
IIRA Maintains Ratings of Al Baraka Islamic Bank B.S.C. (c)

Manama, June 19, 2022 – Islamic International Rating Agency (“IIRA”) has reaffirmed the international scale ratings of Al Baraka Islamic Bank B.S.C. (c) (“ABIB” or “the Bank”) at BB / A3 (Double B / A Three), while also maintaining the national scale ratings at BBB+ (bh) / A3 (bh) (Triple B Plus / A Three). Outlook on the assigned ratings is ‘Stable’. ABIB operates as a locally incorporated Islamic retail bank in the Kingdom of Bahrain (“Bahrain”), and has overseas operations through its majority-held subsidiary in Islamic Republic of Pakistan (“Pakistan”) (Al Baraka Bank (Pakistan) Limited (“ABPL”)), which exposes the Bank to the country risk in both jurisdictions.

Following the pandemic induced global downturn in 2020, both countries posted growth in 2021 with general improvement in economic indicators. Oil prices ranging around plus US\$100/barrel so far in the ongoing year may continue to support the economic growth in Bahrain. On the other hand, external pressures have mounted in Pakistan due to higher international commodities prices, causing headwinds in the form of tightening policy rates, domestic inflationary pressure, and continuing slide in Pakistani Rupee (“PKR”) value against the USD. Pakistan is also facing fiscal constraints and heightened external vulnerabilities in terms of offshore debt refinancing, thereby raising financial system instability risk. For the Bank, these challenges are largely offset by the prognosis of growth in Bahrain, which is relatively insulated from the presently ongoing Russia-Ukraine war and given that there are no major external payment obligations on the Pakistan based subsidiary. As such, the outlook on the international scale rating has been revised to ‘Stable’ from ‘Negative’. Nonetheless, downside risk from global stagflation may likely weigh on the potential of local banking sector in both jurisdictions.

The Bank continued its growth trajectory, albeit the contribution of the subsidiary to overall expansion was muted in USD terms, due to currency weakness. Steady improvement in core profitability and lower asset impairment charges shored up the overall profitability in 2021. While margin pressure is inevitable in a high policy rate environment, expectation of new business volumes and growth in fee-based services may buffer the earnings in the ongoing year. Adverse currency fluctuation at ABPL may dampen the Bank’s income aggregation in the near term.

Consolidated capitalization ratios were reported strong, albeit headroom in total equity position of ABIB and CET ratio requirements remains narrow. The subsidiary Bank has been granted extension by the regulator for converting into share capital, the capital support fund extended by ABIB to meet local capital requirements, until end-June 2022. The Bank is in the process of reinforcing capital in both jurisdictions, which cuts potential growth prospects in the current year. Portfolio quality is noted to have improved on a timeline. Liquidity buffer in both jurisdictions is adequate, although reliance on institutional funding remains noteworthy.

Al Baraka Banking Group’s (“ABG” or “the Group”) majority ownership of ABIB provides support to the ratings assessment of the Bank. Despite the change of regulatory license held by ABG, from erstwhile ‘wholesale banking license’ to that of an ‘investment firm’, IIRA expects the Group financial support and operational oversight to continue for the Bank and ABPL.

IIRA has assessed ABIB's fiduciary score in the '71 – 75' range, reflecting adequate fiduciary standards, wherein the rights of various stakeholders are considered to be adequately protected. Asset manager quality score has been uplifted to the higher band vis-à-vis prior review due to improvement in Mudarib's efficiency and overall asset quality. Broad improvement in other components of fiduciary score has also been noted in terms of deployment of advanced systems by control functions, and a sustained high level of transparency. Regulatory environment in both jurisdictions of ABIB's operations support strong governance practices and adequate disclosures. Governance infrastructure at ABIB reflects both the regulatory requirements and ABG's secondary oversight. The Bank remained compliant with Shari'a principles, also supported by the Group's Shari'a Board oversight. Well-versed members at the Shari'a Board, adequate Shari'a controls and disclosures along with external Shari'a overview, and supervision at the Group level strengthen the Bank's Shari'a governance framework.

For further information on this rating announcement, please contact IIRA at iira@iirating.com.