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Ratings

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Sharjah Islamic Bank

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Sharjah Islamic Bank

Ratings Score Snapshot

Issuer Credit Rating
A-/Stable/A-2

SACP: bbb- → **Support: +3** → **Additional factors: 0**

Anchor	bbb-	
Business position	Moderate	-1
Capital and earnings	Strong	+1
Risk position	Adequate	0
Funding	Adequate	0
Liquidity	Adequate	
CRA adjustment		0

ALAC support	0
GRE support	0
Group support	0
Sovereign support	+3

Issuer credit rating
A-/Stable/A-2

ALAC--Additional loss-absorbing capacity. CRA--Comparable ratings analysis. GRE--Government-related entity. ICR--Issuer credit rating. SACP--Stand-alone credit profile.

Credit Highlights

Overview	
Key strengths	**Key risks**
Strong capitalization.	Sizable lending exposure to the real estate and construction sectors.
Strong relationships with the government of Sharjah.	Limited geographic diversification.
High likelihood of extraordinary support.	High single-name concentrations.

We expect SIB's asset quality to improve over the next 12 months as exposures exit the cure period. We understand that Sharjah Islamic Bank (SIB) has reached settlement agreements with a handful of its problematic borrowers. As a result, we expect the share of stage 3 exposures in gross financings to decline toward 5% from 6.2% on March 31, 2023, as the cure period for these financings elapses.

SIB's capitalization will likely remain strong, with a risk-adjusted capital (RAC) ratio of 10.5%-11.0% over the next 18-24 months. This represents a further decline from 11.1% observed at year-end 2022 and is driven by projected growth in financing to the private sector as well as the recent increase in dividends per share to 10 fils (United Arab Emirates [UAE] dirham 0.1)--although still below 50% of profits. We expect higher profitability--including our forecast of net income margin of 30 basis points (bps)-40 bps higher in 2023-2024 than 2021-2022--though we believe that this will only partially offset the increase in risk-weighted assets.

We believe that SIB's recent expansion into retail will marginally affect its business profile, but may improve the diversity of its funding sources. In 2023, SIB introduced a retail offering, including a range of deposit and lending products. We believe that these initiatives will primarily contribute to SIB's funding profile, diversifying its tenor and single-name concentrations. However, cross-selling opportunities on the lending side appear more remote.

Outlook

The stable outlook reflects our view that the bank's creditworthiness will continue to benefit from strong capitalization and exposure to the Sharjah government and its related entities over the next 18-24 months.

Upside scenario

A positive rating action is remote in the next 18-24 months, since it would require SIB to materially strengthen both its franchise and capitalization, with the RAC ratio sustainably exceeding 15%. Alternatively, it would require a material improvement in the already-strong creditworthiness of the UAE government.

Downside scenario

We could consider a negative rating action if we observed a deterioration of asset quality or weaker capitalization than expected. This would be signaled by the RAC ratio dropping below 10%, which could come from faster-than-expected growth. We could also take a negative rating action if we see a material deterioration in the creditworthiness of the Sharjah government, the bank's largest counterparty, or if we consider SIB's systemic importance to have declined.

Key Metrics

Sharjah Islamic Bank--Key ratios and forecasts

	--Fiscal year ended Dec. 31--				
(%)	**2021a**	**2022a**	**2023f**	**2024f**	**2025f**
Growth in operating revenue	12.6	12.8	14.1-17.3	(0.0)-(0.1)	5.4-6.6
Growth in customer loans	-0.7	6.2	7.2-8.8	6.3-7.7	6.3-7.7
Growth in total assets	2.5	7.6	6.3-7.7	5.9-7.2	5.9-7.2
Net interest income/average earning assets (NIM)	2.3	2.4	2.7-2.9	2.5-2.7	2.5-2.7
Cost to income ratio	41.1	38.6	34.4-36.2	36.2-38.0	35.8-37.7
Return on average common equity	8.8	11.2	13.4-14.9	11.0-12.2	11.0-12.2
Return on assets	0.9	1.1	1.2-1.5	1.0-1.2	1.0-1.2
New loan loss provisions/average customer loans	0.8	1.0	1.0-1.1	0.9-1.0	0.9-1.0
Gross nonperforming assets/customer loans	4.8	6.0	4.1-4.5	4.3-4.8	4.3-4.7
Net charge-offs/average customer loans	0.4	0.2	0.3-0.3	0.3-0.3	0.3-0.3
Risk-adjusted capital ratio	13.1	11.1	10.7-11.3	10.6-11.1	10.5-11.0

