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Inter-American Development Bank

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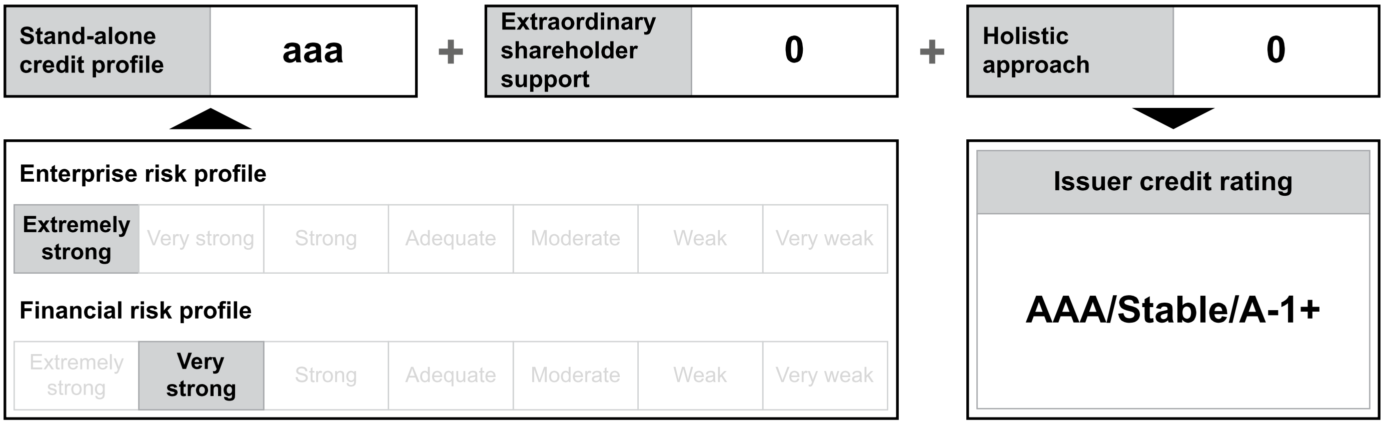
Inter-American Development Bank



Issuer Credit Rating

Foreign Currency

AAA/Stable/A-1+

Outlook

The stable outlook reflects our expectation that over the next 24 months, Inter-American Development Bank (IADB) will apply sound governance and risk management and prudently manage its capital and liquidity, particularly in light of increased credit stress. At the same time, we expect that IADB will retain its role as the main supplier of developmental financing in the region. We believe that sovereign borrowing members will continue to treat IADB as a preferred creditor.

We could downgrade IADB if other borrowers fall into nonaccrual status, indicating weaker preferred creditor treatment (PCT). A significant deterioration in IADB's funding and liquidity could also lead us to lower the rating. That said, significant erosion of the risk-adjusted capital (RAC) ratio would most likely be mitigated by the existing callable capital from IADB's highly rated sovereign shareholders.

Rationale

In our view, IADB has an unparalleled role in Latin America, evidenced by its robust response to its borrowing members as a result of COVID-19, and we expect it to provide $15 billion in funding support during 2020. The institution also has a strong governance and risk management framework, which largely counterbalances the potential agency risk stemming from its borrowing member countries having slightly more than 50% of the voting power on its board.

Credit stresses in the region from COVID-19 have weighed on IADB's capital adequacy, which declined to 19.5% as of December 2019 (with rating parameters as of July 2020). We expect that the institution will carefully manage rising risks in its portfolio with the demand for resources to stabilize its capital position and expect the ratio to remain above 15%. This notwithstanding, callable capital from IADB's highly rated shareholders would enhance our RAC ratio and mitigate the impact on the bank's financial risk profile in the event that its capital adequacy were to deteriorate. At the same time, IADB maintains robust funding and liquidity.

Environmental, Social, And Governance

IADB has two overarching objectives: to reduce poverty and inequality and to achieve sustainable growth. It aims to accomplish these by addressing:

- Three critical development challenges (social inclusion and equality, productivity and innovation, and economic integration), and
- Three cross-cutting issues (gender equality and diversity, climate change and environmental sustainability, and institutional capacity and the rule of law).

In 2019, IADB reported that 56% of its lending volumes supported gender equality and diversity, 73% supported productivity and innovation, and 80% supported institutional capacity and rule of law.

As a public-sector lender in Latin America, it is highly exposed to Brazil, Argentina, Mexico, Colombia, and Ecuador, each of which is subject to modest environmental and social risks. A high proportion of IADB's projects are designed to tackle these risks, for example, by creating resilient infrastructure or addressing social challenges in these countries.

