



الوكالة الإسلامية الدولية للتصنيف
Islamic International Rating Agency

ECONOMIC & BANKING SECTOR OVERVIEW

Kingdom of Bahrain

June, 2022

BAHRAIN - ECONOMIC OUTLOOK

The Kingdom of Bahrain is one of the six member states of the Cooperation Council (“GCC”) states, which has a nominal GDP of about US\$39bn in 2021 (2020: US\$34bn). Housing a population of around 1.5mn, Bahrain is classified as a ‘high-income earning’ country as per the World Bank.

Bahrain’s economy and public finances have displayed a high degree of correlation to the oil and gas sector. Oil prices recovered to US\$71/barrel¹ in 2021 from the average lows of 2020 at about US\$42/barrel, while having hovered mostly over US\$100/ barrel YTD May 2, 2022². The Country’s economy posted 2.2% growth in 2021 (2020: -4.9%). Given that the oil-based economy witnessed marginal contraction in 2021, the rebound was mainly underpinned by non-oil based economy mostly in the transportation and communications sectors. While the global growth outlook for 2022 has been revised downward to 3.6% triggered by the ongoing conflict, Bahrain economy is expected to gradually gather pace at 3.3%³, which is slightly above its long-term growth potential, boosted by oil prices and continued recovery in non-oil economy as the pandemic pressure continues to fade.

With Bahraini Dinar (“BHD”) being officially pegged to the U.S. Dollar at US\$/BHD @ 0.376, the Country has been able to maintain price stability and growth as an oil-centric small economy, albeit gradually diversifying. The pegged currency allows for limited monetary policy transmission, largely following the monetary policy of the United States Federal Reserve (“Fed rate”) to preserve the peg. Mirroring the U.S. Fed rate, in March and May 2022 CBB raised the benchmark one-week deposit facility rate by 25bps and 75bps, respectively to 1.75%, in addition to increasing the overnight deposit and lending rates. Expectations of further policy rate hikes is on the anvil aligned to the U.S. interest rates movements in the remaining part of the year. While deflationary trends persisted through most part of 2021, pick-up in price pressures has been noted since Q4’21. Spill-over effects of global inflationary pressure due to the ongoing Russia-Ukraine conflict are most likely to be felt across the GCC region in the ongoing year.

After having registered external imbalance over the last few years, Bahrain experienced notable reversal in current account in 2021 posting surplus of 6.7% to GDP. This was supported by improvement in export prices and relatively lower outward remittances by workers. On the fiscal side, preliminary estimates indicate 23% Y-o-Y growth in revenues and 3% Y-o-Y lower total expenditures in 2021, translating into a fiscal deficit of about 11%⁴. Further, during Q4’21 Bahrain announced resumption of fiscal consolidation

Table 3: Bahrain Economic Snapshot

Figures as stated	2019	2020	2021
Population ('000)	1,484	1,472	1,504
Nominal GDP (US\$'bn)	38	34	39
GDP per capita (US\$) #	25,862	23,399	25,844
Real GDP Growth (%)	2.1	-4.9	2.2*
Oil-GDP Growth (%)	2.2	-0.1	-0.3
Non-oil GDP Growth (%)	2.1	-6.0	2.8
Average CPI (%)	1.0	-2.3	1.0
Current Account Balance (% of GDP)	-2.1	-9.3	6.7
Fiscal Balance (% of GDP)	-4.7	-13.0	-11.1 [^]
Overall Government Debt (% of GDP) @	103.6	132.0	128.5 [^]

(Source: Bahrain Government bond prospectus – Jan. 2021 & Mar. 2021, EDB, CBB; negative current and fiscal balance indicates deficit; @ gross, and inclusive of CBB’s Government claims and retail banks’ loans to Government; # Derived; ^ IMF regional economic outlook April 2022; * provisional)

¹ Source: EIA, Brent crude spot prices

² Averaged YTD until May 2, 2022: US\$101.8/barrel

³ Source: IMF – April 2022

⁴ Source: 11.1% as per IMF and about 11.4% as per IIRA’s calculation

program that was side-lined by the pandemic. As a result, VAT rate was announced to be doubled to 10% starting January 2022. While the fiscal deficit remains high due to continuing emergency spending; public finances may improve substantially in the ongoing year given that Bahrain's fiscal breakeven price is estimated at US\$127.5/barrels in 2022. Domestic government debt at end-2021 edged up 10.2% Y-o-Y with the issuance of local development bonds. In November 2021, the government also raised US\$2bn in two tranches (US\$1bn Sukuk and US\$1bn bond) with maturities in 2029 and 2034, respectively. Debt in relation to GDP is likely to remain elevated as the Country continues to draw more funds to meet its fiscal needs and service the yearly principal amortizations. While stabilizing and lowering debt gradually remains a key target under the fiscal balance program, there is need for clarity in terms of setting specific debt management strategy.