All figures are S&P Global Ratings-adjusted. a--Actual. f--Forecast. NIM--Net interest margin.

Anchor: 'bbb-' For Banks Operating Only In The UAE

The United Arab Emirates (UAE) has a wealthy economy with strong fiscal and external positions. We expect economic activity in the UAE will slow in 2023 due to OPEC-agreed oil production cuts and deceleration in the non-oil sector on the back of higher interest rates. This, in turn, will lead to lower credit demand and growth. We expect problem loans to increase slightly in 2023 due to the slowdown. Combined with higher interest rates, this could increase problem loans in sectors such as construction and trade, as well as for some small and midsize enterprises that operate on thin margins. Nonetheless, we believe that a still-supportive domestic economy will help contain new nonperforming loans (NPLs). In addition, banks have proactively booked precautionary provisions over the past couple of years, which will help them to weather the challenges. We project that the banking sector's Stage 3 loans will stabilize at 5.8%-6.2% of systemwide loans in 2023-2024, compared with 5.5% at the end of 2022. Nevertheless, structural weaknesses persist, including high exposure to cyclical sectors, high single-name concentration, and exposure to some struggling GREs.

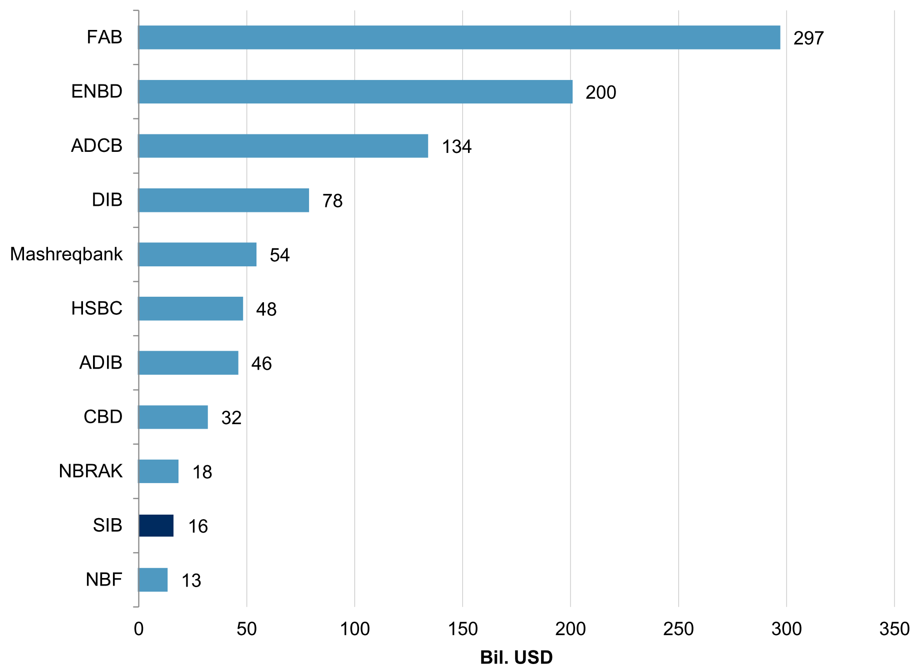
UAE's inclusion on the Financial Action Task Force's grey list in 2022 had a limited impact on banks' business or credit profiles. The Central Bank of the UAE has implemented directives and initiatives to ensure transparency of financial transactions and compliance with anti-money-laundering and counter financing of terrorism in the country, which we see as a positive step. Although the grey listing might increase the cost of external debt, we believe that UAE banks have ample margins to withstand this. We expect higher interest rates will support banks' performance. While banks will face greater pressure on funding costs, we believe that higher policy rates will facilitate wider margins for UAE banks. We expect the cost of risk to increase only slightly, so we think that banks' profitability will continue to improve. In our view, UAE banks enjoy sound funding profiles, with stable deposits from public-sector and government entities providing more than a quarter of total deposits. Moreover, banks remain in a net external asset position, and we don't expect that to change over the next 12-24 months.

