FitchRatings

Bank of London and The Middle East plc

Update

Key Rating Drivers

Bank of London and The Middle East plc's (BLME) Issuer Default Ratings (IDRs) reflect potential support from its parent, Kuwait's Boubyan Bank K.S.C.P. (BBY; A/Stable). BLME's IDRs are equalised with BBY's, which are in turn based on potential support from the Kuwaiti authorities', given its key role for the parent as a strategically important subsidiary that provides BBY with access to the highly developed UK market.

Fitch Ratings does not assign a Viability Rating to BLME due to the bank's high reliance on, and close integration with, BBY. We believe BLME's business is driven by, and related to, its parent; its franchise therefore cannot be assessed meaningfully in its own right.

Integral to Parent's Strategy: BLME is a key and integral part of the group, building BBY's private-banking and wealth-management offerings, mainly to group and broader Gulf Cooperation Council (GCC) clients. It is therefore key in executing BBY's strategic objectives. BLME accounted for about 7% of BBY's total assets at end-2022.

Close Integration: BLME's strategy and risk management are highly integrated with those of BBY. BLME's management has reporting lines to the parent in Kuwait. BBY's chief executive is BLME's chairperson, and four of BLME's 10-member board currently represent BBY.

Other Support Factors: The equalisation of BLME's ratings with those of BBY also considers the very high reputational risk that a default of BLME would cause to BBY's franchise in light of the close links between the two entities.

Ongoing Strategic Change: BLME provides wealth-management solutions to GCC clients, as well as real-estate finance and digital-banking products through its digital bank, Nomo. A strategic change was initiated when BBY took over, reflected through the launch of Nomo in 2021. In addition, BLME launched operations in Saudi Arabia in May 2023 through BLME Capital, which will provide major growth opportunities in real estate and wealth management.

Conservative Risk Profile: Risks associated with high concentrations are mitigated by appropriate risk control tools and, overall, the reasonably good quality of the largest exposures.

Deteriorating Asset Quality: The impaired financing ratio rose to 8.3% at end-2022 (end-2021: 3.4%) due to the migration of a few large real estate exposures, which will be restructured in 2023. The largest impaired financings are well covered, either by reserves or collateral.

High Costs Weigh on Profitability: BLME's 2022 pre-impairment profit was undermined by a 42% increase in operating costs from 2021 levels. The bank continued to build up its staff and marketing capabilities in line with the recent launch of Nomo and BLME Capital. Impairment charges rose by 7%, driving a GBP9million operating loss. We expect the bank to break even in 2023 on stronger net financing income and reducing operating expenses.

Strong Capitalisation: At end-2022, the bank's high 23% CET1 ratio was well above the minimum regulatory requirement. We expect capital ratios will reduce as the bank grows, but any capital needs will be addressed by BBY on an ongoing basis.

Concentrated but Stable Deposits: Customer deposits are the bank's main source of funding. The bank focuses on retail deposits sourced from the UK savings market to achieve granularity in the deposit base. BLME has ample liquidity, with a liquidity coverage ratio of 465% at end-2022.

Banks
Islamic Banks
United Kingdom

Ratings

Foreign Currency	
Long-Term IDR	A
Short-Term IDR	F1
Long-Term IDR (xgs)	BBB(xgs)
Short-Term IDR (xgs)	F2(xgs)
Shareholder Support Rating	a
Sovereign Risk (United Kingdom)	
Long-Term Foreign-Currency IDR	AA-
Long-Term Local-Currency IDR	AA-
Country Ceiling	AAA
Outlooks	
Long-Term Foreign-Currency IDR	Stable
Sovereign Long-Term Foreign-Currency IDR	Negative
Sovereign Long-Term Local-Currency IDR	Negative

Applicable Criteria

Bank Rating Criteria (September 2022)

Related Research

EM100 Banks Tracker - End-2022 (June 2023)

EMEA Islamic Banks Outlook 2023 (December 2022)

Fitch Affirms Boubyan Bank at 'A'; Stable Outlook (January 2023)

Boubyan Bank K.S.C.P. (February 2023)

Analysts

Redmond Ramsdale
+44 20 3530 1836
redmond.ramsdale@fitchratings.com

Jamal El Mellali
+44 20 3530 2763
jamal.elmellali@fitchratings.com

Rating Sensitivities

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

A downgrade of BBY's ratings would trigger a downgrade of BLME's. BLME's ratings would also be downgraded if Fitch views the propensity of BBY or the Kuwaiti authorities to support BLME as diminishing. This would most likely be the result of a reduction of BLME's strategic role for BBY, or its integration with BBY, or in BBY's ownership stake. However, this is unlikely in the near term.

