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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 extremely strong financial profile, as Standard & Poor's defines these terms. Together, these form CDB's 'aa' stand-alone credit profile (SACP). Our credit ratings pertain only to CDB's Ordinary Capital Resources (OCR), the bank's primary operations. CDB's higher-rated shareholders have provided the bank $328 million in eligible callable capital (enough to raise its capital adequacy by one notch). However, because CDB's balance-sheet capital adequacy now reaches the top of our scale, we do not incorporate any uplift above the SACP for our expectation of extraordinary shareholder support to the 'AA' long-term foreign currency issuer credit rating.

Established in 1969, CDB provides loans and guarantees aimed at aiding the economic development of governments and companies in the Caribbean. CDB had $1.4 billion in adjusted total assets as of Dec. 31, 2014.

CDB's strong business profile reflects, first, its role as a prominent lender in the Caribbean and its ability to lend to sovereigns throughout 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 continued to be late in paying their subscriptions. Third, the bank's borrowing members have treated CDB's OCR as a preferred creditor in most periods of stressed external liquidity, with one exception in 2012. 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 OCR. The bank has also continued to strengthen its governance structure through the consolidation of its risk management and monitoring framework, as well as through the introduction of new institutional checks and balances.

Working against these factors, CDB has significant embedded credit risk in its portfolio, and the majority of voting rights rest 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.

CDB's extremely strong financial profile reflects its strengthening capital adequacy, its less diversified funding profile, and its solid liquidity. 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 to the common characteristics of many of its borrowers. These include economic structure, monetary arrangements, fiscal challenges, and reliance on foreign savings. The bank's concentration in its top three sovereign exposures has declined moderately over the past several years, but it remains significant. 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 we don't rate (Saint Vincent and the Grenadines and Saint Lucia) (see "Sovereign Ratings And Country T&C Assessments," published April 17, 2015).

CDB's risk-adjusted capital (RAC) ratio continued to improve to 26% as of Dec. 31, 2014, from 23% a year earlier because of additional shareholder general capital increase (GCI) payment installments, higher internal capital generation, and persistently weak borrower demand. Although the bank's net loans outstanding increased in 2014, they were up by only 1.5% compared with 2013, which did not push loans above the levels reached in 2011. Additionally, CDB decided not to refinance its $150 million bond due in July 2014, and instead used its liquid assets to pay the bond, shrinking the size of its balance sheet.

We expect these factors and CDB's long-dated funding profile will minimize its financing needs over 2015-2016. As of year-end 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, CDB 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 profile.

## Outlook

The rating outlook is stable. In our view, CDB will maintain high capitalization to offset the embedded credit risk in its sovereign loan portfolio, particularly as its borrower members continue their fiscal consolidation efforts in 2015. We believe that the fiscal reform continued this year by the bank's borrowing members, in addition to the further improvement of the external liquidity vulnerabilities of some of CDB's lowest-rated members, strengthen borrowers' capacity to service their U.S. dollar-denominated debt to the bank. Potential moderate credit deterioration of some of CDB's borrowing members would have only a limited effect on the bank's capital adequacy, by our calculations.

That said, if CDB's embedded credit risk declined significantly, or its nonborrowing membership markedly increased, we could raise the ratings. On the other hand, we could lower the ratings if--contrary to our expectations--any of CDB's members no longer treated 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 extremely strong financial profile.

Our analysis draws comparisons with several peers (see table 1). We selected this sample of multilateral development banks for their concentration of activities in emerging and frontier markets, as well as their regional or subregional focus. 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 2014 financial statements as of the date of this report.



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**Table 1**

**Selected Comparative Statistics For CDB And Peers**

**As of Fiscal Year-End 2013**

| | | Total adjusted assets (mil. US$) | 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 one year (x) |
|---|---|---|---|---|---|---|---|
| Caribbean Development Bank | (CDB) | 1,493.25 | 24 | 66 | 1.0 | 24 | 1.3 |
| Corporacion Andina de Fomento | (CAF) | 27,418.32 | 15 | 66 | 2.0 | 30 | 1.2 |
| Central American Bank for Economic Integration | (CABEI) | 7,537.24 | 11 | 72 | 2.1 | 26 | 1.5 |
| Fondo Latinoamericano de Reservas | (FLAR) | 6,037.41 | 120 | 7 | N.M. | 92 | 1.3 |
| Eurasian Development Bank | (EDB) | 4,593.66 | 18 | 59 | 1.7 | 43 | 5.2 |
| Black Sea Trade and Development Bank | (BSTDB) | 932.20 | 42 | 83 | 0.5 | 19 | 7.6 |

RAC--Risk adjusted capital ratio. ACE--Adjusted common equity. *Ratings parameters as of July 31, 2014. N.M.--Not meaningful.

