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Caribbean Development Bank

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Caribbean Development Bank

Rationale

Counterparty Credit Rating
Foreign Currency
AA/Stable/A-1+

The ratings on CDB are based on its "strong" business profile and its "very strong" financial profile, as Standard & Poor's Ratings Services defines these terms. Together they form CDB's 'aa-' stand-alone credit profile (SACP). Our credit ratings pertain only to the Caribbean Development Bank's Ordinary Capital Resources (OCR), the bank's primary operations. We incorporate one notch of uplift to CDB's SACP based on our expectation of extraordinary shareholder support to arrive at our 'AA' long-term issuer credit rating (ICR). This expectation derives from $328 million eligible callable capital, which CDB's higher-rated shareholders provide the bank.

Established in 1969, CDB provides loans and guarantees to governments and companies in the Caribbean. CDB had $1.5 billion adjusted total assets as of Dec. 31, 2013.

CDB's strong business profile reflects first its role as a prominent lender in the Caribbean and its ability to lend to sovereigns through the credit cycle. Second, CDB's members demonstrated their support for the bank's mandate by granting a 38% increase of paid-in capital in 2010, although some members have been late in paying their subscriptions. The bank's membership is also expanding. Suriname joined CDB during 2013. Third, the bank's borrowing members have treated CDB's OCR as a preferred creditor in most, but not all, periods of stressed external liquidity. Significant support from nonregional members, including funding of CDB's Special Funds Resources (SFR; not rated), which provides grants and concessional loans to lower-income countries, has helped sustain the credit quality of the OCR. The bank has also strengthened its risk management structures and monitoring over the past 18 months.

Offsetting these factors, CDB has significant embedded credit risk in its portfolio and the majority of voting rights rests with borrowing-eligible member countries. In addition, the accounting treatment of some of CDB's derivative positions affects its ability to generate capital internally. Although the bank expects its hedges to be economically effective, the accounting requirement of marking its derivatives to market while recording its financing at historical cost adds volatility to CDB's comprehensive earnings.

We assess CDB's financial profile as very strong. Historically, CDB has maintained a high level of capitalization to offset the correlation risk of borrowing members. This correlation pertains not only to the bank's region of operations, but also the common characteristics of many of its borrowing members. These include economic structure, monetary arrangements, fiscal challenges, and reliance on foreign savings. The bank has significant concentration in its top three sovereign exposures. In addition, CDB carries embedded credit risk in its sovereign loan portfolio, reflected in the speculative-grade ratings on three of its top five sovereign exposures (Jamaica, Barbados, and Belize) and in the fiscal, economic, and external positions of two members we don't rate (Saint Vincent and the Grenadines and Saint Lucia) (see "Sovereign Ratings And Country T&C Assessments," June 3, 2014.).

CDB's risk-adjusted capital (RAC) ratio improved to 23% as of Dec. 31, 2013, from 21% the previous December because of less embedded credit risk in the portfolio (as implied by sovereign ratings, with improvements particularly in Jamaica and Belize), lower loan growth (as many borrowing members undergo fiscal consolidation), and receipts of paid-in capital.

We expect these factors and CDB's long-dated funding profile will reduce CDB's financing needs over 2014-2015. We expect CDB will not refinance a $150 million bond maturing in July 2014. Through the first quarter of 2014, CDB retained sufficient balance sheet liquidity to fund its scheduled obligations for up to one year without capital market access under an extreme stress scenario, but similar to many other supranational financial institutions, it would have to defer a portion of its loan disbursements. CDB's funding sources and investor base are less diversified than those of many peers, which has contributed to the historical unevenness of its debt amortization schedule.

Outlook

The stable outlook reflects our expectation CDB will maintain a high level of capital to offset its sovereign borrower concentrations and correlation risk. It also reflects our expectation that CDB's sovereign borrowers will treat the bank as a preferred creditor via continued debt service and in any upcoming sovereign debt restructurings, including that of Grenada (rated 'SD' [selective default]), which we expect to exit from default to its commercial creditors this year. This expectation reflects reduced external liquidity vulnerabilities among some of CDB's lowest-rated borrowers and the fiscal consolidation that many of its sovereign borrowers have begun over the past year, both of which strengthen borrowers' capacity to service their U.S. dollar-denominated debt to CDB. In our calculations, a potential moderate credit deterioration of some of CDB's borrowing members would have limited effect on the bank's capital adequacy.

The stable outlook implies that we see less than a one-in-three probability that we will raise or lower the ratings over the next two years. Over time, we could raise the ratings if CDB's embedded credit risk declined or its nonborrowing membership markedly increased.

On the other hand, we could lower the ratings if--contrary to our expectations--any of CDB's members were not to treat the bank's OCR as a preferred creditor, or if either the bank's capital adequacy or liquidity notably deteriorates.

Stand-Alone Credit Profile: 'aa-'

We assess CDB's SACP at 'aa-', reflecting the bank's strong business profile and its very strong financial profile.

Our analysis draws comparisons with several peers (see table 1). We selected this sample of multilateral development banks for their common mandate--to provide long-term project and other financing, often with concessional terms to their borrowing member countries; their substantial activity in emerging and frontier markets; the prominence of their public-sector lending activities; and the regional or subregional scope of most, with the inclusion of IBRD as a global benchmark. We publish our comparative statistics in this report with a one-year lag to respect the confidentiality of those institutions whose respective boards have not approved their fiscal year-end 2013 financial statements as of the date of this report.

Table 1

Selected Comparative Statistics For CDB And Peers

(Fiscal year-end 2012)

		Total adjusted assets (US$ mil.)	RAC ratio after adjustments* (%)	Purpose-related assets (gross) / adjusted total assets (%)	Gross debt / adjusted common equity (x)	Liquid assets / adjusted total assets (%)	Static funding gap at 1 year (x)
Caribbean Development Bank	(CDB)	1,683	21	59	1.4	29	1.4
International Bank for Reconstruction and Development	(IBRD)	324,367	29	40	4.0	12	0.9
African Development Bank	(AFDB)	32,603	15	54	2.5	35	1.3
Central American Bank for Economic Integration	(CABEI)	7,506	10	74	2.2	24	1.3
Eurasian Development Bank	(EDB)	3,884	17	49	1.2	49	20.3
Black Sea Trade and Development Bank	(BSTDB)	1,298	39	75	0.6	27	4.0

RAC--Risk adjusted capital ratio. ACE--Adjusted common equity. *Ratings parameters as of Dec. 31, 2013. N/A--Not available.

Business Profile: Strong

CDB has a strong business profile, in our opinion, reflecting the bank's policy importance in addition to its governance and management expertise.

