



IIRA Assesses Sovereign Ratings of Bahrain

Manama, March 24, 2016 – The Islamic International Rating Agency has assessed the long-term and short-term sovereign credit rating of the Kingdom of Bahrain ('Bahrain' or 'the Kingdom') at BBB / A3 (Triple B / Single A Three) respectively, on both the foreign and local currency scale. Outlook on the ratings is 'Stable' The investment grade assessment is underpinned by fundamental strengths, including the Kingdom's status as a high income economy, its cohesiveness with the larger Gulf Cooperative Council, and a well developed physical and social infrastructure.

Despite an adverse commodity price cycle bearing on key economic indicators, Bahrain is on a steady growth path, buoyed by the continued momentum in the non-hydrocarbon segment of its economy. Having achieved diversification in terms of economic output, future growth is linked almost exclusively to the non-oil segment over the next few years, with anticipated increase in manufacturing, tourism and hospitality sectors. This, in addition to infrastructure development and increased construction activity, particularly in the wake of an expected escalation in the drawdown of the GCC Development Fund, underlies the positive forecast for non-oil growth in Bahrain.

Nevertheless, the Kingdom's balance of payments position and more critically its fiscal structure remains hinged on oil prospects. The inevitable squeeze in the oil trade surplus, which has traditionally supported the Kingdom's historically strong external account, has driven the current account into a deficit in 2015. While a non-oil trade surplus is surely emerging, it may not be enough to outweigh the effects of a narrower oil surplus on the net position, in the near future.

With government's revenues being strongly correlated to oil receipts, the sustained fall in oil prices explains the significant fiscal deficit, expected to have exceeded 10% in 2015. A region wide drive to reorient government expenditures and diversify revenues, with a single-minded focus on reducing subsidies to both the public and the corporate sector, has surfaced. Cut back of subsidies, emphasis on recouping lost revenue on government services and steps taken to enhance government efficiency, may lift some of the prevailing stress on Bahrain's budget. The drive to bring the fiscal balance to a sustainable level has emerged as a clear national priority. Success on this front will be monitored over time.

Bahrain's external debt has continued to mount, reaching almost 60% of GDP by year-end 2015. Further increase in these levels can reasonably be expected with meaningful fiscal reengineering to require a

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time span of 2-3 budget cycles and the fiscal deficit likely to persist meanwhile, failing a significant rebound in oil prices.

Social indicators in Bahrain point to steady improvements in the area of health care and education. Bahrain is committed to the Millennium Development Goals set in conjunction with the United Nations Development Programme. The Kingdom continues to climb the ladder vis-à-vis its global position on the Human Development Index, which exemplifies national commitment to social development.

Factors that will drive the future direction of ratings include meaningful achievement of targets set for fiscal rebalancing, aimed at reducing reliance on oil revenues, and a corresponding taper down of what has lately been a sharp incline in debt to GDP levels. The success of ongoing fiscal re-engineering in other GCC countries will translate into enhanced resilience across the region and benefit each of the Gulf countries in its wake. Meaningful progress towards further integration within the GCC as an economic union could also provide upward impetus to Bahrain's ratings.

For further information on this rating announcement, please contact the undersigned or email at iira@iirating.com

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