit the results of those tests as per the financial position on 31/3/2009.

J) Circular No. (2/BS/245/2009) concerning the amendment of instructions on Capital Adequacy Ratio Basel (2).

K) Circular No. (2/BS/246/2009) on conducting appropriate stress testing according to the amendments made to Capital Adequacy Ratio Basel (2).

L) Circular concerning the findings revealed by stress testing conducted by banks according to the financial position on 31/3/2009, and the need to regularly conduct stress testing on a semi-annual basis.

M) Circular No. (2/BS, IBS/303/2010) concerning providing the Central Bank of Kuwait, on a half year basis, with reports on financial stress testing and internal capital adequacy assessment process (ICAAP).

N) Circular No. (2/BS,IBS/260/2010) to all foreign banks operating in Kuwait to provide the Central Bank of Kuwait with annual models relating to reports on financial stress testing.

GOVERNOR

Thu Alqi'da 10, 1426 H
December 12, 2005

THE CHAIRMAN,

Circular No. (2/BS/184/2005)
To all Local Conventional Banks and Foreign Banks Branches
Regarding the Implementation of the Revised
Capital Adequacy Ratio Basel (2)

Within the Central Bank of Kuwait's endeavors to upgrade the regulatory methods and instruments so as to cope with the latest developments in the global banking industry, the Central Bank of Kuwait Board of Directors approved at its meeting of 11/12/2005 the application of the revised capital adequacy ratio to local conventional banks, including foreign banks branches operating in Kuwait, with effect from 31/12/2005, by implementing the standardized approach in measuring credit risk and operational risk.

Attached are the instructions issued in this regard, as well as the set of reports banks will have to submit to the Central Bank of Kuwait concerning the measurement and calculation of capital adequacy ratio, while taking the following rules into account:

1) These instructions will replace, effective 31/12/2005, the currently applied instructions regarding capital adequacy ratio, while continuing to apply the current minimum capital adequacy ratio of 12%.

2) The data on capital adequacy ratio must be prepared on a quarterly bases (31/12, 31/3, 30/6, 30/9), and should be received by the Central Bank of Kuwait supervision sector, along with the closing financial data, not later than 14 days from the date used as a base for preparing the data.

3) The reports submitted on the measurement and calculation of capital adequacy ratio must be signed be your Chief General Manager **and reviewed** by your external auditors for the quarterly periods ending on (31/3, 30/6, 30/9). As for the closing financial period ending on 31/12, the data on the capital adequacy ratio must be signed by your Chief General Manager **and audited** by your external auditors.

The Central Bank of Kuwait would like to mention that the implementation of the revised capital adequacy ratio Basel (2), and the issuance of the attached instructions regarding the mechanism of implementation, have been decided in the light of the meetings and correspondence between the Central Bank of Kuwait and local banks during the second half of 2004 and the beginning of 2005, and after local banks have conducted experimental tests for the draft proposed instructions, and made their comments that were taken into account when preparing the relevant instructions.

The Central Bank of Kuwait would also like to stress the importance of the following pillars included in these instructions, as follows:

First: The revised ratio included essential differences from the ratio currently applied, which work towards reducing capital requirements for banks, including :

1) Giving a risk weight of 75% for the exposures of retail loans, and loans to small and medium size institutions. Since this risk weight is lower than the current risk weight of 100%, this will result in reducing the exposures for these claims, and accordingly the capital requirements, particularly that these claims represent a significant portion of banks loans portfolios. Therefore, the Central Bank would like to stress the importance of strictly implementing these instructions, especially in terms of identifying retail loans with relevant criteria, and claims on small and medium size institutions while taking into account the nature of their business as commercial institutions of regular debts, as well as ascertaining that these institutions fall within the groups that require a risk weight based on external rating, or a risk weight of 100%. The same note applies to housing loans qualified for a risk weight of 35%, and which must also be identified in the light of the relevant criteria qualifying them for this risk weight (1).

2) The revised capital adequacy ratio, and the Central Bank of Kuwait relevant instructions, allow banks to benefit from credit risk mitigation techniques through reducing credit exposures by a set of specified collaterals.

   The Central Bank of Kuwait also stresses the importance of accurately implementing the relevant instructions.

(1) The risk weight of the retail loans (excluding loans to small and medium size enterprises) was raised from 75% to 100% pursuant to circular No. (2/BS/220/2008) issued on 12/5/2008.

3) Since the basic direction of the standarized approach in measuring credit risk is based on the degrees of credit worthiness determined by external rating agencies, particularly in relation to claims on corporates, the Central Bank expects local banks to adopt this direction as an overall approach in rating such claims, and not as part of a selective process for a certain group of companies for the sake of benefiting from low risk weights.

It's also noticed that Basel (2) capital adequacy ratio, and the Central Bank of Kuwait relevant instructions, have allowed banks to include the interim profits within the components of the capital, as well as to benefit from the general reserves to the extent that covers 1.25% of the credit exposures. All of these matters require banks to be careful when applying the benefits or preferential treatment in measuring and calculating capital adequacy ratio. **Therefore, as clearly stated in the instructions, the Central Bank of Kuwait will amend the credit risk weights if the regulatory review so justifies.**

Second: In the light of the above comments, the Central Bank of Kuwait will take into account the significance of integration among the three pillars of Basel (2), in terms of stressing the effective implementation of the second pillar (regulatory review), and the third pillar (market discipline – public disclosure) in the manner detailed in the revised ratio and in the Central Bank of Kuwait relevant instructions.

In this context, and following the experimental implementation of the ratio and the discussions held in this connection, the Central Bank would like to underline the significance of the following accepts within the scope of implementing these instructions:

1) Regarding the requirements for implementing the second pillar of the ratio, the instructions urged banks senior managements to develop strategies for measuring capital adequacy to be approved by their boards of directors, as well as appropriate policies and procedures designed for identifying and measuring risks and the process of evaluating capital adequacy versus those risks. The instructions also require the banks to develop the systems and regulatory reports on these risk exposures and their effects on the capital, in addition to enhancing internal control systems, and other relevant requirements under those instructions.

2) Regarding the implementation of **the third pillar** of the ratio, the Central Bank of Kuwait stresses the importance of disclosure as an essential part of the revised capital adequacy ratio. The instructions illustrated in detail the general requirements of disclosure, including the presence of a disclosure policy approved by the board of directors, and the requirements for quantitative and qualitative information disclosure.

Banks are required to provide the Central Bank of Kuwait with approved copies of the set of policies and procedures relating to the applications of the second and third pillars of the revised capital adequacy ratio.

The Central Bank of Kuwait hopes that the implementation of the revised ratio will motivate banks to enhance risk management and control, as well as to develop an appropriate method for this purpose, in preparation for implementing more advanced standards in the future, as mentioned in the proposal of Basel Committee on Banking Supervision.

With my best wishes,

SALEM ABDUL AZIZ AL-SABAH

Rules & Regulations Concerning Capital Adequacy Standard

Basel (2)

Central Bank of Kuwait

11- CAPITAL ADEQUACY RATIO

A) Circular No. (2/BS/184/2005) Regarding the Implementation of the Revised Capital Adequacy Ratio Basel (2).

First: Introduction:

1. Pursuant to the provisions of Article 72 of Law No. (32) of year 1968 concerning currency, the Central Bank of Kuwait and the organisation of banking business, and in keeping with the Basel Committee's revised capital adequacy framework issued in June 2004, the Board of the Central Bank of Kuwait has resolved that such revised framework shall be applied to the banks in Kuwait using the risk measurement options stipulated in these regulations.

(a) Purpose:

2. These directives set out the new capital adequacy requirements for calculating and maintaining the minimum capital required for credit, operational and market risks under the Standardized Approach.

11- CAPITAL ADEQUACY RATIO
A) Circular No. (2/BS/184/2005) Regarding the Implementation of the Revised Capital Adequacy Ratio Basel (2).

3. The Central Bank of Kuwait requires in particular that all licensed banks maintain adequate capital, in accordance with these Regulations, against their risks as capital provides banks with a cushion to absorb losses without endangering customer deposits.

Second: Scope of Application:

4. Regulations in this document are applicable to all banks – except Islamic banks - which locally incorporated and branches of foreign banks licensed and operating in the State of Kuwait, therein called 'licensed banks'.

5. These regulations are effective on 31st December 2005.

6. Locally incorporated banks are required to observe these regulations on a consolidated group basis. At its discretion, the Central Bank of Kuwait may require locally incorporated banks to observe these regulations on a stand-alone basis.

(a) Investments in banking, securities and other financial entities:

7. Majority-owned or – controlled banking entities, securities entities and other financial entities (more than 50% equity interest) should generally be ***fully consolidated.*** In cases where this is not feasible, such as where the holding is temporary in nature and non-consolidation is a legal requirement of the host supervisor or the entity is subject to different regulation, the carrying value of the subject equity interest should be deducted from the bank's capital base.

8. In case of ***non-consolidated subsidiaries which have capital shortfall*** as determined by its regulator, the relevant licensed bank should immediately inform the Central Bank of the capital shortfall. The Central Bank of Kuwait shall then monitor the actions taken by the subsidiary to correct the shortfall, and if it is not corrected in a timely manner, the shortfall will also be deducted from the licensed bank's capital base.

9. The Central Bank of Kuwait will assess the appropriateness of recognising in consolidated capital the ***minority interests*** that arise from the consolidation of less than wholly owned banking, securities or other financial entities with a focus on the availability of such minority interest capital to the locally incorporated bank. More specifically, the Central Bank of Kuwait will adjust the amount of such minority interests that may be included in capital base in the event the capital from such minority interests is not available to the locally incorporated bank.

10. **Significant minority investments (more than 20% but less than 50% equity interests)** in banking, securities and other financial entities**, where control does not exist**, should be deducted from the bank's capital base. This also includes other investments in any capital instrument defined under capital base. Alternatively, such investments might be, under certain conditions, consolidated on a pro rata basis. More specifically, **pro rata consolidation** may be appropriate for joint ventures or where the Central Bank of Kuwait is satisfied that the locally incorporated bank is legally or de facto expected to support the entity on a proportionate basis only and the other significant shareholders have the means and the willingness to proportionately support it. If the equity investment is 20% or below, the fair value of such investment, net of the 55% discount referred to under paragraph 17 (c), should be risk weighted at 100%. An example of the calculation of the risk weighted amount of the investment is given in annex (N).

11. Any **reciprocal cross-holdings of bank capital** that is artificially designed to inflate the capital position of locally incorporated banks will be deducted from capital base for capital adequacy purposes. In determining such reciprocal cross-holdings, the Central Bank of Kuwait will take into account any bilateral agreement, dates and timings of such transactions and the amount of the two transactions involved.

b) Significant investments in commercial entities:

12. Significant minority and majority investments in commercial entities which exceed certain materiality levels will be deducted from the licensed banks' capital base.

13. In accordance with Article 67 of Law No. (32) of year 1968 concerning currency, the Central Bank of Kuwait and the organisation of banking business, and the Central Bank's various instructions in connection with the organisation of local banks investment policy, materiality levels of 10% of the licensed bank's capital base for individual significant investment in a commercial entity and 50% of the licensed bank's capital base for the aggregate of such investments will be applied. The amount to be deducted will be that portion of the investment at fair value net of the proportionate 55% discount referred to under paragraph 17 (c), which exceeds the materiality levels. However, in case of investment in excess of 10% level and which are pre-approved by the Central Bank the materiality level for deduction purposes will be 15% for a single

investment, i.e., the amount to be deducted will the portion which is in excess of 15% net of the proportionate 55% discount. An example showing the calculation of the amount that should be deducted is given in annex (O).

14. Investment in commercial entities which is below the materiality thresholds mentioned above will be treated under 'Other Exposures'.

c) Investments in Insurance entities:

15. Equity investment in excess of 20% in an insurance entity should be deducted from the bank's capital base. In case of 20% or less equity investment, the investment exposure should be risk weighted based on the corporates credit quality grades detailed in paragraph 50 below.

Third: Capital Base Components:

(1) Core Capital (Tier 1)"

16. Core Capital shall consist of the following items:

a. **Permanent shareholders' equity** (including issued and fully paid ordinary shares / common stock and perpetual non-cumulative preference shares, but excluding cumulative preference shares);

b. **Disclosed reserves**, which are audited and approved by the shareholders, in the form of legal, general and other reserves established by appropriations of retained earnings, share premiums and other surplus but excluding asset revaluation and fair value reserves; and

c. **Minority interests**, arising on consolidation, in the equity of subsidiaries which are less than wholly owned, provided it meets the conditions stated in paragraph 9 above.

LESS:

d. **Treasury shares** (licensed bank's own shares purchased),

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A) Circular No. (2/BS/184/2005) Regarding the Implementation of the Revised Capital Adequacy Ratio Basel (2).

e. **Goodwill** arising through consolidation of subsidiaries, merger or combination of businesses. Goodwill relating to entities subject to a deduction approach pursuant to this regulations should be deducted from Tier 1 in the same manner as goodwill relating to consolidated subsidiaries, and the remainder of the investments should be deducted as provided under "Capital Deduction" section below, and

f. **Current year's cumulative net losses** which have been reviewed or audited as per the International Standards on Auditing (ISA) by the external auditors.

(2) Supplementary Capital (Tier 2):

17. Supplementary Capital shall consist of the following items:

a. **Interim retained profits** which <u>have been reviewed as per the ISA by the external auditors;</u> (1)

b. **Asset revaluation reserves,** which arise from the revaluation of fixed assets from time to time in line with the change in market values, and are reflected on the face of the balance sheet as a revaluation reserve. A discount of 55% will be applied to the difference between the historical book value and the market value to reflect the potential volatility of this form of unrealised capital. Banks should observe the conditions stipulated in Circular No. (2/BS/28/97) with respect to this type of reserves.

c. **Fair value reserves** may be included in tier (2) capital, with the concurrence of the external auditors, provided that the subject assets are prudently valued, fully reflecting the possibility of price fluctuation and forced sale. A discount of 55% will be applied to the difference between the historical book value and the fair value to reflect the potential volatility of this form of unrealised capital. This shall be applied on an aggregate net-basis (portfolio-wise). For the purpose of capital adequacy and any relevant capital deductions, the discount amount referred to above should be deducted from the relevant asset. Moreover, banks should observe, wherever applicable, the conditions stipulated in Circulars No. (2/BS/28/97) and (2/BS/94/2002) with respect to this type of reserves.

(1) This item was excluded from capital base components pursuant to circular No. (2/BS/220/2008) issued on 12/5/2008.

d. **General provisions** held against future, presently unidentified losses which are freely available to meet losses which subsequently materialise and, therefore, qualify for inclusion within supplementary elements of capital, subject to a maximum of 1.25% of total credit risk-weighted assets. Provisions ascribed to impairment of particular assets or known liabilities should be excluded. The 2%(1) general provisions required in accordance with the Central Bank of Kuwait instructions shall be included within this item subject to the limit above. The remaining balance over and above the 1.25% limit should be deducted from the licensed bank's total credit risk weighted assets.

e. **Hybrid instruments**, which include a range of instruments which combine characteristics of equity capital and of debt, and which meet the following requirements:

   i. They are unsecured, subordinated and fully paid-up;

   ii. They are not redeemable at the initiative of the holder or without the prior consent of the Central Bank of Kuwait;

   iii. They are available to participate in losses without the bank being obliged to cease trading (unlike conventional subordinated debt); and

   iv. Although the capital instrument may carry an obligation to pay interest that cannot permanently be reduced or waived (unlike dividends on ordinary shareholders' equity), it should allow service obligations to be deferred (as with cumulative preference shares) where the profitability of the bank would not support payment.

   v. **Cumulative preference shares**, having the above characteristics, would be eligible for inclusion in tier (2) capital. Debt capital instruments which do not meet the above criteria may be eligible for inclusion under item (f) below.

f. **Subordinated term debt**, which comprises all conventional unsecured borrowing subordinated (in respect of both interest and principal) to all other liabilities of the bank except the share capital and **limited life redeemable preference shares**. Unlike instruments included in item (d) above, these instruments are not normally available to participate in the losses of a bank which continues trading. For this reason, these instruments will be limited to a maximum of 50% of tier (1) capital. To be eligible for inclusion in tier (2) capital, such debt must meet the following conditions:

(1) The ratio of general provision has been reduced for the Credit facilities (cash and non-cash) was amended according to Circular No. (2/BS/204/2007) issued on 12/3/2007.

1) Maturity: The subordinated debt should have a minimum original fixed term to maturity of over five years;

2) It should be fully paid up;

3) Subordination: The term of the debt agreement should ensure that the claims of the lender are fully subordinated to those of the unsubordinated creditors. More specifically, the subordination provisions should ensure the following:

    - The claims of the subordinated creditors should rank behind those of all unsubordinated creditors;

    - To the fullest extent possible creditors should waive their right to set off any amounts they owe the bank against subordinated amounts owed to them by the bank;

    - The only events of default should be (a) non-payment of any amount due and payable (principal and interest only) under the debt agreement (or guarantee), and (b) the winding-up of the institution (or borrower where this is not the same)

    - The only remedies available to the subordinated creditor in the event of default in respect of the subordinated debt should normally be limited to:

        a) Petitioning for the winding up of the institution (and the borrower where this is not the same, i.e. in circumstances where the borrower is a subsidiary of the bank or some other related company but the bank is acting as guarantor of the debt)

        b) Proving for its debt and claiming in the liquidation of the bank (and the borrower where this is not the same). The Central Bank of Kuwait does not consider that there should be the right to sue for unpaid amounts because this might enable subordinated creditors to obtain full repayment through the courts shortly before the bank goes into liquidation, thus reducing the cash available to depositors. However, if it is legally impossible to limit the remedies available to lenders to those stated above, the lender may have the right to sue for unpaid principal which is due and payable under the debt agreement, provided the bank has an option to defer repayment for at least six months after the contractual repayment date. The bank should also have the option to defer interest payments until a dividend is paid.

Moreover. An event of default should not accelerate the debt in the sense of weakening the subordination provisions or permitting repayment outside a winding-up;

c) The debt agreement should expressly exclude all other remedies. A bank should always provide the Central Bank of Kuwait with written confirmation that it has received a written legal opinion from its legal adviser stating that these subordination requirements have been met.

4) Applicable Law: The debt agreement should normally be subject to Kuwaiti Law. Other law is acceptable, but only where it is necessary for the success of the issue. In cases where the debt is issued under overseas law, the Central Bank should be satisfied that an adequate degree of subordination can be achieved under the overseas law. More specifically, the issuing bank should obtain an opinion confirming that an adequate degree of subordination can be achieved. This should be obtained from lawyers with a demonstrable track record, and a high level of expertise in this area of law, in the country concerned.

5) Trigger clauses: The debt agreement should not contain any clause which might require early repayment of the debt (e.g. cross default clauses, negative pledges and restrictive covenants), or which might make the debt more expensive (e.g. a clause which leads to an increase in the interest paid on the debt under a given circumstance). This should not however prejudice any right to petition for the winding-up of the borrower, for example, in the event of non-payment of interest on the debt.

6) Repayment: No early repayments should be made without the Central Bank's prior written agreement. This includes purchases of capital notes by the bank or its subsidiaries for cancellation. The Central Bank of Kuwait will only agree where it is satisfied that the bank's capital is adequate after repayment, and that it is likely to remain so for at least two years.

   The Central Bank of Kuwait considers it essential that note-holders should be made aware of the restriction on early repayment, either through the loan agreement, or in the offer documents, or through other information sources commonly used in the markets.

Prior to agreeing to early repayment the bank should provide the Central bank with a capital plan showing that its capital will remain adequate (above the minimum capital adequacy ratio) after repayment, and that it is likely to remain so for at least two years.

7) Amortisation: During the last four years to maturity, a cumulative discount (or amortisation) factor of 20% per year will be applied to reflect the diminishing value of these instruments as a continuing source of strength.

Calculation of the percentages eligible for inclusion within supplementary capital shall be based on the following:

Remaining Term to Maturity	**Percentages**
From 4 to less than 5 years	80
From 3 to less than 4 years	60
From 2 to less than 3 years	40
From 1 to less than 2 years	20

8) Step-ups: There are two methods of treating subordinated debt which includes a step-up, depending on the size of the step-up involved, which a bank should adopt.

- Where the sum of all possible step-ups is no more than 50 basis points in the first ten years of the issue or no more than 100 basis points over the whole life of the issue, the debt may be treated as at its original maturity.

- Issues with step-ups of more than 50 basis points in the first ten years of an issue, or more than 100 basis points over the life of an issue should be treated as term debt which matures at the date the step-up is triggered (i.e. at the date of the call option).

The limits on step-ups are cumulative and apply to the all-in cost of the debt to the bank.

The Central Bank of Kuwait objects to high step-ups, as they can make a bank's capital expensive at a time when the reason that the issue has not been called is that alternative sources of finance are not readily available.

Subordinated debt issues with step-ups in the first five years should not be included in the capital base.

Banks should discuss proposed step-ups with the Central Bank of Kuwait in advance to establish whether they are acceptable in this context. On occasion a floating-rate debt issue may contain a provision that the benchmark interest rate changes from one standard to another (e.g. from a Treasury bill rate to a LIBOR rate), the change in benchmark typically occurs following the failure to exercise a call. The Central Bank of Kuwait will wish to consider issues where the step-up involves changes in the reference rate to see whether this together with any margin change indicates an excessive step-up. The Central Bank of Kuwait will also wish to consider issues containing embedded options, e.g. issues containing options for the interest rate after the step-up to be at a margin over the higher of two (or more) reference rates, or for the interest rate in the previous period to act as a floor. The inclusion of such options may affect the funding costs of the borrower and imply a step-up.

18. The total elements of supplementary capital that is eligible for inclusion within capital base shall not exceed 100% of the total core capital after deducting goodwill and treasury shares.

(3) Ancillary Capital (Tier 3):

19. Tier (3) capital shall consist of short-term subordinated debt which, if circumstances demand, needs to be capable of becoming part of the bank's permanent capital and thus be available to absorb losses in the event of insolvency. It must, therefore, at a minimum meet the following conditions:

    a. Be unsecured, subordinated and fully paid up;

    b. Have an original maturity of at least two years;

    c. Not be repayable or redeemable before the agreed repayment date and without prior approval by the Central Bank of Kuwait;

    d. Be subject to a lock-in clause which stipulates that neither interest nor principal may be paid (even at maturity) if such payment means that the licensed bank falls below or remains below its minimum capital requirement; and

e. Tier (3) capital instruments must not contain restrictive covenants or default clauses that would allow the holder to trigger acceleration of repayment in circumstances other than the insolvency, bankruptcy or winding up of the issuer. Further, the debt agreement should be subject to Kuwaiti or English law, whichever is applicable.

20. The following limitations will apply to the use of tier (3) capital:

    a. Tier (3) capital can be used solely to support market risk;

    b. Tier (3) capital will be limited to 250% of a bank's tier (1) capital that is required to support market risks. Accordingly a minimum of about 28.5% of market risk needs to be supported by tier (1) capital that is not required to support risks in the remainder of the book;

    c. Tier (2) elements may be substituted for tier (3) up to the same limit of 250% in so far as the overall limits are not breached, i.e., eligible tier (2) capital may not exceed total tier (1) capital, and long term subordinated debt may not exceed 50% of tier 1 capital.

(4) Capital Deductions from Total Capital Base:

21. Where deductions of investments are made pursuant to this section and 'Scope of Application" section above, the deduction will be 50% from Tier (1) and 50% from Tier (2) capital.

22. The limits on Tier (2) and Tier (3) capital will be based on the amount of Tier (1) capital after deduction of goodwill and treasury shares but before the deductions of any other items, including investments subject to deductions.

23. The following items shall be deducted from the licensed bank's capital base:

    a. Investment in unconsolidated majority-owned or –controlled banking, securities and other financial entities (more than 50% equity interest) subsidiaries,

    b. Any capital shortfall in non-consolidated banking, securities and other financial entities subsidiaries subject to the discretion of the Central Bank of Kuwait,

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A) Circular No. (2/BS/184/2005) Regarding the Implementation of the Revised Capital Adequacy Ratio Basel (2).

c. Significant minority investment in banking, securities and other financial entities unless pro-rata consolidated,

d. Minority interests arising from consolidation of banking, securities and other financial subsidiaries subject to the Central Bank of Kuwait discretion,

e. Reciprocal cross-holdings of bank capital subject to the Central Bank of Kuwait discretion,

f. The excess amount over the materiality thresholds stated under "Scope of Application" section above in case of equity investment in commercial entities.

g. Investment in excess of 20% of an insurance company based on its fair value,

h. The excess amount over and above the maximum permitted credit concentration limit subject to the discretion of the Central Bank of Kuwait,

i. Securitization and credit derivative exposures that are subject to deductions, and

j. Any other exposure that the Central Bank of Kuwait deems necessary.

(5) Minimum Capital Adequacy Ratio:

24. The Capital Adequacy Ratio (CAR) for each licensed bank shall not be less than 12%. Such ratio shall be calculated on the basis of the licensed bank's consolidated financial statements in the case of locally incorporated banks. Branches of foreign banks, on the other hand, should calculate their CAR based on their Kuwaiti operations only.

25. However, the Central Bank of Kuwait may require certain target and trigger ratios for each licensed bank depending on each licensed bank's risk profile as assessed by the Central Bank of Kuwait. Such assessment will be conducted based on certain risk profiling methodology which shall be discussed with and communicated to the banks in due course.

11- CAPITAL ADEQUACY RATIO

A) Circular No. (2/BS/184/2005) Regarding the Implementation of the Revised Capital Adequacy Ratio Basel (2).

26. Licensed banks must give the Central Bank, immediate written notification of any actual breach of the 12%. Where such notification is made, the licensed bank must also provide written action plan setting out how the licensed bank proposes to restore its CAR to the 12% limit.

27. The action plan should also describe how the licensed bank will ensure that a breach of the minimum CAR will not occur again in the future. The licensed bank should report its CAR calculation on a weekly basis thereafter until its CAR has reached the minimum level of 12%.

28. An illustration of the calculation of capital adequacy ratio is set out in example (1) of annex (K).

Fourth: Credit Risk Weighting of On-balance Sheet Exposures (Assets):

(a) General requirements:

29. This section sets out the weighting framework to be adopted by licensed banks to quantify their credit risk for calculating the capital adequacy ratio under the Standardised Approach developed by the Basel Committee on Banking Supervision.

30. All licensed banks are required to use the Standardised Approach for credit risks. The qualifying criteria for the use of this approach are detailed below.

31. Under the Standardised Approach, different categories of on- and off-balance sheet exposures of a licensed bank are to be risk-weighted according to the ratings assigned by external credit assessment institutions (ECAIs), where available and applicable, or the risk weights assigned by the Central Bank of Kuwait based on certain standard characteristics of the exposure (such as nature of exposure, repayment status, etc).

32. Where the risk weights are determined by external credit assessments, licensed banks should only use those assigned on a solicited basis by institutions (i.e. ECAIs) that are recognised by the Central Bank of Kuwait. Recognition criteria, approval process and the list of ECAIs are set out in annex (B) related to "Recognition of ECAIs".

33. The requirements set out in this section apply to all credit exposures of a licensed bank except for credit exposures related to securities in the trading book which should be captured as part of a licensed bank's market risk exposures.

(b) Standard Portfolios:

34. For the purpose of risk-weighting[1] under the Standardised Approach, credit exposures should first be categorised into the following 12 standard portfolios:

    1) Claims on sovereigns.
    2) Claims on International Organisations.
    3) Claims on public sector entities (PSEs).
    4) Claims on multilateral development banks (MDBs).
    5) Claims on banks.
    6) Claims on corporate.
    7) Cash items.
    8) Regulatory retail exposures.
    9) Qualifying residential housing loans.
    10) Past due exposures.
    11) Other exposures.
    12) Securitization exposures.

35. These 12 standard portfolios are mutually exclusive and therefore any given exposure should be categorised under only one of them. <u>For example, no qualifying residential housing loans should be categorised under regulatory retail exposure.</u> Each of the portfolios has its own risk-weighting scale. The risk weight for an exposure under portfolios (1) to (6) and (12) is based on credit assessments of ECAIs. These are discussed in detail below. The risk weight for an exposure under portfolios (7) to (11) is assigned based on certain standard characteristics of the exposures (such as the nature of borrower, repayment status, etc). These are also discussed in detail below.

(c) Calculation of credit risk-weighted amount for on-balance sheet exposure (Assets):

36. The credit risk of any exposure for which a licensed bank has to set aside regulatory capital is measured in terms of the **Weighted Amount** of the exposure.

(1) a risk weight of 150% was determined for loans accorded to finance real estate activity and share trading activity, regardless of whether there is a credit rating for the customer, pursuant to circular No. (2/BS/220/2008) issued on 12/5/2008.

37. Licensed banks may use **Credit Risk Mitigation (CRM)** techniques to reduce its credit risk exposures. CRM techniques that are recognised by the Central Bank for capital adequacy purposes are collateral, guarantees and netting. Provided the relevant qualifying criteria are met, the weighted amount of a credit exposure supported by any of these techniques can be reduced. Detailed list of CRMs, the criteria for their recognition and the extent to which each of these techniques can reduce the capital requirement of a credit exposure are discussed in detail below.

38. The weighted amount is calculated by multiplying the principal amount, net of specific provisions, if any, with the applicable risk weight. For an exposure covered by eligible CRM techniques, the weighted amount of the exposure can be reduced based on the treatment described in the Credit Risk Mitigation section below.

(d) The risk weights for individual on-balance sheet claims

39. The standard portfolios (1) to (6) and (12) above should be risk-weighted based on their Credit Quality Grades and other relevant considerations.

Claims on Sovereigns

40. Any claim on the governments, central banks and monetary authorities of the Gulf Cooperation Council Countries (GCC governments) should be risk weighted at 0%.

41. Claims on other sovereigns should be risk-weighted based on the following **sovereign credit quality grades**:

Sovereigns Credit Quality Grades	1	2	3	4	5	6	Unrated
Risk weight	**0%**	**20%**	**50%**	**100%**	**100%**	**150%**	**100%**

42. Where an overseas national supervisory authority allows its local banks to apply a preferential risk weight to domestic currency claims on its sovereign, licensed banks may also apply the same preferential risk weight to such domestic currency exposures to the sovereign of that supervisory authority. Foreign currencies exposures of such sovereign should, however be subject to the sovereign risk weighting scale.

Claims on International Organisations

43. Claims on international organisations such as the International Monetary Fund, Bank for International Settlements, European Central Bank, European Commission will receive a 0% risk weight.

Claims on Public Sector Entities (PSEs)

44. Claims on Kuwaiti PSEs in Kuwaiti Dinar should be treated as claims on the Kuwaiti Government, whereas foreign currency claims on such PSEs should be risk weighted one grade less favourable than Kuwaiti Government, i.e. a risk weight of 20%.

45. Domestic currency claims on other GCC PSEs should be treated as claims on their sovereigns if their central bank or monetary authority treats it as such. Foreign currency claims on such PSEs should be risk weighted one grade less favourable than its sovereign, i.e., 20% risk weight.

46. Claims on other foreign PSEs should be risk weighted one grade less favourable than its sovereigns.

47. Claims on commercial companies owned by PSEs shall be treated as claims on corporates and assigned risk weight based on the corporate credit quality grade.

Claims on Multilateral Development Banks (MDBs)

48. Claims on MDBs that fulfill the eligibility criteria provided below in paragraph 49 should be risk-weighted at 0%. All other MDBs should be risk weighted based on ECAIs' ratings using the credit quality grades applicable to claims on banks but without using the preferential treatment for short-term claims.

49. The eligibility criteria for 0% risk weight treatment of MDBs are:

    a. Very high quality long-term issuer ratings, i.e. a majority of an MDB's external assessments must be AAA;

    b. Shareholder structure is comprised of a significant proportion of sovereigns with long-term issuer credit assessments of AA- or better, or the majority of the MDB's fund-raising are in the form of paid-in equity/capital and there is little or no leverage;

c. Strong shareholder support demonstrated by the amount of paid-in capital contributed by the shareholders; the amount of further capital the MDBs have the right to call, if required, to repay their liabilities; and continued capital contributions and new pledges from sovereign shareholders;

d. Adequate level of capital and liquidity (a case-by-case approach is necessary in order to assess whether each MDB's capital and liquidity are adequate); and,

e. Strict statutory lending requirements and conservative financial policies, which would include among other conditions a structured approval process, internal creditworthiness and risk concentration limits (per country, sector, and individual exposure and credit category), large exposures approval by the board or a committee of the board, fixed repayment schedules, effective monitoring of use of proceeds, status review process, and rigorous assessment of risk and provisioning to loan loss reserve.

Claims on Banks

50. Claims on licensed banks, including their overseas branches, should be assigned a risk weight one grade less favourable than that assigned to claims on the Kuwaiti Government, i.e., applying a risk weight of 20%. Claims on foreign banks outside Kuwait including Kuwaiti banks' overseas banking subsidiaries, should be risk weighted based on the banks credit quality grades below, i.e., assigning risk weight based on the external credit assessment of the bank itself.

51. Short-term claims on foreign banks shall be those which have an original maturity of three months or less and are not expected to be rolled over.

Banks Credit Quality Grades	**1**	**2**	**3**	**4**	**5**	**6**	**Unrated**
Risk weight for long-term claims	20%	50%	50%	100%	100%	150%	50%
Risk weight for short-term claims	20%	20%	20%	50%	50%	150%	20%

11- CAPITAL ADEQUACY RATIO
A) Circular No. (2/BS/184/2005) Regarding the Implementation of the Revised Capital Adequacy Ratio Basel (2).

Claims on Corporates

52. Claims on corporates should be risk-weighted as follows:

Sovereigns Credit Quality Grades	1	2	3	4	5	6	Unrated
Risk weight	20%	50%	100%	100%	150%	150%	100%

53. No claim on an unrated corporate should be given a risk weight lower than that assigned to its sovereign of incorporation.

54. Claims on securities firms, including Investment Firms licensed by the Central Bank of Kuwait, should be risk-weighted as claims on corporates.

55. The Central Bank of Kuwait may increase the above standard risk weight for unrated claims where it judges that a higher risk weight is warranted by the overall default experience in Kuwait. As part of the supervisory review process, the Central Bank may also consider whether the credit quality of corporate claims held by individual licensed banks should warrant a standard risk weight higher than 100%.

56. Equity interest of 20% or less in and claims on insurance companies should be risk weighted as corporates based on the above corporate credit quality grades.

Cash Items

57. The following types of asset are regarded as cash items which, except item (e), should attract a 0% risk weight:

a. Notes and coins.

b. All gold bullion held in the licensed bank's own vaults or in the vaults of other institutions.

c. Cheques, drafts and other items drawn on other banks that are payable immediately upon presentation and that are in the process of collection.

d. All receivable funds arising from the sale of securities, for the licensed bank's own account or on behalf of a customer, which are outstanding up to and including the fifth working day after the due settlement date.

e. All receivable funds arising from the purchase of securities on behalf of a customer, which are outstanding up to and including the fifth working day after the due settlement date should attract 20% risk weight.

Regulatory Retail Exposures

58. Regulatory retail exposures will include consumer loans, instalment loans, credit cards receivables, housing loans up to KD 250,000 but not qualifying for residential housing loans subject to the conditions below, small loans given to individuals such as advances against salary, temporary loans against floats/deposits, and exposures to qualifying small and medium sized enterprise (SMEs).

59. Except those that are past due as defined under 'past due exposures' below, claims that meet all of the following three criteria may be categorised as regulatory retail exposures and subject to a 75% preferential risk weight:

    a. **Orientation criterion:** The exposure must be either to an individual person or persons or to a SME.

    b. **Product criterion:** The exposure must take the form of any of the following: revolving credits and lines of credit (including credit cards and overdrafts); personal term loans and leases (including installment loans, auto loans and leases, student and educational loans, personal finance), residential housing loans which do not qualify for a preferential risk weight of 35%; and small business facilities and commitments.

    c. **Granularity criterion:** The maximum aggregate retail exposure limit to one SME or to any group of SMEs that can be considered as a single customer based on Circular (IBS/101/1995) and its amendments, including any past due claims, must not exceed KD 250,000. In the case of off-balance sheet exposures, the amount is taken to be the credit equivalent amount determined using the applicable credit conversion factors set out in paragraph 122.

60. The Central Bank may from time to time evaluate whether the 75% risk weight is considered too low for exposures in the regulatory retail portfolio based on the default experience in Kuwait.

61. For the purposes of this portfolio, a "small and medium sized enterprise" ("SME") is taken to mean an unlisted company or an unincorporated enterprise such as a partnership or sole proprietorship. The Central Bank of Kuwait, however, expect each licensed bank to develop their own internal identification criteria for SMEs that could include, among other things, the turnover factor, etc. Such criteria should be over and above the above conditions. Such criteria and its implementation shall be assessed by the Central Bank of Kuwait on a regular basis during the examination process. Moreover, the external auditors will be required, during their review of capital adequacy returns, to assess the reasonableness of the identification criteria through performing certain test using a sample of SMEs exposures.

62. Claims on enterprises that do not satisfy the criteria for inclusion as SMEs within the regulatory retail exposures should be treated as claims on corporate.

63. Claims on individuals that do not satisfy the criteria for inclusion as regulatory retail exposures should be treated as corporates or other exposures, whichever is applicable.

64. Residential housing loans eligible for the preferential risk weight of 75% should satisfy the following criteria:

    a) The loan is to an individual (person / individual persons) or a small business;

    b) The maximum aggregate exposure limit does not exceed KD 250,000; and

    c) The loan to value ratio does not exceed 90% at the time of loan origination.

Qualifying Residential Housing Loans (RHLs) 35%

65. RHLs are those loans granted to finance the construction or purchase of a residential house subject to a maximum limit of KD 70,000. The limit for each counterparty is calculated inclusive of consumer and instalment loans, if any. It should be noted that consumer and instalment loans should be included under "Regulatory Retail Exposures".

66. RHLs are assigned a preferential risk weight of 35% subject to satisfying the following criteria:

    a) The loan is to an individual person / individual persons, The loan is secured by a first legal charge on the residential house;

    b) The licensed bank has the legal right to foreclose on the residential house;

    c) The residential house is self-occupied by the borrower or rented; and

    d) At origination of the loan facility, the valuation of the property should be based on the lowest valuation generated from the use of three independent valuers. Such properties should thereafter be revaluated on a regular basis based on the Central Bank of Kuwait regulation on the rationalisation and organisation of banks credit policies.

67. The Central Bank of Kuwait may evaluate whether the risk weight above are considered to be too low based on default experience for these types of exposures.

Past Due Exposures

68. This portfolio should include any exposure that is more than 90 days past due or those against which specific provision has been allocated.

69. The unsecured portion of any loan (other than a qualifying residential housing loan) that is classified as past due, net of specific provisions (including partial write offs), will be risk-weighted as follows:

    a) 100% risk weight when specific provisions are less than 50% of the outstanding amount of the loan;

    b) 50% risk weight when specific provisions are no less than 50% of the outstanding amount of the loan.

    c) If past due loan is fully secured by unrecognized collaterals then 100% risk weight shall be applied.

70. Risk weights should be applied to the net amount after deducting specific provisions and after applying the eligible CRMs.

71. In case of past due qualifying residential housing loans, they will be risk weighted at 100%, net of specific provisions. But if specific provisions are no less than 20% of the outstanding amount of the loan, then the risk weight applicable to the remainder of the loan can be reduced to 50%.

Other Exposures

72. These include all exposures not specified elsewhere, other than those which are deducted in determining the capital base of the licensed bank. Such exposures are subject to a 100% risk weight, or a higher risk weight as may be specified by the Central Bank, if the asset concerned, other than those that are past due, is considered to be of higher risk.

73. Such exposures may include, but not limited to:

a) Investments in commercial entities below the materiality levels noted in paragraph 13 above.

b) Loans secured by commercial real estate.

c) Investment in banking, securities and other financial entities below 20% shareholding interest.

Fifth: Credit Risk Weighting of Securitisation Exposures:

(a) Introduction:

74. Securitisation implies creation of securities out of a pool of underlying assets, normally receivables, which are put under the legal control of the investors through a special intermediary (Special Purpose Entity or "SPE"), established for this purpose.

75. The original concept of securitization was to create securities based on financial assets, say, receivables on mortgage loans, auto loans, credit cards, etc. However, innovations have extended the application of securitized pools to cover non-financial assets such as aircraft, buildings as well. With continuous innovations, the horizon of securitization applications is constantly increasing.

76. The directives contained in these regulations are for the determination of regulatory capital according to the Standardized Approach on exposures arising from traditional securitizations only. Licensed banks are allowed to securitize assets to banks that are subject to the Central Bank of Kuwait regulations.

77. The capital treatment of a securitization exposure must be determined on the basis of its economic substance rather than form. Banks are encouraged to consult with the Central Bank of Kuwait when there is uncertainty about whether a given transaction should be considered a securitization or a specialized lending exposure.

(b) Operational requirements for traditional securitisation exposures:

78. An originating bank may exclude securitised exposures from the calculation of risk-weighted assets only if **all** of the following conditions have been met. Banks meeting these conditions must still hold regulatory capital against any securitisation exposures it retains or repurchases.

a) All credit risk associated with the securitised exposures has been transferred to third parties.

b) The transferor does not maintain effective or indirect control over the transferred exposures. The assets are legally isolated from the transferor in such a way (e.g. through the sale of assets or through sub-participation) that the exposures are put beyond the reach of the transferor and its creditors, even in bankruptcy or receivership. These conditions must be supported by an opinion provided by a qualified legal counsel.

   The transferor is deemed to have maintained effective control over the transferred credit risk exposures if it: (i) is able to repurchase from the transferee the previously transferred exposures in order to realize their benefits; or (ii) is obligated to retain the risk of the transferred exposures. The transferor's retention of servicing rights to the exposures will not necessarily constitute indirect control of the exposures.

c) The securities issued are not obligations of the transferor. Thus, investors who purchase the securities only have claim to the underlying pool of exposures.

d) The transferee is an SPE and the holders of the beneficial interests in that entity have the right to pledge or exchange them without restriction.

e) Clean-up calls must satisfy the conditions set out in paragraph 79 below.

f) The securitisation documentation does not contain clauses that:

   i. require the originating bank to alter systematically the underlying exposures such that the pool's weighted average credit quality is improved unless this is achieved by selling assets to independent and unaffiliated third parties at market prices;

   ii. allow for increases in a retained first loss position or credit enhancement provided by the originating bank after the transaction's inception; or

   iii. increase the yield payable to parties other than the originating bank, such as investors and third-party providers of credit enhancements, in response to a deterioration in the credit quality of the underlying pool.

(c) Operational requirements and treatment of clean-up calls:

79. No capital will be required for securitization transactions that include a clean-up call, if the following conditions are met:

    a) The exercise of the clean-up call is at the discretion of the originating bank. It should not be mandatory either in form or in substance.

    b) The clean-up call is not structured to avoid allocating losses to credit enhancements or positions held by investors or otherwise structured to provide credit enhancement.

    c) The clean-up call must only be exercisable when 10% or less of the original underlying portfolio or securities issued remains.

80. Securitisation transactions that include a clean-up call that does not meet all of the conditions stated above would result in a capital requirement for the originating bank. For a traditional securitisation, the underlying exposures must be treated as if they were not securitised. Additionally, banks must not recognise in regulatory capital any gain-on-sale, as defined in paragraph 85.

81. A clean up call, when exercised, if found to serve as a credit enhancement, the exercise of the clean-up call must be considered as a form of implicit support provided by the bank and must be treated in accordance with the guidance in paragraph 87.

(d) Capital requirements:

82. Banks are required to hold regulatory capital against all of their securitization exposures, including those arising from:

    a) investments in asset-backed / mortgage-backed securities;

    b) retention of a subordinated tranche;

    c) extension of a liquidity facility / cash servicer facility or credit enhancement, and

    d) the provision of credit risk mitigants/ collaterals to a securitisation transaction.

83. Repurchased securitisation exposures must be treated as retained securitisation exposures. Provisions provided for securitisation exposures and implicit support provided by a bank to securitised exposures is explained in paragraph 84 and 86 respectively.

84. When a bank is required to deduct a securitisation exposure from its regulatory capital, the deduction must be 50% from Tier (1) and 50% from Tier (2) with the one exception noted in paragraph 85. Credit enhancing I/Os (net of the amount that must be deducted from Tier (1) as in paragraph 85) are deducted 50% from Tier (1) and 50% from Tier (2). Deductions from capital may be calculated net of any specific provisions taken against the relevant securitisation exposures.

85. Banks must deduct from Tier (1) any increase in equity capital resulting from a securitisation transaction, such as that associated with expected future margin income (FMI) resulting in a gain-on-sale that is recognised in regulatory capital. Such an increase in capital is referred to as a "gain-on-sale" for the purposes of the securitisation framework.

86. When a bank provides **implicit support** to a securitisation, it must, at a minimum, hold capital against all of the exposures associated with the securitisation transaction as if they had not been securitised. Additionally, banks would not be permitted to recognise in regulatory capital any gain-on-sale, as defined in paragraph 85. Furthermore, the bank is required to disclose publicly that (a) it has provided non- contractual support and (b) the capital impact of doing so.

11- CAPITAL ADEQUACY RATIO

A) Circular No. (2/BS/184/2005) Regarding the Implementation of the Revised Capital Adequacy Ratio Basel (2).

(e) Operational requirements for use of external credit assessments:

87. The following operational criteria concerning the use of external credit assessments apply in the Standardised approach of the securitization framework:

    a. To be eligible for risk-weighting purposes, the external credit assessment must take into account and reflect the entire amount of credit risk exposure the bank has with regard to all payments owed to it. For example, if a bank is owed both principal and interest, the assessment must fully take into account and reflect the credit risk associated with timely repayment of both principal and interest.

    b. The external credit assessments must be from an eligible ECAI as recognised by the Central Bank of Kuwait in accordance with Annexure (B) with the following exception. In contrast to Annexure (B), 3.c, an eligible credit assessment must be publicly available. In other words, a rating must be published in an accessible form and included in the ECAI's transition matrix. Consequently, ratings that are made available only to the parties to a transaction do not satisfy this requirement.

    c. Eligible ECAIs must have a demonstrated expertise in assessing securitisations, which may be evidenced by strong market acceptance.

    d. A bank must apply external credit assessments from eligible ECAIs consistently across a given type of securitisation exposure. Furthermore, a bank cannot use the credit assessments issued by one ECAI for one or more tranches and those of another ECAI for other positions (whether retained or purchased) within the same securitisation structure that may or may not be rated by the first ECAI. Where two or more eligible ECAIs can be used and these assess the credit risk of the same securitisation exposure differently, Annexure (B), 3.9 and 3.10 will apply.

    e. Where CRM is provided directly to an SPE by an eligible guarantor defined in paragraph 280 and is reflected in the external credit assessment assigned to a securitisation exposure(s), the risk weight associated with that external credit assessment should be used. In order to avoid any double counting, no additional capital recognition is permitted. If the CRM provider is not recognised as an eligible guarantor, the covered securitisation exposures should be treated as unrated.

f. In the situation where a credit risk mitigant is not obtained by the SPE but rather applied to a specific securitisation exposure within a given structure (e.g. ABS tranche), the bank must treat the exposure as if it is unrated and then use the CRM treatment outlined in the Credit Risk Mitigation section of these regulations to recognise the hedge.

(f) Standardised approach for securitisation exposures (Treatment for investing and originating banks):

88. For purposes of regulatory capital requirement, risk-weighted asset amount for a securitisation exposure (exposure on the securities issued based on the underlying pool of securitised assets) is given as:

RWA = amount of securitisation exposure × risk weight

89. With respect to off-balance sheet exposures for risk-based capital purposes, banks must determine whether, according to the criteria outlined below, an off-balance sheet securitisation exposure qualifies as an 'eligible liquidity facility' or an 'eligible servicer cash advance facility'. All other off-balance sheet securitisation exposures will receive a 100% CCF. Then apply the applicable risk weight to the resultant credit equivalent amount.

90. For eligible liquidity facility as defined in paragraph (94) below and where the conditions for use of external credit assessments in paragraph (87) are not met, the risk weight applied to bank exposure's on-balance sheet credit equivalent amount is equal to the highest risk weight assigned to any of the underlying individual exposures covered by the facility.

91. The applicable risk weights for long and short term rating category are provided below and detailed in Annexure (I) & (J).

Long-term rating category

Credit Quality Grades	**1**	**2**	**3**	**4**	**5 & 6 or unrated**
Risk Weight (for investing banks)	20%	50%	100%	350%	Deduction from Capital
Risk Weight (for originating banks)	20%	50%	100%	Deduction from Capital	Deduction from Capital

Short-tem rating category

Credit Quality Grades	**1**	**2**	**3**	**4 or unrated**
Risk Weight	20%	50%	100%	Deduction from Capital

(g) Exceptions to deduction from capital for unrated securitization exposures:

92. As noted in the tables above, unrated securitisation exposures must be deducted with the following exceptions:

    a. A bank that holds or guarantees an *unrated securitization exposure* that is the most senior exposure in a traditional securitization, may determine the risk weight by applying the 'look-through' treatment as described below, provided the composition of the underlying pool is known at all times and it is able to determine the risk weights assigned to the underlying exposures. Banks are not required to consider interest rate or currency swaps when determining whether an exposure is the most senior in a securitization for the purpose of applying the 'look-through' treatment.

       In the look-through treatment, the unrated most senior position receives the average risk weight of the underlying exposures. Where the bank is unable to determine the risk weights assigned to the underlying credit risk exposure, the unrated position must be deducted.

    b. A bank that is an ABCP programme sponsor and holds an unrated securitization exposure to the ABCP programme is not required to deduct the unrated securitization exposure if the following conditions are satisfied:

       i. The securitization exposure is economically in a second loss or better and the first loss position provides significant credit protection to the second loss position.

       ii. The associated credit risk is the equivalent of investment grade (BBB) or better.

       iii. The bank holding the unrated securitization exposure does not retain or provide the first loss position.

       Where the above conditions are satisfied, the risk weight is greater of (a) 100% or (b) the highest risk weight assigned to any of the underlying individual exposures covered by the facility / exposures under the credit enhancement.

    c. Eligible liquidity facilities.

(h) Treatment of eligible liquidity facilities:

93. For risk based capital purposes, banks must determine if an off-balance sheet securitization exposure qualifies as an ‘eligible liquidity facility’ or an ‘eligible cash servicer cash advance facility’ as defined in paragraphs 94 and 97 below.

94. A bank may treat an off-balance sheet securitization exposure as an eligible liquidity facility if the following requirements are satisfied:

    a. The facility documentation clearly identifies the nature, purpose and extent of any undertaking or commitment provided to the SPE, which shall help to smooth the timing differences faced by the SPE between the receipt of cash flows connected with the underlying pool of exposures and the payments to be made to investors;

    b. The facility shall be limited to a specified amount and duration, unless the bank is able to withdraw, at its absolute discretion, the facility at any time with a reasonable period of notice;

    c. The facility is documented in a way which clearly separates it from any other facility provided by the bank;

    d. The facility documentation shall clearly identify and limit the circumstances under which it may be drawn.

    e. Any draws made under the facility shall be for the SPE and not for direct payments to investors, and be limited to the amount that is likely to be repaid fully from the liquidation of the underlying exposures and any seller- provided credit enhancements.

    f. The facility shall not cover any losses incurred in the underlying pool of exposures prior to a draw, or be structured such that draw-down is certain (as indicated by regular or continuous draws or continuous revolving funding);

    g. The facility shall be subject to an asset quality test that precludes it from being drawn to cover credit risk exposures that are classified substandard or worse;

    h. If the exposures that a liquidity facility is required to fund are externally rated securities, the facility can only be used to fund securities that are externally rated investment grade at the time of funding;

i. The facility shall not be drawn after all applicable (e.g. transaction-specific and programme-wide) credit enhancements from which the liquidity facility would benefit have been exhausted;

j. If the facility is provided to an ABCP programme, repayment of draws on the facility shall not be subordinated to any interests of any note holder in the programme or subject to deferral or waiver.

95. Where the above conditions are met, the bank may apply a 20% CCF to the amount of eligible liquidity facility if the facility has an original maturity of one year or less, or a 50% CCF if the facility has an original maturity of more than one year. However, if an external rating of the facility itself is used for risk weighting the facility, a 100% CCF must be applied.

