FitchRatings

RATING ACTION COMMENTARY

Fitch Affirms Inter-American Development Bank at 'AAA'; Outlook Stable

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Fitch Ratings - London - 18 Nov 2021: Fitch Ratings has affirmed Inter-American Development Bank's (IADB) Long-Term Issuer Default Rating (IDR) at 'AAA' with a Stable Outlook and Short-Term IDR at 'F1+'.

KEY RATING DRIVERS

IADB's rating reflects its Standalone Credit Profile (SCP) of 'aaa'. The SCP is underpinned by the bank's solvency assessment of 'aa+', liquidity assessment of 'aaa' and a one-notch positive adjustment to the lower of these two assessments, in this case the solvency assessment, to reflect a 'low' risk business environment.

The Stable Outlook reflects our view that IADB's SCP will remain consistent with its 'AAA' rating, despite the recent increase in leverage and pressures on Latin American sovereign creditworthiness. The bank's large policy response in 2020 highlights the strength of IADB's business profile and public mandate.

In 2020, the bank disbursed a record level of loans totalling USD 14.9 billion to help sovereigns mitigate public health pressures and ameliorate the economic impact from the coronavirus pandemic. The large volume of disbursements in 2020 was well above the pre-pandemic five-year average of USD10.3 billion and led to a rise in leverage (debt-to-equity as calculated by the bank) to 3.3x at end-September 2021 from 2.9x at end-2019. The bank's equity-to-adjusted assets (e/a) ratio similarly fell to 22.1% from 25.2% over the same period and below Fitch's 'excellent' capitalisation threshold of 25%.

Fitch expects lending volumes to be above the pre-pandemic trend but below 2020 levels in 2021 and over the coming years as internal capital generation will not be sufficient to maintain this level of lending growth, given capitalisation and leverage constraints. IADB recently revised its lending spreads upwards by 10bp, which partially offsets the negative impact derived from lower market rates on net interest income. The bank is also exploring options to increase its lending volumes over the medium term, given the strong financing demand from its sovereign borrowers.

The overall capitalisation assessment remains 'excellent' considering the bank's Fitch usable capital to risk-weighted assets (FRA) ratio at 49.3% as of end-September 2021, which is expected to remain well above the 35% threshold for an 'excellent' assessment, despite the prospect of further sovereign downgrades across its loan portfolio. We expect a moderate decline in the FRA ratio but for the e/a ratio to remain close to current levels, consistent with its 'excellent' capitalisation assessment.

Fitch assesses IADB's solvency risks as 'low', given the bank's sovereign lending focus (94.6% of banking exposures as of end-September 2021), 'excellent' preferred creditor status (PCS), 'very low' exposure to market risk, and 'excellent' risk management policies.

The bank's exposure to credit risk is assessed as 'low' and is primarily driven by the 'low' nonperforming loan (NPL) ratio of 2.4% as of end-September 2021, which has historically been below 1.0%. The weighted average rating of loans and guarantees is unchanged at 'BB-' ('BBB-' after PCS uplift) compared with a year prior, despite recent downgrades across key sovereign borrowers such as Colombia (BB+/Stable) and Peru (BBB/Stable).

Exposure to Venezuela (1.9% of total loans) is the only sovereign NPL and accounts for most of the bank's NPLs, while the balance comprises non-sovereign exposures. Fitch expects no new sovereigns NPLs and for the NPL ratio to remain in the 'low' risk category (1-3%)

The risk of further sovereign credit quality deterioration is evidenced by the high number of Latin American sovereigns with Negative Outlooks. One-third of the loan portfolio is to sovereigns with Negative Outlooks, including Brazil (BB-/Negative), the bank's second-largest exposure (14.8% of total loans).

The share of exposures rated 'CCC' or below (15.7% of total loans) also highlights the bank's exposure to distressed sovereigns with very low margin for safety. Fitch expects Argentina (CCC/12.4% of loans) to continue to honour its debt service obligations to the bank, given its record as well as the fact that the sovereign will benefit from positive net disbursements in 2021 and 2022.

Concentration risk has historically been a rating weakness, but has continued to improve, with the five-largest banking exposures now accounting for 53.5% of the total as of end-September 2021 (compared with 64.0% in 2014).

IADB's 'aaa' liquidity assessment reflects the bank's 'excellent' liquidity buffers, the credit quality of its treasury portfolio, and its access to capital markets, all of which compare favourably with 'AAA' rated peers. The ratio of liquid assets-to-short-term debt is expected to remain well above the 1.5x threshold for an 'excellent' assessment through 2024 (2.3x at end-September 2021). The bank raised a record USD26.8 billion in debt issues in 2020.

IADB's overall business environment is assessed as low-risk, which translates into a one-notch positive adjustment from Fitch's solvency assessment. IADB's low-risk business profile is mainly driven by a low-risk strategy, characterised by an almost exclusive focus on sovereign lending and moderate lending growth targets. In addition, our assessment captures IADB's very important policy mandate as the largest multilateral lender for many of the bank's member countries. The importance of the bank's policy mandate has been further evidenced during the coronavirus pandemic as the bank has played a key role in supporting sovereigns with limited market access and growing financing needs. This assessment balances the medium-risk environment in which IADB operates.

