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Research Update:

Credit Guarantee and Investment Facility 'AA/A-1+' Ratings Affirmed; Outlook Stable

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Overview

- The ratings on CGIF reflect CGIF's mandate from ASEAN+3 countries to help develop local bond markets, the entity's conservative guarantee and investment strategies, and operational support from the AsDB. Balancing these strengths is its short track record and some concentration risk.
- CGIF has an extremely strong financial profile and an adequate business profile by our assessment, resulting in a 'aa' stand-alone credit profile.
- We are affirming our 'AA/A-1+' foreign currency and 'axAAA' ASEAN regional scale ratings on CGIF.
- The stable outlook reflects our view that the risks to the rating on CGIF are balanced over the next 24 months.

Rating Action

On June 19, 2015, Standard & Poor's Ratings Services affirmed its 'AA' long-term and 'A-1+' short-term issuer credit ratings on the Credit Guarantee and Investment Facility (CGIF). The outlook is stable.

At the same time, we affirmed our 'axAAA' long-term ASEAN regional scale credit rating on CGIF.

Rationale

The ratings on the CGIF reflect our assessment of the facility's business profile as adequate and its financial profile as extremely strong, as our criteria define these terms. In combining these assessments, we assess the stand-alone credit profile as 'aa'. The ratings do not benefit from extraordinary support as CGIF does not have callable capital.

CGIF is a supranational institution with a mandate to develop deep and liquid local currency bond markets in the ASEAN region. It achieves this by providing guarantees on local currency denominated bonds issued by companies in the region. As of December 2014, a little over four years since the facility's inception, it had issued seven guarantees in the markets of Singapore, Thailand, Indonesia, and Vietnam.

Our assessment of CGIF's business profile as adequate rests on our view of its role, mandate, governance, and the strength of its relationship with its contributors. CGIF is established as a trust of the Asian Development Bank (AsDB). We believe that CGIF's creditworthiness benefits from its relationship with its contributors and the mandate they have entrusted it with. The voting rights are dominated by four contributors: China (28.6%), Japan (28.6%), Korea (14.3%), and the AsDB (18.6%). The 10 ASEAN governments collectively have the last 10%. However, the contributors' commitment to CGIF is limited to their capital contribution.

The facility has a relatively short track record of fulfilling its policy mandate given it was only established in 2010. Although CGIF has more transactions in the pipeline, we believe that the deepening of the ASEAN bond markets by credit enhancement, and therefore the role of the institution, will be more limited than originally envisioned. The relative small size of its capital base (US$700 million) suggest that CGIF's role is meant to be catalytic rather than deepening capital markets through volume.

CGIF's articles of agreement delineate its governance standards. The management team has the necessary expertise and experience to conduct its business in order to achieve its mandate. Its guarantee operations are controlled by conservative risk parameters. The management has also chosen to grow at a gradual pace, allowing its staffing capacity to catch up to the scale of operations. Treasury portfolio management is delegated to the AsDB, which results in very conservative investment policies.

We assess CGIF's financial profile as extremely strong. The facility's risk-adjusted capital (RAC) ratio was 74% before adjustments at year-end 2014. After adjustments specific to multilateral institutions, CGIF's RAC ratio falls to 32%, which is still extremely strong. The main adjustment is its single-name exposure to the portfolio of guarantees for regional corporates, inherent to its start-up nature. Although CGIF's RAC ratio could fall over the next two years as its guarantee portfolio expands, we expect that a potential capital increase could compensate the deterioration, and support our assessment of an extremely strong financial profile.

Unlike supranational institutions that mainly lend directly to governments, CGIF may not benefit from preferred creditor treatment, in our view. Private-sector companies cannot expect multilateral institutions to be a lender (or guarantor) of last resort. Hence, we envisage potential future losses on the guaranteed bonds to commensurate with market trends. The CGIF had run small yearly profits since inception and we expect it to maintain its profitability.

Our assessment of CGIF's funding and liquidity also informs our view of its extremely strong financial profile. CGIF does not borrow. It obtains funding for its activities solely through contributors' equities and retained earnings. Our liquidity ratios indicate that the CGIF would be able to pay out its guarantees for at least a year under stressed market conditions, without recourse to liquidity facilities from contributors or from the market. Its liquid assets, managed by the AsDB, are invested mostly in bonds of highly rated governments or government-related entities. They form the bulk of its balance-sheet assets as of year-end 2014.

Outlook

The stable outlook reflects our view that the risks to the rating on CGIF are balanced over the next 24 months. Any changes to the rating will likely be determined by our projections on the facility's capital adequacy and the effectiveness of its role in local currency regional capital markets.

Downside scenario

We may lower the rating if: (1) CGIF struggles to execute its mandate at a profit; or (2) its financial metrics weaken more than we expect, which may happen with the facility accumulating a guarantee portfolio with lower credits, or without a commensurate increase in capital.

Upside scenario

Upward pressure on the rating could emerge when CGIF has built a track record and an ability to significantly contribute to a vibrant local currency regional capital market.

Related Criteria And Research

Related Criteria

- Multilateral Lending Institutions And Other Supranational Institutions Ratings Methodology, Nov. 26, 2012
- Bank Capital Methodology And Assumptions, Dec. 6, 2010

Related Research

- Asian Development Bank 'AAA/A-1+' Ratings Affirmed, Outlook Stable, June 3, 2014

Ratings List

Ratings Affirmed

Credit Guarantee and Investment Facility	
Issuer Credit Rating	
Foreign Currency	AA/Stable/A-1+
ASEAN Regional Scale	axAAA/--/--

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