96. In the event of a general market disruption, a 0% CCF may be applied to eligible liquidity facilities (provided the eligible liquidity facilities satisfy conditions as per paragraph 94). Additionally the funds advanced by the bank to pay investors of the securitisation, must be secured by the underlying pools of assets and must rank at least pari passu with the claims of the investors.

(i) Treatment of eligible servicer cash advance facilities:

97. If contractually provided for, servicers may advance cash to ensure an uninterrupted flow of payments to investors so long as the servicer is entitled to full reimbursement and this right is senior to other claims on cash flows from the underlying pool of exposures. Such undrawn servicer cash advances or facilities that are unconditionally cancellable without prior notice should be eligible for a 0% CCF.

(j) Treatment of credit risk mitigation (CRM) for securitization exposures:

98. The treatment below applies to a bank that has obtained a credit risk mitigant on a securitisation exposure. Credit risk mitigants include guarantees, collateral and on-balance sheet netting. Collateral in this context refers to that used to hedge the credit risk of a securitisation exposure rather than the underlying exposures of the securitization transaction.

99. When a credit risk mitigants is provided directly to an SPE by an eligible guarantor as defined in paragraph 280 and is reflected in the external credit assessment assigned to a securitisation exposure(s), the risk weight for the securitisation exposure, associated with the external credit assessment should be used. If the CRM provider is not recognized as an eligible guarantor, the securitisation exposures should be considered as unrated and treated accordingly.

100. When a CRM is not obtained by the SPE but rather applied to a specific securitisation exposure, the bank must treat the exposure as if it is unrated and for calculating the actual amount of exposure (taking CRM effect into account), should use the CRM treatment as underlined under the Credit Risk Mitigation section of these regulations.

101. Eligible collateral applied to securitisation exposures is limited to that recognised under paragraph 255. Collateral pledged by SPEs may be recognised.

102. Guarantees provided by the entities listed in paragraph 280 may be recognized. SPEs cannot be recognised as eligible guarantors.

103. Where guarantees fulfil the minimum operational conditions as specified in paragraph 273, banks can take account of such credit protection in calculating capital requirements for securitisation exposures.

104. Capital requirements for the guaranteed portion will be calculated according to paragraphs 274 to 279.

105. For the purpose of setting regulatory capital against a **maturity mismatch**, the capital requirement will be determined in accordance with paragraphs 283 to 286. When the exposures being hedged have different maturities, the longest maturity must be used.

(k) Treatment for early amortisation provisions (for originating banks):

106. An originating bank is required to hold capital against all or a portion of the investors interest (i.e. against both the drawn and undrawn balances related to the securitised exposures) when:

   a. It sells exposures into a structure that contains an early amortisation feature; and

   b. The exposures sold are of a revolving nature. These involve exposures where the borrower is permitted to vary the drawn amount and repayments within an agreed limit under a line of credit (e.g. credit card receivables and corporate loan commitments).

107. The capital requirement should reflect the type of mechanism through which an early amortisation is triggered.

108. For securitisation structures wherein the underlying pool comprises revolving and term exposures, a bank must apply the relevant early amortisation treatment as outlined in paragraph 109 to 113 to that portion of the underlying pool containing revolving exposures.

109. For a bank subject to the early amortisation treatment, the total capital charge for all of its positions will be subject to a maximum capital requirement (i.e. a 'cap') equal to the greater of (i) that required for retained securitisation exposures, or (ii) the capital requirement that would apply had the exposures not been securitised. In addition, banks must deduct the entire amount of any gain-on-sale and credit enhancing I/Os arising from the securitization transaction in accordance with paragraphs 84 and 85 .

110. The originator's capital charge for the investors interest is determined as the product of (a) the investors interest, (b) the appropriate CCF (as discussed below), and (c) the risk weight appropriate to the underlying exposure type, as if the exposures had not been securitised.

111. As described below, the CCFs depend upon whether the early amortization repays investors through a controlled or non-controlled mechanism. They also differ according to whether the securitised exposures are uncommitted retail credit lines (e.g. credit card receivables) or other credit lines (e.g. revolving corporate facilities). A line is considered uncommitted if it is unconditionally cancellable without prior notice.

(l) Determination of CCFs for controlled early amortisation features (for originating banks):

112. An early amortisation feature is considered controlled when the definition as specified in annexure (A) paragraph 22 is satisfied.

a. Uncommitted retail exposures:

i. For uncommitted retail credit lines (e.g. credit card receivables) in securitizations containing controlled early amortisation features, banks must compare the three- month average excess spread defined in annexure (A) paragraph 24 to the point at which the bank is required to trap excess spread as economically required by the structure (i.e. excess spread trapping point).

ii. In cases where such a transaction does not require excess spread to be trapped, the trapping point is deemed to be 4.5 percentage points.

iii. The bank must divide the excess spread level by the transaction's excess spread trapping point to determine the appropriate segments and apply the corresponding conversion factors, as outlined in the following table.

iv. Banks are required to apply the conversion factors set out below for controlled mechanisms to the investors interest referred to in paragraph 110.

b. All other securitized revolving exposures (those that are committed and are non-retail) with controlled amortization features will be subject to a CCF of 90% against the off-balance sheet exposures.

Controlled early amortization features

	Uncommitted	**Committed**
Retail Credit Lines	**3-month average excess spread Credit Conversion Factor (CCF)**	90% CCF
	133.33% of trapping point or more is eligible for 0% CCF	
	Less than 133.33% to 100% of trapping point is eligible for 1% CCF	
	Less than 100% to 75% of trapping point is eligible for 2% CCF	
	Less than 75% to 50% of trapping point is eligible for 10% CCF	
	Less than 50% to 25% of trapping point is eligible for 20% CCF	
Non-retail credit lines	90% CCF	90% CCF

(m) Determination of CCFs for non-controlled early amortisation features (for originating banks):

113. Early amortisation features that do not satisfy the definition of a controlled early amortisation as specified in annexure (A) paragraph 22 will be considered non-controlled and created as follows.

a. Uncommitted retail exposures:

i. For uncommitted retail credit lines (e.g. credit card receivables) in securitizations containing non-controlled early amortisation features, banks must make the comparison described in paragraph 112.a.i and 112.a.ii .

ii. The bank must divide the excess spread level by the transaction's excess spread trapping point to determine the appropriate segments and apply the corresponding conversion factors, as outlined in the following table.

b. All other securitised revolving exposures (i.e. those that are committed and all non-retail exposures) with non-controlled early amortisation features will be subject to a CCF of 100% against the off-balance sheet exposures.

Non-controlled early amortization features

	Uncommitted	**Committed**
Retail Credit Lines	**3-month average excess spread Credit Conversion Factor (CCF)**	90% CCF
	133.33% of trapping point or more is eligible for 0% CCF	
	Less than 133.33% to 100% of trapping point is eligible for 5% CCF	
	Less than 100% to 75% of trapping point is eligible for 15% CCF	
	Less than 75% to 50% of trapping point is eligible for 50% CCF	
	Less than 50% of trapping point is eligible for 100% CCF	
Non-retail credit lines	100% CCF	100% CCF

Sixth: Credit Risk Weighting of Off-balance Sheet Exposures:

114. This section sets out the treatment of off-balance sheet items and their applicable conversion factors for contingent items and add-on factors for derivatives for the purpose of determining the risk weighted amount.

(a) Calculation of credit risk-weighted amount for off-balance sheet items:

115. For each off-balance sheet exposure, other than derivatives, the weighted amount is calculated based on the **Credit Equivalent Amount** of the exposure, which is determined by applying a percentage to those obligations that will vary according to the nature of the obligation. Such a percentage is known as the **"Credit Conversion Factor" (CCF).**

116. The Credit Equivalent Amount is then multiplied by the applicable risk weight of the original obligor in the same way as in on-balance sheet exposures to arrive at the weighted amount for the exposure.

117. For derivative contracts, licensed banks shall first calculate the **Replacement Cost** by marking the contract to market. The licensed bank shall then adjust the notional amount by a factor **(the "Add-on Factor")** to reflect the potential future exposure over the remaining life of the contract. Add-on factors are listed below in paragraph 123. This amount is then added to the replacement cost calculated above. The resultant amount shall then be multiplied by applicable risk weight of the original obligor in the same way as in on-balance sheet exposures to arrive at the weighted amount for the exposure.

118. For exposures covered by eligible CRM techniques, the weighted amount can be reduced based on the treatments described in the Credit Risk Mitigation section below.

First-to-default credit derivatives:

119. There are cases where licensed banks provide credit protection for a basket of assets and the underlying contract specifically states that the first default among the assets triggers the credit protection. This kind of protection is defined as a first to default credit derivative. The credit exposure to the protection provider is equal to the notional amount of the credit derivative. For banks providing credit protection through such an instrument, if the product (in this case the basket of assets) has an external credit assessment from an eligible credit assessment institution, the risk weighted asset will be calculated by first applying a credit conversion factor (CCF) of 100 % to the credit derivative amount and then applying the relevant risk weights to the credit asset equivalent based on credit quality grades related to the exposures. The risk weights will be applied based on the following credit quality grades:

Long-term rating category

Credit Quality Grades	**1**	**2**	**3**	**4**	**5 & 6**
Risk Weights	20%	50%	100%	350%	Deduction

Short-term rating category

Credit Quality Grades	**1**	**2**	**3**	**4**
Risk Weights	20%	50%	100%	350%

120. However, if the product is not rated by an eligible external credit assessment institution, the risk weighted asset will be calculated as follows:

a) Aggregate the risk weights of all the assets included in the basket (aggregation up to a maximum of 833% is allowed), and

b) Multiply the aggregated risk weights with the notional amount of the protection provided by the credit derivative and apply a CCF of 100% on the resultant to obtain the risk weighted asset amount.

Second-to-default credit derivatives:

121. For banks providing credit protection through a second-to-default credit derivative, the capital treatment is the same as in paragraphs 119 and 120 above with one exception. The exception is that, in aggregating the risk weights, the asset with the lowest risk weighted amount can be excluded from the calculation.

11- CAPITAL ADEQUACY RATIO
A) Circular No. (2/BS/184/2005) Regarding the Implementation of the Revised Capital Adequacy Ratio Basel (2).

(b) Credit conversion factors for off-balance sheet items:

122. The following list gives the CCFs for individual types of off-balance sheet exposures, other than derivatives:

Particulars	CCF %
Commitments which can be cancelled at any time: These are unconditionally cancellable at any time by the licensed bank without prior notice other than for "force majeure" reasons, or that effectively provide for automatic cancellation due to deterioration in a borrower's creditworthiness.	0
Trade-related contingencies: These include liabilities arising from issuing and confirming letters of credit arising from the movement of goods (e.g. documentary LC's collateralized by the underlying shipments), acceptances on trade bills, shipping guarantees issued, trade-related revolving/ standby letters of credit and any other trade related contingencies.	20
Commitments representing the undrawn portion of any binding arrangements with an original maturity of up to one year or less.	20
Commitments representing the undrawn portion of any binding arrangements with an original maturity of over one year.	50
Transaction-related contingencies: These include performance bonds, bid bonds, warranties, and standby letters of credit related to particular transactions.	50
Note issuance and revolving underwriting facilities: These are arrangements whereby a borrower may draw down funds up to a prescribed limit over a predefined period by making repeated note issues to the market, and where, should the issue prove unable to be placed in the market, the unplaced amount is to be taken up or funds made available by the underwriter of the facility.	50
Direct credit substitutes: These include guarantees, acceptances and standby letters of credit serving as financial guarantees for loans. This item also includes exposure arising from the selling of credit derivatives (credit default swap and total return swap), i.e., where a licensed bank is acting as the protection seller.	100

Particulars	CCF %
Asset sales or other transactions with recourse: These refer to transactions of asset sales where the credit risk of the assets sold remains with the licensed bank, as the holder of the asset is entitled to put the asset back to the licensed bank within an agreed period or under certain prescribed circumstances. This item also includes Repurchase Agreements, which are not included in the on-balance-sheet items, where the credit risk remains with the bank.	100
Forward asset purchases: These refer to commitments to purchase at a specified future date and on prearranged terms, a loan, security or other asset from another party including commitments to repurchase securities in repo-style transactions (i.e. repo of securities where the terms of the agreement are such that all risks and rewards of ownership are substantially transferred to the counterparty).	100
Partly paid shares and securities: These refer to the unpaid portion of partly-paid shares or securities which the issuer may call upon the bank to pay at a predetermined or unspecified date in the future.	100
Forward deposits placed: These refer to any agreement between the licensed bank and another party whereby the licensed bank will place a deposit at an agreed rate of interest with that party at a predetermined future date.	100

(c) Add-on factors for derivatives contracts:

123. The following list gives the add-on factors for foreign exchange, gold and interest rate contracts:

Foreign exchange contracts: These include cross-currency interest rate swaps, forward foreign exchange contracts, currency futures, currency options purchased, gold contracts and similar instruments bearing credit risk. The add-on factor for such contracts shall be determined based on residual maturity as follows:

1 year or less	1.0%
Over 1 year to 5 years	5.0%
Over 5 years	7.5%

11- CAPITAL ADEQUACY RATIO
A) Circular No. (2/BS/184/2005) Regarding the Implementation of the Revised Capital Adequacy Ratio Basel (2).

Interest rate contracts: They include single currency interest rate swaps; forward interest rate agreements; all types of interest rate options purchased, and similar instruments involving credit risk. The add-on factors for such contracts shall be determined based on residual maturity as follows:

1 year or less	Nil
Over 1 year to 5 years	0.5%
Over 5 years	1.5%

Seventh: Treatment of Credit Risk Weighted Amount for Repo-style Transactions:

124. The capital treatment of repo-style transactions (repos and reverse repos of securities) in the banking book depends mainly on whether there is any substantial transfer of risk and rewards of ownership to the counterparty.

125. Where all risks and rewards of ownership are substantially transferred to the counterparty, the following treatment shall apply:

a) The securities sold under the repo agreement should be treated as an off-balance sheet commitment to repurchase with a capital requirement provided for the credit risk to the issuer of the securities.

b) Securities purchased (reverse repo transaction) should be treated as an asset with a capital requirement provided for the credit risk to the issuer of the securities

126. Where there is **no substantial transfer** of all risks and rewards of ownership to the counterparty, the following treatment shall apply:

a) The securities sold under the repo agreement should be treated as an asset with a capital requirement provided for the credit risk to the issuer of the securities.

b) A reverse repo transaction should be treated as collateralised lending with a capital requirement provided for the credit risk to the counterparty, but shall be mitigated through applying the general capital rules for CRM treatment of collateralised transactions.

127. For securities borrowing and lending, the capital treatment will be as follows:

   a) For securities borrowing, the capital treatment depends on whether the collateral is cash or other securities.

      1- If the collateral is cash, the exposure should be treated as a collateralised loan to the counterparty. If the securities borrowed qualify as eligible collateral, the rules for CRM treatment of collateralised transactions shall apply.

      2- If the collateral is securities, it should be treated as an asset with a capital requirement provided for the credit risk to the issuer of the securities.

   b) Securities lent should continue to be treated as an asset with a capital requirement provided for the credit risk to the issuer of the securities.

Eighth: Market Risk Weighted Exposures:

(a) General requirements:

128. This section sets out the weighting framework to be adopted by licensed banks to quantify their market risk for calculating the capital adequacy ratio under both the Standardised and the Internal Model Approaches developed by the Basel Committee on Banking Supervision.

129. Licensed banks must use the standardised approach in determining the capital required for market risk. Any licensed bank intending to use an internal model approach should apply to the Central Bank for prior approval.

(b) Definition of trading book:

130. A trading book consists of positions in financial instruments and commodities held either with trading intent or in order to hedge other elements of the trading book. To be eligible for trading book capital treatment, financial instruments must either be free of any restrictive covenants on their tradability or able to be hedged completely. In addition, positions should be frequently and accurately valued, and the portfolio should be actively managed.

131. A financial instrument is any contract that gives rise to both a financial asset of one entity and a financial liability or equity instrument of another entity. Financial instruments include both primary financial instruments (or cash instruments) and derivative financial instruments. A financial asset is any asset that is cash, the right to receive cash or another financial asset; or the contractual right to exchange financial assets on potentially favourable terms, or an equity instrument. A financial liability is the contractual obligation to deliver cash or another financial asset or to exchange financial liabilities under conditions that are potentially unfavourable.

132. Positions held with trading intent are those held intentionally for short-term resale and/or with the intent of benefiting from actual or expected short-term price movements or to lock in arbitrage profits, and may include for example proprietary positions, positions arising from client servicing (e.g. matched principal broking) and market making.

133. The following will be the basic requirements for positions eligible to receive trading book capital treatment:

a) Clearly documented trading strategy for the position/instrument or portfolios, approved by senior management (which would include expected holding horizon).

b) Clearly defined policies and procedures for the active management of the position, which must include:

1- Positions are managed on a trading desk;

2- Position limits are set and monitored for appropriateness;

3- Dealers have the autonomy to enter into/manage the position within agreed limits and according to the agreed strategy;

4- Positions are marked to market at least daily and when marking to model the parameters must be assessed on a daily basis;

5- Positions are reported to senior management as an integral part of the bank's risk management process; and

6- Positions are actively monitored with reference to market information sources (assessment should be made of the market liquidity or the ability to hedge positions or the portfolio risk profiles). This would include assessing the quality and availability of market inputs to the valuation process, level of market turnover, sizes of positions traded in the market, etc.

c) Clearly defined policy and procedures to monitor the positions against the bank's trading strategy including the monitoring of turnover and stale positions in the bank's trading book.

134. A hedge is a position that materially or entirely offsets the component risk elements of another trading book position or portfolio.

(c) Scope and coverage of capital charges for market risk:

135. The risks subject to capital charges for market risk shall include the following:

a) Interest rate position risk relating to instruments in the trading book.
b) Equity position risk relating to instruments in the trading book.
c) Foreign exchange risk throughout the bank.
d) Commodities risk throughout the bank.
e) Options.

136. The capital charges for interest rate related instruments and equities will apply to the market value of items in bank's trading books. The capital charges for foreign exchange risk and commodities risk will apply to banks total currency and commodity positions.(trading books and banking books).

137. Positions and exposures that are not in the trading book are deemed to be in the banking (non-trading) book. Banks should have an established written policy for allocating transactions to the trading or non-trading (i.e. banking) book as well as procedures to ensure compliance with such policy. A copy of such instructions should be submitted to the Central Bank of Kuwait along with the first return.

138. Total market risk weighted exposures are determined by multiplying the market risk capital charge, calculated based on these regulations, by 8.33 (i.e. the reciprocal of the minimum capital ratio of 12%) and adding the resulting figure to the sum of credit and operational risk weighted assets to yield the total risk weighted exposures which will then be used to calculate the capital adequacy ratio (CAR).

139. Banks should document the rationale and procedures for determining when positions should be netted and not netted. (credit risk mitigation).

(d) Valuation requirements:

140. A framework for prudent valuation practices should at a minimum include robust systems and controls; proper valuation methodologies and valuation adjustments or reserves

a) Systems and controls:

141. All licensed banks must establish and maintain adequate systems and controls sufficient to give management and the Central Bank the confidence that their valuation estimates are prudent and reliable.

142. These systems must be integrated with other risk management systems within the bank (such as credit analysis). Such systems must include:

    a. Documented policies and procedures for the process of valuation. This includes clearly defined responsibilities of the various areas involved in the determination of the valuation, sources of market information and review of their appropriateness, frequency of independent valuation, timing of closing prices, procedures for adjusting valuations, end of the month and ad-hoc verification procedures; and

    b. Clear and independent (i.e. independent of front office) reporting lines for the department accountable for the valuation process. The reporting line should ultimately be to the chief executive of the licensed bank.

b) Valuation methodologies:

143. **Marking-to-market** is at least the daily valuation of positions at readily available close out prices that are sourced independently. Examples of readily available close out prices include exchange prices, screen prices, or quotes from several independent reputable brokers.

144. Licensed banks must mark-to-market as much as possible. The more prudent side of bid/offer must be used unless the bank is a significant market maker in a particular position type and it can close out at mid-market.

145. Where marking-to-market is not possible, licensed banks may ***mark-to-model***, where this can be demonstrated to be prudent. Marking-to-model is defined as any valuation which has to be benchmarked, extrapolated or otherwise calculated from a market input. When marking to model, an extra degree of conservatism is appropriate. The Central Bank of Kuwait will consider the following in assessing whether a mark-to-model valuation is prudent:

a. Senior management should be aware of the elements of the trading book which are subject to mark to model and should understand the materiality of the uncertainty this creates in the reporting of the risk/performance of the business.

b. Market inputs should be sourced, to the extent possible, in line with market prices (as discussed above). The appropriateness of the market inputs for the particular position being valued should be reviewed regularly.

c. Where available, generally accepted valuation methodologies for particular products should be used as far as possible.

d. Where the model is developed by the licensed bank itself, it should be based on appropriate assumptions, which have been assessed and challenged by suitably qualified parties independent of the development process. The model should be developed or approved independently of the front office. It should be independently tested. This includes validating the mathematics, the assumptions and the software implementation.

e. There should be formal change control procedures in place and a secure copy of the model should be held and periodically used to check valuations.

f. Risk management unit should be aware of the weaknesses of the models used and how best to reflect those in the valuation output.

g. The model should be subject to periodic review to determine the accuracy of its performance (e.g. assessing continued appropriateness of the assumptions, analysis of P&L versus risk factors, comparison of actual close out values to model outputs).

h. Valuation adjustments should be made as appropriate, for example, to cover the uncertainty of the model valuation (see also valuation adjustments below).

146. Independent price verification is distinct from daily mark-to-market. It is the process by which market prices or model inputs are regularly verified for accuracy. While daily marking-to-market may be performed by dealers, verification of market prices or model inputs should be performed by a unit independent of the dealing room, at least monthly (or, depending on the nature of the market/trading activity, more frequently). It needs not be performed as frequently as daily mark-to-market, since the objective, i.e. independent, marking of positions, should reveal any error or bias in pricing, which should result in the elimination of inaccurate daily marks.

147. Independent price verification entails a higher standard of accuracy in that the market prices or model inputs are used to determine profit and loss figures, whereas daily marks are used primarily for management reporting in between reporting dates. For independent price verification, where pricing sources are more subjective, e.g. only one available broker quote, prudent measures such as valuation adjustments may be appropriate.

3) Valuation adjustments or reserves:

148. Banks must establish and maintain procedures for considering valuation adjustments/reserves. The Central Bank of Kuwait expects banks using third-party valuations to consider whether valuation adjustments are necessary. Such considerations are also necessary when marking to model.

149. The Central Bank of Kuwait expects the following valuation adjustments/reserves to be formally considered at a minimum: unearned credit spreads, close-out costs, operational risks, early termination, investing and funding costs, and future administrative costs and, where appropriate, model risk.

150. In addition, the Central Bank of Kuwait will require banks to consider the need for establishing reserves for less liquid positions (and on an ongoing basis review their continued appropriateness). Reduced liquidity could arise from market events. Additionally, close-out prices for concentrated positions and/or stale positions are more likely to be adverse. Banks must consider several factors when determining whether a valuation reserve is necessary for less liquid items. These factors include the amount of time it would take to hedge out the position/risks within the position, the average volatility of bid/offer spreads, the availability of market quotes (number and identity of market makers) and the average and volatility of trading volumes.

(e) Standardized Approach:

151. The standardized methodology uses a “building-block” approach. Under this approach the capital charge is determined separately for specific risk and general risk.

152. Specific risk is defined as the risk of loss caused by an adverse price movement of a debt instruments or securities due principally to factors related to the issuer.

153. General market risk is defined as the risk of loss arising from adverse changes in market prices.

154. The capital charge for market risk under the standardised approach is the sum of capital required to cover the following:

a. Interest rate risk;
b. Equity position risk;
c. Foreign exchange risk;
d. Commodities risk; and
e. Option risk.

1) Interest rate risk

155. The capital requirement for interest rate risk should be calculated in accordance with these regulations for all interest rate positions held in the trading book except for interest rate options. The instruments covered by interest rate position risk include, but are not limited to, the following:

a. Bonds.
b. Debentures.
c. Certificates of deposits.
d. Treasury bills.
e. Floating rate notes.

156. The capital charge for interest rate risk is the sum of the capital required for specific risk and general risk.

Specific market risk

157. The specific market risk charge applies to all on-and-off balance sheet trading book interest rate positions except for derivative contracts that are not based on an underlying instrument. For example, where an interest rate swap is based on an interest rate index (e.g. LIBOR), there will not be a specific risk charge. However, a futures contract based on a corporate bond will generate a specific risk charge.

158. In measuring specific risk charge, long positions can be netted only if they satisfy the conditions set out in paragraph 175.

159. The specific risk charge for on-balance sheet interest rate positions, whether long or short, is calculated by multiplying the market value of the debt positions by the specific risk factors in Table (A) below that correspond to the category and residual term of the debt instrument.

Table (A)

Category of Debt Instruments	Credit Quality Grades	Residual Term to Maturity	Risk Factor (%)
i) Government Debt instruments	1, including those denominated and funded in the domestic currency	N/A	0.00
	2 and 3	6 months or less	0.25
		Over 6 to 24 months	1.00
		Over 24 months	1.60
	4, 5 and 6	N/A	8.00
ii) Fully Guaranteed Debt Instruments issued by Public Sector Enterprises (Qualifying)		6 months or less	0.25
		Over 6 to 24 months	1.00
		Over 24 months	1.60
iii) Other Debt instruments		N/A	8.00
Note: In respect of the above table and all other tables set out in these regulations, the period of one month should be regarded as comprising of 30 days.			

160. Government debt instruments include all forms of debt instruments, including but not limited to bonds, treasury bills and other short-term instruments issued by, fully guaranteed by, or fully collateralised by central governments of the OECD-based group of countries, and GCC countries whose debts are, by virtue of their enabling legislation, direct obligations of the parent government.

161. Fully guaranteed debt instruments issued by public sector institutions (qualifying) include debt securities:

a. Issued by, or fully guaranteed by, OECD or GCC public sector entities treated as sovereign, including Kuwaiti public sector entities.

b. Issued by, or fully guaranteed by, a MDB that fulfil the eligibility criteria provided in paragraph (49) above.

c. Issued by, or fully guaranteed by, Kuwaiti banks or OECD or GCC banks where the instrument does not qualify as capital of the issuing bank.

d. Rated investment-grade by at least two of the following ECAIs:

i. Moody’s Investor Service (Moody's).
ii. Standard & Poors (S&P).
iii. Fitch IBCA.

162. The specific risk charges for derivative contracts is calculated by multiplying the market value of the effective notional amount of the debt instrument that underlies an interest rate swap, future or forward by the specific risk factors in Table (A) above that correspond to the category and residual term of the underlying debt instrument.

General market risk

163. The general market risk applies to all on-and-off balance sheet trading book interest rate positions.

164. A bank should measure its exposure to general market risk using either the simplified method or the maturity method.

165. Banks should note that since the simplified method is less precise than the maturity method, the capital requirement generated by the application of the simplified method would be higher than that which would result from applying the maturity method.

Simplified method for interest rate risk

166. The general market risk charge under the simplified method should be calculated as follows:

a. First distribute the long or short position at current market value of each debt instrument and other source of interest rate exposure, including derivatives, into the time bands and three zones of the maturity ladder outlined in Table (B) below.

b. A separate maturity ladder must be constructed for each currency in which a bank has significant positions (KD 30,000 or more), and capital requirements must be calculated for each currency separately. Offsetting of positions shall not be permitted between different currencies in which positions are significant (KD 30,000 or more).

c. Positions in currencies that are not significant (less than KD 30,000) may be combined into a common maturity ladder, with the net long or short position of each currency entered in the applicable time band.

d. Opposite positions of the same amount in the same issues (but not different issues by the same issuer), whether actual or notional, may be excluded from the interest rate maturity framework. Banks may also exclude closely matched swaps, forwards, futures and forward rate agreements (FRAs) that meet the conditions set out in paragraph (175) on netting.

e. Once all long and short positions are placed into the appropriate time-bands, the long and short positions in each time-band are summed. The summed positions are multiplied by the appropriate risk-weight factor in table (B) which reflecting price sensitivity of the positions to changes in interest rates to determine the risk-weighted figures which are summed to give capital requirement for general market risk.

Table (B)
Zones, Time-bands and Weights

Zone	Time-bands For Coupons 3% or more	Time-bands For Coupons less than 3% and zero coupon bonds	Risk Weight (%)
1	Up to 1 month	Up to 1 month	0.00
	Over 1 month up to 3 months	Over 1 month up to 3 months	0.20
	Over 3 months up to 6 months	Over 3 months up to 6 months	0.40
	Over 6 months up to 12 months	Over 6 months up to 12 months	0.70
2	Over 1 year up to 2 years	Over 1 year up to 1.9 years	1.25
	Over 2 years up to 3 years	Over 1.9 years up to 2.8 years	1.75
	Over 3 years up to 4 years	Over 2.8 years up to 3.6 years	2.25
3	Over 4 years up to 5 years	Over 3.6 years up to 4.3 years	2.75
	Over 5 years up to 7 years	Over 4.3 years up to 5.7 years	3.25
	Over 7 years up to 10 years	Over 5.7 years up to 7.3 years	3.75
	Over 10 years up to 15 years	Over 7.3 years up to 9.3 years	4.50
	Over 15 years up to 20 years	Over 9.3 years up to 10.6 years	5.25
	Over 20 years	Over 10.6 years up to 12 years	6.00
		Over 12 years up to 20 years	8.00
		Over 20 years	12.50

167. An illustration of the calculation of general market risk under the simplified method is set out in example (2) of annex (K).

Maturity method for interest rate risk

168. To calculate capital requirement for general market risk charge under maturity method, the bank should first construct a maturity ladder for each currency and allocate all long and short positions (at market value) into the time-bands and zones outlined in Table (B) above in the same way as described above in the simplified method.

169. The capital requirement for general market risk under the maturity method is the sum of:

a. Basis risk charge.
b. Yield curve risk charge; and
c. Net position charge.

170. The capital requirement for basis risk charge is the sum of matched weighted position in all time bands × 10%. The basis risk charges for each time band should be absolute values, that is, neither long nor short. The charges for all time-bands in the maturity ladder should be summed and included as an element of the general market risk capital requirement.

171. The capital requirement for yield curve risk charge is sum of the following:

   a. Matched weighted positions in zone (1) × 40%
   b. Matched weighted positions in zone (2) × 30%
   c. Matched weighted positions in zone (3) × 30%
   d. Matched weighted positions between zones (1) and (2) × 40%
   e. Matched weighted positions between zones (2) and (3) × 40%
   f. Matched weighted positions between zones (1) and (3) × 100%.

172. Capital requirements, referred to as the yield curve risk charge, are assessed to allow for the imperfect correlation of interest rates along the yield curve. There are two elements to the capital requirement for yield curve risk charge:

   a. The first element is a charge on the matched weighted position in zones (1), (2) and (3).

   b. The second element is a capital charge on the matched weighted positions between zones.

173. The capital requirement for net position charge is residual unmatched weighted positions × 100%. The net position charge for a currency is the absolute value of the sum of the weighted net open positions in each time band.

174. An illustration of the calculation of general market risk under the maturity method is set out in example (3) of annex (K).

175. Netting of long and short positions is permitted for positions in identical issues. Instruments will be considered to be identical where the issuer is the same, they have the equivalent ranking in liquidation, and the currency, the coupon, and the maturity are the same.

2) Equities risk

176. The capital requirement for equities risk applies to all equity positions in the trading book excluding options. The instruments covered include, but are not limited to the following:

   a. Ordinary shares.

   b. Convertible securities that behave like equities.

   c. Depository receipts (these should be converted into the underlying shares and allocated to the same country as the underlying shares).

   d. Any other instruments exhibiting equity characteristics or which the bank believes carries equity risk.

   e. Equity derivatives or derivatives based on above securities.

177. In order to compute capital charge for equities risk, equity positions should first be allocated to the country in which each equity is listed. Where an equity is listed in more than one country, one country should be chosen and used consistently. Conversion into Kuwaiti Dinars should be done at spot foreign exchange rates using mid market prices.

178. The capital charge for equities risk is the sum of the following:

   a. A specific risk charge of 8% of the gross position (i.e. sum of the absolute value of all short equity positions and all long equity positions, including derivatives), calculated for each country; and

   b. General risk charge of 8% of the net position (i.e. long minus short position), calculated for each country.

179. Matched positions in each identical equity or stock index in each country may be fully offset, resulting in a single net short or long position to which the specific and general market risk charges will apply.

180. In order to calculate the specific and general market risk, positions in derivatives should be converted into notional equity positions as follows:

   a. Futures and forward contracts relating to individual equities should be reported at current market price of the underlying

   b. Futures relating to stock indices should be reported as the marked-to-market values of the notional underlying equity portfolio; and

   c. Equity swaps are to be treated as two notional positions.

3) Foreign exchange risk

181. The capital requirement for foreign exchange risk applies to foreign exchange risk of the entire business (i.e., both trading and non-trading books) and gold.

182. In order to calculate the capital charge for foreign exchange risk, the net position in each foreign currency (excluding the structural positions) and gold should be converted into Kuwait Dinars at spot rates using mid market prices.

183. The capital charge for foreign exchange risk is 8% of the sum of the following:

    a. The greater of the sum of the net open short positions or the sum of the net open long positions (absolute values); and

    b. The net open position in gold, either long or short, regardless of sign.

184. The net open position in each foreign currency (excluding the structural positions) and gold should be the total of:

    a. The net spot position (i.e., all asset items less all liability items, including accrued interest and accrued expenses, denominated in the relevant currency).

    b. The net forward position (i.e., all net amounts under forward, future agreements and foreign exchange transactions, including currency futures and the principal on currency swaps not included in the spot position).

    c. Guarantees (and similar instruments) that are certain to be called and are likely to be irrecoverable; and

    d. Net future income/expenses not yet accrued but already fully hedged.

185. All position, spot and forward, should be valued at spot market exchange rates using mid-market prices. Forward currency positions should not be valued using forward exchange rates since to some extent they reflect current interest rate differentials.

186. Structural positions (i.e., non-dealing positions) shall be exempt from the calculation of net open currency positions.

11- CAPITAL ADEQUACY RATIO
A) Circular No. (2/BS/184/2005) Regarding the Implementation of the Revised Capital Adequacy Ratio Basel (2).

4) Commodity risk

187. The capital requirement for commodities risk covers the market risk of holding or taking positions in commodities including precious metals but (excluding gold is treated as a foreign currency) and commodity options. The capital requirement applies to the commodities risk of the entire business (i.e., both the trading and non-trading book).

188. A commodity is defined as a physical product which is or can be traded on a secondary market, e.g. agricultural products, minerals (including oil) and precious metals (excluding gold).

189. The capital charge for commodities risk should be measured using either the simplified method or the maturity ladder method.

Simplified method for commodity risk

190. The capital charge for commodity risk under the simplified method should be calculated as follows:

a. First each long and short commodity position (spot and forward) should be expressed in terms of the standard unit of measurement (such as barrels, kilos or grams). The open position in each commodity should then be converted at spot rates into Kuwait Dinars, and the long and short positions should be offset to arrive at the net open position in each commodity;

b. Positions in different commodities should not be offset;

c. Commodity derivatives should be converted into notional commodity positions using the mid-market spot price.

d. The capital charge for commodities risk is the sum of :

   i. 15% of net open position in each commodity; and
   ii. 3% of gross position (long position plus absolute value of short position) in each commodity.

Maturity ladder method for commodity risk

191. The capital charge for commodities risk under the maturity ladder method should be calculated as follows:

a. First each long and short commodity position (spot and forward) should be expressed in terms of the standard unit of measurement (such as barrels, kilos, or grams). The open position in each commodity should then be converted at spot rates into Kuwaiti Dinars.

b. The long and short commodity position should be distributed into the time bands of the maturity ladder outlined in Table (C) below.

c. A separate maturity ladder must be constructed for each commodity in which the bank has significant positions (KD 30,000 or more) and capital requirements must be calculated for each commodity separately.

Table (C)

Time-band			Spread rate
0	Up to	1 month	1.5%
Over 1 month	Up to	3 months	1.5%
Over 3 months	Up to	6 months	1.5%
Over 6 months	Up to	12 months	1.5%
Over 1 year	Up to	2 years	1.5%
Over 2 years	Up to	3 years	1.5%
Over 3 years			1.5%

i. Commodity derivatives should be converted into notional commodity positions using the mid-market spot price.

ii. Once all long and short positions are placed into the appropriate time-bands, the positions should be matched. The sum of the matched long and short positions in each time bands should then be multiplied by the appropriate spread rate for that band (1.5%) according to table (C).

iii. The residual unmatched position should be carried forward to offset exposures in time bands that are further out. A capital charge of 0.6% should be applied in respect of each time and that the unmatched position is carried forward.

iv. At the end of the above process, the bank will have either only long or short positions to which a capital charge of 15% is applied.

v. The total capital charge for commodities risk is the sum of capital charges calculated in e, f and j above.

192. An illustration of the calculation of the capital charge under the simplified method and the maturity ladder method is set out in example (4) of annex (G).

5) Options risk:

193. The capital requirement for options applies to option contracts and related hedging positions in the associated underlying instrument, commodity or index, cash or forward.

194. In calculating capital requirement for options, banks which solely use purchased options may use the simplified method or the scenario method. Banks which write options must use the scenario method.

195. Banks using the scenario method for calculating capital required for the options should meet the appropriate qualitative standards applicable to the Internal Models Approach. The approval of the Central Bank of Kuwait should be obtained prior to use of the scenario method.

Simplified method for option risk:

196. Under the simplified method the capital charge for options risk should be computed as set out in Table (D) below:

Table (D)

<table>
<tr><th>Position</th><th>Treatment</th></tr>
<tr><td>Long the underlying and Short the put
or
Short the underlying and Long the call</td><td>The capital charge will be: the market value of the underlying instrument multiplied by the sum of (specific and general) market risk charges[2] specified in the preceding paragraphs for the underlying less the amount the option is in the money[3] (if any) bounded at zero[3]</td></tr>
<tr><td>Long call
or
Long put</td><td>The capital charge will be lesser value of:
i. The market value of the underlying instrument multiplied by the sum of (specific and general) market risk charges for the underlying
ii. The market value of the option</td></tr>
<tr><td colspan="2">1. In some cases such as foreign exchange it may be uncles which side is the “underlying instrument”; this should be taken to be the asset which would be received if the option were exercised. In addition the nominal value should be used for items where the market value of the underlying instrument could be zero, e.g. caps and floors.

2. To determine the appropriate specific risk and general market risk factors, refer back to the preceding paragraphs on interest rate positions risk, equity risk, foreign exchange risk and commodity risk. Some options (e.g., where the underlying is an interest rate, a currency or a commodity) bear no specific risk but specific risk will be present in the case of option on certain interest rate relating instruments (e.g., options on a corporate debt security or corporate bond index) and for options on equities and stock indices (see the section on equity position risk). Accordingly, the combined charge under this measure for currency options will be 8% and for options on commodities 15% (the additional 3% charge is not added because options are not netted).

3. In the money means the exercise level of a:
- “call option’ is less than the current mark to the market value of the underlying instrument.
- “put options” that the current mark to market value of the underlying instrument is less than the exercise level of the put option.

4. For options with a residual maturity of more than six months the strike price should be compared with the forward, not current price. A bank unable to do this must take in the money amount to be zero.</td></tr>
</table>

197. An illustration of calculation of capital charge under the simplified method is set out in example (5) of annex (K).

Scenario method for option risk:

198. Under the scenario method, a bank is required to make separate calculations of specific risk and general market risk of options and their related hedging positions. Specific risk charges must be calculated on each issue in which the bank has a net option position that is subject to interest rate risk or to equity risk. General risk charges are calculated on portfolios of options.

199. Under the scenario method the specific risk charge for options on debt securities should be calculated by multiplying the market value of the effective notional amount of the debt instrument that underlines the option by:

   a. The option's delta equivalent; and

   b. By the specific risk factors in Table (A) that correspond to the category and residual term of the underlying debt instrument.

200. The specific risk charge for options on equity securities and options on an equity index should be calculated by multiplying the market value of the effective notional amount of the equity instrument or equity index that underlines an option by:

   a. The options delta equivalent; and

   b. Then by 8%

201. General market risk for options under the scenario method should be calculated by constructing a two-dimensional matrix for each of the options portfolios.

202. Under this method simulation techniques are used to calculate charges in the value of an options portfolio for changes in the level and volatility of the prices of its associated underlying instruments. The general market risk charge is determined by the scenario "matrix" (i.e. the specified combination of underlying and volatility changes) that produces the largest loss. The total general market risk capital requirement for all option portfolios is the sum of the largest losses of individual option portfolios.

203. Options portfolios include options and any related hedging positions grouped together as follows:

a. For interest rates, options on underlying instruments whose residual maturity is bounded by one of at least six groups of time bands from Table (E) set out below where no more than three contiguous time bands are grouped together;

b. For equities and equity indices, each national market;

c. For foreign currencies and gold, each currency pair and gold and;

d. For commodities, each individual commodity.

204. The first dimension of each matrix requires the bank to evaluate the portfolio over a specified range above and below the current value of the underlying instrument, commodity or index. For interest rates the range is consistent with the assumed changes in yield for the time bands in Table (E) below. Banks should use the highest of the assumed changes in yield applicable to the time bands that it grouped together.

205. The other ranges are ± 8% for equities, ± 8% for foreign exchange and gold and ± 15% for commodities.

206. The time bands and assumed changes in yield are:

Table (E)
Time bands and assumed changes in yield

Coupon 3% or more	Coupon less than 3%	Assumed changes in yield
1 month or less	1 month or less	1.00%
Over 1 to 3 months	Over 1 to 3 months	
Over 3 to 6 months	Over 3 to 6 months	
Over 6 months to 12 months	Over 6 months to 12 months	
Over 1 to 2 years	Over 1.0 to 1.9 years	0.90
Over 2 to 3 years	Over 1.9 to 2.8 years	0.80
Over 3 to 4 years	Over 2.8 to 3.6 years	0.75
Over 4 to 5 years	Over 3.6 to 4.3 years	0.75
Over 5 to 7 years	Over 4.3 to 5.7 years	0.70
Over 7 to 10 years	Over 5.7 to 7.3 years	0.65
Over 10 to 15 years	Over 7.3 to 9.3 years	0.60
Over 15 to 20 years	Over 9.3 to 10.6 years	0.60
Over 20 years	Over 10.6 to 12 years	0.60
	Over 12 to 20 years	
	Over 20 years	

207. For all option portfolios, at least seven observations (including the current observation) should be used to divide the range into equally spaced intervals.

208. The second dimension of the matrix entails a change in the volatility of the underlying rate or price equal to ± 25 per cent of the current volatility.

209. An illustration of how the options scenario matrices are constructed is set out in example (6) of annex (K).

Treatment of counterparty credit risk in the trading book

210. Banks are required to calculate the counterparty credit risk charge for repo-style and other transactions booked in the trading book, separate from the capital charge for general market risk and specific risk.

211. The risk weights to be used in this calculation must be consistent with those used for calculating the capital requirements in the banking book, i.e., banks should use the applicable standard portfolio risk weights.

212. In the trading book, for repo-style transactions, all instruments, which are included in the trading book, may be used as eligible collateral. Those instruments which fall outside the banking book definition of eligible collateral shall be subject to a haircut at the level applicable to non-main index equities listed on recognised exchanges as noted in paragraph 264. Consequently, for instruments that count as eligible collateral in the trading book, but not in the banking book, the haircuts must be calculated for each individual security.

213. The calculation of the counterparty charge for repo-style transactions will be conducted using the rules in paragraphs 261 to 269 spelt out for such transactions booked in the banking book.

(f) Internal models approach

214. The use of internal models for the calculation of capital charges shall be subject to the prior approval of the Central Bank of Kuwait. The Central Bank of Kuwait will permit the use of internal models subject to satisfying the following:

a. The Central Bank of Kuwait is satisfied that the bank's risk management system is conceptually sound and is implemented with integrity;

b. The bank has sufficient numbers of staff skilled in the use of sophisticated internal models not only in the trading area but also in the risk control, audit, and if necessary, back office areas;

c. The bank's internal model has, in the Central Bank of Kuwait judgement, a proven track record of reasonable accuracy in measuring risk;

d. The bank fulfils the qualitative and quantitative standards, specifications of market risk factors and conditions on stress testing set out in this regulation.

1) Treatment of specific risk under the internal models approach"

215. Generally internal models are used to measure general risk exposure, typically leaving specific risk to be measured through separate risk measurement systems. Banks using internal models shall be subject to capital charges for the specific risk that is not captured by their internal models. Accordingly, if the bank's internal model does not capture specific risk; the capital charge for specific risk should be calculated using the standardized methodology. However, for banks using internal models that include specific risk, the total specific risk charge applied to debt securities or to equities should in no case be less than half the specific risk charges calculated according to the standardized methodology.

2) Capital requirement

216. Capital requirement under the internal model approach is the higher of:

a. The previous day's value-at-risk number measured according to the Quantitative Standards stated below; and

b. An average of daily value-at-risk measures on each of the proceeding 60 business days multiplied by 3. The Central Bank of Kuwait will require banks to add to this factor a "plus" ranging from 0 to 1 directly related to ex-post performance of the model.

3) Qualitative standards

217. Banks should meet the following qualitative standards before they are permitted to use an internal models-based approach.

218. The bank must be able to satisfy the Central Bank of Kuwait that the period of initial monitoring and live testing of its internal model is satisfactory before the model can be used for capital purposes.

219. The bank should have an independent risk control unit that is responsible for the design and implementation of the bank's risk management system. The unit should produce and analyze daily reports on the output of the bank's risk measurement model, including an evaluation of the relationship between measures of risk exposure and trading limits. This unit must be independent from the business trading units and should report directly to the chief executive of the bank.

220. The daily reports prepared by the risk control unit must be reviewed by a level of management with sufficient seniority and authority to enforce both reductions of positions taken by individual traders and reductions in the bank's overall risk exposure.

221. The risk control unit must conduct a regular back-testing program, i.e., an ex post comparison of the risk measure generated by the model against actual daily changes in portfolio value over longer periods of time (at least one year), as well as hypothetical changes based on static positions.

222. Board of Directors and senior management should be actively involved in the risk control process and must regard risk control as an essential aspect of its business to which significant resources need to be devoted.

223. The bank's internal risk measurement model must be closely integrated into the day-to-day risk management process of the bank. Its output should accordingly be an integral part of the process of planning, monitoring and controlling the bank's market risk profile.

224. The risk measurement system should be used in conjunction with internal trading and exposure limits. While trading limits for individual dealers do not need to be explicitly stated in terms of value-at-risk, trading limits should be related to the bank's risk measurement model in a manner that it is consistent over time and that is well understood by both traders and senior management.

225. A routine and rigorous program of stress testing should be in place as a supplement to the risk analysis based on day-to-day output of the bank's risk measurement model. The results of stress testing should be reviewed periodically by senior management and should be reflected in policies and limits set by management and the board of directors. Where stress tests reveal particular vulnerability to a given set of circumstances, prompt steps should be taken to manage those risks appropriately.

226. Banks should have a routine in place for ensuring compliance with a documented set of internal policies, controls and procedures concerning the risk measurement system. The bank's risk measurement system must be well documented, for example through a risk management manual that describes the basic principles of risk management system and that provides an explanation of the empirical techniques used to measure market.

227. An independent review of the risk measurement system should be carried out regularly in the bank's own internal auditing process. This review should include both the activities of the business trading units and of the independent risk control unit. A review of the overall risk management process should take place at regular intervals (ideally not less than once a year) and should specifically address, at a minimum:

    a. The adequacy of the documentation of the risk management system and process;

    b. The organization of risk management unit;

    c. The integration of market risk measures into daily risk management;

    d. The approval process for risk pricing internal models and valuation systems used by front and back-office personnel;

    e. The validation of any significant change in the risk measurement process;

    f. The scope of market risks captured by the risk measurement model;

    g. The integrity of the management information system;

    h. The accuracy and completeness of position data;

    i. The verification of the consistency, timeliness and reliability of data sources used to run internal models, including the independence of such data sources;

    j. The accuracy and appropriateness of volatility and correlation assumptions;

    k. The accuracy of valuation and risk transformation calculations; and

    l. The verification of the model's accuracy through frequent back-testing.

4) Specifications of market factors

228. In specifying the risk factors (i.e., the market rates and prices that affect the value of the bank's trading positions) for their internal models, banks should meet the guidelines set out below:

a. Interest rates

i. There must be a set of risk factors corresponding to interest rates in each currency in which the bank has interest-rate-sensitive on- or off-balance sheet positions.

ii. The risks measurement system should model the yield curve using one of a number of generally accepted approaches, for example by estimating forward rates of zero coupon yields. The yield curve should be divided into various maturity segments in order to capture variations in the volatility of rates along the yield curve; there will typically be one risk factor corresponding to each maturity segment. For material exposures to interest rate movements in the major currencies and markets, banks must model the yield curve using a minimum of six risk factors.

iii. The risk measurement system must incorporate separate risk factors to capture spread risk (e.g., between bonds and swaps). A variety of approaches may be used to capture the spread risk arising from less than perfectly correlated movements between government and other fixed-income interest rates, such as specifying a completely separate yield curve for non-government fixed-income instruments or estimating the spread over government rates at various points along the yield curve.

b. Exchange Rates

i. The risk measurement system should incorporate risk factors corresponding to the individual foreign currencies in which the bank's positions are denominated. Since the value-at-risk figure calculate by the risk measurement system will be expressed in Kuwaiti Dinar, any net position denominated in a foreign currency will introduce a exchange rate risk. Thus, there must be risk factors corresponding to the exchange rate between the Kuwaiti Dinar and each foreign currency in which the has a significant exposure.

c. Equity Prices

i. There should be risk factors corresponding to each of the equity markets in which the bank holds significant positions.

ii. At a minimum, there should be a risk factor that is designed to capture market-wide movements in equity prices (e.g., a market index). Positions in individual securities or in sector indices could be expressed in “beta-equivalents” relative to this market-wide index.

iii. A somewhat more detailed approach would be to have risk factors corresponding to various sectors of the overall equity market (for instance, industry sectors or cyclical and non-cyclical sectors). As above, positions in individual stocks within each sector could be expressed in “beta-equivalents” relative to the sector index.

iv. The most extensive approach would be to have risk factors corresponding to the volatility of individual securities issues.

v. The sophistication and nature of the modelling technique for a given market should correspond to the bank’s exposure to the overall market as well as its concentration in individual securities issues in that market.

d. Commodity Prices

i. There should be risk factors corresponding to each of the commodity markets in which the bank holds significant positions.

ii. For banks with relatively limited positions in commodity-based instruments, a straightforward specification of risk factors would be acceptable. Such a specification would likely entail one risk factor for each commodity price to which the bank is exposed. In cases where the aggregate positions are quite small, it might be acceptable to use a single risk factor for a relatively broad classes of commodities (for instance, a single risk factor for all types of oil).

iii. For more active trading the model should encompass:

(1) Directional risk, to capture the exposure from changes in spot prices arising from net open positions;

(2) Forward gap and interest rate risk, to capture the exposure to changes in forward prices arising from maturity mismatches;

(3) Basis risk, to capture the exposure to changes in the price relationships between two similar, but not identical, commodities;

(4) The model must also take account of variances in the “convenience yield” between derivatives positions, such as forwards and swaps, and cash positions in the commodity.

5) Quantitative standards

229. The following minimum quantitative standards will apply to banks adopting the internal model approach:

a. “Value at risk” should be computed on a daily basis.

b. In calculating the value-at-risk, 99%, one-tailed confidence interval is to be used.

c. In calculating the value-at-risk, the minimum holding period will be ten trading days.

230. The historical observation period (sample period) for calculating value-at-risk will be constrained to a minimum length of one year. For banks that use a weighting scheme or other methods for the historical observation period, the “effective” observation period must be at least one year.

231. Banks should update their data sets no less frequently than once every three months and should also reassess them whenever market prices are subject to material changed. The Central Bank of Kuwait may also require a bank to calculate its value-at-risk using a shorter observation period if, in the Central Bank of Kuwait judgment, this is justified by a significant upsurge in price volatility.