Fitch assesses shareholders' support at 'a-', which is based on the weighted average rating of key shareholders (WARKS) as its medium-term forecast for coverage of net debt by callable capital is expected to fall below this level by end-2024 (full coverage from shareholders rated above 'A' at end-September 2021). The WARKS is sensitive to a downgrade of the sovereign rating of the US (AAA/Negative), the bank's largest shareholder. Fitch views shareholders' propensity to support the bank as strong.

RATING SENSITIVITIES

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

The rating is at the highest level on Fitch's scale and cannot be upgraded.

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

- Solvency (Capitalisation): Decline in capitalisation metrics with an equity to assets and guarantees ratio sustained at a level well below 25% and closer to the 15% threshold for a 'strong' assessment, and/or a FRA ratio below 35% that affect our 'excellent' capitalisation assessment. This could be driven by further rise in leverage or significant increase in risk-weighted assets, potentially caused by faster than expected loan growth and/or sovereign downgrades.

- Solvency (Risk): A revision of our 'low' credit risk assessment, caused by either a decline in the average rating of loans and guarantees below 'BB-' or a new breach of PCS on sovereign loans.

- Solvency (Risk): An increase in concentration risk metrics above the 60% 'high' risk threshold as outlined in our criteria, could lead to an overall revision of the 'low' solvency risk assessment. Greater exposure to distressed sovereigns would also be negative for the rating.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Sovereigns, Public Finance and Infrastructure 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 three 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.

Sources of Information

The sources of information used to assess these ratings were IADB's financial statements and other information provided by IADB.

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

IADB has an ESG Relevance Score of '4[+]' for Human Rights, Community Relations, Access and Affordability. The IADB provides concessional loans to its member states owing to contributions provided by its shareholders. It also provides funding to sovereigns that have lost market access. This supports IADB's policy importance and has a positive impact on the credit profile, and is relevant to the ratings in conjunction with other factors.

IADB has an ESG Relevance Score of '4' for 'Exposure to Social Impact'. IADB has a counter-cyclical mandate and development role, as demonstrated by IADB's policy response to the coronavirus crisis as the bank substantially increased loan disbursements in 2020 (in comparison with initial lending plans for 2020). This has a negative impact on the credit profile, and is relevant to the ratings in conjunction with other factors.

IADB has an ESG Relevance Score of '4' for 'Governance Structure'. The US (30% of voting rights) as the largest shareholder exerts a strong influence on the bank's board, management, and strategy. This has a negative impact on the credit profile, and is relevant to the ratings in conjunction with other factors.

IADB has an ESG Relevance Score of '4' for Rule of Law, Institutional & Regulatory Quality. All supranationals attract a score of '4'. Supranationals are neither subject to bank regulation nor supervised by an external authority. Instead, supranationals comply with their own set of rules. Fitch pays particular attention to internal prudential policies, including compliance with these policies. This factor has a negative impact on the credit profile, and is relevant to the ratings in conjunction with other factors.

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
Inter-American Development Bank	LT IDR	AAA Rating Outlook Stable	Affirmed	AAA Rating Outlook Stable
	ST IDR	F1+	Affirmed	F1+
senior unsecured	LT	AAA	Affirmed	AAA

VIEW ADDITIONAL RATING DETAILS

FITCH RATINGS ANALYSTS

Enrique Bernardez, CFA
Director
Primary Rating Analyst
+44 20 3530 1964
enrique.bernardez@fitchratings.com

Fitch Ratings Ltd
30 North Colonnade, Canary Wharf London E14 5GN

Nick Perry
Associate Director
Secondary Rating Analyst
+40 20 3530 2727
nick.perry@fitchratings.com

Theresa Paiz-Fredel
Senior Director
Committee Chairperson
+1 212 908 0534
theresa.paiz-fredel@fitchratings.com

MEDIA CONTACTS

Peter Fitzpatrick
London
+44 20 3530 1103
peter.fitzpatrick@thefitchgroup.com

Additional information is available on www.fitchratings.com

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APPLICABLE CRITERIA

Supranationals Rating Criteria (pub. 20 May 2021) (including rating assumption sensitivity)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Inter-American Development Bank	UK Issued, EU Endorsed

UNSOLICITED ISSUERS

Inter-American Development Bank (Unsolicited)

With Rated Entity or Related Third Party Participation	Yes
With Access to Internal Documents	Yes
With Access to Management	Yes

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UNSOLICITED ISSUERS

ENTITY/SECURITY	ISIN/CUSIP	RATING TYPE	SOLICITATION STATUS
Inter-American Development Bank USD 200 mln 0.5% Notes 17 Apr 2023	XS0165771113	Long Term Rating	Unsolicited
Inter-American Development Bank USD 200 mln 6.75% Notes 15 Sep 2027	US45818QAE98	Long Term Rating	Unsolicited
Inter-American Development Bank USD 500mln 3.875% Notes 28 Oct 2041	US4581X0BT40	Long Term Rating	Unsolicited

ENTITY/SECURITY	ISIN/CUSIP	RATING TYPE	SOLICITATION STATUS

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