Policy Importance Assessment

Since its establishment in 1969, CDB has served a prominent role as the cornerstone lender to Caribbean governments (95% of loans, as of Dec. 31, 2013) and to several private financial institutions and companies (5% of loans) in the region. CDB provides long-term project financing often accompanied by grace periods and below-market rates of interest. In addition, CDB provides guarantees, including partial guarantees on rescheduled commercial bonds of St. Kitts & Nevis as well as Dominica that were effective in increasing commercial creditors' participation. The bank also provides grants and low-interest loans to its poorest member countries via the SFR.

Table 2

Principal Business Activities

	--As of Dec. 31--				
	2013	**2012**	**2011**	**2010**	**2009**
Purpose-related assets (gross)/adjusted total assets (%)	66	59	64	76	62
Net loans/adjusted total assets (%)	65	58	64	76	62
Public-sector (including sovereign-guaranteed) loans/total loans (%)	95	95	95	95	95
Private-sector loans/total loans (%)	5	5	5	5	5
Equity investments/adjusted total assets (%)	0	0	0	0	0

Table 2

Principal Business Activities (cont.)					
Memo (US$ mil.)					
Total guarantees	12	12	12	8	8
Total adjusted assets*	1,493	1,694	1,592	1,308	1,329

N/A--Not available. N.M.--Not meaningful. *Adjustments made to reported shareholders' equity to calculate adjusted common equity (an institution's cash capital) are carried through to total assets.

A second important characteristic for multilateral development banks is their ability to lend countercyclically in periods of economic downturn. CDB increased its net loans outstanding by 6% and 21% during 2009 and 2010, respectively. Sovereign customer demand has slackened over 2012-2014. Many borrowing members are consolidating their fiscal positions, lowering their official funding needs.

CDB's members demonstrated in 2010 their support for the bank's public policy mandate by granting a 38% increase of paid-in capital, payable 2011-2016. Some members have been delinquent paying their subscriptions. These totaled $7.4 million, as of Dec. 31, 2013. Mexico and Italy have experienced parliamentary delays; whereas, budgetary difficulties of some small Eastern Caribbean members have delayed their subscriptions. Overall, CDB received $37.6 million in installments of the general capital increase (GCI) during 2013.

Shareholders remain highly supportive of the bank. The bank's membership expanded to 27 members, with the addition of Suriname during 2013. Shareholders enable the bank to retain 100% of earnings in most years, building capital internally. France was the only member to withdraw from the bank more than a decade ago (in 2000).

The bank's borrowing members have treated CDB's OCR as a preferred creditor in most, but not all, periods of stressed external liquidity and recent debt reschedulings. The latest exception occurred in 2012 when Grenada defaulted to CDB's OCR while paying debt service on a global bond, then subsequently cured its arrears with penalty interest to CDB. Significant support from nonregional members, including funding of CDB's SFR, which provides grants and concessional loans to lower-income countries, has helped sustain the credit quality of CDB's OCR. On more than one occasion, CDB has restructured all or part of an OCR using SFR resources. CDB's governors have approved cases following hurricanes (Dominica and Grenada), volcano eruptions (Montserrat), a member's commercial debt restructuring (St. Kitts & Nevis). We view this as a weaker form of preferred creditor treatment, but it has been a valuable tool to the bank for preserving the credit quality of its main balance sheet (and a means to provide their members fiscal flexibility).

Governance And Management Expertise

CDB bank has strengthened its risk management structures and monitoring over the past two years, supporting our view of its governance and management expertise. During 2013, CDB established the Office of Risk Management to monitor and manage the mitigation of all risks that CDB faces including strategic, financial, operational, and reputational risks.

The bank carries large single-name sovereign loan exposures, particularly to its top three borrowers, on its balance sheet. CDB sets portfolio exposure limits, but these are more expansive than development banks' with more diversified exposure. CDB's large sovereign loan portfolio also has significant geographic (Caribbean) and economic (tourism-intensive and U.S.- and European-market driven) risk embed in it. CDB's exposure limits are less stringent than other multilateral lending institutions (MLIs). The exposure limit to its single largest borrower (Jamaica) is the greater of 40% of loans or 50% of the bank's internally calculated available capital. The exposure limit to its three largest borrowers (Jamaica, Barbados, and St. Vincent and the Grenadines) is the greater of 60% of loans or 90% of available capital. To offset this credit risk, CDB's shareholders have enabled management to maintain a high level of capitalization over the years. In turn, this high level of capitalization continues to anchor the bank's creditworthiness and is a governance strength.

CDB's culture of consensus-based voting on major issues has in practice mitigated the agency risk posed by borrowing-eligible members' majority control (58%) of voting shares.

Table 3

Shareholder Concentrations

(%)	Share of votes controlled by eligible borrower member countries	Share of votes controlled by nonborrowing eligible member countries	Share of votes controlled by private-sector shareholders (if any)
Votes of shareholders	58	42	0

As of Dec. 31, 2013.

CDB does not pay dividends. In practice, shareholders have also minimized transfers from retained earnings to the bank's soft loan window and grant facility, the SFR. Shareholders have largely funded the SFR separately over periodic replenishment cycles. This stands in contrast with some other banks, such as Inter-American Development Bank (IADB) and International Bank for Reconstruction and Development (IBRD), that regularly transfer a large portion of earnings to their concessional financing facilities (Special Fund for Operations [SFO] and International Development Association [IDA], respectively). CDB's high earnings retention rate has enabled it to build capital internally.

In 2013, CDB adopted a new capital adequacy framework that risk weights its loan exposures. The bank must sustain available capital (as CDB defines it) of at minimum 150% of baseline economic capital. CDB's available capital was 192% of its economic capital and therefore was compliant with its internal policy, as of Dec. 31, 2013. We expect this new framework will better enable the bank to monitor possible changes in its RAC ratio.

CDB has traditionally used leverage conservatively, with 1.2x average debt-to-adjusted common equity (ACE) over the past decade. CDB's policy limits borrowing and guarantees of the OCR to 100% of the callable capital of its investment-grade nonborrowing members plus the paid-in capital and retained earnings net of receivables from members. The bank's ratio of total outstanding borrowings and undrawn commitments to the borrowing limit was 65.2%, as of the end of 2013.

CDB's liquidity policy contributes to the maintenance of cash and high-grade securities investments to provide it sufficient balance sheet liquidity. The bank's policy is to maintain a net three years' funding requirement or 40% of undisbursed commitments, whichever is greater. CDB was compliant with its internal liquidity policy throughout 2013.

Ernst & Young (Barbados), independent external auditors for the bank, issued a clean opinion of CDB's annual financial statements prepared in accordance with International Financial Reporting Standards (IFRS) for the periods ending Dec. 31, 2013 and 2012. The CBD restated its financial position for both years because of the application of IAS 19 (see Earnings below).

Financial Profile: Very Strong

CDB's financial profile is very strong, in our view, reflecting the strengths of its very strong capital adequacy and sufficient balance sheet liquidity, as well as the limited diversity of its funding and investor base.