## Business Profile: Strong

CDB has a strong business profile, in our opinion, reflecting the bank's role, public policy mandate, and governance.

## Policy Importance Assessment

Since its establishment in 1969, CDB has served a prominent role as the cornerstone lender to Caribbean governments (96% of loans, as of Dec. 31, 2014) and to several private financial institutions (4% of loans) in the region. CDB provides long-term project financing, often with grace periods and below-market rates of interest. In addition, CDB has provided guarantees, including partial guarantees on rescheduled commercial bonds that were effective in increasing commercial creditors' participation. The bank also provides grants and low-interest loans to its poorest members via the SFR.

**Table 2**

**Principal Business Activities**

| | --As of Dec. 31-- | | | | |
|---|---|---|---|---|---|
| | **2014** | **2013** | **2012** | **2011** | **2010** |
| Purpose-related assets (gross) / adjusted total assets (%) | 70 | 66 | 59 | 64 | 76 |
| Net loans / adjusted total assets (%) | 69 | 65 | 58 | 64 | 76 |
| Public-sector (including sovereign-guaranteed) loans / total loans (%) | 96 | 95 | 95 | 95 | 95 |
| Private-sector loans / total loans (%) | 4 | 5 | 5 | 5 | 5 |
| **Memo (mil. US$)** | | | | | |
| Total guarantees | 12 | 12 | 12 | 12 | 8 |

**Table 2**

| Principal Business Activities (cont.) | | | | | |
|---|---|---|---|---|---|
| Total adjusted assets* | 1,430 | 1,493 | 1,694 | 1,592 | 1,308 |

*Adjustments made to reported shareholders' equity to calculate adjusted common equity (an institution's cash capital) are carried through to total assets.

CDB demonstrated its ability to lend countercyclically in the wake of the Great Recession. The bank increased its net loans outstanding by 6% and 21% during 2009 and 2010, respectively. Sovereign customer demand slackened from 2012-2013 as many borrowing member countries consolidated their fiscal positions, reducing their capital project financing demands. Net loans outstanding picked up very slightly, by 1.5% compared with 2013, following two years of decline. However, we expect the uptick in demand to remain subdued over the next couple of years as borrowing members continue to focus on fiscal consolidation.

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 late in paying their subscriptions because of, among other issues, parliamentary delays and budgetary difficulties. These totaled $5.6 million as of April 15, 2015. Overall, CDB received $43.2 million in instalments of the GCI during 2014.

Shareholders remain highly supportive of CDB. 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. In 2014, the bank allocated $6 million out of its operating income into its concessionary funds (the SFR) to finance its special operations, which the bank uses to provide resources on concessional terms to borrowing members for poverty reduction.

The bank's borrowing members have treated CDB's OCR as a preferred creditor in most periods of stressed external liquidity and recent debt reschedulings, with one exception, in 2012. During that year, a sovereign borrower defaulted on an OCR loan that CDB issued 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 directors have approved these cases following hurricanes (Dominica and Grenada), volcano eruptions (Montserrat), and 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 continues to strengthen its governance structure through the consolidation of its risk management and monitoring framework, as well as through the introduction of new institutional checks and balances. In 2013, CDB established the Office of Risk Management to monitor and manage all risks that CDB faces, including strategic, financial, operational, and reputational risks. Since then, CDB has fully incorporated this office into the bank's operations. Additionally, in 2015, CDB introduced a new strategic framework for "Integrity, Compliance, and

Accountability" for matters of fraud, corruption, ethics, financial crimes and project-related accountability, for which it expects to develop a new independent office shortly.

The bank carries large single-name sovereign loan exposures, particularly to its top three borrowers, on its balance sheet, though this concentration slightly decreased in 2014. CDB sets portfolio exposure limits, but these are more expansive than development banks with more diversified exposure. 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. CDB's large sovereign loan portfolio also has significant geographic (Caribbean) and economic (tourism-intensive and U.S. and European market) risk embedded in it. 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 (57% as of Dec. 31, 2014) 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 | 57 | 43 | 0 |

As of Dec. 31, 2014.