Business Position: A Small Financial Institution With An Entrenched Niche

SIB is a small institution in the UAE market, with total assets representing around 1.6% of the systemwide total (see chart 1). However, it ranks fourth among local Islamic banks with a share of around 7%-8% in the UAE Islamic market at year-end 2022 and has the role of the flagship financial institution in the emirate of Sharjah. The government owns 37.5% of SIB and the bank draws around 60% of its revenue from business in Sharjah.

Chart 1

SIB is a smaller financial institution in the UAE
Largest UAE banks by assets, year end 2022



Source: S&P Global Ratings.

Lending to the Sharjah government and GREs will remain key exposures. Exposure to the bank's major shareholders and other related parties (mostly various government vehicles) stands around 30% of SIB's financings. We believe that the bank will continue to lend to the emirate and its GREs, further linking its intrinsic credit quality with those of the Sharjah government.

More recently, SIB has been expanding into retail by offering lucrative rates on longer-term deposits and cash back on credit cards. We believe that these efforts will help SIB to refinance its April 2023 bond maturity, potentially at cheaper rates. However, we will we continue to observe how the bank progresses in cross-selling products to its new client base and the impact of these activities its business profile.

Capital And Earnings: Improving Profitability While Capital Levels Gradually Decline

We see capitalization as a positive rating factor for SIB. This reflects our expectation that the bank's projected RAC ratio (before concentration adjustments) will remain at 10.5%-11.1% over the next 12-24 months. Specifically, we expect that:

- SIB will continue expanding its financing portfolio by 7% per year over 2023-2025, broadly in line with market average.
- The intermediation margins will further improve in 2023 to 2.7%-2.8%, but will gradually revert to 2.6% owing to our expectations for a rate reversal.
- SIB will either refinance on roll over the SIB Tier 1 Sukuk callable in mid-2025. There are, however, no firm plans to do that at this stage.
- SIB will maintain its recently increased dividend payout at 10 fils (AED 0.1) per share.
- The cost of risk will likely stay at about 100 bps in line with historical levels.

Based on our calculations, SIB's three-year average earnings buffer is about 70 bps, which indicates good capacity for earnings to cover expected losses over a complete economic cycle. We consider the bank's quality of capital to be satisfactory--hybrids account for around a quarter of total adjusted capital (TAC) at year-end 2022. Our forecasts exclude any materialization of concentration risk or any escalation in geopolitical risk in the region, which could lead to higher pressure on the UAE economy.