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

BLME's IDRs could be upgraded if BBY's IDRs are upgraded.

Other Debt and Issuer Ratings

BLME's Long-Term (LT) IDR (xgs) is aligned with BBY's LT IDR (xgs). The Short-Term (ST) IDR (xgs) is in accordance with the LT IDR (xgs) and Fitch's short-term rating mapping.

Significant Changes from Last Review

XGS Ratings Assigned

Fitch assigned a Long-Term IDR (xgs) and a Short-Term IDR (xgs) to BLME on 2 May 2023. The ex-government support (xgs) ratings exclude assumptions of extraordinary government support from the underlying ratings.

Financials

Financial Statements

	31 Dec 22		31 De 21	31 Dec 20	31 Dec 19
	Year end (USDm) Audited - unqualified	Year end (GBPm) Audited - unqualified	Year end (GBPm) Audited - unqualified	Year end (GBPm) Audited - unqualified	Year end (GBPm) Audited - unqualified
Summary income statement					
Net financing & dividend income	43	36.0	31.7	31.4	31.0
Net fees and commissions	-1	-0.6	-1.8	-3.4	0.4
Other operating income	11	9.4	4.0	8.7	12.6
Total operating income	54	44.8	33.9	36.7	44.0
Operating costs	49	40.4	28.5	28.6	30.0
Pre-impairment operating profit	5	4.4	5.4	8.1	14.0
Financing & other impairment charges	16	13.4	12.5	7.5	1.7
Operating profit	-11	-9.0	-7.1	0.6	12.3
Other non-operating items (net)	0	0.0	-0.1	0.7	-2.4
Tax	-3	-2.2	-2.9	0.4	1.2
Net income	-8	-6.8	-4.3	0.9	8.7
Other comprehensive income	0	0.0	-0.2	0.0	0.9
Fitch comprehensive income	-8	-6.8	-4.5	0.9	9.6
Summary balance sheet					
Assets					
Gross financing	1,162	962.5	883.5	1,076.2	1,288.7
- Ow impaired	96	79.4	29.8	38.5	15.2
Financing loss allowances	17	14.1	15.4	15.3	8.8
Net financing	1,145	948.4	868.1	1,060.9	1,279.9
Interbank	545	451.7	479.2	339.6	23.5
Islamic derivatives	1	0.6	0.7	2.9	4.9
Other securities and earning assets	45	37.0	61.0	92.0	151.3
Total earning assets	1,735	1,437.7	1,409.0	1,495.4	1,459.6
Cash and due from banks	163	135.3	112.1	231.5	66.7
Other assets	48	39.4	27.8	16.5	22.3
Total assets	1,946	1,612.4	1,548.9	1,743.4	1,548.6
Liabilities					
Customer deposits	1,598	1,323.9	1,031.9	1,455.8	1,155.3
Interbank and other short-term funding	62	51.0	272.6	30.8	137.9
Other long-term funding	n.a.	n.a.	n.a.	n.a.	n.a.
Trading liabilities and Islamic derivatives	1	1.1	2.0	0.8	1.8
Total funding and Islamic derivatives	1,661	1,376.0	1,306.5	1,487.4	1,295.0
Other liabilities	16	13.5	12.7	21.7	20.1
Preference shares and hybrid capital	n.a.	n.a.	n.a.	n.a.	n.a.
Total equity	269	222.9	229.7	234.3	233.5
Total liabilities and equity	1,946	1,612.4	1,548.9	1,743.4	1,548.6
Exchange rate		USD1 = GBP0.828638	USD1 = GBP0.74438	USD1 = GBP0.745156	USD1 = GBP0.76211

