الوكالة الإسلامية الدولية للتصنيف
Islamic International Rating Agency

IIRA revises Trust Bank's Ratings

Manama, November 02, 2023 – Islamic International Rating Agency ("IIRA") has lowered the local and foreign currency ratings assigned to Trust International Islamic Bank ("TIIB" or "the Bank") to 'B-/B' (Single B Minus / Single B) from 'B/B' (Single B / Single B) on the international scale while also revising its national scale ratings to 'BBB- (iq) / A3 (iq)' (Triple B (iq) Minus/ Single A Three (iq)) from 'BBB+ (iq) / A3 (iq)' (Triple B (iq) Plus/ Single A Three (iq). Outlook on the assigned ratings is 'Negative'.

The downgrade has been triggered by the sanctions placed on the Bank, restricting it from undertaking USD denominated transactions, by the US Treasury Department and the Federal Reserve Bank of New York. This is expected to lead to a contraction in business volumes and in particular for trade finance business, to result in sharp decline in fee & commission income, which has been the main source of revenue for the Bank.

After significant GDP growth in the past two years, economic activity in Iraq is estimated to slowdown during 2023 with reduction in average oil prices, despite the recent rally. Expansionary fiscal stance in the current year may also deplete the oil windfall, thereby putting pressure on public finances, however, economic activity may continue to be driven by fiscal stimulus and lead to opportunities for the banking sector. Local banking sector remains underdeveloped with low financial inclusion. The recent restrictions placed by Federal Reserve on several Iraqi banks, for potential evasion of sanctions imposed on countries including Syria, Lebanon and Iran, highlights the heightened vigilance that the domestic financial system is under. Currently, of over 70 private banks in the Country, just under a third (although limited so far, in terms of their contribution to the financial system) are facing restrictions on USD transactions inclusive of the Trust Bank.

In H1'2023, 70% growth was noted in the financing portfolio of TIIB; yet allocation to financings overall remained low at 15.4% (2022: 8.7%) of assets. There was a marked increase in NPFs during 2022 mainly related to repercussions of Covid-19, although gross impairment ratio eased during H1'2023 with focus on collections. At 0.17%, net impairment to assets denotes decline vis-a-vis YE2022 of 0.27% and relatively low net non-performance. However, recent increase in financing portfolio and slowdown in GDP growth in Iraq may pose risk to asset quality going forward.

After growing over 27% in 2022, Trust Bank's non-shareholder funds depicted 14.3% decline in 2023, on account of withdrawal of some corporate deposits, since the bank ceased its dealings in USD. On the other hand, the Bank has launched new deposit accounts for retail customers which may support the building of a more stable funding profile going forward. With LCR and NSFR at 425.2% and 177.1% respectively as of June 2023, liquidity buffers are strong.

At the end of June 2023, CAR and the tier-1 ratio reduced to 136.0% and 129.4% respectively, with 74.0% increase in risk- weighted assets and 4.8% decrease in regulatory capital, the former due to sharp increase in financing portfolio and the latter due to regulatory amendments to the calculation. Despite this decline, the capital adequacy ratio of the Bank is substantially above the regulatory minimum of 12% and is forecasted to remain significantly in excess vis-a-vis expected low growth in the medium-term. An unfavorable outlook for profitability follows the CBI ban for Trust to participate in foreign currency auctions, which could lead to modest erosion in buffers. Capitalization profile derives strength from Trust's balance sheet, given the large quantum of liquid assets, and limited deployment in risk assets.

Trust Bank registered consolidated net loss of IQD0.3bn in 2022, as against IQD2.1bn net profit during 2021, due mainly to sharp rise in provisioning expenses. In H1'23, net loss was IQD0.8bn as opposed to IQD15bn net earnings for H1'22 with revenue base negatively impacted from lower fee & commissions income as well as the reversal of FCY income, due to loss from IQD appreciation. In the same period, net earnings adjusted for the FCY losses and provisioning charges also depicted worsening, partly due to the Bank's withdrawal from foreign currency auctions. Going forward, the profitability prospects are considered to be notably depressed, unless the sanctions on the Bank for USD currency auctions are lifted, as both FCY auction revenue and LG fees are likely to significantly contract and pressure the revenue stream of the Bank.

The Bank's overall fiduciary score was revised to '61-65' range due to the changes in the sub-scores for Asset Manager Quality and Corporate Governance as a reflection of compliance issues as evidenced by the sanctions of the US Treasury Department and the Federal Reserve Bank of New York. On the Board level, the appointment of three female board members is noted positively. There was no major change in the Bank's Shari'a governance framework, which is in line with local regulations.

On the ESG front, the Bank implements its social responsibility efforts within the context of Social Responsibility Policy whereby it has been participating in community-based initiatives fund (TAMKEEN) through monthly subscription fees to support humanitarian, environmental, and cultural initiatives, in addition to supporting employment generation. Trust Bank has begun to transition to renewable energy sources, in order to save costs, minimize carbon emissions and reduce electricity load with provision of most appropriate renewable and solar power systems. These systems have been installed in three of the Bank's branches. We have however not seen any traction in terms of greenification of the portfolio, given the absence of specific directives to this effect. The present degree of emphasis on incorporation of climate risk related changes in the bank's policies and procedures has not impacted assigned credit ratings in any way.

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