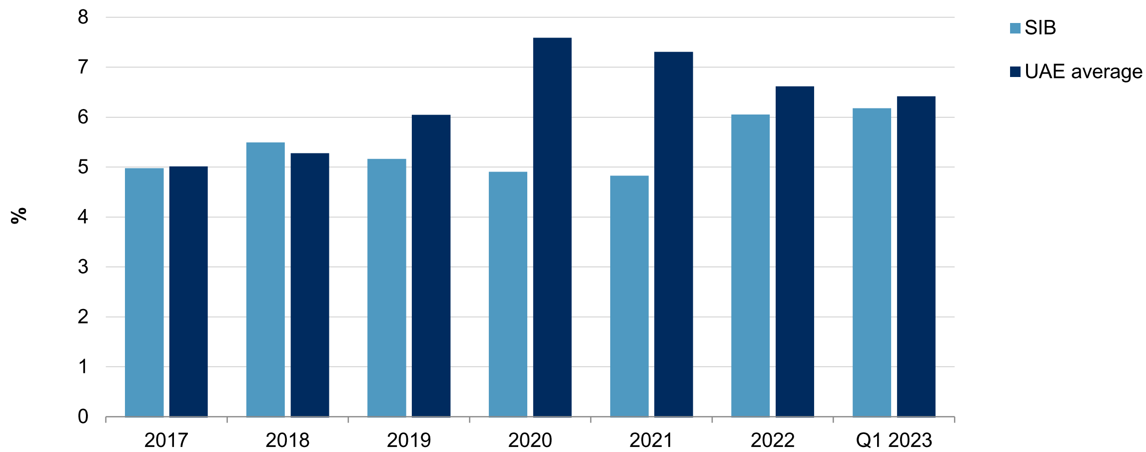
Risk Position: Asset Quality Commensurate With The Sector Average

Similar to other GCC banks, a key source of risk for SIB lies in high single-party concentration. The 20-largest funded and unfunded corporate gross credit exposures represented 19.8% of the bank's loan book as of year-end 2022 (excluding those to the government of Sharjah and its GREs). Similar to its peers, SIB exhibits high real estate and construction exposures. At year-end 2022, financings to these sectors comprised about 20% of the financings book, similar to the UAE banking industry average. This is further inflated by the bank's exposure to high-net-worth individuals, which is frequently linked to underlying income-generating real estate risks.

SIB's stock of problematic financings (Stage 3, as per IFRS 9) as a share of total financings has historically been commensurate with the systemwide average. At year-end 2022, Stage 3 financings accounted for 6.0% of total financings, an uncharacteristic deterioration relative to the industry average, which we estimate at about 5.6% for large domestic banks. However, we expect this ratio will improve to below 5% over 2023 on the back of restructurings exiting cool-off periods, which will also improve coverage ratios.

Chart 2

SIB's asset quality is commensurate with system average
Share of non-performing loans to total gross loans



Q1--Quarter. Source: S&P Global Ratings.

SIB's stand-alone credit quality remains closely linked to that of the government of Sharjah. With 38% of its financing book being to government departments and authorities (mostly the government of Sharjah), SIB's credit quality is tightly linked to that of the government of Sharjah. Any deterioration in the government's financial profile will likely strain the bank's stand-alone credit profile.

Funding And Liquidity: Replacing Wholesale Funding With Retail Deposits

SIB's funding profile is in line with its domestic peers. The bank funds itself predominantly from domestic customer deposits. As of Dec. 31, 2022, SIB's loan-to-deposit ratio stood at 77.5% and the ratio of stable funding resources to funding needs was a healthy 106%, according to our calculations. SIB enjoys steady access to deposits from the government of Sharjah and its cash-rich related entities, thanks to its privileged relationship. Like most banks in the Gulf Cooperation Council, SIB exhibits funding concentrations. Its ratio of top-20 depositors to total deposits remained high at 37% at year-end 2022, and mainly comprised deposits from government and public-sector entities. More recently, however, the bank has been trying to attract retail deposits, capping maximum amounts under its new offering at AED100 million per person in a bid to replace its sukuk maturing in April 2023 with more granular--and possibly cheaper--funding.

The bank has a relatively liquid balance sheet. Broad liquid assets covered short-term wholesale funding needs by a healthy 1.6x and net broad liquid assets covered 11% of short-term customer deposits as of December 2022. We note, however, that SIB managed to increase the tenor of its repurchase agreement (repo) facilities over 2022, reducing immediate liquidity pressures.