CDB does not pay dividends. In practice, shareholders have also minimized transfers from retained earnings to the SFR, the bank's grant facility, which offers low, fixed interest rates and extended maturities. In 2014, CDB transferred $6 million from operating income to the SFR, and we expect similar transfers in the future. This transfer represented about 15% of 2014 comprehensive income. This is in contrast with some other banks, such as the Inter-American Development Bank (IADB) and the International Bank for Reconstruction and Development (IBRD), which regularly transfer a large portion of earnings to their concessional financing facilities (Special Fund for Operations and International Development Association, 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) at a minimum of 150% of baseline economic capital. CDB's available capital was 204% of its economic capital and therefore was compliant with its internal policy as of Dec. 31, 2014. This framework better enables the bank to monitor possible changes in its RAC ratio.

CDB has traditionally used leverage conservatively, with 1.2x average over the past decade. CDB's policy limits borrowing and guarantees 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 48% as of the end of 2014.

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 this policy through 2014.

In 2014, CDB had two private-sector impaired loans, which were more than fully provisioned. Impaired loans reached $5.4 million as of Dec. 31, 2014, which represents 15% of nonsovereign loans and 0.5% of total loans. The impaired loans originated from a Caribbean developmental financial institution. Total provisions for nonsovereign loans reached approximately $6.3 million as of year-end 2014. In addition, collateral for impaired nonsovereign loans was about $5.9 million as of the same period.

Ernst & Young (Barbados), independent external auditors of the bank, issued a clean opinion of CDB's annual financial statements prepared in accordance with International Financial Reporting Standards (IFRS) for the period ending Dec. 31, 2014.

## Financial Profile: Extremely Strong

In our opinion, CDB has an extremely strong financial profile. This opinion is based on our assessment of CDB's capital adequacy as well as its funding and liquidity profile.

## Capital Adequacy

CDB's RAC adequacy continued to improve over 2014, reflecting shareholder payments of GCI instalments, higher internal capital generation, and still-subdued borrower demand.

The quality of CDB's cash capital, what we call 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.

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. In 2014, realized rates of return were lower than those initially estimated, and contributed to a $7.8 million net actuarial loss, which raised CDB's net actuarial liability to $14.9 million as of Dec. 31, 2014, from $9.6 million as of Dec. 31, 2013.

Similar to other multilateral institutions (MLIs) founded in the same era, CDB enabled members to post their capital contributions in cash or promissory notes ("nonnegotiable 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 discounting 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 means it can be less profitable than a commercial bank. In return for providing the bank with high earnings retention, borrowing members receive concessional loans, often at below-market interest rates.

CDB's earnings improved slightly in 2014, compared with 2013, though they still remain below historical averages. The bank's $20 million net income from operations (from which we exclude unrealized gains and losses on securities and derivatives) increased to 1.4% of average adjusted assets in 2014 from 1.1% in 2013, though this is still lower than the 2% plus in 2010 and earlier. CDB's net interest income relative to average net loans was 2.3% in 2014, slightly up from 2013 (but lower than 4.2% in 2010), while the bank's interest expense has continued to rise to 3.4% of average borrowings. However, the latter reflects the decrease of borrowings, as the nominal interest expense has declined. In September 2014, CDB entered an interest-rate swap to hedge the second half of its $300 million 4.375% bond due 2027 (the bank hedged the first half in 2013). CDB's efficiency ratio, or administrative expense per average ACE, remained low and stronger than many peers' at 1.5% in 2014.

The bank's loan income is highly sensitive to the performance of its top three borrowers. The bank derived about 49% of the its loan-related income from these borrowers in 2014, and 23% was from Jamaica.

Higher internal capital generation, despite a $6 million transfer to its SFR funds, as well as shareholders' payment of GCI instalments, contributed to a 9.6% growth in ACE in 2014, following 9.7% growth in 2013.

**Table 4**

| Profitability | | | | | |
|---|---|---|---|---|---|
| **(%)** | **2014** | **2013** | **2012** | **2011** | **2010** |
| Net income / average adjusted assets | 1.4 | 1.1 | 1.3 | 1.6 | 2.2 |
| Net income / average adjusted common equity | 2.7 | 2.6 | 3.5 | 3.9 | 5.3 |
| Comprehensive income / average adjusted assets | 2.8 | 0.7 | 0.6 | 2.8 | 3.2 |
| Comprehensive income / average adjusted common equity | 5.5 | 1.8 | 1.7 | 6.9 | 7.7 |
| Net interest income / average net loans | 2.3 | 2.2 | 3.0 | 3.6 | 4.2 |
| Interest expense / average borrowings | 3.4 | 2.7 | 1.5 | 1.0 | 1.2 |
| Administrative expense / average adjusted common equity | 1.5 | 1.6 | 1.8 | 1.7 | 1.9 |
| **Memo:** | | | | | |
| Net income (US$ mil.) | 20 | 17 | 22 | 23 | 29 |
| Net increase (decrease) in cash and cash equivalents during the year | (34) | (29) | 17 | 70 | (89) |

## Treasury risk

CDB takes on more treasury-related risk than its regional and subregional peers. The bank uses two different accounting methods to report its derivatives relative to the 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 the risk prudently, in our view. At the close of 2014, the bank had invested the bulk of its liquidity investments--16% of adjusted total assets--in unencumbered securities that we rate 'AA-' or higher (or the equivalent by another agency).