232. No particular type of model is prescribed. So long as each model used captures all the material risks run by the bank, as set out in the section above on market risk factors, banks will be free to use internal models based on variance-covariance matrices, historical simulations, or Monte Carlo simulations.

233. Banks will have discretion to recognize empirical correlations within broad risk categories (e.g., interest rates, exchange rates, equity prices and commodity prices), including related options volatilities in each risk factor category. The Central Bank of Kuwait may also recognize empirical correlations across broad risk factor categories, provided the Central Bank of Kuwait is satisfied that the bank’s system for measuring correlations is sound and implemented with integrity.

234. Banks internal models must accurately capture the unique risks associated with options within each of the broad risk categories. The following criteria apply to measurement of options risks:

a. Banks internal models must capture the non-linear price characteristics of options positions;

b. Each bank's risk measurement system must have a set of risk factors that captures the volatilities of the rates and prices underlying option positions, i.e., Vega risk. Banks with relatively large and/or complex options portfolios should have detailed specifications of relevant volatilities. This means that banks should measure the volatilities of the positions broken down by different maturities.

6) Stress testing

235. Banks that use the internal models approach for meeting market risk capital requirements must have in place a rigorous and comprehensive stress testing program.

236. Banks stress scenarios should cover a range that can create extraordinary losses or gains in trading books, or make the control of risk in those books very difficult. These factors include low-probability events in all major types of risks. Stress scenarios need to shed light on the impact of such events on positions that display both linear and non-linear price characteristics (i.e., options and instruments that have options-like characteristics).

237. Banks stress tests should be both of a quantitative and qualitative nature, incorporating both market risk and liquidity aspects of market disturbances. Quantitative criteria should identify plausible stress scenarios to which banks should be exposed. Qualitative criteria should emphasize that two major goals of:

a. Stress testing is to evaluate the capacity of the bank's capital to absorb potential large losses.

b. Identify steps the bank can take to reduce its risk and conserve capital. This assessment is integral to setting and evaluating the bank's management strategy and the results of stress testing should be routinely communicated to senior management and, periodically, to the bank's board of directors.

238. Banks should combine the use of supervisory stress scenarios with stress tests developed by banks themselves to reflect their specific risk characteristics. Specifically, the Central Bank of Kuwait may ask banks to provide information on stress testing in three broad areas:

a. Supervisory scenarios requiring no simulations by the bank**:** Banks should have information on largest losses experienced during the reporting period available for supervisory review. This loss information could be compared to the level of capital that results from a bank's internal measurement system. For example, it could provide the Central Bank of Kuwait with a picture of how many days of peak day losses would have been covered by a given value-at-risk estimate.

b. Scenarios requiring a simulation by the bank: Banks should subject their portfolios to a series of simulated stress scenarios and provide the Central Bank with results on a quarterly basis. These scenarios could include testing the current portfolio against past periods of significant disturbance (for example the 1987 equity crash). A second type of scenario would evaluate the sensitivity of the bank's market risk exposure to changes in the assumptions about volatilities and correlations.

c. Scenarios developed by the bank itself to capture the specific characteristics of its portfolios: In addition to the scenarios prescribed by the Central Bank of Kuwait under (a) and (b) above, a bank should also develop its own stress tests which it identifies as most adverse based on the characteristics of its portfolio (e.g., problems in a key region of the world combined with a sharp move in oil prices). Banks should provide the Central Bank of Kuwait with a description of the methodology used to identify and carry out the scenarios as well as with a description of the results derived from these scenarios.

7) Model validation

239. In reviewing the bank's internal model the Central Bank of Kuwait shall require assurance that:

a. The internal validation processes described in paragraph 226 of Qualitative Standards are operating in a satisfactory manner;

b. The formulae used in the calculation process as well as for the pricing of options and other complex instructions are validated by a qualified unit, which in all cases should be independent from the trading area;

c. The structure of internal models is adequate with respect to the bank's activities and geographical coverage;

d. The results of the bank's back-testing of its internal measurement system (i.e. comparing value-at-risk estimates with actual profits and losses) ensure that the model provides a reliable measure of potential losses over time. The results as well as the underlying inputs to their value-at-risk calculations should be available to the Central Bank of Kuwait on request;

e. Data flows and processes associated with the risk measurement system are transparent and accessible.

(g) Combination of internal models and standardized methodology:

240. Except under circumstances outlined in paragraph 215, combination of internal models and standardized methodology for calculating capital charge for market risk is not allowed.

Ninth: Operational Risk Weighted Exposure:

241. This section sets out the risk measurement framework, i.e. the quantitative criteria for calculating the capital charge for operational risk under the Standardised Approach developed by the Basel Committee on Banking Supervision.

(a) Qualifying criteria

242. All licensed banks are required to have in place an operational risk management framework in accordance with the Central Bank of Kuwait Circulars on "Guiding Principles on Sound Practices for the Management and Supervision of Operational Risk" dated 13 October 2003 and "Internal Control Systems" dated 14 November 1996. All licensed banks should also comply with the Central Bank Circular on "The Establishment of Risk Management Unit".

243. If the Central Bank of Kuwait determines that a licensed bank no longer meets the qualifying criteria stated above, it may require the licensed bank to maintain a higher capital adequacy ratio and/or impose other conditions on the licensed bank.

(b) Measurement of capital charge

244. All licensed banks activities should be divided into eight business lines; namely, Corporate Finance, Trading and Sales, Retail Banking, Commercial Banking, Payment and Settlement, Agency Services, Asset Management, and Retail Brokerage. These business lines are defined in detail in annex (L).

245. Within each business line, gross income is a broad indicator that serves as a proxy for the scale of business operations and thus the likely scale of operational risk exposure within each of these business lines. Refer to annex (A) for the definition of gross income.

246. The operational risk capital charge for each business line is calculated by multiplying its gross income by a factor (denoted beta) assigned to that business line. Beta serves as a proxy for the relationship between the operational loss for a business line and the gross income for that business line. It should be noted that gross income is measured for each business line, not the whole institution, i.e. in retail banking, the indicator is the gross income generated in the retail banking business line.

247. The total operational risk capital charge is calculated as the summation of the three-year average gross income multiplied by the beta factor across each of the business lines in each year. In any given year, negative gross income in any business line may offset positive gross income in other business lines. However, where the aggregate gross income across all business lines within a given year is negative, the input to the numerator for that year in calculating the average gross income will be zero. The total capital charge can be expressed as:

$$\mathbf{K = \sum_{\text{business lines 1-8}} \{max\ [(\sum_{\text{years1-3}} GI1\text{-}8 / 3)\ X\ \beta 1\text{-}8], 0\}}$$

Where:

K = The capital charge

GI1-8 = Annual (year end) gross income for each of the eight business lines

β1-8 = A fixed percentage assigned to each of the eight business lines, as follows:

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Business lines	Beta Factors (%)
Corporate finance	18
Trading and sales	
Payment and settlement	
Commercial banking	15
Agency services	
Retail banking	12
Asset management	
Retail brokerage	

248. In case of a licensed bank with negative gross income for the previous three years, a newly licensed bank with less than 3 years of operations, or a merger, acquisition or material restructuring, the Central Bank of Kuwait shall discuss with the concerned licensed bank an alternative method for calculating the operational risk capital charge. For example, a newly licensed bank may be required to use the projected gross income in its 3 years business plan. Another approach that the Central Bank of Kuwait may consider is to require such licensed banks to observe a higher Capital Adequacy Ratio (CAR).

249. Total operational risk weighted exposures are determined by multiplying the operational risk capital charge by 8.33 (i.e. the reciprocal of the minimum capital ratio of 12%) and adding the resulting figure to the sum of credit and market risk weighted assets to yield the total risk weighted exposures which will then be used to calculate the capital adequacy ratio (CAR).

(c) Mapping principles

250. All licensed banks should develop specific policies and documented procedures for mapping gross income into the predefined business lines. It should be able to demonstrate to the satisfaction of the Central Bank of Kuwait the reasons behind their mapping. These policies and procedures must be regularly reviewed and adjusted for new or changing business activities.

251. The approach used by a bank to map its activities into the eight business lines must meet the following mapping principles:

a. Senior management should be responsible for the mapping policy, which should be properly approved by the board of directors;

b. All business activities of the licensed bank must be mapped into the eight level (1) business lines in a mutually exclusive and jointly exhaustive manner;

c. Any banking or non-banking activity which cannot be readily mapped into the business line framework, but which represents an ancillary function to an activity included in the framework, must be allocated to the business line it supports. If more than one business line is supported through the ancillary activity, an objective mapping criteria must be used (e.g. proportional allocation according to the time spent or sole allocation to the business line on which most time is spent);

d. When mapping gross income, if an activity cannot be mapped into a particular business line, then the business line yielding the highest charge must be used (i.e. 18%). Any associated ancillary activities will follow the same business line treatment;

e. A licensed bank may use its internal fund transfer pricing method to allocate net interest income and interest expense between business lines, provided that the total gross income and net interest income of the licensed bank equals the sum of gross income and net interest income of the eight business lines respectively;

f. The mapping activities into business lines for operational risk capital purposes must be consistent, wherever applicable, with the definitions of business lines used for regulatory capital calculations in other risk categories, e.g. credit and market risk. Any deviations must be clearly explained and documented;

g. The mapping process used must be clearly documented and be detailed enough for third parties to replicate the business line mapping. Any exceptions or overrides must be properly documented;

h. Processes must be in place to define the mapping of any new activities or products; and

i. The mapping process must be subject to regular independent review by the risk management function, internal auditors and external auditors.

Tenth: Credit Risk Mitigation:

252. This annex sets out the detailed requirements for the recognition and use of credit risk mitigation techniques (CRM) under the ***comprehensive approach*** developed by the Basel Committee on Banking Supervision. In particular, this section sets out the recognition requirements, the types of CRM techniques recognised by the Central Bank of Kuwait (eligible collaterals, netting and guarantees), and the calculation of adjusted weighted amount for exposures with recognised CRM techniques.

(a) Recognition requirements

253. Licensed banks may use, for capital adequacy purposes, CRM techniques to reduce their weighted amount of credit risk exposures for capital adequacy purposes. In order for a licensed bank to take benefit of such techniques, it must satisfy the following recognition requirements:

a. All documentation used for CRM purposes must be binding on all parties and legally enforceable in all relevant jurisdictions. Banks must have conducted sufficient legal reviews to verify this and have a well-founded legal basis to reach this conclusion. Such reviews should be re-conducted whenever necessary to ensure continued enforceability of the documents,

b. No transaction in which recognised CRM techniques are used should be subject to a higher capital requirement than an otherwise identical transaction where such techniques are not used, and

c. The effects of CRM should not be double counted. Therefore, no additional supervisory recognition of CRM will be granted for claims with an issue-specific or principal-only rating in which the CRM effects have already been taken into account.

d. The legal mechanism by which collateral is pledged or transferred must ensure that licensed banks have the right to liquidate or to take legal possession of the collateral in a timely manner in the event of default, insolvency, bankruptcy (or other pre-defined credit events in the transaction documentation) of the counterparty (and, where applicable, of the custodian holding the collateral).

e. Licensed banks must take all necessary steps to fulfil the requirements under the law applicable to the bank's interest in the collateral for obtaining and maintaining an enforceable security interest, e.g., by registering it with a register, or for exercising a right to net or set off in relation to title transfer collateral.

f. Licensed banks must have clear and robust procedures for the timely liquidation of collateral to ensure that any legal conditions required for declaring the default of the counterparty and liquidating the collateral are properly observed, and that collateral can be liquidated promptly.

g. Where the collateral is held by a custodian, licensed banks must take reasonable steps to ensure that the custodian segregates the collateral from its own assets.

h. The credit quality of the counterparty and the value of the collateral must not have a material positive correlation. For example, securities issued by the counterparty, or by any related group entity, would provide little protection and so would be ineligible for capital adequacy purposes.

i. Where a licensed bank, acting as an agent, arranges a repo-style transaction between a customer and a third party and provides guarantee to the customer that the third party will perform on its obligations, then the risk to the bank is the same as if the bank had entered into the transaction as a principal. In such circumstances, the bank will be required to calculate capital requirements as if it were the principal itself.

254. The following types of CRM techniques are recognised for the reduction of the weighted amount of a credit exposure, provided that they fulfill the recognition conditions set out above:

a. Collateral: A collateralised transaction is one in which licensed banks have a credit exposure or potential credit exposure which is hedged in whole or in part by collateral posted by a counterparty or by a third party on behalf of the counterparty.

b. Netting: Where licensed banks have legally enforceable netting arrangements for loans and deposits they may calculate capital requirements on the basis of net credit exposures subject to the conditions set out below.

c. Guarantees: Where guarantees are direct, explicit, irrevocable and unconditional, and the Central Bank is satisfied that the licensed bank fulfils certain minimum operational conditions relating to risk management processes it may allow licensed banks to take account of such guarantees in calculating capital requirements. Only guarantees issued by entities with a lower risk weight than the counterparty will lead to reduced capital charges. The uncovered portion, however, should retain the risk weight of the underlying counterparty.

(b) Eligible collaterals (1) (2)

255. The following types of financial collateral are eligible for recognition:

a. Cash on deposit with the licensed bank, including certificates of deposit or comparable instruments issued by the licensed bank.

b. Gold.

c. Debt securities issued by:

i. The government of any GCC country.

ii. GCC PSEs in their domestic currencies.

iii. Other sovereigns or foreign PSEs that are treated as sovereigns in the relevant countries. The sovereigns or the sovereigns in which the PSE are incorporated must be rated by a recognised ECAIs with their ratings equivalent to Credit Quality Grade (Sovereigns) of 4 or better. Debt securities issued by GCC PSEs in foreign currencies will be subject to this minimum rating condition.

iv. Foreign PSEs that are not treated as sovereigns in the relevant countries. The sovereigns in which the PSEs are incorporated must be rated by a recognised ECAIs with their ratings equivalent to Credit Quality Grade (Sovereigns) of 3 or better.

v. MDBs, or those issued by banks or securities firms and rated by a recognised ECAIs with their ratings equivalent to Credit Quality Grade (Banks) of 3 or better.

d. Short-term debt instruments issued by banks and with a short-term rating from a recognised ECAIs equivalent to Credit Quality Grade (banks) of 3 or better.

(1) According to Circular No. (2/BS/225/2008) dated 8/10/2008, included under Item " G" of this section, real estate properties were considered as one of the acceptable (eligible) collaterals for mitigating credit risk.
(2) According to Circular No. (2/BS, IBS/ 227/2008) dated 19/10/2008, included under Item "R" of section (10) of this Guide, banks were allowed to add real estate properties to credit risk mitigation tools in banks' financial deals with investment companies.

e. Debt securities not rated by a recognised ECAIs but meet all of the following conditions:

   i. Issued by a bank;

   ii. Listed on a recognised exchange;

   iii. Classified as senior debt;

   iv. All rated issues of the same seniority by the issuing bank that are rated equivalent to Credit Quality Grade (Banks) of 3 or better by a recognised ECAIs or short-term Credit Quality Grade (Banks) of 3 or better; and

   v. The concerned licensed bank holding the securities as collateral has no information to suggest that the issue justifies a rating below the Credit Quality Grade (Banks) of 3 or short-term Credit Quality Grade (Banks) of 3.

f. Equities that are included in a main index or listed on a recognised exchange.

g. Real Estate (1)

h. Collective investment schemes (CIS) where:

   i. A price for the units is publicly quoted daily; and

   ii. The CIS is limited to investing in instruments recognised as eligible collateral.

256. Where a licensed bank takes eligible collateral from a counterparty of a credit exposure or a third party on behalf of the counterparty, it is allowed to take account of the risk mitigating effect of the collateral in calculating the capital requirement.

257. However, regulatory capital relief will only be allowed if the collateral instruments and the risk mitigation process satisfy all the specific requirements for individual CRMs in addition to the minimum conditions mentioned above.

(1) According to Circular No. (2/BS/225/2008), dated 8/10/2008, included under Item " G" of this section, real estate properties were considered as one of the acceptable (eligible) collaterals for mitigating credit risk.

(c) Collateral Measurement methodology

258. All licensed banks are required to use the comprehensive approach for both their banking book credit exposures and their credit exposures in the trading book. The comprehensive approach for calculation of collateralized exposures allows for fuller offset of collateral against exposures, by effectively reducing the exposure amount by the value ascribed to the collateral.

259. The comprehensive approach calculates, through the formula given below, the capital requirement of a collateralised transaction based on the net credit exposure to a counterparty (E*). In determining the net exposure, haircuts should be applied to the value of the gross exposure to the counterparty (He) and the value of any collateral received in support of the counterparty (Hc) to take account of future fluctuations in value. When the exposure and collateral are denominated in different currencies, an additional haircut (Hfx) will be applied to the collateral to make some allowance for future fluctuations in foreign exchange rates.

$$\mathbf{E^* = \max \{0, [E \times (1 + H_e) - C \times (1 - H_c - H_{fx})]\}}$$

where:

E^* = Net credit exposure (i.e. exposure value after CRM)

E = Principal Amount, which is net of specific provisions, if any. For off-balance sheet, it is the credit equivalent amount

H_e = Haircut appropriate to the underlying exposure

C = Value of the collateral before CRM

H_c = Haircut appropriate to the collateral

H_{fx} = Haircut appropriate for currency mismatch between the exposure and the collateral fixed at 8%

260. Where the collateral is a basket of assets, the haircuts on the basket (Ha) will be calculated as:

$$\mathbf{H_a = \sum a_i \times H_i}$$

where:

a_i = Weight of the asset in the basket

H_i = Haircut applicable to that asset

261. To obtain the weighted amount of a collateralised transaction, licensed banks should multiply the value of the net credit exposure (E*) by the risk weight of the counterparty, not that of the collateral instruments.

(d) Standard supervisory haircuts [1]

262. Licensed banks are required to use the Standard Supervisory Haircuts under the Comprehensive approach for the calculation of collateralized exposures. The assumptions under the standard supervisory haircuts are daily mark-to-market, daily remargining, and a 10-business-day holding period. The haircuts as given below in percentages, apply to both the collateral value (Hc) as well as the value of the gross exposure to the counterparty (He). Exposure amount may vary where, for example, securities are being lent or where the bank is exposed to securitises supported by collaterals.

Credit Quality Grade /Short-term Credit Quality Grade (Issue Rating) For Debt Securities	**Residual Maturity**	**Sovereigns** (includes PSEs treated as sovereigns and MDBs)	**Other issuers** (includes PSEs not treated as sovereigns)
Grade 1	≤ 1 year	0.5	1
	> 1 year, ≤ 5 years	2	4
	> 5 years	4	8
Grade 2 & 3 Includes unrated securities issued by banks satisfying the criteria for eligible collateral	≤ 1 year	1	2
	> 1 year, ≤ 5 years	3	6
	> 5 years	6	12
Grade 4	All	15	
Main index equities and gold		15	
Other equities listed on a recognised exchange and non-investment grade corporate debt securities		25	
Collective investment schemes (CIS)		Highest haircut applicable to any security in which CIS can invest	
Cash in the same currency			

(1) According to Circular No. (2/BS/225/2008) dated 8/10/2008, included under Item " G" of this section, real estate properties were considered as one of the acceptable (eligible) collaterals for mitigating credit risk, banks have to apply a hair cut of 50%.

(e) Adjustment for different holding periods and non-daily revaluation and remargining

263. The framework for collateral haircuts distinguishes between repo-style transactions, other capital market driven transactions (i.e. OTC derivatives and margin lending) and secured lending. The appropriate haircut to be used for each of these types of transactions depends on the frequency of the remargining and revaluation and the assumed minimum holding period for the type of transaction. Provided the transactions are subject to daily revaluation or remargining, their minimum holding periods are as follows:

Transaction Type	Minimum Holding Period	Condition
Repo-style transactions	5 business days	Daily remargining
Other capital market transactions	10 business days	Daily remargining
Secured lending	20 business days	Daily revaluation

264. For a repo-style or secured lending or any other transactions which has a holding period different from 10 business days or is not remargined or revalued daily as assumed in the standard supervisory haircuts, licensed banks are required to scale up or down the standard haircuts (He, Hc and Hfx) depending on the type of transaction and the frequency of remargining or revaluation. The calculation can be expressed as follows:

$$\mathbf{H = H_{10} \times \frac{\sqrt{NR + (T_m - 1)}}{10}}$$

where:

H = Haircut after adjustment for differences in holding period and revaluation frequency

H_{10} = Standard supervisory haircuts based on a minimum holding period of 10 business days

T_m = Minimum holding period for the type of transaction (i.e. 5 business days for repo-style transactions or 20 business days for secured lending)

NR = Actual number of business days between remargining for capital market transactions or revaluation for secured transactions.

265. As the determination of appropriate haircuts is based on the type of transaction, as well as on certain assumptions about the revaluation frequency and holding period of the collateral, licensed banks intending to use the comprehensive approach are required to have robust internal policies, systems and procedures for collateral management, covering the revaluation of collateral, and the assumptions on the holding periods of collateral.

266. For repo-style transactions in the trading book that are treated as collateralised loans (i.e. reverse repo transactions or securities borrowing against cash collateral), all assets received by the licensed bank may be recognised for CRM purposes. Assets falling outside the definition of eligible collateral (as set out in the table above) should be subject to a 25% haircut.

(f) Conditions for zero haircuts

267. For certain type of repo-style transactions that satisfy all of the following conditions, the supervisory haircut will be zero:

a. The counterparty is one of the following core market participants:

   i. Sovereigns, central banks and PSEs;

   ii. Banks;

   iii. Other financial entities and insurance companies eligible for a 20% risk weight;

   iv. Regulated CIS that are subject to capital or leverage requirements;

   v. Regulated pension funds; and

   vi. Recognised clearing organisations.

b. Both the exposure and the collateral are cash or a sovereign security or PSE security qualifying for a 0% risk weight;

c. Both the exposure and the collateral are denominated in the same currency;

d. Either the transaction is overnight or both the exposure and the collateral are marked-to-market daily and are subject to daily remargining;

e. Following the counterparty's failure to remargin, the time that is required between the last mark-to-market before the failure to remargin and the liquidation of the collateral is considered to be no more than four business days;

f. The transaction is settled across a settlement system proven for that type of transaction;

g. Standard market documentation in the securities concerned is used for the agreement covering the repo-style transactions;

h. The documentation of the transaction should specify that the transaction is immediately terminable if the counterparty fails to satisfy an obligation to deliver cash or securities or to deliver margin or otherwise defaults; and

i. Upon any event of default, regardless of whether the counterparty is insolvent or bankrupt, the licensed bank should have an unfettered and legally enforceable right to immediately seize and liquidate the collateral for its benefit.

(g) Capital treatment of netting

268. Where a licensed bank,

a. Has a well-founded legal basis for concluding that the netting or offsetting agreement is enforceable in each relevant jurisdiction regardless of whether the counterparty is insolvent or bankrupt;

b. Is able at any time to determine those assets and liabilities with the same counterparty that are subject to the netting agreement;

c. Monitors and controls its roll-off risks; and

d. Monitors and controls the relevant exposures on a net basis,

It may use the net exposure of loans and deposits as the basis for its capital adequacy calculation in accordance with the formula in paragraph 259 above. Assets (loans) are treated as exposure and liabilities (deposits) as collateral. The haircuts will be zero except when a currency mismatch exists. A 10-business days holding period will apply when daily mark-to-market is conducted and all the requirements contained in paragraphs 262, 264 and 283 to 286 will apply.

269. The net credit exposure with a counterparty, adjusted for the CRM effect of a valid on-balance sheet netting agreement, is calculated using the following formula:

Net credit exposure = max [0, assets - liabilities x (1 - Hfx)],

Where:

Hfx is the haircut, which is 8%, to be applied in the case of a currency mismatch between assets and liabilities. The haircut assumes a minimum holding period of 10-business days and a daily mark-to-market. It should be adjusted according to the formula set out in paragraph 264 for a different minimum holding period and/or frequency of revaluation.

270. The Weighted Amount for transactions with netting agreements is calculated by multiplying the net credit exposure by the risk weight of the counterparty.

271. For off balance sheet items, licensed banks are required to calculate the credit equivalent amount after taking into effect the netting arrangements, and multiply the credit equivalent amount by the risk weight of the counterparty to derive the weighted amount.

272. Licensed banks are allowed to net exposures arising from exchange rate, gold and interest rate contracts with the same counterparty provided that they are subject to a valid bilateral netting agreement. The bilateral netting agreement for derivative contracts may cover only a single type or more than one type of contracts.

(h) Capital treatment of guarantees and related conditions

273. In order for a guarantee or a counter-guarantee to be recognised, the following conditions must be satisfied:

i. It must represent a direct claim on the guarantor;

ii. The guarantee should be explicitly referenced to specific exposures or a pool of exposures, so that the extent of cover is clearly defined and incontrovertible;

iii. Other than a non-payment by a protection purchaser of money due in respect of the guarantee contract, there should be no clause in the guarantee contract that would allow the guarantor to cancel the credit cover unilaterally or that would increase the effective cost of cover as a result of deteriorating credit quality in the hedged exposure;

iv. It must also be unconditional, i.e., there should be no clause in the guarantee contract that could prevent the guarantor from being obliged to pay out promptly in the event that the underlying borrower fails to make the payment(s) due;

v. The country where the guarantor is located or incorporated should either have no exchange controls or, where there are exchange controls, approval should have been obtained for the funds to be remitted freely in the event of a call on the obligation;

vi. On the qualifying default/non-payment of the counterparty, the licensed bank may in a timely manner pursue the guarantor for any monies outstanding under the documentation governing the transaction. The guarantor may make one lump sum payment of all monies under such documentation to the licensed bank, or the guarantor may assume the future payment obligations of the counterparty covered by the guarantee. The licensed bank must have the right to receive any such payments from the guarantor without first having to take legal actions in order to pursue the counterparty for payment;

vii. The guarantee is an explicitly documented obligation assumed by the guarantor; and

viii. The guarantee covers all types of payments the underlying obligor is expected to make under the documentation governing the transaction, for example notional amount, margin payments etc. Where a guarantee covers payment of principal only, interests and other uncovered payments should be treated as an unsecured amount.

274. When calculating the weighted amount for exposures covered by guarantees, the secured portion is assigned the risk weight of the guarantor and the unsecured portion is assigned the risk weight of the underlying obligor.

275. Where the amount guaranteed is less than the whole amount of the underlying exposure, and the licensed bank and the guarantor share losses on a pro-rata basis, the protected portion is assigned the risk weight of the guarantor while the uncovered portion is assigned the risk weight of the underlying obligor.

276. Where a foreign currency mismatch occurs i.e. when the credit protection is denominated in a currency different from that of the underlying obligation, the portion covered by the credit protection should be reduced by a standard haircut of 8%.

$$Ga = G \times (1 - Hfx)$$

where:

Ga = The amount of the exposure covered by credit protection and adjusted for currency mismatch

G = Nominal amount of the credit protection

Hfx = Haircut appropriate for currency mismatch between the credit protection and underlying obligation (8%)

277. The 8% haircut is based on a 10-business days holding period and daily mark-to-market. This haircut has to be adjusted by using the formula set out in paragraph 264 when the minimum holding period or the mark-to-market frequency of the transactions is different from that of the standard supervisory haircut.

278. Where an exposure is guaranteed by a sovereign, such an exposure may be treated as a claim on a sovereign and assigned a risk weight in accordance with the treatment applicable to an on-balance sheet claim on a sovereign.

279. Where an exposure is counter-guaranteed by a sovereign, such an exposure may be treated as a claim on a sovereign and assigned a risk weight in accordance with the treatment applicable to an on-balance sheet claim on a sovereign provided that:

i. The sovereign counter-guarantee covers all credit risk elements of the underlying exposure;

ii. Both the original guarantee and the counter-guarantee meet all requirements for guarantees above, except that the counter-guarantee need not be direct and explicit to the original claim; and

iii. The cover is robust and there is no evidence to suggest that the coverage of the counter-guarantee is less effective than that of a direct sovereign guarantee.

(i) Eligible guarantors (counter-guarantors)

280. Credit protection given by the following entities will be recognised for capital adequacy purposes:

   i. Sovereign entities, PSEs, MDBs, banks with a lower risk weight than the underlying obligor; or

   ii. Other entities rated by a recognised ECAI with their ratings as equivalent to Corporates Credit Quality Grade of 2 or better. This would include credit protection provided by parent, subsidiary and affiliate companies when they have a lower risk weight than the underlying obligor.

(j) Treatment of pools of CRM techniques

281. Where a licensed bank has multiple CRM techniques covering a single exposure, for example, having both guarantees and collateral partially supporting an exposure, the bank is required to divide this exposure into different portions covered by different CRM techniques and to calculate the Weighted Amount of each portion separately. Furthermore, when credit protection provided by a single protection provider has different maturities, they must be divided into separate protection as well.

282. Where the exposure to the borrower is in the form of a general banking facility consisting of several types of credit lines, the licensed bank has the discretion to allocate the effect of the CRM technique(s) among the exposures under these lines to arrive at their respective Weighted Amounts.

(k) Maturity mismatches

283. A maturity mismatch occurs when the residual maturity of a hedge is less than that of the underlying exposure.

284. The maturity of the underlying exposure and the maturity of the hedge should both be defined conservatively. The effective maturity of the underlying should be gauged as the longest possible remaining time before the obligor is scheduled to fulfill its obligation, taking into account any applicable grace period. For the hedge, embedded options which may reduce the term of the hedge should be taken into account such that the shortest possible effective maturity should be used. Where a call is at the discretion of the protection provider, the maturity will always be the first

call date. If the call is at the discretion of the licensed bank as the protection buyer but the terms of the arrangement of obligation of the hedge contain a positive incentive for the licensed bank to call the transaction before contractual maturity, the remaining time to the first call date will be deemed to be the effective maturity.

285. All CRM techniques will be recognised for capital purposes when the hedge has an original maturity of longer than or equal to one year. As a result, the maturity of hedges for exposures with original maturities of less than one year must be matched to be recognised. In all cases, hedges with maturity mismatches will no longer be recognised when the hedges have a residual maturity of three months or less.

286. Where a recognised maturity mismatch exists, the value of the CRM protection should additionally be adjusted based on the following formula:

Pa = P x (t - 0.25) / (T - 0.25)

where:

Pa = Value of credit protection adjusted for maturity mismatch

P = Value of credit protection adjusted for any haircuts

t = Min (T, residual maturity of the credit protection arrangement) expressed in years

T = Min (5, residual maturity of the underlying exposure) expressed in years.

Eleventh: Public Disclosure Requirements

287. This section sets out the detailed qualitative and quantitative public disclosure requirements. The purpose of these requirements is to complement the above capital adequacy requirements and the supervisory review process. Moreover, these disclosure requirements shall enable and allow market participants to assess key pieces of information about a licensed bank's exposure to risks and provides a consistent and understandable disclosure framework that enhances comparability.

(a) General requirements

288. The disclosure requirements stipulated in this section should be applied at the top consolidated level of a banking group by all licensed banks, i.e., at the level of the parent licensed bank. Disclosures related to individual banks within a banking group would not generally be required. An exception to this arises in the disclosure of total and Tier (1) capital ratios of subsidiary banks by the top consolidated bank where an analysis of significant subsidiary banks within the group is appropriate in order to recognise the need for these subsidiaries to comply with the relevant capital adequacy framework and other applicable limitations on the transfer of funds or capital within the group.

289. Licensed banks should have a formal disclosure policy approved by the board of directors that addresses the licensed bank's approach for determining what disclosures it will make and the internal controls over the disclosure process. In addition, licensed banks should implement a process for assessing the appropriateness of their disclosures, including validation and frequency of them.

290. Senior management of licensed banks should ensure that appropriate verification of the information takes place.

291. The disclosures specified under this regulation will be required to be reviewed by the bank's external auditors. Such disclosures will not be required to be audited unless otherwise required by applicable accounting standards or other authorities.

292. All quantitative disclosures set out in this section should be made on a half yearly basis along with the relevant reviewed financial statement report, as well as on an annual basis in a separate section of the licensed bank's audited financial statements Qualitative disclosures, on the other hand, that provide a general summary of a licensed bank's risk management objectives and policies, reporting system and definitions should be published only on an annual basis in the same section of the licensed bank's audited financial statements referred to above. As such, all half yearly disclosures must be **reviewed**, where as, all annual disclosures must be **audited.**

293. In situations where disclosures required under this regulation is in conflict with those required under the International Accounting Standards (IAS), the International Financial Reporting Standards (IFRS) and/ or the listing requirements promulgated by securities regulators, licensed banks should rely on the latter requirements. In such situations, licensed banks should explain any material differences between the accounting or other disclosures and the disclosure required under this regulation. This explanation does not have to take the form of a line by line reconciliation. Moreover, a formal notification to the Central Bank of Kuwait would be required in such situation.

294. A licensed bank should decide which disclosures are relevant for it based on the materiality concept and subject to the concurrence of the Central Bank of Kuwait . For the licensed banks' guidance, information would be regarded as material if its omission or misstatement could change or influence the assessment or decision of a user relying on that information for the purpose of making economic decisions.

295. Non-compliance with these disclosure requirements could lead to an additional capital requirement such as not allowing the subject licensed bank to apply a lower weighting for a particular portfolio or increasing a particular risk weight for a specific portfolio(s).

(b) Proprietary and confidential information

296. Proprietary information encompasses information (for example on products or systems), that if shared with competitors would render a licensed bank's investment in these products/systems less valuable, and hence would undermine its competitive position. Information about customers is often confidential, in that it is provided under the terms of a legal agreement or counterparty relationship. This has an impact on what licensed banks should reveal in terms of information about their customer base, as well as details on their internal arrangements, for instance methodologies used, parameter estimates, data etc.

297. If a licensed bank considers that disclosure of certain information required below may prejudice seriously its position by making public information that is either proprietary or confidential in nature, it may not disclose those specific items subject to the prior approval of the Central Bank of Kuwait. In such situation, the Central Bank of Kuwait may require the disclosure of more general information about the subject matter of the requirement,

together with the fact that, and the reason why, the specific items of information have not been disclosed. This limited exemption is not intended to conflict with the disclosure requirements under the IAS and/ or IFRS.

(c) Disclosure Requirements

298. All licensed banks should disclose qualitative and quantitative information, based on the detailed requirements below, on their subsidiaries and significant investments, capital structure, capital adequacy, credit risk, market risk, operational risks, interest rate and equity risks in the banking book, and credit risk mitigation techniques used.

Information on subsidiaries and significant investments

299. The following information is related to the licensed bank's subsidiaries and significant investments:

a. Qualitative information

i. The name of the top corporate entity in the group to which this regulation applies.

ii. An outline of differences in the basis of consolidation for accounting and regulatory purposes, with a brief description of the entities within the group such as securities, insurance, other financial subsidiaries, commercial subsidiaries, significant minority equity investments in insurance, financial and commercial entities:

1. That are fully consolidated;
2. That are pro-rata consolidated;
3. That are given a deduction treatment;
4. Those from which surplus capital is recognised, and
5. That are neither consolidated nor deducted (e.g. where the investment is risk-weighted).

iii. Any restrictions, or other major impediments, on transfer of funds or regulatory capital within the group.

11- CAPITAL ADEQUACY RATIO
A) Circular No. (2/BS/184/2005) Regarding the Implementation of the Revised Capital Adequacy Ratio Basel (2).

b. Quantitative information

1. The aggregate amount of surplus capital of insurance subsidiaries (whether deducted or subjected to an alternative method) included in the capital of the consolidated group. Surplus capital in unconsolidated regulated subsidiaries is the difference between the amount of the investment in those entities and their regulatory capital requirements.

2. The aggregate amount of capital deficiencies in all subsidiaries not included in the consolidation i.e. that are deducted and the name(s) of such subsidiaries.

3. The aggregate amounts (e.g. current book value) of the licensed bank's total interests in insurance entities, which are risk-weighted rather than deducted from capital or subjected to an alternate group-wide method, as well as their name, their country of incorporation or residence, the proportion of ownership interest and, if different, the proportion of voting power in these entities. In addition, indicate the quantitative impact on regulatory capital of using this it's required to method versus using the deduction or alternate group-wide method.

Information related to the capital structure of a licensed bank

300. The following information is related to the licensed bank's consolidated capital structure:

a. Qualitative information

i. Summary information on the terms and conditions of the main features of all capital instruments, especially in the case of innovative, complex or hybrid capital instruments.

b. Quantitative information

1. The amount of Tier (1) capital, with separate disclosure of:

   a. Paid-up share capital/common stock;
   b. Reserves;
   c. Minority interests in the equity of subsidiaries;
   d. Innovative capital instruments;
   e. Other capital instruments;
   f. Surplus capital from insurance companies; and
   g. Other amounts deducted from Tier (1) capital, including goodwill and investments.

2. The total amount of Tier (2) and Tier (3) capital.
3. Other deductions from capital.
4. Total eligible capital after deductions.

Information on a licensed bank’s capital adequacy

301. The following disclosure requirements are related to the licensed bank’s capital adequacy assessment approach and capital requirements for all risk exposures:

a. Qualitative information

1. A summary discussion of the licensed bank's approach to assessing the adequacy of its capital to support current and future activities.

b. Quantitative information

1. Capital requirement for each standard portfolio disclosed separately.
2. Capital requirement for market risk under the standardised approach and/ or internal model approach.
3. Capital requirement for operational risk.
4. Total and Tier (1) capital ratios for:
   a. The licensed bank on a consolidated basis; and
   b. Each own subsidiary bank.

Information related to a licensed bank’s risk management

302. The following disclosure requirements are related to licensed banks’ risk management objectives and policies:

a. Qualitative information

1. For each separate risk area (e.g. credit, market, operational, banking book interest rate risk and equity) licensed banks should describe their risk management objectives and policies, including:
   a. Strategies and processes;
   b. The structure and organisation of the relevant risk management function;
   c. The scope and nature of risk reporting and/or measurement systems, and

11- CAPITAL ADEQUACY RATIO
A) Circular No. (2/BS/184/2005) Regarding the Implementation of the Revised Capital Adequacy Ratio Basel (2).

d. Policies for hedging and/or mitigating risk and strategies and processes for monitoring the continuing effectiveness of hedges/mitigants.

Information related to licensed banks' credit exposures

303. The following information includes all credit risk exposures of the licensed bank. The following information is in addition to the general credit risk information disclosed under the general risk management information required above.

a. Qualitative information

i. Definitions of past due and impaired (for accounting purposes);

ii. Description of approaches followed for specific and general allowances and statistical methods;

iii. Discussion of the licensed bank's credit risk management policy;

iv. Names of ECAIs used for each standard portfolio, plus reasons for any changes; and

v. A description of the process used to transfer public issue ratings onto comparable assets in the banking book.

b. Quantitative information

1. Total gross credit risk exposures (gross outstanding before any risk mitigation), plus average gross exposure over the period broken down by standard portfolio into funded and unfunded. Where the period end position is representative of the risk positions of the licensed bank during the period, average gross exposures need not be disclosed.

   Where average amounts are disclosed in accordance with an accounting standard or other requirement which specifies the calculation method to be used, that method should be followed. Otherwise, the average exposures should be calculated using the most frequent interval that an entity's systems generate for management, regulatory or other reasons, provided that the resulting averages are representative of the licensed bank's operations. The basis used for calculating averages need be stated only if not on a daily average basis.

2. Geographic distribution of exposures, broken down in significant areas by standard portfolio. Geographical areas may comprise individual countries, groups of countries or regions within countries. Licensed banks might choose to define the geographical areas based on the way the portfolio is geographically managed. The criteria used to allocate the loans to geographical areas should be specified.

3. Distribution of exposures, broken down by standard portfolio or by industry, broken down by funded and unfunded exposures.

4. Residual contractual maturity breakdown of the whole portfolio, broken down by standard portfolio.

5. By major industry or standard portfolio:

   a. Amount of impaired loans and if available, past due loans, provided separately;
   b. Specific and general provisions; and
   c. Charges for specific provision and charge-offs during the period.

6. Amount of impaired loans and, if available, past due loans provided separately broken down by significant geographic areas including, if practical, the amounts of specific and general provision related to each geographical area. The portion of general provision that is not allocated to a geographical area should be disclosed separately.

7. Reconciliation of changes in the provision for loan impairment.

8. The amount of credit exposure for each standard portfolio.

9. For exposure amounts after risk mitigation and credit conversion factor, amount of outstanding (rated and unrated) in each standard portfolio as well as those that are deducted.

Information related to credit risk mitigation

304. The following information details the credit risk mitigation techniques used by licensed banks:

a. Qualitative information

i. Policies and processes for, and an indication of the extent to which the licensed bank makes use of, on- and off-balance sheet netting;

ii. Policies and processes for collateral valuation and management;

iii. A description of the main types of collateral taken by the licensed bank;

iv. The main types of guarantor counterparty and their creditworthiness; and

v. Information about (market or credit) risk concentrations within the mitigation taken.

b. Quantitative Disclosures

i. For each separately disclosed standard portfolio, the total exposure (after, where applicable, on- or off- balance sheet netting) that is covered by:

1. Eligible financial collateral (after application of haircuts), and
2. Eligible guarantees.

Information related to market risk for trading portfolio, foreign exchange and commodities exposures

305. The following information is related to the licensed bank's risk measurement approach used for capital adequacy purposes and its market risk exposure. The following information is in addition to the general market risk information disclosed under the general risk management information required above.

a. Qualitative information

1. The portfolios covered by the standardised and internal model approaches separately.
2. For licensed banks using the internal model approach (IMA).

a. For each portfolio covered by the IMA:

(1) The characteristics of the model(s) used;

(2) A description of stress testing applied to the portfolio; and

(3) A description of the approach used for backtesting/ validating the accuracy and consistency of the model(s) and modelling processes.

b. The scope of acceptance by the Central Bank; and

b. Quantitative Disclosures

1. For licensed banks using the standardised approach, the capital requirements for:
   a. Interest rate risk;
   b. Equity position risk;
   c. Foreign exchange risk; and
   d. Commodity risk.
2. For trading portfolios under the IMA:
   a. The high, mean and low Value at Risk (VaR) values over the reporting period and period end; and
   b. A comparison of VaR estimates with actual gains/losses experienced by the licensed bank, with analysis of important "outliers" in backtest results.

Information related to operational risk

306. In addition to the general qualitative disclosure requirements related to risk management above, the measurement approach used (i.e., standardised approach) that the licensed bank uses for calculating its operational risk capital charge.

Information related to the licensed bank's equity position in the banking book

307. The following information is related to the licensed bank's equity position risk in its banking book. The following information is in addition to the general qualitative disclosure requirements related to risk management above.

a. Qualitative information

i. Differentiation between holdings on which capital gains are expected and those taken under other objectives including for relationship and strategic reasons; and

ii. Discussion of important policies covering the valuation and accounting of equity holdings in the banking book. This includes the accounting techniques and valuation methodologies used, including key assumptions and practices affecting valuation as well as significant changes in these practices.

b. Quantitative information

i. Value of investment disclosed in the balance sheet;

ii. The types and nature of investments, including the amount of investments that can be classified as publicly traded and privately held;

iii. The cumulative realised gains/(losses) arising from sales and liquidations in the reporting period;

iv. Total unrealised gains/(losses) recognised in the balance sheet but not through profit and loss account;

v. Total latent revaluation gains/(losses) in relation to investment recorded at cost which are not recognised either in the balance sheet or the profit and loss account;

vi. Any amounts of item (4) and (5) above included in Tier (1) and/or Tier (2) capital;

vii. Capital requirements broken down by appropriate equity groupings, consistent with the licensed bank's methodology.

Information related to the licensed bank's interest rate risk in the banking book (IRRBB)

308. The following information is related to the licensed bank's interest rate risk in its banking book. The following information is in addition to the general qualitative disclosure requirements related to risk management above.

a. Qualitative information

i. The nature of IRRBB and key assumptions, including assumptions regarding loan prepayments and behaviour of non-maturity deposits, and frequency of IRRBB measurement.

b. Quantitative information

i. The increase (decline) in earnings (or other relevant measure used by management) for upward and downward rate shocks according to management's method for measuring IRRBB, broken down by currency (as relevant).

Twelfth: Capital Adequacy Assessment Process: (1)

309. This section sets out the minimum requirements that all licensed banks should observe in establishing and managing the capital adequacy assessment process (CAAP).

310. CAAP is a regular process through which senior management assesses their bank's capital against its risk profile (type and level of risk). The purpose of CAAP is to complement the above capital adequacy requirements and the supervisory review process, and it enables senior management to ensure that their bank has adequate capital to support all material risks it is exposed to.

311. The main components of CAAP are:

    a. Board and senior management oversight;
    b. Comprehensive assessment of risks;
    c. Monitoring and reporting; and
    d. Internal control review.

a. Board and senior management oversight

312. Senior management of the licensed bank should develop a capital adequacy strategy which must be discussed and approved by the board. In constructing such strategy, the board and senior management should take into their consideration the following factors:

    a. The current risk profile of the licensed bank;
    b. The local and other relevant external regulations;
    c. The strategy and business plan with a focus on risk exposure growth (lending, investments and off-balance sheet);
    d. The current operating environment in terms of market practice, competition, consumer behaviour;
    e. Access to external capital sources;
    f. Future sources and uses of funds;
    g. The licensed bank's dividends policy; and
    h. The desired level of capital.

(1) According to circular No. (2/BS/245/2009) issued on 15/6/2009, Part 12 of the "Internal Capital Adequacy Assessment Process" (Paragraphs from 309 to 330) was replaced to become "Supervisory Review Process" included in Item (J) of this section

313. The licensed bank's board of directors has the responsibility for:

    a. Setting the licensed bank's tolerance for risks;

    b. Should ensure that management establishes a framework for assessing the various risks, develops a system to relate risk to the licensed bank's capital level, and establishes a method for monitoring compliance with internal policies;

    c. Should adopts and supports strong internal controls and written policies and procedures; and

    d. Should ensure that management effectively communicates these policies and procedures throughout the organisation.

b. Comprehensive assessment of risks

314. Each licensed bank should have in place adequate policies and procedures designed to ensure that the licensed bank identifies, measures, and reports all material risks it is exposed to.

315. The major risks that should be covered through CAAP are credit, market, operational, interest rate in the banking book and liquidity risks. Where such risks cannot be measured precisely, a process should be developed to estimate these risks.

1. For credit risk

316. The credit review assessment of capital adequacy, at a minimum, should cover four areas: risk grading, portfolio analysis/aggregation, large exposures and risk concentrations.

317. Risk grading is an important tool in monitoring credit risk. It should therefore be adequate to support the identification and measurement of risk from all credit exposures, and should be integrated into the licensed bank's overall analysis of credit risk and capital adequacy. The grading framework should provide detailed grading for all credit exposures, not only for problem assets. Loan loss provisions should be included in the credit risk assessment for capital adequacy.

318. The analysis of credit risk should adequately identify any weaknesses at the portfolio level, including any concentrations of risk. It should also adequately take into consideration the risks involved in managing credit concentrations.

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319. For inter-bank cross border exposures, the analysis of counterparty credit risk should include consideration of public evaluation of the relevant foreign supervisor's compliance with the Core Principles for Effective Banking Supervision.

2. Market risk

320. This assessment of market risk is based largely on the licensed bank's own measure of value-at-risk or the standardised approach for market risk. Emphasis should also be placed on the licensed bank conducting stress testing in evaluating the adequacy of capital to support the trading function.

3. For operational risk

321. Similar rigour should be applied to the management of operational risk, as is done for the management of other significant banking risks. The failure to properly manage operational risk can result in a misstatement of a licensed bank's risk/return profile and expose it to significant losses.

322. Each licensed bank should develop a framework for managing operational risk and evaluate the adequacy of capital based on this framework. The framework should cover the licensed bank's appetite and tolerance for operational risk, as specified through the policies for managing this risk, including the extent and manner in which operational risk is transferred outside the licensed bank. It should also include policies outlining the licensed bank's approach to identifying, assessing, monitoring and controlling/mitigating operational risk.

4. Interest rate risk in the banking book

323. The measurement process should include all material interest rate positions of the licensed bank and consider all relevant repricing and maturity data. Such information will generally include current balance and contractual rate of interest associated with the instruments and portfolios, principal payments, interest reset dates, maturities, the rate index used for repricing, and contractual interest rate ceilings or floors for adjustable-rate items. The system should also have well-documented assumptions and techniques.

5. Liquidity risk

324. Licensed bank's capital positions can have an effect on their ability to obtain liquidity, especially in a crisis. Each licensed bank must therefore have adequate systems for measuring, monitoring and controlling liquidity risk. It should evaluate the adequacy of capital given its own liquidity profile and the liquidity of the markets in which it operates.

6. Other risks

325. Although other risks, such as reputational and strategic risks, are not easily measurable, the Central Bank of Kuwait expects all licensed banks to further develop techniques for managing all aspects of these risks.

c. Monitoring and reporting

326. Each licensed bank should establish an adequate system for monitoring and reporting risk exposures and assessing how its changing risk profile affects the need for capital.

327. The licensed bank's senior management or board of directors should, on a regular basis, receive reports on the bank's risk profile and capital needs. These reports should allow senior management to:

a. Evaluate the level and trend of material risks and their effect on capital levels;

b. Evaluate the sensitivity and reasonableness of key assumptions used in the capital assessment measurement system;

c. Determine that the licensed bank holds sufficient capital against the various risks and is in compliance with established capital adequacy strategy and targets; and

d. Assess its future capital requirements based on the bank's reported risk profile and make necessary adjustments to the licensed bank's business plan accordingly.

e. Internal controls and risk management review

328. A process of internal controls, reviews and audit to ensure the integrity of the overall management process should be in place.

329. Effective control of the capital assessment process includes an independent review and, where appropriate, the involvement of internal or external audits. The licensed bank's board of directors has a responsibility to ensure that management establishes a system for assessing the various risks, develops a system to relate risk to the bank's capital level, and establishes a method for monitoring compliance with internal policies. The board should regularly verify whether its system of internal controls is adequate to ensure well-ordered and prudent conduct of business.

330. Each licensed bank should conduct annual reviews of its internal controls and risk management process to ensure its integrity, accuracy, and reasonableness. Areas that should be reviewed include:

a. Appropriateness of the licensed bank's capital assessment process given the nature, scope and complexity of its activities;

b. Identification and management of large exposures and risk concentrations;

c. Accuracy and completeness of data inputs into the licensed bank's assessment process;

d. Reasonableness and validity of scenarios used in the capital adequacy assessment process; and

e. Stress testing and analysis of assumptions and inputs.

Forms and instructions

General instructions

331. Specific instructions for completing the forms are provided with the forms.

332. All amounts should be expressed in thousands of Kuwaiti Dinars equivalents.

333. The capital adequacy forms should be prepared in accordance with these regulations. The forms are to be completed and submitted as applicable within 14 days of the end of each quarter.

334. Each capital adequacy returns should be reviewed by the licensed bank's external auditors.

Specific instructions related to market risk capital charge

335. Net positions (also known as open positions) should be arrived at by offsetting long and short positions. Long positions are denoted as positive values and short positions are denoted as negative values. Therefore, to arrive at the net position the long and short positions should be added together (i.e., the sum of +8 and –2 is +6).

336. Gross positions should be arrived at by adding the absolute value of a short position and the long position. Absolute value is denoted by a vertical bar on both sides of a number or column letter (i.e., the sum of +8 and –2 is +10).

337. Separate capital calculations are made for interest rate position risk, equities position risk, foreign exchange risk and commodities risk. In addition, there is a separate from for reporting the capital charge for options.

Annexes:

Annex (A): Definitions

Abbreviations and other terms used in this regulation, including all annexes have the following meanings:

1. **Asset-backed** commercial paper (ABCP) program: Issues asset-backed commercial paper with an original maturity of not more than one year that is backed by assets or underlying pool of exposures held in a bankruptcy-remote, special purpose entity (SPE or SIV).
2. **At-The-Money**: An option is at-the-money when the price of the underlying instrument is equal to the option's exercise price.
3. **Back-Testing**: Is the comparison of actual trading results with computer model-generated risk measures primarily to gauge the quality and accuracy of risk measurement models.
4. **"Bank":** Means any bank fully recognized as such by the appropriate regulator of the country in which they are registered except such a bank which:

a. In the opinion of the Central Bank of Kuwait, is not adequately supervised by the relevant banking supervisory authority; or

b. The license or other authorization of which to carry on banking business is for the time being suspended.