The institution does not fund coal, although it has financed fossil fuels. In 2019, 29% of its projects had a climate adaptation component, which supports a greener portfolio. IADB has robust mechanisms to identify and address environmental and social challenges arising from its projects and programs. We view its oversight and accountability mechanisms in this area as transparent and robust.

In terms of shareholder diversity, a majority of IADB's borrowers have low rankings in World Bank governance effectiveness indicators. This may expose the bank to potential agency risks. However, the bank has implemented comprehensive and conservative financial and risk reforms over the past few years and has shown that it can adhere to these during times of stress, which supports the rating.

Enterprise Risk Profile: Long Record Of Fulfilling Policy Mandate Combined With Improved Governance And Risk Management

- In our view, IADB plays a key role in the region, supported by its long track record of fulfilling its policy mandate.
- This, coupled with the institution's strengthened governance and risk management framework, underpins its

extremely strong enterprise risk profile.

Policy importance

Established in 1959, IADB's purpose is to accelerate economic and social development in Latin American and the Caribbean, with an emphasis on poverty reduction and social equality, modernization and sector reform, economic integration, and the environment.

The bank was initially established by 19 Latin American and Caribbean countries and the U.S., and between 1976 and 1993, it grew to encompass an additional 18 nonregional member countries. In 2005, the Republic of Korea joined the bank, followed by the People's Republic of China in 2009, bringing the total number of member countries to 48. No major shareholder has withdrawn from IADB, and we do not expect any to do so in the medium term.

In 2010, IADB's ninth general capital increase was approved, which increased the bank's ordinary capital resources to roughly $170 billion from $100 billion. Of this amount, US$1.7 billion was paid-in. Of the 48 member countries, The Netherlands and Venezuela decided not to participate in the capital increase, and in January 2013, the bank reallocated these additional shares to other member countries. As of today, IADB has received all of the paid-in capital.

In addition, the bank committed to transfer US$200 million annually in income to the grant facility to support Haitian reconstruction and development between 2011 and 2020. In 2016, the bank updated its policy of disbursing grants to Haiti contingent on the level of undisbursed grant funds given the country's inability to fully execute the grants disbursed. IADB also changed the grant agreement with Haiti to make it uncommitted so that it can decide whether to disburse, as well as changed the GRF funding approach to be a function of its remaining balance.

IADB lends mainly to the public sector, and its main financing instruments include investment loans and policy-based financing, while also providing emergency financing.

Recently, IADB announced that it would be approving approximately $15 billion in additional financing to respond to COVID-19 and its economic effects. The bank will now focus on four main priority areas: the immediate public health response, safety nets for vulnerable populations, economic productivity and employment, and fiscal policies. We expect an increase in the share of policy-based lending for the year.

All private-sector lending activities have been consolidated in IDB Invest, which is part of the IADB Group, following the March 2015 approval of "Delivering the Renewed Vision: Organizational and Capitalization Proposal for the IDB Group Private Sector Merge-out." The consolidation plan became effective Jan. 1, 2016, including transferring administrative supervision of IADB's NSG loan portfolio to IDB Invest, even while this portfolio remains on IADB's balance sheet. All new private-sector lending operations are originated by IDB Invest, though they will be partially cross-booked on IADB's balance sheet until 2022.

Furthermore, IADB will transfer $725 million to IDB Invest from its net income between 2018 and 2025, subject to annual approval and conditional upon compliance with its capital adequacy policy, among others.

We view IADB's role in Latin America as unparalleled, supported by continued growth in its outstanding loan portfolio, which reached $97 billion as of year-end 2019. We don't believe IADB can be replaced by another multilateral lending institution (MLI) or by a commercial bank.

Aside from lending activities, we believe that IADB is a key provider of technical assistance and research to the region, as well as an important provider of concessional funds to its eligible members. In 2017, net assets from its concessional financing window--the Fund for Special Operations (FSO)--were transferred to the bank's ordinary capital.

The performance of its sovereign loan portfolio has been excellent compared with commercial creditors', as is generally the case for MLIs. Borrowing member sovereigns that have defaulted on their commercial foreign currency debt in the past 15 years (Argentina, Belize, Dominican Republic, Ecuador, Jamaica, Paraguay, and Uruguay) have not gone into arrears with IADB.

