FitchRatings

Insurance
Financial Guarantors
Philippines

Credit Guarantee and Investment Facility

Key Rating Drivers

Leverage to Stay Manageable: Fitch Ratings Indonesia expects Credit Guarantee and Investment Facility (CGIF) to judiciously manage its net par/capital leverage ratio – defined as total outstanding guarantee exposure after reinsurance relative to members' equity – as its guarantee portfolio expands. Fitch expects the ratio, which stood at 1.6x at end-2021, to remain at or below 2.0x.

Prudent Investment Strategy: CGIF invests only in fixed-income securities with maturities of more than one year that are rated at least 'A+' on an international scale for government-related issuers of CGIF contributor countries and 'AA-' for other issuers. Its investments in short-term fixed-income instruments cannot be lower than 'F1' on Fitch's rating scale.

Operational Linkage with ADB: CGIF is set up as a trust fund of the Asian Development Bank (ADB, AAA/Stable) rather than as a separate, independent legal entity. Therefore, ADB has close ties with CGIF and provides strong operational support. ADB appoints CGIF's staff and manages its funds and assets. These linkages reduce risks as CGIF's operation is conducted according to its policies and all applicable ADB operational policies, and it shares the bank's multilateral supranational status.

High-Risk Insured Portfolio: CGIF's insured portfolio is exposed to issuers with non-investment-grade ratings, as it provides largely local-currency-denominated guarantees on emerging-market Asian debt. CGIF is exposed to volatile credit risks because it guarantees non-investment-grade corporate issuance.

It is also exposed to foreign-currency risk, as it provides local currency-denominated guarantees to emerging markets. However, the risk is low because any reduction in the US dollar value of guarantee fees receivable due to the depreciation of a local currency against the US dollar is counterbalanced by the reduction in the US dollar amount of the principal guaranteed.

Diversified Ownership Structure: CGIF's initial capital of USD700 million was contributed by ADB and various ASEAN + 3 (China, Japan and South Korea) sovereign nations, several of which are highly rated. The funds were used to form CGIF to support the development of ASEAN + 3 capital markets. The contributors have committed to raise CGIF's paid-in capital to USD1.2 billion by end-2023.

Ratings

Credit Guarantee and Investment Facility

National IFS Rating	AAA(idn)
National Long-Term Rating	AAA(idn)

Outlooks

National IFS Rating	Stable
National Long-Term Rating	Stable

Financial Data

Credit Guarantee and Investment Facility

(USDm)	2021 Audited	2020 Audited
Total equity	1,292	1,264
Total assets	1,373	1,351
Return on equity (%)	2	2
Net income	30	24

Source: Fitch Ratings, Fitch Solutions, CGIF

Applicable Criteria

Insurance Rating Criteria (July 2022)

National Scale Rating Criteria (December 2020)

Related Research

Global Insurance 2023 Outlook Compendium (January 2023)

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Rating Sensitivities

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade:

- A surge in after-reinsurance notional insured par/capital leverage ratio to consistently higher than 6x;
- Losses in the guarantee portfolio adversely deviating from the company's expectation;
- Material increase in reliance on reinsurance protection for a prolonged period.

Factors that Could, Individually or Collectively, Lead To positive Rating Action/Upgrade:

- CGIF's ratings are already at the highest possible level and therefore cannot be upgraded.

Company Profile

'Moderate' Business Profile and 'Moderate/Favourable' Corporate Governance

Fitch ranks CGIF's business profile as 'Moderate', factoring in our view of CGIF's competitive position, business risk and diversification as 'Moderate'.

Substantive Business and Smaller Operating Scale

CGIF was established in 2010 to support the development of debt capital markets in the ASEAN + 3 region by providing financial guarantees on debt issues. It commenced operations in 2012 and wrote its first bond guarantee in 2013. Its capitalisation of USD1.2 billion is above that of a guarantor with a 'Favourable' operating scale, while its revenue aligns with that of a 'Least Favourable' operating scale. However, we regard CGIF as a much larger organisation, based on operational infrastructure, in light of its linkage with ADB.

Premiums from the guarantee business amounted to USD19.4 million in 2021. Fitch expects CGIF to build up its operating record steadily in the bond guarantee segment as its coverage expands. CGIF targets first-time issuers without, or with limited, local bond-market access and mainly supports corporates in south-east Asia as well as China, Korea and Japan.

CGIF provides guarantees to existing issuers to extend their bond maturities, expand their investor base, and support cross-border transactions.