Capital Adequacy

CDB's RAC adequacy improved over 2013, reflecting the shareholder payment of GCI installments, lower borrower demand, and upgrades on Jamaica and Belize because of lower risk to their external liquidity.

The quality of CDB's cash capital, what we call its ACE, is strong. It is composed primarily of paid-in capital and retained earnings. However, the large swings in shareholders' equity that result from the unhedged portion of the bank's yen borrowings (and that are passed through other comprehensive income to shareholders' equity) raises the volatility of the bank's earnings and lowers the quality of its internal capital generation (see table 12).

During 2013, CDB adopted IAS 19, which removed the corridor approach that enabled employers to delay recognition of actuarial variances of the funding status of their defined-benefit employee benefit plans. This revaluation caused an unrecognized net actuarial loss of $7.7 million as of Jan. 1, 2012. The bank recorded $5.2 million unrecognized net actuarial loss in other comprehensive income for 2012. Improved performance of the plans' equity investments contributed an $8.9 million net actuarial gain during 2013, which lowered CDB's net actuarial liability to $9.6 million as of Dec. 31, 2013, from $16.8 million as restated for Dec. 31, 2012.

Similar to other MLIs founded in the same era, CDB enabled members to post their capital contributions in cash or promissory notes ("non-negotiable demand notes," in the bank's parlance). Likewise, members were able to pay their cash capital subscriptions in U.S. dollars or their national currency (most often an inactively traded Caribbean or "restricted" currency). Over the years and through the depreciation of several members' currencies, the major development banks determined that their financial stability was best sustained by converting their capital to U.S. dollars (or another hard currency) and the discounting of promissory notes from capital. We deduct these legacy instruments (and the maintenance of value payment receivable resulting from the remaining capital denominated in restricted currencies) from CDB's shareholders' equity to calculate ACE (see table 11). Neither does CDB count these instruments for purposes of its core capital metrics.

Earnings

Akin to other MLIs, CDB's public policy mandate imparts a lower rate of profitability than a commercial bank would sustain. In return for providing the bank nearly 100% earnings retention, borrowing members receive concessional loans, often at below-market interest rates.

CDB's earnings have declined steadily since 2009. The bank's $17 million net income from operations (from which we exclude unrealized gains and losses on securities and derivatives) declined to 1.1% average adjusted assets in 2013 versus 5.9% in 2009. CDB's net interest income relative to average net loans fell to 2.2% in 2013 (from 5.1% in 2009) while the bank's interest expense has risen to 2.7% of average borrowings in 2013 (from 1.8% in 2009). The latter reflects the hedging of the bank's borrowings. In August 2013, CDB entered an interest rate swap to hedge half its $300 million 4.375% bond due 2027. CDB's efficiency ratio, administrative expense per average ACE, remained low and stronger than many peers' at 1.5% in 2013.

The bank's loan income is highly sensitive to the performance of its top three borrowers. Almost 50% of the bank's loan related-income was derived from these borrowers in 2013, and 24% was from Jamaica.

Despite lower internal capital generation, shareholders' payment of GCI installments has supported 7.5% average annual growth of ACE over the past three years (2011-2013).

Table 4

Profitability

(%)	2013	2012	2011	2010	2009
Net income/average adjusted assets	1.1	1.3	1.6	2.2	2.4
Net income/average adjusted common equity	2.6	3.5	3.9	5.3	5.9
Comprehensive income/average adjusted assets	0.7	0.6	2.8	3.1	1.6
Comprehensive income/average adjusted common equity	1.8	1.6	6.9	7.6	4.1
Net interest income/average net loans	2.2	3.0	3.6	4.2	5.1
Interest expense/average borrowings	2.7	1.5	1.0	1.2	1.8
Administrative expense/average adjusted common equity	1.5	1.7	1.7	1.9	1.8
Memo:					
Net income (US$ mil.)	17	22	23	29	30
Net increase (decrease) in cash and cash equivalents during the year (US$ mil.)	(29)	17	70	(89)	2

Treasury risk

CDB takes on more treasury-related risk than its (sub)regional peers. The bank uses two different accounting methods to report its derivatives relative to the yen-denominated borrowings they cover. This contributes significant volatility to the bank's comprehensive income, although the bank expects its hedges are economically effective over time.

Credit risk. CDB assumes counterparty risk via its cash and securities investments as well as its derivative counterparties. The bank manages this risk prudently, in our view. At the close of the first quarter of 2014, the bank had invested the bulk of its liquidity investments--19% of adjusted total assets--in unencumbered securities rated 'AA-' or above by Standard & Poor's (or the equivalent by another agency).

The remaining liquidity investments were cash and deposits--totaling 6% of adjusted total assets--in investment-grade banks. Bank accounts that CDB does not require for operational purposes in the Caribbean are held with well-reputed global banks.

The counterparties for CDB's derivative transactions are global banks. CDB was in a net positive position relative to its commercial bank counterparts, as of March 31, 2014.

Interest rate risk. CDB manages its interest rate risk fundamentally by using moderate leverage historically. Its use of shareholders' equity funding (totaling about half of adjusted total assets over the past five years) acts as a natural hedge against market interest rate changes.

The bank also manages its interest rate risk by providing floating-rate loans, to which it attempts to match the structure its borrowings. Interest and principal is payable quarterly, and CDB may reset the interest rate semiannually. The bank issues floating-rate debt (32% of debt as of the end of 2013) when possible, or it swaps fixed-rate issues effectively to floating-rate obligations when this is cost effective.

CDB manages its risk of asset-liability maturity mismatch by maintaining sufficient balance sheet liquidity. By our simple static funding gap analysis, CDB has a surplus of assets over liabilities at the one-, two-, and five-year horizons, as of March 31, 2014. In practice, it also matches the long-dated loans with borrowings of similar maturity. The bank's average loan maturity was 6.9 years versus 9.4 years for its borrowings. It does not use short-term financing, such as issuing certificates of deposit or commercial paper.

Exchange rate risk. CDB denominates all its loan assets and debt service receivable in U.S. dollars and reports its financial position in the same. Its most recent GCI installments are also payable in dollars. Seventy-six percent of CDB's debt is denominated in its currency of operation. The remainder--$160 million equivalent of yen-denominated bonds (27% of borrowings, as of Dec. 31, 2013)--CDB partially hedges by swapping a portion of the underlying exposure into floating-rate U.S. dollars cash flows using currency-currency interest rate swaps. Interest on the notes is payable in U.S. dollars, while the final principal is payable in yen.

Although the bank expects its hedges to be economically effective, CDB's use of two different accounting treatments adds significant volatility to CDB's comprehensive earnings. The bank marks its derivatives (cross-currency interest rate swaps) to market while recording its related yen-denominated bonds at historical cost.