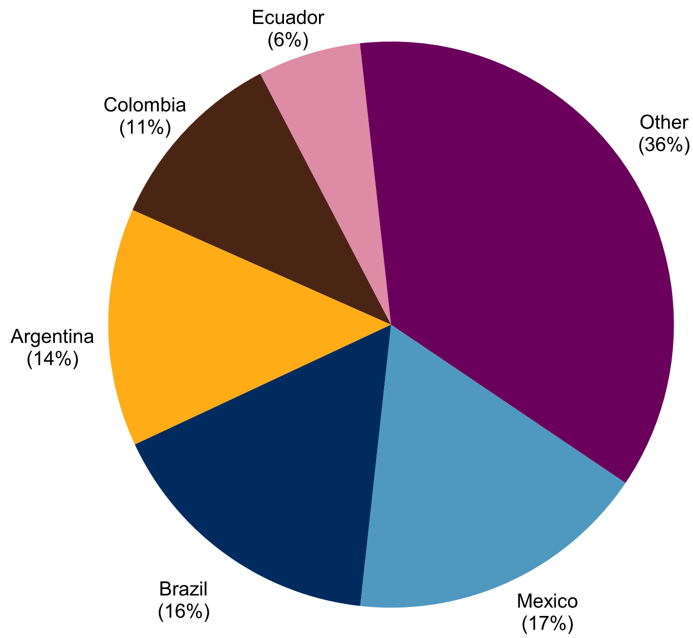
However, on May 14, 2018, Venezuela entered into nonaccrual status with IADB. By Dec. 31, 2019, US$492 million in principal and interest was due and unpaid that reached 180 days. The country defaulted on its commercial obligations in November 2017. Our calculated PCT ratio of 2.2% reflects Venezuela's payment arrears with IADB, in which the total loan balance of US$2.01 billion has been placed in nonaccrual status.

Venezuela continued making payments to other MLIs, which gave it further loans, whereas IADB did not grant any additional financing. We believe Venezuela has demonstrated its willingness to repay IADB but has run out of capacity to keep its payments up to date. U.S. sanctions and mounting pressure from the international community contribute to a very difficult environment in Venezuela, in our view. However, we don't believe they are the main reason for the nonaccruals with IADB.

We believe this event to be relatively contained given that Venezuela accounts for about 2.1% of IADB's lending book and 1.5% of its total assets. We also expect the rest of IADB's sovereign borrowers to continue to afford it PCT.

Chart 1

IADB--Five Largest Countries Purpose-Related Exposures
As a percentage of gross purpose-related assets plus guarantees



Source: S&P Global Ratings.

Governance and management expertise

The agreement establishing IADB, as amended, stipulates that the voting power of regional developing country members will not be less than 50.005% of the total. In addition, the voting power of the U.S. is no less than 30% and that of Canada no less than 4%.

As of year-end 2019, the largest non-borrowing shareholders were the U.S. (30.01% voting share), Japan (5.00%), and Canada (4.00%). The largest regional vote holders were Argentina and Brazil, with 11.35% each; Mexico, with 7.29%; and Venezuela, with 3.40%.

Half of IADB's voting members are borrowing members and, as such, have important influence over decision-making. We have considered this a limiting factor because the interests of borrowing members could diverge from those of creditors.

IADB scores somewhat lower in terms of its members' governance standards compared with 'AAA' rated peers that have a more diversified shareholder composition.

That said, the institution has built a track record following the implementation of updated financial and risk measures, which has translated in a more conscious risk-based culture. In our view, this largely counterbalances the potential agency risk stemming from the IADB's borrowing member countries having slightly more than 50% of the voting power on the bank's board.

In 2013, IADB embarked on a roadmap to strengthen its governance and risk management framework, underpinned by its capital adequacy mandate that reaffirmed the bank's commitment to preserving the 'AAA' rating. Central to its mandate was the establishment of capital buffers to facilitate ongoing countercyclical lending in times of need.

The bank implemented various measures to support the rapid buildup of capital buffers, including a change to its policy on disbursing grant funds to Haiti, the transfer of its FSO net assets to its ordinary capital balance sheet, and an exposure exchange agreement to improve sovereign diversification.

In addition, IADB updated its income management model (IMM) in 2015, which integrates income allocation and budgeting decisions (transfers to the grant facility, administrative expenses, and loan charges) with capital accumulation and lending/approval decisions. This has created a more consistent and comprehensive capital management framework and includes clear action plans if capital falls below specified levels.

