Liquidity Risk Management

The Liquidity Coverage Ratio (LCR) report for Burgan Bank Group ("Burgan" or "the Bank" or "the Group") has been prepared in accordance with the public/market disclosure requirements and guidelines in respect of the Liquidity Coverage Ratio Disclosure Standards as published by Central Bank of Kuwait ("CBK") in December 2014.

The purpose of this document is to disclose both qualitative and quantitative information regarding Burgan's liquidity position, LCR results and internal liquidity risk measurement and management processes.

Liquidity risk is the risk to earnings or capital arising from a bank's inability to meet its obligations or commitments to a customer, creditor, or investor as they fall due without incurring unacceptable losses. It generally arises from either an inadequate liabilities profile or a bank's failure to recognize or address changes in market conditions that affect its ability to liquidate assets (i.e. convert them to cash) quickly and with minimal loss in value. The primary objective of Burgan Bank`s Liquidity Risk management framework is to ensure that the Bank has sufficient liquidity to meet its obligations in both normal and stressed conditions without having to make unplanned sales of assets or borrow expensive funds under emergency conditions.

The Bank's Board of Directors ("the Board") has overall responsibility for liquidity risk management and for ensuring that risk exposures are maintained at prudent levels. To this end, the Board has established an appropriate liquidity risk management framework for the management of the Bank's funding and liquidity management requirements. The Board defines the Bank's liquidity risk strategy based on recommendations made by the Asset and Liability Committees ("ALCO"). The Board reviews and approves the liquidity management policies and ensures that senior management manages liquidity risk effectively in the context of the Bank's business plan and long term funding strategy, taking into account prevailing economic and financial conditions.

The Bank adopts a multipronged approach to managing liquidity risk. This involves monitoring and managing several liquidity metrics, such as a conservative loans to deposits ratio, more than adequate reserves, a portfolio of high quality liquid assets and banking facilities, and the continuous monitoring of forecast and actual cash flows. In addition, the Bank uses liquidity ratios and liquidity scenarios (behavioral, contractual and stressed) as key metrics to establish its liquidity risk tolerance levels. These metrics measure the Bank's ability to fulfill all its payment obligations stemming from ongoing business operations under various scenarios. The tolerance levels are defined either in the form of limits or management action triggers and are part of the Bank's overall liquidity management framework which is approved and reviewed by the Board on regular basis.

The Bank's Treasury unit is responsible for managing day-to-day funding activities within the established liquidity risk management policies and limits. It is responsible for establishing effective communication channels within the Bank's operational and business areas to alert the funding desks of imminent funding requirements including loan drawdowns, deposit withdrawals and off-balance sheet commitments. Treasury and Market Risk personnel monitor market developments, understand their implications for the Bank's liquidity risk exposures and recommend appropriate risk management measures to ALCO.

Group Market Risk (GMR), a unit of the Risk Management Group (RMG), periodically reviews liquidity risk policies and procedures, the adequacy of the risk measurement system, including key assumptions and scenarios used and reports its findings and recommendations to ALCO. GMR is also responsible for monitoring and reporting adherence to the various liquidity ratios and limits, both internal and regulatory on a regular basis.

Funding strategy

The Bank's funding strategy is to develop a diversified funding base, while providing protection against unexpected fluctuations. It aims to align sources of funding with their use. As such, earning assets (Loans and Investments) are largely funded with customer deposits. The funding gap for these assets is met using medium to long term debt issuance and other secured/unsecured long and short term funding sources.

Funding strategy (continued)

The Bank maintains access to a variety of sources of wholesale funds in multiple currencies across a variety of distribution channels, maturities, instruments and geographies, including those available from syndications, bond investors, money markets, repo markets and term depositors. It is an active participant in the money market and has direct access to local and international liquidity providers. On 30 June 2016, the Bank successfully established a US$1.5BN Reg S EMTN Program, under which the Bank may issue senior unsecured debt securities (through public or private placements). The Bank issued bonds worth US$500MM under this program in Q3'16.

Liquidity risk mitigation techniques

The Bank maintains excess liquidity in the form of cash and unencumbered high-quality liquid securities that together serve as the Bank's primary means of liquidity risk mitigation. Additionally, the Bank remains focused on diversifying funding sources. Access to both local and international money markets allows the Bank to maintain liquidity in both local and foreign currencies.

Stress Testing

The Bank's Liquidity management policies and limits ensure that liquidity is maintained at sufficiently comfortable levels to support operations and meet payment demands even under stressed market conditions. The Bank also has in place comprehensive stress testing policies and liquidity contingency funding that incorporate multiple scenarios covering both specific and general market-related events. The purpose of liquidity stress testing is to determine the incremental funding that may be required under extreme scenarios.

Stress testing is fully integrated into the Bank's liquidity risk management framework. It assesses the Bank's ability to generate sufficient liquidity under extreme conditions and is a key input when defining liquidity targets and limits.