Risk Position

The bank's RAC ratio rose to 23% after adjustments as of Dec. 31, 2013, from 21% as of Dec. 31, 2012 (both reflecting rating parameters as of May 5, 2014). This change reflects lower customer demand due to continuing fiscal budgetary constraints and the high debt burdens of many (potential) borrower governments, lower near-term external liquidity risks for several borrowers that contributed to upgrades of Belize and Jamaica during 2013, and receipts of paid-in capital. At 23%, CDB's post-adjustment RAC ratio is borderline between extremely strong and very strong.

We expect the limited fiscal flexibility of many Caribbean sovereigns will continue to slacken customer demand for sovereign loans during 2014. Tourism receipts are picking up on improving U.S. and European economic growth prospects, which will likely stimulate investment in economies where governments have greater fiscal space. We expect that CDB's relative exposures will not alter much in 2014. Because most loans carry long-dated maturities, the composition of CDB's loan book evolves slowly.

Table 5

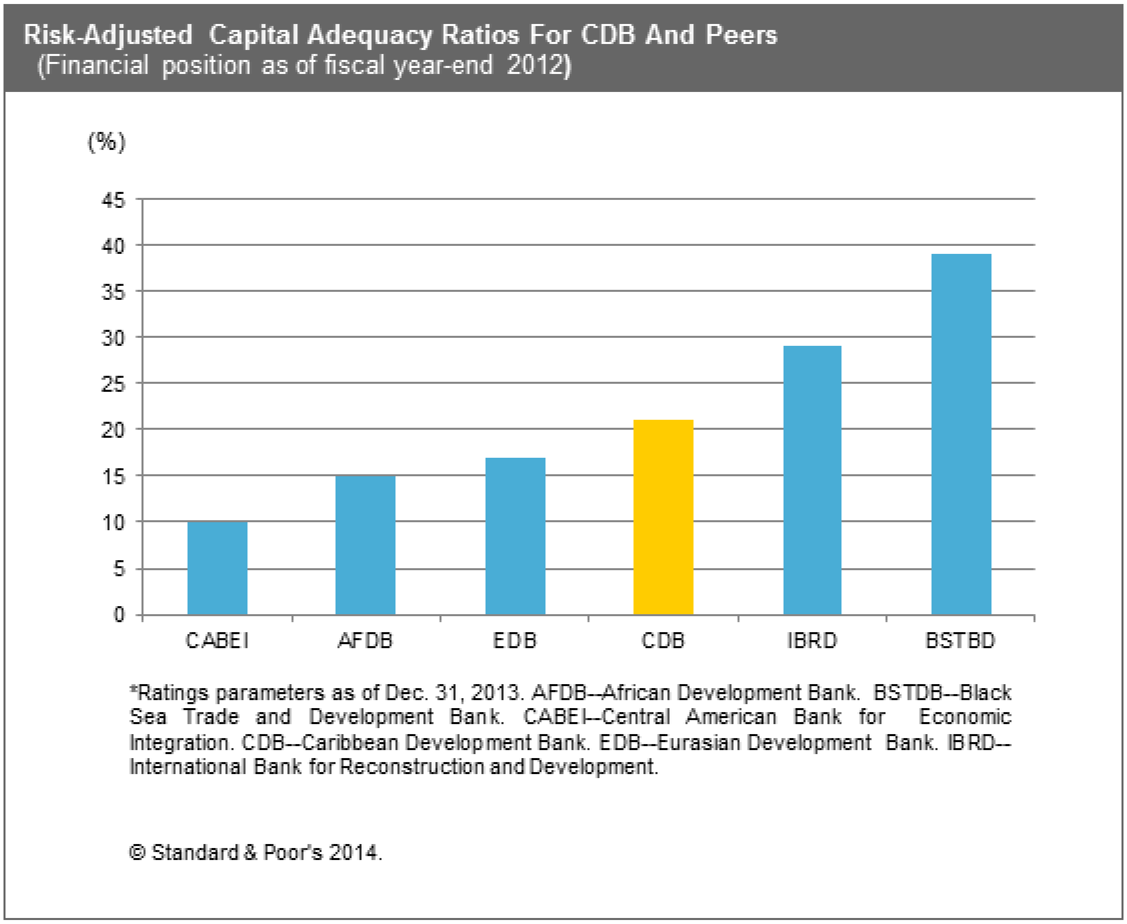
CDB's Risk-Adjusted Capital Adequacy As Of Dec. 31, 2013

	--Ratings as of May 8, 2014--		
	Exposure (US$ mil.)	**Standard & Poor's RWA (US$ mil.)**	**Average Standard & Poor's RW (%)**
Credit risk			
Government and central banks	1,309	1,490	114
Institutions	226	85	38
Corporate	0	0	--
Securitization	0	0	--
Other assets	24	26	108
Total credit risk	1,560	1,600	103
Market risk			
Equity in the banking book	0	0	--
Trading book market risk	--	0	--
Total market risk	--	0	--
Operational risk			
Total operational risk	--	102	--
RWA before MLI adjustments		1,702	100
MLI adjustments			
Industry and geographic diversification		(104)	(6)
Preferred creditor treatment		(332)	(22)
Single-name concentration		1,732	116
High-risk exposure cap		0	0
Total MLI adjustments		1,296	76
RWA after MLI adjustments		2,999	176
		Adjusted Common Equity (US$ mil.)	**Standard & Poor's RAC ratio (%)**
Capital ratio before adjustments		703	41
Capital ratio after adjustments			23

RAC ratio--Risk-adjusted capital ratio, defined as adjusted common equity (ACE) divided by risk-weighted assets (RWA). RW--Risk weighting. MLI--Multilateral lending institution. Ratings parameters as of May 8, 2014.

In comparison with peers, CDB is well-capitalized for its risk position. As of the end of fiscal year-end 2012, CDB maintained higher relative capital adequacy than Central American Bank for Economic Integration (CABEI), African Development Bank (AFDB), and Eurasian Development Bank (EDB)--which are also (sub)regional multilateral development banks with sizable public-sector portfolios of similar loan products. IBRD, a large global bank, and Black Sea Trade and Development Bank (BSTDB), a newer and growing subregional bank, had higher levels of capitalization as of their respective 2012 fiscal year-ends. Similar to CDB, AFDB and IBRD have soft loan windows that have helped them channel concessional financing to their lowest-income member countries while safeguarding the credit quality of the respective banks' primary balance sheets.