IADB has demonstrated its willingness to take corrective actions to prevent capital erosion in line with its capital adequacy and IMM policies. In 2015, the bank applied a 30-basis-points retroactive increase on its sovereign loan charges given increasing rating pressures in the region. IADB, unlike many other MLIs, can adjust charges on its entire non-concessional sovereign-guaranteed loan book, which allowed it to generate additional interest revenue to counterbalance rising risks.

IADB also updated other key policies, including its liquidity policy, the investment authority, the asset and liability management framework, and its borrowing authority and borrower limits.

We think the bank demonstrated its strengthened governance and risk management framework in its approach to the situation in Venezuela. Unlike some regional MLIs, IADB did not grant any emergency financing to the country, in line with its established risk and governance principles, although Venezuela is a borrowing member.

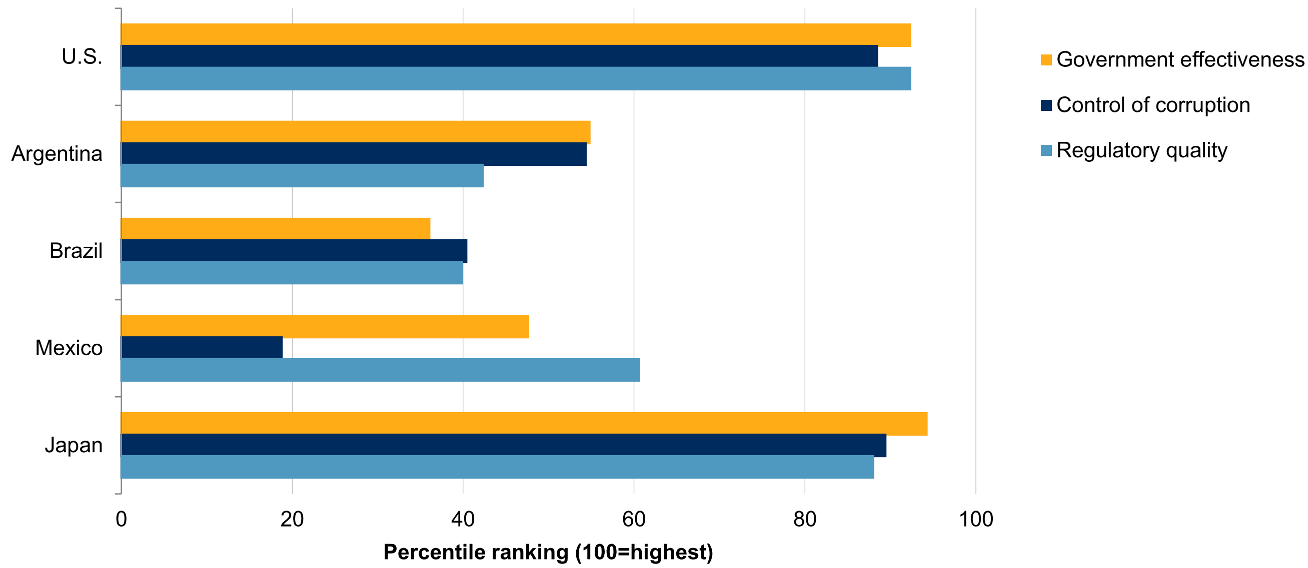
Furthermore, while IADB canceled its 60th annual meeting in China in 2019 given political dynamics stemming from Venezuela's opposition leader Juan Guaido's appointment of a government representative to IADB, we believe this incident will not undermine shareholder support. We also do not think the incident is reflective of potential governance conflicts, since the recognition of the interim government in Venezuela was approved by a supermajority of governors. The postponement of the bank's annual meeting (that took place on July 16-17, 2019, in Guayaquil, Ecuador) resulted in no operational consequences.

The board of governors elects IADB's president. Mr. Luis Alberto Moreno, a citizen of Colombia, is serving his third five-year term following his reelection in July 2015. The U.S. nominated the candidate Mauricio Claver-Carone despite the unwritten tradition of the bank being run by a Latin American. We believe that this will not affect the effectiveness of IADB given the institutional depth to counterbalance political agendas inherent in any multilateral organization.

Together, senior staff possesses considerable expertise and experience.

Chart 2

IADB--Five Largest Shareholders
Selected World Bank governance indicators



Source: S&P Global Ratings.

Financial Risk Profile: Strong Levels Of Capital And Robust Liquidity

- In our view, IADB maintains robust capital levels, which can support additional lending and counterbalance increased risk in the region.
- IADB also has a solid liquidity position, combined with a diverse and active funding program.

