FitchRatings

RATING ACTION COMMENTARY

Fitch Places Doha Bank on Rating Watch Negative

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Fitch Ratings - Dubai - 21 Oct 2021: Fitch Ratings has placed Doha Bank Q.P.S.C.'s (Doha Bank) Long-Term Issuer Default Rating (IDR) of 'A' on Rating Watch Negative (RWN). The Short-Term IDR and the Support Rating Floor (SRF) were also placed on RWN. Doha Bank's Viability Rating (VR) has been affirmed at 'bb'. A full list of rating actions is provided below.

The RWN reflects the Qatari banking sector's increasing reliance on external funding and recent rapid asset growth, which may have moderately weakened the sovereign's ability to provide support to the system, in case of need.

KEY RATING DRIVERS

Non-resident funding reached USD193 billion or 48% of the Qatari banking sector's liabilities at end-August 2021 (up from USD121 billion or 38% at end-2018), while banks' foreign assets remained broadly stable (USD60 billion at end-August). As a result, the banking sector's net external debt at end-August 2021 increased to a substantial USD133 billion or 82% of forecast 2021 GDP (USD57 billion or 31% at end-2018). This high level of external funding, coupled with the large size of the banking system (total assets increased to 302% of forecast 2021 GDP at end-August 2021 from 212% at end-2018), could have moderately weakened the authorities' ability to support the banking sector, if needed, notwithstanding the substantial resources at the sovereign's disposal.

The 'A' domestic systemically important bank (D-SIB) SRF for Qatari banks is at the higher end of the typical range for D-SIB SRFs in jurisdictions where the sovereign is rated 'AA-' and, in Fitch's view, reflects a high propensity to support the banking system.

Fitch will resolve the RWN following further analysis of the current composition and stability of Qatari banks' non-resident funding, the evolution of this funding in volumes and sources, banks' liquidity-management plans and the sovereign's ability to provide liquidity support to banks, in case of need. In case of a downgrade, Doha Bank's Long-Term IDR and SRF are expected to remain in the 'A' category.

IDRs, SR and SRF

Doha Bank's IDRs, Support Rating (SR) and SRF continue to reflect an extremely high probability of support from the Qatari authorities for domestic banks, if needed. This considers Qatar's still strong ability to support domestic banks, as reflected in the sovereign's 'AA-'/Stable rating and substantial net foreign assets (end-2020: equivalent to 187% of GDP) and revenues.

It also reflects Fitch's view of a strong propensity to support the banking sector, including Doha Bank, based on past episodes of support. These include in 2H17, when the authorities placed significant deposits with banks to support sector liquidity, following the start of the blockade between Qatar and some of its neighbours, and between 2009 and 2011, when some banks received capital injections to enhance their capital buffers and the government purchased some problem assets from the banks. The government owns stakes in all Qatari banks.

The Short-Term IDR of 'F1' is the lower of two options mapping to an 'A' Long-Term IDR, reflecting that a significant proportion of the banking sector's funding is government-related and a stress on Doha Bank is likely to come at a time when the sovereign itself is experiencing some form of stress.

VR

Fitch has revised the outlook on Qatari banks' operating environment to stable from negative as short-term downside risks from the pandemic fallout on banks' credit profiles have subsided. Fitch forecasts Qatar's real GDP growth to rebound to 1.6% in 2021 (2022: 2.5%), following a 3.6% contraction in 2020, supported by higher hydrocarbon prices and the North Field LNG expansion. The sector's credit growth was 6.7% (annualised) in 1H21 (2020: 8.5%), despite cutbacks in capex by the government.

We believe the near-term risks on the sector's asset quality (end-1H21: average Stage 3 loans ratio of about 2%) are largely contained - even after the expiry of the Qatar Central Bank (QCB) credit deferrals - and offset by the recovering operating environment and banks' strong provisioning levels (end-1H21: 140% average total reserve coverage of impaired loans). Qatari banks have adequate capital buffers (end-1H21: average CET1 ratio of 14% against an 8.5% regulatory minimum requirement) and healthy pre-impairment operating profitability offsetting a potential moderate increase in problem loans.

Doha Bank's 'bb' VR reflects a high-risk profile, historically weak asset quality, below-average profitability and ensuing pressures on core capitalisation, as well as a high reliance on foreign funding. However, the VR is underpinned by the bank's well-established domestic franchise (end-1H21: 6% market share of assets) and the execution of the bank's consolidation strategy.

We view the bank's underwriting and risk controls as weaker than peers', due to high single-name and sector concentrations, which expose the bank to material credit risk. However, Doha Bank has tightened its risk framework and increased monitoring efforts of its weak GCC operations as part of a loan book clean-up. It aims to contain asset-quality risks through a reduction in high-risk construction and real-estate exposures (end-1H21: 33% of loans; end-2019: 40%) and growth in higher-quality government lending (end-1H21: 25%; end-2019: 11%). The latter was a driver of the bank's rapid loan growth in 1H21 (10%; target 7% in 2022).

The bank's non-performing loans (NPL) ratio (end-1H21: 5.6%) is higher than peers', reflecting the seasoning of high-risk contracting and GCC exposures. NPL generation was still high in 1H21 (3.1% annualised basis; 2020: 6%). The NPL ratio was flattered by large write-offs (1H21: 120bp of gross loans; 2020: 550bp), as part of the clean-up exercise. Risks are high from Stage 2 loans (25% of gross loans) at end-1H21 and loans that are subject to deferrals (29%; a much lower 2% considering deferred instalments only). Total reserves coverage of NPLs decreased to 79% at end-1H21 (specific coverage of 53%), due to write-offs.