Source: Fitch Ratings, Fitch Solutions, Bank of London and The Middle East plc

Key Ratios

	31 Dec 22	31 Dec 21	31 Dec 20	31 Dec 19
Ratios (annualised as appropriate)				
Profitability				
Operating profit/risk-weighted assets	-0.9	-0.8	0.0	0.8
Net financing income/average earning assets	2.5	2.2	2.1	2.4
Non-financing expense/gross revenue	90.4	84.3	77.9	68.2
Net Income/average equity	-3.0	-1.9	0.4	3.8
Asset quality				
Impaired financing ratio	8.3	3.4	3.6	1.2
Growth in gross financing	8.9	-17.9	-16.5	30.6
Financing loss allowances/impaired financing	17.8	51.7	39.7	57.9
Financing impairment charges/average gross financing	1.5	1.3	0.6	0.2
Capitalisation				
Common equity Tier 1 ratio	23.0	24.5	15.9	15.1
Fully loaded common equity Tier 1 ratio	n.a.	n.a.	n.a.	n.a.
Fitch Core Capital ratio	n.a.	n.a.	n.a.	n.a.
Tangible common equity/tangible assets	13.6	14.1	13.1	15.0
Basel leverage ratio	n.a.	n.a.	n.a.	n.a.
Net impaired financing/common equity Tier 1	29.3	6.3	9.9	2.9
Net impaired financing/Fitch Core Capital	n.a.	n.a.	n.a.	n.a.
Funding & liquidity				
Gross financing/customer deposits	72.7	85.6	73.9	111.6
Liquidity coverage ratio	465.0	194.0	n.a.	234.2
Customer deposits/total non-equity funding	96.3	79.1	97.9	89.3
Net stable funding ratio	n.a.	n.a.	n.a.	n.a.

Source; Fitch Ratings, Fitch Solutions, Bank of London and The Middle East plc

Support Assessment

Shareholder Support	
Shareholder IDR	A
Total Adjustments (notches)	0
Shareholder Support Rating	a
Shareholder ability to support	
Shareholder Rating	A/ Stable
Shareholder regulation	Equalised
Relative size	1 Notch
Country risks	Equalised
Shareholder propensity to support	
Role in group	Equalised
Reputational risk	Equalised
Integration	Equalised
Support record	Equalised
Subsidiary performance and prospects	1 Notch
Legal commitments	2+ Notches

The colours indicate the weighting of each KRD in the assessment.
Higher influence Moderate influence Lower influence

We believe BBY would have a strong propensity to support BLME due to BLME's key role in the group, and this has a higher influence on our assessment. BLME helps the parent in building its wealth-management and private banking franchise. BLME also offers digital banking services, benefitting from BBY's support, advanced technology, and expertise in Kuwait. BLME's strategic objectives are a continuation of BBY's own objectives and its franchise, business model and risk management are highly correlated with those of the parent. We also believe that a default of BLME would create a very high reputational risk for BBY's franchise given the close links between the two entities. This constitutes a strong incentive for BBY to support its subsidiary in case of need.

We believe the Kuwaiti authorities would not restrict support from BBY to BLME as a default of BLME could affect BBY's reputation, and given there are some links between BLME and Kuwait via the state's indirect stake in the bank through government-related entities.

Environmental, Social and Governance Considerations

FitchRatings **Bank of London and The Middle East plc**

Banks
Ratings Navigator

Credit-Relevant ESG Derivation

Bank of London and The Middle East plc has 1 ESG rating driver and 5 ESG potential rating drivers

- Bank of London and The Middle East plc has exposure to board independence and effectiveness; ownership concentration; protection of creditor/stakeholder rights; legal /compliance risks; business continuity; key person risk; related party transactions which, in combination with other factors, impacts the rating.
- Bank of London and The Middle East plc has exposure to compliance risks including fair lending practices, mis-selling, repossession/foreclosure practices, consumer data protection (data security) but this has very low impact on the rating.
- Bank of London and The Middle East plc has exposure to shift in social or consumer preferences as a result of an institution's social positions, or social and/or political disapproval of core banking practices but this has very low impact on the rating.
- Bank of London and The Middle East plc has exposure to operational implementation of strategy but this has very low impact on the rating.
- Bank of London and The Middle East plc has exposure to organizational structure; appropriateness relative to business model; opacity; intra-group dynamics; ownership but this has very low impact on the rating.
- Bank of London and The Middle East plc has exposure to quality and frequency of financial reporting and auditing processes but this has very low impact on the rating.

			Overall ESG Scale
key driver	0	issues	5
driver	1	issues	4
potential driver	5	issues	3
not a rating driver	3	issues	2
	5	issues	1

Environmental (E)

General Issues	E Score	Sector-Specific Issues	Reference	E Scale
GHG Emissions & Air Quality	1	n.a.	n.a.	5
Energy Management	1	n.a.	n.a.	4
Water & Wastewater Management	1	n.a.	n.a.	3
Waste & Hazardous Materials Management; Ecological Impacts	1	n.a.	n.a.	2
Exposure to Environmental Impacts	2	Impact of extreme weather events on assets and/or operations and corresponding risk appetite & management; catastrophe risk; credit concentrations	Business Profile (incl. Management & governance); Risk Profile; Asset Quality	1

How to Read This Page
ESG scores range from 1 to 5 based on a 15-level color gradation. Red (5) is most relevant and green (1) is least relevant.