Capital adequacy

As of year-end 2019, our RAC ratio for IADB is 19.5%, down 370 basis points (bps) from 23.3% as of December 2018. This is largely due to the recent sovereign downgrades of Argentina, Mexico, and Ecuador. However, we expect the RAC ratio to remain above 15%, which would indicate a very strong capital base.

We expect asset quality to hold up in light of the COVID-19 pandemic, though we expect provisions to increase throughout the year, bringing down the capital generation in 2020.

Following the incorporation of IADB's concessional window into the bank in 2017, the RAC ratio had increased by about 300 bps. The bank has been using this additional capital in its core operations, which led to the lower capital ratio in 2019, in line with our expectation.

Callable capital from IADB's highly rated shareholders would enhance our RAC ratio and mitigate the impact on the bank's financial risk profile in the event that its capital adequacy were to deteriorate.

The bank has a high single-name concentration because of the limited number of borrowing member countries and the distribution of economic activity in the region. IADB's lending is heavily skewed toward Brazil, Mexico, Argentina, Colombia, and Ecuador--which are 65% of the total lending exposure as of 2019, although the bank has made efforts to diversify its lending book.

In 2015, the bank entered into an exposure exchange agreement (EEA) with other MLIs to reduce portfolio concentration by simultaneously exchanging coverage for potential nonaccrual events for exposures from borrowing countries. It executed two bilateral EEA transactions (with IBRD and AfDB), but these transactions remain within 10% of the outstanding loan balance of the sovereign portfolio, and individual country exposures do not exceed the bank's 10th largest sovereign exposure.

As of Dec. 31, 2019, the bank's sovereign- and non-sovereign-guaranteed loans classified as impaired totaled $2.011 billion and $315 million, respectively. (In 2018, they were $2.011 billion and $379 million, respectively.) The sovereign-guaranteed loans impaired are related to Venezuela, and no other sovereign-guaranteed loans were 180 days or more past due, impaired or in nonaccrual status as of December 2019.

Table 1

IADB--RACF (Risk-Adjusted Capital Framework) Data: December 2019

(Mil. US$)	Exposure	S&P Global Ratings RWA	Average S&P Global Ratings RW (%)
Credit risk			
Government and central banks	123,666	170,261	138
Institutions	15,332	5,907	39
Corporate	4,781	6,510	136
Retail			
Securitization	540	228	42
Other assets	873	982	113
Total credit risk	145,191	183,888	127
Credit valuation adjustment			
Total credit valuation adjustment			
Market risk			
Equity in the banking book			
Trading book market risk			
Total market risk			
Operational risk			
Total operational risk		8,408	
Risk transfer mechanisms			
Risk transfer mechanisms RWA			
RWA before MLI adjustments		192,297	100
MLI adjustments			
Single name (on corporate exposures)		1,097	17
Sector (on corporate portfolio)		(273)	(4)