The remaining liquidity investments were cash and deposits--totaling 3% of adjusted assets--in investment-grade 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 Dec. 31, 2014.

### Interest rate risk

Historically, CDB has managed its interest rate risk fundamentally by using moderate leverage. Its use of shareholders' equity funding (totaling about half of adjusted 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 in its borrowings. Interest and principal is payable quarterly, and CDB may reset the interest rate semiannually. The bank issues floating-rate debt when possible, or it swaps fixed-rate issues effectively to floating-rate obligations when this is cost effective.

At the end of 2014, all of CDB's long-term market borrowings were fixed rate. However, the bank held two dual currency interest-rate swaps in order to transform its two yen-denominated borrowings, one which carries an interest rate of 2.75% and the other, 4.35%, into floating-rate obligations, and two additional interest-rate swaps in order to transform the entire amount of its $300 million fixed-rate bond, which carries a 4.375% interest rate, into a floating-rate obligation.

CDB manages its risk of asset-liability maturity mismatch through the use of appropriate durations, by maintaining sufficient balance-sheet liquidity and via access to contingency financing. 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 Dec. 31, 2014. In practice, it also matches the long-dated loans with borrowings of similar maturity. The bank's average loan maturity was 6.6 years versus 10.0 years for its borrowings.

### 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 instalments are also payable in dollars. CDB had 70% of outstanding debt, as of Dec. 31, 2014, denominated in its currency of operation. The remaining 30% are CDB's two outstanding yen-denominated bonds. Interest on the bonds is payable in U.S. dollars, while the final principal is payable in yen. CDB hedges the exchange rate risk on these bonds using currency swap agreements, which converted the proceeds of these obligations into U.S. dollars.

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 bonds at historical cost.

## Risk Position

The bank's RAC ratio continued to rise to 26% after adjustments as of Dec. 31, 2014, from 23% as of Dec. 31, 2013. This change reflects receipts of paid-in capital, higher internal capital generation, and customer demand that is still subdued as borrowing governments with persistently high debt burdens continue their fiscal consolidations.

Although 2014 saw a very slight pickup in net loans outstanding, by 1.5%, following two years of decline, we expect the uptick in demand to remain subdued over the next couple of years as borrowing members continue to focus on fiscal consolidation. We expect that CDB's relative exposures will not alter much in 2015. 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, 2014**

| | Exposure (mil. US$) | Standard & Poor's RWA (mil. US$) | Average Standard & Poor's RW (%) |
|---|---|---|---|
| **Credit Risk** | | | |
| Government and central banks | 1,278 | 1,572 | 123 |
| Institutions | 191 | 53 | 28 |
| Corporate | 0 | 0 | 0 |
| Securitization | 0 | 0 | 0 |
| Retail | 10 | 6 | 61 |
| Other assets | 11 | 12 | 104 |
| Total credit risk | 1,490 | 1,644 | 110 |
| **Market risk** | | | |
| Equity in the banking book | 0 | 0 | 0 |
| Trading book market risk | -- | 0 | -- |
| Total market risk | -- | 0 | -- |
| **Operational risk** | | | |
| Total operational risk | -- | 116 | -- |
| RWA before MLI adjustments | | 1,759 | 100 |
| **MLI adjustments** | | | |
| Industry and geographic diversification | | (101) | (6) |
| Preferred creditor treatment | | (354) | (20) |
| Single-name concentration | | 1,629 | 93 |
| High-risk exposure cap | | 0 | 0 |
| Total MLI adjustments | | 1,175 | 67 |
| RWA after MLI adjustments | | 2,934 | 167 |
| | | **Adjusted common equity (mil. US$)** | **Standard & Poor's RAC ratio (%)** |
| Capital ratio before adjustments | | 770 | 43.8 |

