FitchRatings

RATING ACTION COMMENTARY

Fitch Affirms Arap Turk Bankasi at 'B-', Outlook Positive

Wed 24 Jul, 2024 - 11:48 AM ET

Fitch Ratings - Paris - 24 Jul 2024: Fitch Ratings has affirmed Arap Turk Bankasi A.S.'s (ATB) Long-Term Foreign-Currency (LTFC) and Local-Currency (LTLC) Issuer Default Ratings (IDRs) at 'B-' with Positive Outlooks. Fitch has also affirmed the bank's Viability Rating (VR) at 'b-'. A full list of rating actions is detailed below.

KEY RATING DRIVERS

Niche Franchise: ATB's ratings reflect the bank's concentration in the volatile Turkish operating environment, its small niche franchise within the trade-finance sector, weak profitability and only adequate capitalisation. It also reflects contained asset-quality risks, and stable, but concentrated, funding. The Positive Outlooks reflect an improving operating environment in Turkyie, which should result in improved performance that could ultimately lead to an upgrade of the bank's ratings.

The bank's 'B' Short-Term IDRs are the only option mapping to Long-Term IDRs in the 'B' category.

Improving but Challenging Operating Environment: ATB's operations are concentrated in the improving but challenging Turkish operating environment. The normalisation of monetary policy has reduced near-term macro-financial stability risks and external financing pressures but banks remain exposed to high inflation, potential further lira depreciation, slowing economic growth, and multiple macroprudential regulations, despite simplification efforts.

Small Trade-Finance Bank: ATB is a small Turkish trade-finance bank primarily specialising in facilitating trade between Turkiye and Libya, and, to a lesser extent, the Middle East and North Africa region. The bank has close ties with its largest shareholder, Libyan Foreign Bank (LFB; 62.4%), which provides it with low-cost foreign-currency (FC) funding.

High FC Lending: ATB's underwriting standards compare fairly well with Fitch-rated trade finance peers', although the bank faces risks from its concentrated operations in challenging emerging markets. On-balance sheet lending is mainly in FC (end-1Q24: 75% of total loans) and therefore sensitive to Turkish lira depreciation.

Negligible Impairments: ATB's asset quality benefits from the short-term nature of its loan book, as well as counter-guarantees by Turkish banks against a significant proportion of its Libyan country risk in its trade-finance operations. The bank's impaired loans ratio was a low 0.1% at end-1Q24, while Stage 2 loans were negligible. Nevertheless, asset-quality risk remains from high FC lending and concentration in the volatile Turkish operating environment.

Weak Profitability: ATB's operating profit remained subdued at 1.2% of risk weighted assets (RWAs) in 3M24 after declining to 0.8% in 2023 due to rising operating costs fueled by inflation and significant one-off impairment charges. The bank's profitability remains below its historical average (four-year average 2.6%) due to muted loan growth and a high cost-to-income ratio (3M24: 81%). Nevertheless, ATB's net interest margin remained stable and above the sector-average, benefiting from low-cost funding from its parent.

Only Adequate Capitalisation: ATB's CET1 ratio remained stable at 17.0% (net of forbearance: 14.6%) at end-1Q24 (end-2023: 17.0%), as internal capital generation offset RWA growth. We view ATB's capitalisation as only adequate considering the sensitivity of capital to lira depreciation (84% of its balance sheet is in FC) and its small capital base.

High Parent Funding: ATB is mainly wholesale-funded (62% of total funding at end-1Q24), similar to other trade finance banks. ATB relies heavily on FC funding from its parent, which accounted for around 40% of total funding at end-1Q24. The remaining funding is in the form of customer deposits, largely non-resident, from Libyan clients. ATB is exposed to refinancing risk given its high reliance on FC wholesale funding, although the short-term maturity profile of the loan book and trade finance exposures supports liquidity.

RATING SENSITIVITIES

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

ATB's VR and IDRs could be downgraded due to a substantial withdrawal in parent funding, prompting a significant reduction in the bank's FC liquidity, or if the bank's CET1 ratio falls to levels not commensurate with the bank's risk profile on a sustained basis. ATB's IDRs are also potentially sensitive to a sovereign downgrade.

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

ATB's ratings could be upgraded following an upward revision of its operating environment score, which could follow an upgrade of the Turkish sovereign, provided that the operating environment should enable the bank's performance to improve

OTHER DEBT AND ISSUER RATINGS: KEY RATING DRIVERS

The bank's National Long-Term Rating of 'BBB(tur)'/Positive reflects our view of the bank's unchanged creditworthiness in local currency relative to other Fitch-rated Turkish issuers'.

The bank's 'no support' Government Support Rating (GSR) reflects Fitch's view that support from the Turkish authorities cannot be relied on, given the bank's small size and limited systemic importance. In addition, support from ATB's shareholders, while possible, cannot be relied on in view of the uncertain political environment in Libya.

OTHER DEBT AND ISSUER RATINGS: RATING SENSITIVITIES

The National Rating is sensitive to a change in the bank's creditworthiness in LC relative to that of other Turkish issuers.

VR ADJUSTMENTS

The operating environment score of 'b' for Turkish banks is lower than the category implied score of 'bb', due to the following adjustment reasons: sovereign rating (negative) and macroeconomic stability (negative).

The asset quality score of 'b' is below the category implied score of 'bb', due to the following adjustment reason: concentrations (negative).

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.

ESG CONSIDERATIONS

ATB has an ESG Relevance Score for Management Strategy of '4', reflecting the high regulatory burden on most Turkish banks. Management ability across the sector to determine their own strategy is constrained by regulatory intervention and also by the operational challenges of implementing regulations at the bank level. This has a moderately negative impact on banks' credit profiles and is relevant to banks' ratings in combination with other factors.

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' 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. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit https://www.fitchratings.com/topics/esg/products#esg-relevance-scores.

RATING ACTIONS

ENTITY / DEBT	RATING			PRIOR
Arap Turk Bankasi A.S.	LT IDR	B- Rating Outlook Positive	Affirmed	B- Rating Outlook Positive
	ST IDR	B	Affirmed	B
	LC LT IDR	B- Rating Outlook Positive	Affirmed	B- Rating Outlook Positive
	LC ST IDR	B	Affirmed	B
	Natl LT	BBB(tur) Rating Outlook Positive	Affirmed	BBB(tur) Rating Outlook Positive
	Viability	b-	Affirmed	b-
	Government Support	ns	Affirmed	ns

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

National Scale Rating Criteria (pub. 22 Dec 2020)

Bank Rating Criteria (pub. 15 Mar 2024) (including rating assumption sensitivity)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Arap Turk Bankasi A.S.	EU Issued, UK Endorsed

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