5. **Banking Groups**: Are groups that engage predominantly in banking activities and/ or registered as a bank in the relevant jurisdiction.

6. **Basis Risk**: Is the risk that the relationship between the prices of two similar, but not identical, instruments will change. Thus, even if maturities are perfectly matched, basis risk could remain.

7. **Building-Block Approach**: Is a method for measuring change price risk which disaggregates risk specific to a security/issuer and general market risk.

8. **"CCF"**: Means credit conversion factor, by which the principal amount of an off-balance sheet exposure is multiplied to derive the credit equivalent amount.

9. **Clean-up call**: Is an option that permits the securitisation exposures to be called before all of the underlying exposures or securitization exposures have been repaid. In the case of traditional securitisations, this is generally accomplished by repurchasing the remaining securitisation exposures once the pool balance or outstanding securities have fallen below some specified level.

10. **Confidence Level:** Is the degree of protection observed against price movements judged appropriate in setting a capital requirement.

11. **Convertible Bond**: Is a bond which gives the investor the option to switch into equity at a fixed conversion price.

12. **Counterparty Risk**: Is the risk that the counterparty to a financial contract will not meet the terms of the contract.

13. **Credit enhancement:** Refers to a contractual arrangement in which a bank retains or assumes securitisation exposure (like an investing bank) and in substance, provides some degree of protection to other investors of the transaction by way of enhancement of the credit quality of the securitization structure / credit or the rating of the securitized instrument (due to association with a recognized banking institution).

A credit enhancer can, if contractually agreed, provide liquidity facility or cash advance services to the securitisation structure as an added degree of protection.

14. **Credit-enhancing interest-strip only (I/O)**: Is an on-balance sheet asset that:

    a. Represents a valuation of cash flows related to future margin income, and

    b. Is subordinated.

15. **Cross default clause**: Is a clause which says that the loan goes into default if any of the borrower's other loans go into default. It is intended to prevent one creditor getting an advantage over other creditors, e.g. obtaining full repayment through the courts.

16. **Currency Swap**: Is a transaction involving an exchange of principal of two different currencies. Interest payments are exchanged over the life of the contract and the principal amounts are repaid either at maturity or according to a predetermined amortisation schedule.

17. **"Corporate"**: Refers to any proprietorship, partnership or limited company that is neither a PSE and a bank nor borrower within the definition of regulatory retail exposures. For capital adequacy purposes, the term also includes insurance companies.

18. **"CRM"**: Means credit risk mitigation, which refers to techniques banks use to reduce the credit risk of their exposures.

19. **"Credit Quality Grade":** Means a grade represented by the numerals 1, 2, 3, 4, 5 or 6, to which the credit assessment of an ECAI for a credit exposure is mapped for determining the appropriate risk weight for a rated exposure.

20. **Delta**: Is the expected change of an option's price as a proportion of a small change in the price of the underlying instrument. An option whose price changes by $1 for every $2 change in the price of the underlying instrument has a delta of 0.5. The delta rises toward 1.0 for options that are deep-in-the-money and approaches 0 for deep out-of-the-money options.

21. **"Domestic Currency Claim"**: Means any claim which is denominated and funded in the currency used domestically in the place in which the obligor is incorporated.

22. **Early amortisation provisions**: Are mechanisms that, once triggered, allow investors to be paid out prior to the originally stated maturity of the securities issued. For risk- based capital purposes, an early amortisation provision will be considered either controlled or non-controlled. A controlled early amortisation provision must meet all of the following conditions.

    a. The originating bank must have an appropriate capital / liquidity plan in place to ensure that it as sufficient capital and liquidity available in the event of an early amortisation.

    b. Throughout the duration of the transaction, including the amortisation period, there is the same pro rata sharing of interest, principal, expenses, losses and recoveries based on the bank's and investors relative shares of the receivables outstanding at the beginning of each month.

    c. The bank must set a period for amortisation that would be sufficient for at least 90% of the total debt outstanding at the beginning of the early amortisation period to have been repaid or recognised as in default; and

    d. The pace of repayment should not be any more rapid than would be allowed by straight-line amortisation over the period set out in criterion (c) above.

    An early amortisation provision that does not satisfy the conditions for a controlled early amortisation provision will be treated as a non-controlled early amortisation provision.

23. **"ECAI"**: Means an external credit assessment institution recognised by the Central Bank of Kuwait for capital adequacy purposes.

24. **Excess Spread**: Is generally defined as gross finance charge collections and other income received by the trust or special purpose entity (SPE) minus certificate interest, servicing fees, charge-offs, and other senior trust or SPE expenses.

25. **"Financial entities"**: Are defined as those entities that are involved in financial leasing, issuing credit cards, portfolio management, investment advisory, custodial and safekeeping services and other similar activities that are ancillary to the business of banking.

26. **Gamma**: Is the sensitivity of an option's delta to small changes in the price of the underlying; alternatively, the sensitivity of a delta-hedged position to large unit changes in the price of the underlying.

27. **General Market Risk**: Is the risk of loss arising from adverse changes in market prices, i.e., general market movement such as a change in interest rates or effect of official policy on market prices.

28. **Gross income**: Is defined as net interest income plus net non-interest income, gross of operating expenses (including fees paid for outsourcing services) and before any provisions. Specifically, it should:

    a. Include net interest income, gains less losses arising from foreign exchange operations and trading in derivatives, income from securities investment held for trading (i.e. securities carried at fair value through profit or loss under IAS 39), dividend from associated companies and other equity investments, income from fees and commissions (including fees received for insourcing service), and other income arising from ordinary activities of the bank,

    b. But exclude realised profits/losses from the sale of non-trading investments (i.e. securities classified as "held to maturity" or "available for sale" under IAS 39), profit/loss arising from extraordinary or irregular items (e.g. profit from sale of fixed assets and income derived from insurance claims).

29. **Holding Period**: Is the length of time that a financial institution is assumed to hold a given financial instrument for the purpose of calculating the sensitivity of price volatility.

30. **Host supervisor**: Is the supervisor of overseas entities of Kuwaiti banks.

31. **Implicit Support**: Refers to any support provided by a bank whether directly or indirectly to investors in a securitization in excess of its contractual obligation.

32. **Interest Rate Risk**: Is the risk that changes in market interest rates might adversely affect an institution's financial condition.

33. **In-The-Money**: An Option contracts are in the money when there is a net financial benefit to be derived from exercising the option immediately. A call option is in the money when the price of the underlying instrument is above the exercise price and a put option is in the money when the price of the underlying instrument is below the exercise price.

34. Liquidity facility provided as per a contractual agreement, by an entity, ensures sufficient liquidity of a securitisation structure (for senior and mezzanine tranches) in the event where the cash received by the SPE from the performance of the underlying assets is delayed compared to the payments to be made to investors.

35. **Long Option Position**: Is the position of a trader who has purchased an option regardless of whether it is a put or a call.

36. **Marking-To-Market**: Is the process of revaluing a portfolio on the basis of prevailing market prices.

37. **Matched Weighted Position:** Is the smaller of the sum of the risk weighted long positions or the sum of the risk weighted short positions within a time band or a zone or between zones.

38. **"MDB"**: Means a multilateral development bank, which refers to any bank or lending or development body established by agreement between, or guaranteed by, two or more countries, territories or international organisations other than for purely commercial purposes.

39. **Negative pledge:** Is a clause which puts the loan into default if the borrower gives any further charge over its assets.

40. **Observation Period**: Is the period over which it is judged appropriate to review historical data in setting a capital requirement. For example, the requirement might be set according to observed price changes over the past five years.

41. **Off-Balance-Sheet Activities**: Are bank's business that does not generally involve booking assets or liabilities. Examples include trading in swaps, options, futures and foreign exchange forwards, and the granting of standby commitments and letters of credit.

42. **Operational Risk**: Is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. This definition includes legal risk, but excludes strategic and reputational risk.

43. **Originating Bank** is:

    a. An entity that directly or indirectly was involved in the original agreement which created the underlying exposures included in the securitization; or

b. An entity that serves as a sponsor of an asset-backed commercial paper (ABCP) conduit or similar programme that acquires exposures from third-party entities. In the context of such programmes, a bank would generally be considered a sponsor and, in turn, an originator if it, in fact or in substance, manages or advises the programme, places securities into the market, or provides liquidity and/or credit enhancements.

44. **OTC (Over-The-Counter)**: Is trading in financial instruments transacted off organized exchanges. Generally the parties negotiate all details of the transactions, or agree to certain simplifying market conventions.

45. **Out-of-The-Money**: An option contract is out of the money when there is no benefit to be derived from exercising the option immediately. A call option is out of the money when the price of the underlying is below the option's exercise price. A put option is out of the money when the price of the underlying is above the option's exercise price.

46. **"Past due"**: Is a term used in this regulation to describe any exposure that is more than 90 days past due or those against which specific provision has been allocated.

47. **"Principal Amount":** Means the amount of any outstanding claim (excluding any interest and other expenses) on, or contingent liability in respect of, the relevant counterparty.

48. **"PSE"**: Means a public sector entity which is specified as such either by the Central Bank of Kuwait ("domestic PSE") or by an overseas banking supervisory authority ("foreign PSE"). Domestic PSEs include those entities owned by the government, excluding the subsidiaries of such institutions undertaking commercial activities.

49. **"Recognised exchanges"**: Means those stock exchanges recognized by the Central Bank.

50. **"Repo-style transactions":** Means transactions involving the sale and repurchase ("repo") of assets, purchase and resale ("reverse repo") of assets, as well as securities lending and securities borrowing. For capital adequacy purposes, the term "repo-style transactions" is generally taken to refer to any of the following transactions of an bank:

a. *Sale & repurchase ("repo") of securities* – the bank agrees to sell securities to a third party for cash with a commitment to repurchase the securities at an agreed price on an agreed future date.

b. *Securities lending* – the bank lends securities to a third party and receives either cash or other securities from that party in exchange as collateral.

c. *Purchase and resale ("reverse repo") of securities* – the bank agrees to acquire securities from a third party for cash with a commitment to resell the securities at an agreed price on an agreed future date (i.e. the reverse of repo transactions).

d. *Securities borrowing* – the bank borrows securities from a third party and gives cash or other securities to that party in exchange as collateral.

51. **Restrictive covenant**: Is a term of contract that directly, or indirectly, could lead to early repayment of the debt.

52. **"Securities firm"**: Means any entity licensed and supervised by relevant securities regulator. Domestically, these include all non banking financial entities including investment companies and funds that are under the supervision of the Central Bank of Kuwait. Securities brokers are also included under this definition.

53. **Securitisation exposure:** The exposures of a bank which are exposed to securitisation are referred to as securitisation exposures. These exposures get created when banks invest in securities issued on an underlying asset pool (the securitised pool). Hence the exposures are said to be exposed to securitisation. Securitisation exposures include:

    a. On-balance sheet exposure to securities (which are issued based on the pool of securitized exposures) and can include but is not limited to asset-backed securities, mortgage-backed securities and collateralized debt obligations, or

    b. Any off-balance sheet exposure to a securitisation which can include but is not limited to credit enhancements, liquidity facilities, credit risk mitigants (guarantees, derivatives) or tranched cover.

54. **Short Option Position**: Is the position of a trader who has sold or written an option. The writer's maximum potential profit is the premium received.

55. **Simulation**: Is a mathematical technique for measuring the likely performance of a given portfolio for changes in certain parameters such as market interest rates or foreign exchange rates.

56. **"Sovereign":** Means the central government or the Central Bank of Kuwait, or a specified international organisation. "Specified international organisations" include:

    a. The Bank for International Settlements;

    b. The International Monetary Fund;

    c. The European Central Bank;

    d. The European Commission; and other entities as may be specified by the Central Bank from time to time.

57. **Special purpose entity (SPE):** Means any corporation, trust, or other entity constituted or established for a specific purpose with the following key characteristics:

    a. The activities of a SPE are limited to those for accomplishing the purpose of the corporation, trust or other entity as the case may be; and

    b. It is structured in a manner intended to isolate the corporation, trust or entity as the case may be, from the credit risk of an originator or entity selling the underlying exposure or pool of exposures;

58. "**Specific provisions"**: Include partial write-offs and cover those set aside for bad and doubtful debts, country risk and depreciation of fixed assets.

59. **Specific Risk:** Is the risk of loss caused by an adverse price movement of a debt instrument or security due principally to factors related to the issuer (e.g. risk of default).

60. **Step-ups**: Issues of subordinated debt can contain options for the bank to repay the debt (in the case of perpetual debt), or prepay the debt prior to its maturity date (in the case of term debt). Failure to exercise the option sometimes leads to an increase in the interest rate paid on the debt. This is called a step-up.

61. **Structural Positions include the following:**

   a. Any position arising from an instrument which qualifies to be included in the bank's capital base;

   b. Any position entered into in relation to the net investment of a capital nature in a self-sustaining subsidiary, the accounting consequence of which is to reduce or eliminate what would otherwise be a movement in the foreign currency translation reserve; and

   c. Investments in overseas subsidiaries which are fully deducted from bank's capital for capital adequacy purposes.

62. **Subordinated loans**: Is a debt instrument issued by financial institutions which in liquidation is subordinated to claims by general creditors but which ranks above ordinary and preferred shares.

63. **Traditional Securitisation is a structure where-in**:

   a. Cash flow from an underlying pool of exposures is used to service at least two different stratified risk positions or tranches reflecting different degrees of credit risk (tranches are supported by the underlying pool of exposures / assets);

   b. Payments to the investors depend upon the performance of the specified underlying exposures, as opposed to being derived from an obligation of the entity originating those exposures;

   c. Junior tranches can absorb losses without interrupting contractual payments to more senior tranches.

64. Tranche refers to a segment of the credit risk corresponding to an underlying exposure or pool of exposures where in the risk of credit loss for each tranche is different without considering the credit protection provided to that tranche.

65. Tranched cover refers to transferring a portion of risk of an exposure in one or more tranches to a protection seller(s) where in the bank retains some level of risk of the loan and the risk transferred and the risk retained are of different seniority.

66. Underlying pool of exposures being securitized may include but is not limited to loans, commitments, asset and mortgage-backed securities, corporate bonds, equity / private equity. The underlying pool may include more than one type of exposure.

67. **Value-At-Risk (VaR)**: Is the estimate of the likely maximum amount that could be lost on a bank's portfolio with a certain degree of statistical confidence.

68. **Volatility**: Is a measure of the variability of the price of an asset, usually defined as the annualized standard deviation of the natural log of asset prices.

Annex (B): Application of External Credit Assessment

Application of external credit assessment

1. There are a number of general principles that licensed banks should follow for the selection of the appropriate external credit assessment for risk-weighting a claim. These principles will give further guidance on:

    a. Which assessment to choose if more than one external assessment are applicable to a claim;

    b. When to use the assessment of an issuer or that of an issue;

    c. Whether a foreign currency assessment can be used to determine the risk weight of a claim denominated in domestic currency; and

    d. The use of short-term and long-term assessments.

2. For each of the relevant portfolios, risk weights are mapped to a scale of uniform Credit Quality Grades represented by the numerals of 1 to 5 or 6. The scale is to provide a common platform into which different notations used by different ECAIs (such as AA+ of Standard & Poor's, Aaa of Moody's and AA+ of Fitch) can be mapped. In addition, specific risk weights are assigned to unrated exposures under each of the portfolios. Also, there is a separate scale for risk-weighting rated short-term paper issued by banks and corporates.

3. The Central Bank of Kuwait have selected Moody's, Standard &Poor's and Fitch IBCA for the purpose of assigning risk weights to exposures. Any other ECAIs the licensed banks would like to utilize for this purpose then the licensed banks must ensure that these ECAIs satisfy the following six criteria and then apply to the Central Bank of Kuwait to obtain the prior approval:

   a. Objectivity: The methodology for assigning credit assessments must be rigorous, systematic, and subject to some form of validation based on historical experience. Moreover, assessments must be subject to ongoing review and responsive to changes in financial condition. Before being recognised by the Central Bank of Kuwait, an assessment methodology for each market segment, including rigorous backtesting, must have been established for at least one year and preferably three years.

   b. Independence: An ECAI should be independent and should not be subject to political or economic pressures that may influence the rating. The assessment process should be as free as possible from any constraints that could arise in situations where the composition of the board of directors or the shareholder structure of the assessment institution may be seen as creating a conflict of interest.

   c. International access/Transparency: The individual assessments should be available to both domestic and foreign institutions with legitimate interests and at equivalent terms. In addition, the general methodology used by the ECAI should be publicly available.

   d. Disclosure: An ECAI should disclose the following information: its assessment methodologies, including the definition of default, the time horizon, and the meaning of each rating; the actual default rates experienced in each assessment category; and the transitions of the assessments, e.g. the likelihood of (AA) ratings becoming (A) over time.

   e. Resources: An ECAI should have sufficient resources to carry out high quality credit assessments. These resources should allow for substantial ongoing contact with senior and operational levels within the entities assessed in order to add value to the credit assessments. Such assessments should be based on methodologies combining qualitative and quantitative approaches.

f. Credibility: To some extent, credibility is derived from the criteria above. In addition, the reliance on an ECAI's external credit assessments by independent parties (investors, insurers, trading partners) is evidence of the credibility of the assessments of an ECAI. The credibility of an ECAI is also underpinned by the existence of internal procedures to prevent the misuse of confidential information. In order to be eligible for recognition, an ECAI does not have to assess firms in more than one country.

4. For illustration, annexes (C) to (J) are a set of tables summarising how the notations used by Moody's, Standard & Poor's and Fitch IBCA are mapped to the uniform Credit Quality Grades.

5. Because there is a potential for ECAIs to use unsolicited ratings to put pressure on licensed banks to obtain solicited ratings, licensed banks shall not be allowed to use unsolicited ratings.

6. Licensed banks must use the chosen ECAIs and their ratings consistently for each type of claim, for both risk weighting and risk management purposes. Licensed banks will not be allowed to "cherry-pick" the assessments provided by different ECAIs.

7. Licensed banks must disclose ECAIs that they use for the risk weighting of their assets by type of claims, the risk weights associated with the particular rating grades as determined in this regulation through the mapping process as well as the aggregated risk-weighted assets for each risk weight based on the assessments of each eligible ECAI.

8. External assessments for one entity within a corporate group cannot be used to risk weight other entities within the same group.

Multiple assessments

9. If there is only one assessment by an ECAI chosen by a licensed bank for a particular claim, that assessment should be used to determine the risk weight of that claim.

10. In case there are multiple credit assessments by different ECAIs for a claim, the following principles shall apply:

    a. If there are two assessments by ECAIs which attract different risk weights, the assessment that results in a higher risk weight should be used.

    b. If there are three or more assessments with different risk weights, the assessments corresponding to the two lowest risk weights should be referred to and the higher of those two risk weights should be applied.

Issuer versus issue assessments

11. Where a licensed bank holds a particular issue of debt instrument that has an issue-specific assessment, the licensed bank can use the assessment to risk-weight its claim against the instrument. Where the licensed bank's claim is not an investment in a specific assessed issue, the following general principles shall apply:

    a. Where the borrower has a specific assessment for an issued debt instrument that attracts a risk weight lower than that for an unrated claim (i.e. a high quality assessment), such an assessment may be applied to the bank's unassessed claim which ranks pari passu or senior to the assessed issue in all respects. If not, the credit assessment cannot be used and the unassessed claim will receive the risk weight for unrated claims.

    b. Where the borrower has an issuer assessment, this assessment typically applies to senior unsecured claims on that issuer. Consequently, only senior claims on that issuer will benefit from a high quality issuer assessment. Other unassessed claims of a highly assessed issuer will be treated as unrated.

    c. Where either the issuer or a single issue of debt instrument has a low quality assessment, i.e. one that attracts a risk weight equal to or higher than that for unrated claims, any unassessed claim on the same borrower will be assigned the same risk weight as is applicable to the low quality assessment.

12. Whether the bank intends to rely on an issuer assessment or an issue-specific assessment, the assessment must take into account and reflect the entire amount of credit risk exposure the bank has with regard to all payments owed to it. For example, if a bank is owed both principal and interest, the assessment must fully take into account and reflect the credit risk associated with repayment of both principal and interest.

Domestic currency and foreign currency assessments

13. In circumstances where unrated exposures are risk-weighted based on the rating of an equivalent exposure to that borrower, the general rule is that foreign currency ratings would be used for exposures in foreign currency. Domestic currency ratings, if separate, would only be used to risk-weight claims denominated in the domestic currency.

14. However, when an exposure arises through a bank's participation in a loan that has been extended to, or has been guaranteed against convertibility and transfer risk, by specified MDBs, its convertibility and transfer risk is considered to be effectively mitigated. In such cases, the borrower's domestic currency rating may be used for capital adequacy purposes instead of its foreign currency rating. The portion of the loan not benefiting from such a guarantee will however be risk-weighted based on the foreign currency rating.

Short-term and long-term assessments

15. Short-term assessments may only be used for short-term claims on banks and corporates. Short-term assessments can only be used to derive risk weights for claims arising specifically from the rated short-term facilities and cannot be generalized to other short term claims. In no event should they be used to support a risk weight for an unrated long-term exposure.
16. If a rated short-term issue attracts a 50% risk weight, other unrated short-term exposures to the same issuer cannot attract a risk weight lower than 100%. If an issuer has a short-term facility with an assessment that attracts a risk weight of 150%, all unrated exposures to the issuer, whether long-term or short-term, should also receive a 150% risk weight, unless the licensed bank uses recognised CRM techniques for such claims.

Annex (C): Table for Mapping Notations of ECAIs into the Credit Quality Grades for Claims on Sovereigns

Sovereigns Credit Quality Grades	Risk Weights (%)	S&P	Moody's	Fitch
1	0	AAA	Aaa	AAA
		AA+	Aa1	AA+
		AA	Aa2	AA
		AA-	Aa3	AA-
2	20	A+	A1	A+
		A	A2	A
		A-	A3	A-
3	50	BBB+	Baa1	BBB+
		BBB	Baa2	BBB
		BBB-	Baa3	BBB-
4	100	BB+	Ba1	BB+
		BB	Ba2	BB
		BB-	Ba3	BB-
5	100	B+	B1	B+
		B	B2	B
		B-	B3	B-
6	150	CCC+	Caa1	CCC+
		CCC	Caa2	CCC
		CCC-	Caa3	CCC-
		CC	Ca	CC
		C	C	C
		D		D
Unrated	100			

Annex (D): Table for Mapping Notations of ECAIs into the Credit Quality Grades for Claims on Banks

Banks Credit Quality Grade	Risk Weight	Risk Weight for Short-term Claims	S & P	Moody's	Fitch
1	20%	20%	AAA	Aaa	AAA
			AA+	Aa1	AA+
			AA	Aa2	AA
			AA-	Aa3	AA-
2	50%	20%	A+	A1	A+
			A	A2	A
			A-	A3	A-
3	50%	20%	BBB+	Baa1	BBB+
			BBB	Baa2	BBB
			BBB-	Baa3	BBB-
4	100%	50%	BB+	Ba1	BB+
			BB	Ba2	BB
			BB-	Ba3	BB-
5	100%	50%	B+	B1	B+
			B	B2	B
			B-	B3	B-
6	150%	150%	CCC+	Caa1	CCC+
			CCC	Caa2	CCC
			CCC-	Caa3	CCC-
			CC	Ca	CC
			C	C	C
			D		D
Unrated	50%	20%			

Annex (E): Table for Mapping Notations of ECAIs into the Credit Quality Grades for Claims on Corporates

Corporates Credit Quality Grades	Risk Weight	S & P	Moody's	Fitch
1	20%	AAA	Aaa	AAA
		AA+	Aa1	AA+
		AA	Aa2	AA
		AA-	Aa3	AA-
2	50%	A+	A1	A+
		A	A2	A
		A-	A3	A-
3	100%	BBB+	Baa1	BBB+
		BBB	Baa2	BBB
		BBB-	Baa3	BBB-
4	100%	BB+	Ba1	BB+
		BB	Ba2	BB
		BB-	Ba3	BB-
5	150%	B+	B1	B+
		B	B2	B
		B-	B3	B-
6	150%	CCC+	Caa1	CCC+
		CCC	Caa2	CCC
		CCC-	Caa3	CCC-
		CC	Ca	CC
		C	C	C
		D		D
Unrated	100%			

Annex (F): Table for Mapping Short Term Assessment Notations of ECAIs into the Credit Quality Grades for Short Term Claims on Banks and Corporates

Short-term Credit Quality Grades	Risk Weight	S & P	Moody's	Fitch
1	20%	A-1	P-1	TBD
2	50%	A-2	P-2	TBD
3	100%	A-3	P-3	TBD
4	150%	Others*	Others*	TBD

- **This category 'others' includes all non-prime and B or C ratings.**

Annex (G): Table for Mapping Notations of ECAIs into the Credit Quality Grades for First and Second to Default Credit Derivatives (Long Term Rating Category)

Credit Quality Grades (Long Term Rating Category	Risk Weight	S & P	Moody's	Fitch
1	20%	AAA	Aaa	AAA
		AA+	Aa1	AA+
		AA	Aa2	AA
		AA-	Aa3	AA-
2	50%	A+	A1	A+
		A	A2	A
		A-	A3	A-
3	100%	BBB+	Baa1	BBB+
		BBB	Baa2	BBB
		BBB-	Baa3	BBB-
4	350%	BB+	Ba1	BB+
		BB	Ba2	BB
		BB-	Ba3	BB-
5	Deduction	B+	B1	B+
		B	B2	B
		B-	B3	B-
6	Deduction	CCC+	Caa1	CCC+
		CCC	Caa2	CCC
		CCC-	Caa3	CCC-
		CC	Ca	CC
		C	C	C
		D		D

Annex (H): Table for Mapping Notations of ECAIs into the Credit Quality Grades for First and Second to Default Credit Derivatives (Short Term Rating Category)

Credit Quality Grades (Short Term Rating Category)	Risk Weight	S & P	Moody's	Fitch
1	20%	A-1	P-1	TBD
2	50%	A-2	P-2	TBD
3	100%	A-3	P-3	TBD
4	Deduction	Others*	Others*	TBD

- **This category 'others' includes all non-prime and B or C ratings.**

Annex (I): Table for Mapping Notations of ECAIs into the Credit Quality Grades for Securitisation Exposures (Long Term Rating Category)

Credit Quality Grades for Securitisation Exposures (Long Term Rating)	Risk Weight	S & P	Moody's	Fitch
1	20%	AAA	Aaa	AAA
		AA+	Aa1	AA+
		AA	Aa2	AA
		AA-	Aa3	AA-
2	50%	A+	A1	A+
		A	A2	A
		A-	A3	A-
3	100%	BBB+	Baa1	BBB+
		BBB	Baa2	BBB
		BBB-	Baa3	BBB-
4	350% for Investor, but deduction for Originating Bank	BB+	Ba1	BB+
		BB	Ba2	BB
		BB-	Ba3	BB-
5	Deduction	B+	B1	B+
		B	B2	B
		B-	B3	B-
6	Deduction	CCC+	Caa1	CCC+
		CCC	Caa2	CCC
		CCC-	Caa3	CCC-
		CC	Ca	CC
		C	C	C
		D		D
Unrated	Deduction			

Annex (J): Table for Mapping Notations of ECAIs into the Credit Quality Grades for Securitisation Exposures (Short Term Rating Category)

Credit Quality Grades for Securitisation Exposures (Short Term Rating)	Risk Weight	S & P	Moody's	Fitch
1	20%	A-1	P-1	TBD
2	50%	A-2	P-2	TBD
3	100%	A-3	P-3	TBD
4	Deduction	Others*	Others*	TBD
Unrated	Deduction			

- **This category 'others' includes all non-prime and B or C ratings.**

Annex (K): Explanatory Notes

The explanatory notes are provided to give examples on the calculation of certain market risk related items set out in these regulations and the calculation of capital adequacy ratio. In particular, this annex contains five examples on market risk capital charge calculation and one example on the calculation of capital adequacy ratio.

Example (1): Calculation of Capital Adequacy Ratio

1. If a bank had: Tier (1) capital of 1000
   Tier (2) capital of 300
   Tier (3) capital of 800

   The bank has credit risk weighted assets of 7,500, market risk capital charge of 525 and operational risk capital charge of 240.

   The bank has to first: Multiply the measure of market risk and operational risk by 8.33 to determine the risk weighted assets (see Table below).

   After the calculation of the minimum capital charge, the amount of capital that is eligible for meeting capital adequacy requirements must be computed starting with credit and operational risks, covered in this example by (840) tier (1) capital and (300) tier (2) capital.

   This leaves (160) tier (1) capital available to support the bank's market risk requirements, which – because of the 250% rule-means that only (400) of tier (3) capital is eligible. Because the bank only needs to use (150) tier (1) capital and (375) tier (3) capital to meet its market risk capital requirement, the bank has (10) tier (1) capital and (25) tier (3) capital that is unused but eligible for future market risk requirements.

2. For calculating the capital ratio, excess tier (1) capital should be taken into account as it can be used to meet credit and/or market risk requirements. Therefore, the capital ratio is calculated by:

   Dividing the eligible capital (excluding unused tier (3) by the total (notional) risk assets (1,700/13,872.45 = 12.25%). Excess tier (3) capital which is unused but eligible can also be calculated as an excess tier (3) capital ratio (375/11,872.45 = 0.25%).

11- CAPITAL ADEQUACY RATIO
A) Circular No. (2/BS/184/2005) Regarding the Implementation of the Revised Capital Adequacy Ratio Basel (2).

Based on the data given above, the bank's capital adequacy ratio can be calculated as follows:

(KD)

Risk assets	**Minimum Capital charge of 12%**	**Available capital**	**Minimum capital for meeting risks**	**Eligible capital (excluding unused Tier 3)**	**Unused but eligible Tier (3)**	**Unused But not Eligible Tier (3)**
Credit risk (7,500)	900	Tier (1) : 1,000 Tier (2) : 300 Tier (3) : 800	Tier (1): 600 Tier (2): 300	Tier (1): 1,000 Tier (2) : 300 Tier (3) : 400	35	400
Operational Risk 1,999.2 (240 x 8.33)	240		Tier (1): 240			
Market risk 4,373.25 (525 x 8.33)	525		Tier (1): 160 Tier (3) : 365			
				Capital ratio : 1,700/ 13,872.45 = 12.25%		

11- CAPITAL ADEQUACY RATIO
A) Circular No. (2/BS/184/2005) Regarding the Implementation of the Revised Capital Adequacy Ratio Basel (2).

Example (2): Calculating general market risk charge on interest rate position under the simplified method

A hypothetical bank has the following given positions designated as trading:

1. Qualifying bond: $13.33 million (market value), remaining maturity 8 years, coupon 8%;

2. Government bond: $75 million (market value), remaining maturity 2 months, coupon 7%;

3. Interest rate swap: $ 150 million, bank receives floating rate interest and pays fixed, next interest reset after 12 months, remaining life of swap is 8 years (assumes the current interest rate is identical to the one the swap is based on); and

4. Long position in interest rate future: $ 50 million, delivery date after 6 months, life of underlying government security is 3.5 years (assumes the current interest rate is identical to the one on which the swap is based).

The bank would calculate general market risk using the simplified method as shown below:

Zone	Time-band	Position for instruments: (in $ millions)				Gross position (In $ millions)	Risk weights [%]	Capital charge (In $ millions)
		A	B	C	D			
1	0-1 month						0.00	
	Over 1-3 months		$75			$75	0.20	$0.15
	Over 3-6 months				($50)	$50	0.40	$0.20
	Over 6-12 months			$150		$150	0.70	$1.05
2	Over 1-2 years						1.25	
	Over 2-3 years						1.75	
	Over 3-4 years				$50	$50	2.25	$1.125
3	Over 4-5 years						2.75	
	Over 5-7 years						3.25	
	Over 7-10 years	$13.33		($150)		$163.33	3.75	$6.125
	Over 10-15 years						4.50	
	Over 15-20 years						5.25	
	Over 20 years						6.00	
Total		$13.33	$75	-	-	$488.33		$8.65
General interest rate risk capital requirement under simplified method							$8,650,000	

Example (3): on calculating general market risk charge on interest rate position under the maturity method

A hypothetical bank has the following given positions designated as trading:

1. Qualifying bond: $13.33 million (market value), remaining maturity 8 years, coupon 8%;

2. Government bond: $75 million (market value), remaining maturity 2 months, coupon 7%;

3. Interest rate swap: $ 150 million, bank receives floating rate interest and pays fixed, next interest reset after 12 months, remaining life of swap is 8 years (assumes the current interest rate is identical to the one the swap is based on), and

4. Long position in interest rate future: $ 50 million, delivery date after 6 months, life of underlying government security is 3.5 years (assumes the current interest rate is identical to the one on which the swap is based).

The bank would record these instructions as positions in a maturity ladder as shown below:

Zone	Time-band	Position for Instruments (in $ millions)				Risk Weights [%]	Risk weighted Long Positions (in $ millions)	Risk Weighted (Short) Positions (in $ millions)
		A	B	C	D			
1	**0-1 month**					0.00		
	Over 1-3 months		$75			0.20	0.15	
	Over 3-6 months				($50)	0.40		(0.20)
	Over 6-12 months			$150		0.70	1.05	
2	**Over 1-2 years**					1.25		
	Over 2-3 years					1.75		
	Over 3-4 years				$50	2.25	1.125	
3	**Over 4-5 years**					2.75		
	Over 5-7 years					3.25		
	Over 7-10 years	$13.33		($150)		3.75	0.50	(5.625)
	Over 10-15 years					4.50		
	Over 15-20 years					5.25		
	Over 20 years					6.00		

- Each position would be multiplied by the risk weight corresponding to the time band in which it is recorded. The risk-weighted long and risk weighted short positions in each maturity band are the basis of calculating the general market risk capital charges.

- The first step in the process of calculating general market risk is to calculate a 10% basis risk charge on the matched weighted position in each time band.

- In this example there are partially offsetting long and short positions in the (7-10 year) time-band, the matched portion of which is equal to $ 500,000 (0.50 Million Dollar). Ten percent of this matched portion is equal to $50,000 [0.10 x 0.50=0.5($50,000)].

In $ millions					
Zone	**Time-band**	**Risk weighted Long Positions**	**Risk Weighted (Short) Positions**	**Unmatched weighted position**	**Step 1 10% Basis risk charge**
1	**0-1 month**				
	Over 1-3 months	0.15		0.15	N/A
	Over 3-6 months		(0.20)	(0.20)	N/A
	Over 6-12 months	1.05		1.05	N/A
2	**Over 1-2 years**				
	Over 2-3 years				
	Over 3-4 years	1.125		1.125	N/A
3	**Over 4-5 years**				
	Over 5-7 years				
	Over 7-10 years	0.50	(5.625)	(5.125)	0.050
	Over 10-15 years				
	Over 15-20 years				
	Over 20 years				
TOTAL					0.050

Step 2 requires the calculation of **the yield curve risk charge**. The yield curve risk charge is calculated on the matched weighted position in each zone using the percentage risk factors in the table on zone l disallowances.

11- CAPITAL ADEQUACY RATIO

A) Circular No. (2/BS/184/2005) Regarding the Implementation of the Revised Capital Adequacy Ratio Basel (2).

In this example, a charge would be calculated for zone 1 (step 2(a)). It would be 40% of the total offsetting in the zone 40% x 0.20 = 0.08 ($80,000). No charge is required if offsetting does not occur within a zone.

Zone	Time-band	Unmatched weighted positions	Step 2(a) 30% to 40% of Matched weighted Zone position	Step 2(b) 40% to 100% Matched between Zones
1	**0-1 month**			
	Over 1-3 months	0.15		
	Over 3-6 months	(0.20)		
	Over 6-12 months	1.05		
Zone 1 totals		Long 1.20 Short (0.20) Unmatched 1.00	0.20 x 40% = 0.08	N/A (Zone 1 & 2 net totals are both long)
2	**Over 1-2 years**			
	Over 2-3 years			
	Over 3-4 years	1.125		N/A
Zone 2 totals		Long 1.125	N/A	0.45 = 40% x the lesser of 1.125 and 5.125 [charge on the offsetting between Zone 2 (long) and Zone 3 (short)]
3	**Over 4-5 years**			
	Over 5-7 years			
	Over 7-10 years	(5.125)		
	Over 10-15 years			
	Over 15-20 years			
	Over 20 years			
Zone 3 total		Short (5.125)	N/A	1.0= 100% x 1.00 Charge on the offsetting between remaining net long position in Zone 1 (1.0) and net short position in Zone 3 (4.0)

In step (2b) the yield curve risk charges on matching between residual unmatched weighted positions in the three zones are calculated. Zone (1) and Zone (2) are offset, if possible, reducing or eliminating the unmatched weighted positions in Zone (1) and Zone (2) as appropriate. Zone (2) and Zone (3) are then offset, if possible, reducing or eliminating the unmatched weighted position in Zone (2) or Zone (3) as appropriate. Zone (3) and Zone (1) are then offset, if possible, reducing or eliminating the unmatched weighted position in Zone (3) and Zone (1) as appropriate. A capital requirement is calculated as a percentage of the position eliminated by the inter-zone offsetting.

In the example, a charge would be calculated for adjacent zones (2) and (3) (step 3). It would be 40% of the matched weighted positions between the zones 40% x 1.125 = 0.45 ($450,000).

A charge would be calculated between zones (1) and (3) (step 3). It would be 100% of the matched positions between the zones 100% x 1.00 =1.00 ($ 1,000,000).

Step 3 calculates **a net position charge** equal to the residual unmatched weighted position.

In this example this amounts to $3 million (being the absolute value of the sum of 0.15 - 0.20 + 1.05 + 1.125 - 5.125 = 3.00) and would be included as the net position charge for general market risk.

The total capital requirement for general market risk for this portfolio would be:

1. **Basis risk charge**

   Matched weighted positions in all time bands $ 50,000

2. **Yield curve risk charge**

   Matched weighted positions in zone (1) $ 80000
   Matched weighted positions in Zone (2) N/A
   Matched weighted positions in Zone (3) N/A
   Matched weighted positions between zones (1) and (2) N/A
   Matched weighted positions between zones (2) and (3) $ 450,000
   Matched weighted positions between zones (1) and (3) $ 1,000,000

3. **Net position charge**

   Residual unmatched weighted positions = $ 3,000,000

TOTAL GENERAL MARKET RISK = $4,580,000

The return in respect of the above will be filled as set out in the attached schedule.

Example of calculating general interest rate risk under the maturity method

Zone	Time Band		Individual Net positions		Weighting Factors	Weighted Net positions		By Band		By Zone		Between Adjacent Zones	Between Zones (1) &(3)
	Coupon of 3% or more	Coupon of under 3% and zero coupon	Long	Short		Long	Short	Matched	Unmatched	Matched	Unmatched	Matched	Matched
1	1 month & under	1 month & under			0.00%			-				Zones (1) & (2)	
	Over 1 to 3 months	Over 1 to 3 months	75		0.20%	0.15		-	0.15	0.20	1.0	0.0	
	Over 3 to 6 months	Over 3 to 6 months		(50)	0.40%		(0.20)	-	(0.20)				Zones (1) &(3)
	Over 6 to 12 months	Over 6 to 12 months	150		0.70%	1.05		-	1.05	**B**		**E**	1.0
2	Over 1 to 2 years	Over 1 to 1.9 years			1.25%					0.00 **C**	1.125		
	Over 2 to 3 years	Over 1.9 to 2.8 years			1.75%								
	Over 3 to 4 years	Over 2.8 to 3.6 years	50		2.25%	1.125		-	1.125				
3	Over 4 to 5 years	Over 3.6 to 4.3 years			2.75%							Zones (2) & (3)	
	Over 5 to 7 years	Over 4.3 to 5.7 years			3.25%								**G**
	Over 7 to 10 years	Over 5.7 to 7.3 years	13.33	(150)	3.75%	0.50	(5.625)	0.50	(5.125)				
	Over 10 to 15 years	Over 7.3 to 9.3 years			4.50%								
	Over 15 to 20 years	Over 9.3 to 10.6 years			5.25%					0.0	(5.125)	1.125	
	Over 20 years	Over 10.6 to 12 years			6.00%								
		Over 12 to 20 years			8.00%								
		Over 20 years			12.5%					**D**		**F**	
Total				288.33	(200)				0.50			3.0	
										A		**H**	

Total General Interest Rate Risk Capital Requirement =
10% x 0.5 + 40% x 0.20 +30% (0+0) + 40% (0+1.25) + 100% x 1.0 + 100% x 3.0 = $\boxed{4.58}$

Example (4): Calculating capital charge for commodities risk under the simplified method and the maturity ladder method

A bank has the following given positions in one commodity. All positions are designated as trading:

Position	Amount	Maturity
Long position	KD 80,000	4 months
Short position	KD 100,000	5 months
Long position	KD 60,000	18 months
Short position	KD 60,000	3 years

Simplified method

Under the simplified method the capital charge for commodities risk in respect of the above positions will be calculated as follows:

	Gross position KD	Net position KD	Capital charge KD
3% capital charge on gross position	300,000	-	9,000
15% capital charge on net position	-	20,000	3,000
Total capital charge			12,000

Maturity Ladder Method:

Under the maturity ladder method the bank would first record the above positions in a maturity ladder and then calculate the capital charge as shown on the attached schedule.

Example of calculating capital charge for commodities under the maturity ladder method

Time Band	Spread Rate A	Long Position B	Short Position C	Matched Position D	Unmatched Position carried forward (long) short E	No. of bands unmatched Positions carried forward F	Net Position G	Capital Charge Matched Position H=D x 2 x A	Capital Charge Net Position I=[E] x F x 0.6%	Capital Charge Net Position J=Gx15%	Total Capital Charge K=H+I+J
0-1 month	1.5%										
Over 1-3 months	1.5%										
Over 3-6 months	1.5%	80,000	(100,000)	80,000	(20,000)	2	-	80,000x2x1.5% =2,400	20,000x2x0.6% =240	-	2,640
Over 6- 12 months	1.5%										
Over 1-2 years	1.5%	60,000	-	20,000	40,000	2	-	20,000x2x1.5% =600	40,000x2x0.6% =480	-	1,080
Over 2-3 years	1.5%										
Over 3 years	1.5%		(60,000)	40,000			20,000	40,000x2x1.5% =1,200	-	20,000x15% = 3,000	4,200
Total capital requirement under the maturity ladder method											7,920

Once the long and short positions are placed into the appropriate time bands, the matched positions are determined. In the above example there is a short position of KD 80,000 and long position of KD 100,000 in the 3-6 months band. Therefore the matched long position and is KD 80,000 (i.e., the smaller of the long position and the absolute value of the short position).

The matched positions are summed (i.e. KD 80,000 short position plus KD 80,000 long position) and multiplied by the spread rate of 1.5% to give a capital charge of KD 2,400.

The unmatched long position of KD 20,000 is carried forward to the time band 1-2 years to offset it against the long position of KD 60,000 in this time band. Since the unmatched position is carried across two time bands; the capital charge for the unmatched position is calculated by multiplying the unmatched position by 2 and again by 0.6%.

The capital charge for the time band 1-2 years and over 3 years is calculated in the same manner as above.

The total capital charge is the sum of capital charges calculated as above plus a 15% capital charge on the net position.

Example (5): Calculation of capital charge for options under the simplified method

If the bank holds 100 shares with a market value of $ 10 each and the bank has an equivalent put option with a strike price of $11, the capital charge will be calculated as follows:

1- Step (1) is to calculate the market value of the underlying instrument which is $1,000 (i.e., 100 shares multiplied by the market value of $ 10 per share).

2- Step (2) is to determine the sum of specific and general market risk charges applicable to the underlying which is 16% (i.e., 8% of specific risk charge plus 8% of general risk charge).

3- Step (3) is to calculate the amount the option is in the money which is $100 i.e., ($11-$10) x 100= $100.

4- Step (4) is to calculate the capital charge which is [($1,000 x 16%) – ($100) = $60].

Example (6): Options Scenario Matrices

A hypothetical bank has purchased and sold options on Australian interest rates, and options to purchase and sell U.S. dollars with Australian funds. The bank might use the scenario approach to calculate the general market risk of these options portfolios by calculating the following matrices:

1) Options on instruments maturing up to 3 months.

Yield	-100 basis points	- 66 basis points	-33 basis points	Current yield	+ 33 basis point	+66 basis point	+100 basis point
Volatility							
+25%	Gain/loss	gain/loss	gain/loss	gain/loss	gain/loss	gain/loss	gain/loss
Current% Volatility	Gain/loss	gain/loss	gain/loss	gain/loss	gain/loss	gain/loss	gain/loss
-25%	Gain/loss	gain/loss	gain/loss	gain/loss	gain/loss	gain/loss	gain/loss

Repeat the interest rate matrix above for each of the following:

Group of maturity bands	**Assumed yield changes in basis points**
3 up to 6 months	100
Over 6 up to 12 months	100
Over 1 up to 4 years	90
Over 4 up to 10 years	75
Over 10 years	60

2) Options on Australian / U.S. dollar exchange rate.

Exchange rate	-8%	-5.33%	-2.67%	Current exchange rate	+2.67%	+5.33%	+8%
Volatility							
+25%	gain/loss	gain/loss	gain/loss	gain/loss	gain/loss	gain/loss	gain/loss
Current% Volatility	gain/loss	gain/loss	gain/loss	gain/loss	gain/loss	gain/loss	gain/loss
-25%	gain/loss	gain/loss	gain/loss	gain/loss	gain/loss	gain/loss	gain/loss

Annex (L): Detailed definition of business lines

Business lines	Major business segments	Activity Groups
Corporate Finance	Government Finance	Mergers and Acquisitions, Underwriting, Privatisations, Research, Debt (Government, High Yield), Equity, Syndications, IPO, Secondary Private Placements
	Merchant Banking	
	Advisory Services	
Trading & Sales	Sales	Fixed income, equity, foreign exchanges, commodities, credit, funding, own position securities, lending and repos, brokerage, debt, prime brokerage
	Market Making	
	Proprietary Positions	
	Treasury	
Retail Banking	Retail banking	Retail lending and deposits, banking services, trust and estates
	Private banking	Private lending and deposits, banking services, trust and estates investment advice
	Card Services	Merchant/ Commercial/ Corporate cards, private labels and retail
Commercial Banking	Commercial Banking	Project finance, real estate, export finance, trade finance, factoring, leasing, lending, guarantees, bills of exchange
Payment and Settlements(1)	External Clients	Payments and collections, fund transfer, clearing and settlement
Agency Services	Custody	Escrow, Depository Receipts, Securities lending (Customers), Corporate actions
	Corporate Agency	Issuer and paying agents
	Corporate Trust	
Asset Management	Discretionary Fund Management	Polled, segregated, retail, institutional, closed, open
	Non-Discretionary Fund Management	Pooled, segregated, retail, institution, closed, open
Retail Brokerage	Retail Brokerage	Execution and full service

(1) Payment and settlement losses related to a licensed bank's own activities would be incorporated in the loss experience of the affected business lines.

Annex (M): An example of allocating gross income to business lines

Business lines	Gross income
Retail Banking	Net interest income on loans and advances to retail customers and SMEs treated as retail. Fees related to traditional retail activities. Net income from swaps and derivatives held to hedge the retail banking book.
Commercial Banking	Net interest income on loans and advances to corporate and SMEs treated as corporate, interbank and sovereign customers. Fees related to traditional commercial banking activities including commitments, guarantees, and bills of exchange. Net income on securities held in the banking book. Profits/losses on swaps and derivatives held to hedge the commercial banking book.
Trading and Sales	Profits/losses on instruments held for trading purposes, net of funding cost. Fees from wholesale broking.
Payment and Settlement / Agency Services / Brokerage	Net fees/commissions earned. Fees to cover provision of payments/settlement facilities for wholesale counterparties.
Corporate Finance / Agency Services / Asset Management / Retail Brokerage	Net fees/commissions earned in each business.

Annex (N): Example showing the calculation of risk weighted amount of an investment subject to fair value treatment

Equity investment at fair value = KD 100

Fair value reserve applicable to this investment = KD 20

Fair value reserve eligible as Tier 2 = KD 20 X 0.45 = KD 9

Risk weighted amount of the investment = KD 100 - (20 X 0.55) = KD 89

Annex (O): Example showing the calculation of the investment amount, based on its fair value that should be deducted from capital base

In case of an equity investment, other than associate, in a commercial company that is in excess of the 10% concentration limit but pre-approved by the Central Bank of Kuwait, the materiality level for deduction purposes will be 15% (of capital base), i.e., the amount to be deducted will the portion which is in excess of 15% net of the related 55% discount.

Calculation:

Assuming no changes in fair value and profitability, last quarter capital base before any deduction except goodwill, fair value reserve adjustment and treasury shares = KD 1018

Equity investment at fair value = KD 200 (equivalent to 19.65 % of capital base)

Total fair value reserve applicable to this investment = KD 40

Excess investment amount above the 15% level = 200 – (1018 X 0.15) = 47.3

Proportion of fair value reserve that is related to (KD 47.3) = (40/200) X 47.3
= 9.46

The capital base of 1018 already includes 45% of the fair value reserve i.e.
9.46 x 45% = 4.25

The deduction should be as follows:

1. The asset side should be reduced by KD 47.3
2. The Capital Base shall be reduced as follows:

Excess Investment above the 15 % level at Fair Value	47.3
Less: Fair Value Reserve	(9.46)
Cost Price of Investment	37.84
Add Back:	
45 % of Fair Value Reserve included in the Capital Base	4.25
Total deduction from capital base	42.09

11- CAPITAL ADEQUACY RATIO
A) Circular No. (2/BS/184/2005) Regarding the Implementation of the Revised Capital Adequacy Ratio Basel (2).

Central Bank of Kuwait
Capital Adequacy Returns

Confidential

<table>
<tr><td colspan="2">Quarterly Capital Adequacy Returns for submission to the Central Bank of Kuwait in accordance with Chapter Two of the 'Rules and Regulations concerning Capital Adequacy Standard'</td></tr>
<tr><td colspan="2">For the quarter ending on / /</td></tr>
<tr><td>Name of Bank</td><td>Date of Submission</td></tr>
<tr><td></td><td>/ /</td></tr>
<tr><td colspan="2">We certify that this return is, to the best of our knowledge and belief, correct.</td></tr>
<tr><td>Name of person filing return</td><td>Designation</td></tr>
<tr><td>Signature</td><td>Contact Number in case of Query by the Central Bank of Kuwait</td></tr>
</table>

Bank Seal

11- CAPITAL ADEQUACY RATIO
A) Circular No. (2/BS/184/2005) Regarding the Implementation of the Revised Capital Adequacy Ratio Basel (2).

Central Bank of Kuwait
Capital Adequacy Returns

Confidential

Note: This return is to be prepared in accordance with the completion instructions issued with these returns by the Central Bank of Kuwait. Please complete and submit the following returns, as applicable, within 14 days after the last day of each quarter.

Form No	Return Description
Credit Input Sheets	
CR1	Credit Input Sheet - On Balance sheet exposures - Assets
CR2a	Credit Input Sheet - Off Balance sheet exposures - Contingencies
CR3a	Credit Input Sheet - Off Balance sheet exposures - Commitments
CR4a	Credit Input Sheet - Off Balance sheet exposures - Derivative contracts
Replacement Cost for Derivatives	
CR4b	Replacement Cost for Derivative Contracts - Off balance sheet exposure
Credit Conversion Factors Sheet	
CR2c	Credit Conversion Sheet for off balance sheet exposures- Credit Equivalent Amount for Contingencies
CR3c	Credit Conversion Sheet for off balance sheet exposures- Credit Equivalent Amount for Contingencies
CR4c	Credit Conversion Sheet for off balance sheet exposures- Credit Equivalent Amount for Derivative contracts
Credit Risk Mitigation and Risk Weighting	
CR5a	Risk Weighted Assets -Total Credit Exposure before CRM
CR5b	Risk Weighted Assets - Credit Risk Mitigation and Risk Weighting
Market Risk Capital Charge	
CMR	Capital charge for market risk
MRI1	Interest Rate Risk Position
MRI2	Specific Interest Rate Risk Position
MRI3a & MRI3b	General Interest Rate Risk Position (Simplified Approach)
MRI4a & MRI4b	General Interest Rate Risk Position (Maturity Approach)
MRE	Equity Position Risk
MRF	Foreign Exchange Position Risk
MRC1	Commodity risk (Simplified Method)
MRC2a & MRC2b	Commodity risk (Maturity Ladder Method)
MRO1	Options risk (Simplified Approach)
MRO2	Options risk (Scenarios Method)
Operational Risk Capital Charge	
OR	Capital Charge for operational risk
Capital Adequacy Calculation	
CA1	Calculation of Capital Base
CA2	Capital Adequacy Ratio Calculation

11- CAPITAL ADEQUACY RATIO
A) Circular No. (2/BS/184/2005) Regarding the Implementation of the Revised Capital Adequacy Ratio Basel (2).

