

RATING ACTION COMMENTARY

Fitch Revises CDB's Outlook to Stable; Affirms at 'AA+'

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Fitch Ratings - London - 01 Mar 2022: Fitch Ratings has revised the Outlook on Caribbean Development Bank's (CDB) Long-Term Issuer Default Rating (IDR) to Stable from Negative and affirmed the IDR at 'AA+'.

KEY RATING DRIVERS

Reduced Credit Risk: The revision of the Outlook to Stable reflects the reduced risk of payment arrears on the bank's loan portfolio following resumption of regular debt service by seven of the bank's sovereign borrowers. The performance of the loan book has been better than expected with no new non-performing loans (NPLs) incurred since the onset of the Covid-19 crisis. This is reflected in the bank's 'very low' NPL ratio with no sovereign arrears and only one non-sovereign NPL accounting for 0.1% of total loans at end-June 2021. Broadly unchanged capitalisation metrics and stability in the weighted average rating of the loan portfolio also supports the bank's solvency assessment.

'AA+' Driven by SCP: CDB's 'AA+' Long-Term IDR reflects its Standalone Credit Profile (SCP), underpinned by liquidity and solvency assessments of 'aaa' and 'aa+', respectively. Fitch assesses CDB's business environment as medium-risk, which does not translate into

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support to its BMCs by leveraging donor funds. The large off-balance sheet policy response enabled the bank to provide cheap and flexible financing while preserving the bank's 'excellent' capitalisation buffers.

Excellent Capitalisation: CDB's solvency assessment is supported by the bank's 'excellent' capitalisation. As of end-June 2021, the bank's equity-to-adjusted-assets and guarantees ratio was 45.4%, well above the 25% threshold for an 'excellent' assessment. Fitch's usable capital to risk-weighted assets ratio was 69.0%, also comfortably above the 35% threshold for an 'excellent' assessment. These metrics are broadly in line with pre-pandemic levels, which highlights the limited impact of the pandemic on the bank's capitalisation, given strong loan performance and the bank's recourse to off-balance sheet concessional financing.

Liquidity Supports Rating: Fitch assesses CDB's liquidity at 'aaa'. This is driven by the bank's 'excellent' liquidity buffers (coverage of short-term debt was 5.4x at end-June 2021) and the 'excellent' credit quality of the bank's treasury portfolio. Fitch expects the bank to continue to operate with large and high-quality liquidity buffers, despite recent deterioration in the credit quality of the bank's treasury portfolio. Conservative policies on asset liability management, and the long-term and the staggered structure of its borrowings should support the liquidity buffer remaining well above the 1.5x threshold we deem as 'excellent' over the medium term.

Concentration Risk Key Rating Weakness: CDB's five largest borrowers accounted for 54.0% of total banking exposures at end-June 2021. This is a 'moderate' level based on Fitch's Supranational Rating Criteria. However, Fitch notes that concentration risk is inherently higher than peers with comparable metrics, given the geographical proximity and correlation between BMCs' economies. Concentration risk should marginally decline over the medium term as the bank targets loan portfolio diversification towards higher-rated sovereigns.

Regional Challenges Increase Financing Needs: The pandemic and natural hazards have negatively impacted the bank's poverty reduction efforts and development objectives. The bank's Strategic Plan Update approved in December 2021 highlights the needs for more financial resources, including crowding-in resources, co-financing opportunities, and

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- Solvency (Risk): A material improvement in concentration and credit risk, potentially driven by greater exposure to higher rated borrowers.

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

- Solvency (Risk): An increase in credit risk potentially leading to sovereign arrears and/or higher NPLs in the non-sovereign loan book leading to a rise in the NPL ratio above the upper bound 'very low' risk threshold of 1%. Increased concentration risk, driven by a rise in the share of existing exposures and/or increased exposure to sovereigns in financial distress, would also be negative for the rating.

- Solvency (Capitalisation): Greater than expected decline in capitalisation metrics. This could be driven by losses, rapid growth in banking operations, and/or a significant increase in risk-weighted assets.

- Liquidity: Significant reduction in liquidity buffers and/or continued decline in the credit quality of the bank's treasury portfolio with the share of 'AAA'-'AA' rated assets in the treasury portfolio falling close to 40%.

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 source(s) of information used to assess these ratings were CDB's financial statements,

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The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

CDB has an ESG Relevance Score of '4[+]' for Human Rights, Community Relations, Access & Affordability. CDB provides grants funded by donor contributions and that are a significant part of the bank's business model. CDB has also acted as a lender of last resort to countries that had lost market access. This supports CDB's policy importance. This has a positive impact on the credit profile, and is relevant to the ratings in conjunction with other factors.

Caribbean Development Bank has an ESG Relevance Score of '4' for Policy Status and Mandate Effectiveness. Geographically concentrated exposure to small Caribbean islands with economies largely interconnected and highly vulnerable due to large tourism exposure and risk of natural disasters. This has a negative impact on the credit profile, and is relevant to the ratings in conjunction with other factors.

CDB has an ESG Relevance Score of '4' for 'Rule of Law, Institutional and 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.

CDB has an ESG Relevance Score of '3' for 'Exposure to Environmental Impacts'. Environmental risk is a key risk to CDB's borrowers but this is actively managed by the bank. CDB has set up (with other partners, such as the World Bank) an insurance vehicle against natural disasters and requires its sovereign borrowers to acquire minimum insurance cover. CDB has never suffered a loss due to the realisation of environmental risk.

The ESG Relevance Score assigned to 'Labour Relations and Practices' (SLB) has been changed to '2' from '3', given that restrictions on recruitment based on nationality or quotas is no longer considered to be relevant to multilateral development banks' ratings'

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a

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RATING ACTIONS

ENTITY / DEBT ⚡	RATING ⚡		PRIOR ⚡
Caribbean Development Bank	LT IDR	AA+ Rating Outlook Stable	AA+ Rating Outlook Negative
	Affirmed		
	ST IDR	F1+ Affirmed	F1+

[VIEW ADDITIONAL RATING DETAILS](#)

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APPLICABLE CRITERIA

[Supranationals Rating Criteria \(pub. 20 May 2021\) \(including rating assumption sensitivity\)](#)

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Caribbean Development Bank

UK Issued, EU Endorsed

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