Risk Appetite on a Par with Insurance Sector

Fitch regards CGIF as unique, as it is sponsored and operated by ADB, an established multilateral supranational. CGIF is set up as a trust fund of ADB rather than as a separate, independent legal entity. Hence, it is accorded the same supranational status, as incorporated under Article 13.2 of its Articles of Association, which states that "the privileges, immunities, and exemptions accorded to ADB pursuant to the Agreement Establishing the Asian Development Bank shall apply to (i) the Trustee, and (ii) the property, assets, archives, income, operations and transactions of CGIF". The organisation, like the ADB, is not subject to the laws of the Philippines, where it is based, and, as such, is immune from taxation, local business laws and bank or insurance regulations.

ADB has close ties with CGIF and provides strong operational support, appointing staff as well as holding in trust and managing CGIF's funds and assets, as set out in the Articles of Association. CGIF's risk-management culture and procedures are largely adopted from ADB.

Fitch also thinks CGIF's growth strategy is more favourable than that of commercial operators. There is no time pressure from ADB or the capital contributors to quickly utilise capital for guaranteeing bond obligations, giving CGIF leeway to carefully select the issuance it guarantees, instead of adopting an aggressive or fast-growth path. This approach is in line with ADB's philosophy.

Nonetheless, CGIF is focused on undeveloped business segments, as the use of debt guarantees in ASEAN + 3 is limited. This carries higher-than-average risk of making an adverse selection, as it is difficult to judge the business viability of the companies that seek to issue insured debt. This risk is core to CGIF's business model and is not mitigated by operational linkages with ADB. CGIF guarantees bonds in diverse sectors, including telecommunications, financial institutions and healthcare. It also supports cross-border transactions within its target markets by looking for opportunities to provide guarantees to local corporations.

'Moderate/Favourable' Corporate Governance

Fitch considers CGIF's corporate governance to be effective and neutral to the ratings. The governance structure consists of the meeting of contributors, an eight-member board, three board committees and two management committees. The board comprises the CEO, two representatives, each from China and Japan, and one each from ASEAN, Korea and ADB. These country representatives are from the ministries of finance or development banks. The board meets at least three times a year.

Ownership

Japan, China and Korea contributed around 75% of the capital. The number of votes for each contributor is equivalent to the proportion of its capital contribution. Hence, the largest contributors retain the strongest decision-making power.

Callable capital facilities are used for some supranational organisations, but CGIF's capital providers chose not to use such an approach.

CGIF Capital Contributors at End-November 2022

	(%)	Rating/Outlook
ADB	15.72	AAA/Stable
Japan	29.94	A/Stable
China	29.94	A+/Stable
Korea	14.97	AA-/Stable
Brunei Darussalam	0.49	n.a.
Cambodia	0.02	n.a.
Indonesia	1.62	BBB/Stable
Lao People's Democratic Republic	0.02	n.a.
Malaysia	1.54	BBB+/Stable
Republic of the Union Myanmar	0.01	n.a.
Philippines	1.89	BBB/Negative
Singapore	1.89	AAA/Stable
Thailand	1.81	BBB+/Stable
Vietnam	0.17	BB/Positive
Total	100.00	

Source: Fitch Ratings, Fitch Solutions, CGIF

Capitalization and Leverage

CGIF guaranteed 52 bonds amounting to a cumulative total of USD2.6 [1]billion by end-2021, including bonds denominated in Singapore dollars, Vietnamese dong, Philippine peso, Japanese yen, Cambodian riel, Thai baht, Malaysian ringgit, Chinese yuan and Indonesian rupiah. The guaranteed bonds had average tenures of three to 10 years and were issued by corporations in various sectors, including telecommunications and automobiles. CGIF's net par/capital leverage rose to 1.6x by end-2021, from 1.1x at end-2020, although several transactions were still in the pipeline.

CGIF contributors approved a USD500 million increase in CGIF's authorised capital in light of its growth pace, which will increase total capital to USD1.2 billion when the additional capital is fully subscribed by end-2023. The capital increase is implemented in stages, with the first paid-in capital made in December 2017. The current capital amount may be sufficient for CGIF's business, while the second round of increase in the paid-in capital will provide additional support.

Financial Highlights

(USDbn)	2021	2020
Total shareholders' equity	1.3	1.3
Notional insured par [a]	2.3	2.3
Net par/capital leverage (x)	1.6	1.1
Financial leverage (%)	0	0

[a] Maximum guaranteed amount includes principal and coupon
Source: Fitch Ratings, Fitch Solutions, CGIF

Fitch's Expectations

- Capitalisation to remain solid, with a net par/capital ratio of below 2.0x over the long term.