Support: Three Notches Of Uplift For Government Support

The issuer credit rating on SIB is three notches higher than its stand-alone credit profile, reflecting our view of a high likelihood of extraordinary government support for SIB if needed. This is in line with the bank's high systemic importance in the UAE. SIB is the fourth-largest Islamic bank in the UAE, with a market share of 7%-8% in terms of Islamic loans and deposits. The assessment also reflects the bank's strong relationship with the government of Sharjah, which owns 37.6% of SIB. We also consider the UAE authorities as highly supportive toward their banking system, with a strong track record of support provision.

Additional Rating Factors

No additional factors affect the ratings on SIB.

Environmental, Social, And Governance

ESG Credit Indicators

E-1	**E-2**	E-3	E-4	E-5	S-1	**S-2**	S-3	S-4	S-5	G-1	**G-2**	G-3	G-4	G-5

ESG credit indicators provide additional disclosure and transparency at the entity level and reflect S&P Global Ratings' opinion of the influence that environmental, social, and governance factors have on our credit rating analysis. They are not a sustainability rating or an S&P Global Ratings ESG Evaluation. The extent of the influence of these factors is reflected on an alphanumerical 1-5 scale where 1 = positive, 2 = neutral, 3 = moderately negative, 4 = negative, and 5 = very negative. For more information, see our commentary "ESG Credit Indicators: Definition And Applications," published Oct. 13, 2021.

We believe environmental, social, and governance (ESG) credit factors influence SIB's credit quality to a similar extent as industry and country peers. Although we estimate that the bank has relatively limited direct lending to sectors exposed to energy transition risk, the indirect exposure (via the overall dependence of the UAE economy on hydrocarbons) is higher. Social risks are not significantly different from those of its industry peers. Sharjah's government directly and indirectly owns 37.5% of the bank, which helps SIB maintain key account relationships with the Sharjah government and GREs. That said, we believe the ownership structure has not resulted in any governance weakness. In the past few years, SIB has not been involved in any material reputational controversies, has not experienced any incidents related to noncompliance with laws and regulations, and has not been subject to any significant legal or regulatory fines or settlements. Finally, we believe that bank regulation in the UAE is less focused on consumer protection than in more developed economies, meaning SIB's exposure to misselling penalties or other retail conduct risks is rather limited.

Key Statistics

Table 1

Sharjah Islamic Bank--Key figures

	--Year-ended Dec. 31--				
(Mil. AED)	**2023***	**2022**	**2021**	**2020**	**2019**
Adjusted assets	60,185.0	59,060.9	54,956.8	53,600.8	46,390.5
Customer loans (gross)	32,024.8	32,208.9	30,340.3	30,556.4	26,261.3
Adjusted common equity	5,880.8	5,689.7	5,559.2	5,405.6	5,389.8
Operating revenues	478.7	1,584.2	1,404.5	1,247.4	1,219.9
Noninterest expenses	156.1	610.8	576.8	561.5	585.4
Core earnings	227.9	659.7	583.2	430.1	537.7

*Data as of March 31. AED--UAE dirham.

Table 2

Sharjah Islamic Bank--Business position

	--Year-ended Dec. 31--				
(%)	**2023***	**2022**	**2021**	**2020**	**2019**
Total revenues from business line (currency in millions)	483.8	1,609.1	1,427.5	1,259.2	1,227.7
Commercial banking/total revenues from business line	36.8	43.5	54.6	52.9	45.6
Retail banking/total revenues from business line	17.9	20.7	24.6	28.2	30.9
Commercial and retail banking/total revenues from business line	54.6	64.2	79.2	81.1	76.5
Other revenues/total revenues from business line	45.4	35.8	20.8	18.9	23.5
Return on average common equity	16.3	11.2	8.8	7.1	9.8

*Data as of March 31.