ISLAMIC RETAIL BANKING SECTOR - BAHRAIN

Contribution from financial sector in Bahrain has been strengthening over the years, having dominant share within the services over the last few years, and led by the Banking system. Retail banks in Bahrain account for about 45.7%⁶ of the overall banking sector assets at end-2021 (2020: 45.3%). This segment is highly competitive, having evolved over the years, and represented by 24 conventional and 6 Islamic banks.

With 14 Islamic Banks representing an asset base of US\$34.6bn as of end-2021 (2020: US\$31.6bn), the Country has the largest concentration of Islamic Financial Institutions. Share of Islamic banks in total banking sector assets is gradually growing, having stood at 15.9%⁷ at end-2021 (2020: 15.2%). During 2021, the IRB industry assets⁸ and deposits posted Y-o-Y growth of 10.9% and 15.0%, respectively (2020: 5.7%; 6.6%, respectively). The IRB segment's profitability improved in 2021 vis-a-vis 2020, and the segment remains adequately capitalized. Due to CBB forbearance measures being still in effect, overall sector's (including IRB) profitability metrics posted improvement vis-a-vis 2020. Asset quality trends also indicate favorable movement in 2021 vis-à-vis 2020 with improvement in IRB's gross impairment and provisioning coverage.

During Q1'20 the CBB issued several concessionary and forbearance measures for the banking sector in response to Covid-19. Since then, the CBB has extended the financing customers' payment deferrals four

Table 4: Key Financial Indicators - Banking and IRB Sector

Figures as stated	Q4'19	Q4'20	Q4'21*	Q4'19	Q4'20	Q4'21*
	Overall			IRB		
CAR (%)	19.4%	18.6%	18.6%	18.3%	20.3%	21.2%
Tier I CAR (%)	18.1%	17.3%	17.1%	15.7%	17.9%	19.7%
Gross Impairment (%)	4.8%	4.2%	3.2%	10.4%	6.5%	5.1%
Specific Provisions Coverage (%)	62%	68.6%	70.0%	36.7%	42.9%	55.3%
RoA (%)	1.1%	0.7%	1.1%	0.4%	0.2%	0.6%
RoE (%)	7.9%	2.6%	7.8%	4.7%	2.1%	7.0%
Liquid Assets to Total Assets (%)	25.5%	24.4%	26.5%	17.5%	17.8%	19.9%
Financings to Deposits (%)	71.5%	70.9%	69.9%	92.5%	79.7%	74.1%

(Source: CBB; IRB: Islamic Retail Banks; * provisional data)

⁵ Source: IMF Regional Economic Outlook April 2022

⁶ CBB Statistical Bulletin

⁷ CBB – Statistical Bulletin

⁸ Both adjusted for effect of consolidation

times⁹ until end-June 2022, subject to set conditions, and may likely be extended until the end of the ongoing year as the proposal was recently approved by the parliament in April 2022. IIRA remains cautious in this regard as the sector may witness reclassification of vulnerable exposures once the deferment period has passed; however, given that sufficient ECL provisions are in place mitigating threat of any substantial losses.

Banking sector in Bahrain is in the consolidation phase with merger negotiations of some banks underway. Further the sector is also gearing to address the climate related risks, for which CBB has issued guidance note in March 2022.

⁹ (Mar. 2020 – Sept. 2020), (Sept. 2020 – Dec. 2020), (Jan. 2021 – June 2021), (June 2021 – Dec. 2021), (Jan. 2022 – June 2022)



الوكالة الإسلامية الدولية للتصنيف
Islamic International Rating Agency

About the ratings: IIRA's sovereign ratings were initiated under the Technical Assistance Agreement with Islamic Development Bank (IsDB) and initial fee was provided under the said agreement. The ratings have been independently assessed by IIRA, with no liability on the part of IsDB.

Disclaimer: The information contained herein is obtained by IIRA from sources believed to be accurate and reliable. IIRA does not audit or verify the truth or accuracy of any such information. As a result, the information herein is provided "as is" without any representation or warranty of any kind. IIRA, the analysts involved in the rating process and members of its rating committee do not have any conflict of interest relating to the rating(s) mentioned. Rating is an opinion and not a warranty of a rated entity's current or future ability to meet contractual obligations, nor is it a recommendation to buy, sell or hold any security.