The Environmental (E), Social (S) and Governance (G) tables break out the individual components of the scale. The right-hand box shows the aggregate E, S, or G score. General Issues are relevant across all markets with Sector-Specific Issues unique to a particular industry group. Scores are assigned to each sector-specific issue. These scores signify the credit-relevance of the sector-specific issues to the issuing entity's overall credit rating. The Reference box highlights the factor(s) within which the corresponding ESG issues are captured in Fitch's credit analysis.

The Credit-Relevant ESG Derivation table shows the overall ESG score. This score signifies the credit relevance of combined E, S and G issues to the entity's credit rating. The three columns to the left of the overall ESG score summarize the issuing entity's sub-component ESG scores. The box on the far left identifies some of the main ESG issues that are drivers or potential drivers of the issuing entity's credit rating (corresponding with scores of 3, 4 or 5) and provides a brief explanation for the score.

Classification of ESG issues has been developed from Fitch's sector ratings criteria. The General Issues and Sector-Specific Issues draw on the classification standards published by the United Nations Principles for Responsible Investing (PRI) and the Sustainability Accounting Standards Board (SASB).

Sector references in the scale definitions below refer to Sector as displayed in the Sector Details box on page 1 of the navigator.

Social (S)

General Issues	S Score	Sector-Specific Issues	Reference	S Scale
Human Rights, Community Relations, Access & Affordability	2	Services for underbanked and underserved communities: SME and community development programs; financial literacy programs	Business Profile (incl. Management & governance); Risk Profile	5
Customer Welfare - Fair Messaging, Privacy & Data Security	3	Compliance risks including fair lending practices, mis-selling, repossession/foreclosure practices, consumer data protection (data security)	Operating Environment; Business Profile (incl. Management & governance); Risk Profile	4
Labor Relations & Practices	2	Impact of labor negotiations, including board/employee compensation and composition	Business Profile (incl. Management & governance)	3
Employee Wellbeing	1	n.a.	n.a.	2
Exposure to Social Impacts	3	Shift in social or consumer preferences as a result of an institution's social positions, or social and/or political disapproval of core banking practices	Business Profile (incl. Management & governance); Financial Profile	1

Governance (G)

General Issues	G Score	Sector-Specific Issues	Reference	G Scale
Management Strategy	3	Operational implementation of strategy	Business Profile (incl. Management & governance)	5
Governance Structure	4	Board independence and effectiveness; ownership concentration; protection of creditor/stakeholder rights; legal /compliance risks; business continuity; key person risk; related party transactions	Business Profile (incl. Management & governance); Earnings & Profitability; Capitalisation & Leverage	4
Group Structure	3	Organizational structure; appropriateness relative to business model; opacity; intra-group dynamics; ownership	Business Profile (incl. Management & governance)	3
Financial Transparency	3	Quality and frequency of financial reporting and auditing processes	Business Profile (incl. Management & governance)	2
				1

CREDIT-RELEVANT ESG SCALE

How relevant are E, S and G issues to the overall credit rating?

5	Highly relevant, a key rating driver that has a significant impact on the rating on an individual basis. Equivalent to "higher" relative importance within Navigator.
4	Relevant to rating, not a key rating driver but has an impact on the rating in combination with other factors. Equivalent to "moderate" relative importance within Navigator.
3	Minimally relevant to rating, either very low impact or actively managed in a way that results in no impact on the entity rating. Equivalent to "lower" relative importance within Navigator.
2	Irrelevant to the entity rating but relevant to the sector.
1	Irrelevant to the entity rating and irrelevant to the sector.

Islamic banks need to ensure compliance of their entire operations and activities with sharia principles and rules. This entails additional costs, processes, disclosures, regulations, reporting and sharia audit. This results in a Governance Structure relevance score of ‘4’ instead of a typical ESG relevance score of ‘3’ for comparable conventional banks, which has a negative impact on the bank’s credit profile in combination with other factors.

In addition, Islamic banks have an Exposure to Social Impacts score of '3' instead of a typical ESG relevance score of '2' for comparable conventional banks, which reflects the sharia limitations embedded in Islamic banks' operations and obligations, although this has a minimal credit impact on the entities.

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.