Central Bank of Kuwait
Capital Adequacy Returns

List of abbreviations used	
PSE	Public Sector Entity
CQG	Credit Quality Grade
MDB	Multi Development Bank
SME	Small to Medium Sized Enterprises
RHL	Residential Housing Loan
RW	Risk Weight
L/T	Long Term
S/T	Short Term
CRM	Credit Risk Mitigation
OBS	Off Balance Sheet

CREDIT RISK – THE STANTARDISED APPROACH
Table CR1 - Credit Input Sheet
On balance sheet exposures

For the quarter ending on / /

" In Thousand KD"

Asset Categories for Credit Risk	On balance sheet exposures (Note 1)
	A
1. Cash items	**0.00**
1.1 Notes and Coins	
1.2 Gold Bullions Held and backed by gold bullion liabilities	
1.3 Cheques and Drafts Drawn on other Banks and Immediately Payable or in the Process of Collection	
1.4 Receiveable Funds arising from the sale of securities (Note 2)	
1.5 Receivable Funds arising from the purchase of securities (Note 2)	
2.Total Claims on Sovereigns	**0.00**
2.1 Total State of Kuwait	**0.00**
State of Kuwait - Local Currency	
State of Kuwait - Foreign Currency	
2.2 Total Other GCC Sovereigns	**0.00**
Other GCC Sovereigns- Local Currencies	
Other GCC Sovereigns- Foreign Currencies	
2.3 Total Claims on Other Sovereigns (Note3)	**0.00**
CQG 1 (AAA to AA-)	
CQG 2 (A+ to A-)	
CQG 3 (BBB+ to BBB-)	
CQG 4 (BB+ to BB-)	
CQG 5 (B+ to B-)	
CQG 6 (Below B-)	
Unrated	
Preferentially Risk Weighted Domestic Currency Claims **(Note 4)**	
3. Total Claims on International Organisations (Note 5)	
4. Total Claims on PSEs	**0.00**
4.1 Total Kuwaiti PSEs	**0.00**
Kuwaiti PSEs - Local Currency	
Kuwaiti PSEs - Foreign Currency	
4.2 Total Other GCC PSEs	**0.00**
Other GCC PSEs- Local Currencies	
Other GCC PSEs- Foreign Currencies	
4.3 Total Foreign PSEs	**0.00**
CQG 1 (AAA to AA-)	
CQG 2 (A+ to A-)	
CQG 3 (BBB+ to BBB-)	
CQG 4 (BB+ to BB-)	
CQG 5 (B+ to B-)	
CQG 6 (Below B-)	
Unrated	

Asset Categories for Credit Risk	On balance sheet exposures (Note 1)
5. Total Claims on MDBs	**0.00**
5.1 Those fulfilling eligibility criteria (Note 6)	
5.2 Those not fulfilling eligibility criteria:	**0.00**
CQG 1 (AAA to AA-)	
CQG 2 (A+ to A-)	
CQG 3 (BBB+ to BBB-)	
CQG 4 (BB+ to BB-)	
CQG 5 (B+ to B-)	
CQG 6 (Below B-)	
Unrated	
6. Total Claims on Banks	**0.00**
6.1 Total Claims on Licensed Banks	
6.2 Total Claims on Foreign Banks	0.00
6.2.1 L/ T Claims on Foreign Banks	0.00
CQG 1 (AAA to AA-)	
CQG 2 (A+ to A-)	
CQG 3 (BBB+ to BBB-)	
CQG 4 (BB+ to BB-)	
CQG 5 (B+ to B-)	
CQG 6 (Below B-)	
Unrated	
6.2.2 S/ T Claims on Foreign Banks	0.00
CQG 1 (AAA to AA-)	
CQG 2 (A+ to A-)	
CQG 3 (BBB+ to BBB-)	
CQG 4 (BB+ to BB-)	
CQG 5 (B+ to B-)	
CQG 6 (Below B-)	
Unrated	
7. Claims on Corporates (Note 7)	**0.00**
CQG 1 (AAA to AA-)	
CQG 2 (A+ to A-)	
CQG 3 (BBB+ to BBB-)	
CQG 4 (BB+ to BB-)	
CQG 5 (B+ to B-)	
CQG 6 (Below B-)	
Unrated	
8. Claims on Securitised Assets (as Investor)	0.00
8.1 Long Term Claims	0.00
CQG 1 (AAA to AA-)	
CQG 2 (A+ to A-)	
CQG 3 (BBB+ to BBB-)	
CQG 4 (BB+ to BB-)	
8.2 Short Term Claims	0.00
CQG 1 (AAA to AA-)	
CQG 2 (A+ to A-)	
CQG 3 (BBB+ to BBB-)	
9. Regulatory Retail	**0.00**
9.1 Claims on Qualifying SMEs (Note 8)	
9.2 Housing Loans Eligible for 75% RW (Note 9)	
9.3 Other Retail Loans (Note 10)	

11- CAPITAL ADEQUACY RATIO
A) Circular No. (2/BS/184/2005) Regarding the Implementation of the Revised Capital Adequacy Ratio Basel (2).

Asset Categories for Credit Risk	On balance sheet exposures (Note 1)
10. RHLs Eligible for 35% RW (Note 11)	
11. Past Due Exposure (Note 12)	**0.00**
11.1 Where Specific Provision less than 50%	
11.2 Where Specific Provision 50% or more	
11.3 For RHLs where specific provision is 20% or more	
11.4 For RHLs where specific provision is less than 20%	
11.5 Fully secured by unrecognized collateral	
12. Other Assets	**0.00**
12.1 Venture Capital and private equity investment	
12.2 Investment in Commercial Entities Below Materiality Thresholds	
12.3 Loans Secured by Commercial Real Estate	
12.4 Others - (Note 13)	
TOTAL BANKING BOOK ASSETS	**0.00**

Note (Table CR1):

1. All claims should be net of specific provisions and before applying the eligible CRMs. In case of a guaranteed exposure by an eligible guarantor, the exposure should be reported under the guarantor.
2. Include all receivable funds arising from the sale or purchase of securities for the bank's own account or on behalf of clients.
3. Claims should be segregated by Credit Quality Grades (CQG).
4. Report domestic currency claim on any other foreign sovereign that is assigned preferential risk weight by its own bank regulator.
5. International organisations refer to the IMF, BIS, ECB or EC.
6. Refer to paragraph No. 49 of the capital adequacy regulation for the eligibility criteria.
7. Include claims on corporates, commercial companies owned by PSEs, securities and investment firms, insurance companies and enterprises that do not qualify for SMEs and equity interest of 20% or less in insurance companies.
8. Include all claims on SMEs which satisfy the criteria set out in paragraph No. 59 and 61 of the capital adequacy regulation.
9. Include only those residential housing loans that satisfy the criteria set out in paragraph No. 64 of the capital adequacy regulation.
10. Include all consumer and installment loans, credit cards receivables, and small personal loans.
11. Report all residential housing loans that satisfy the conditions set out in paragraphs No. 65 and 66 of the capital adequacy regulation.
12. Include all exposures that are identified as non-performing in accordance with the Central Bank rules and regulations concerning classification of credit facilities.
13. Report all other assets, e.g., premises and equipments, equity investment of 20% or less in banks, securities and other financial entities, excluding trading book assets (i.e. assets held for trading).

CREDIT RISK – THE STANTARDISED APPROACH
Table CR2a - Credit Input Sheet
Off balance sheet exposures
Contingencies
For the quarter ending on / /

" In Thousand KD"

Categories for Credit Risk	Off Balance Sheet (OBS) (Note 1)		
	Trade-related Contingencies (Note 2)	Transaction-related Contingencies (Note 2)	Total Contingencies
	A	B	A+B=C
1. Claims on Sovereigns	**0.00**	**0.00**	**0.00**
1.1 Total State of Kuwait	**0.00**	**0.00**	**0.00**
State of Kuwait - Local Currency			**0.00**
State of Kuwait - Foreign Currency			**0.00**
1.2 Total Other GCC Sovereigns	**0.00**	**0.00**	**0.00**
Other GCC Sovereigns - Local Currency			**0.00**
Other GCC Sovereigns - Foreign Currency			**0.00**
1.3 Total Other Sovereigns - (Note 3)	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)			**0.00**
CQG 2 (A+ to A-)			**0.00**
CQG 3 (BBB+ to BBB-)			**0.00**
CQG 4 (BB+ to BB-)			**0.00**
CQG 5 (B+ to B-)			**0.00**
CQG 6 (Below B-)			**0.00**
Unrated			**0.00**
Preferentially Risk Weighted Domestic Claims **(Note 4)**			**0.00**
2. Total International Organisations (Note 5)			**0.00**
3. Total Claims on PSEs	**0.00**	**0.00**	**0.00**
3.1 Total Kuwaiti PSEs	**0.00**	**0.00**	**0.00**
Kuwaiti PSEs - Local Currency			**0.00**
Kuwaiti PSEs - Foreign Currency			**0.00**
3.2 Total Other GCC PSEs	**0.00**	**0.00**	**0.00**
Other GCC PSEs - Local Currency			**0.00**
Other GCC PSEs - Foreign Currency			**0.00**
3.3 Total Foreign PSEs	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)			**0.00**
CQG 2 (A+ to A-)			**0.00**
CQG 3 (BBB+ to BBB-)			**0.00**
CQG 4 (BB+ to BB-)			**0.00**
CQG 5 (B+ to B-)			**0.00**
CQG 6 (Below B-)			**0.00**
Unrated			**0.00**

Categories for Credit Risk	Off Balance Sheet (OBS) (Note 1)		
	Trade-related Contingencies (Note 2)	Transaction-related Contingencies (Note 2)	Total Contingencies
	A	B	A+B=C
4. Total Claims on MDBs	**0.00**	**0.00**	**0.00**
4.1 Those fullfilling eligibility criteria (Note 6)			**0.00**
4.2 Those not fullfilling eligibility criteria	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)			**0.00**
CQG 2 (A+ to A-)			**0.00**
CQG 3 (BBB+ to BBB-)			**0.00**
CQG 4 (BB+ to BB-)			**0.00**
CQG 5 (B+ to B-)			**0.00**
CQG 6 (Below B-)			**0.00**
Unrated			**0.00**
5. Total Claims on Banks	**0.00**	**0.00**	**0.00**
5.1 Total Claims on Licensed Banks			**0.00**
5.2 Total Claims on Foreign Banks	**0.00**	**0.00**	**0.00**
5.2.1 L/T Claims on Foreign Banks	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)			**0.00**
CQG 2 (A+ to A-)			**0.00**
CQG 3 (BBB+ to BBB-)			**0.00**
CQG 4 (BB+ to BB-)			**0.00**
CQG 5 (B+ to B-)			**0.00**
CQG 6 (Below B-)			**0.00**
Unrated			**0.00**
5.2.2 S/T Claims on Foreign Banks	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)			**0.00**
CQG 2 (A+ to A-)			**0.00**
CQG 3 (BBB+ to BBB-)			**0.00**
CQG 4 (BB+ to BB-)			**0.00**
CQG 5 (B+ to B-)			**0.00**
CQG 6 (Below B-)			**0.00**
Unrated			**0.00**
6. Total Claims on Corporates (Note 7)	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)			**0.00**
CQG 2 (A+ to A-)			**0.00**
CQG 3 (BBB+ to BBB-)			**0.00**
CQG 4 (BB+ to BB-)			**0.00**
CQG 5 (B+ to B-)			**0.00**
CQG 6 (Below B-)			**0.00**
Unrated			**0.00**
7. Regulatory Retail	**0.00**	**0.00**	**0.00**
7.1 Claims on Qualifying SMEs (Note 8)			**0.00**
7.2 Housing Loans Eligible for 75% RW (Note 9)			**0.00**
7.3 Other Retail (Note 10)			**0.00**

Categories for Credit Risk	Off Balance Sheet (OBS) (Note 1)		
	Trade-related Contingencies (Note 2)	Transaction-related Contingencies (Note 2)	Total Contingencies
	A	B	A+B=C
8. RHLs Eligible for 35% RW (Note 11)	**0.00**	**0.00**	**0.00**
9. Past Due Exposures	**0.00**	**0.00**	**0.00**
9.1 Where specific provision less than 50%			**0.00**
9.2 Where specific provision 50% or more			**0.00**
9.3 Fully secured by unrecognized collateral			**0.00**
10. Other Assets Not Reported Above	**0.00**	**0.00**	**0.00**
10.1 Venture Capital and private equity investment			**0.00**
10.2 Investment in Commercial Entities Below Materiality Thresholds			**0.00**
10.3 Loans Secured by Commercial Real Estate			**0.00**
10.4 Others			**0.00**
TOTAL BANKING BOOK OBS	**0.00**	**0.00**	**0.00**

Note (Table CR2a):

1. All off balance sheet exposures should be reported net of specific provisions and before applying the eligible CRMs. In case of a guaranteed amount by an eligible guarantor, the exposure should be reported under the guarantor.
2. Refer to paragraph No. 122 of the capital adequacy regulations for the components of trade-related and transaction-related contingencies.
3. Exposures should be segregated by Credit Quality Grades (CQG's).
4. Report domestic currency exposures to any other foreign sovereign that is assigned preferential risk weight by its own bank regulator.
5. International organisations refer to the IMF, BIS, ECB or EC.
6. Refer to paragraph No. 49 of the capital adequacy regulation for the eligibility criteria.
7. Include exposures to corporates, commercial companies owned by PSEs, securities and investment firms, insurance companies and enterprises that do not qualify for SMEs and underwriting of equity interest of 20% or less in insurance companies.
8. Include all claims on SMEs which satisfy the criteria set out in paragraph No. 59 and 61 of the capital adequacy regulation.
9. Include only the untilised amounts related to those residential housing loans that satisfy the criteria set out in paragraph No. 64 of the capital adequacy regulation.
10. Include all unutilised amounts related to consumer and installment loans, credit cards, and small personal loans.
11. Report all untilised amounts related to residential housing loans that satisfy the conditions set out in paragraphs No. 65 and 66 of the capital adequacy regulation.

CREDIT RISK – THE STANTARDISED APPROACH
Table CR3a - Credit Input Sheet
Off balance sheet exposures
Commitments
For the quarter ending on / /

“ In Thousand KD”

Categories for Credit Risk	Off Balance Sheet (OBS)- (Note 1)						
	Direct Credit Substitutes	Notes Issuance And Revolving Underwriting Facilities	Asset Sale with Recourse/ Forward Asset Purchases/ Partly Paid Shares/ Forward Deposits	Other Commitments: Commitments which can be cancelled at any time	Other Commitments: Up to 1 year	Other Commitments: Over 1 year	Total Commitments
	A	B	C	D	E	F	G = A+B+C+D+E+F
1. Claims on Sovereigns	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
1.1 Total State of Kuwait	0.00	0.00	0.00	0.00	0.00	0.00	0.00
State of Kuwait - Local Currency							0.00
State of Kuwait - Foreign Currency							0.00
1.2 Total Other GCC Sovereigns	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Other GCC Sovereigns - Local Currency							0.00
Other GCC Sovereigns - Foreign Currency							0.00
1.3 Total Other Sovereigns - (Note 2)	0.00	0.00	0.00	0.00	0.00	0.00	0.00
CQG 1 (AAA to AA-)							0.00
CQG 2 (A+ to A-)							0.00
CQG 3 (BBB+ to BBB-)							0.00
CQG 4 (BB+ to BB-)							0.00
CQG 5 (B+ to B-)							0.00
CQG 6 (Below B-)							0.00
Unrated							0.00
Preferentially Risk Weighted Domestic Claims **(Note 3)**							0.00
2. Total International Organisations (Note 4)							**0.00**
3. Total Claims on PSEs	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
3.1 Total Kuwaiti PSEs	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Kuwaiti PSEs - Local Currency							0.00
Kuwaiti PSEs - Foreign Currency							0.00
3.2 Total Other GCC PSEs	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Other GCC PSEs - Local Currency							0.00
Other GCC PSEs - Foreign Currency							0.00
3.3 Total Foreign PSEs	0.00	0.00	0.00	0.00	0.00	0.00	0.00
CQG 1 (AAA to AA-)							0.00
CQG 2 (A+ to A-)							0.00
CQG 3 (BBB+ to BBB-)							0.00
CQG 4 (BB+ to BB-)							0.00
CQG 5 (B+ to B-)							0.00
CQG 6 (Below B-)							0.00
Unrated							0.00

Categories for Credit Risk	Off Balance Sheet (OBS)- (Note 1)						
	Direct Credit Substitutes	Notes Issuance And Revolving Underwriting Facilities	Asset Sale with Recourse/ Forward Asset Purchases/ Partly Paid Shares/ Forward Deposits	Other Commitments			Total Commitments
				Commitments which can be cancelled at any time	Up to 1 year	Over 1 year	
	A	B	C	D	E	F	G = A+B+C+D+E+F
4. Total Claims on MDBs	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
4.1 Those fullfilling eligibility criteria **(Note 5)**							0.00
4.2 Those not fullfilling eligibility criteria	0.00	0.00	0.00	0.00	0.00	0.00	0.00
CQG 1 (AAA to AA-)							0.00
CQG 2 (A+ to A-)							0.00
CQG 3 (BBB+ to BBB-)							0.00
CQG 4 (BB+ to BB-)							0.00
CQG 5 (B+ to B-)							0.00
CQG 6 (Below B-)							0.00
Unrated							0.00
5. Total Claims on Banks	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
5.1 Total Claims on Licensed Banks							0.00
5.2 Total Claims on Foreign Banks	0.00	0.00	0.00	0.00	0.00	0.00	0.00
5.2.1 L/T Claims on Foreign Banks	0.00	0.00	0.00	0.00	0.00	0.00	0.00
CQG 1 (AAA to AA-)							0.00
CQG 2 (A+ to A-)							0.00
CQG 3 (BBB+ to BBB-)							0.00
CQG 4 (BB+ to BB-)							0.00
CQG 5 (B+ to B-)							0.00
CQG 6 (Below B-)							0.00
Unrated							0.00
5.2.2 S/T Claims on Foreign Banks	0.00	0.00	0.00	0.00	0.00	0.00	0.00
CQG 1 (AAA to AA-)							0.00
CQG 2 (A+ to A-)							0.00
CQG 3 (BBB+ to BBB-)							0.00
CQG 4 (BB+ to BB-)							0.00
CQG 5 (B+ to B-)							0.00
CQG 6 (Below B-)							0.00
Unrated							0.00
6. Total Claims on Corporates (Note 6)	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)							0.00
CQG 2 (A+ to A-)							0.00
CQG 3 (BBB+ to BBB-)							0.00
CQG 4 (BB+ to BB-)							0.00
CQG 5 (B+ to B-)							0.00
CQG 6 (Below B-)							0.00
Unrated							0.00
7. Credit Derivative Claims (Protection Seller)	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
7.1 Long Term Claims	**0.00**						**0.00**
CQG 1 (AAA to AA-)							0.00
CQG 2 (A+ to A-)							0.00
CQG 3 (BBB+ to BBB-)							0.00
CQG 4 (BB+ to BB-)							0.00

Categories for Credit Risk	Off Balance Sheet (OBS)- (Note 1)						
	Direct Credit Substitutes	Notes Issuance And Revolving Underwriting Facilities	Asset Sale with Recourse/ Forward Asset Purchases/ Partly Paid Shares/ Forward Deposits	Other Commitments: Commitments which can be cancelled at any time	Other Commitments: Up to 1 year	Other Commitments: Over 1 year	Total Commitments
	A	B	C	D	E	F	G = A+B+C+D+E+F
7.2 Short Term Claims	**0.00**	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	**0.00**
CQG 1 (AAA to AA-)		[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	0.00
CQG 2 (A+ to A-)		[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	0.00
CQG 3 (BBB+ to BBB-)		[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	0.00
7.3 Unrated Claims		[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	**0.00**
8. Regulatory Retail	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
8.1 Claims on Qualifying SMEs (Note 7)							0.00
8.2 Housing Loans Eligible for 75% RW (Note 8)							0.00
8.3 Other Retail (Note 9)							0.00
9. RHLs Eligible for 35% RW (Note 10)							**0.00**
10. Past Due Exposures	0.00	0.00	0.00	0.00	0.00	0.00	**0.00**
10.1 Where specific provision less than 50%							**0.00**
10.2 Where specific provision 50% or more							**0.00**
10.3 Fully secured by unrecognized collateral							**0.00**
11. Other Exposures Not Reported Above	0.00	0.00	0.00	0.00	0.00	0.00	**0.00**
11.1 Venture Capital and private equity investment							**0.00**
11.2 Investment in Commercial Entities Below Materiality Thresholds							**0.00**
11.3 Loans Secured by Commercial Real Estate							**0.00**
11.4 Others							**0.00**
TOTAL BANKING BOOK OBS	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**

Note (Table CR3a):

1. All off balance sheet exposures should be reported net of specific provisions and before applying the eligible CRMs. In case of a guaranteed amount by an eligible guarantor, the exposure should be reported under the guarantor.
2. Exposures should be segregated by Credit Quality Grades (CQG's).
3. Report domestic currency exposures to any other foreign sovereign that is assigned preferential risk weight by its own bank regulator.
4. International organisations refer to the IMF, BIS, ECB or EC.
5. Refer to paragraph No. 49 of the capital adequacy regulation for the eligibility criteria.
6. Include exposures to corporates, commercial companies owned by PSEs, securities and investment firms, insurance companies and enterprises that do not qualify for SMEs and underwriting of equity interest of 20% or less in insurance companies.
7. Include all exposures to SMEs which satisfy the criteria set out in paragraph No. 59 and 61 of the capital adequacy regulation.
8. Include only the untilised amounts related to those residential housing loans that satisfy the criteria set out in paragraph No. 64 of the capital adequacy regulation.
9. Include all unutilised amounts related to consumer and installment loans, credit cards, and small personal loans.
10. Report all untilised amounts related to residential housing loans that satisfy the conditions set out in paragraphs No. 65 and 66 of the capital adequacy regulation.

CREDIT RISK – THE STANTARDISED APPROACH
Table CR4a - Credit Input Sheet
Off balance sheet exposures
Derivative Contract
For the quarter ending on / /

" In Thousand KD"

Categories for Credit Risk	Derivative Contracts - (Note 1)						
	Foreign Exchange Contracts (Note 2)			Interest Rate Contracts			Total Derivative Contracts
	Up to 1 year	Over 1 to 5 years	Over 5 years	Up to 1 year	Over 1 to 5 years	Over 5 years	
	A	B	C	D	E	F	G =A+B+C+D+E+F
1. Claims on Sovereigns	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
1.1 Total State of Kuwait	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
State of Kuwait - Local Currency							**0.00**
State of Kuwait - Foreign Currency							**0.00**
1.2 Total Other GCC Sovereigns	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
Other GCC Sovereigns - Local Currency							**0.00**
Other GCC Sovereigns - Foreign Currency							**0.00**
1.3 Total Other Sovereigns (Note 3)	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)							**0.00**
CQG 2 (A+ to A-)							**0.00**
CQG 3 (BBB+ to BBB-)							**0.00**
CQG 4 (BB+ to BB-)							**0.00**
CQG 5 (B+ to B-)							**0.00**
CQG 6 (Below B-)							**0.00**
Unrated							**0.00**
Preferentially Risk Weighted Domestic Claims **(Note 4)**							**0.00**
2. Total International Organisations (Note 5)							**0.00**
3. Total Claims on PSEs	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
3.1 Total Kuwaiti PSEs	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
Kuwaiti PSEs - Local Currency							**0.00**
Kuwaiti PSEs - Foreign Currency							**0.00**
3.2 Total Other GCC PSEs	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
Other GCC PSEs - Local Currency							**0.00**
Other GCC PSEs - Foreign Currency							**0.00**
3.3 Total Foreign PSEs	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)							**0.00**
CQG 2 (A+ to A-)							**0.00**
CQG 3 (BBB+ to BBB-)							**0.00**
CQG 4 (BB+ to BB-)							**0.00**
CQG 5 (B+ to B-)							**0.00**
CQG 6 (Below B-)							**0.00**
Unrated							**0.00**

Categories for Credit Risk	Derivative Contracts - (Note 1)						
	Foreign Exchange Contracts (Note 2)			Interest Rate Contracts			Total Derivative Contracts
	Up to 1 year	Over 1 to 5 years	Over 5 years	Up to 1 year	Over 1 to 5 years	Over 5 years	
	A	B	C	D	E	F	G =A+B+C+D+E+F
4. Total Claims on MDBs	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
4.1 Those fullfilling eligibility criteria (Note 6)							**0.00**
4.2 Those not fullfilling eligibility criteria:	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)							**0.00**
CQG 2 (A+ to A-)							**0.00**
CQG 3 (BBB+ to BBB-)							**0.00**
CQG 4 (BB+ to BB-)							**0.00**
CQG 5 (B+ to B-)							**0.00**
CQG 6 (Below B-)							**0.00**
Unrated							**0.00**
5. Total Claims on Banks	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
5.1 Total Claims on Licensed Banks							**0.00**
5.2 Total Claims on Foreign Banks	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
5.2.1 L/T Claims on Foreign Banks	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)							**0.00**
CQG 2 (A+ to A-)							**0.00**
CQG 3 (BBB+ to BBB-)							**0.00**
CQG 4 (BB+ to BB-)							**0.00**
CQG 5 (B+ to B-)							**0.00**
CQG 6 (Below B-)							**0.00**
Unrated							**0.00**
5.2.2 S/T Claims on Foreign Banks	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)							**0.00**
CQG 2 (A+ to A-)							**0.00**
CQG 3 (BBB+ to BBB-)							**0.00**
CQG 4 (BB+ to BB-)							**0.00**
CQG 5 (B+ to B-)							**0.00**
CQG 6 (Below B-)							**0.00**
Unrated							**0.00**
6. Total Claims on Corporates (Note 7)	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)							**0.00**
CQG 2 (A+ to A-)							**0.00**
CQG 3 (BBB+ to BBB-)							**0.00**
CQG 4 (BB+ to BB-)							**0.00**
CQG 5 (B+ to B-)							**0.00**
CQG 6 (Below B-)							**0.00**
Unrated							**0.00**
7. Regulatory Retail	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
7.1 Claims on Qualifying SMEs (Note 8)							**0.00**
7.2 Housing Loans Eligible for 75% RW (Note 9)							**0.00**
7.3 Other Retail (Note 10)							**0.00**

Categories for Credit Risk	Derivative Contracts - (Note 1)						
	Foreign Exchange Contracts (Note 2)			Interest Rate Contracts			Total Derivative Contracts
	Up to 1 year	Over 1 to 5 years	Over 5 years	Up to 1 year	Over 1 to 5 years	Over 5 years	
	A	B	C	D	E	F	G =A+B+C+D+E+F
8. RHLs Eligible for 35% RW (Note 11)							**0.00**
9. Past Due Exposures	0.00	0.00	0.00	0.00	0.00	0.00	**0.00**
9.1 Where specific provision less than 50%							**0.00**
9.2 Where specific provision 50% or more							**0.00**
9.3 Fully secured by unrecognized collateral							**0.00**
10. Other Exposures Not Reported Above	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
10.1 Venture Capital and private equity investment							**0.00**
10.2 Investment in Commercial Entities Below Materiality Thresholds							**0.00**
10.3 Loans Secured by Commercial Real Estate							**0.00**
10.4 Others							**0.00**
TOTAL BANKING BOOK	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**

Note (Table CR4a):

1. All nominal amounts of exposures should be reported net of specific provisions and before applying the eligible CRMs. In case of a guaranteed amount by an eligible guarantor, the exposure should be reported under the guarantor.
2. Including gold contracts.
3. Exposures should be segregated by Credit Quality Grades (CQG's).
4. Report domestic currency exposures to any other foreign sovereign that is assigned preferential risk weight by its own bank regulator.
5. International organisations refer to the IMF, BIS, ECB or EC.
6. Refer to paragraph No. 49 of the capital adequacy regulation for the eligibility criteria.
7. Include exposures to corporates, commercial companies owned by PSEs, securities and investment firms, insurance companies and enterprises that do not qualify for SMEs and underwriting of equity interest of 20% or less in insurance companies.
8. Include all exposures to SMEs which satisfy the criteria set out in paragraph No. 59 and 61 of the capital adequacy regulation.
9. Include only exposures related to those residential housing loans that satisfy the criteria set out in paragraph No. 64 of the capital adequacy regulation.
10. Include all exposures related to consumer and installment loans, credit cards, and small personal loans.
11. Report all exposures related to residential housing loans that satisfy the conditions set out in paragraphs No. 65 and 66 of the capital adequacy regulation.

CREDIT RISK – THE STANTARDISED APPROACH
Table CR4b - Credit Input Sheet
Replacement Cost
Off balance sheet exposures
Derivative Contract
For the quarter ending on / /

" In Thousand KD"

Categories for Credit Risk	Replacement Cost for Derivative Contracts - (Note 1)					
	Foreign Exchange Contracts			Interest Rate Contracts		
	Up to 1 year	Over 1 to 5 years	Over 5 years	Up to 1 year	Over 1 to 5 years	Over 5 years
	A	B	C	D	E	F
1. Claims on Sovereigns	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
1.1 Total State of Kuwait	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
State of Kuwait - Local Currency						
State of Kuwait - Foreign Currency						
1.2 Total Other GCC Sovereigns	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
Other GCC Sovereigns - Local Currency						
Other GCC Sovereigns - Foreign Currency						
1.3 Total Other Sovereigns	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)						
CQG 2 (A+ to A-)						
CQG 3 (BBB+ to BBB-)						
CQG 4 (BB+ to BB-)						
CQG 5 (B+ to B-)						
CQG 6 (Below B-)						
Unrated						
Preferentially Risk Weighted Domestic Claims **(Note 4)**						
2. Total International Organisations (Note 5)	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
3. Total Claims on PSEs	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
3.1 Total Kuwaiti PSEs	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
Kuwaiti PSEs - Local Currency						
Kuwaiti PSEs - Foreign Currency						
3.2 Total Other GCC PSEs	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
Other GCC PSEs - Local Currency						
Other GCC PSEs - Foreign Currency						
3.3 Total Foreign PSEs	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)						
CQG 2 (A+ to A-)						
CQG 3 (BBB+ to BBB-)						
CQG 4 (BB+ to BB-)						
CQG 5 (B+ to B-)						
CQG 6 (Below B-)						
Unrated						

Categories for Credit Risk	Replacement Cost for Derivative Contracts - (Note 1)					
	Foreign Exchange Contracts			Interest Rate Contracts		
	Up to 1 year	Over 1 to 5 years	Over 5 years	Up to 1 year	Over 1 to 5 years	Over 5 years
	A	B	C	D	E	F
4. Total Claims on MDBs	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
4.1 Those fullfilling eligibility criteria (Note 6)	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
4.2 Those not fullfilling eligibility criteria	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)						
CQG 2 (A+ to A-)						
CQG 3 (BBB+ to BBB-)						
CQG 4 (BB+ to BB-)						
CQG 5 (B+ to B-)						
CQG 6 (Below B-)						
Unrated						
5. Total Claims on Banks	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
5.1 Total Claims on Licensed Banks	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
5.2 Total Claims on Foreign Banks	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
5.2.1 L/T Claims on Foreign Banks	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)						
CQG 2 (A+ to A-)						
CQG 3 (BBB+ to BBB-)						
CQG 4 (BB+ to BB-)						
CQG 5 (B+ to B-)						
CQG 6 (Below B-)						
Unrated						
5.2.2 S/T Claims on Foreign Banks	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)						
CQG 2 (A+ to A-)						
CQG 3 (BBB+ to BBB-)						
CQG 4 (BB+ to BB-)						
CQG 5 (B+ to B-)						
CQG 6 (Below B-)						
Unrated						
6. Total Claims on Corporates	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)						
CQG 2 (A+ to A-)						
CQG 3 (BBB+ to BBB-)						
CQG 4 (BB+ to BB-)						
CQG 5 (B+ to B-)						
CQG 6 (Below B-)						
Unrated						
7. Regulatory Retail	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
7.1 Claims on Qualifying SMEs (Note 8)						
7.2 Housing Loans Eligible for 75% RW (Note 9)						
7.3 Other Retail (Note 10)						
8. RHLs Eligible for 35% RW (Note 11)	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**

Categories for Credit Risk	Replacement Cost for Derivative Contracts - (Note 1)					
	Foreign Exchange Contracts			Interest Rate Contracts		
	Up to 1 year	Over 1 to 5 years	Over 5 years	Up to 1 year	Over 1 to 5 years	Over 5 years
	A	B	C	D	E	F
9. Past Due Exposures	0.00	0.00	0.00	0.00	0.00	**0.00**
9.1 Where specific provision less than 50%						**0.00**
9.2 Where specific provision 50% or more						**0.00**
9.3 Fully secured by unrecognized collateral						**0.00**
10. Other Exposures Not Reported Above	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
10.1 Venture Capital and private equity investment						**0.00**
10.2 Investment in Commercial Entities Below Materiality Thresholds						**0.00**
10.3 Loans Secured by Commercial Real Estate						**0.00**
10.4 Others						**0.00**
TOTAL BANKING BOOK	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**

Note (Table CR4b):

1. All exposures should be reported net of specific provisions and before applying the eligible CRMs. In case of a guaranteed amount by an eligible guarantor, the exposure should be reported under the guarantor.
2. Including gold contracts.
3. Exposures should be segregated by Credit Quality Grades (CQG's).
4. Report domestic currency exposures to any other foreign sovereign that is assigned preferential risk weight by its own bank regulator.
5. International organisations refer to the IMF, BIS, ECB or EC.
6. Refer to paragraph No. 49 of the capital adequacy regulation for the eligibility criteria.
7. Include exposures to corporates, commercial companies owned by PSEs, securities and investment firms, insurance companies and enterprises that do not qualify for SMEs and underwriting of equity interest of 20% or less in insurance companies.
8. Include all exposures to SMEs which satisfy the criteria set out in paragraph No. 59 and 61 of the capital adequacy regulation.
9. Include only exposures related to those residential housing loans that satisfy the criteria set out in paragraph No. 64 of the capital adequacy regulation.
10. Include all exposures related to consumer and installment loans, credit cards, and small personal loans.
11. Report all exposures related to residential housing loans that satisfy the conditions set out in paragraphs No. 65 and 66 of the capital adequacy regulation.

CREDIT RISK – THE STANTARDISED APPROACH
Table CR2c - Credit Conversion Sheet
Off balance sheet exposures
Contingencies Credit Equivalent Amount

For the quarter ending on / /

" In Thousand KD"

Categories for Credit Risk	Off Balance Sheet - Credit Conversion Factors (CCF)		
	Trade-related Contingencies (Note 1)	**Transaction related Contingencies (Note 1)**	**Contingencies Credit Equivalent Amount**
	A= Table (CR2a), Column (A) * 20%	**B= Table (CR2a), Column (B) * 50%**	**C = A+B**
1. Claims on Sovereigns	**0.00**	**0.00**	**0.00**
1.1 Total State of Kuwait	0.00	0.00	0.00
State of Kuwait - Local Currency	0.00	0.00	0.00
State of Kuwait - Foreign Currency	0.00	0.00	0.00
1.2 Total Other GCC Sovereigns	0.00	0.00	0.00
Other GCC Sovereigns - Local Currency	0.00	0.00	0.00
Other GCC Sovereigns - Foreign Currency	0.00	0.00	0.00
1.3 Total Other Sovereigns (Note 3)	0.00	0.00	0.00
CQG 1 (AAA to AA-)	0.00	0.00	0.00
CQG 2 (A+ to A-)	0.00	0.00	0.00
CQG 3 (BBB+ to BBB-)	0.00	0.00	0.00
CQG 4 (BB+ to BB-)	0.00	0.00	0.00
CQG 5 (B+ to B-)	0.00	0.00	0.00
CQG 6 (Below B-)	0.00	0.00	0.00
Unrated	0.00	0.00	0.00
Preferentially Risk Weighted Domestic Claims	0.00	0.00	0.00
2. Total International Organisations	**0.00**	**0.00**	**0.00**
3. Total Claims on PSEs	**0.00**	**0.00**	**0.00**
3.1 Total Kuwaiti PSEs	0.00	0.00	0.00
Kuwaiti PSEs - Local Currency	0.00	0.00	0.00
Kuwaiti PSEs - Foreign Currency	0.00	0.00	0.00
3.2 Total Other GCC PSEs	0.00	0.00	0.00
Other GCC PSEs - Local Currency	0.00	0.00	0.00
Other GCC PSEs - Foreign Currency	0.00	0.00	0.00
3.3 Total Foreign PSEs	0.00	0.00	0.00
CQG 1 (AAA to AA-)	0.00	0.00	0.00
CQG 2 (A+ to A-)	0.00	0.00	0.00
CQG 3 (BBB+ to BBB-)	0.00	0.00	0.00
CQG 4 (BB+ to BB-)	0.00	0.00	0.00
CQG 5 (B+ to B-)	0.00	0.00	0.00
CQG 6 (Below B-)	0.00	0.00	0.00
Unrated	0.00	0.00	0.00

Categories for Credit Risk	Off Balance Sheet - Credit Conversion Factors (CCF)		
	Trade-related Contingencies (Note 1)	**Transaction related Contingencies (Note 1)**	**Contingencies Credit Equivalent Amount**
	A= Table (CR2a), Column (A) * 20%	**B= Table (CR2a), Column (B) * 50%**	**C = A+B**
4. Total Claims on MDBs	**0.00**	**0.00**	**0.00**
4.1 Those fullfilling eligibility criteria (Note 5)	0.00	0.00	0.00
4.2 Those not fullfilling eligibility criteria:	0.00	0.00	0.00
CQG 1 (AAA to AA-)	0.00	0.00	0.00
CQG 2 (A+ to A-)	0.00	0.00	0.00
CQG 3 (BBB+ to BBB-)	0.00	0.00	0.00
CQG 4 (BB+ to BB-)	0.00	0.00	0.00
CQG 5 (B+ to B-)	0.00	0.00	0.00
CQG 6 (Below B-)	0.00	0.00	0.00
Unrated	0.00	0.00	0.00
5. Total Claims on Banks	**0.00**	**0.00**	**0.00**
5.1 Total Claims on Licensed Banks	0.00	0.00	0.00
5.2 Total Claims on Foreign Banks	0.00	0.00	0.00
5.2.1 L/T Claims on Foreign Banks	0.00	0.00	0.00
CQG 1 (AAA to AA-)	0.00	0.00	0.00
CQG 2 (A+ to A-)	0.00	0.00	0.00
CQG 3 (BBB+ to BBB-)	0.00	0.00	0.00
CQG 4 (BB+ to BB-)	0.00	0.00	0.00
CQG 5 (B+ to B-)	0.00	0.00	0.00
CQG 6 (Below B-)	0.00	0.00	0.00
Unrated	0.00	0.00	0.00
5.2.2 S/T Claims on Foreign Banks	0.00	0.00	0.00
CQG 1 (AAA to AA-)	0.00	0.00	0.00
CQG 2 (A+ to A-)	0.00	0.00	0.00
CQG 3 (BBB+ to BBB-)	0.00	0.00	0.00
CQG 4 (BB+ to BB-)	0.00	0.00	0.00
CQG 5 (B+ to B-)	0.00	0.00	0.00
CQG 6 (Below B-)	0.00	0.00	0.00
Unrated	0.00	0.00	`
6. Total Claims on Corporates	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)	0.00	0.00	0.00
CQG 2 (A+ to A-)	0.00	0.00	0.00
CQG 3 (BBB+ to BBB-)	0.00	0.00	0.00
CQG 4 (BB+ to BB-)	0.00	0.00	0.00
CQG 5 (B+ to B-)	0.00	0.00	0.00
CQG 6 (Below B-)	0.00	0.00	0.00
Unrated	0.00	0.00	0.00
7. Regulatory Retail	**0.00**	**0.00**	**0.00**
7.1 Claims on Qualifying SMEs	0.00	0.00	0.00
7.2 Housing Loans Eligible for 75% RW	0.00	0.00	0.00
7.3 Other Retail	0.00	0.00	0.00

Categories for Credit Risk	Off Balance Sheet - Credit Conversion Factors (CCF)		
	Trade-related Contingencies (Note 1)	Transaction related Contingencies (Note 1)	Contingencies Credit Equivalent Amount
	A= Table (CR2a), Column (A) * 20%	B= Table (CR2a), Column (B) * 50%	C = A+B
8. RHLs Eligible for 35% RW	**0.00**	**0.00**	**0.00**
9. Past Due Exposures	0.00	0.00	**0.00**
9.1 Where specific provision less than 50%	0.00	0.00	**0.00**
9.2 Where specific provision 50% or more	0.00	0.00	**0.00**
9.3 Fully secured by unrecognized collateral	0.00	0.00	**0.00**
10. Other Exposures Not Reported Above	**0.00**	**0.00**	**0.00**
10.1 Venture Capital and private equity investment	**0.00**	**0.00**	**0.00**
10.2 Investment in Commercial Entities Below Materiality Thresholds	**0.00**	**0.00**	**0.00**
10.3 Loans Secured by Commercial Real Estate	**0.00**	**0.00**	**0.00**
10.4 Others	**0.00**	**0.00**	**0.00**
TOTAL BANKING BOOK OBS	**0.00**	**0.00**	**0.00**

Note:

1. Refer to paragraph No. 122 of the capital adequacy regulations for the components of trade-related and transaction-related contingencies.

CREDIT RISK – THE STANTARDISED APPROACH
Table CR3c - Credit Conversion Sheet
Off balance sheet exposures
Commitments Credit Equivalent Amount

For the quarter ending on / /

" In Thousand KD"

Categories for Credit Risk	Off Balance Sheet (OBS)					
	Direct Credit Substitutes	Notes Issuance and Revolving Underwriting Facilities	Asset Sale with Recourse/ Forward Asset Purchases/ Partly Paid Shares / Forward Deposits	Other Commitments		Total Commitments
				Up to 1 year	Over 1 year	
	A= Table CR3a, Column A*100%	B= Table CR3a, Column B *50%	C= Table CR3a, Column C * 100%	D= Table CR3a, Column E * 20%	E= Table CR3a, Column F * 50%	F =A+B+C+D+E
1. Claims on Sovereigns	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
1.1 Total State of Kuwait	0.00	0.00	0.00	0.00	0.00	0.00
State of Kuwait - Local Currency	0.00	0.00	0.00	0.00	0.00	0.00
State of Kuwait - Foreign Currency	0.00	0.00	0.00	0.00	0.00	0.00
1.2 Total Other GCC Sovereigns	0.00	0.00	0.00	0.00	0.00	0.00
Other GCC Sovereigns - Local Currency	0.00	0.00	0.00	0.00	0.00	0.00
Other GCC Sovereigns - Foreign Currency	0.00	0.00	0.00	0.00	0.00	0.00
1.3 Total Other Sovereigns	0.00	0.00	0.00	0.00	0.00	0.00
CQG 1 (AAA to AA-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 2 (A+ to A-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 3 (BBB+ to BBB-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 4 (BB+ to BB-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 5 (B+ to B-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 6 (Below B-)	0.00	0.00	0.00	0.00	0.00	0.00
Unrated	0.00	0.00	0.00	0.00	0.00	0.00
Preferentially Risk Weighted Domestic Claims	0.00	0.00	0.00	0.00	0.00	0.00
2. Total International Organisations	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
3. Total Claims on PSEs	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
3.1 Total Kuwaiti PSEs	0.00	0.00	0.00	0.00	0.00	0.00
Kuwaiti PSEs - Local Currency	0.00	0.00	0.00	0.00	0.00	0.00
Kuwaiti PSEs - Foreign Currency	0.00	0.00	0.00	0.00	0.00	0.00
3.2 Total Other GCC PSEs	0.00	0.00	0.00	0.00	0.00	0.00
Other GCC PSEs - Local Currency	0.00	0.00	0.00	0.00	0.00	0.00
Other GCC PSEs - Foreign Currency	0.00	0.00	0.00	0.00	0.00	0.00
3.3 Total Foreign PSEs	0.00	0.00	0.00	0.00	0.00	0.00
CQG 1 (AAA to AA-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 2 (A+ to A-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 3 (BBB+ to BBB-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 4 (BB+ to BB-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 5 (B+ to B-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 6 (Below B-)	0.00	0.00	0.00	0.00	0.00	0.00
Unrated	0.00	0.00	0.00	0.00	0.00	0.00

Categories for Credit Risk	Off Balance Sheet (OBS)					
	Direct Credit Substitutes	Notes Issuance and Revolving Underwriting Facilities	Asset Sale with Recourse/ Forward Asset Purchases/ Partly Paid Shares / Forward Deposits	Other Commitments		Total Commitments
				Up to 1 year	Over 1 year	
	A= Table CR3a, Column A*100%	B= Table CR3a, Column B *50%	C= Table CR3a, Column C * 100%	D= Table CR3a, Column E * 20%	E= Table CR3a, Column F * 50%	F =A+B+C+D+E
4. Total Claims on MDBs	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
4.1 Those fullfilling eligibility criteria (Note 5)	0.00	0.00	0.00	0.00	0.00	0.00
4.2 Those not fullfilling eligibility criteria:	0.00	0.00	0.00	0.00	0.00	0.00
CQG 1 (AAA to AA-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 2 (A+ to A-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 3 (BBB+ to BBB-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 4 (BB+ to BB-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 5 (B+ to B-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 6 (Below B-)	0.00	0.00	0.00	0.00	0.00	0.00
Unrated	0.00	0.00	0.00	0.00	0.00	0.00
5. Total Claims on Banks	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
5.1 Total Claims on Licensed Banks	0.00	0.00	0.00	0.00	0.00	0.00
5.2 Total Claims on Foreign Banks	0.00	0.00	0.00	0.00	0.00	0.00
5.2.1 L/T Claims on Foreign Banks	0.00	0.00	0.00	0.00	0.00	0.00
CQG 1 (AAA to AA-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 2 (A+ to A-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 3 (BBB+ to BBB-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 4 (BB+ to BB-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 5 (B+ to B-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 6 (Below B-)	0.00	0.00	0.00	0.00	0.00	0.00
Unrated	0.00	0.00	0.00	0.00	0.00	0.00
5.2.2 S/T Claims on Foreign Banks	0.00	0.00	0.00	0.00	0.00	0.00
CQG 1 (AAA to AA-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 2 (A+ to A-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 3 (BBB+ to BBB-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 4 (BB+ to BB-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 5 (B+ to B-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 6 (Below B-)	0.00	0.00	0.00	0.00	0.00	0.00
Unrated	0.00	0.00	0.00	0.00	0.00	0.00
6. Total Claims on Corporates	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 2 (A+ to A-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 3 (BBB+ to BBB-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 4 (BB+ to BB-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 5 (B+ to B-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 6 (Below B-)	0.00	0.00	0.00	0.00	0.00	0.00
Unrated	0.00	0.00	0.00	0.00	0.00	0.00
7. Credit Derivative Claims (Protection Seller)	**0.00**	[redacted]				**0.00**
7.1 Long Term Claims	**0.00**					**0.00**
CQG 1 (AAA to AA-)	0.00					0.00
CQG 2 (A+ to A-)	0.00					0.00
CQG 3 (BBB+ to BBB-)	0.00					0.00
CQG 4 (BB+ to BB-)	0.00					0.00

Categories for Credit Risk	Off Balance Sheet (OBS)					
	Direct Credit Substitutes	Notes Issuance and Revolving Underwriting Facilities	Asset Sale with Recourse/ Forward Asset Purchases/ Partly Paid Shares / Forward Deposits	Other Commitments		Total Commitments
				Up to 1 year	Over 1 year	
	A= Table CR3a, Column A*100%	B= Table CR3a, Column B *50%	C= Table CR3a, Column C * 100%	D= Table CR3a, Column E * 20%	E= Table CR3a, Column F * 50%	F =A+B+C+D+E
7.2 Short Term Claims	**0.00**	[redacted]	[redacted]	[redacted]	[redacted]	**0.00**
CQG 1 (AAA to AA-)	0.00	[redacted]	[redacted]	[redacted]	[redacted]	0.00
CQG 2 (A+ to A-)	0.00	[redacted]	[redacted]	[redacted]	[redacted]	0.00
CQG 3 (BBB+ to BBB-)	0.00	[redacted]	[redacted]	[redacted]	[redacted]	0.00
7.3 Unrated	**0.00**	[redacted]	[redacted]	[redacted]	[redacted]	**0.00**
8. Regulatory Retail	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
8.1 Claims on Qualifying SMEs	0.00	0.00	0.00	0.00	0.00	0.00
8.2 Housing Loans Eligible for 75% RW	0.00	0.00	0.00	0.00	0.00	0.00
8.3 Other Retail	0.00	0.00	0.00	0.00	0.00	0.00
9. RHLs Eligible for 35% RW	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
10. Past Due Exposures	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
10.1 Where specific provision less than 50%	0.00	0.00	0.00	0.00	0.00	**0.00**
10.2 Where specific provision 50% or more	0.00	0.00	0.00	0.00	0.00	**0.00**
10.3 Fully secured by unrecognized collateral	0.00	0.00	0.00	0.00	0.00	**0.00**
11. Other Exposures Not Reported Above	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
11.1 Venture Capital and private equity investment	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
11.2 Investment in Commercial Entities Below Materiality Thresholds	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
11.3 Loans Secured by Commercial Real Estate	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
11.4 Others	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
TOTAL BANKING BOOK OBS	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**

CREDIT RISK – THE STANTARDISED APPROACH
Table CR4c - Credit Conversion Sheet
Off balance sheet exposures
Derivative Contracts Credit Equivalent Amount

For the quarter ending on / /

" In Thousand KD"

Categories for Credit Risk	Derivatives Contracts - Credit Equivalent Amounts (CEAs)					
	Foreign Exchange Contracts			Interest Rate Contracts		Total Credit Equivalent Amount
	Up to 1 year	Over 1 to 5 years	Over 5 years	Over 1 to 5 years	Over 5 years	
	A=(Table CR4a, Column A * 1%) + Table CR4b Column A - Note 1	B= (Table CR4a, Column B * 5%) + Table CR4b Column B	C= (Table CR4a, Column C * 7.5%) + Table CR Column C	D = (Table CR4a, Column E *0.5%) + Table CR Column E	E=(Table CR4a, Column F * 1.5%) + Table CR Column F	F=A+B+C+D+E
1. Claims on Sovereigns	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
1.1 Total State of Kuwait	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
State of Kuwait - Local Currency	0.00	0.00	0.00	0.00	0.00	0.00
State of Kuwait - Foreign Currency	0.00	0.00	0.00	0.00	0.00	0.00
1.2 Total Other GCC Sovereigns	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
Other GCC Sovereigns - Local Currency	0.00	0.00	0.00	0.00	0.00	0.00
Other GCC Sovereigns - Foreign Currency	0.00	0.00	0.00	0.00	0.00	0.00
1.3 Total Other Sovereigns	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 2 (A+ to A-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 3 (BBB+ to BBB-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 4 (BB+ to BB-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 5 (B+ to B-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 6 (Below B-)	0.00	0.00	0.00	0.00	0.00	0.00
Unrated	0.00	0.00	0.00	0.00	0.00	0.00
Preferentially Risk Weighted Domestic Currency Claims	0.00	0.00	0.00	0.00	0.00	0.00
2. Total International Organisations	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
3. Total Claims on PSEs	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
3.1 Total Kuwaiti PSEs	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
Kuwaiti PSEs - Local Currency	0.00	0.00	0.00	0.00	0.00	0.00
Kuwaiti PSEs - Foreign Currency	0.00	0.00	0.00	0.00	0.00	0.00
3.2 Total Other GCC PSEs	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
Other GCC PSEs - Local Currency	0.00	0.00	0.00	0.00	0.00	0.00
Other GCC PSEs - Foreign Currency	0.00	0.00	0.00	0.00	0.00	0.00
3.3 Total Foreign PSEs	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 2 (A+ to A-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 3 (BBB+ to BBB-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 4 (BB+ to BB-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 5 (B+ to B-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 6 (Below B-)	0.00	0.00	0.00	0.00	0.00	0.00
Unrated	0.00	0.00	0.00	0.00	0.00	0.00

Categories for Credit Risk	Derivatives Contracts - Credit Equivalent Amounts (CEAs)					
	Foreign Exchange Contracts			Interest Rate Contracts		Total Credit Equivalent Amount
	Up to 1 year	Over 1 to 5 years	Over 5 years	Over 1 to 5 years	Over 5 years	
	A=(Table CR4a, Column A * 1%) + Table CR4b Column A - Note 1	B= (Table CR4a, Column B * 5%) + Table CR4b Column B	C= (Table CR4a, Column C * 7.5%) + Table CR Column C	D = (Table CR4a, Column E *0.5%) + Table CR Column E	E=(Table CR4a, Column F * 1.5%) + Table CR Column F	F=A+B+C+D+E
4. Total Claims on MDBs	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
4.1 Those fullfilling eligibility criteria (Note 6)	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	0.00
4.2 Those not fullfilling eligibility criteria	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	0.00
CQG 1 (AAA to AA-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 2 (A+ to A-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 3 (BBB+ to BBB-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 4 (BB+ to BB-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 5 (B+ to B-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 6 (Below B-)	0.00	0.00	0.00	0.00	0.00	0.00
Unrated	0.00	0.00	0.00	0.00	0.00	0.00
5. Total Claims on Banks	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
5.1 Total Claims on Licensed Banks	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
5.2 Total Claims on Foreign Banks	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
5.2.1 L/T Claims on Foreign Banks	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 2 (A+ to A-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 3 (BBB+ to BBB-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 4 (BB+ to BB-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 5 (B+ to B-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 6 (Below B-)	0.00	0.00	0.00	0.00	0.00	0.00
Unrated	0.00	0.00	0.00	0.00	0.00	0.00
5.2.2 S/T Claims on Foreign Banks	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 2 (A+ to A-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 3 (BBB+ to BBB-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 4 (BB+ to BB-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 5 (B+ to B-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 6 (Below B-)	0.00	0.00	0.00	0.00	0.00	0.00
Unrated	0.00	0.00	0.00	0.00	0.00	0.00
6. Total Claims on Corporates	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 2 (A+ to A-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 3 (BBB+ to BBB-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 4 (BB+ to BB-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 5 (B+ to B-)	0.00	0.00	0.00	0.00	0.00	0.00
CQG 6 (Below B-)	0.00	0.00	0.00	0.00	0.00	0.00
Unrated	0.00	0.00	0.00	0.00	0.00	0.00
7. Regulatory Retail	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
7.1 Claims on Qualifying SMEs (Note 8)	0.00	0.00	0.00	0.00	0.00	0.00
7.2 Housing Loans Eligible for 75% RW (Note 9)	0.00	0.00	0.00	0.00	0.00	0.00
7.3 Other Retail (Note 10)	0.00	0.00	0.00	0.00	0.00	0.00

Categories for Credit Risk	Derivatives Contracts - Credit Equivalent Amounts (CEAs)					
	Foreign Exchange Contracts			Interest Rate Contracts		Total Credit Equivalent Amount
	Up to 1 year	Over 1 to 5 years	Over 5 years	Over 1 to 5 years	Over 5 years	
	A=(Table CR4a, Column A * 1%) + Table CR4b Column A - Note 1	**B= (Table CR4a, Column B * 5%) + Table CR4b Column B**	**C= (Table CR4a, Column C * 7.5%) + Table CR Column C**	**D = (Table CR4a, Column E *0.5%) + Table CR Column E**	**E=(Table CR4a, Column F * 1.5%) + Table CR Column F**	**F=A+B+C+D+E**
8. RHLs Eligible for 35% RW (Note 11)	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
9. Past Due Exposures	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
9.1 Where specific provision less than 50%	0.00	0.00	0.00	0.00	0.00	**0.00**
9.2 Where specific provision 50% or more	0.00	0.00	0.00	0.00	0.00	**0.00**
9.3 Fully secured by unrecognized collateral	0.00	0.00	0.00	0.00	0.00	**0.00**
10. Other Exposures Not Reported Above	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
10.1 Venture Capital and private equity investment	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
10.2 Investment in Commercial Entities Below Materiality Thresholds	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
10.3 Loans Secured by Commercial Real Estate	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
10.4 Others	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
TOTAL BANKING BOOK	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**

Note (Table CR4c):

1- Banks have to add the replacement cost of their derivatives, which is the mark to market value of the derivative.

