الوكالة الإسلامية الدولية للتصنيف
Islamic International Rating Agency

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

Manama, June 22, 2023 – 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). The national scale ratings on the Bank remain unchanged at BBB+ (bh) / A3 (bh) (Triple B Plus /A Three). Outlook on the assigned ratings is 'Stable'. ABIB is an Islamic retail bank incorporated in the Kingdom of Bahrain ("Bahrain") and licensed by the Central Bank of Bahrain ("CBB"). The Bank also conducts overseas operations through its majority-held subsidiary in Islamic Republic of Pakistan ("Pakistan") (Al Baraka Bank (Pakistan) Limited ("ABPL")).

The assigned ratings consider Al Baraka Group's ("ABG" or "the Group") majority ownership in the Bank, which has demonstrated timely financial support in the past. Despite license change, IIRA expects the Group financial support and operational oversight to continue for both Bank and ABPL.

High oil price environment remained supportive of growth trends in Bahrain in 2022. However, Pakistan's economy suffered multiple setbacks last year due to the floods with repercussions on the economy, most prominently on agricultural output in addition to local industrial and service sectors, exacerbated by supply-chain disruptions amidst lingering political uncertainty. While Bahrain's economic activity may continue to benefit from existing, albeit moderate oil price levels, Pakistan economy is likely to continue to face headwinds, with elevated external vulnerabilities in the form of external financing and liquidity pressure, high commodity prices, high inflation despite tightening policy rates, continuing slide in Pakistani Rupee ("PKR") value against the USD and decline in reserves. Constrained global trade flow and inflationary pressure may likely weigh on the potential of local banking sector in both jurisdictions. However, given that there are no major external payment obligations on the Pakistan based subsidiary, provides comfort for ABIB.

Downward pressure on PKR led to slight contraction in the Bank's assets in USD terms last year and continuing into Q1'23, which has also contracted the subsidiary's contribution to ABIB. Higher margin income, continued cost rationalization and lower asset impairment charges boosted overall profitability last year. However, amidst high policy rates and expectation of subdued new business generation, core earnings are likely to be constrained in the ongoing year, which combined with PKR weakness may constrain the Bank's income aggregation.

As anticipated, the Bank converted part of its additional perpetual Tier 1 capital into equity, thereby raising the Bank's paid-up capital and uplifting CET 1 ratio during 2022. ABIB's consolidated and solo capitalization ratios remained strong. However, CBB's minimum equity requirement (in absolute terms) was breached in Mar'23. The Bank is considering various options to reinforce capital to meet the regulatory requirement. Further, ABPL's regulatory capital comprises USD denominated deposits placed by ABIB, with pending directives from the SBP to convert to share capital although an extension until June 2023 is in effect. In the absence of alternate capital plans being effected and resultant conversion, the Bank's exposure to PKR may stand enhanced by a further US$9mn.

Portfolio quality is noted to have improved on a timeline. IIRA maintains a cautious outlook on emerging asset quality trends for any further potential increase in non-performance, although the Bank has set aside sufficient provisions. Liquidity indicators point to sufficient capacity to make liquidity available as needed, in both jurisdictions.

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. Both ABIB and ABPL benefit from a robust regulatory environment that supports strong governance practices in addition to ABG's secondary oversight. ABIB's financial and governance-related disclosures are deemed satisfactory despite being an unlisted entity. The control framework at ABIB remains sound with well-defined reporting lines. Risk management framework is comprehensive. Tools deployed are at par with international banking standards and are continually upgraded. The Bank is still in the early stages of embedding ESG related objectives within its underwriting mechanism; however, IIRA expects gradual scale up in this regard, driven by regulatory developments and believes that current practices do not constitute a risk to the Bank's creditworthiness.

Shari'a governance framework is deemed strong, also supported by the Group's Shari'a Board oversight. Utilization of structured products, adequate Shari'a controls and disclosures along with external Shari'a audit review being conducted regularly, are notable strengths.

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