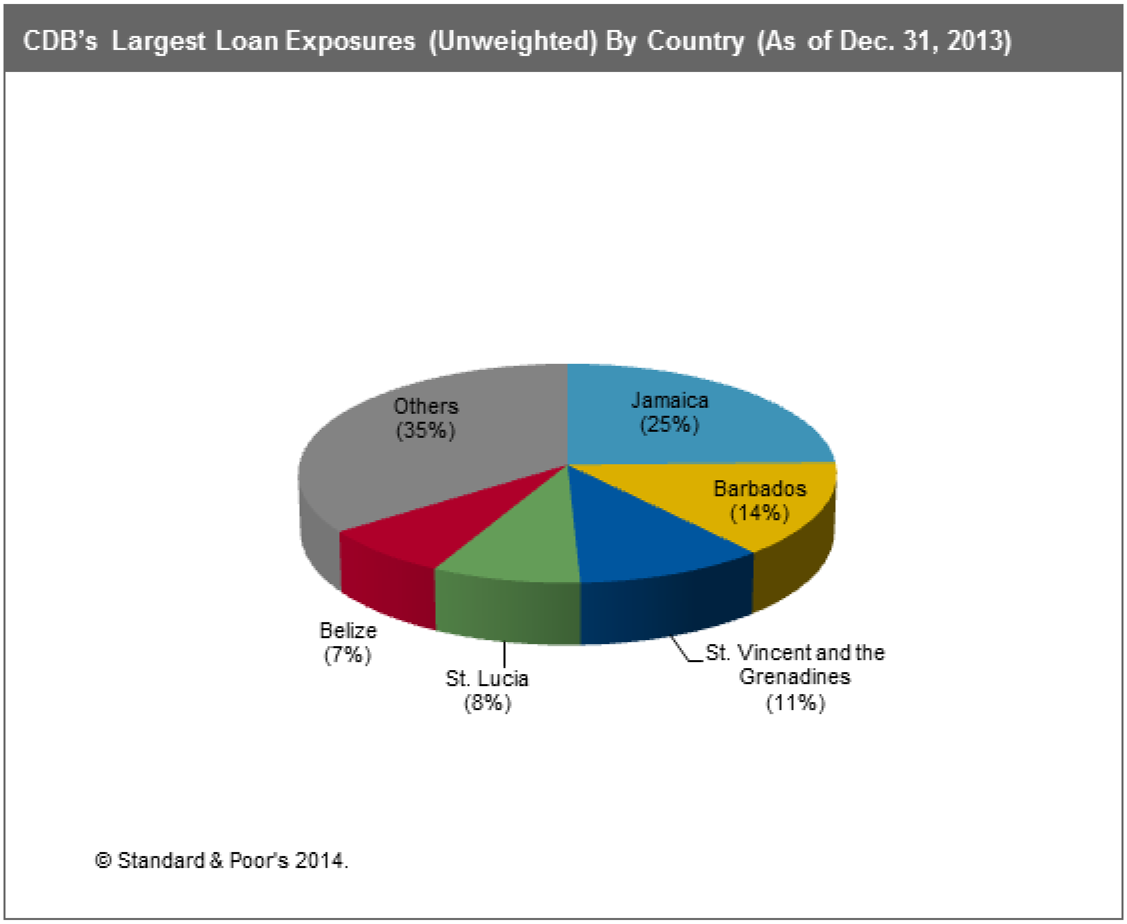
Chart 1



Exposure concentrations

CDB maintains significant exposure concentration to a handful of Caribbean sovereign borrowers, many of which have high default risk. The sovereign single-name concentration adjustment for the potential loss on these exposures--partially offset by our expectation of preferred creditor treatment--explains the difference between the 41% RAC before MLI-specific adjustments and the 23% RAC after.

Chart 2



The bank's top three loan exposures represented 49% of loans and 67% of ACE (before risk-weighting) at the end of 2013. The largest, Jamaica, represented 25% of loans, followed by Barbados (14%), and St. Vincent and the Grenadines (11%). The capital charge for the potential loss on CDB's largest exposures is calibrated to an 8% minimum capital ratio. The large sovereign concentration adjustment reflects both the lower relative creditworthiness of some of CDB's borrowers and the top five sovereigns' large share of CDB's exposure at default (EAD, which includes assets, half of committed undisbursed loans and equity investments, plus the full amount of guarantees and letters of credit).

Table 6

Country Data And Projections For CDB's Top 10 Borrowing Members

	--Real GDP growth (% change)--		GDP per capita (US$)	Net general government debt (% GDP)	General government interest expense/revenues (%)
	2014f	2015f	2013	2013	2013
Anguilla*	N/A	N/A	N/A	N/A	N/A
Antigua and Barbuda*	2	2	13,838	92	N/A
Barbados	1	2	15,373	70	14
Belize	3	3	4,602	73	9
Grenada	1	2	7,697	95	12
Guyana*	4	4	3,729	55	N/A

Table 6

Country Data And Projections For CDB's Top 10 Borrowing Members (cont.)					
Jamaica	2	2	5,134	133	32
St. Kitts and Nevis*	3	3	13,115	N/A	N/A
St. Lucia*	0	1	7,801	N/A	N/A
St. Vincent and the Grenadines*	2	3	6,563	73	N/A

*Standard & Poor's Ratings Services does not rate these entities. Data source for countries Standard & Poor's does not rate: International Monetary Fund World Economic Outlook, April 2014. f--Forecast. N/A--Not available.

Asset quality: loan loss experience

Preferred creditor treatment and the ability to restructure loans through the SFR in advance of a borrower default have supported the asset quality of CDB's sovereign loan portfolio over the years. The recent exception to this practice occurred in 2012 when Grenada fell more than 180 days past due on interest and principal payments to the OCR. The government cured its default by the fiscal year-end with penalty interest. No public-sector loans were past due as of either Dec. 31, 2013, or March 31, 2014.

CDB does not provision for expected losses on its public-sector loan portfolio. Like many other MLIs, any losses on CDB's sovereign loans would be charged off from shareholders' equity. CDB's ACE was 0.8x public-sector loans, as of the end of 2013.

The bank has experienced a higher rate of impairment on its small private-sector loan portfolio. This rose to 1.3% of loans in 2009, in the wake of the financial crisis. In 2013, CDB recovered $3.7 million recovery on one impaired loan dating from 2009, lowering the ratio of impaired loans to 0.5% of total loans. Loan restructuring and obtaining a suitable buyer for foreclosed properties can be prolonged in the Caribbean's shallow capital markets. Overall, CDB's private-sector portfolio has stabilized since 2009, although the bank has reduced its private-sector investment in tune with limited viable opportunities. The bank's sole remaining impaired exposure is a regional financial institution, for which the bank had provisioned 90% of the exposure.