Table 3

Sharjah Islamic Bank--Capital and earnings

	--Year-ended Dec. 31--				
(%)	**2023***	**2022**	**2021**	**2020**	**2019**
Tier 1 capital ratio	18.3	17.9	19.7	19.5	21.6
S&P Global Ratings' RAC ratio before diversification	N/A	11.1	13.1	13.8	15.6
S&P Global Ratings' RAC ratio after diversification	N/A	8.5	10.2	7.9	11.9
Adjusted common equity/total adjusted capital	76.2	75.6	75.2	75.2	75.2
Net interest income/operating revenues	77.4	76.6	77.9	78.1	73.6
Fee income/operating revenues	12.1	14.2	16.1	14.9	15.3
Market-sensitive income/operating revenues	5.9	5.7	2.7	3.6	4.8
Cost to income ratio	32.6	38.6	41.1	45.0	48.0
Preprovision operating income/average assets	2.2	1.7	1.5	1.4	1.4
Core earnings/average managed assets	1.5	1.2	1.1	0.9	1.2

*Data as of March 31. N/A--Not applicable. RAC--Risk Adjusted Capital.

Table 4

Sharjah Islamic Bank--Risk-adjusted capital framework data

Table 4

Sharjah Islamic Bank--Risk-adjusted capital framework data (cont.)

(Mil. AED)	Exposure*	Basel III RWA	Average Basel III RW(%)	S&P Global Ratimgs' RWA	Average S&P Global Ratimgs' RW (%)
Credit risk					
Government and central banks	19,757	2,923	15	5,079	26
Of which regional governments and local authorities	0	0	0	0	0
Institutions and CCPs	7,106	2,114	30	4,226	59
Corporate	22,765	20,881	92	30,377	133
Retail	4,707	3,573	76	4,915	104
Of which mortgage	1,298	1,169	90	774	60
Securitization§	0	0	0	0	0
Other assets†	6,476	8,733	135	11,726	181
Total credit risk	60,810	38,224	63	56,324	93
Credit valuation adjustment					
Total credit valuation adjustment	--	0	--	0	--
Market risk					
Equity in the banking book	857	9	1	8,302	969
Trading book market risk	--	184	--	448	--
Total market risk	--	192	--	8,750	--
Operational risk					
Total operational risk	--	2,584	--	2,970	--
	Exposure	**Basel III RWA**	**Average Basel II RW (%)**	**S&P Global Ratimgs' RWA**	**% of S&P Global Ratimgs' RWA**
Diversification adjustments					
RWA before diversification	--	41,001	--	68,044	100
Total diversification/ Concentration adjustments	--	--	--	20,012	29
RWA after diversification	--	41,001	--	88,056	129
		Tier 1 capital	**Tier 1 ratio (%)**	**Total adjusted capital**	**S&P Global Ratimgs' RAC ratio (%)**
Capital ratio					
Capital ratio before adjustments		7,362	18.0	7,526	11.1
Capital ratio after adjustments‡		7,362	17.9	7,526	8.5

*Exposure at default. §Securitization exposure includes the securitization tranches deducted from capital in the regulatory framework. †Exposure and S&P Global Ratings' risk-weighted assets for equity in the banking book include minority equity holdings in financial institutions. ‡Adjustments to tier 1 ratio are additional regulatory requirements (e.g. transitional floor or pillar 2 add-ons). RWA--Risk-weighted assets. RW--Risk weight. RAC--Risk-adjusted capital. AED--United Arab Emirates dirham. Sources: Company data as of Dec. 31, 2022, S&P Global Ratings.

Table 5

Sharjah Islamic Bank--Risk position

	--Year-ended Dec. 31--				
(%)	**2023***	**2022**	**2021**	**2020**	**2019**
Growth in customer loans	-2.3	6.2	-0.7	16.4	2.7
Total diversification adjustment/S&P Global Ratings' RWA before diversification	N/A	29.4	29.1	75.0	31.4
Total managed assets/adjusted common equity (x)	10.2	10.4	9.9	9.9	8.6
New loan loss provisions/average customer loans	1.2	1.0	0.8	0.9	0.4
Net charge-offs/average customer loans	0.0	0.2	0.4	0.2	1.6
Gross nonperforming assets/customer loans + other real estate owned	6.2	6.0	4.8	4.9	5.1
Loan loss reserves/gross nonperforming assets	82.3	79.1	91.3	86.2	82.8

*Data as of March 31. N/A--Not applicable. RWA--Risk Weighted Assets.