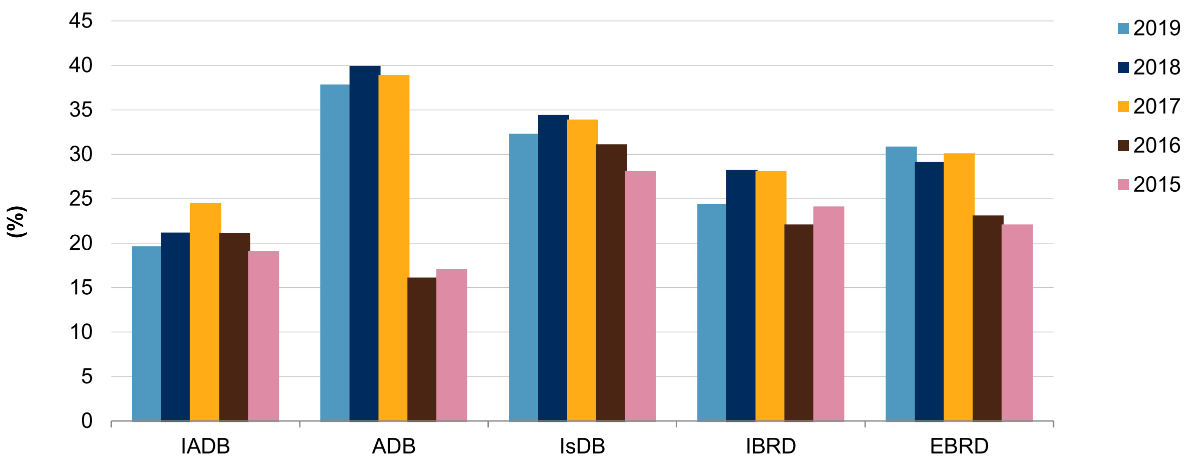
Table 1

IADB--RACF (Risk-Adjusted Capital Framework) Data: December 2019 (cont.)		
Geographic	(19,759)	(11)
Preferred creditor treatment (on sovereign exposures)	(86,636)	(51)
Preferential treatment (on FI and corporate exposures)	(907)	(7)
Single name (on sovereign exposures)	86,806	51
Total MLI adjustments	(19,672)	(10)
RWA after MLI adjustments	172,625	90
	Total adjusted capital	**S&P Global Ratings RAC ratio (%)**
Capital ratio before adjustments	33,707	17.5
Capital ratio after adjustments	33,707	19.5

MLI--Multilateral lending institutions. RW--Risk weight. RWA--Risk-weighted assets.

Chart 3

IADB--Risk-Adjusted Capital Ratio Peer Comparison



Source: S&P Global Ratings.

Funding and liquidity

Funding. We estimate that IADB is structurally able to cover its scheduled short-term debt liabilities without recourse to new issuance. Our static funding gap ratio, excluding loan disbursements, was 1.3x at the one-year time horizon as of year-end 2019--unchanged from year-end 2018. The five-year funding gap was 1.35x. With the inclusion of scheduled loan disbursements, the one-year funding ratio drops to 1.09x.

Qualitatively, we view IADB's funding as well-diversified by both geographic market and type of investor, reflecting IADB's frequent issuance in multiple markets and currencies. The bank regularly raises funds in the international capital markets through the issuance of debt securities, with currently 28 U.S. dollar benchmarks outstanding. While 79% of the total debt stock as of year-end 2019 is denominated in U.S. dollars, the bank has bonds in 17 different currencies, supporting our view that it has a global investor base.

The bank has been active in the capital markets in 2020, especially since the announcement of COVID-19 support. IADB issued its largest ever sustainable development bond for $4.25 billion in April.

Liquidity. Under our liquidity stress scenario, IADB would fully cover its balance-sheet liabilities without market access for one year.

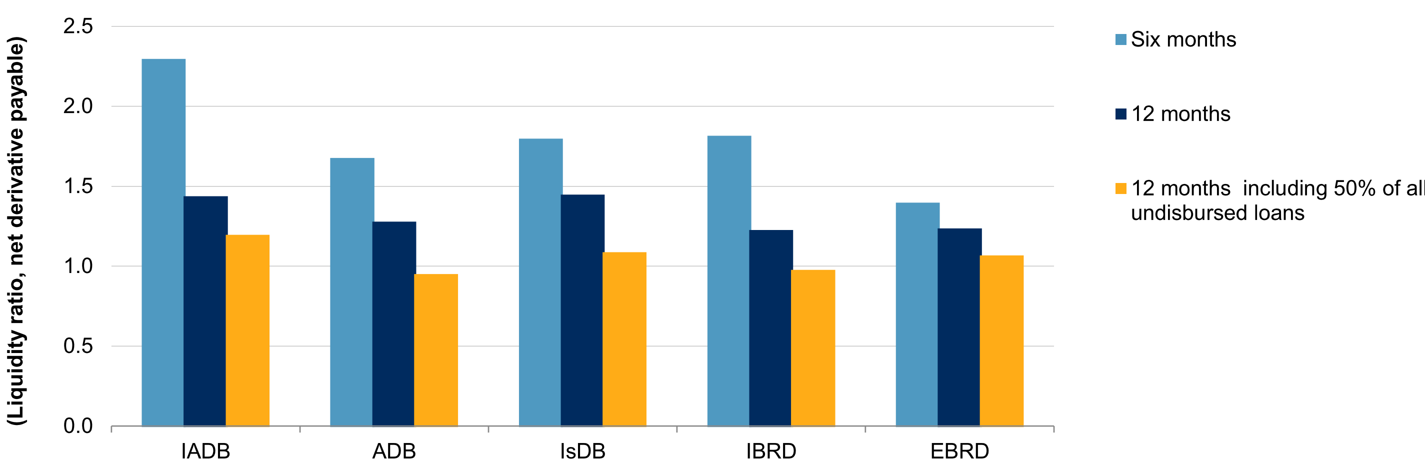
Using year-end 2019 data, our 12-month liquidity coverage ratio is 1.43x, including scheduled loan disbursements, while the six-month ratio is 2.29x. IADB's liquidity has recently been higher, as measured by our additional stress scenario, which takes into account 50% of all undisbursed loans coming due in the next 12 months. But we believe this liquidity might decline and that IADB may need to spread out potential disbursements in a stress scenario.