Operating profitability has improved (1H21: 1.8% of risk-weighted assets (RWAs); 2020: 1%) but remains below sector average and is still dampened by high impairment charges (45% of pre-impairment operating profit; 2020: 66%). Net interest margin (NIM) was resilient in 1H21 at 2.6% (2019: 2.4%), underpinned by lower funding costs. Cost efficiency has also slightly improved (costs/income ratio of 28%) as per the bank's strategy.

We expect some moderate NIM pressure in the medium term to result from a higher share of low-yielding government lending and an increase in long-term deposits and foreign funding. Impairments are likely to remain high in 2021-2022, given asset-quality pressures, although the bank's net cost of risk (1H21: 150bp) should gradually wane in the medium term, due to fewer write-offs and potential recoveries from lumpy NPLs conservatively provisioned for or written-off.

Doha Bank's CET1 ratio of 13.2% at end-1H21 (end-2019: 11.5%) was weak, considering the bank's high-risk profile, single-name risk and the potential for further asset-quality impairments due to a large stock of unreserved Stage 2 and 3 loans (end-1H21: 2.1x CET1; end-2019: 2.0x). However, core capitalisation has improved, primarily due to profit retention and loan deleveraging in 2020, as per the bank's strategy. The bank's Tier 1 ratio (18.9%) and total capital adequacy ratio (CAR; 20%) are supported by QAR4 billion of additional Tier 1 capital notes.

Buffers over regulatory minimum capital requirements are sound (about 470bp for the CET1 ratio at end-1H21). We expect the CET1 ratio to be only slightly eroded from its current level by renewed private-sector loan growth and dividend distributions.

The bank's gross loans/deposits ratio of 128% and net loans/deposits of 122% (versus banking sector average of 125%) at end-1H21 reflect a high reliance on wholesale funding (end-1H21: 39% of total funding), with the majority from foreign sources and due within one year. Additionally, about 47% of customer deposits was sourced from non-residents, exposing the bank's funding to changes in investor sentiment. The bank's funding profile remains fairly short-term , although Doha Bank has lengthened the average tenor of its wholesale liabilities in 1H21 through longer-term bilateral borrowings and the issuance of a USD500 million Eurobond maturing in 2026.

Liquid assets represented an adequate 20% of total assets or 38% of customer deposits at end-1H21. However, liquidity risk is heightened by a high share of concentrated and confidence-sensitive foreign deposits (end-1H21: 47% of total deposits), which have increased in 2020-1H21, as has for the sector. Its regulatory liquidity coverage ratio was 125% at end-1H21, above the 100% minimum requirement.

SPVs and SENIOR DEBT

The ratings of senior debt issued by Doha Bank's special purpose vehicle (SPV) are in line with the bank's Long or Short-Term IDRs, because Fitch views the likelihood of default on any senior unsecured obligation issued by the SPV the same as the likelihood of default by the bank.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to negative rating action/downgrade:

IDRs, SR, and SRF

The IDRs and SRF could be downgraded and revised lower, respectively, if Fitch concludes that the Qatari authorities' ability to support the banking sector or the bank has moderately reduced as a result of the increase in external funding and the growth in system assets. In case of a downgrade, Doha Bank's Long-Term IDR and SRF are likely to remain in the 'A' category.

A downgrade of the sovereign or a negative change in Fitch's assessment of the government's propensity to provide support could also result in a downgrade of Doha Bank's IDRs and downward revision of the SRF.

VR

The VR is primarily sensitive to further material weakening in the bank's asset quality and core loss-absorption capacity or to large foreign deposit outflows, if not offset by liquidity support from the Qatari authorities.

SPVs and Senior Debt

The ratings of debt issued by the SPV are sensitive to negative changes in the bank's IDR.

Factors that could, individually or collectively, lead to positive rating action/upgrade:

IDRs, SR, and SRF

Doha Bank's IDRs and SRF could be affirmed at their current levels if Fitch concludes that the sovereign's ability to support the sector has not materially reduced, notwithstanding the increase in external funding and system assets.

Rating upgrades are highly unlikely given the RWN on the ratings, their already high level relative to the sovereign's, and the Stable Outlook on the sovereign's ratings.

VR

The VR could be upgraded if the bank successfully executes its consolidation strategy, reduces its stock of problem loans - with its real-estate and contracting exposure decreasing substantially compared with the sector average - and the bank maintaining its CET1 ratio above 13% in the medium term. A lower reliance on foreign funding could also provide upside to the VR.

SPVs and Senior Debt

The ratings of debt issued by the SPV are sensitive to positive changes in the bank's IDR.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Financial Institutions and Covered Bond issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

PUBLIC RATINGS WITH CREDIT LINKAGE TO OTHER RATINGS

Doha Bank's IDRs are driven by sovereign support. The ratings of senior debt issued by Doha Bank's special purpose vehicle (SPV) are in line with the bank's Long- or Short-Term IDRs.

ESG CONSIDERATIONS

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

RATING ACTIONS

ENTITY/DEBT	RATING			PRIOR
Doha Bank Q.P.S.C.	LT IDR	A Rating Watch Negative	Rating Watch On	A Rating Outlook Stable
	ST IDR	F1 Rating Watch Negative	Rating Watch On	F1
	Viability	bb	Affirmed	bb

ENTITY/DEBT	RATING			PRIOR
	Support	1	Affirmed	1
	Support Floor	A Rating Watch Negative	Rating Watch On	A

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

Bank Rating Criteria (pub. 28 Feb 2020) (including rating assumption sensitivity)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Doha Bank Q.P.S.C.	UK Issued, EU Endorsed
Doha Finance Limited	UK Issued, EU Endorsed

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