MOODY'S
INVESTORS SERVICE

CREDIT OPINION
18 September 2020

Update

Rate this Research

Contacts

Renzo Merino +1.212.553.0330
VP-Senior Analyst
renzo.merino@moodys.com

Giovanni Pagan Velez +1.212.553.4515
Associate Analyst
giovanni.paganvelez@moodys.com

Mauro Leos +1.212.553.1947
Associate Managing Director
mauro.leos@moodys.com

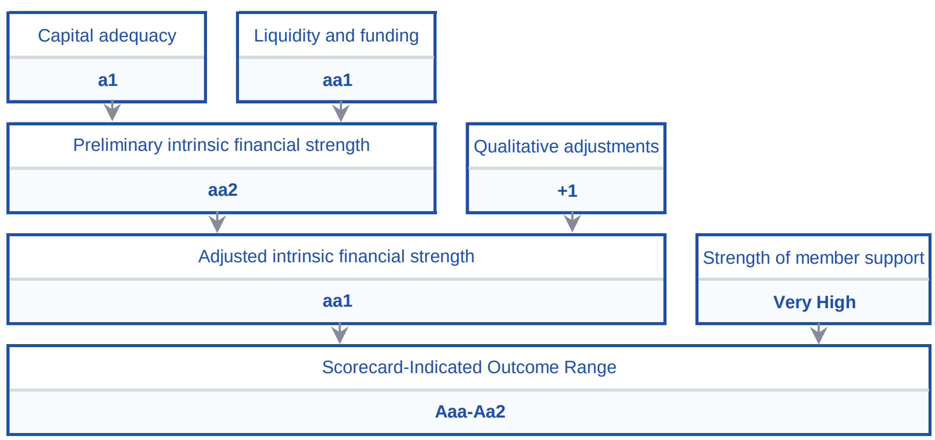
Inter-American Development Bank – Aaa stable

Regular update

Summary

The Inter-American Development Bank (IADB) is one of the premier development institutions focused on Latin America. The Bank's credit profile is underpinned by a strong capital base, solid commitment from shareholders, prudent financial management and preferred creditor status. The IADB's loan book is subject to concentration risk, given its regional lending focus, although this risk is partially offset through an exposure exchange program.

Exhibit 1
Inter-American Development Bank's credit profile is determined by three factors



Source: Moody's Investors Service

Credit strengths

» A solid capital base and preferred creditor status

» Strong commitment from non-borrowing shareholders

» Sound financial management

Credit challenges

» Credit concentration in high-risk countries with volatile macroeconomic environments

» Balancing a development mandate with sound financial practices and reasonable profitability

Rating outlook

The stable outlook reflects our view that the IADB's credit profile will remain supported by the credit quality and support of its shareholders, the institution's ample capital base and its preferred creditor status.

Factors that could lead to a downgrade

Downward pressure on the credit profile could emerge if (1) asset quality were to deteriorate should a large number of the IADB's sovereign-guaranteed loans go into nonaccrual status, or (2) in the case of severe financial stress, member countries were perceived to be unable or unwilling to provide aid to the Bank in the form of contractual or other extraordinary support to preserve its financial health. We consider these low probability outcomes.

Key indicators

IADB	2014	2015	2016	2017	2018	2019
Total Assets (USD million)	106299.0	111116.0	113325.0	126240.0	129459.0	136358.0
Development-related Assets (DRA) / Usable Equity [1]	315.8	312.6	310.6	277.3	284.9	287.0
Non-Performing Assets / DRA	0.2	0.2	0.3	0.3	0.3	0.4
Return on Average Assets	0.5	0.9	0.8	0.5	0.7	1.0
Liquid Assets / ST Debt + CMLTD	184.9	201.6	197.0	190.8	191.5	187.9
Liquid Assets / Total Assets	25.6	25.2	24.2	26.5	24.2	25.2
Callable Capital / Gross Debt	179.7	191.1	205.3	186.5	183.4	170.0

[1] Usable equity is total shareholder's equity and excludes callable capital

Source: Moody's Investors Service

Detailed credit considerations

We assess **capital adequacy** to be "a1," reflecting the Bank's strong asset coverage and performance, and preferred creditor status. The IADB's capital position, measured by the leverage ratio, has been improving over the past few years. Development-related assets represented 287% of equity in 2019, which is the same as the median for Aaa-rated MDBs. IADB compares favorably to large peers such as the World Bank (IBRD, Aaa stable) and the European Investment Bank (Aaa stable) at 475% and 643%, respectively. The IADB's capital adequacy mandate aims to ensure that the Bank has sufficient equity to enable it to maintain its Aaa rating status during times of economic distress.