Contingency Funding Plan

The Bank's contingency funding plan sets out the action the Bank would take to fund business activity in crisis situations and periods of market stress. The plan outlines a list of potential risk factors, key reports and metrics that are reviewed on an ongoing basis to assist in assessing the severity of a liquidity crisis and/or market dislocation. It also describes in detail the Bank's potential response if the assessment indicates it has entered a liquidity crisis. Mitigants and action items to address specific risks are also described and assigned to groups and/or individuals responsible for implementation.

The contingency funding plan identifies key groups of individuals to ensure effective coordination, control and distribution of information that is critical to the management of a crisis or period of funding stress. It also details the responsibilities of these groups and/or individuals, which include making and disseminating key decisions, coordinating all contingency activities throughout the duration of the crisis or period of market stress, implementing liquidity maintenance activities and managing internal and external communication.

Other Qualitative Information

The Liquidity Coverage Ratio (LCR) is a Basel III metric that measures the sufficiency of High Quality Liquid Assets (HQLA) available to meet net short-term financial obligations over a thirty day period in an acute stress scenario. In December 2014, CBK released the final guideline on "Liquidity Coverage Ratio Disclosure Standards", requiring banks to disclose the LCR ratio beginning in Q1, 2016. LCR is disclosed using CBK's template and is calculated using the average of daily positions during the quarter. The Central Bank of Kuwait's ("CBK") regulatory minimum coverage level for LCR is currently 80%.

High Quality Liquid Assets (HQLA)

HQLAs are assets which can be easily and immediately converted into cash at little or no loss of value. There are two categories of assets that can be included in the stock of HQLA. Level 1 assets can be included without limit and with no haircut and are comprised of coins and banknotes, central bank reserves, Kuwaiti government securities, balances with central banks of countries where the Bank has subsidiaries, and securities issued by highly-rated foreign sovereigns, multilateral development banks and supranationals. Level 2 assets can be included subject to the requirement that they comprise no more than 40% of the overall stock of HQLA after haircuts have been applied. These may include certain qualifying government securities, public sector and corporate bonds. For the quarter ended Q4, 2017, the stock of HQLA held by the Bank includes 92% Level 1 assets and 8% Level 2 assets. Also, on a conservative basis and as required by regulators, it is assumed that HQLAs held in excess of the total cash outflows of any Group entity are not considered as surplus liquidity at the overall Group level.

Net Cash Outflows

Net cash outflows are defined as the total expected cash outflows minus total expected cash inflows in the specified stress scenario for the subsequent 30 calendar days. Total expected cash outflows are calculated by multiplying the outstanding balances of various categories of liabilities and off-balance sheet commitments by the rates at which they are expected to run off or drawn down. Total expected cash inflows are calculated by multiplying the outstanding balances of various categories of contractual receivables by the rates at which they are expected to flow in under the stress scenario up to an aggregate cap of 75% of total expected cash outflows. All cash outflows and inflows are considered and disclosed for LCR reporting purposes.

Table 6: Disclosure Form on LCR during the quarter ended on 31/12/2017*

			"KWD '000's"
No.	**Statement**	**Value before implementing flow rates (average)****	**Value after implementing flow rates(21) (average)****
High Quality Liquid Assets (HQLA)			
1	Total HQLA (before amendments)	**1,260,583**	**1,238,988**
Cash Outflow:			
2	Retail deposits and small enterprises	1,804,531	237,657
3	Stable deposits	109,993	5,583
4	Less stable deposits	1,694,538	232,074
5	Unsecured wholesale funding, excluding deposits of small enterprises clients	1,461,438	941,479
6	Operating deposits	229	58
7	Non-operating deposits (other unsecured liabilities)	1,461,209	941,421
8	Secured funding	20,809	-
9	Other cash outflows, including:	495,649	361,106
10	Resulting from derivatives	337,217	342,326
11	Resulting from securities and commercial papers supported by assets (on the assumption of not being to re-finance)	-	-
12	Credit lines and binding liquidity	158,432	18,780
13	Possible future financing needs	971,854	49,329
14	Other contractual cash outflows	3,603	3,658
15	**Total cash outflows**	**4,757,884**	**1,593,229**
16	Secured lending transactions	-	-
17	Cash outflows resulting from regular loans	848,293	648,864
18	Other cash inflows	341,041	346,209
19	**Total cash inflows**	**1,189,334**	**995,073**
Liquidity Coverage Ratio (LCR)			
20	Total HQLA (after amendments)		**1,049,770**
21	Net cash outflows		**598,156**
22	LCR		**176%**

*Quarterly statement.
** (Simple Average) for all work days during the period for which the form is prepared.
21) Is the value after implementing haircut percentages of HQLA and cash outflow and inflow.