Table 7

Asset Quality					
	--As of Dec. 31--				
	2013	**2012**	**2011**	**2010**	**2009**
Loan portfolio					
Impaired loans/total loans (%)	0.5	1.1	1.1	1.1	1.3
Impaired loans/total adjusted assets (%)	0.4	0.7	0.7	0.8	0.8
Impaired public-sector (including sovereign/sovereign-guaranteed) loans/total loans (%)	N.M.	N.M.	N.M.	N.M.	N.M.
Impaired public-sector (including sovereign/sovereign-guaranteed) loans net of loan loss provisions/total loans (%)	N.M.	N.M.	N.M.	N.M.	N.M.
Impaired private-sector loans/total loans (%)	0.5	1.2	1.1	1.1	1.3
Impaired private-sector loans net of loan loss provisions/total loans (%)	0.0	0.4	0.6	0.9	1.1
Loan loss reserves for private-sector loans/impaired private-sector loans (%)	92	67	47	19	19
Loans loss provisions made in current year/net loans at previous year end (%)	0.5	0.8	0.5	0.3	0.3
Loan write-offs/impaired loans at previous fiscal year end (%)	0.0	0.0	0.0	0.0	0.0
Recoveries/impaired loans at previous fiscal year end (%)	32	0	0	0	0

Table 7

Asset Quality (cont.)					
ACE/impaired loans (x)	135	57	57	53	48
Guarantees					
Guarantees called by third parties during the current year/guarantees outstanding at the end of the previous fiscal year (%)	0.0	0.0	49.4	0.0	0.0

ACE--Adjusted common equity. N.M.--Not meaningful.

Guarantees

CDB has one outstanding guarantee, a $12 million partial guarantee for rescheduled bonds issued by the government of St. Kitts and Nevis in 2011. As of March 31, 2013, the guarantee had not been called.

Funding and Liquidity

Funding

CDB has a less developed funding profile and less diversified global investor base than several peers, such as CABEI, AFDB, and (a benchmark issuer) IBRD. This, coupled with the institution's small size relative to larger regional and global banks, has contributed to the historical unevenness of its debt amortization profile. To reduce its rollover risk, in 2012 CDB incorporated a feature--which amortizes the principal over the last five years to maturity--into its last $300 million, 15-year bond issue. More than 90% of CDB's borrowings are bonds, which are long-dated. After this year, CDB's next bullet maturity is 2021. The remainder of the bank's borrowings is loans sourced from EIB and IADB.

In line with its conservative funding strategy, CDB does not use short-term financing vehicles. It does not issue certificates of deposit or commercial paper.

We expect that CDB would be able to fund its operations and meet its debt service obligations for up to one year without capital market access. It would have to defer a portion of its loan disbursements, not uncommon among the MLIs. CDB's static funding gap at one year (without consideration of loan disbursements) rose to 1.7x by March 31, 2014, from 1.3x as of Dec. 31, 2013. The bank incremented its cash reserves early in 2014, planning to pay a $150 million bond maturing in July in cash to reduce its cost of carry.

CDB has been reducing its leverage. The bank's gross debt-to-ACE declined to 1.0x in 2013 from 1.4x in 2012, and we expect it to recede further this year. The bank continues to receive GCI capital installments and is limiting the cost-of-carry on its liquid assets (cash, due from banks, and securities totaling 23% of adjusted total assets at the end of 2013) on the back of slowing demand from their government borrowers (many of whom are undergoing fiscal consolidation).

Table 8

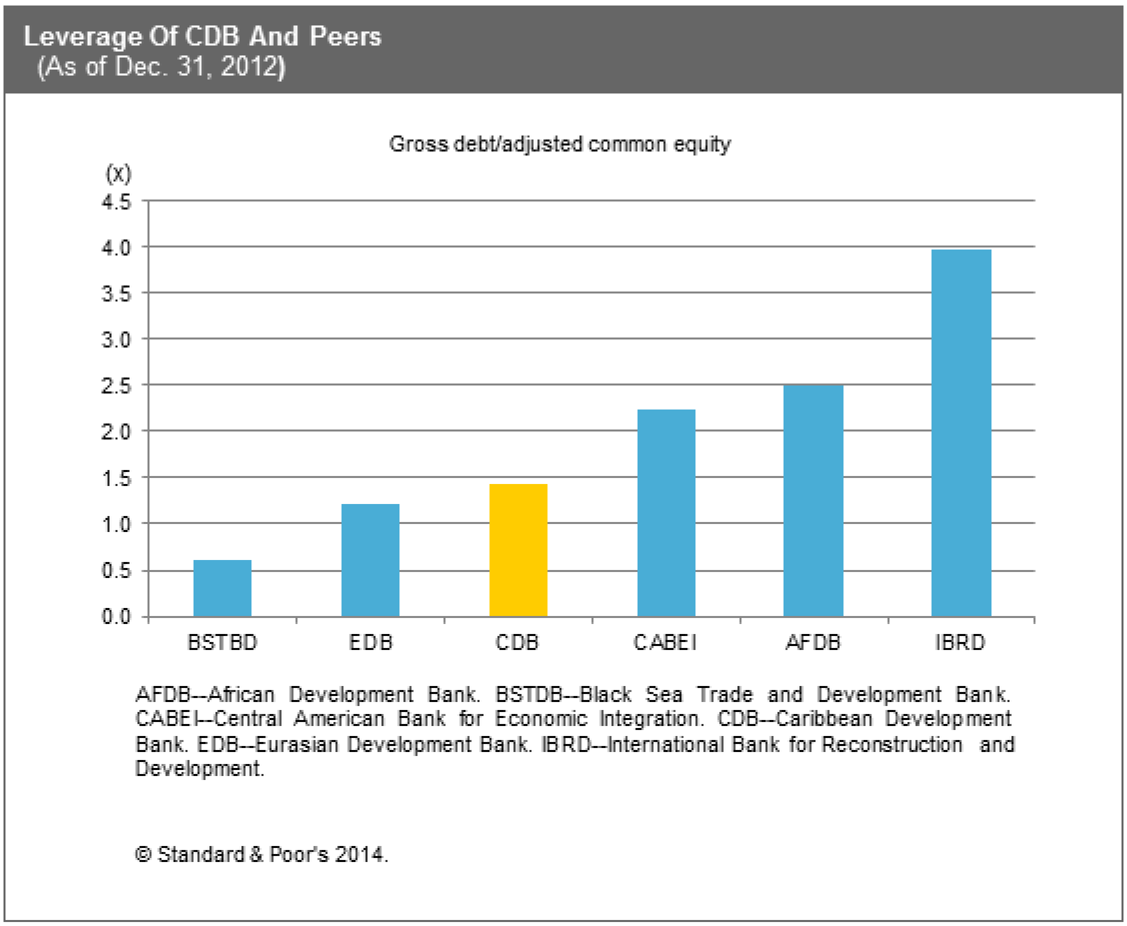
Funding Ratios					
	--As of Dec. 31--				
	2013	**2012**	**2011**	**2010**	**2009**
Static funding gap§ without loan disbursements at 1 year (x)	1.3	1.4	1.0	N/A	N/A
Static funding gap§ with half of scheduled loan disbursements at 1 year (x)	0.7	1.0	0.7	N/A	N/A
Short-term debt (by remaining maturity)/adjusted total assets (%)	10	12	15	1	9

Table 8

Funding Ratios (cont.)					
Gross debt/adjusted total assets (%)	45	54	54	50	54
Gross debt net of liquid assets/adjusted total assets (%)	22	25	34	41	28
Short-term liabilities (by remaining maturity)/total liabilities (%)	21	22	27	2	16
Total liabilities/adjusted total assets (%)	47	56	55	51	54
Gross debt/adjusted common equity (x)	1.0	1.4	1.4	1.2	1.4
Short-term debt (by remaining maturity)/gross debt (%)	22	23	27	2	17

Short-term debt by remaining maturity includes short-term debt (maturing in less than 12 months) and long-term debt maturing in the next 12 months. §The static funding gap is maturing assets divided by maturing liabilities. It is cumulative and based on scheduled receipts and payments. N/A--Not available.