The Bank's asset performance has been very strong throughout its history, curently scoring "aaa". As of year-end 2019, the nonperforming assets (NPA) ratio was 0.4%. Historically, NPLs have corresponded to the Bank's non-sovereign guaranteed loan book. However, in May 2018, the IADB announced that Venezuela had missed payments on its loans for over 180 days, placing the sovereign in nonaccrual status. This was the first sovereign to hold that designation since Suriname (Caa3 negative) cleared its arrears with the Bank in 2001. The IADB's extraordinary repayment record is explained by the special relationship that it enjoys with its borrowing countries, reflected by its preferred creditor status. Historically, borrowing countries have been less likely to default on IADB loans than on their financial obligations with commercial or private creditors, with only five sovereigns ever going into nonaccrual status.

We score the IADB's development asset credit quality "baa". The initial basis of our assessment is a weighted average borrower rating of B1. We consider that the IADB's preferred creditor status vis-à-vis its sovereign borrowers strengthens the portfolio's credit quality. Additionally, the IADB participates in an exposure exchange agreement (EEA) with the IBRD and the African Development Bank (AfDB, Aaa stable). The EEA is designed to address the IADB's main credit challenge – namely, the high degree of concentration in its lending portfolio. Ten countries consistently account for around 80% of the total (closer to 70% including the EEA), including Brazil (Ba2 stable), Mexico (Baa1 negative) and Argentina (Ca negative), which have historically been the Bank's largest public sector borrowers. However, the Bank has shown a declining trend in concentration levels, particularly in terms of the top three largest borrowers. The

EEA synthetically exchanges risk between the IADB, the IBRD and the AfDB, helping decrease the IADB's geographic concentration. Overall, strong capital levels on the IADB's balance sheet and active management of its concentration risks combined with the largely sovereign-guaranteed nature of its loan portfolio places the Bank's capital adequacy in a strong position.

Our assessment of **liquidity** is “aa1,” recognizing the Bank's strong liquidity position as a result of a conservative liquidity risk management policy and its ample market access. We assess IADB's liquidity coverage to be strong in case of a stress scenario, which would include the Bank not being able to tap financial markets and also exclude scheduled cash inflows from shareholders. IADB's liquid resources ratio, which sizes its high-quality liquid assets relative to its net outflows from uninterrupted net loan disbursements, debt repayment and administrative costs, shows that the Bank holds enough assets to sustain its functioning for 18 months.

We consider that IADB's market access is one of the strongest within the supranational universe, scored at “aaa”. The IADB maintains a relatively large borrowing program, can access market funding at low costs, has a diversified investor base by type and geography and is able to issue in over 20 currencies.

Combining capital adequacy and liquidity and funding scores, we position IADB's intrinsic financial profile at “aa2”, among the highest in our rated universe. The qualitative factors that we additionally consider include an MDB's operating environment and the quality of its management. We do not apply an adjustment for the operating environment. We assign a “+1” adjustment due to the quality of management, to reflect IADB's very strong willingness and capacity to adopt best-in-class practices, and also its practice of proactive update of risk policies to adapt to changing financial and economic conditions affecting its own credit profile and that of its borrowing members

Finally, we assess **strength of member support** to be “Very High”, above the scorecard indicated “High”. Our score reflects the Bank's favorable member base profile, which counts as members both borrowing and non-borrowing countries. Members' willingness to provide support is very strong. Contractually, the IADB has an ample callable capital buffer in the very unlikely event of significant asset deterioration. We also consider that members have demonstrated a track record of willingness to provide extraordinary support to the Bank, through several capital increases, and also the Bank's unique ability to modify the loan charge's structure – members, including borrowing ones, have to agree to reprice the lending spread on its portfolio – to support the Bank's capital base. We also consider that members, including the United States (Aaa stable) as the largest member, have a very strong sense of ownership and assign a high economic importance to the IADB. Finally, we assess members' willingness to provide extraordinary support as very high, as reflected in members' recent capital increases and the economic scale of key member countries. This compensates for a moderate ability to support from the whole member base as reflected by a weighted average shareholder rating of Ba1.

ESG considerations

How environmental, social and governance risks inform our credit analysis of IADB

Moody's takes account of the impact of environmental (E), social (S) and governance (G) factors when assessing supranational issuers' credit profile. In the case of the Inter-American Development Bank, the materiality of ESG to the credit profile is as follows:

Environmental considerations are not material for IADB’s rating. However, we note that as part of its mission, the IADB has committed to increase its lending for projects that look to address or mitigate climate change risks in the Latin American region, with a target approved by the Governors which states that 30% of the Bank's projects should have a climate change component.

Social considerations are not material for IADB’s rating. While we regard the coronavirus outbreak as a social risk under our ESG framework given the substantial implications for public health and safety worldwide, we do not expect these considerations to materially affect IADB's capital adequacy or liquidity.

Governance is very strong and a key driver of IADB’s Aaa rating. We have adjusted the quality of management upwards by one notch from the level indicated by the scorecard to reflect the IADB’s superior institutional strength and best-in-class practices.

All of these considerations are further discussed in the “Detailed credit considerations” section above. Our approach to ESG is explained in our cross-sector methodology General Principles for Assessing ESG Risks. Additional information about our rating approach is provided in our Rating Methodology for Multilateral Development Banks and other Supranational Entities.