[1]The amount refers to the gross notional principal amount of all 40 CGIF guaranteed bonds since its inception of operations. The amounts were converted to US dollars by the use of spot exchange rate on the date of bond issuance.

Financial Performance and Earnings

Steady Financial Performance

CGIF's operating results have remained manageable over the last three years, with a return on equity of 2.3% in 2021 (2020: 2.0%). CGIF does not have specific profit targets or mandates, aside from its objective of supporting the development of the Asian bond market. This differs from most privately owned and commercially run organisations, which have earnings growth and dividend targets. This makes CGIF's performance goals similar to those of mutual insurance companies and government agencies whose profit margins are set to ensure reasonable compensation for the risk assumed, and to support long-term capital growth that is commensurate with forecast business growth.

Fitch sees CGIF's insured portfolio as high risk within the context of our ratings criteria for guarantors; a high-risk portfolio is characterised by high frequency and severity of losses and uncapped currency risk. CGIF's underwriting and controls appear well-thought-out and prudent, albeit untested, to manage the high risk from its insured portfolio. CGIF is exposed to volatile guarantee risks because it guarantees non-investment-grade corporate issuance. It is also exposed to foreign-currency risk, as it provides local currency-denominated guarantees to emerging markets.

In 2021, one guaranteed bond issuer defaulted on its obligation at bond maturity. The issuer of the defaulted bond reimbursed CGIF for coupon payments and additional accrued interest from the maturity date until the guarantee payment date, and legal expenses. CGIF is working with the defaulted bond issuer for the reimbursement of guarantee payments and the costs and expenses incurred by CGIF after the guarantee payments.

CGIF caps the size of each bond guarantee at 20% of its paid-in capital, with sub-limits of up to 20% of its maximum guarantee capacity per country and up to 40% of its maximum guarantee capacity per currency. This ensures business diversification, and curbs exposure to any single country or currency. CGIF factors in the level of paid-in capital and retained surplus, credit-loss reserves, foreign-exchange loss reserves, the amount of illiquid investments and the maximum leverage ratio to determine the level of maximum guarantee capacity. Bonds guaranteed by CGIF are generally limited to tenors of 10 years or below.

Financial Highlights

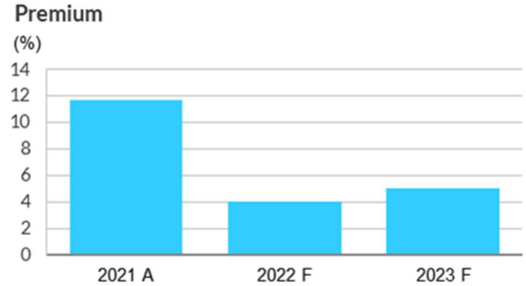
(%)	2021	2020
Net income (USDm)	29.8	23.9
Return on equity	2.3	2.0

Source: Fitch Ratings, Fitch Solutions, CGIF

Fitch's Expectations

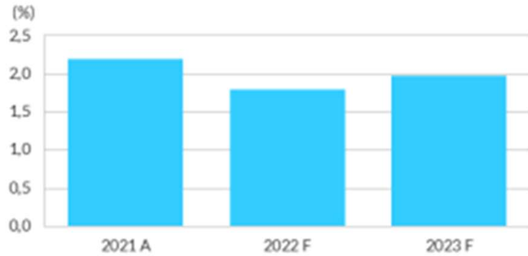
- Maintain its prudent underwriting practice in light of its business focus on a high-risk-insured portfolio.
- Gross written premium (guarantee fee) growth is estimated by Fitch to remain moderate at 3%-5% in 2022 and 2023 driven by interest rates hikes. Growth already slowed to 3% in 3Q22.
- Fitch forecasts return on equity to rise to 2% in 2023 on improved investment yields and lower impairment losses.

Fitch Forecast - Growth in Gross Written Premium



Source: Fitch Ratings

Fitch Forecast — Return on Equity



Source: Fitch Ratings

Investment and Asset Risk

CGIF's key investment objective is to protect the principal amount of its investments by investing in liquid, low-risk and high-credit-quality instruments. Investments are managed by ADB's treasury in accordance with CGIF's treasury risk-management guidelines, which have been adopted in agreement with the contributors. CGIF invests in only cash and deposits and fixed-income securities. No equity investments are considered. Eligible fixed-income securities with maturity terms of more than one year must be rated at least 'A+' on an international scale for government-related issuers of CGIF contributor countries and 'AA-' for other issuers. CGIF may invest in fixed-income securities with remaining terms to maturity of up to one year with short-term credit ratings of at least 'F1' or the equivalent.