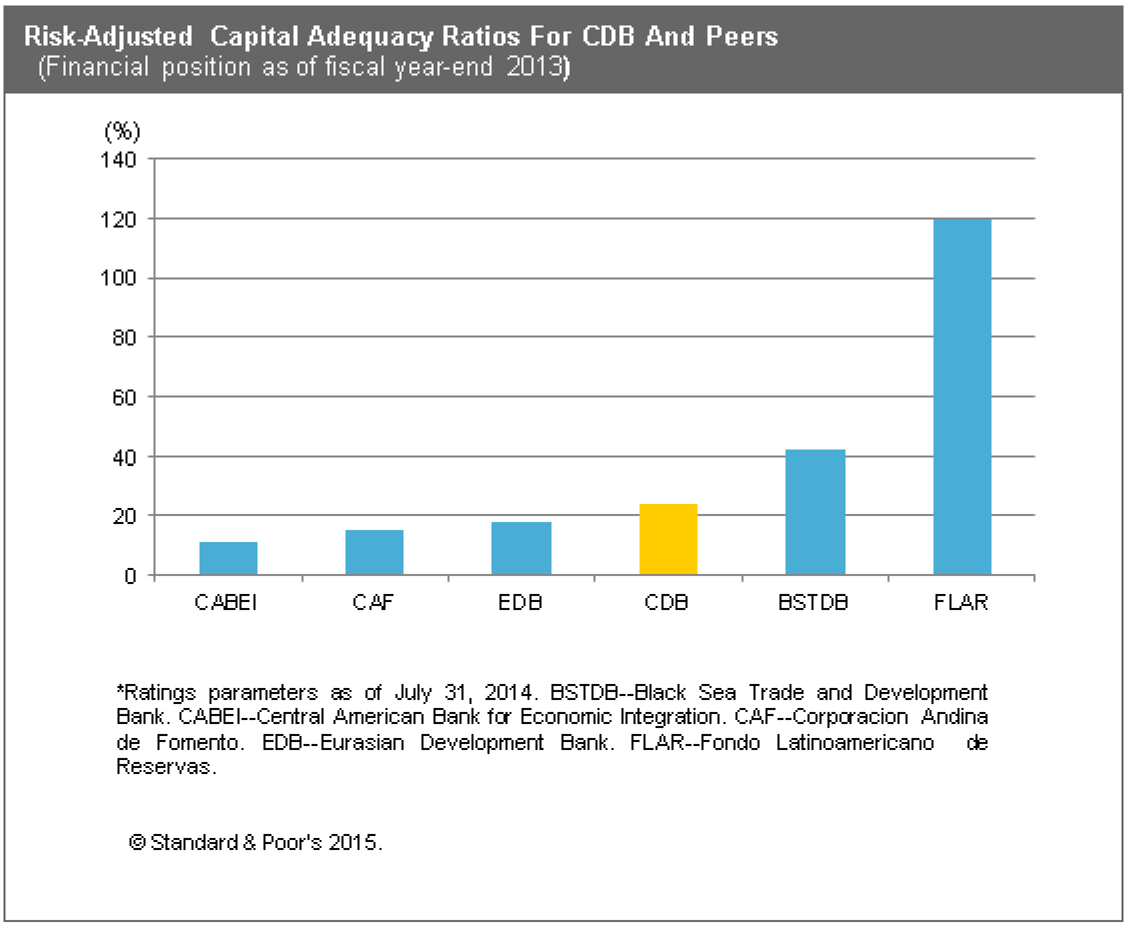
**Table 5**

| CDB's Risk-Adjusted Capital Adequacy As Of Dec. 31, 2014 (cont.) | |
|---|---|
| Capital ratio after adjustments | 26.3 |

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 April 30, 2015.

In comparison with peers, CDB is well-capitalized for its risk position. As of the end of fiscal year-end 2013, CDB maintained higher relative capital adequacy than the Central American Bank for Economic Integration (CABEI) and the Eurasian Development Bank (EDB), which are also subregional multilateral development banks with sizeable public-sector portfolios of similar loan products to CDB. In addition, CDB's capital adequacy was higher than that of the Development Bank of Latin America (CAF), a regional supranational institution.