CREDIT RISK – THE STANTARDISED APPROACH
Table CR5a – Risk Weighted Assets
Total Credit Exposure before CRM

For the quarter ending on / /

“ In Thousand KD”

Asset Categories for Credit Risk	On Balance Sheet	Off Balance Sheet			
	Outstanding from Table CR1 column A	Contingencies Credit Equivalent from Table CR2c – Column C	Commitments Credit Equivalent from Table CR3c - Column G	Derivatives Credit Equivalent from Table CR4c - Column F	Credit Exposure – before CRM
	A	B	C	D	E=A+B+C+D
1. Cash items	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
1.1 Notes and Coins	0.00				0.00
1.2 Gold Bullions Held and backed by gold bullion liabilities	0.00				0.00
1.3 Cheques and Drafts Drawn on other Banks and Immediately Payable or in the Process of Collection	0.00				0.00
1.4 Receiveable Funds arising from the sale of securities	0.00				0.00
1.5 Receiveable Funds arising from the purchase of securities	0.00				0.00
2. Total Claims on Sovereigns	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
2.1 Total State of Kuwait	0.00	0.00	0.00	0.00	0.00
State of Kuwait - Local Currency	0.00	0.00	0.00	0.00	0.00
State of Kuwait - Foreign Currency	0.00	0.00	0.00	0.00	0.00
2.2 Total Other GCC Sovereigns	0.00	0.00	0.00	0.00	0.00
Other GCC Sovereigns- Local Currencies	0.00	0.00	0.00	0.00	0.00
Other GCC Sovereigns- Foreign Currencies	0.00	0.00	0.00	0.00	0.00
2.3 Total Claims on Other Sovereigns	0.00	0.00	0.00	0.00	0.00
CQG 1 (AAA to AA-)	0.00	0.00	0.00	0.00	0.00
CQG 2 (A+ to A-)	0.00	0.00	0.00	0.00	0.00
CQG 3 (BBB+ to BBB-)	0.00	0.00	0.00	0.00	0.00
CQG 4 (BB+ to BB-)	0.00	0.00	0.00	0.00	0.00
CQG 5 (B+ to B-)	0.00	0.00	0.00	0.00	0.00
CQG 6 (Below B-)	0.00	0.00	0.00	0.00	0.00
Unrated	0.00	0.00	0.00	0.00	0.00
Preferentially Risk Weighted Domestic Currency Claims	0.00	0.00	0.00	0.00	0.00
3. Total Claims on International Organisations	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
4. Total Claims on PSEs	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
4.1 Total Kuwaiti PSEs	0.00	0.00	0.00	0.00	0.00
Kuwaiti PSEs - Local Currency	0.00	0.00	0.00	0.00	0.00
Kuwaiti PSEs - Foreign Currency	0.00	0.00	0.00	0.00	0.00
4.2 Total Other GCC PSEs	0.00	0.00	0.00	0.00	0.00
Other GCC PSEs- Local Currencies	0.00	0.00	0.00	0.00	0.00
Other GCC PSEs- Foreign Currencies	0.00	0.00	0.00	0.00	0.00

Asset Categories for Credit Risk	On Balance Sheet	Off Balance Sheet			
	Outstanding from Table CR1 column A	Contingencies Credit Equivalent from Table CR2c – Column C	Commitments Credit Equivalent from Table CR3c - Column G	Derivatives Credit Equivalent from Table CR4c - Column F	Credit Exposure – before CRM
	A	B	C	D	E=A+B+C+D
4.3 Total Foreign PSEs	0.00	0.00	0.00	0.00	0.00
CQG 1 (AAA to AA-)	0.00	0.00	0.00	0.00	0.00
CQG 2 (A+ to A-)	0.00	0.00	0.00	0.00	0.00
CQG 3 (BBB+ to BBB-)	0.00	0.00	0.00	0.00	0.00
CQG 4 (BB+ to BB-)	0.00	0.00	0.00	0.00	0.00
CQG 5 (B+ to B-)	0.00	0.00	0.00	0.00	0.00
CQG 6 (Below B-)	0.00	0.00	0.00	0.00	0.00
Unrated	0.00	0.00	0.00	0.00	0.00
5. Total Claims on MDBs	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
5.1 Those fulfilling eligibility criteria	0.00	0.00	0.00	0.00	0.00
5.2 Those not fulfilling eligibility criteria	0.00	0.00	0.00	0.00	0.00
CQG 1 (AAA to AA-)	0.00	0.00	0.00	0.00	0.00
CQG 2 (A+ to A-)	0.00	0.00	0.00	0.00	0.00
CQG 3 (BBB+ to BBB-)	0.00	0.00	0.00	0.00	0.00
CQG 4 (BB+ to BB-)	0.00	0.00	0.00	0.00	0.00
CQG 5 (B+ to B-)	0.00	0.00	0.00	0.00	0.00
CQG 6 (Below B-)	0.00	0.00	0.00	0.00	0.00
Unrated	0.00	0.00	0.00	0.00	0.00
6. Total Claims on Banks	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
6.1 Total Claims on Licensed Banks	0.00	0.00	0.00	0.00	0.00
6.2 Total Claims on Foreign Banks	0.00	0.00	0.00	0.00	0.00
6.2.1 L/ T Claims on Foreign Banks	0.00	0.00	0.00	0.00	0.00
CQG 1 (AAA to AA-)	0.00	0.00	0.00	0.00	0.00
CQG 2 (A+ to A-)	0.00	0.00	0.00	0.00	0.00
CQG 3 (BBB+ to BBB-)	0.00	0.00	0.00	0.00	0.00
CQG 4 (BB+ to BB-)	0.00	0.00	0.00	0.00	0.00
CQG 5 (B+ to B-)	0.00	0.00	0.00	0.00	0.00
CQG 6 (Below B-)	0.00	0.00	0.00	0.00	0.00
Unrated	0.00	0.00	0.00	0.00	0.00
6.2.2 S/ T Claims on Foreign Banks	0.00	0.00	0.00	0.00	0.00
CQG 1 (AAA to AA-)	0.00	0.00	0.00	0.00	0.00
CQG 2 (A+ to A-)	0.00	0.00	0.00	0.00	0.00
CQG 3 (BBB+ to BBB-)	0.00	0.00	0.00	0.00	0.00
CQG 4 (BB+ to BB-)	0.00	0.00	0.00	0.00	0.00
CQG 5 (B+ to B-)	0.00	0.00	0.00	0.00	0.00
CQG 6 (Below B-)	0.00	0.00	0.00	0.00	0.00
Unrated	0.00	0.00	0.00	0.00	0.00
7. Claims on Corporates	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)	0.00	0.00	0.00	0.00	0.00
CQG 2 (A+ to A-)	0.00	0.00	0.00	0.00	0.00
CQG 3 (BBB+ to BBB-)	0.00	0.00	0.00	0.00	0.00
CQG 4 (BB+ to BB-)	0.00	0.00	0.00	0.00	0.00
CQG 5 (B+ to B-)	0.00	0.00	0.00	0.00	0.00
CQG 6 (Below B-)	0.00	0.00	0.00	0.00	0.00
Unrated	0.00	0.00	0.00	0.00	0.00

Asset Categories for Credit Risk	On Balance Sheet	Off Balance Sheet			
	Outstanding from Table CR1 column A	Contingencies Credit Equivalent from Table CR2c – Column C	Commitments Credit Equivalent from Table CR3c - Column G	Derivatives Credit Equivalent from Table CR4c - Column F	Credit Exposure – before CRM
	A	**B**	**C**	**D**	**E=A+B+C+D**
8. Claims on Securitised Assets (as Investor)	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
8.1 Long Term Claims	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)	0.00	0.00	0.00	0.00	0.00
CQG 2 (A+ to A-)	0.00	0.00	0.00	0.00	0.00
CQG 3 (BBB+ to BBB-)	0.00	0.00	0.00	0.00	0.00
CQG 4 (BB+ to BB-)	0.00	0.00	0.00	0.00	0.00
8.2 Short Term Claims	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
CQG 1 (AAA to AA-)	0.00	0.00	0.00	0.00	0.00
CQG 2 (A+ to A-)	0.00	0.00	0.00	0.00	0.00
CQG 3 (BBB+ to BBB-)	0.00	0.00	0.00	0.00	0.00
9. Credit Derivative Claims (Protection Seller)			**0.00**		**0.00**
9.1 Long Term Claims			**0.00**		**0.00**
CQG 1 (AAA to AA-)			0.00		0.00
CQG 2 (A+ to A-)			0.00		0.00
CQG 3 (BBB+ to BBB-)			0.00		0.00
CQG 4 (BB+ to BB-)			0.00		0.00
9.1 Short Term Claims			**0.00**		**0.00**
CQG 1 (AAA to AA-)			0.00		0.00
CQG 2 (A+ to A-)			0.00		0.00
CQG 3 (BBB+ to BBB-)			0.00		0.00
9.3 Unrated Claims			**0.00**		**0.00**
10. Regulatory Retail	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
10.1 Claims on Qualifying SMEs	0.00	0.00	0.00	0.00	0.00
10.2 Housing Loans Eligible for 75% RW	0.00	0.00	0.00	0.00	0.00
10.3 Other Retail Loans	0.00	0.00	0.00	0.00	0.00
11. RHLs Eligible for 35% RW	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
12. Past Due Exposures	0.00	0.00	0.00	0.00	0.00
12.1 Where Specific Provision less than 50%	0.00	0.00	0.00	0.00	0.00
12.2 Where Specific Provision 50% or more	0.00	0.00	0.00	0.00	0.00
12.3 For RHLs where specific provision is 20% or more	0.00	0.00	0.00	0.00	0.00
12.4 For RHLs where specific provision is less than 20%	0.00	0.00	0.00	0.00	0.00
12.5 Fully secured by unrecognized collateral	0.00	0.00	0.00	0.00	0.00
13. Other Assets	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
13.1 Venture Capital and private equity investment	0.00	0.00	0.00	0.00	0.00
13.2 Investment in Commercial Entities Below Materiality Thresholds	0.00	0.00	0.00	0.00	0.00
13.3 Loans Secured by Commercial Real Estate	0.00	0.00	0.00	0.00	0.00
13.4 Others	0.00	0.00	0.00	0.00	0.00
TOTAL BANKING BOOK ASSETS	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**

CREDIT RISK – THE STANTARDISED APPROACH
Table CR5b – Risk Weighted Assets
Credit Risk Mitigation and Risk Weighting

For the quarter ending on / /

“ In Thousand KD”

Asset Categories for Credit Risk	Credit Exposure before CRM from Table CR5a Column E	Adjustment for Credit Risk Mitigation (CRM) (Notes 1)	Net Credit Exposure after CRM	Risk Weights	Credit Risk Weighted Asset
	A	**B**	**C =A - B**	**D**	**E= C * D**
1. Cash items	**0.00**	**0.00**	**0.00**		**0.00**
1.1 Notes and Coins	0.00		0.00	**0.00**	0.00
1.2 Gold Bullions Held and backed by gold bullion liabilities	0.00		0.00	**0.00**	0.00
1.3 Cheques and Drafts Drawn on other Banks and Immediately Payable or in the Process of Collection	0.00		0.00	**0.00**	0.00
1.4 Receiveable Funds arising from the sale of securities	0.00		0.00	**0.00**	0.00
1.5 Receiveable Funds arising from the purchase of securities	0.00		0.00	**0.00**	0.00
2.Total Claims on Sovereigns	**0.00**	**0.00**	**0.00**		**0.00**
2.1 Total State of Kuwait	0.00	0.00	0.00	**0.00**	0.00
State of Kuwait - Local Currency	0.00		0.00	**0.00**	0.00
State of Kuwait - Foreign Currency	0.00		0.00	**0.00**	0.00
2.2 Total Other GCC Sovereigns	0.00	0.00	0.00	**0.00**	0.00
Other GCC Sovereigns- Local Currencies	0.00		0.00	**0.00**	0.00
Other GCC Sovereigns- Foreign Currencies	0.00		0.00	**0.00**	0.00
2.3 Total Claims on Other Sovereigns	0.00	0.00	0.00		0.00
CQG 1 (AAA to AA-)	0.00		0.00	**0.00**	0.00
CQG 2 (A+ to A-)	0.00		0.00	**0.20**	0.00
CQG 3 (BBB+ to BBB-)	0.00		0.00	**0.50**	0.00
CQG 4 (BB+ to BB-)	0.00		0.00	**1.00**	0.00
CQG 5 (B+ to B-)	0.00		0.00	**1.00**	0.00
CQG 6 (Below B-)	0.00		0.00	**1.50**	0.00
Unrated	0.00		0.00	**1.00**	0.00
Preferentially Risk Weighted Domestic Currency Claims	0.00		0.00	**0.00**	0.00
3. Total Claims on International Organisations	**0.00**		**0.00**	**0.00**	**0.00**
4. Total Claims on PSEs	**0.00**	**0.00**	**0.00**		**0.00**
4.1 Total Kuwaiti PSEs	0.00	0.00	0.00		0.00
Kuwaiti PSEs - Local Currency	0.00		0.00	**0.00**	0.00
Kuwaiti PSEs - Foreign Currency	0.00		0.00	**0.20**	0.00
4.2 Total Other GCC PSEs	0.00	0.00	0.00		0.00
Other GCC PSEs- Local Currencies	0.00		0.00	**0.00**	0.00
Other GCC PSEs- Foreign Currencies	0.00		0.00	**0.20**	0.00

Asset Categories for Credit Risk	Credit Exposure before CRM from Table CR5a Column E	Adjustment for Credit Risk Mitigation (CRM) (Notes 1)	Net Credit Exposure after CRM	Risk Weights	Credit Risk Weighted Asset
	A	**B**	**C =A - B**	**D**	**E= C * D**
4.3 Total Foreign PSEs	0.00	0.00	0.00		0.00
CQG 1 (AAA to AA-)	0.00		0.00	**0.20**	0.00
CQG 2 (A+ to A-)	0.00		0.00	**0.50**	0.00
CQG 3 (BBB+ to BBB-)	0.00		0.00	**1.00**	0.00
CQG 4 (BB+ to BB-)	0.00		0.00	**1.00**	0.00
CQG 5 (B+ to B-)	0.00		0.00	**1.00**	0.00
CQG 6 (Below B-)	0.00		0.00	**1.50**	0.00
Unrated	0.00		0.00	**1.00**	0.00
5. Total Claims on MDBs	**0.00**	**0.00**	**0.00**		**0.00**
5.1 Those fulfilling eligibility criteria	0.00		0.00	**0.00**	0.00
5.2 Those not fulfilling eligibility criteria	0.00	0.00	0.00		0.00
CQG 1 (AAA to AA-)	0.00		0.00	**0.20**	0.00
CQG 2 (A+ to A-)	0.00		0.00	**0.50**	0.00
CQG 3 (BBB+ to BBB-)	0.00		0.00	**0.50**	0.00
CQG 4 (BB+ to BB-)	0.00		0.00	**1.00**	0.00
CQG 5 (B+ to B-)	0.00		0.00	**1.00**	0.00
CQG 6 (Below B-)	0.00		0.00	**1.50**	0.00
Unrated	0.00		0.00	**0.50**	0.00
6. Total Claims on Banks	**0.00**	**0.00**	**0.00**		**0.00**
6.1 Total Claims on Licensed Banks	0.00		0.00	**0.20**	0.00
6.2 Total Claims on Foreign Banks	0.00	0.00	0.00		0.00
6.2.1 L/ T Claims on Foreign Banks	0.00	0.00	0.00		0.00
CQG 1 (AAA to AA-)	0.00		0.00	**0.20**	0.00
CQG 2 (A+ to A-)	0.00		0.00	**0.50**	0.00
CQG 3 (BBB+ to BBB-)	0.00		0.00	**0.50**	0.00
CQG 4 (BB+ to BB-)	0.00		0.00	**1.00**	0.00
CQG 5 (B+ to B-)	0.00		0.00	**1.00**	0.00
CQG 6 (Below B-)	0.00		0.00	**1.50**	0.00
Unrated	0.00		0.00	**0.50**	0.00
6.2.2 S/ T Claims on Foreign Banks	0.00	0.00	0.00		0.00
CQG 1 (AAA to AA-)	0.00		0.00	**0.20**	0.00
CQG 2 (A+ to A-)	0.00		0.00	**0.20**	0.00
CQG 3 (BBB+ to BBB-)	0.00		0.00	**0.20**	0.00
CQG 4 (BB+ to BB-)	0.00		0.00	**0.50**	0.00
CQG 5 (B+ to B-)	0.00		0.00	**0.50**	0.00
CQG 6 (Below B-)	0.00		0.00	**1.50**	0.00
Unrated	0.00		0.00	**0.20**	0.00
7. Claims on Corporates	**0.00**	**0.00**	**0.00**		**0.00**
CQG 1 (AAA to AA-)	0.00		0.00	**0.20**	0.00
CQG 2 (A+ to A-)	0.00		0.00	**0.50**	0.00
CQG 3 (BBB+ to BBB-)	0.00		0.00	**1.00**	0.00
CQG 4 (BB+ to BB-)	0.00		0.00	**1.00**	0.00
CQG 5 (B+ to B-)	0.00		0.00	**1.50**	0.00
CQG 6 (Below B-)	0.00		0.00	**1.50**	0.00
Unrated	0.00		0.00	**1.00**	0.00

Asset Categories for Credit Risk	Credit Exposure before CRM from Table CR5a Column E	Adjustment for Credit Risk Mitigation (CRM) (Notes 1)	Net Credit Exposure after CRM	Risk Weights	Credit Risk Weighted Asset
	A	B	C =A - B	D	E= C * D
8. Claims on Securitised Assets (as Investor)	**0.00**	**0.00**	**0.00**		**0.00**
8.1 Long Term Claims	**0.00**	**0.00**	**0.00**		**0.00**
CQG 1 (AAA to AA-)	0.00		0.00	**0.20**	0.00
CQG 2 (A+ to A-)	0.00		0.00	**0.50**	0.00
CQG 3 (BBB+ to BBB-)	0.00		0.00	**1.00**	0.00
CQG 4 (BB+ to BB-)	0.00		0.00	**3.50**	0.00
8.2 Short Term Claims	**0.00**	**0.00**	**0.00**		**0.00**
CQG 1 (AAA to AA-)	0.00		0.00	**0.20**	0.00
CQG 2 (A+ to A-)	0.00		0.00	**0.50**	0.00
CQG 3 (BBB+ to BBB-)	0.00		0.00	**1.00**	0.00
9. Credit Derivative Claims (Protection Seller)	**0.00**	**0.00**	**0.00**		**0.00**
9.1 Long Term Claims	**0.00**	**0.00**	**0.00**		**0.00**
CQG 1 (AAA to AA-)	0.00		0.00	**0.20**	0.00
CQG 2 (A+ to A-)	0.00		0.00	**0.50**	0.00
CQG 3 (BBB+ to BBB-)	0.00		0.00	**1.00**	0.00
CQG 4 (BB+ to BB-)	0.00		0.00	**3.50**	0.00
9.2 Short Term Claims	**0.00**	**0.00**	**0.00**		**0.00**
CQG 1 (AAA to AA-)	0.00		0.00	**0.20**	0.00
CQG 2 (A+ to A-)	0.00		0.00	**0.50**	0.00
CQG 3 (BBB+ to BBB-)	0.00		0.00	**1.00**	0.00
9.3 Unrated (Note 2)	**0.00**		**0.00**		**0.00**
10. Regulatory Retail	**0.00**	**0.00**	**0.00**	**0.75**	**0.00**
10.1 Claims on Qualifying SMEs	0.00		0.00	**0.75**	0.00
10.2 Housing Loans Eligible for 75% RW	0.00		0.00	**0.75**	0.00
10.3 Other Retail Loans	0.00		0.00	**0.75**	0.00
11. RHLs Eligible for 35% RW	**0.00**		**0.00**	**0.35**	**0.00**
12. Past Due Exposures	**0.00**	**0.00**	**0.00**		**0.00**
12.1 Where Specific Provision less than 50%	0.00		0.00	**1.00**	0.00
12.2 Where Specific Provision 50% or more	0.00		0.00	**0.50**	0.00
12.3 For RHLs where specific provision is 20% or more	0.00		0.00	**0.50**	0.00
12.4 For RHLs where specific provision is less than 20%	0.00		0.00	**1.00**	0.00
12.5 Fully secured by unrecognized collateral	0.00		0.00	**1.00**	0.00
13. Other Assets	**0.00**	**0.00**	**0.00**		**0.00**
13.1 Venture Capital and private equity investment	0.00		0.00	**1.00**	0.00
13.2 Investment in Commercial Entities Below Materiality Thresholds	0.00		0.00	**1.00**	0.00
13.3 Loans Secured by Commercial Real Estate	0.00		0.00	**1.00**	0.00
13.4 Others	0.00		0.00	**1.00**	0.00
TOTAL CREDIT RISK WEIGHTED ASSETS	**0.00**	**0.00**	**0.00**		**0.00**

Note (Table CR5b):

1. In this column include (as a negative figure) adjusted amount of collateral. This amount should not exceed the outstanding claim.
2. Insert the applicable risk weight into Column D, which is the aggregate of the risk weights of all the assets in the basket upto a maximum of 1250%.

Capital Adequacy Return
Market Risk Capital Charge
FORM CMR

For the quarter ending on / /

" In Thousand KD"

No.	Market Risk Position	Form No.	Amount
1	**Interest rate position risk**	**MRI1**	**0.22**
2	**Equities position risk**	**MRE**	**0.00**
3	**Foreign exchange risk**	**MRF**	**0.00**
4	**Commodities risk**	**MRC 1 or MRC 2a**	**0.00**
5	**Options**	**MRO 1 or MRO 2**	**0.00**
6	**Total Minimum Capital required for Market Risk**	**A**	
7	**Multiplier**	**B**	**8.33**
8	**Total market risk weighted assets**	**C= A x B**	**0.00**

Note (Form CMR):

1- This form should be used to gather information on total risk charges from forms MRI 1, MRE, MRF, MRC 1 or MRC 2a, and MRO 1 OR MRO 2 as applicable.

2- The total capital required for market risk (A) should be converted into a notional risk weighted assets amount (C) using the multiplier.

Capital Adequacy Return
FORM MRI 1
Interest Rate Risk Position

For the quarter ending on / /

INTEREST RATE RISK POSITION
Specific and General Risk (Summary Page)

" In Thousand KD"

	Form No.	Amount
Specific Interest Rate Risk Charge	**MRI 2**	**0.217**
General Interest Rate Risk Charge		
Simplified method *	**MRI 3a**	**0.00**
Maturity Method *	**MRI 4a**	**0.00**

* Use either the simplified or maturity method consistently.

Note (Form MRI 1):

1- Record the specific interest rate charge calculated in Form MRI 2 of the return.

2- If the simplified method is used to calculate general interest rate risk charge, record the capital charge calculated in Table MRI 3a of the return.

3- If the maturity method is used to calculate general interest rate risk charge, record the capital charge calculated in Table MRI 4a of the return.

Capital Adequacy Return
FORM MRI 2
Specific Interest Rate Risk

For the quarter ending on / /

INTEREST RATE POSITION
SPECIFIC RISK

" In Thousand KD"

Obligor	Credit Quality Grades	Remaining Maturity	Risk Factor	Current Market Value	Capital charge
			A	B	C = A x B
Government	1	N/A	0.00%		0
	2 & 3	6 months or less	0.25%		0.0025
		Over 6 months to 24 months	1.00%		0.01
		Over 24 months	1.60%		0.016
	4, 5 & 6	N/A	8.00%		0.08
Qualifying		6 months or less	0.25%		0.0025
		Over 6 months to 24 months	1.00%		0.01
		Over 24 months	1.60%		0.016
Others		N/A	8.00%		0.08
Total Specific Risk Charge					0.217

Note (Form MRI 2):

1- Current market value (B)

Report the total market value (sum of absolute value of long and short positions) of debt instruments in the trading book broken down by obligor, i.e., government, qualifying (broken down further by residual term to maturity), and others.

All currencies are combined on a single schedule.

To arrive at the total for each category, (i.e., total of government, qualifying and others) express all values, whether representing long or short positions, as positive amounts.

2- Capital Charge (C)

Multiply the current market value in each obligor category (Column B) by the associated risk factor (Column A).

The total of the risk-weighted amounts is the Specific Risk Capital Charge.

Capital Adequacy Return
General Interest Rate Risk
Simplified Methods
FORM MRI 3a

For the quarter ending on / /

INTEREST RATE RISK POSITION

General Risk: Simplified Method
Summary total all currencies

Currencies in which position is KD 30,000 or more	Form No.	Foreign currency In Thousand KD	Equivalent In Thousand KD
Kuwaiti Dinar			
US Dollar			
Euro			
UK Pound			
Swiss Franc			
Japanese Yen			
Saudi Riyal			
Sub-total	**0**		
Other currencies			
Total General Interest Rate Risk Charge			**0.00**

Note (Form MRI 3a):

Record the general interest rate risk charge for each of the currencies calculated in Form MRI 3b of the return. Translate into equivalent Kuwaiti Dinars by using spot exchange rates.

Capital Adequacy Return
General Interest Rate Risk
Simplified Methods
FORM MRI 3b

For the quarter ending on / /

INTEREST RATE RISK POSITION

General Risk: Simplified Method

Use separate schedule for each currency where position is KD 30,000 or more and one total schedule for other insignificant currencies where position is less than KD 30,000

" In Thousand KD"

Zone	Time-band		Long Position	Short Position	Gross Position*	Weighting Factor	Capital Requirement
	Coupon of 3% or more	Coupon of under 3% and zero coupon	A	B	C = A+[B]	D	C X D
1	1 month or under	1 month or under			0	0.00%	0
	Over 1-3 months	Over 1-3 months			0	0.20%	0
	Over 3-6 months	Over 3-6 months			0	0.40%	0
	Over 6 - 12 months	Over 6 - 12 months			0	0.70%	0
2	Over 1-2 years	Over 1-1.9 years			0	1.25%	0
	Over 2-3 years	Over 1.9-2.8 years			0	1.75%	0
	Over 3-4 years	Over 2.8-3.6 years			0	2.25%	0
3	Over 4-5 years	Over 3.6-4.3 years			0	2.75%	0
	Over 5-7 years	Over 4.3-5.7 years			0	3.25%	0
	Over 7-10 years	Over 5.7-7.3 years			0	3.75%	0
	Over 10-15 years	Over 7.3-9.3 years			0	4.50%	0
	Over 15-20 years	Over 9.3-10.6 years			0	5.25%	0
	Over 20 years	Over 10.6-12 years			0	6.00%	0
		Over 12-20 years			0	8.00%	0
		Over 20 years			0	12.50%	0
		Total	0	0	0		
	General Interest Rate Risk Capital Requirement						

* Gross Position is based on Long Position (A) and the absolute value of the short Position (B)

Note (Form MRI 3b):

1- Allocate the market value of all debt instruments in the trading book, together with other instruments in the trading book that are subject to interest rate exposure (such as derivatives), into the zones/time bands shown on the return. Show long and short positions separately (column A and B).

2- Sum the absolute value of long position and the absolute value of short position to produce a gross positions figure (column C).

3- Multiply the gross positions amounts by the respective risk weight factor (column D) to arrive at the risk weighted figures which should be summed to give the capital requirement for general market risk.

Capital Adequacy Return
General Interest Rate Risk Position
Maturity Method
FORM MRI 4a

For the quarter ending on / /

INTEREST RATE RISK POSITION

General Risk: Maturity Method
Summary total all currencies

General Interest Rate Risk Charge

Currencies in which position is KD30,000 or more	Form No.	Foreign Currency In Thousand KD	Equivalent In Thousand KD
Kuwaiti Dinar			
US Dollar			
Euro			
UK Pound			
Swiss France			
Japanese Yen			
Saudi Riyal			
Sub-total			
Other currencies			
Total General Interest Rate Risk Charge			**0**

Note (Form MRI 4a):

Record the general interest risk rate charge for each of the currencies calculated in Form MRI 4b of the return. Transfer this into equivalent Kuwaiti Dinars by using the spot exchange rates.

Capital Adequacy Return
Interest Rate Risk Position
General Risk - Maturity Method
FORM MRI 4b

For the quarter ending on / /

INTEREST RATE RISK POSITION
General Risk: Maturity Method

Use separate schedule for each currency where position is KD30,000 or more and one total schedule for other insignificant currencies where position is less than KD30,000

" In Thousand KD"

Zone	Time band		Individual Net Positions		Weighting Factors	Weighted Net Positions		By Band		By Zone		Between Adjacent Zones	Between Zones 1 &3
	Coupon of 3% or more	Coupon of under 3% and zero coupon	Long	Short		Long	Short	Matched	Unmatched	Matched	Unmatched	Matched	Matched
1	1 months or under	1 months & under			0.00%					B			
	Over 1 to 3 months	Over 1 to 3 months			0.20%								
	Over 3 to 6 months	Over 3 to 6 months			0.40%								
	Over 6 to 12 months	Over 6 to 12 months			0.70%								
2	Over 1 to 2 years	Over 1 to 1.9 years			1.25%					C			
	Over 2 to 3 years	Over 1.9 to 2.8 years			1.75%								
	Over 3 to 4 years	Over 2.8 to 3.6 years			2.25%								
3	Over 4 to 5 years	Over 3.6 to 4.3 years			2.75%					D			Unmatched
	Over 5 to 7 years	Over 4.3 to 5.7 years			3.25%								0.92
	Over 7 to 10 years	Over 5.7 to 7.3 years			3.75%								
	Over 10 to 15 years	Over 7.3 to 9.3 years			4.50%								
	Over 15 to 20 years	Over 9.3 to 10.6 years			5.25%								
	Over 20 years	Over 10.6 to 12 years			6.00%								
		Over 12 to 20 years			8.00%								
		Over 20 years			12.50%								
Total			0			0	0	0	0				
									A		H		

Total General Interest Rate Risk Capital Requirement = 10% A + 40% B + 30% (C+D) + 40% (E+F) + 100% G + 100%H	**0.93**

Note (Form MRI 4b):

Allocate the market value of all debt instruments in the trading book, together with other instruments in the trading book that are subject to interest rate exposure (such as derivatives), into the zones/time bands shown on the return. Show long and short positions separately.

1- Multiply the long and the short positions amounts by the respective risk weight factor to arrive at the risk - weighted long and short positions.

2- Matched Positions by Band: Matched position are always expressed as positive amounts. Matched position is the smaller of the risk-weighted long position in a given time-band and the absolute value of the risk-weighted short position in that time bond. If a time-band has only a short position, then matched position for that time-band is Nil.

3- Unmatched Positions by Band: Net the risk-weighted long positions against the risk-weighted short positions to arrive at the unmatched position in each time-band.

4- Matched Weighted Positions by Zone: Each time-band within a zone will either be in an unmatched weighted long position or in an unmatched weighted short position, for each zone record:

- The lesser of the zone's total unmatched weighted long position and the absolute value of the zone's total unmatched weighted short positions.

- In case all time-bands in a zone include long positions or short positions, then record Nil as the matched weighted position for the zone.

5- Unmatched Weighted Positions by Zone: The sum of weighted long positions and weighted short positions within a zone is the unmatched weighted position for the zone.

6- Matched Weighted Positions Between Zones: Determine a zone's matched risk-weighted position by performing an ordered matching of its total unmatched risk weighted position with that of another zone. The order and combination of zone matching are explained in more detail in the directives.

7- Total General Interest Rate Risk Charge: 10% of (A) + 40% of (B) + 30% of (C+D) + 40% of (E+F) + 100% of (G) + 100% of (H).

Capital Adequacy Return
Equity Position Risk
FORM MRE

For the quarter ending on / /

EQUITY POSITION RISK

" In Thousand KD"

Country	Long Position Securities	Short Position Securities	Long Position Derivatives	Short Position Derivatives	Gross Position*	Net Position	Specific Charge	General Charge	Total Capital Charge
	A	B	C	D	E= A+(B)+C+(D)	F= A+B+C+D	G= E x 8%	H= F x 8%	I= G+H
Kuwait					0	0	0	0	0
United States					0	0	0	0	0
United Kingdom					0	0	0	0	0
Germany					0	0	0	0	0
Switzerland					0	0	0	0	0
Japan					0	0	0	0	0
Singapore					0	0	0	0	0

* Gross Position is based on long position (A+C) and the absolute value of the short position (B+D)

Note (Form MRE):

1- Equity positions, in securities as well as those arising either directly or indirectly through derivatives, should be allocated to the country in which each equity is listed.

The calculations outlined below should be applied to each country. Blank rows are left for banks to mention countries not outlined in the return. For purposes of reporting, the terms "country " and " national market " are synonymous.

In case an equity is listed in more than one country, one country should be chosen. Matched positions in each identical equity or stock index in each country may be fully offset, resulting in a single net short or net long position to which the specific and general market risk charges will apply.

2- Long Positions (A) & (C): For each national market (country), the long positions should be reported for both securities and derivatives.

3- Short Positions (B) & (D): For each national market (country), the short positions should be reported for both securities and derivatives.

4- Gross Positions (E): The gross position represents the absolute sum of the value of all long positions and the absolute value of all short position i.e., A+(B)+C+(D).

5- Net position (F): Sum the long positions and the short positions and report the absolute value i.e., A+[B]+C+[D].

6- Specific Capital Charge (G): Multiply the gross positions in Column E by 8%.

7- General Capital Charge (H):Multiply the net position in Column F by 8%.

8- Total Capital Charge (I): Record the sum of capital charges reported in (G) and (H).

Capital Adequacy Return
Foreign Exchange Risk
FORM MRF

For the quarter ending on / /

Foreign Exchange Risk

" In Thousand KD"

Currency	Net Spot Position	Net Forward Position	Guarantee and similar instruments	Net Unearned Income / Expenses	Net Open Position E=A+B+C+D
	A	B	C	D	E
US dollar					0
UK pound					0
Euro					0
Swiss franc					0
Japanese yen					0
Saudi Riyal					0
					0
					0
					0
Others - Long					0
Others - Short					0
Gold					0

Sum of net open long position	F	0
Sum of net open short position (expressed in absolute value)	G	0
Greater of box (F) and box (G)	H	0
Absolute value of open position in gold	I	0
Sum of box (H) and box (I)	J	0
Capital charge (8% of box J)	K	0

Note (Form MRF):

1- All on and off-balance sheet items denominated in a foreign currency are subject to this charge.

2- Bank should report separately their exposure in each foreign currency where the exposure is greater than KD 30,000. The calculation of positions in all other currencies should be performed separately and then aggregated. Structural positions **should be excluded.**

3- Net Spot Position (A): For each currency, report the difference between all assets items and liabilities items. Include the accrued interest and accrued expenses.

4- Net Forward Position (B):For each currency, report all net amounts under forward foreign exchange transactions, including currency futures and the principal on currency swaps not included in the net spot position. Value the position at spot market exchange rates using mid-market rates.

5- Guarantees (C)For each currency, report guarantees and other similar instruments. Guarantees must be certain to be called and likely to be irrecoverable.

6- Net unearned Incomes and Expenses (D): For each currency, report any net unearned incomes or expenses that are not yet accrued but have already been fully hedged.

7- Net Open Position (E): For each currency, report the sum of net open positions in Column (E).

8- Gold:Record the net long or net short position in gold.

11- CAPITAL ADEQUACY RATIO

A) Circular No. (2/BS/184/2005) Regarding the Implementation of the Revised Capital Adequacy Ratio Basel (2).

9- Required Capital Calculation:

- In box (F): record sum of the absolute value of the total net long positions reported in Column (E).
- In box (G): record sum of the absolute value of the total net short positions reported in Column (E).
- In box (H): record the greater of the absolute values of the total net long positions (F) or the total net short positions (G).
- In box (I): record the absolute value of the open positions in gold.
- In box (J): record the sum of box (H) and box (I).
- To arrive at the capital requirement for foreign exchange risk, multiply the sum recorded in box (J) by 8%

Capital Adequacy Return
Commodity Risk
Simplified Method
FORM MRC 1

For the quarter ending on / /

COMMODITY RISK: SIMPLIFIED METHOD

" In Thousand KD"

Commodity	Long Position	Short Position	Gross Position*	Net Position	Capital Charge on Net Position	Capital Charge on Gross Position	Total Capital Charge
	A	B	C= A+[B]	D= A+B	E= D×15%	F= C×3%	G= E+F
Platinum			0	0	0	0	0
Palladium			0	0	0	0	0
Silver			0	0	0	0	0
Copper			0	0	0	0	0
Natural Gas			0	0	0	0	0
Wheat			0	0	0	0	0
Corn			0	0	0	0	0
Canola			0	0	0	0	0
Other (mention each commodity separately)			0	0	0	0	0
Total	0	0	0	0	0	0	0

* Gross Position is based on Long Position (A) and the absolute value of the Short Position (B).

Note (Form MRC 1):

1- All on and off-balance sheet commodity positions are subject to this charge. Commodities include any physical product that can be traded on a secondary market, (e.g., agricultural products, minerals (including oil), and precious metals excluding gold) .

2- Banks should report their exposure in platinum, palladium, silver, Oil, natural gas, wheat, corn, canola and each of the other commodities separately. Rows should be added by banks to mention commodities not outlined in the return.

3- Positions in commodities should be based on the respective standard unit of measurement (e.g., barrels, Kilograms, etc.) and converted into Kuwait dinars at spot rates using mid-market prices. Commodity derivatives and other off-balance sheet positions that are affected by changes in commodity prices (excluding options) are to be converted into notional positions using the current spot prices.

4- Long Positions (A): For each commodity, record the sum of all long positions, in equivalent Kuwaiti Dinars.

5- Short Positions (B): For each commodity, record the sum of all short positions, in equivalent Kuwaiti Dinars.

6- Gross Position (C): For each commodity. record the sum of the absolute values of the long and short positions [column (A) + column (B)].

7- Net Gross Position (D): For each commodity. record the sum of the long position value (i.e., appositive) and short positions (i.e., a negative value) [column (A) + column (B)].

8- Capital Charge on Net Position (E): Multiply the net positions [in column (D)] by 15%

9- Capital Charge on Gross Position (F): Multiply the gross positions [in column (C)] by 3%.

10- Total Capital Charge on Commodity Risk (G): Record the sum of the net position requirements [column (E)] and the gross position requirements [column (F)].

Capital Adequacy Return
Commodity Risk
Maturity Ladder Method
FORM MRC 2a

For the quarter ending on / /

COMMODITY RISK: MATURITY LADDER METHOD CONSOLIDATED (all Commodities)

" In Thousand KD"

Commodity	Capital Charge
Platinum	
Palladium	
Silver	
Copper	
Natural Gas	
Wheat	
Corn	
Canola	
Others (mention each commodity where the position is KD 30,000 or more, separately)	
Total Capital Charge (maturity ladder method)	0

Capital Adequacy Return
Commodity Risk
Maturity Ladder Method
FORM MRC 2b

For the quarter ending on / /

COMMODITY RISK: MATURITY LADDER METHOD (Individual Commodity)

Commodity :___________________________

(Separate schedules for each commodity where position is KD 30,000 or more and one total schedule for others where position is less than KD 30,000)

“ In Thousand KD”

Time Band	Spread Rate	Long Position	Short Position	Matched Position	Unmatched Position carried forward long/(short)	No. of bands Unmatched positions carried forward	Net position	Capital Charge Matched position	Capital Charge Unmatched Position	Capital Charge Net Position	Total Capital Charge
	A	B	C	D	E	F	G	H= D×F×A	I= [E]×F×0.6%	J= G×15%	K= H+I+J
0-1 month								0	0	0	0
Over 1-3 months								0	0	0	0
Over 3 -6 months								0	0	0	0
Over 6 to 12 months	1.50%							0	0	0	0
Over 1 - 2 years								0	0	0	0
Over 2 - 3 years								0	0	0	0
over 3 years								0	0	0	0
Total capital requirement under the maturity ladder method											

Note (Form MRC 2b):

1- All on and off-balance sheet commodity positions are subject to this charge. Commodities include any physical product that can be traded on a secondary market, e.g., agricultural products, minerals (including oil), and precious metals excluding gold.

2- Separate form should be completed for each commodity in which the bank has position of KD 30,000 or more and one form must be completed for all other commodities in which the bank has a position of less than KD 30,000.

3- Positions in commodities should be based on the respective standard unit of measurement (e.g., barrels, Kilograms, etc.) and converted into Kuwaiti dinars at spot rates using mid-market prices. Commodity derivatives and other off-balance sheet positions that are affected by changes in commodity prices (excluding options) are to be converted into notional positions using the current spot price.

4- Long Position (B): For each commodity, record the sum of all long positions, in equivalent Kuwaiti Dinars, in the appropriate time bands.

5- Short Position (C): For each commodity, record the sum of all short positions, in equivalent Kuwaiti Dinars, in the appropriate time bands.

6- Matched Position (D): For each time band, record the matched position, i.e., the smaller of the long position and the absolute value of the short position [columns (B)+(C)]

7- Unmatched positions (E): The unmatched long and short positions are carried forward to offset it against opposite positions in other time bands.

8- No. of bands (F): Record number of times the positions are carried across time bands.

9- Net position (G): Record the residual net positions.

10- Capital charge on matched positions (H): Multiply values in column (D) by column (F) and column (A).

11- Capital Charge on unmatched positions (I): Multiply the absolute values in column (E) by column (F) and by 0.6%.

12- Capital Charge on net position (J)Multiply values of column (G) by 15%.

13- Total Capital Charge (K): Record the sum of the capital charges calculated in columns (H), (I) and (J) and total capital charges for all time bands.

Capital Adequacy Return
Commodity Risk
Maturity Ladder Method
FORM MRO 1

For the quarter ending on / /

OPTIONS
Simplified Method

" In Thousand KD"

Position	Risk exposure	Market Value of the Options Underlying	Sum of Specific and General Market risk percentage	Market value of option	Amount option is in the money	Capital charge: Long underlying/ Long put or Short underlying/ Long call	Capital charge: Long call or Long put	Total Capital Charge
		A	B	C	D	E= D-(A X B)	F	G =E+F
Long underlying/ Long put or Short underlying/ Long call	Interest rate position risk							0
	Equity risk					0		0
	Foreign Exchange risk					0		0
	Commodity risk					0		0
	Total	0	0	0	0	0	0	0
Long call or Long put	Interest rate position risk							0
	Equity risk							0
	Foreign Exchange risk							0
	Commodity risk							0
	Total	0	0	0	0	0	0	0
Total Options		0	0	0	0	0	0	0

Note (Form MRO 1):

1- Market value of the options underlying (A): Report aggregate information on the market value of the options' underlying by position and risk exposure.

2- Sum of specific and general market risks percentages (B): Report the sum of the appropriate specific risk and general market risk factors by referring to sections on interest rate positions risk, equity risk, foreign exchange risk and commodity risk.

3- Market value of option (C): Calculate and report the market value of the option.

4- Amount option is in the money (D): Report the amount by which the option is in the money. In the money means that the exercise level of a " call option " is less than the mark to market value of the underlying instrument, and for "put option" that the mark to market of the underlying is less than the exercise level of the put option.

5- Capital Charge (E) and (F): Calculate capital charge in accordance with the method described in the directives.

6- Total Capital Charge (G): The total capital charge is sum of column (E) and column (F).

Capital Adequacy Return
Commodity Risk
Maturity Ladder Method
FORM MRO 2

For the quarter ending on / /

OPTIONS
Scenario Method

" In Thousand KD"

Risk Exposure	Market Value of the Options Underlying	Specific Risk Charge*	Market Value of the Option Portfolios	General Risk Charge**	Total Capital Charge
	A	B	C	D	E= B + D
Interest rate position risk					0
Equity risk					0
Foreign exchange risk					0
Commodity risk					0
TOTAL	0	0	0	0	0

* A specific risk charge is determined individually for each option. The charge for each is calculated as the current market value of the option's underlying times the option's delta times the appropriate specific risk factor. The source of these factors is summarized in the directives. A sum of these underlying charges is reported here, by type of exposure.

** A general risk charge is determined individually for each portfolio, where a portfolio can combine certain options, as outlined in the directives. For each option portfolio the general risk charge is the absolute value of the largest loss calculated in the scenario matrix (scenario matrices are explained further in the directives). A sum of these portfolio charges is reported here, by type of exposure.

Instructions:

1- Report aggregate information by risk exposure on this return after calculating the specific and general risk charges separately. Specific risk charges must be calculated on each issue in which the bank has a net option position that is subject to interest rate risk or to equity risk. General risk charges must be calculated on portfolios of options (details of the individual capital charges do not have to be reported).

2- Report aggregate information on :

- Market value of the options underlying (A);
- Specific risk charge (B);
- Market value of the options portfolios (C); and
- General risk charge (D).

3- Sum columns (B) and (D) for each risk exposure and report the total capital charge on options in column (E), Calculate a total for this column.

Capital Adequacy Return
Capital Charge for Operational Risk
FORM OpR

For the quarter ending on / /

Computation of Operational Risk Capital Charge

" In Thousand KD"

Business Line	2002				2003				2004				3 Year Average Gross Income	Beta Factor	Operational Risk Capital Charge
	Net interest income	Net – Non interest income (Note 1)	Profit/ Losses on Securities Trading (Note 2)	Gross Income (Notes 3 & 4)	Net Interest income	Net – Non interest Income (Note 1)	Profit/ Losses on Securities Trading (Note 2)	Gross Income (Notes 3 & 4)	Net interest income	Net – Non interest Income (Note 1)	Profit/ Losses on Securities Trading (Note 2)	Gross Income (Notes 3 & 4)			
	A	B	C	D= A+B+C	E	F	G	H= E+F+G	I	J	K	L= I+J+K	M= (D+H+L)/3	N	O
Corporate Finance				0				0				0	0		0
Trading and Sales				0				0				0	0	18%	0
Payment and Settlement				0				0				0	0		0
Commercial Banking				0				0				0	0	15%	0
Agency Services				0				0				0	0		0
Retail Banking				0				0				0	0		0
Asset Management				0				0				0	0	12%	0
Retail Brokerage				0				0				0	0		0
Total		0	0	0	0	0	0	0	0	0	0	0	0		0
Total operational risk weighted exposure															0

* For new banks who do not have three years data, projected three year data from its business plan may be used, subject to approval by the Central Bank.

Instructions:

1- Net non interest income includes (a) gains less losses arising from FX operations and trading in derivatives, (b) dividends from subsidiaries and associated companies and other equity investments, (c) fees and commissions, and (d) other income arising from the the bank's ordinary activities. Exclude extraordinary and irregular items (e.g., profit from sale of fixed assets or income derived from insurance claims).

2- Realised profits/losses from securities classified as "held to maturity" and "available for sale", which typically constitute items of the banking book are excluded.

3- In any given year, negative gross income in any business line may offset positive gross income in other business lines. However, if the overall gross income for all business lines is negative for any given year, then replace all the values for that year with zero.

4- If the overall gross income for all business lines is negative for two or more years, then this should be discussed with the Central Bank of Kuwait.