CGIF has significant exposure to foreign-currency risk because it guarantees bonds denominated in various currencies of the market of issuance, while its functional currency is the US dollar. However, CGIF is free from a convertibility risk as it has an option to settle guarantee obligations in US dollars (or substitute currency) in principle. As a result, CGIF is not at a risk of defaulting on a guarantee due to lack of access to the bond issue's currency.

Fitch does not expect CGIF to face severe liquidity problems due to its appropriate management of liquidity risk. All CGIF investments, by policy, must be marketable within a reasonable time. CGIF allocated 80% of its investments in bonds and time deposits with maturity durations of less than five years in 2020, giving the portfolio a duration of three years at the end of the year. The possibility of a liquidity crisis is limited due to CGIF's right to accelerate or retain the original interest or principal payment schedule in the event of a default on an insured bond, eliminating liability-acceleration risk.

Financial Highlights

(%)	2021	2020
Risky asset ratio	0	0
Equity investment capital	0	0

Source: Fitch Ratings, Fitch Solutions, CGIF

Fitch's Expectations

- No significant change to the risk profile of CGIF's investments in light of its investment approach.

Reserve Adequacy

CGIF assesses credit loss reserves according to Basel standards. Credit-loss reserves are assessed as the amount of expected loss, the product of each account's probability of default and loss given default, where probabilities of default correspond to the internal credit ratings of individual bond issuers. CGIF commissions an internationally renowned rating advisory company to independently assess the credit rating of each proposed guaranteed bond issuer, according to its operational policies and to ensure that it correctly applies international technical standards in its credit ratings.

Each outstanding guarantee is reviewed and re-rated at least annually. Additional provisions are set aside should a bond issuer's credit profile deteriorate, based on the perceived lower credit rating. Management also makes specific provisions for any at-risk guarantee on a case-by-case basis based on ongoing monitoring of all guarantees outstanding.

Financial Highlights

(%)	2021	2020
Reinsurance recoverable to capital	0.2	0
Single-risk par/capital	10	9
Net notional par/gross notional par insured	67	71

Source: Fitch Ratings, Fitch Solutions, CGIF

Fitch's Expectations

- Short-term volatility in CGIF's claim reserve ratio due to its limited claim liability development record.

Reinsurance, Risk Mitigation and Catastrophe Risk

CGIF has arranged a quota-share reinsurance treaty to support its underwriting capacity. All reinsurers under this treaty have an IFS rating of at least 'A-'. There has been no material change to the 25% quota share reinsurance treaty programme. Nonetheless, several accounts were reinsured under a special acceptance cession to ensure sound diversity in the guarantee portfolio. This exception was allowed under the investment committee's approval.

Financial Highlights

(%)	2021	2020
Reinsurance recoverable to capital	0.2	0
Single risk par/capital	10	9
Net notional par/gross notional par insured	67	71

Source: Fitch Ratings, Fitch Solutions, CGIF

Fitch's Expectations

- CGIF's risk management and risk-mitigating capabilities to remain robust

Appendix A: Peer Analysis

CGIF has no equivalent like-for-like peers for a relevant peer comparison, given its specialised nature and focus on supporting the development of debt capital markets in Asia by providing financial guarantees on debt issues.

Fitch compares CGIF with GuarantCo Ltd., a financial guarantor that is also owned by government agencies and follows development objectives. GuarantCo proves infrastructure guarantees in Africa and Asia.

Peer Comparison

(USDm)	IFS Rating	Shareholders' equity	Gross par	Net par/capital (x)	Financial leverage (%)	Return on equity (%)	Risky assets/equity (%)
CGIF	AAA(idn)/ Stable	1,292	2,009	1.6	0	2.3	0
GuarantCo	AA-/Negative	280	661	1.2	0	0.8	0

Source: Fitch Ratings, CGIF, GuarantCo

Appendix B: Industry Profile and Operating Environment

Industry Profile and Operating Environment (IPOE)

Click here for a link to a report that summarizes the main factors driving the above IPOE score.

Appendix C: Other Rating Considerations

Below is a summary of additional ratings considerations that are part of Fitch's *Insurance Rating Criteria*.

Short-Term Ratings

Not applicable.

Recovery Analysis and Recovery Ratings

Not applicable.

Transfer and Convertibility Risk (Country Ceiling)

None.

Criteria Variations

None.

The ratings above were solicited and assigned or maintained at the request of the rated entity/issuer or a related third party. Any exceptions follow below.