Chart 3



Liquidity

CDB retains appropriate balance sheet liquidity of sufficient quality to fund its operations, debt service, and at least half of committed loan disbursements for up to one year without capital market access under a severe stress scenario. The bank met this threshold at year-end 2013, and its greater cash reserve raised its liquidity ratios at the end of the first quarter. This assumes that CDB will disburse $90 million loans this year and that the bank receives debt service from borrowers on time and in full.

CDB holds greater balance sheet liquidity--and hence its liquidity ratios are by necessity stronger by our measure--than its larger regional and global peers that maintain a stronger capital market presence (AFDB and IBRD). CDB has a similar static funding gap as CABEI, another subregional development bank, after we discount its deposit liabilities (which we assume would behave as wholesale funding in a crisis) and its commercial paper program (for which we assume demand would erode under our stress scenario). BSTDB and EDB, similarly sized small banks with infrequent capital market issuance, have higher static funding gaps.

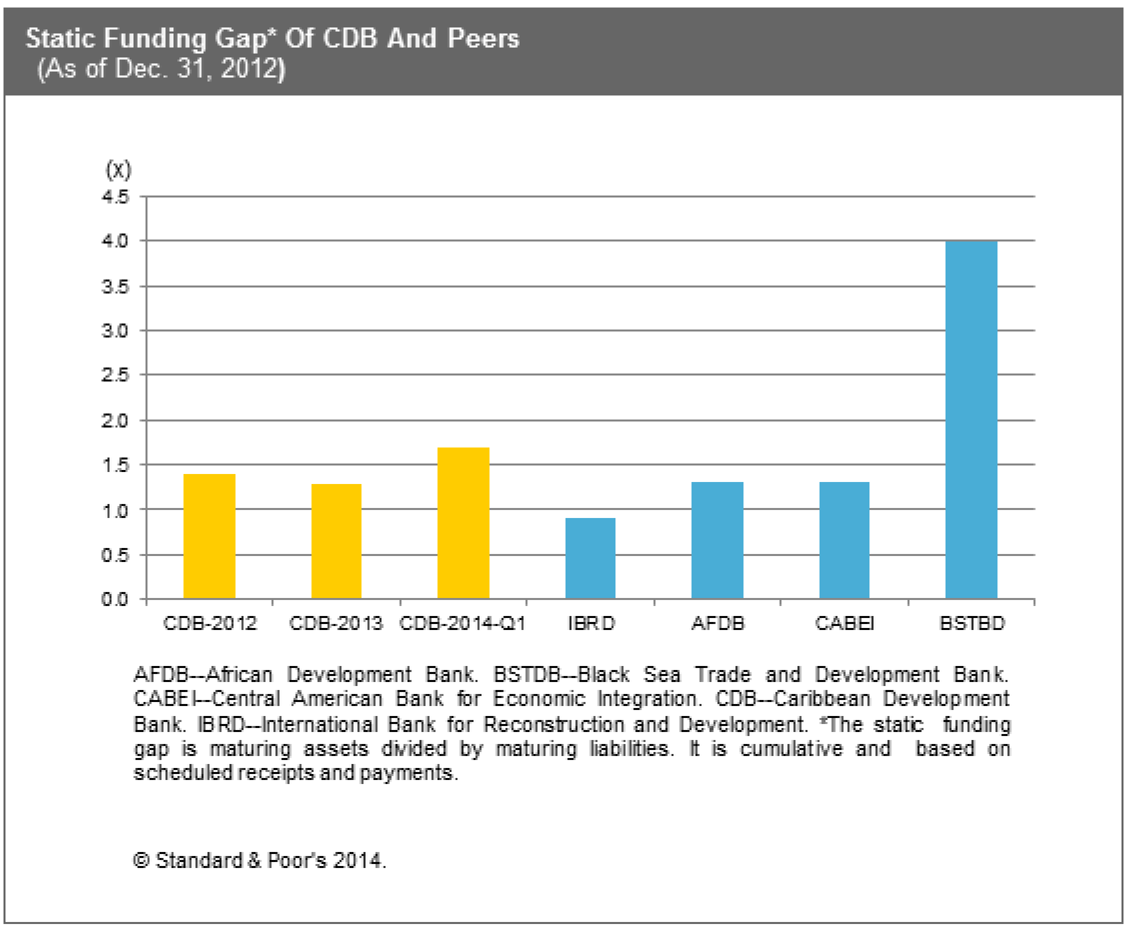
Table 9

Liquidity Ratios

	--As of Dec. 31--				
(%)	**2013**	**2012**	**2011**	**2010**	**2009**
Liquid assets/adjusted total assets	23	29	20	8	26
Cash and cash equivalents/liquid assets	19	20	25	9	29
Securities/liquid assets	81	80	75	91	71
Liquid assets/gross debt	52	54	38	17	47
Liquid assets/short-term debt by remaining maturity	234	236	138	809	285

Note: Short-term debt by remaining maturity includes short-term debt (maturing in less than 12 months) and long-term debt maturing in the next 12 months.

Chart 4



Likelihood of Extraordinary Shareholder Support

The 'AA' long-term foreign-currency ICR on CDB incorporates one notch of uplift to CDB's 'aa-' SACP based on our expectation of extraordinary shareholder support. CDB's higher-rated shareholders (Canada, Germany, and the U.K.) provide the bank $328 million eligible callable capital. In the event of a capital call, we expect these shareholders would provide the bank this extraordinary support. The amount of this callable capital is sufficient to raise CDB's RAC with callable capital firmly into the highest, "extremely strong" capital adequacy bracket.