Table 6

Sharjah Islamic Bank--Funding And Liquidity

	--Year-ended Dec. 31--				
(%)	**2023***	**2022**	**2021**	**2020**	**2019**
Core deposits/funding base	81.4	79.3	83.0	74.5	72.0
Customer loans (net)/customer deposits	72.6	77.6	75.4	87.1	92.1
Long-term funding ratio	88.7	87.3	93.1	87.5	88.7
Stable funding ratio	107.4	106.0	117.5	104.2	107.2
Short-term wholesale funding/funding base	13.0	14.6	8.1	14.6	13.5
Broad liquid assets/short-term wholesale funding (x)	1.8	1.6	3.3	1.4	1.7
Broad liquid assets/total assets	19.4	20.1	22.2	17.6	19.1
Broad liquid assets/customer deposits	27.9	30.0	31.7	28.0	32.5
Net broad liquid assets/short-term customer deposits	12.0	11.6	22.1	8.4	13.7
Short-term wholesale funding/total wholesale funding	58.4	59.8	38.4	49.5	41.2
Narrow liquid assets/3-month wholesale funding (x)	N/A	N/A	N/A	1.7	1.9

*Data as of March 31. N/A--Not applicable.

Sharjah Islamic Bank--Rating component scores

Issuer credit rating	**A-/Stable/A-2**
SACP	bbb-
Anchor	bbb-
Economic risk	6
Industry risk	5
Business position	Moderate
Capital and earnings	Strong
Risk position	Adequate
Funding	Adequate
Liquidity	Adequate
Comparable ratings analysis	0
Support	+3
ALAC support	0

Sharjah Islamic Bank--Rating component scores (cont.)	
Issuer credit rating	**A-/Stable/A-2**
GRE support	0
Group support	0
Sovereign support	+3
Additional factors	0

ALAC--Additional loss-absorbing capacity. GRE--Government-related entity. SACP--Stand-alone credit profile.

Related Criteria

- General Criteria: Hybrid Capital: Methodology And Assumptions , March 2, 2022
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions , Dec. 9, 2021
- Criteria | Financial Institutions | General: Financial Institutions Rating Methodology , Dec. 9, 2021
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings , Oct. 10, 2021
- General Criteria: Group Rating Methodology , July 1, 2019
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology , July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings , April 7, 2017
- General Criteria: Methodology For Rating Sukuk , Jan. 19, 2015
- General Criteria: Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions , Nov. 19, 2013
- General Criteria: Principles Of Credit Ratings , Feb. 16, 2011

Related Research

- Sharjah Islamic Bank's Ratings Affirmed At 'A-/A-2' On Anticipated Asset Quality Recovery; Outlook Stable, June 8, 2023
- Credit FAQ: Can GCC Banks Weather Funding Risks?, June 5, 2023
- Emirate of Sharjah, May 22, 2023

Ratings Detail (As Of July 25, 2023)*	
Sharjah Islamic Bank	
Issuer Credit Rating	A-/Stable/A-2
Issuer Credit Ratings History	
25-Mar-2021	A-/Stable/A-2
26-Mar-2020	A-/Negative/A-2
27-May-2019	A-/Stable/A-2

Ratings Detail (As Of July 25, 2023)*(cont.)	
Sovereign Rating	
Abu Dhabi (Emirate of)	AA/Stable/A-1+
Related Entities	
SIB Sukuk Co. III Ltd.	
Senior Unsecured	A-

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.