IADB's liquidity policy was updated in 2015. It calls for the maintenance of liquidity sufficient to cover at least 12 months of debt repayments and loan disbursements with no access to capital markets, although it allows for prefunding to support generally stable funding.

Liquidity, as defined by IADB, for this purpose is nonborrowing countries' convertible currency cash and investments, excluding the assets that the discount note program funds and assets with limited or restricted availability. As of Dec. 31, 2019, the liquid asset portfolio totaled $34 billion--within the policy limits at that time.

Chart 4

IADB--Liquidity Stress Test Ratios Peer Comparison



Source: S&P Global Ratings.

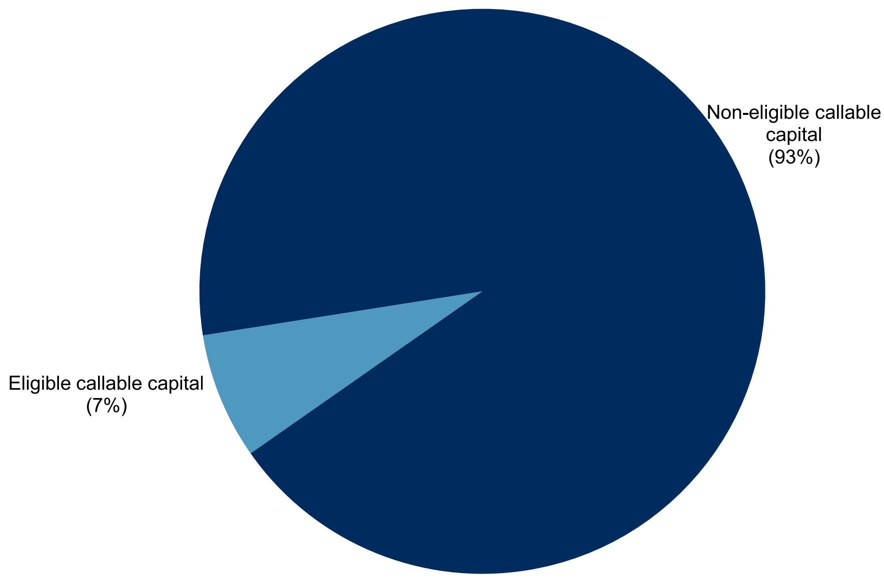
Extraordinary Shareholder Support

We don't factor extraordinary support in the form of callable capital into the rating because IADB, on its own, can achieve our highest assessment. This notwithstanding, callable capital from IADB's highly rated shareholders would enhance our RAC ratio and mitigate the impact on the bank's financial profile in the event that its capital adequacy were to deteriorate.

IADB's largest 'AAA' and 'AA+' rated shareholders include the U.S., Canada, Germany, and the Nordic countries combined. Our measure of eligible callable capital includes sovereigns rated at least equal to an MLI's stand-alone credit profile. For IADB, this would include shareholders rated 'AAA'.

Chart 5

IADB--Callable Capital
As a percentage of total callable capital



Source: S&P Global Ratings.

Table 2

IADB--Selected Indicators

	2019	2018	2017	2016	2015
ENTERPRISE PROFILE					
Policy importance					
Total purpose-related exposure (loans, equity, etc.) (mil. $)	97,221	93,831	89,435	82,182	78,952
Public-sector (including sovereign-guaranteed) loans/purpose-related exposure (%)	94.3	93.9	93.4	92.8	92.4
Private-sector loans/purpose-related exposures (%)	5.7	6.1	6.6	7.2	7.6
Gross loan growth (%)	3.6	4.8	8.7	4.1	5.6
Preferred creditor treatment ratio (%)	2.2	2.3	2.4	N.A	N.A

Table 2

IADB--Selected Indicators (cont.)