Capital Adequacy Return
Capital Base Calculation
FORM CA 1

" In Thousand KD"

Capital Components	Tier 1	Tier 2	Tier 3	Total General Provision
	A	B	C	
Permanent Shareholders' equity	**0.00**			
Disclosed Reserves				
Minority Interest in consolidated subsidiaries - Note 1				
Less:				
Treasury Shares				
Goodwill				
Current year's cumulative net losses				
Tier 1 Capital	**0.00**			
Interim retained profits				
Asset Revaluation Reserve (45% only)				
Fair Value Reserve (45% only with the concurrence of external auditors)		**0.00**		
General Provisions (subject to a maximum of 1.25% of total credit risk weighted assets)		0.00		0.00
Hybrid Instruments				
Subordinated Debt - Note 2				
Tier 2 Capital (up to 100% of Tier 1)		**0.00**		
Excess Tier 2 capital (over 100% of Tier 1)				
Tier 3 Capital (up to 250% of Tier 1 allocated to market risk)			**0.00**	
Total Subordinated Debt				
Total Available Capital				
Unconsolidated majority-owned or controlled banking, securities or other financial entities - Note 3				
Capital shortfall of non-consolidated subsidiaries (subject to Central Bank discretion)				
Significant minority investments in banking, securities and other financial entities unless pro-rata consolidated- Note 4				
Minority interests in consolidated subsidiaries - Note 1				
Excess amount over materiality thresholds in case of investment in commercial entities - Note 5				
Investment in insurance entity over 20%				
Reciprocal cross-holdings of bank capital - Note 6				
Excess amount over maximum permitted credit concentration limit (subject to Central Bank discretion)	**0.00**	**0.00**		
Securitisation exposures subject to deduction				
Credit derivatives exposures subject to deduction				
Other deductions	**0.00**	**0.00**		
Total Deductions- Note 7	**0.00**	**0.00**		
Net Available Capital	**0.00**	**0.00**	**0.00**	

Instructions:

1- This refers minority interest arising from consolidation of less than wholly owned banking, securities or other financial entities. It should be reported in one applicable cell only. If such minority interest is not available to the licensed bank, the Central Bank may require deduction instead. Refer to paragraph (9) of the regulation.

2- Percentage of subordinated debt that can be included here is based on the remaining term to maturity and is limited to 50% of Tier I Capital. Refer to paragraph 17 (f) of the regulations.

3- Where holding is temporary and non consolidation is a legal requirement by the host supervisor. Refer to paragraph 7 of the regulations.

4- This refers to significant minority investments of more than 20% but less than 50% where control does not exist. Refer to paragraph 10 of the regulation.

5- If investments exceed the materiality levels specified by Article 67 of Law No 32 of year 1968. Refer to paragraph 12 and 13 of the regulations.

6- That is artificially designed to inflate capital position. Refer to paragraph 11 of the regulation.

7- Deductions shall be 50% from Tier 1 and 50% from Tier 2.

Capital Adequacy Return
Capital Base Calculation
FORM CA 2

For the quarter ending on / /

" In Thousand KD"

No	Capital Base/ Risk Weighted Exposure	Form Reference	Amount
a.	Net Available Capital Base	CA1	0.00
	Tier 1	CA1	0.00
	Tier 2	CA1	0.00
	Tier 3	CA1	0.00
b.	Net credit risk weighted exposure (Note 1)	CR5b, column E	0.00
c.	Minimum capital requirement for credit risk	(b) x12%	0.00
d.	Total operational risk weighted exposure	OPR, Column	0.00
e.	Minimum capital requirement for operational risk	(d) x12%	0.00
f.	Total capital requirement for credit and operational risks	(c) + (e)	0.00
	Tier 1		
	Tier 2		
	Total	Should equal (f) above	0.00
g.	Total market risk weighted assets	CMR	0.00
h.	Minimum capital requirement for market risk	(g) x 12%	0.00
i.	Total capital allocated to market risk	should equal (h) above	0.00
	Residual Tier 1 - Note 2		
	Residual Tier 2 - Note 3		
	Tier 3 (maximum of 250% of residual Tier 1)		
j.	Total risk weighted exposures	(b)+(d)+(g)	0.00
k.	Total Capital Requirements	(f) + (i)	0.00
l.	Eligible Capital Base	250 % of residual Tier 1 above limited to CA 1	0.00
	Tier 1	CA1	0.00
	Tier 2	CA1	0.00
	Tier 3	CA1	0.00
m.	Ineligible Capital	(a) - (l)	0.00
n.	Unused but eligible capital	(l) - (k)	0.00
o.	Capital Adequacy Ratio	(l) - (j)	0.00

Note (Form CA 2):

1- Net of excess general provision.

2- Total available Tier 1 capital minus Tier 1 capital utilised for credit and operational risks.

3- Total available Tier 2 capital minus Tier 2 capital utilised for credit and operational risks.

GOVERNOR

Moharram 20, 1418 H
May 27, 1997

THE CHAIRMAN,

CIRCULAR TO ALL LOCAL BANKS
NO. (2/BS/28/97)

With reference to our letter dated 28/12/1992 to which we attached the Central Bank of Kuwait Board's resolution No. (60/195/1992), relating to the instructions on capital adequacy ratio*, and to our letter dated 10/4/1997, concerning the instructions on the increase of the minimum capital adequacy ratio*.

Please note that the Central Bank of Kuwait Board has decided, at its meeting held on 26/5/1997, to effect an amendment to the instructions issued in relation to the capital adequacy ratio, by incorporating the conditions required to be observed upon evaluating the fixed assets and long-term financial investments and determining the deduction coefficient to the revaluation reserve, as follows:

"The following rules must be observed while determining the amount of the revaluation reserve banks are allowed to include into components of the subordinated capital, so as to determine the capital in its comprehensive concept for the purpose of measuring the capital adequacy ratio:

1) The acceptable revaluation reserve is confined to the balance appearing in the published financial statements and resulting from revaluation of the fixed assets and long-term financial investments, at current value (i.e. the selling value at which the asset can be disposed of at the revaluation date). The values of such assets must be adjusted in order reflect this revaluation.

2) The evaluation must be conducted on annual basis. Evaluation of the real-estate assets shall be assigned to at least two independent professional firms, and the lower valuation shall be adopted.

* This Instructions has been canceled under Circular No. (2/BS/184/2005) dated 12/12/2005 on the application of the Capital Adequacy Ratio – Basel (2).

3) The deduction coefficient shall be computed at 55% of the amount of difference between the historical cost of the long-term financial investments and the market value.

Your bank is required to adhere to the aforesaid instructions while computing the capital adequacy ratio which statement is supplied to the Central Bank of Kuwait on regular basis.

With my best wishes,

SALEM ABDUL AZIZ AL-SABAH

11- CAPITAL ADEQUACY RATIO

B) Instructions No. (2/BS/28/97) on the conditions to be observed when evaluating fixed assets and long-term financial investments, and when determining the valuation provision which is allowed to be included within the components of subordinated capital for the purposes of measuring capital adequacy ratio.

THE MANAGER

Ramadhan 24, 1422 H
December 9, 2001

THE GENERAL MANAGER,

"Circular to All Local Banks"

It has been noticed that when calculating the ratios required under the instructions on maximum credit concentration limits, credit facilities extended by banks for financing securities trading transactions and for other purposes, as well as the ratios required under the instructions on rationalizing local banks investment policy, some banks do not take into account the changes to the components of the capital in its broad concept during various periods of the year, and in the manner detailed in the instructions relevant to the capital adequacy ratio.

We would like to re-affirm the requirement to calculate the ratios required under Central Bank of Kuwait's instructions (that take the capital in its broad concept as a basis for calculating such ratios) on the basis of the capital in its broad concept as on the data submission date.

Best regards,

Manager of Supervision
Ibrahim Ali Al-Qadhi

11- CAPITAL ADEQUACY RATIO

C) Circular Dated 9/12/2001 requiring banks to calculate the ratios required under Central Bank of Kuwait's instructions (Maximum credit concentration limit, financing securities trading, liquidity… etc) on the basis of the capital in its broad concept as on the data submission date.

GOVERNOR

Ramadhan 1st, 1423 H
November 6, 2002

THE CHAIRMAN,

Circular to All Local Banks
No. (2/BS/94/2002)

This has reference to Central Bank of Kuwait circular No. (2/BS/28/97) of 27/5/1997 concerning the Central Bank of Kuwait Board resolution adopted at its meeting of 26/5/1997 regarding the amendments to its instructions on Capital Adequacy Ratio, whereby those instructions incorporated the conditions which must be observed when evaluating fixed assets and long-term financial investments, and according to which a deduction coefficient for long-term financial investments revaluation reserve was determined at 55% of the amount of the difference between the book cost and the market value of the long-term financial investments .

Within the framework of local banks commitment to implement IAS No. (39) starting from the beginning of 2001, which necessitated the change of the accounting policy on recognition and measurement of financial instruments, including the policy on financial investments, whereby the fair value reserve resulting from "Financial Investments Available for Sale" is taken to the shareholders equity, your bank is required to report the said reserve within the components of the subordinated capital for the purpose of computing the capital adequacy ratio, while observing the applicable rules in evaluating financial investments available for sale and in computing the deduction coefficient for this reserve, in accordance with the above mentioned circular No. (2/BS/28/97).

With my best wishes,

SALEM ABDUL AZIZ AL-SABAH

11- CAPITAL ADEQUACY RATIO

D) Instructions No. (2/BS/94/2002) requiring banks to report the fair value reserve resulting from Financial Investments Available for Sale, within the components of the subordinated capital when calculating capital adequacy ratio.

GOVERNOR

Rabi Al-Akhir 28, 1428 H
May 5, 2008

THE GENERAL MANAGER,

Circular No. (2/BS/217/2008)
to all branches of foreign banks operating in the State of Kuwait
concerning the amendment of the implementation of the instructions
of the revised Basel (2) Capital Adequacy Ratio

Reference to The Central Bank of Kuwait's instructions on the implementation of the revised Basel (2) Capital Adequacy Ratio, I would like to advise you that the Central Bank of Kuwait has decided to amend these instructions with regard to the branches of foreign banks operating in the State of Kuwait. According to the amendment, these branches shall be granted exemption, allowing them to compute the capital adequacy ratio by considering the branch's capital base as KD 75 million, i.e. five times the amount allocated for the branch operations, of KD 15 million.

This amendment, which is made for the purpose of computing the capital adequacy, shall allow branches of foreign banks to continue to grow their banking activity, while meeting the requirements of capital adequacy ratio, as determined by The Central Bank of Kuwait's instructions in this respect.

With my best wishes,

SALEM ABDUL AZIZ AL-SABAH

GOVERNOR

Jumada Al-Aula 7, 1423 H
May 12, 2008

THE CHAIRMAN,

Circular No. (2/BS/220/2008)
To all conventional banks operating in the State of Kuwait
concerning the amendment of the instructions of
Basel II Capital Adequacy Ratio

This has reference to The Central Bank of Kuwait's instructions on applying the revised Basel (2) capital adequacy ratio.

I would like to advise you that the board of directors of the Central Bank of Kuwait has resolved, at its session held on 11/5/2008, to make certain amendments on these instructions, as follows:

1. Increasing the risk weight for consumer and installment loans (housing), and debit balances of credit cards from 75%, which is a preferential risk weight under Basel (2) ratio, to 100%, while maintaining the risk weight 75% for loans granted to small and medium enterprises (SME's) , which volume of facilities does not exceed KD 250,000, and for which other standards and terms are satisfied as in The Central Bank of Kuwait's instructions in this respect .
2. Applying risk weight at 150% for credit facilities granted by banks to finance real estate activities (except private housing), and credit facilities granted to finance share purchase, irrespective of the borrower's credit rating in this regard.
3. Interim retained profits shall be excluded from the components of the capital base, reported under Item A of subordinated capital (Tier 2) in the above-mentioned instructions.

Banks should include these amendments in the financial statements to be submitted to the Central Bank of Kuwait on the capital adequacy ratio, with effect from June 2008 statements.

With my best wishes,

SALEM ABDUL AZIZ AL-SABAH

GOVERNOR

Shawwal 9, 1429 H
October 8, 2008

THE CHAIRMAN,

Circular No. (2/BS/225/2008)
to all conventional banks

This has reference to The Central Bank of Kuwait's instructions on the application of the amended Basel (2) Capital Adequacy Ratio.

I would like to advise you that the Board of Directors of the Central Bank of Kuwait has resolved, at its meeting held on 8/10/2008, to consider the real estate properties as one of the acceptable (eligible) collateral for mitigation of credit risk, as stated under Item (B) of Section (10) of the above instructions. The following should be observed:

First: The detailed requirements, as stated in Section (10) of the above instructions, shall be implemented to achieve the application of credit risk mitigation methods.

Second: Banks shall apply a hair cut of 50% according to the comprehensive method of computing the secured exposures, as well as in accordance with the same regulatory hair cut methodology stated under Item (D) of Section (10) of the instructions.

Third: These real estate properties shall be valuated at least once a year by two independent, specialized firms. The lower valuation shall be adopted.

Your bank has to observe the above with effect from above date.

With my best wishes,

SALEM ABDUL AZIZ AL-SABAH

11- CAPITAL ADEQUACY RATIO

G) Circular No. (2/BS/225/2008) on considering real estate properties as one of the acceptable (eligible) collaterals for mitigating credit risk, when calculating the capital adequacy ratio.

GOVERNOR

Rabi Al-Awal 8, 1429 H
March 5, 2009

THE CHAIRMAN,

Circular to all local banks

Within the framework of the Central Bank of Kuwait's assessment of the status of local banks under the global financial crisis, your bank is required to provide us with findings of the Stress Testing conducted by your bank, according to the financial position as at 31/12/2008, so as to assess the bank's ability to face the exposures under stress situations, and to analyze potential events and changes that may have an adverse impact on the bank's performance, specifically the impact on profit, and capital adequacy.

Your bank should provide the required findings of the stress testing no later than 20 March 2009.

With my best wishes,

SALEM ABDUL AZIZ AL-SABAH

GOVERNOR

Jumada Al-Aula 18, 1430 H
May 13, 2009

THE CHAIRMAN,

Circular to all local banks

I would like to refer to the circular to local banks dated 5/3/2009 requesting local banks to provide us with the findings of the stress testing, conducted by banks in accordance with the financial position as at 31/12/2008.

In light of the responses submitted by banks in this respect, it was revealed that there are shortcomings in the studies conducted by banks, and that the testing and scenarios aimed at recognizing the probable changes that may have a negative impact on banks, are incomplete.

I would like to confirm the conclusion reached during the meeting held on 5/4/2009 with Chairmen of Kuwaiti banks as to the need that banks should give adequate care for the stress testing, which should be conducted on a regular basis, so as to measure the sensitivity of risks inherent in the activities of each bank, by analyzing the scenarios of various assumptions under difficult stress situations. Such testing should be complete, covering the various significant aspects of business, which may have adverse effects on the bank's activity, and, consequently, adversely affecting the bank's performance. This will enable banks to manage risk, set up proper strategies, and specify the need to restructure the bank's activity.

Your bank should submit, no later than 31/5/2009, the new findings of the stress testing, as required, in accordance with the financial position as at 31/3/2009.

With my best wishes,

SALEM ABDUL AZIZ AL-SABAH

11- CAPITAL ADEQUACY RATIO

I) Circular stressing that banks should give due attention to stress testing, and to submit the results of those tests as per the financial position on 31/3/2009.

GOVERNOR

Jumada Al-Akhir 22, 1430 H
June 15, 2009

THE CHAIRMAN,

Circular No. (2/BS/245/2009)
To all local conventional banks,
Amending instructions on Basel (2) Capital Adequacy Ratio

This has reference to the Central Bank of Kuwait instructions dated 12/12/2005 regarding the application of Basel (2) Capital Adequacy Ratio, to conventional banks with effect from 31/12/2005.

We would like to advise you that the Central Bank of Kuwait Board of Directors has resolved, at its session held on 14/6/2009, to amend those instructions by deleting Part 12 “Capital Adequacy Assessment” (Paragraphs 309-330), to be replaced by the attached part, which will replace that part of the above-mentioned instructions.

Notably, the new amendment relates to Pillar 2 of the Basel (2) Capital Adequacy Ratio relevant to supervisory review process, stressing the importance of supervisory review process and banks’ internal assessment of capital adequacy ratio (ICAAP).

It should be noted that the amended part includes an appendix containing directives to banks regarding the stress testing. This amendment in the instructions will come into force with effect from 30/6/2009.

With my best wishes,

SALEM ABDUL AZIZ AL-SABAH

Capital Adequacy Ratio Regulations

Basel (2)

Local Conventional Banks

Section 12

Supervisory Review Process*

* This section must replace Section 12 "Capital Adequacy Assessment Process" (Items 309 to Item 330), of the Capital Adequacy Ratio Regulations, Basel (2), issued to the conventional banks, dated 12/12/2005.

Supervisory Review Process

1- This section of the capital adequacy ratio regulations addresses the banks supervisory review process (known as Pillar II of capital adequacy ratio), within the framework of the following basic areas:

- Statement of the minimum requirements to be complied with by the banks in the setting-up and management of the capital adequacy assessment process.

- Encouragement of banks to use and develop the best techniques and methods in the control and management of the banking business risks, as well as achieving a higher degree of Corporate Governance.

- Emphasizing the responsibility of banks to ensure that they have adequate capital to cover all the aspects of risks they are exposed to. This method is called: "Internal Capital Adequacy Assessment Process "ICAAP".

  The Regulatory Capital specified on the basis of the minimum requirement of the capital (Pillar I of the Capital Adequacy Ratio) is different from the Internal Capital specified on the basis of the Internal Capital Adequacy Assessment Process. The difference is that the regulatory capital represents the minimum capital limits to cover three types of risks: credit risks, operational risks and market risks, while the Internal Capital represents the capital necessary to cover all aspects of risks to which the bank is exposed, known as the overall risks as explained later in these regulations.

- The capital adequacy assessment process is a supervisory process by which the senior management of the bank assesses the capital against the various types and levels of risks. The objective of the capital adequacy assessment process is to support the minimum requirements of the capital adequacy and the supervisory review process. Further, it enables the senior management of the bank to make sure that the bank has the appropriate capital to face all major risks that it may exposed to.

- The Central Bank of Kuwait will regularly review the Internal Capital Adequacy Assessment Process (ICAAP), in order to ensure that the banks comply with the assessment of their capital requirements in facing all the

J) Circular No. (2/BS/245/2009) concerning the amendment of instructions on Capital Adequacy Ratio Basel (2).

aspects of the risks, and of the existence of strong and efficient risk management, in addition to the adequacy and effectiveness of banks internal controls system.

- The Central Bank of Kuwait, through its various supervisory methods, will verify the banks' ability to follow up their various business activities in terms of the capital adequacy requirements, and ensure their compliance with the regulatory capital ratio, and will take the appropriate regulatory measures in case of any weakness in the compliance process, including the request to banks to keep higher capital ratios.

First: Internal Capital Adequacy Assessment Process (ICAAP):

2- ICAAP represents a set of policies and procedures set up by the bank within the framework of managing and controlling the banking risks in order to assess the capital adequacy in facing the overall risks to which the bank is exposed. Every bank has to develop and use ICAAP and maintain the capital commensurate with the overall risks to which the bank is exposed.

3- ICAAP has to consider the current stage of the bank's business cycle, in addition to the Forward Looking Process, in order to be able to timely respond to the changes in the face of the risks and strategies of the bank's business, and the changes in the external business environment.

4- ICAAP has to be integrated into the management process. The assessment process has to play a role in making credit decisions or any other decisions in respect of the expansion plans and budgets of the bank.

5- ICAAP has to be able to specify the strategy of the bank and its risks appetite. It has to be able to give reasonable results of the overall capital level.

6- The proper factors of ICAAP have to include the policies and measures to identify, measure, and report the business activity related risks, to link the internal capital with the risks, and to specify the objectives of the capital adequacy in respect of the risks, while taking into account the strategic concentration and the bank's business plans. The bank must have internal control systems that include the review and auditing of the capital assessment to ensure the soundness and completeness of the overall management of the bank.

7- The bank must conduct stress testing to assess its ability to face the exposures under the stressed situations and conditions, as well as analyze the scenarios that can identify the potential events and changes that arise in the market and may

11- CAPITAL ADEQUACY RATIO

J) Circular No. (2/BS/245/2009) concerning the amendment of instructions on Capital Adequacy Ratio Basel (2).

have negative effect on the performance of the bank. The results of these tests, whenever necessary, have to be included in the ICAAP. An appendix that includes "Guidelines to the Banks Regarding the Stress Testing" is enclosed with this section of the regulations.

8- ICAAP has to be applied in a methodological manner and fully documented in business policies, processes and procedures. The degree of complexity of ICAAP is varied from one bank to another, according to the size and complexity of the bank's activities and strategies.

9- Because there is no specific method agreed upon for ICAAP, **the instructions issued by the Central Bank of Kuwait must be obligatory directives for banks to apply**, more than being specific criteria for the methodology of ICAAP or the techniques to be used, considering the difficulty in carrying out a quantitative measurement of particular risks such as reputation and strategic risks. Therefore, the bank must be responsible for explaining the manner by which its ICAAP satisfies the supervisory criteria, and that the objectives of the capital are appropriate in the light of the volume and complexity of the bank's business.

10- Despite the fact that there is no particular assessment and application in respect of the best practices of ICAAP, yet there is a set of factors and characteristics that have to be available in the process of internal assessment process for each bank. **These factors and characteristics are as follows**:

A) Control and follow-up method by the Board of Directors and senior management.
B) Overall assessment of risks.
C) Sound assessment of the capital.
D) Supervision and reporting.
E) Internal control and independent review of the risk assessment systems.

A) Control and follow-up method by the Board of Directors and senior management:

11- The proper assessment of the capital adequacy depends upon the existence of a sound system of risk management. The board of directors and the senior management of the bank Professional Translator & Copywriter have to understand the nature and rating of risks to which the bank is exposed. They have to make sure that the bank sets up the appropriate policies and procedures to manage and hedge risks. Further, **they have to make sure that the bank maintains adequate capital** (in addition to the capital required in accordance with the regulatory requirements) **to cover the risks to which it is exposed, and to allow it to continue growth in its activities**.

12- The Board of Directors and Senior Management of the Bank must be responsible for setting up a sound system for the risk management and ICAAP. The Board of Directors must set up acceptable levels of risk appetite and a strategy for the capital, and make sure that the senior management has taken the following steps:

- Analysis of the current and future requirements of the capital in respect of the strategic objectives.
- Setting up a system to evaluate the types of risks faced by the bank and develop a system to link these risks with the level of the capital required to cover them.
- Establish the methods appropriate to supervise the degree of compliance with the internal polices related to the same.
- Enhance the adequacy and effectiveness of internal controls within the bank.

13- Considering the nature and risks of the bank's business, **the board of directors and the senior management of the bank**, Professional Translator & Copywriter when setting up the strategy of the capital adequacy, have to consider the following factors:

- The current risks faced by the bank.
- The bank's strategy and business plan, with focus on the growth of exposures to the financing risks, investments and activities of a particular nature related to the bank's business and off balance sheet items.
- The current operational environment in terms of the marketing practices, competition and consumer behavior.
- Sources of obtaining the capital.
- Sources and future uses of the funds.

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- Profit distribution policy.
- The local and external laws and regulations related to the sources of obtaining the capital.
- Level of the capital required.

To make sure that the capital is adequate to cover the risks to which the bank is exposed, the Board of Directors has to approve and review the objectives of the levels of the capital required, and to monitor the achievement of these objectives regularly, and annually as a minimum requirement.

14- Considering the nature of the bank's business, **the senior management of the bank must**:

- Set up clear policies and procedures to define, identify and measure all the risks and the manner of reporting them.
- Evaluate the level and trend of risks and their effect on the levels of the capital.
- Evaluate the logic and sensitivity of the basic assumptions used in the capital assessment and measuring system.
- Specify whether the Bank maintains adequate capital to face the risks to which it is exposed, and identify the future capital requirements based upon the risks to which the bank is exposed, and to effect the amendments necessary to the bank's strategic plan.
- Make sure that ICAAP is subject to an independent annual review.

B) Overall Assessment of Risks:

15- The bank must make sure that the ICAAP exhaustively identifies and measures all the significant risks to which the bank is exposed. The assessment process must cover the following:

- Credit risks, market risks, operational risks covered under Pillar I of the Capital Adequacy Ratio (minimum capital requirements).

- Risks related to the activities not covered under Pillar I, which are:
  - ⇨ Credit Concentration Risks.
  - ⇨ Residual Operational Risk.
  - ⇨ Legal Risks.
  - ⇨ Interest Rate Risks.
  - ⇨ Liquidity Risks.
  - ⇨ Strategic Risks.
  - ⇨ Reputation Risks.
  - ⇨ External Factors that affect the performance of the bank, which are beyond the bank's control. They include the supervisory instructions, accounting rules, changes in the business environment and the economic cycles.

Risk Management Policies and Procedures:

16- The Bank must set up and develop risk management systems and measures. Such systems have to be strong, comprehensive and able to identify the nature and importance of all the effective risks to which the bank is exposed, and must identify the manner of integrating these risks in ICAAP.

17- The Bank has to " **Fully Document the Risk Assessment Process** ". It has to be clear to the Central Bank of Kuwait that ICAAP covers all the major risks to which the bank is exposed.

18- With each type of risks covered in ICAAP, the Bank must:

- Conduct a detailed analysis to specify the effectiveness and suitability of the techniques used for risk management.
- Make sure that the risk assessment is always characterized by objectivity and consistency.
- In the assessment of risks, the bank in due course must address the changes in the aspect of the risks it may face due to the entry of new products, or as result of a change in the volume of business, or as a result of the changes in the operational environment, change in the concentrations, type of the portfolio, economic environment, and must input such changes in the risk measuring tools.

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- Make sure that the risk measuring inputs are of good quality, and ensure the integrity of the data used in the risk measuring process and the authenticity of these data.
- The bank must not depend only on the quantitative methods to assess the capital adequacy, as some major risks such as the reputation risk and strategic risk are difficult to be measured quantitatively and require qualitative methods to assess them.

19- The Bank must regularly review its ICAAP to make sure that all risks identified are still existing and considered. Any new risks must be included. Furthermore, the bank has to make the necessary amendments in the internal assessment in the light of the changes in the aspects of the bank's business or its operational environment.

C) Sound Assessment of the Capital:

Setting up the Objectives for the Capital Adequacy:

20- The Bank must have a system to identify the objectives of the capital adequacy in respect of the risks, considering the strategy and plans of the bank's business. The bank must specify the objectives related to the volume of the capital it needs. The objectives have to be beyond the requirements of the minimum requirements of the capital as specified by Pillar I of the Capital Adequacy Ratio.

Such objectives have to include the desired level to cover the risks, the credit evaluation or the creditworthiness of the bank that enables it to easily access the financial resources. The bank has to state clearly the future requirements of the capital and how to cover these requirements in the light of the various situations. The capital management process has to include the extent of the bank's need of additional capital to face the risks of unexpected incidents.

21- The Bank has to specify whether **its long-term objectives of the capital are essentially different from its short-term objectives**. Because the bank needs some time to support is capital base, it has to take precautionary measures for this by keeping an additional capital to face the unexpected incidents. In this framework, **the bank must have emergency plans for additional increase in the capital**.

The bank must keep the appropriate capital, considering the uncertainty of the precision of the risk measurement and fluctuation in their exposures.

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22- The bank must clearly show that its applied method in specifying the capital on the basis of risks to which it is exposed, is based upon sound basics and that the outputs and results of the internal assessment of the capital are reasonable.

The bank must have a clear capital plan approved by its board of directors. This plan must include the objectives and timeframe to achieve them. It must outline the capital planning and responsibility for this process. It has to show how the bank complies with the requirements of the capital and the appropriate limits, the general emergency plan to deal with deviations, and unexpected incidents **(such as: additional increase of the capital, restriction of the bank's activities or using of methods to mitigate the risks)**.

The capital objectives have to be reviewed by the board of directors. This review must be on regular basis (minimum once a year) to make sure that the objectives are still appropriate.

23- The bank has to carry out Stress Testing which takes into consideration the risks of the environment in which the bank operates its business, and the stage related to the economic cycle, in order to evaluate the effect of the potential adverse incidents on the capital. The bank must analyze, and consider the effect of the new legislations, reactions of the competitors that may affect the performance of the bank, in order to verify the adverse changes that can be continuous.

D) Supervision and Reporting:

24- Each bank must set up the system appropriate for monitoring and reporting the risk exposures, as well as assessing how the change of such risks affects the requirements of the capital.

25- The senior management or the board of directors of the bank must periodically receive the reports related to the risks and capital requirements of the bank. Such report should enable the senior management to:

A) Assess the level and trends of the major risks and their effect on the capital levels.

B) Assess the sensitivity and appropriateness of the major assumptions used in the measurement and assessment of the capital adequacy.

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C) Make sure that the bank maintains adequate capital for the various risks, and that it complies with the approved strategy and objectives of the capital adequacy.

D) Assess the future capital requirement on the basis of the details of risks to which the bank is exposed, as mentioned in the reports submitted to the senior management, and to carry out the necessary amendments to the bank's plan accordingly.

E) Internal Control and Independent Review of the Risk Assessment Systems:

26- The bank must have effective internal control systems, including auditing and review process to ensure the soundness of the overall system of ICAAP.

27- The systems applied by the bank in the assessment of risks to which the bank is exposed for specifying the capital levels, must be subject to an independent review by members other than those responsible for the assessment or application of the ICAAP. The review process must be conducted once a year at least by a senior level management in the bank.

28- The senior management of the bank has to make sure that the independent review is made by an independent team so as to ensure non-conflict of interests. Policies and procedures must be established to ensure that the team entrusted with the review of the ICAAP is not affected by any pressures or influence by persons who have interests in the results of the assessment. The senior management is responsible for ensuring that the review team owns all technical tools to perform an independent review of the capital. The results of the report of the review team must be presented to the board and the senior management of the bank.

29- The internal control review must cover **the capital assessment process, major exposures, concentrations risks, the appropriateness of ICAAP, in terms of the accuracy and adequacy of the input data, validity and reasonability of the scenarios and stress testing, and analysis of assumptions and inputs**. The review and audit process must cover and verify the adequacy and effectiveness of the assessment process, monitoring of the actual performance and comparison thereof with the capital objectives agreed upon and how it accords with the strategy and objectives of the specified assessment process.

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30- The bank Board of Directors must be provided with a report on any weakness in the ICAAP, or in case of non-compliance with the approved policies.

Design of the ICAAP:

31- The banks can design the ICAAP in various ways according to their requirements. There are some options that can be used as a reference for the banks in this regard such as:

- **Use of the minimum limit of the capital adequacy** (ratio determined under the instructions issued by the Central Bank of Kuwait) **as a starting point**. The bank has to start adding the considerations which are not included or inadequately included. The bank in the first place must establish ICAAP on the basis of the methodology stated under Pillar I of the Capital Adequacy Ratio in respect of the minimum requirements of the capital. It must be supported by other factors related to the aspects of risks such **as those related to the volume, sectors and products**. For example, in order to obtain an objective of the capital, the bank has to take the minimum limit determined and amend it by additions to be included (calibration) from factors outside the considerations of the minimum limit determined, including the factors related to the future outlook of the bank's activities including the effect on the bank's performance in stress conditions.

  The bank has to be able to explain that it conducted an adequate analysis for all major risks beyond the minimum limit determined, and that all such risks are covered together with the additions made to the capital.

- **Use of various methodologies for other types of risks**, including all the risks to be subject to the minimum limit determined and additions to the capital, and then to calculate the overall capital requirements resulting from that.

- **Use of other complicated methodologies and measurement methods** or a blend of a set of systems including the probability forms.

32- The Bank must not depend only on the quantitative methodologies to assess the capital adequacy. There are major risks which can not be quantitatively measured – as mentioned above – that have to be included by using qualitative assessment and management discretion. **This is because the sound common sense can not be replaced by statistics and model calculations**).

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33- The Central Bank of Kuwait, via its various supervisory methods (on-site and off-site) must verify whether the overall assessment and verification processes are appropriate to the nature, volume and degree of complexity of the bank's activity and nature of its business, and whether the results and outputs of the processes are reasonable.

Requirements For Consolidated Capital:

34- The banks must carry out ICAAP on consolidated basis. The banks carrying out ICAAP at group level must ensure that the consolidated capital is adequate to face the risks of all activities of the parent company and its subsidiaries in addition to the provision of an adequate coverage to cope with the potential risks of such activities.

35- The banks must be able to clarify to the Central Bank of Kuwait the following:

- That ICAAP is based upon a consolidated basis, and that the overall capital estimated to be appropriate for the group has been allocated to each member of the group according to the aspects of risks related to that member.
- All members of the group, including the bank itself, have assessed the risks they face (including the reputation risk resulting from the failure of another member of the group, and the risks the members face due to exposure to other members in the same group or due to their reliance on other members of the group).
- The capital must be freely transferable within the group (even in cases where the group is under financial stress, particularly in respect of the group's cross-border operations). In case that the transfer of capital process among the legal entities of the group is not possible, the bank must have excluded the capital which is not transferable among the members of the group, from the assessment of the capital adequacy.

36- In the assessment of the capital on consolidated basis, the Central Bank of Kuwait must apply the same criteria and requirements as required for the assessment of the capital adequacy on the basis of the bank as an independent unit.

Application to Subsidiaries:

37- All the bank's subsidiaries must have an adequate capital on the basis of their needs (stand-alone-basis). They must have their own ICAAP appropriate to the volume and complexity of their activities.

38- The subsidiaries of the foreign bank group (in case that the existence of foreign banks is allowed in the State of Kuwait through their subsidiaries) can adopt the methodology of ICAAP used by the parent institution at the group level, if its capital is run centrally at the group level, depending upon ICAAP applied by the group in the assessment of the capital adequacy. In this case, ICAAP applied by the group has to be designed in accordance with the supervisory criteria similar to those applied by the Central Bank of Kuwait. The results of ICAAP of the subsidiary have to take into account the strategies of their local activity and the risks related to this activity.

Second: Review by the Central Bank of Kuwait (CBK):

39- The Central Bank of Kuwait (CBK) must review ICAAP and must consider the following basic factors:

* The soundness of ICAAP in the light of the nature and volume of the banking business.
* Extent of the Board and the senior management supervision of the capital objectives and its levels.
* Extent of using ICAAP within the bank in the decision-making purposes.
* Extent of considering the unexpected incidents in the specification of the capital levels.
* Rationality and logic of the results of the assessment process in terms of:
  - Extent of adequacy of capital required as per ICAAP to cover the risks faced by the bank.
  - Extent of comprehensiveness and suitability of the levels and components of the capital selected for the current business environment and the nature and volume of the bank's operations.

* The manner of selecting the internal objectives of the capital and how these objectives are consistent with the aspects of the overall risks of the bank, the current business environment and the bank's planned processes.

* The bank has to clarify the similarities and differences between the levels of the capital calculated under ICAAP and the level of the capital calculated under the minimum requirements of the capital (regulatory capital).

* In the assessment of the capital adequacy, the Central Bank of Kuwait must not only consider the capital ratios as indicators of the capital strength, but should also consider – inter alia – the ability of the capital structure to accommodate the losses and the manner in which this structure is negatively affected by the changes in the performance. **The basic capital must be an essential component of the capital structure because it allows for the accommodation of losses on a continuous basis and it is always available for this purpose.**

* If the capital to be taken into consideration is not the same amount resulting from ICAAP (particularly if the capital resulting from the assessment process is less than the capital expected by the Central Bank of Kuwait), then the Central Bank must discuss these differences with the bank to know the factors that have led to such results and to assess these factors.

* To facilitate the review process, the Central Bank of Kuwait will request information from the banks about the results of the assessment process of the bank, with clarifications on the process used. The Central Bank of Kuwait must request information about the capital it deems appropriate and the components of the capital. As for the Group ICAAP, there must be a detailed analysis of the Group Capital as per each unit per se.

Third: General Guidelines to determine risks for ICAAP:

1) Credit Risks:

40- The banks must assess the overall credit risks and make sure that the Credit Risk Management is part of an integrated methodology to manage all risks.

41- The banks when assessing the credit risks for the purpose of specifying the capital required in accordance with the capital requirements, must have:

- Risk rating system.

- Overall credit portfolio analysis.

- Specification of major exposures and concentration risks.

The banks must have credit risk internal rating system that can assess the credit exposure risks on the level of each client or on the level of overall portfolio. This system should be able to specify and measure all the credit exposures. The assessment must be consistent with the total credit risks and the capital required in accordance with the capital requirements.

42- The credit review measures must be comprehensive and able at minimum to cover the following:

- Detailed classification of all credit exposures.
- Ascertain the sufficiency of provisions against the losses expected in the credit portfolio.
- Evaluation of weakness points in the credit portfolio in general, and in the major exposures in particular, and the credit concentrations.

2) Credit Concentration Risks:

43- The credit concentration risks are the major exposure risks towards a client or a group of risk exposures that lead to major losses related to the capital or the total assets with the bank, and may threaten its financial stability. The banks must consider that the concentration risks may originate from assets, liabilities or off-balance sheet items.

44- There are various types of credit concentration risks, including the following:

- Major credit exposure of a client or a group of related clients.
- Credit exposures for a group of clients in a particular economic, industrial or geographical sector.
- Indirect credit exposures resulting from the credit risk management with banks, such as exposure to one type.

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45- The following considerations must be an integral part of banks credit concentration risks management:

- The senior management of banks has to develop policies and procedures to identify, measure and control the credit risks. This must be done bank-wise and bank group-wise, as well as on the level of all risks faced by the bank. There must be an office or a department responsible for measuring, and following up of credit concentrations, and must be independent from the decision making unit or officer that makes the decision of the credit exposure.

- The Board of Directors must monitor and develop particular rules to manage the credit risks exposure. The bank's board of directors must be periodically informed of the exposure risks.

- The credit concentration risks have to be clearly defined to ensure the measurement of the maximum limit of such risks. The bank must have an information management and comprehensive periodical reports to specify the credit concentrations and monitor their risks on the overall level of the portfolio.

- The Bank’s must set up internal maximum limits for the credit concentration apart from the regulatory controls issued by the Central Bank of Kuwait in respect of the maximum limits of the credit concentration.

- The bank's management must consider the factors that affect the assessment of the risks of credit concentration, including – for example – the political, legal and regulatory conditions, market conditions, economic sectors and local conditions through which the banks work and which directly or indirectly affect the banks' clients in the finance field.

- The banks have to conduct a periodical analysis of the effect of some potential scenarios and the stress testing on the effective credit concentrations. The results have to be analyzed to know the potential effects on banks credit portfolio when an essential factor is changed (such as the economic cycle, fluctuation in the rate of return or liquidity available in the market). The banks must ensure their ability to continue activity in case that they are exposed to difficult conditions.
- There must be adequate internal control measures to manage the credit concentration risks, in addition to the capital requirements, in accordance with the instructions of the Central Bank of Kuwait.

3) Residual Risks that result from the mitigation of the credit risks:

46- The credit risk mitigants such as collaterals and guarantees may reduce the minimum requirements of the regulatory capital under Pillar I of the capital adequacy ratio. However, the application of these mitigants may lead to other risks **such as the legal risks, documentation risk, operational risk, liquidity risk and market risk, collectively known as residual risks**. These risks may result in the weakness of the effect of credit mitigants. Therefore, although the bank may be able to meet the minimum requirements of the capital adequacy under Pillar I of the capital adequacy ratio, the residual risks may lead to more than expected exposure in the credit risks towards other parties.

47- Each bank must apply **an effective system to manage the residual risks** resulting from using credit risks mitigants. The system must include the following factors:

- Define the responsibility of managing and monitoring the credit risks mitigants. This responsibility must be assigned to a particular officer or department within the bank, based upon policies and measures approved by the senior management at the Bank. The senior management must have sufficient knowledge of the bank's products and appropriate management of all major risks (such as credit, market, client, liquidity and legal risks).

- This system must include proper policies and procedures that cover the strategic risks and essential considerations to grant the credit facilities, systems and management of concentration risks resulting from credit risks mitigants and their interference with the overall aspects of the credit risks.

- The policies and measures must be accompanied by effective internal control to manage the activities of the credit risks mitigants, including a sufficient legal review so as to convince the bank that the documentation used in the credit risks mitigants is binding to all parties and has legal force. Further, there must be regular review and reports for the activities of managing credit risks, to be presented to the bank's board of directors.
- The banks, when calculating the requirements of the capital, must show the appropriateness of recognition of all credit risks hedging instruments according to Pillar I. The banks must show how their policies and measures of managing credit risks are appropriate for the capital to be maintained.

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- The banks must have an independent review of the risk management of the credit risks mitigants in order to verify compliance with policies and procedures approved in this regard, and to detect any weakness in the internal control systems.

48- The banks must maintain additional capital to cover the residual risks resulting from using the credit risks mitigants.

4) Market Risks:

General Principles of Managing Market Risks:

49- The banks must use the techniques that enable them to assess and manage all the basic market risks to which they may be exposed, **such as: concentration risks, activities risks, various products and bank group risks**.

50- Through the internal assessment process, the bank must show the extent of the capital adequacy in facing the requirements of Pillar I requirements, in addition to the capital required to face the effect of the market fluctuations. In particular, the internal assessment of the capital must include the following factors:

- Tightness of liquidity in the market and price gaps.
- Concentrations in positions as compared to the volume of trading in the market.
- Other risks which are not covered on the basis of Value-at-Risk (VAR).

51- The banks must establish measures and design systems to manage risks in addition to the use of VAR method and Stress Testing, in a manner that measures the basic risks in the financial instruments and strategies followed by the banks.

52- The banks must ascertain the adequacy of the systems used to measure the risks regardless of the type and degree of complexity used in these systems. The banks must ascertain the validity of the information inputted and the various assumptions used in the risk measuring models.

53- The banks must document the method on the basis of which the risks are measured to reach at the capital required to cover the market risk.

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Policies and Measures for the Trading Portfolio:

54- The banks must establish clear policies and procedures to identify exposures in the trading portfolio and other exposures, so as to ensure consistency and integration of the calculation of the capital required in accordance with the requirements of the capital adequacy. The banks must ensure that the policies and measures set up by them for the trading portfolio are within a framework which is clear and consistent with the risk management at banks.

Assessment:

55- The sound assessment policies and measures are the basis in the process of assessment of the capital necessary to cover the market risk. In this context, the Central Bank of Kuwait urges the banks to develop new sound policies and strong measures with the application of the world best practices in this field. The banks must provide additional capital for the financial portfolios exposed to the following:

- Financial portfolios which investments are not properly allocated to the financial markets or across economic sectors.
- The financial portfolios which include financial instruments which are not of high liquidity.
- The financial portfolios which are concentrated in financial markets that do not witness relatively high trading activities.
- The financial portfolios which include a large number of positions assessed through using the assessment models.

The banks must make sure that they maintain adequate capital to cover the risks of the financial portfolios with no trading activities or do not have prices that can be specified. The weak trading and inability to specify trustworthy prices will weaken the effectiveness of the models used by the banks to measure the risks of the financial instruments.

5) Interest Rate Risk:

56- The banks must have a system to manage the interest rate risks. The banks which have regional exposures must assess the effect of the change in the interest rate on their operations in these countries.

Sources of Interest Rate Risks:

57- The sources of the interest rate risk include the following:

- Re-pricing risks: They are risks resulting from mismatch of maturities among the assets and liabilities and off-balance sheet items.
- Profit Curve Risks: They are risks resulting from the negative effect of the unexpected change in the profit curve.
- Basic Risks: They are risks of unexpected negative change in the cash flows and the income margin between assets, liabilities, and off balance sheet items.
- Non-compliance Risks: They are risks of negative effect on the revenues resulting from non-compliance with the maturity dates of assets and liabilities.

Effective Management of Interest Rate Risks:

58- The following principles support the prudent management of the interest rate risks:

- The board of directors has to approve plans and policies to manage the interest rate risks, and to ensure that the bank's management takes the necessary steps to have tight control over these risks within the approved limits in accordance with the bank's policies and strategies.
- The board of directors must regularly be advised of the interest risk exposures in order to have tight control over this type of risks within the limits approved by the bank's board of directors.
- The senior management of the bank must make sure that the measures and policies are appropriate for the effective management of the interest risks.
- The regulatory policies and procedures for the interest rate risks must be clear and accord with the nature of the banking activities and their complexity. They have to cover the bank group activities.
- The banks have to be well versed in the interest rate risks related to their new products and activities. There must be clear policies and measures for these products and activities. The methods of hedging and managing the risks of these products must have prior approval of the bank's board of directors.

- Define and identify the main sources of interest rate risks related to the assets, liabilities and positions in the off-balance sheet items, on regular basis.

- To measure the sensitivity of the interest rate fluctuation on-balance sheet and off-balance sheet in accurate and meaningful manner by using appropriate assumptions and scenarios. The banks must use approved techniques to measure the risks.

- The interest rate risk measuring system at banks must be integral with their risk management. The system outputs must explain the degree of risk in the interest rate. The bank board of directors must be advised of these risks.

- The risks of the interest rate positions must be regularly subject to the stress testing and scenario analysis.

- The internal control system of the banks must be subject to independent regular tests to specify the effectiveness of the control system. The system has to be developed and improved whenever necessary.

- Banks have to maintain a capital appropriate for the degree of the interest rate risk they face.

6) Operational Risks:

59- The banks must consider the risks which are not directly specified in Pillar I during the process of capital adequacy assessment.

Operational Risks Management:

60- The board of directors and the senior management of the bank must be advised of all major aspects of the operational risks. The have to be responsible of the effective implementation of the system of managing these risks, including the approval of regular review of that system.

61- The banks must develop an overall framework to manage the operational risks so as to be an integral part of the risk management processes in general. The framework must cover all types of operational risks resulting from the various activities.

Each bank must establish a framework for the operational risk management including the policies and procedures that explain the bank's method to identify, assess, monitor, control and hedge the operational risks inherent in all the basic products, activities, operations and systems used by the bank. The board of directors or the senior management must be advised of any deviation resulting from non-compliance with the policies laid down.

62- The senior management of the bank must make sure that the operational risk management system is consistently applied in the bank. The bank must continuously monitor the exposures to operational risks and report the major operational risks to the board of directors. The systems and policies of the operational risk management must be subject to an independent regulatory review.

63- The banks must take into consideration the operational risks resulting from non-compliance with the laws and regulations and the consequent legal risks.

Operational Risks Measuring:

64- The reliance of Pillar I of the capital adequacy ratio on the total income as a tool to measure the scope of the bank’s exposure to the operational risks, does not accurately reflect the level of that exposure to these risks, which may arise from a failure in the systems of the various bank businesses, electronic banking security intrusion, risks of internal and external embezzlements, risks that accompany the provision of particular services and products.

65- The bank must follow a particular methodology to measure the operational risks that accord with the level of complexity and diversification of its activities. The bank must review the capital calculated in accordance with Pillar I and its appropriateness to cover the operational risks, or support the capital base with additional capital if necessary, in accordance with the internal assessment of the capital adequacy.

7) Legal Risks:

66- The legal risks are represented in the risks of loss resulting from the bank's inability to implement contracts or any other rights vested in it. The banks are exposed to the legal risks in the light of the losses resulting from shortage in the documents, shortage in obtaining necessary authorizations from customers who carry out trading transactions through the bank, contracts which are not signed,

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violation of legal rules, or the effect of legal changes after carrying out transactions, and the like.

67- Although the definition of the operational risks include the legal risks, yet the calculation of the capital requirements to face the operational risks under Pillar I, does not include the bank's whole exposure to the legal risks. Such risks have to be considered in the process of internal assessment of the capital.

8) Liquidity Risk:

68- The banks must have adequate and effective systems to manage the liquidity risks in a manner appropriate for the volume and complexity of the bank's activities. The liquidity risk management systems must include the following factors as a minimum requirement:

- Existence of liquidity strategy to identify clear policies for managing the liquidity available with the bank.

- Existence of policies and strategies related to the liquidity risks and approved by the board of directors. The senior management of the bank must take the steps necessary to monitor and control the liquidity risks, including the inception of appropriate policies and procedures, review of the liquidity positions limits during particular periods, and advising the board of directors on regular basis and immediately of any major changes that occur in the current or expected liquidity position of the bank.

- Existence of sufficient data to measure, monitor and control the liquidity risks and reporting them during the specified periods to the board of directors, the senior management and the concerned staff at the bank.

- The bank must conduct the appropriate analysis of the net financial resources required under the various scenarios. **The assumptions used in the management of liquidity must be continuously reviewed to ascertain their validity.**

- The bank, within the framework of liquidity risk management, must ensure the diversification of the financial resources. The bank must in particular conduct tests of the bank's dependability on a particular financial resource or a particular geographic market. A periodical review must be conducted to maintain good and continuous relationships with the funding parties to ensure the diversification of the financial resources.

- The bank must have in place emergency plans that address particular strategies to deal with the liquidity crises that may occur. These plans have to include specific measures to handle the shortage in the cash flows in emergency cases.

- The banks must measure, monitor and control the liquidity positions in the major currencies and make sure that the mismatch between the foreign currency and the local currency maturities is within acceptable limits. The banks must have strategies for each foreign currency per se. A periodical review of the mismatching cash flows limits of the foreign currencies against the local currency limits during particular periods, and of the major foreign currency against the local currency.

- The bank must be fully aware of the scope of the liquidity risks to which it may be exposed in order to specify the capital required to cover the liquidity risks. The bank must support its capital base with additional capital if required. The bank's measures to support its liquid assets in terms of the structure of such assets and their adequacy must be considered.

9) Other Risks:

69- The risks detailed in this part may not cover all types of risks the bank faces. The Central Bank of Kuwait requests the Bank to have in place an accurate process to specify the capital required to cover all the risks to which it is exposed.

Fourth: Allocation Matrix Scoring System used by the Central Bank of Kuwait When Specifying the Internal Capital Adequacy:

70- This aspect of the regulatory process includes an additional explanation of the method adopted by the Central Bank of Kuwait when reviewing the assessment of the internal capital adequacy of the banks. This is based on a set of **common assessment** factors and a set of **specific assessment** factors. Scores must be assigned to these factors and will be integrated into a matrix in the manner shown in the attached model.

J) Circular No. (2/BS/245/2009) concerning the amendment of instructions on Capital Adequacy Ratio Basel (2).

71- The Matrix model attached is an explanatory example only. The Central Bank will specify the relative importance of the assessment factors and the appropriate scores in the light of the results and measures of on-site and off-site supervision.

72- The banks must set up and develop their own assessment models, supported by the appropriate working papers. They have to consider as minimum the set of common assessment factors and specific assessment factors as stated in the enclosed forms (Form#1, Form#2 and Form#3).

73- **The Common Assessment Factors include** the following elements:

- Level of risk associated with the bank's activity in respect of the risks not addressed, or not sufficiently addressed under the requirements of the minimum capital adequacy, which concentrates, for example, in the credit concentration risks, residual operational risks (such as legal risks), interest rates risks in the banking records, liquidity risks, strategic risks, reputation risks and other risks.

- Adequacy and effectiveness of the bank's systems and the internal controls for the types of risks associated with the various activities including: the risk management systems, internal control systems, infrastructure for practicing the activity, other support systems such as the information technology, anti-money laundry systems.

- The effectiveness of the internal capital assessment within the bank such as: Adequacy of the stress testing, type and strength of the capital, ability to face the risks in case of stress and economic cycles, and ability to access the financial markets to support the capital.

- Quality of the governance criteria applied in the bank and how far the bank continuously complies with these criteria.

74- **The specific evaluation factors include** any other specific factors related to the bank's activities and operations that result in the increase or mitigation of risks related to the bank. Examples of the risk mitigation factors are as follows:

Advantages obtained by the bank as a result of diversification of activities, insurance coverage of some important operational risks, and any other factors conducive to the reduction of the requirements of the capital adequacy.

75- The Central Bank of Kuwait must consider, when reviewing the common assessment factors, how far the bank continuously complies with the capital adequacy regulations, in addition to the quality of the systems applied within the bank, the adequacy and effectiveness of the internal monitoring controls, including **the level of supervision by the Board of Directors and the senior management**. The Central Bank of Kuwait must use appropriate methodologies and techniques for the assessment of the effect of these factors, including the weights and scoring system for the common assessment factors for all banks. The specific factors will be used separately on the basis of each case per se by using the appropriate methodology.