Recent developments

Balance sheet developments during H1 2020

As of 30 June 2020, loans outstanding were $97.9 billion, higher than the $95 billion in loans outstanding at this point in 2019. These development assets represented 289% of equity, slightly above the 283% of equity in June of 2019.

Loans and guarantees approved totaled $7.5 billion at the end of the second quarter, which is about half of the bank's $15.5 billion approval target for 2020. By September 10th, loan approvals were $10.2 billion – representing two-thirds of the approvals target. Despite the expansion of the loan book in response to the coronavirus pandemic, impaired non-sovereign guaranteed (NSG) exposures amounted to $319 million (5.5% of $5.8 billion in total NSG exposures) as of June 2020, lower than the $390 million in impaired NSG exposures in June of 2019 (6.3% of $6.2 billion) – this development is in line with the consolidation of the IADB Group's private sector operations within the IDB Invest (IIC, Aa1 stable).

As of 30 June 2020, the IADB issued bonds for a total of $17.8 billion, compared to $10.8 billion in the same period last year. The IADB expects to issue $27 billion in 2020 in order to fund its response to the coronavirus pandemic.

Total equity for the IADB was $33.8 billion by the end of Q2, slightly below the $33.9 billion at the end of 2019. Net loss for the bank during the first half of 2020 was $49 million, markedly lower than the $769 million in net income in H1 2019. While Operating income during H1 2020 was $247 million, down from $531 million in H1 2019. The decrease was mainly due to a lower loan net interest margin, which decreased by $88 million to $736 million from $824 million for the six month period last year, as well as loan loss provisions of $132 million.

IADB's coronavirus response centered on financial support

The IADB's response to the coronavirus pandemic has centered on providing financial support to Latin American sovereigns while also maintaining the solid capital and liquidity measures that allow it to execute its core mission. The Bank's strategy has been to prioritize disbursement of approved projects, redeployed to address coronavirus priorities in some cases. The Bank has also adopted measures to increase the policy-based lending limit, streamline the approval process of loans, and expand contingent credit facilities to address the coronavirus pandemic. As a result, program execution by the end of June was already over 50% of the 2020 lending approved by the Board of Directors – compared to just 36% in the same period in 2019.

Of the loans approved in H1 2020, 54% were dedicated to coronavirus-related lending. Coronavirus-related loans have been devoted to 5 key priority areas: Vulnerable populations (18% of total loan approvals), Productivity (14%), Fiscal Management (9%), Special Development (8%), and Immediate Public Health Response (4%).

Rating methodology and scorecard factors

Rating factor grid - Inter-American Development Bank	Initial score	Adjusted score	Assigned score
Factor 1: Capital adequacy (50%)		a1	a1
Capital position (20%)		baa1	
Leverage ratio	baa1		
Trend	0		
Impact of profit and loss on leverage	0		
Development asset credit quality (10%)		baa	
DACQ assessment	baa		
Trend	0		
Asset performance (20%)		aaa	
Non-performing assets	aaa		
Trend	0		
Excessive development asset growth	0		
Factor 2: Liquidity and funding (50%)		aa1	aa1
Liquid resources (10%)		aa3	
Availability of liquid resources	aa3		
Trend in coverage outflow	0		
Access to extraordinary liquidity	0		
Quality of funding (40%)		aaa	
Preliminary intrinsic financial strength			aa2
Other adjustments			1
Operating environment	0		
Quality of management	+1		
Adjusted intrinsic financial strength			aa1
Factor 3: Strength of member support (+3,+2,+1,0)		High	Very High
Ability to support - weighted average shareholder rating (50%)		ba1	
Willingness to support (50%)			
Contractual support (25%)	aaa	aaa	
Strong enforcement mechanism	0		
Payment enhancements	0		
Non-contractual support (25%)		Very High	
Scorecard-Indicated Outcome Range			Aaa-Aa2
Rating Assigned			Aaa

Note: Our ratings are forward-looking and reflect our expectations for future financial and operating performance. However, historical results are helpful in understanding patterns and trends of an issuer's performance as well as for peer comparisons. Additional considerations that may not be captured when historical metrics are used in the scorecard may be reflected in differences between the adjusted and assigned factor scores. Furthermore, in our ratings we often incorporate directional views of risks and mitigants in a qualitative way. For more information please see our Multilateral Development Banks and Other Supranational Entities rating methodology.

Moody's related publications

- **Sector In-Depth:** Supranationals – Global: Stress-testing confirms broad resilience of MDB ratings, 1 September 2020
- **Sector Comment:** Sovereigns – Global: Rising multilateral development bank climate financing will support climate-vulnerable sovereigns' resiliency, 21 August 2020
- **Issuer In-Depth**: Inter-American Development Bank - Aaa stable: Annual credit analysis, 30 March 2020
- **Rating Methodology**: Multilateral Development Banks and Other Supranational Entities, 25 June 2019

REPORT NUMBER 1244954

MOODY'S
INVESTORS SERVICE