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Research Update:

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

Primary Credit Analyst:
YeeFarn Phua, Singapore (65) 6239-6341; yeefarn.phua@spglobal.com

Secondary Contact:
Rain Yin, Singapore (65) 6239-6342; rain.yin@spglobal.com

Research Contributor:
Harshleen K Sawhney, CRISIL Global Analytical Center, an S&P Global Ratings affiliate, Mumbai

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Overview

- CGIF continues to execute guarantees to catalyze the ASEAN corporate bond market, fostering economic development in the region.
- CGIF has an extremely strong financial profile underpinned by increasing capital injections. In our view, CGIF has an adequate business profile because it lacks an established track record and faces some concentration risk due to its small size.
- We are affirming our 'AA/A-1+' foreign-currency issuer credit ratings on CGIF.
- The stable outlook reflects our expectation that CGIF will maintain a solid balance sheet and prudent risk-management practices as it pursues new business growth over the next 24 months.

Rating Action

On Feb. 26, 2020, S&P Global Ratings affirmed its 'AA' long-term and 'A-1+' short-term foreign-currency issuer credit ratings on Credit Guarantee and Investment Facility (CGIF). The outlook remains stable.

Rationale

We affirmed the ratings to reflect CGIF's adequate enterprise risk profile and extremely strong financial risk profile. CGIF has no callable capital, so the long-term issuer credit rating reflects our assessment of CGIF's stand-alone credit profile at 'aa'.

Constraining CGIF's adequate enterprise risk profile is its relatively short track record of fulfilling its policy mandate compared with other supranational institutions. We believe that the deepening of the Association of Southeast Asian Nations (ASEAN) bond markets by credit enhancement will remain limited, and as such, CGIF's role could partially be filled by a commercial entity. CGIF acts as a catalyst for bond deals, rather than for deepening the capital markets through volume.

Established in November 2010, CGIF's mandate is to help deepen and develop liquid local-currency bond markets among ASEAN members. CGIF provides guarantees on bonds issued by corporates in the ASEAN region. As of February 2020, CGIF has issued 37 guarantees in Singapore, the Philippines, Thailand, Indonesia, and Vietnam. The guaranteed amount typically ranges between US$50 million and US$100 million, and generally has a tenor of three to 10 years.

CGIF was set up as a trust fund of the Asian Development Bank (ADB). We believe that CGIF's creditworthiness benefits from its relationship with its contributors and the mandate they have entrusted it with. CGIF has a balanced shareholder base and all the shareholders are either governments or government-related agencies with strong government links. The current voting rights are dominated by four contributors: China (32.5%), Japan (32.5%), Korea (9.5%), and ADB (17.1%). The 10 ASEAN governments collectively hold the remaining voting rights (8.4%).

CGIF's shareholders have demonstrated their support by approving its first capital increase to US$1.2 billion from US$700 million in December 2017. The subscription increase is voluntary, and proposed to be a proportional increase across all current shareholders. Shareholder payments are likely to be completed by the end of 2023. By increasing its capital, CGIF's guarantee capacity will be boosted to US$3 billion, from the previous capacity of US$1.75 billion. As of Sept. 30, 2019, 10 shareholders had subscribed to the increase and paid-in capital reached US$1.05 billion. In our view, the successful completion of this exercise will demonstrate a strong track record of shareholder support.

CGIF renewed its annual reinsurance arrangement with a syndicate of reinsurers rated between 'AA-' and 'A' to boost its guarantee capacity and manage credit concentration risk limits. This arrangement covers 25% of the existing guarantee portfolio and all new guarantees written up until the end of 2020. Current country and currency exposures have been alleviated by approximately 25% as a result of the transfer of exposure to the reinsurers. Coupled with the capital increase, these two measures will enhance CGIF's guarantee capacity.

CGIF's private-sector focused mandate excludes it from being treated as a preferred creditor, given that private-sector companies cannot selectively default to one group of creditors while paying others as sovereigns can. Hence, we do not incorporate preferred creditor treatment in our assessment of CGIF's enterprise risk profile. However, given CGIF's status as a multilateral lending institution, we consider preferential treatment granted by the governments of countries in which CGIF operates, which we incorporate into our assessment of its financial risk profile.

We believe CGIF's management team has the necessary expertise and experience to conduct the facility's business and achieve its mandate. That said, CGIF has a short track record of operations. Its guarantee operations are controlled by conservative risk parameters in accordance with governance standards laid out in its articles of agreement. CGIF has expanded at a gradual pace, allowing its staffing capacity to catch up with the scale of operations. ADB manages CGIF's capital, which results in conservative investment policies.

We consider CGIF's extremely strong financial profile to be a positive rating factor. The facility's risk-adjusted capital (RAC) ratio after diversification increased to 40.4% as of year-end 2018, from 39.2% the year before. This was well above our threshold for an extremely strong capital adequacy assessment (23%). CGIF's RAC ratio has remained broadly stable because the increase in guarantees has been counterbalanced by the increase in capital. We expect this trend to continue over the next few years, and the RAC ratio to remain above our threshold of 23%.

CGIF's asset quality has so far been pristine. No bond issuance has defaulted and required the payout on CGIF's guarantees during its 10 years of existence. We believe this to be a result of the guaranteed exposure representing the main companies in the region with relatively high ratings as well as CGIF's conservative risk appetite. Should a default occur, we take some comfort in the fact that the typical sizes of each issue are 7%-11% of the capital levels today.

CGIF does not borrow; it obtains funding for its activities solely through retained earnings and contributors' equity. While we believe sovereign and supranational backing provides one of the most stable sources of funding, this model also represents a concentration risk that could be tested in severe stress. We assign a neutral funding score because we believe the positive factor of paid-in capital base is counterbalanced by the lack of access to the wholesale market.

We assess CGIF's liquidity position as robust. Our liquidity ratios indicate that CGIF would be able to comfortably pay out its guarantees for at least a year under stressed market conditions, without recourse to liquidity facilities from contributors or from the market. As of end-June 2019, our calculated 12-month stressed liquidity ratio for CGIF was 16x. The facility's liquid assets, managed by ADB, are invested mostly in bonds of highly rated governments or government-related entities. They form the bulk of CGIF's balance sheet assets.

Outlook

The stable outlook on CGIF reflects our expectation that the facility will maintain a solid balance sheet and prudent risk-management practices as it pursues new guarantee growth over the next 24 months. We believe changes to the rating will most likely be driven by the effectiveness of CGIF's role in the local-currency ASEAN bond markets.

Downside scenario

We may lower the rating if CGIF struggles to execute its mandate at a profit or its financial metrics weaken. This could happen if the facility aggressively expands its guarantee portfolio beyond the natural growth capacity provided with the likely increase in capital.

Upside scenario

Upward pressure on the rating could emerge if we assess that CGIF's policy importance has strengthened, with significant contributions to a vibrant local-currency regional capital market backed by ongoing shareholder support and the establishment of a track record.

Ratings Score Snapshot

Issuer Credit Rating	AA/Stable/A-1+
SACP	aa
Enterprise Risk Profile	Adequate
Policy Importance	Adequate
Governance and management	Adequate
Financial Risk Profile	Extremely Strong
Capital Adequacy	Extremely Strong
Funding and Liquidity	Strong
Extraordinary Support	0
Callable capital	0
Group Support	0
Holistic Approach	0

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

- 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 List

Ratings Affirmed

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

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.