Form No (1)

Supervisory Review Process

Common (Key) Assessment Factors of Capital Adequacy*

Activity Risks	Effectiveness & Adequacy of Internal Monitoring Control	Effectiveness of the Internal Capital Assessment Process (ICAAP)	Governance Criteria
• **Credit Concentration Risks** • Residual Operational Risks • Legal Risk • Interest Rate Risks in the banking records • Liquidity Risks • Strategic Risks • Reputation Risk	• Risk Management System • Internal Control System • Infrastructure to practice activity • Other supporting systems (IT systems + AML system)	• Adequacy and effectiveness of ICAAP • Adequacy of stress testing • Quality and strength of the capital • Ability to face the risk including the stress conditions, economic cycles, access to the financial markets, shareholders support	• Quality of governance criteria • Continuous compliance with the governance criteria

11- CAPITAL ADEQUACY RATIO

J) Circular No. (2/BS/245/2009) concerning the amendment of instructions on Capital Adequacy Ratio Basel (2).

* The objective of this form is to provide banks with guidelines regarding the common assessment factors to be considered by the Central Bank of Kuwait when reviewing the ICAAP, in respect of the risks which are not covered under the requirements of the minimum capital adequacy, and which the banks have to consider in the supervisory review process.

Form No (2)

Regulatory Review Process
Capital Adequacy Specific Factors*

Risk Mitigating Factors	Risk Increasing Factors
• Advantages of activity Diversification • Insurance coverage - for operational risks - Assets • Other factors conducive to a reduction in the requirements of the capital adequacy	• Securitization • Other factors not adequately considered under the minimum requirement of the capital. • Any other factors

* The objective of this form is to provide banks with guidelines regarding the specific assessment factors to be considered by the Central Bank of Kuwait when reviewing the ICAAP, in the supervisory review process.

Form No (3)

Explanatory Example
Capital Adequacy Allocation Matrix Scoring System

Risk Types	Risk Level*	Allocation of scores under Pillar II (Supervisory Review Process)								Minimum Capital Adequacy Requirement			Relative Allocation Of Minimum Capital Adequacy
		Internal Controls and Systems					ICAAP	Governance Criteria	Total**	Pillar II	Pillar I Requirement	Total	
		Risk Management System	Infernal Control	Infrastructure	Other supporting systems	Total							
Credit	4	5.6	2.8	1.2	0.4	10	10	3	27	1.00%	10.00%	11.00%	68.75%
Market	-	2.8	1.4	0.5	0.3	5	4	1	10	0.30%	0.5%	0.80%	5.00%
Interest Rate	6	2.8	1.4	0.5	0.3	5	3	1	15	0.50%		0.50%	3.12%
Liquidity	6	2.8	1.4	0.5	0.3	5	3	1	15	0.50%		0.50%	3.12%
Operational	3.5	5.4	2.7	0.9	0.3	9.3	2.5	0.7	16	0.70%	1.5%	2.20%	13.75%
Legal	0.5	0.2	0.1	0.2	0.2	0.7	0.5	0.3	2	0.40%		0.40%	2.5%
Reputation	3	0.2	0.1	0.1	0.1	0.5	2.5	1.5	7.5	0.30%		0.30%	1.88%
Strategic	3	0.2	0.1	0.1	0.1	0.5	2.5	1.5	7.5	0.30%		0.30%	1.88%
Total	26	20	10	4	2	36	28	10	100	4.00%	12.00%	16.00%	100%

* Risks not covered under Pillar I.

** The Central Bank of Kuwait must allocate the total scores to the total items in each row. The scores and percentages in this form are for example only. The appropriate changes must be made in the light of the risks of each bank.

* The objective of this form is to give banks guidelines regarding the capital adequacy common assessment factors and how to integrate these factors for the assessment of the appropriate capital under the supervisory review process.

* The minimum capital adequacy ratios above (12% for Pillar I and 4% for Pillar II) are for example only.

Appendix to the Supervisory Review Process
Guidelines to the Banks Regarding the Stress Testing

First: Introduction:

1- Stress Testing means the employment of various techniques by the bank to assess its ability to face exposures under stress situations through measuring the effect of these exposures on the set of financial indicators of the bank, **and in particular the effect on capital adequacy and profitability**.

2- The stress testing is an important factor in the risk management systems at the banks, particularly after the crises witnessed by the markets confirmed that it is not sufficient to manage the risks on the basis of the normal business conditions, because in case of sudden changes in the markets (strong market shocks) the banks may be exposed to major risks as a result of the following:

* The Market responds in a way different from its response in the normal conditions.

* Risks of new concentrations through the unexpected correlation in the various markets.

* Sudden stress in the economic situations in the countries and regions affected by these crises.

* Difficulties faced by the banks in covering their positions during the crises.

3- The stress testing is a part of supervisory control of the general risks. Therefore, the banks must include these tests when using the models of measuring market risks, credit risks, country risks, large exposures and concentration risks, liquidity risks and risks in general.

Second: Basis Purposes of Stress Testing:

1) Stress testing provides banks with the information necessary to assess the risks of potential exposures in stress situations. Therefore, they enable banks to be well hedged for such situations through development and selecting the strategies appropriate to mitigate such risks, particularly restructuring of their positions and development of appropriate emergency plans to face such situations.

2) Stress testing enables the banks board of directors and the senior management to specify whether the exposure risks are in line with the risks trend at these banks.

3) Support the statistical measurements of risks used by the banks in the various business models based upon assumptions and historical data.

4) Evaluation of the banks ability to face the difficult situations in terms of measuring the effects on profitability and adequacy of the capital.

Third: Requirements of design and application of stress testing:

1) The design and application of stress testing carried out appropriately by the banks lead to the enhancement of the risk management system of the banks, and help them in getting prepared to face the difficult market conditions.

2) The banks must include the stress testing in their risk management processes, and must periodically carry out the stress testing.

3) The banks must develop comprehensive programs for stress testing to reflect the characteristics of the specified risks in the portfolio of each bank. The banks must document the policies and methodologies applied in this regard.

4) The banks which have not yet established and developed the stress testing programs, have to establish and develop these programs **within six months from the issue date of these regulations**, within the framework of these regulations. The Central Bank of Kuwait will supervise the progress made by the banks in enhancing their abilities to carry out stress testing. The Central Bank of Kuwait, through the various supervisory methods will evaluate the appropriateness and effectiveness of these measures carried out by the banks in respect of the stress testing. The following will be considered:

   * Degree and complexity of risks for the bank.

   * Adequacy of the stress testing (types of scenarios and parameters) to be tested.

   * Adequacy of the risk management in the bank and stress testing measures.

   * Appropriateness of the risk exposure level (Mild / Medium / Severe) in respect of the announced objectives and the risks permitted.

* Adequacy of the emergency plans in the bank, the measure to be taken in case of occurrence of any stress testing scenarios.

* Level of supervision practiced by the board of directors and the senior management at the bank on the stress testing programs and the results of these programs.

* Adequacy of the internal review and audit for the stress testing programs within the bank.

Fourth: Basic Factors of Stress Testing:

1) The process of establishing stress testing programs is characterized by the following:

   - Review of the nature of the basic activities of the bank, the external environment in which the bank carries out its business, for listing the risk factors to be tested under various stress testing scenarios.
   - Design stress tests appropriate for the bank's activities, including the identification of their potential incidents and scenarios.
   - Documentation of the assumptions upon which the stress testing is made and the manner of inferring these assumptions.
   - Specifying the stress testing measures, such as the identification of responsibilities and allocation thereof, frequency of stress testing.
   - Carrying out the stress testing regularly and analyzing the results of these tests to identify the potential exposures and risks.
   - Reporting the results of these tests to the senior management and the respective managers.
   - Specifying the appropriate treatment measures to be carried out by the banks in facing the potential risks identified through testing process.
   - Provide the board of directors, whenever necessary, with a report that summarizes the stress testing results and the treatment measures taken.
   - To regularly carry out the re-assessment of the appropriateness of these tests, including the verification of the assumptions used in the light of the change in portfolio characteristics and the external environment.

2) The banks must document the stress testing process through setting up a special policy which has to be approved by the Board of Directors or a Committee authorized to that effect by the Board.

3) The board of directors and the senior management must practice a supervisory effective role on the stress testing programs, and must effectively participate in the process of designing these tests and supervise their results, as well as ascertain the measures to be taken for the mitigation of the potential risks.

4) The comprehensive testing process must be managed and coordinated by an independent authority in the bank (such as Risk Management).

5) The stress testing has to include quantitative and qualitative testing parameters. The quantitative parameters must have plausible stress scenarios.

6) The qualitative parameters of testing must emphasize two basic objectives of the stress testing, namely:

   - Assessment of the bank's revenues strength (Revenue Strength of the bank) and the capital to accommodate the major losses the bank may incur.

   - Specify the steps to be taken by the Bank for risk management, and identify the appropriate capital in a conservative manner.

   The above-mentioned assessment procedures are complementary to setting up and assessment of the management strategy in the bank, which may include, for example, the review of the bank's need to effect a change in the limits of the risks in response to the testing results. The bank must have in place an emergency plan to face a particular scenario when it occurs.

7) The stress tests of the banks must cover the basic On-And Off-balance sheet positions in the trading books and the banking records, as well as all the other risk factors.

8) The banks must carry out stress tests on appropriate periods of the risks to which the bank is exposed. In general, the portfolio tests are the most sensitive to the market movement, such as the trading securities portfolio, other marketable bills, and foreign exchange exposures.

These tests must be conducted more frequently (daily, weekly), while the other portfolios which are by nature less fluctuating (such as funding), can be a subject of stress testing over longer periods (monthly or quarterly).

9) The banks must carry out the necessary Ad-hoc stress test, for particular fields, and when it is desirable under particular conditions, including for example a rapid deterioration in the political and economic conditions in a particular country. In this case, the bank must quickly evaluate the potential effect on its exposures in that country.

10) The senior management and the respective managers in the bank must be advised of the results of these tests. Their attention must be drawn to the potential risks and appropriate recommendations should be suggested in respect of the possible treatment measures.

11) The banks must have pre-approved strategies regarding the treatment measures to be taken based upon the results of these tests, enabling the banks in this regard to identify the points at which treatment measures will be taken (such as: volume of potential risk, the effect on the revenues and capital). The authority matrix must be clearly identified to take the treatment measures. Such measures must be documented and applied appropriately.

12) The types of treatment measures taken by the bank are varied based upon the conditions of each case per se. In general they must include the following:

    * Re-structure of the bank's positions (liquidation or covering up of positions).

    * Reduction of risks limits.

    * Tight funding requirements in order to reduce the credit risks.

    * Building additional capital to face the potential effect of the stress situation.

    * Amendment of the pricing policies of the bank (rate of return / revenue and profitability) so as to reflect the risks identified.

    * Making the necessary arrangement to face the shortage in liquidity under stress situations, to ensure the adequate funding during the crises.

In case the bank makes a decision that there is no need for urgent corrective measures, then the bank has to monitor and manage its activities regularly through more stress testing, and to develop emergency plans to face stress conditions.

13) The banks must ensure that they have adequate information systems to support the stress testing programs. These systems have to permit the conduct of tests on all the bank's activities and consolidate the testing results for the bank as a whole.

14) The banks must regularly review and update the methodology of the testing programs to take into consideration the changes in the nature of the bank's activities and the external positions, in order to evaluate whether the assumptions on which these tests are based are still valid. The banks must carry out the said review process once a year at least, or repeatedly in case there are important changes in the portfolios or changes in the operating environment.

    The review process of the methodology of the stress testing programs must cover the following:

    - The adequacy of stress testing documentation, and the extent of integration of these tests with the daily management of risks at the bank.
    - Volume of exposures resulting from the testing programs.
    - Soundness of the information management system and accuracy and integrity of data inputted.
    - Verification of the test results by referring to historical scenarios of previous tests (comparison with previous incidents).

15) Any amendments suggested in the methodology of the stress testing and its measures must be approved by the senior management of the bank.

Fifth: Risk Factors:

1) The basic step in the stress testing is the identification of the main risk factors to be tested. The bank must list these factors of the risks of each portfolio, analyze these factors and specify the correlation amongst them.

2) The common risk factors related to the banking business include the following:

- **Country Risk:** They are risks which are characterized by the potential of customer default or any factors with negative reflections on the bank's business in that country. The major factors which affect the ability to pay or fulfill the obligations towards banks (such as the retreat of economic growth ratios in these countries, the shocks faced by these markets) must be identified.

- **Risk Concentration:** It includes the concentration in the form of exposures towards individuals, or particular industry, concentration in particular sectors of the market, or concentration in countries or regions.

- **Interest Rate Risks:** They result from the changes in the interest curve and changes in the relationships between the interest rates prevailing in the major markets.

- **Market Rates Risks:** They result from the adverse changes in the prices of assets (stocks, commodities, bonds, real estates, currencies, etc) and the effect of these changes on the portfolios and the markets.

- **Liquidity Risks:** They result from the reduction of credit lines and retreat of liquidity levels in the market under stress situations, and the effect of that on the sources of funding for banks and the cash flow assumptions.

- **Operational Risks:** They result from various factors such as the internal or external embezzlement, system failure, the electronic banking security intrusion, and risks that accompany the provision of particular services and products.

- **Risks of Extra-Ordinary Market Movements:** In terms of their effect on the bank exposures in general.

- **Model Design Assumptions** or Pricing Models, including the correlation assumptions and duration of exposure.

- **Overall Economy Factors** in terms of the Gross Domestic Product, change in the real estate prices, unemployment rates, inflation rates and effect on the other risk factors.

- **Various Political and Economic Factors** related to industries, regional markets and emerging markets.

The above-mentioned list of risks is for reference purposes. Banks must identify their own risks. They have to consider that the risk factors to be identified under the supervisory review process must be the basis for envisaging the incidents of stress testing.

Sixth: Interpretation of the Test Results:

1) The banks must be well versed in their scope of interpretation of the stress testing results, because such stress testing estimate the exposures to test a particular incident, without giving probability that incident may occur.

   Therefore, the effectiveness of the test particularly depends on three basic factors, namely:

   - How far the bank selects the right scenarios.
   - How far the bank interprets the test results correctly.
   - How far the bank takes the proper steps in the light of these results.

Seventh: Scenarios:

1- The scenario analysis **measures** the correlated effects of the adverse movements in a number of risk factors. **It identifies** the assumptions appropriate for the various elements of the stress testing risks to be entered in a particular scenario. **It estimates** the effect on the bank's financial position, such as the effect on the asset quality, profitability and the capital.

2- The banks - when evaluating stress testing scenarios – must review the lessons learned from the past, or develop hypothetical scenarios that reflect the risks resulting from the latest market development.

3- It is preferable that the stress testing scenarios must cover various levels of the adverse effects. For example, it could be three levels:

   - Mild Level.
   - Medium Level.
   - Severe Level.

Each bank must develop the stress testing scenario of the nature of its activity, including the use of some models and working papers appropriate in this regard, so as to show the overall results of the test in terms of effect on the profitability, provisions and capital adequacy ratio.

11- CAPITAL ADEQUACY RATIO

J) Circular No. (2/BS/245/2009) concerning the amendment of instructions on Capital Adequacy Ratio Basel (2).

The banks can refer to some incidents and crises of the past, whether local or external incidents and crises to infer their effects in terms of the decrease of assets prices, retreat of economic growth, decline of the shares prices, reduction in the percentage of the collateral coverage of the customers' debts and liabilities, and the effect of these factors combined on the quality of the assets and the profitability.

Eighth: Types of Scenarios:

1) There are various types of stress testing scenarios that can be applied. Each bank has to decide how far these scenarios are appropriate for it of the risks it faces, and to develop these scenarios to suit these risks, while taking into account the correlation or integration among these various scenarios to form the scenario analysis.

The following are examples of scenarios of various risks:

A- Credit/Finance Risks Scenarios:

- **Retreat in the local economic activity:** This scenario estimates the effect of the adverse changes in the most important major economic variables, on the quality of the bank's assets, profitability and capital adequacy. Among these adverse changes in the economic variables, for example, are the retreat of growth in the Gross Domestic Product of non-oil sectors, the retreat in growth rates in the public expenditure, inflation rates, retreat in the growth rates in the private consumption.

- **Cash and Financial Changes in the countries whose money markets and financial markets are linked with the banks activities in Kuwait.** The scenarios can include the assumption of occurrence of cash or financial crises in such countries.

- **Fall in the Real Estate Activities:** This scenario measures the effect of the decrease in the real estate prices on the collateral coverage percentage, the risks of default and the need to take provisions. Therefore, it shows the effect on the capital adequacy ratio, effect of the decrease of real estates prices on the real estate portfolio held by banks.

- **Increase in rates of irregular debts and specific provisions:** This scenario measures the flexibility of the funding portfolio in terms of the effect of the increase of provisions on the profits and the capital adequacy. When designing this scenario, the banks can assume various percentages of the increase in the irregular debts and rate of provisions.

11- CAPITAL ADEQUACY RATIO

J) Circular No. (2/BS/245/2009) concerning the amendment of instructions on Capital Adequacy Ratio Basel (2).

- **Failure of Funding Customers or Major Counterparties:** This scenario clarifies the effect of the default of funding customers or major counterparties on the banks profitability and the capital adequacy. This scenario can be expanded to include those who deal in various sectors or various countries, or for a group of related customers.

- **Weakness in the quality of consumer funding operations and other installment funding operations (Housing):** This scenario gives estimates of the effect of a set of factors which may lead to the customers failure to fulfill their obligations, including their obligations resulting from the use of credit cards.

B- Examples of Stress Testing Scenarios Related to the Interest Rate Risks:

- **Re-Pricing:** This scenario estimates the effects on the bank's profitability due to the time difference of the interest rate changes and the cash flows related to the assets of fixed rates and in respect of the liabilities and off-balance sheet items.
- **Basic Risks:** This scenario estimates the effects on the bank profitability as a result of the changes in the interest rate in the basic market (change in the discount rate and the effect of that on the structure of the prices, and changes of interest rates in the money market, including the interest rate on the public debt instruments), and their reflections on the interest rate applied by the bank.

C- Examples of the Scenarios Related to Other Risks:

- **Decrease in the Net interest Income, and Profit Margins:** This scenario measures the effect on the net interest income and profit margins, due to the retreat in the growth of the financial portfolio, or the decrease in the pricing due to competition.
- **Adverse Changes in the major Exchange Rates**: This scenario measures the effect on the net open positions in the major currencies.
- **Decrease in the Market Value of the Financial Instruments:** This scenario measures the effect of the adverse changes in the market prices and liquidity positions on the market value of the financial instruments.

- **Retreat in Stock Prices Index:** This scenario measures the effect on the funding margins of the bank or its stock holdings.

- **Liquidity Crises:** This scenario measures the adequacy of short-term liquidity of the bank to face the crises (large cash flows abroad, tightening credit limits).

- **Business Turmoil or System Failure:** This scenario measures the effect on the bank in case of turmoil or failure of equipment, software, and problems in communications.

Finally, the above-mentioned scenarios represent a selected group of scenarios. The banks have to develop their own scenarios of the risks they face, together with the development of models, and working papers to show the appropriate factors and estimates. It is preferable that the scenarios and stress testing cover three levels of risks: mild, medium and severe. The following has to be regarded:

(1) The banks must specify their assumptions in conducting the stress testing.

(2) These scenarios must include the assessment of the effect of the stress testing on the overall profitability of the bank and its capital adequacy (as a result of the decrease in the operational profits before taking the provisions and increase in the bad debts).

(3) The stress testing has to include off-balance sheet exposures, if applicable.

(4) When estimating expected operational profits before provisions, the banks can refer to the profits of the previous year and carry out the appropriate deduction which reflects more difficult operating conditions.

Clarifications on the stress testing of credit risks:

1) The economic growth is the model stress testing which can be used to assess the effect on the quality of assets, provisions, and profitability. Some basic indicators of the performance of the overall economic performance such as unemployment rates, growth of Gross Domestic Product (Nominal and real), particularly for non-oil sectors.

2) The banks have to assess the adverse effects of the scenarios of the economic indicators over 12 months period, and under the three types of stress (mild, medium and severe). On the basis of each scenario, banks have to estimate the positions expected at the end of every (6) months and (12) months in terms of:

- The outstanding balance of the financing portfolio.
- Quality of assets (to be measured on the basis of the level of classified debts and their low percentage).
- Value of the classified and non-classified collateral.
- Level of specific and general provisions.

3) When estimating the volume of the financing portfolio, the banks have to consider, among other factors, the falling growth in financing as a result of the decrease in the consumer and investment spending during the period in which the economic activities retreat. This may lead to pressures on the bank's revenues and the profits margin (rate of return) due to the competition among banks on a particular activity.

4) When estimating the levels of the classified debts and the expected provisions (or bad debts), the banks must specify the relationship between particular economic variables, and the quality of credit of the bank. The bank can estimate the effect of a particular decrease in the prices of real estates and the negative effect of the economic conditions on the rate of growth in provisions and bad debts. The banks have to use their professional estimates to build up on their previous experiences.

Reporting the Stress Testing Results to the Central Bank of Kuwait:

Each bank has to carry out the stress testing on regular and overall basis of the portfolio sensitivity of each bank, based upon its own assumptions.

The Central Bank of Kuwait will specify the regular timing of submitting these data on the forms to be developed by each bank particularly for this purpose, or any other forms to be approved by the Central Bank of Kuwait for this purpose.

GOVERNOR

Jumada Al-Akhir 29, 1430 H
June 22, 2009

THE CHAIRMAN,

Circular No. (2/BS/246/2009)
To Kuwaiti conventional banks

This is made further to the Central Bank of Kuwait Circular dated 15/6/2009 regarding the amendments made on Basel II Capital Adequacy Ratio, Second Pillar Supervisory Review Process, within the framework of emphasizing the need for banks to conduct internal capital adequacy assessment process (ICAAP) of the directives relating to stress testing, as attached to the above-mentioned amendments.

Your bank, based on the said instructions, should conduct the proper stress testing of the above-mentioned instructions of the stress testing directives, for your bank's financial statements as at end of June 2009. The results of the above stress testing should be supplied to us no later than end of July 2009.

Also, your bank should provide us with the above stress testing results on a half-yearly basis, within the scope of your bank's internal capital adequacy assessment process (ICAAP) as detailed in the capital adequacy instructions issued on the above date. ICAAP results, including the stress testing results, should reach us together with the capital adequacy ratio statements.

With my best wishes,

SALEM ABDUL AZIZ AL-SABAH

GOVERNOR

Rajab 14, 1430 H
July 7, 2009

THE CHAIRMAN,

CIRCULAT TO ALL LOCAL BANKS

This has reference to the circular dated 13/5/2009, requesting you to advise us of the findings of the stress testing conducted by banks in accordance with the financial position as of 31/3/2009.

I would like to advise you that the data and information provided by banks revealed several observations, mainly:

1) Most of the scenarios assumed by banks in general had a nature that, in the most extreme cases, will not have a considerable adverse impact on their position. In other words, banks have not resorted to extreme scenarios, thus the findings of the used worst scenarios did not pose a considerable threat to the bank's position, which gives the impression that it is easy to overcome the condition if the scenario's events come into reality.

2) A large percentage of banks addressed the impact of their exposure to certain scenarios on both profitability and capital adequacy ratio. However, the statements and studies submitted to us by most of those banks have not included their plan to support the capital, and lacked any mention about treating the conditions resulting in the decline in profitability and in the realization of losses. This should have been addressed and studied by banks in the sense of establishing a methodology to deal with the stress testing, as a supplementary step thereto, because the testing is not a goal in itself, but rather represents precautionary measures and pre-thoughts to face such scenarios if they materialize.

3) The majority of banks have not relied on any independent, professional, neutral entity while conducting the stress testing. Objectivity necessitates that the conductor of such testing, or at least the reviewing party, should be an entity independent from the bank's management. However, if conducted by the management, there should be another independent entity to conduct an audit or review of such testing, within the framework of quality assurance regarding the data and assumptions.

4) Risk Departments of banks were not sufficiently prepared or qualified to conduct the stress testing. Their systems used in risk identification, analysis and measurement have not covered the possibility of conducting such testing in a systematic, pre-specified manner in the business policies and procedures of the risk concerned departments.

In addition to the above observations, your bank should consider the following:

A) Stress testing conducted by banks should cover off-balance sheet items. The majority of responses by banks were void of any indication that they have taken those items in their projections, although they represent part of the banking operations that may contain influential risk, which necessitates considering this point as banks conduct future stress testing.

B) Findings of the stress testing conducted by each bank should be presented to its board of directors, and discussed. This should be given priority and attention at both the top management and board of directors levels. Board of directors contribution to the discussion, and approval of the stress testing procedures, is a strategic matter that is related to the scope of interests and roles of the board of directors.

We hereby stress that your bank should conduct stress testing on a regular basis (half-yearly), and advise the Central Bank of Kuwait, no later than the end of the month for which the testing is prepared, of the results of such testing. Banks should comply with the directives to banks, as stated in the annex to Section Twelve (Supervisory Review Process) of the instructions regarding Basel II Capital Adequacy Ratio Instructions.

With my best wishes,

SALEM ABDUL AZIZ AL-SABAH

GOVERNOR

Rajab 1, 1431 H
June 13, 2010

THE CHAIRMAN,

CIRCULAR NO. (2/BS, IBS/303/2010)
TO ALL KUWAITI BANKS

This has reference to the Central Bank of Kuwait Circular to Kuwaiti banks dated 22/6/2009, regarding providing the Central Bank of Kuwait, on a half-yearly basis, with reports on financial stress testing and internal capital adequacy assessment process (ICAAP).

Attached please find a CD containing a set of forms and appendices that Kuwaiti banks should submit to the Central Bank of Kuwait, together with the financial stress testing and ICAAP reports, accompanying your bank's financial statements.

These forms and appendices were prepared of the Central Bank of Kuwait directives regarding the financial stress testing and ICAAP, and within a regulatory framework that aims at encouraging banks to improve their risk management, while enhancing the regulatory tools of the Central Bank of Kuwait.

It is worth mentioning that the forms and appendices were discussed in detail during meetings held at the Central Bank of Kuwait with risk managers and officials of the Kuwaiti banks.

Your bank should submit these forms and appendices to the Central Bank of Kuwait, on a half-yearly basis, duly signed by the bank's CEO or Chairman, accompanying the financial stress testing and ICAAP reports, together with your bank's financial statements, as well as an e-mail copy.

With my best wishes,

SALEM ABDUL AZIZ AL-SABAH

11- CAPITAL ADEQUACY RATIO

M) Circular No. (2/BS, IBS/303/2010) concerning providing the Central Bank of Kuwait, on a half year basis, with reports on financial stress testing and internal capital adequacy assessment process (ICAAP).

Form No. (1)

Findings of Financial Stress Testing According to the Bank's Methodology and Assumptions
One Year* Outlook
Financial Position as at ………..

Bank: (KD 000's)

Description	**Actual Results for the Period Ended: DD/MM/YYYY**	**First (Mild) Scenario Testing Results**	**Second (Medium) Scenario Testing Results**	**Third (Severe) Scenario Testing Results**
Operating results (before provisions)				
Loan/finance provision (specific)				
Loan/finance provision (general)				
Loan/finance provision (other)				
Losses from impairment of investment securities				
Losses from impairment of non-financial investments				
Losses from impairment of other investments				
Other				
Total provisions and losses from impairment of investments	**0**	**0**	**0**	**0**
Net profit (loss)				
Capital base				
Risk-weighted assets				
Capital adequacy ratio				

* With effect from 1/7/2010.

The set of these forms and schedules shall be attached to the reports provided by the bank on the financial stress testing and Internal Capital Adequacy Assessment Process (ICAAP), signed by the CEO.

Form No. (2)

Findings of Financial Stress Testing According to The Central Bank of Kuwait Methodology and Assumptions One Year* Outlook Financial Position as at ………..

Bank: (KD 000's)

Description	Actual Results for The Period Ended: DD/MM/YYYY	First Scenario Testing Results	Second Scenario Testing Results	Third Scenario Testing Results
Operating results (before provisions)				
Loan/finance provision (specific)				
Loan/finance provision (general)				
Loan/finance provision (other)				
Losses from impairment of investment securities				
Losses from impairment of non-financial investments				
Losses from impairment of other investments				
Other				
Total provisions and losses from impairment of investments	**0**	**0**	**0**	**0**
Net profit (loss)				
Capital base				
Risk-weighted assets				
Capital adequacy ratio				

* With effect from 1/7/2010.

Attached is the financial stress testing scenario as per the Central Bank of Kuwait assumptions (2/A).

Brief Analytic Statement
Operating Results for the Purpose of Financial Stress Testing
In Accordance with the Bank's Methodology and Assumptions
One Year* Outlook
Financial Position as at …………

Bank: (KD 000's)

	Actual Results for the Period Ended DD/MM/YYYY	1st Scenario (Mild)	2nd Scenario (Medium)	3rd Scenario (Severe)
Interest income/returns	0.0	0.0	0.0	0.0
• Loan/finance portfolio				
• Financial instruments				
• Other				
Interest expenses	0.0	0.0	0.0	0.0
• Private sector deposits				
• Government deposits				
• Financial instruments				
• Other				
Net interest income	0.0	0.0	0.0	0.0
• Net fees and commissions				
• Net profit/(loss) from financial investments				
• Net profit/(loss) from non-financial investments				
• Net profit from FX trading				
• Income from profit distribution				
• Net other operating income				
Net operating income	0.0	0.0	0.0	0.0
• Staff cost				
• Other administrative expenses				
• Depreciation				
• Amortization				
Operating expenses	0.0	0.0	0.0	0.0
Operating results before provisions and losses from impairment of investments	0.0	0.0	0.0	0.0
Provisions and losses from impairment of investments				
Operating profit	0.0	0.0	0.0	0.0
Taxes				
Net profit (loss)	0.0	0.0	0.0	0.0

* With effect from 1/7/2010

11- CAPITAL ADEQUACY RATIO
M) Circular No. (2/BS, IBS/303/2010) concerning providing the Central Bank of Kuwait, on a half year basis, with reports on financial stress testing and internal capital adequacy assessment process (ICAAP).

Capital Requirements for Risks of Pillars I and II Of ICAAP In Accordance with the Results of Financial Stress Testing According to the Bank's Methodology and Assumptions Financial Position as at …………..

Bank: (KD 000's)

No.	Description	Actual Results		Scenario (1)		Scenario (2)		Scenario (3)	
		Risk Weighted Assets	**Capital Requirements**	**Risk Weighted Assets**	**Capital Requirements**	**Risk Weighted Assets**	**Capital Requirements**	**Risk Weighted Assets**	**Capital Requirements**
Pillar I Risk									
1	Credit risk								
2	Market risk								
3	Operational								
Total Risk of Pillar I		0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Pillar II Risk									
1	Credit concentrations risk								
2	Residual credit risk								
3	Market risk								
4	Residual operational risk								
5	Interest rate risk								
6	Liquidity risk								
7	Legal risk								
8	Reputation risk								
9	Strategic risk								
10	Other risks ( )								
11	Other risks ( )								
12	Other risks ( )								
Total Risk of Pillar II		0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Grand Total of Risks		0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Capital Base									
A. Capital adequacy ratio under Pillars I & II									
B. Capital adequacy ratio under Pillar I									

The Central Bank of Kuwait Stress Testing Scenarios

<table>
<tr><th rowspan="2">Scenario Components</th><th rowspan="2">Stress Testing items</th><th colspan="3">Stress Testing Scenario</th></tr>
<tr><th>1st Scenario</th><th>2nd Scenario</th><th>3rd Scenario</th></tr>
<tr><td rowspan="5">Retail Exposures (1)</td><td><u>Retail Loans</u>
• Installment Loans</td><td>Increase of existing specific provisions by 2% of portfolio</td><td>Increase of existing specific provisions by 3% of portfolio</td><td>Increase of existing specific provisions by 5% of portfolio</td></tr>
<tr><td>• Consumer Loans</td><td>Increase of existing specific provisions by 2% of portfolio</td><td>Increase of existing specific provisions by 3% of portfolio</td><td>Increase of existing specific provisions by 5% of portfolio</td></tr>
<tr><td>• Credit Cards</td><td>Increase of existing specific provisions by 2% of portfolio</td><td>Increase of existing specific provisions by 3% of portfolio</td><td>Increase of existing specific provisions by 5% of portfolio</td></tr>
<tr><td>• Share financing loans</td><td>Increase of existing specific provisions by 5% of portfolio</td><td>Increase of existing specific provisions by 10% of portfolio</td><td>Increase of existing specific provisions by 20% of portfolio</td></tr>
<tr><td>• Other Personal Loans</td><td>Increase of existing specific provisions by 2% of portfolio</td><td>Increase of existing specific provisions by 5% of portfolio</td><td>Increase of existing specific provisions by 10% of portfolio</td></tr>
<tr><td>Corporate Exposures (1)</td><td>• Loans Portfolio</td><td>Increase of existing specific provisions by 2% of portfolio</td><td>Increase of existing specific provisions by 5% of portfolio</td><td>Increase of existing specific provisions by 10% of portfolio</td></tr>
<tr><td colspan="2">Financial & Real Estate Investments (2)</td><td>Increase of provisions by 10% of total portfolio</td><td>Increase of provisions by 20% of total portfolio</td><td>Increase of provisions by 30% of total portfolio</td></tr>
<tr><td rowspan="4">Interest Rate Risk and Liquidity Risk Exposure (Rate of Return)</td><td>• Interest Rate on Loans</td><td>Decrease by 50 bp</td><td>Decrease by 100 bp</td><td>Decrease by 100 bp</td></tr>
<tr><td>• Interest Rate on Savings</td><td>No change</td><td>Increase by 25 bp</td><td>Increase by 50 bp</td></tr>
<tr><td>• Interest Rate on Fixed Deposits</td><td>No change</td><td>Increase by 25 bp</td><td>Increase by 50 bp</td></tr>
<tr><td>• KIBOR</td><td>No change</td><td>Increase by 25 bp</td><td>Increase by 50 bp</td></tr>
<tr><td>Operating Results before Provisions</td><td>• Non-Interest Income</td><td>Decrease by 10%</td><td>Decrease by 20%</td><td>Decrease by 30%</td></tr>
</table>

(1) Increase in specific provisions is calculated on the basis of net portfolio (portfolio balance less interest in suspense and specific provisions). Exposures include on and off-balance sheet items. Credit amounts equivalent to off-balance sheet items exposure are calculated on the basis of the credit transfer factor in accordance with Basel II Capital Adequacy regulations issued by the Central Bank of Kuwait.

(2) Financial and real estate investments: public debt instruments issued by the government of the State of Kuwait, are excluded from the balance.
Loans portfolio includes off-balance sheet items.

Schedule (A)
Notes to Schedules of Pillar II Risk

(Schedules 1-9)

The bank shall estimate the capital necessary to meet **each type of risk of the general assessment factors**, representing the following:

1. **Level of activity associated risk**, and whether the risk was sufficiently covered under Pillar I. As an example, for illustration purpose: (credit concentration risk, residual risk resulting from mitigation of credit risk, residual operational risk, interest rate risk in bank records, liquidity risk, strategic risk, …. Etc).

2. **Adequacy and efficiency of the bank's systems and internal controls** as for the types of risk under Pillar II, specifically risk management systems, internal control systems, support systems, such as IT systems, and infrastructure necessary to carry out activities …. Etc.

3. **Efficiency of the bank's Internal Capital Adequacy Assessment Process (ICAAP)**, adequacy of stress testing, capital quality and strength, risk appetite, ability to support the bank's liquidity during difficult times, ability to support capital base, **and level of supervision by the Board of Directors and Executive Management … etc**.

4. **Quality of Governance Standards applied by the bank, and the bank's compliance with such standards**.

In addition to the above referenced general assessment factors, the bank should take into consideration **the private assessment factors** relating to the bank's activities and operations, which may lead to increase or mitigation of risk. Examples to the risk mitigation include the benefits achieved by the bank as a result of activity distribution, or the existence of insurance coverage for some types of significant operating risks, and any other factors leading to reduction of capital adequacy requirements, as well as the impact of a set of other factors used by the bank when conducting the stress testing, and any other factors adopted by the bank.

Note: The bank should also state, in each schedule of Pillar II Risks, the methodology followed in the assessment of risk and the additional capital against the risk.

Schedule (A)/1
Additional Capital to Meet Credit Concentration Risk Under Pillar II According to the Financial Position as at …………

(KD 000's)

Additional capital to meet credit concentration risk KD (   ).
The bank's clarification of the assessment factors to estimate the additional capital to meet credit concentration risk. (Additional sheets may be used):
In addition to the assessment factors referred to in Schedule (A), while estimating credit concentration risk, the bank should take into consideration the risk of large exposure to one customer or a group of customers. Such concentrations may be within or off-balance sheet. Also, consideration should be given to the credit exposures to a group of customers in certain business sectors or countries. Banks should estimate such risks of the effectiveness of their concentration risk management, and whether the bank has maximum internal limits policy for credit concentration other than the regulatory controls issued by the Central Bank of Kuwait regarding maximum limits for credit concentration, as well as stress testing they conduct for the risk of such concentrations.

Schedule (A)/2
Additional Capital to Meet Residual Credit Risk Under Pillar II*
According to the Financial Position as at …………

(KD 000's)

Additional capital to meet residual credit risk KD (   ).
The bank's clarification of the assessment factors to estimate the additional capital to meet residual credit risk. (Additional sheets may be used):
In addition to the assessment factors referred to in Schedule (A), the bank should take into consideration the fact that such risks mainly cover the residual risks resulting from the mitigation of credit risk by using credit risk mitigates, such as collaterals, while reducing the minimum requirements of regulatory capital under Pillar I. However, the application of such mitigates may cause emergence of other risks, such as documentation risk, operational risk, and other risks that may undermine the impact of mitigates.

Schedule (A)/3
Additional Capital to Meet Market Risk Under Pillar II
According to the Financial Position as at …………

(KD 000's)

Additional capital to meet market risk KD (   ).
The bank's clarification of the assessment factors to estimate the additional capital to meet market risk. (Additional sheets may be used):
In addition to the assessment factors referred to in Schedule (A), while estimating the additional capital for financial portfolios, banks should take into consideration the risks arising from improper distribution of investments in the financial markets or business sectors, the risks arising from the existence of financial instruments that lack high liquidity, the risks of concentration on markets that lack relatively intensive trading, as well as the risks of financial portfolios that involve large numbers of positions approved using the assessment models, and the country risk.

Schedule (A)/4
Additional Capital to Meet Operational Risk Under Pillar II
According to the Financial Position as at …………

(KD 000's)

Additional capital to meet operational risk KD ( ).
The bank's clarification of the assessment factors to estimate the additional capital to meet operational risk. (Additional sheets may be used):
In addition to the assessment factors referred to in Schedule (A), while estimating the operational risk, the bank should take into consideration the risks not directly specified in Pillar I, which may arise out of failure of the bank's business systems, or security scamming or e-banking, internal and external embezzlement risk, and risks associated with the provision of certain products and services. The bank should ensure that it has in place an efficient and comprehensive framework for operational risk management, which specifies the types of operational risks associated with the various activities.

Schedule (A)/5
Additional Capital to Meet Interest Rate Risk Under Pillar II
According to the Financial Position as at …………

(KD 000's)

Additional capital to meet interest rate risk KD (   ).
The bank's clarification of the assessment factors to estimate the additional capital to meet interest rate risk. (Additional sheets may be used):
In addition to the assessment factors referred to in Schedule (A), while estimating the additional capital, banks should ensure that they have in place proper policies to effectively manage the interest rate risk, and how far they are aware of the interest rate risk relating to the new products they have, while defining and designating the major sources of interest rate risks associated with the assets/liabilities and positions of off-balance sheet items, interest rate sensitivity, and the risks arising from re-pricing, of assets/liabilities match.

Schedule (A)/6
Additional Capital to Meet Liquidity Risk Under Pillar II
According to the Financial Position as at …………

(KD 000's)

Additional capital to meet liquidity risk KD ( ).
The bank's clarification of the assessment factors to estimate the additional capital to meet liquidity risk. (Additional sheets may be used):
In addition to the assessment factors referred to in Schedule (A), while estimating the additional capital for liquidity risk, banks should take into consideration the risks arising from reduction of credit lines and retreat of liquidity levels in the market due to difficult conditions, and the impact of this on the bank's sources of finance, as well as cash flow assumptions.

11- CAPITAL ADEQUACY RATIO

M) Circular No. (2/BS, IBS/303/2010) concerning providing the Central Bank of Kuwait, on a half year basis, with reports on financial stress testing and internal capital adequacy assessment process (ICAAP).

Schedule (A)/7
Additional Capital to Meet Legal Risk Under Pillar II
According to the Financial Position as at …………

(KD 000's)

Additional capital to meet legal risk KD (   ).
The bank's clarification of the assessment factors to estimate the additional capital to meet legal risk. (Additional sheets may be used):
In addition to the assessment factors referred to in Schedule (A), while estimating the legal risk, banks should take into consideration the systems, policies and legal departments they have in place, so as to mitigate the risks on banks as a result of the losses arising from the lack of documents, or failure to obtain the necessary authorizations from customers who are involved in trading with the bank, or failure to sign contracts, or violation by the bank of legal rules.

Schedule (A)/8
Additional Capital to Meet Reputation Risk Under Pillar II
According to the Financial Position as at …………

(KD 000's)

Additional capital to meet reputation risk KD (   ).
The bank's clarification of the assessment factors to estimate the additional capital to meet reputation risk. (Additional sheets may be used):
In addition to the assessment factors referred to in Schedule (A), while estimating reputation risk, banks should take into consideration the various risks arising from the bank's exposure to events that may adversely affect the customer base and the bank's performance, as well as its exposure to various pressures.

Schedule (A)/9
Additional Capital to Meet Strategic Risk Under Pillar II
According to the Financial Position as at …………

(KD 000's)

Additional capital to meet strategic risk KD (   ).
The bank's clarification of the assessment factors to estimate the additional capital to meet strategic risk. (Additional sheets may be used):
In addition to the assessment factors referred to in Schedule (A), while estimating the additional capital, banks should take into consideration the various effects of the existence of administrative or external obstacles affecting the execution of decisions relating to the initiation of banking products or services, expansion of business, restructuring thereof, or other strategic decisions.

Schedule (B)
Summary of Bank's Methodology and Scenarios Applied when Conducting Stress Testing

Summary of the contents of the **Bank's Report** on the methodology adopted when conducting the stress testing (additional sheets may be used:
The part relating to risk appetite (risk appetite is identified taking into consideration the current definition of capital base according to the current instructions for the use of Standardized Approach):
This schedule provides a summary of the methodology relating to stress testing, as stated in the report attached by the bank to the set of schedules and tables, **together with identifying the bank's risk appetite, as approved by the Board of Directors**.

11- CAPITAL ADEQUACY RATIO

M) Circular No. (2/BS, IBS/303/2010) concerning providing the Central Bank of Kuwait, on a half year basis, with reports on financial stress testing and internal capital adequacy assessment process (ICAAP).

Schedule (C)
The Bank's Vision of the Findings of Stress Testing Conducted by the Bank Under the Bank's Methodology and Scenarios

Bank's vision: The bank's clarification of its vision vis-à-vis the findings of the stress testing and the actions it deems appropriate of such findings (additional sheets may be used):
• This schedule lists a summary of the bank's vision regarding the findings of the stress testing conducted by the bank in accordance with its own methodology and scenarios. This includes the results that, in the bank's vision, require certain actions. These include, <u>for example</u>: restructuring of the bank's positions, reducing the risk limits and <u>reconsidering risk appetite</u>, tightening the terms of lending and required collaterals, amending pricing policy of the bank, adopting arrangements in the area of liquidity management, building additional capital to meet the probable impact of difficult situations, and other actions which the bank deems appropriate of such findings.

GOVERNOR

Rajab 2, 1431 H
June 14, 2010

THE GENERAL MANAGER,

Circular No. (2/BS/260/2010)
To all Branches of Foreign Banks
Operating in the State of Kuwait

This is made pursuant to our letter dated 7/7/2009 regarding advising us of the findings of the financial stress testing regularly conducted by your bank (half-yearly).

Attached please find a CD, containing a set of forms and schedules that your bank should submit to the Central Bank of Kuwait, accompanied with the report prepared on financial stress testing.

Those forms and schedules should be signed by the CEO of your bank's branch in the State of Kuwait, **annually with effect from the period ending 31/12/2010**, and submitted together with the financial stress testing report and your bank's financial statements. Forms and schedules should be submitted online.

With my best wishes,

SALEM ABDUL AZIZ AL-SABAH

11- CAPITAL ADEQUACY RATIO

N) Circular No. (2/BS,IBS/260/2010) to all foreign banks operating in Kuwait to provide the Central Bank of Kuwait with annual models relating to reports on financial stress testing.

Form No. (1)

Findings of Financial Stress Testing According to the Bank's Methodology and Assumptions One Year Outlook Financial Position as at ……….. (Foreign Banks' Branches)

Bank: (KD 000's)

Description	**Actual Results for the Period Ended: DD/MM/YYYY**	**First (Mild) Scenario Testing Results**	**Second (Medium) Scenario Testing Results**	**Third (Severe) Scenario Testing Results**
Operating results (before provisions)				
Loan/finance provision (specific)				
Loan/finance provision (general)				
Loan/finance provision (other)				
Losses from impairment of investment securities				
Losses from impairment of non-financial investments				
Losses from impairment of other investments				
Other				
Total provisions and losses from impairment of investments	**0**	**0**	**0**	**0**
Net profit (loss)				
Capital base				
Risk-weighted assets				
Capital adequacy ratio				

The set of these forms and schedules shall be attached to the reports provided by the bank on the financial stress testing, signed by the CEO of your Bank's branch in the State of Kuwait.

Form No. (2)

Findings of Financial Stress Testing According to the Central Bank of Kuwait Methodology and Assumptions
One Year Outlook
Financial Position as at ………..
(Foreign Banks Branches)

Bank: (KD 000's)

Description	**Actual Results for the Period Ended: YYYY/MM/DD**	**First Scenario Testing Results**	**Second Scenario Testing Results**	**Third Scenario Testing Results**
Operating results (before provisions)				
Loan/finance provision (specific)				
Loan/finance provision (general)				
Loan/finance provision (other)				
Losses from impairment of investment securities				
Losses from impairment of non-financial investments				
Losses from impairment of other investments				
Other				
Total provisions and losses from impairment of investments	**0**	**0**	**0**	**0**
Net profit (loss)				
Capital base				
Risk-weighted assets				
Capital adequacy ratio				

Attached are the financial stress testing scenarios as per the Central Bank of Kuwait assumptions (2/A).

Brief Analytic Statement
Operating Results of Financial Stress Testing
In Accordance with the Bank's Methodology and Assumptions
One Year Outlook
Financial Position as at …………
(Foreign Banks' Branches)

Bank: (KD 000's)

	Actual Results for the Period Ended: DD/MM/YYYY	1st Scenario (Mild)	2nd Scenario (Medium)	3rd Scenario (Severe)
Interest income/returns	0.0	0.0	0.0	0.0
• Loan/finance portfolio				
• Securities				
• Other				
Interest expenses	0.0	0.0	0.0	0.0
• Private sector deposits				
• Government deposits				
• Securities				
• Other				
Net interest income	0.0	0.0	0.0	0.0
• Net fees and commissions				
• Net profit/(loss) from financial investments				
• Net profit/(loss) from non-financial investments				
• Net profit from FX trading				
• Income from profit distribution				
• Net other operating income				
Net operating income	0.0	0.0	0.0	0.0
• Staff cost				
• Other administrative expenses				
• Depreciation				
• Amortization				
Operating expenses	0.0	0.0	0.0	0.0
Operating results before provisions and losses from impairment of investments	0.0	0.0	0.0	0.0
Provisions and losses from impairment of investments				
Operating profit	0.0	0.0	0.0	0.0
Taxes				
Net profit (loss)	0.0	0.0	0.0	0.0

The Central Bank of Kuwait Financial Stress Testing Scenarios

Scenario Components	Stress Testing Items	Stress Scenario: 1st Scenario	Stress Scenario: 2nd Scenario	Stress Scenario: 3rd Scenario
Retail Exposures(1)	**Retail loans** • Installment loans	Increase of existing specific provisions by 2% of portfolio	Increase of existing specific provisions by 3% of portfolio	Increase of existing specific provisions by 5% of portfolio
	• Consumer loans	Increase of existing specific provisions by 2% of portfolio	Increase of existing specific provisions by 3% of portfolio	Increase of existing specific provisions by 5% of portfolio
	• Credit cards	Increase of existing specific provisions by 2% of portfolio	Increase of existing specific provisions by 3% of portfolio	Increase of existing specific provisions by 5% of portfolio
	• Share financing loans	Increase of existing specific provisions by 5% of portfolio	Increase of existing specific provisions by 10% of portfolio	Increase of existing specific provisions by 20% of portfolio
	• Other personal loans	Increase of existing specific provisions by 2% of portfolio	Increase of existing specific provisions by 5% of portfolio	Increase of existing specific provisions by 10% of portfolio
Corporate Exposures(1)	• Loan portfolio	Increase of existing specific provisions by 2% of portfolio	Increase of existing specific provisions by 5% of portfolio	Increase of existing specific provisions by 10% of portfolio
Financial and Real Estate Investments(2)		Increase of provisions by 10% of portfolio	Increase of provisions by 20% of portfolio	Increase of provisions by 30% of portfolio
Interest Rate Risk Exposure and Liquidity Risk (Rate of Return)	• Loan interest rate	Decline by 50 bp	Decline by 100 bp	Decline by 100 bp
	• Savings interest rate	Unchanged	Increase by 25 bp	Increase by 50 bp
	• Time deposit interest rate	Unchanged	Increase by 25 bp	Increase by 50 bp
	• KIBOR	Unchanged	Increase by 25 bp	Increase by 50 bp
Operating Results Before Provisions	• Non-interest income	Decline by 10%	Decline by 20%	Decline by 30%

(1) Increase in specific provisions is calculated on the basis of the net portfolio (balance of portfolio less: interest in suspense and specific provisions). Exposures include balance sheet and off-balance sheet items. Credit amounts equivalent to off-balance sheet exposure are calculated on the basis of the credit transfer factor, in accordance with Capital Adequacy Ratio (Basel II) regulations issued by the Central Bank of Kuwait.

(2) Financial and real state investments: public debt instruments issued by the government of the State of Kuwait shall be excluded from the balance.
Loan portfolio includes off-balance sheet items.

11- CAPITAL ADEQUACY RATIO

N) Circular No. (2/BS,IBS/260/2010) to all foreign banks operating in Kuwait to provide the Central Bank of Kuwait with annual models relating to reports on financial stress testing.

Schedule (A)
Summary of the Bank's Methodology
And Applied Scenarios when
Conducting Stress Testing
(Foreign Banks Branches)

Summary of the contents of **the bank's report** on the methodology applied when conducting the stress testing (additional sheets may be used):
This schedule shows a summary of the bank's methodology regarding the stress testing, as against the report attached by the bank to the set of schedules and tables, **specifying the bank's approved risk appetite**.

11- CAPITAL ADEQUACY RATIO

N) Circular No. (2/BS,IBS/260/2010) to all foreign banks operating in Kuwait to provide the Central Bank of Kuwait with annual models relating to reports on financial stress testing.

Schedule (B)
Bank's vision of the Findings of the Stress Testing
Conducted According to the Bank's Methodology and Scenarios
(Foreign Banks Branches)

Bank's vision: Clarify the bank's vision regarding the findings of financial tress testing, and the actions it deems as required in light of such findings (additional sheets may be used):
• This schedule lists a summary of the bank's vision regarding the findings of stress testing conducted according to its methodology and scenarios. This includes the findings that the bank deems as requiring certain actions, including, <u>for example</u>: restructuring the bank's positions, reducing the risk limits and <u>reconsidering the risk appetite</u>, tightening the terms of lending and request for collaterals, amending the bank's pricing policy, adopting measures in the area of liquidity management, building additional capital to meet the potential impact of the difficult conditions, and other actions that the bank deems appropriate of such findings.

N) Circular No. (2/BS,IBS/260/2010) to all foreign banks operating in Kuwait to provide the Central Bank of Kuwait with annual models relating to reports on financial stress testing.