



IIRA Announces its First Ever Ratings in Iraq; Assigns Investment Grade Ratings to Asia AlIraq Islamic Bank on the National Scale

Manama, September 20, 2021 – Islamic International Rating Agency (“IIRA”) has assigned local and foreign currency ratings to Asia AlIraq Islamic Bank for Investment and Finance (“Asia” or “the Bank”) both at B/B (Single B / Single B) on the international scale, with a ‘Stable’ outlook, and taking into consideration the sovereign risk assessment of the Republic of Iraq (“Iraq” or “the Country”). The sovereign ratings assessment gives due consideration to the Country’s significant reserves of natural resources, still moderate external indebtedness in relation to GDP, and coverage through foreign currency reserves on the one hand, and sizable infrastructure building requirements, and political and social strain due to unemployment, on the other. High hydrocarbon dependence caused significant contraction in the economy in 2020, accompanied by deficits on both, the fiscal and external account, marking a deviation from surpluses in prior years, and causing the currency to depreciate sharply in late 2020. With steady recovery in oil prices and waning effects of global recession, Iraqi economy is expected to rebound in 2021.

Domestic economy remains under banked and adverse effects of the pandemic and public protests translated into banking sector slowdown last year, which necessitated temporary forbearance measures by the Central Bank of Iraq (“CBI”). Downside for the sector exists in the form of elevated credit segment concentration and high non-performance amidst prevailing macroeconomic situation. On a positive note, ongoing reforms in the banking sector may strengthen the system-wide governance and control infrastructure, with significant room available for growth in an improving economic and investment climate.

IIRA has also assigned national scale ratings of BBB (iq) / A3 (iq) (Triple B (iq) / Single A Three (iq)) to the Bank, with a ‘Stable’ outlook. Given a fairly short operating track history, the Bank is gradually developing its national footprint. Intense competition is reflected in slow deposit growth also lagging the industry. Although still evolving, Asia’s present non-shareholder funding profile exhibits reliance on wholesale sources and large accounts concentration. On a similar note the banking book of Asia is also limited both in absolute terms and in relation to assets and equity of the Bank, leaving substantial unutilized liquidity. Outstanding SME and relatively vulnerable sector exposures in Asia’s financing portfolio pose credit risk, albeit the delinquency experience so far is noted to be manageable in the light of underlying government guarantees. Relatively low share of financings in relation to assets further contains the risk on the balance sheet.

In line with industry trends, the Bank’s profitability is primarily driven by ancillary income and growth in unfunded business. Steady pace in banking operations and business growth may further cultivate margin income stream over the coming years. Asia posted positive bottom-line within one year of commencement of operations, despite elevated asset charge-offs in 2020. Barring the effect of the one-

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off charges as noted in interim periods of 2021, downside risks to profitability in the form of continued provisions against potential asset losses may undermine the Bank's internal capital generation in the near-term; however, assuming continued steady growth, the Bank's core profit potential appears intact.

The Bank has low leverage with growth primarily funded by equity and capital adequacy indicators are yet high. Further capital reinforcement is on the anvil this year to comply with regulatory thresholds. Overall sound asset quality and excess risk buffers underline the currently low; although yet to evolve risk profile of the Bank and as such support the investment grade rating assigned to the Bank. Shareholder profile exhibits fragmented private individual ownerships, constraining potential for sponsor support in the future if required.

IIRA has assessed Asia's fiduciary score in the '61 – 65' range, reflecting adequate fiduciary standards, wherein the rights of various stakeholders are considered to be adequately protected. Although compliant with CBI's guidelines, the Bank may strengthen corporate governance framework and internal controls to align with international best practices. In addition to corporate governance guide, the CBI has issued also specialized guidelines and regulatory framework for Islamic banks in the Country. Operations of the Bank are well- supported by its Shari'a governance infrastructure.

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

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