**Chart 1**

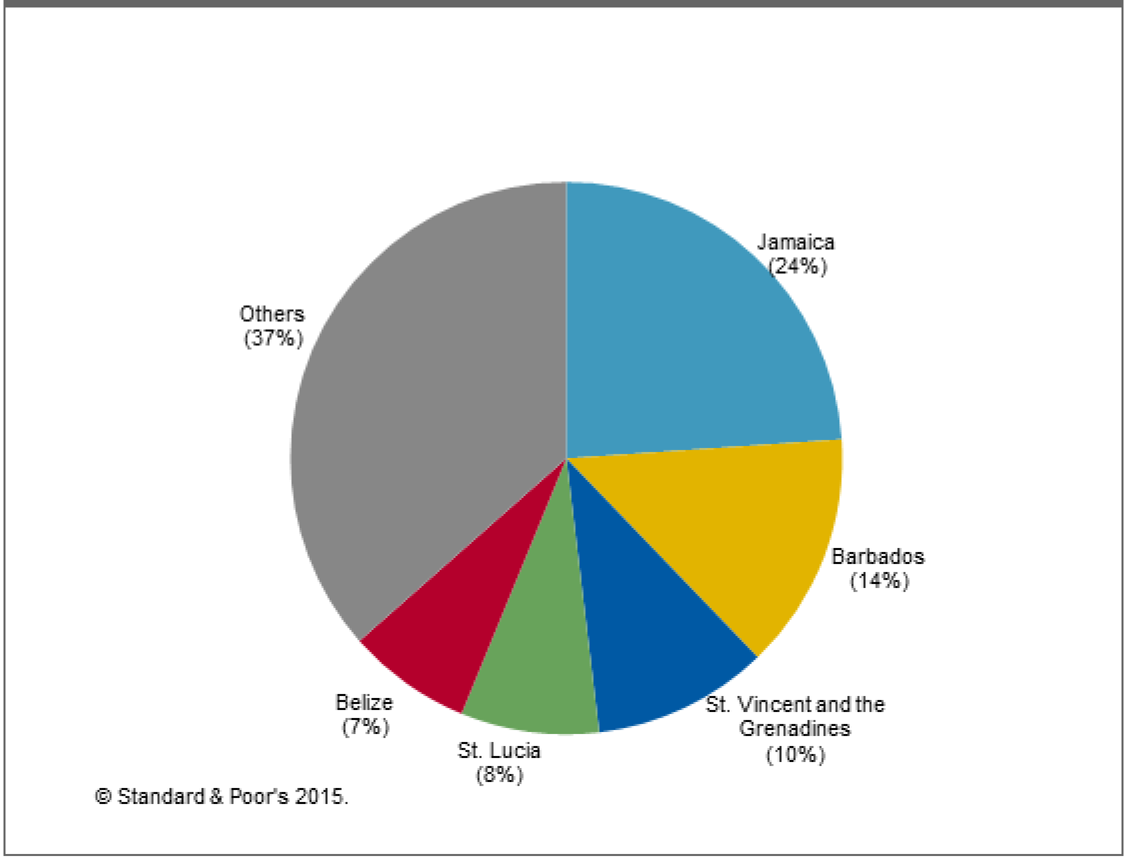



## Exposure concentrations

CDB maintains significant exposure concentrations 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 44% RAC before MLI-specific adjustments and the 26% RAC after.

**Chart 2**

CBD's Largest Loan Exposures (Unweighted) By Country (As of Dec. 31, 2014)




The bank's top three loan exposures represented 48% of loans and 61% of ACE (before risk-weighting) at the end of 2014. Exposure concentration has dropped over the past five years, as CDB's top three loan exposures represented 80% of ACE in 2010. In 2014, the largest exposure, Jamaica, represented 24% of loans, a slight drop from 25% in 2013. The second largest, Barbados, represented 14% in 2014 (same as 2013), followed by St. Vincent and the Grenadines (10% in 2014, compared with 11% in 2013). We calibrate the capital charge for potential loss on CDB's largest exposures 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**

| | 2015F | 2016F | --2014-- | | |
|---|---|---|---|---|---|
| | **Real GDP growth (% change)** | | **GDP per capita (US$)** | **Net general government debt (% GDP)** | **General government interest expense/ revenues (%)** |
| Antigua and Barbuda* | 1.9 | 2.3 | 14,061 | 98.7 | N.A. |
| Barbados | 1 | 2 | 15,063 | 88.8 | 15.3 |

**Table 6**

| Country Data And Projections For CDB's Top 10 Borrowing Members (cont.) | | | | | |
|---|---|---|---|---|---|
| Belize | 3 | 3 | 5,014 | 60.9 | 10.3 |
| Grenada | 1.5 | 1.5 | 8,224 | 97.5 | 9.6 |
| Jamaica | 2 | 2.2 | 5,000 | 116.3 | 30.8 |
| St. Kitts and Nevis* | 3.5 | 3.0 | 14,102 | N.A. | N.A. |
| St. Lucia* | 1.8 | 1.4 | 7,978 | N.A. | N.A. |
| St. Vincent and the Grenadines* | 2.1 | 3.1 | 6,694 | 70.9 | N.A. |
| Trinidad and Tobago | 0.85 | 2.05 | 21,975 | 18.1 | 4.6 |

*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 2015. F--Forecast. N.A.--Not available.