Appendix

Table 10

Summary Balance Sheet

	--As of Dec. 31--				
(US$ mil.)	**2013**	**2012**	**2011**	**2010**	**2009**
Assets					
Cash and money market instruments	68	96	79	9	99
Securities	283	394	242	101	240
Liquid assets	351	491	322	111	339
Net loans	968	981	1,013	994	818
Equity investments	0	0	0	0	0
Purpose-related assets (gross)	979	994	1,019	998	820
Purpose-related assets (net)	975	987	1,014	996	818
Derivative assets	54	95	120	97	56
Accrued receivables	11	2	10	11	18
Total assets	1,452	1,641	1,535	1,269	1,285
Total adjustments to shareholders' equity	(41)	(54)	(56)	(39)	(44)
Total adjusted assets*	1,493	1,694	1,592	1,308	1,329
Liabilities					
Total deposits	52	81	59	7	81
Other borrowings (gross debt)	674	917	857	652	717
Other liabilities	35	29	12	12	6
Memo: Derivative liabilities	7	**	**	**	**
Total liabilities	709	947	869	664	722
Shareholders' equity					
Paid-in capital and surplus	256	219	186	157	157
Retained earnings	487	488	488	447	406
Shareholders' equity	744	694	666	605	563
Memo:					
Dividends (not yet distributed)	0	0	0	0	0
Eligible callable capital	328	328	328	210	137
Total guarantees	12	12	12	8	8

Table 10

Summary Balance Sheet (cont.)					
Undisbursed loans	290	285	132	150	199

*Adjustments made to reported shareholders' equity to calculate adjusted common equity (an institution's cash capital) are carried through to total assets. **Previously the bank consolidated its derivative liablities (cross currency interest rate swaps) in the presentation of its debt liabilities.

Table 11

Adjusted Common Equity

	--As of Dec. 31--				
(US$ mil.)	**2013**	**2012**	**2011**	**2010**	**2009**
Shareholders' equity (reported)	744	694	666	605	563
Plus (+):					
Capital subscription payments received in advance	13	4	5	6	N/A
Less (-):					
Capital payments committed (subscribed) but not yet due	N/A	N/A	N/A	N/A	N/A
Capital payments due but not yet received	7	11	16	N/A	N/A
Promissory notes receivable*	44	44	44	44	43
Maintenance of value receivables on currency holdings§	3	3	1	1	1
Capital subscriptions in restricted currencies	N/A	N/A	N/A	N/A	N/A
Unrecognized employee pension or other postretirement benefit liability	N/A	N/A	N/A	N/A	N/A
Total adjustments to shareholders' equity	(41)	(54)	(56)	(39)	(44)
Adjusted common equity	702.6	640.5	610.2	565.3	519.1

*Promissory notes are notes from shareholders, which a multilateral financial institution may have accepted from shareholders in lieu of cash capital and which are carried on the balance sheet as shareholders' equity. Promissory notes exclude callable capital, which most institutions do not count as balance sheet capital. §Currency fluctuations between an institution's operating currency and capital valued in restricted currency generate maintenance of value (MOV) assets and liabilities for some multilateral financial institutions. Standard & Poor's deducts MOV assets from shareholders' equity. N/A--Not available.

Table 12

Summary Statement of Income

(US$ mil.)	**2013**	**2012**	**2011**	**2010**	**2009**
Interest income	43	43	43	46	52
Interest expense	21	13	8	8	12
Net interest income	22	30	36	38	40
Operating noninterest income	8	6	0	1	0
Other noninterest income	2	1	0	0	0
Operating revenues	51	49	43	47	52
Noninterest expenses	11	11	10	10	9
Credit loss provisions (net new)	1	3	3	-	1
Operating income after loss provisions	17	22	23	29	30
Net income	17	22	23	29	30
Other comprehensive income	(6)	(11)	18	13	(9)
Comprehensive income	12	10	41	41	21
Memo:					
Net increase (decrease) in cash and cash equivalents during the year	(29)	17	70	(89)	2

Table 13

Membership, Capital And Voting Shares

	--As of Dec. 31, 2013--	
	Subscribed capital (mil. US$)	**% voting shares**
Total shareholders		
Total shareholders	1,566	100
Borrowing eligible members	914	58
Non-borrowing-eligible members	652	42
Borrowing-Eligible Members		
Jamaica	292	18
Trinidad & Tobago	292	18
Bahamas	86	5
Guyana	63	4
Barbados	55	4
Suriname	25	2
Belize	13	1
Dominica	13	1
Grenada	11	1
St. Lucia	13	1
St. Vincent and the Grenadines	13	1
Antigua and Barbuda	13	1
St. Kitts and Nevis	5	0
Haiti	5	0
Anguilla*¶	3	*
Montserrat*	3	*
British Virgin Islands*	3	*
Cayman Islands*	3	*
Turks and Caicos Islands*	3	*
Subtotal	914	58
Non-Borrowing-Eligible Members		
Venezuela	47	3
Colombia	47	3
Mexico	19	1
Canada	157	10
U.K.	157	10
Italy	38	2
Germany	94	6
People's Republic of China	94	6
Subtotal	652	42

*These territories collectively share one governor and have 1.01% of shares and 1.04% of votes. ¶Anguilla was formerly part of St. Kitts-Nevis-Anguilla but became an independent entity in 1980; it now shares a governor with the four other territories. Source: Caribbean Development Bank Financial Statements 2013 of the Ordinary Capital Reserves.

Related Criteria And Research

Related Criteria

- Multilateral Lending Institutions And Other Supranational Institutions Ratings Methodology, Nov. 26, 2012
- Methodology: Short-Term/Long-Term Ratings Linkage Criteria For Corporate And Sovereign Issuers, May 15, 2012
- Bank Capital Methodology And Assumptions, Dec. 6, 2010
- Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Supranationals: Special Edition 2013: Comparative Data For Multilateral Lending Institutions, March 11, 2014
- Research Update: Grenada Foreign And Local Currency Ratings Remain 'SD', Jan. 31, 2014
- Research Update: Belize 'B-/B' Ratings Affirmed; Outlook Remains Stable, Nov. 27, 2013
- Research Update: Barbados Long-Term Rating Lowered To 'BB-' From 'BB+'; Outlook Negative, Nov. 20, 2013
- Research Update: Jamaica Ratings Raised To 'B-/B' On Improving External Funding; Outlook Stable, Sept. 24, 2013
- How An Erosion Of Preferred Creditor Treatment Could Lead To Lower Ratings On Multilateral Lending Institutions, Aug. 26, 2013
- For Development Banks, Callable Capital Is No Substitute For Paid-In Capital, Dec. 31, 2009

Ratings Detail (As Of June 4, 2014)		
Caribbean Development Bank		
Counterparty Credit Rating		
Foreign Currency		AA/Stable/A-1+
Senior Unsecured		AA
Counterparty Credit Ratings History		
16-May-2014	*Foreign Currency*	AA/Stable/A-1+
12-Dec-2012		AA/Negative/A-1+
12-Jun-2012		AA+/Stable/A-1+

*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.