	2019	2018	2017	2016	2015
Governance and management expertise					
Share of votes controlled by eligible borrower member countries (%)	50.0	50.0	50.0	50.0	50.0
Concentration of top two shareholders (%)	41.4	41.4	41.4	41.4	41.4
Eligible callable capital (mil. curr)	11,925	11,925	11,925	11,925	11,925
FINANCIAL RISK PROFILE					
Capital and earnings					
RAC ratio (%)	19.5	23.3	24.4	21.0	19.0
Net interest income/average net loans (%)	2.0	1.9	2.2	2.4	2.2
Net income/average shareholders' equity (%)	4.2	2.6	2.1	3.3	3.9
Impaired loans and advances/total loans (%)	2.4	2.6	0.5	0.6	0.6
Liquidity ratios					
Liquid assets/adjusted total assets (%)	26.2	25.4	27.1	24.7	25.7
Liquid assets/gross debt (%)	36.8	36.4	38.5	34.7	36.1
Liquidity coverage ratio (with planned disbursements):					
Six months (net derivate payables) (x)	2.3	3.0	2.9	3.6	4.7
12 months (net derivate payables) (x)	1.4	1.4	1.4	1.5	1.5
12 months (net derivate payables) including 50% of all undisbursed loans (x)	1.2	1.2	1.2	1.2	1.1
Funding ratios					
Gross debt/adjusted total assets (%)	71.2	69.7	70.3	71.0	71.3
Short-term debt (by remaining maturity)/gross debt (%)	18.9	18.2	19.8	15.3	17.6
Static funding gap (with planned disbursements)					
12 months (net derivate payables) (x)	1.3	1.3	1.3	1.4	1.5
SUMMARY BALANCE SHEET					
Total assets (mil. $)	136,358	129,459	126,240	113,325	111,139
Total liabilities (mil. $)	102,487	96,530	93,993	86,865	85,886
Shareholders' equity (mil. $)	33,871	32,929	32,247	26,460	25,253

Source: S&P Global Ratings.

Table 3

IADB--Peer Comparison

	Inter-American Development Bank	Asian Development Bank	Islamic Development Bank	International Bank for Reconstruction and Development	European Bank for Reconstruction and Development
Issuer credit ratings		AAA/Stable/A-1+	AAA/Stable/A-1+	AAA/Stable/A-1+	AAA/Stable/A-1+
Total purpose-related exposure (mil. $)	97,221	121,417	23,163	202,216	36,143
Preferred creditor treatment ratio (%)	2.2	0.1	4.4	0.3	0.0
Risk adjusted capital ratio (%)	19.5	37.7	32.2	24.3	30.7

Table 3

IADB--Peer Comparison (cont.)

	Inter-American Development Bank	Asian Development Bank	Islamic Development Bank	International Bank for Reconstruction and Development	European Bank for Reconstruction and Development
Liquidity ratio 12 months (net derivative payables; %)	1.4	1.3	1.4	1.2	1.2
Funding gap 12 months (net derivative payables; %)	1.3	1.2	2.5	1.3	1.4

Source: S&P Global Ratings.

Ratings Score Snapshot

Enterprise Risk Profile	**Extremely strong**	Very strong	Strong	Adequate	Moderate	Weak	Very weak

Policy Importance	**Very strong**	Strong	Adequate	Moderate	Weak

Governance and Management	**Strong**	Adequate	Weak

Financial Risk Profile	Extremely strong	**Very strong**	Strong	Adequate	Moderate	Weak	Very weak
Capital Adequacy	Extremely strong	**Very strong**	Strong	Adequate	Moderate	Weak	Very weak

Funding and Liquidity	Very strong	**Strong**	Adequate	Moderate	Weak	Very weak

Related Criteria

- Criteria | Governments | General: Multilateral Lending Institutions And Other Supranational Institutions Ratings Methodology, Dec. 14, 2018
- 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: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- How Multilateral Lending Institutions Are Responding To The COVID-19 Pandemic, June 9, 2020
- Can Multilateral Lenders' Capital Bases Hold Up Against COVID-19?, June 9, 2020
- Abridged Supranationals Interim Edition 2020: Comparative Data For Multilateral Lending Institutions, May 8, 2020
- ESG Industry Report Card: Supranationals, Feb. 11, 2020
- Supranationals Special Edition 2019: Report Says MLIs Are Focusing On Sustainable Development Goals, Oct. 25, 2019
- Supranationals Special Edition 2019: Comparative Data For Multilateral Lending Institutions, Oct. 17, 2019
- Introduction To Supranationals Special Edition 2019, Oct. 17, 2019

Ratings Detail (As Of July 16, 2020)*		
Inter-American Development Bank		
Issuer Credit Rating		
Foreign Currency		AAA/Stable/A-1+
Senior Unsecured		AAA
Short-Term Debt		A-1+
Issuer Credit Ratings History		
22-Sep-1997	*Foreign Currency*	AAA/Stable/A-1+
27-Apr-1990		AAA/Stable/--
28-Nov-1962		AAA/--/--

*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.