## Asset quality: loan loss experience

Preferred creditor treatment and the ability to restructure loans through SFR in advance of a borrower default have supported the asset quality of CDB's sovereign loan portfolio over the years. An exception to this practice occurred in 2012 when a sovereign borrower 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 Dec. 31, 2014.

CDB does not currently carry a 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 the bank's equity. CDB's ACE was 0.8x public-sector loans, as of the end of 2014.

The bank has experienced some 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 2014, CDB had minor levels of private-sector impaired loans, which were more than fully provisioned, in order to account for the loss of fees. These impaired loans represented 0.5% of total loans and originated from a Caribbean developmental financial institution.

**Table 7**

| Asset Quality | | | | | |
|---|---|---|---|---|---|
| | **--As of Dec. 31--** | | | | |
| | **2014** | **2013** | **2012** | **2011** | **2010** |
| Loan portfolio | | | | | |
| Impaired loans / total loans (%) | 0.5 | 0.5 | 1.1 | 1.1 | 1.1 |
| Impaired loans/total adjusted assets (%) | 0.4 | 0.3 | 0.7 | 0.7 | 0.8 |
| Impaired private-sector loans/total loans (%) | 0.5 | 0.5 | 1.1 | 1.1 | 1.1 |
| Impaired private-sector loans net of loan loss provisions/total loans (%) | (0.1) | 0.0 | 0.4 | 0.6 | 0.9 |
| Loan loss reserves for private-sector loans/impaired private-sector loans (%) | 118 | 92 | 67 | 47 | 19 |
| Loans loss provisions made in current year/net loans at previous year-end (%) | 0.7 | 0.5 | 0.7 | 0.5 | N.M. |
| Recoveries/impaired loans at previous fiscal year-end (%) | 0 | 32 | 0 | 0 | 0 |
| ACE / impaired loans (x) | 144 | 135 | 57 | 57 | 53 |

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, 2015, the guarantee had not been called.

## Funding and Liquidity

### Funding

CDB has a less-developed funding profile and less-diversified global investor base than peers such as CABEI and CAF. 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, CDB structured its $300 million, 15-year bond issued in 2012 to amortize the principal over the last five years to maturity. In 2014, CDB paid its maturing $150 million floating-rate bond, instead of refinancing, in order to reduce its cost of carry. As of year-end 2014, slightly more than 86% of CDB's borrowings were bonds, which are long-dated. The bank's next bullet maturity is 2022.

In addition to market borrowings and loans from EIB and IADB, CDB had $30 million outstanding in short-term borrowing as of year-end 2014, which represents the partial drawdown of $50 million credit line CDB has with the Royal Bank of Canada. Although CDB has historically not relied on short-term financing vehicles, it decided to use this line, given the favorable terms of the credit. CDB repaid this borrowing in February 2015.

We expect 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 most of its loan disbursements--not uncommon among the MLIs. CDB's static funding gap at one year (without consideration of loan disbursements) fell to 1.04x as of Dec. 31, 2014, from 1.3x as of Dec. 31, 2013. The bank used its cash reserves in July 2014 after paying its $150 million bond.

CDB has continued to reduce its leverage. The bank's gross debt-to-ACE ratio declined to 0.7x in 2014 from 1.9x in 2013, and we expect it to remain low this year. The bank continues to receive GCI capital instalments on the back of still-slow demand from their government borrowers (many of which continue to undergo fiscal consolidation).

