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Overall effect of IFRS 9 on financial profiles of GCC banks is manageable, says S&P

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The impact of International Financial Reporting Standard (IFRS) 9 "Financial Instruments" on the financial profiles of the rated banks in the Gulf Cooperation Council (GCC) will be manageable, according to a recent report by S&P Global Ratings.

Due to be implemented on 1 January 2018, IFRS 9 requires banks to take a more forward-looking approach to provisioning. At the moment, banks are required to set aside specific provisions only when they incur losses, or when the counterparty or financial asset defaults on its obligations. Under IFRS 9, banks will have to set aside provisions in advance, based on their loss expectations.

"Our view that the impact of IFRS 9 will be manageable is due in part to the relatively conservative approach that GCC banks already take to calculating and setting aside loan-loss provisions. Some banks, for example those in Kuwait, take a conservative approach as part of local regulatory requirements to set aside general provisions for all their lending portfolios," said S&P Global Ratings credit analyst Mohamed Damak.

According to S&P's base-case scenario, rated GCC banks will have to set aside additional provisions equivalent to 17 per cent of their net operating income on average following the adoption of IFRS 9. Excluding banks with no provision shortfall, the same measure rises to 27 per cent under the base-case scenario. However, these results mask significant differences between banks.

The least affected rated banks would be in Kuwait. This is because the regulator already requires banks in Kuwait to set aside a general provision on their performing facilities equivalent to one per cent of cash facilities and 0.5 per cent of non-cash facilities.

The most affected rated banks would be in Qatar, primarily due to the specific cases of a couple of Qatari banks that have either seen a significant deterioration in their asset quality indicators, or an increase in past due but not impaired loans, over the past couple of years.

In a statement, S&P clarified that it calibrated its assumptions based on rated GCC banks' balance sheet structures. The same methodology and assumptions might not be applicable to other banks or other jurisdictions.

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