**Table 8**

**Funding Ratios**

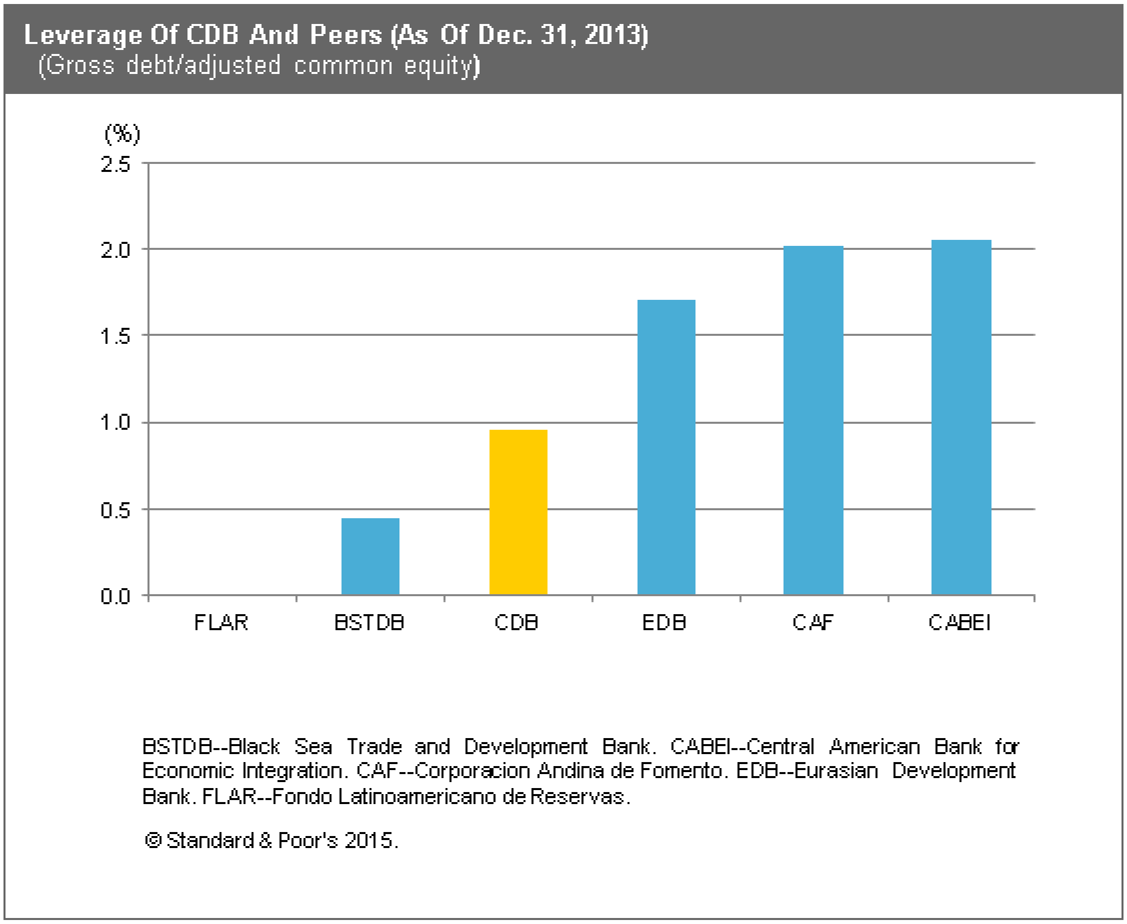
| | --As of Dec. 31-- | | | | |
|---|---|---|---|---|---|
| | **2014** | **2013** | **2012** | **2011** | **2010** |
| Static funding gap§ without loan disbursements at one year (x) | 1.0 | 1.3 | 1.4 | 1.0 | N.A. |
| Static funding gap§ with half of scheduled loan disbursements at one year (x) | 0.9 | 0.7 | 1.0 | 0.7 | N.A. |
| Short-term debt (by remaining maturity) / adjusted total assets (%) | 2 | 10 | 12 | 15 | 1 |
| Gross debt / adjusted total assets (%) | 37 | 45 | 54 | 54 | 50 |
| Gross debt net of liquid assets / adjusted total assets (%) | 18 | 21 | 25 | 33 | 41 |
| Short-term liabilities (by remaining maturity) / total liabilities (%) | 5 | 21 | 22 | 27 | 2 |
| Total liabilities / adjusted total assets (%) | 39 | 47 | 56 | 55 | 51 |
| Gross debt / adjusted common equity (x) | 1 | 1 | 1 | 1 | 1 |
| Short-term debt (by remaining maturity) / gross debt (%) | 6 | 22 | 23 | 27 | 2 |

**Table 8**

**Funding Ratios (cont.)**

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. §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 2014. This assumes that CDB will disburse $154 million this year and that the bank receives debt service from borrowers on time and in full. As of year-end 2014, CDB's liquidity decreased slightly from year-end 2013, which was partly the result of its use of liquid assets to pay the $150 million bond due in July 2014.

CDB holds greater balance-sheet liquidity--and hence its liquidity ratios are by necessity stronger by our measure--than its regional and global peers that maintain a stronger capital market presence (CABEI and CAF). CDB has a similar static funding gap as CABEI, another subregional development bank. However, BSTDB and EDB, similarly sized small banks with infrequent capital market issuance, have higher static funding gaps.

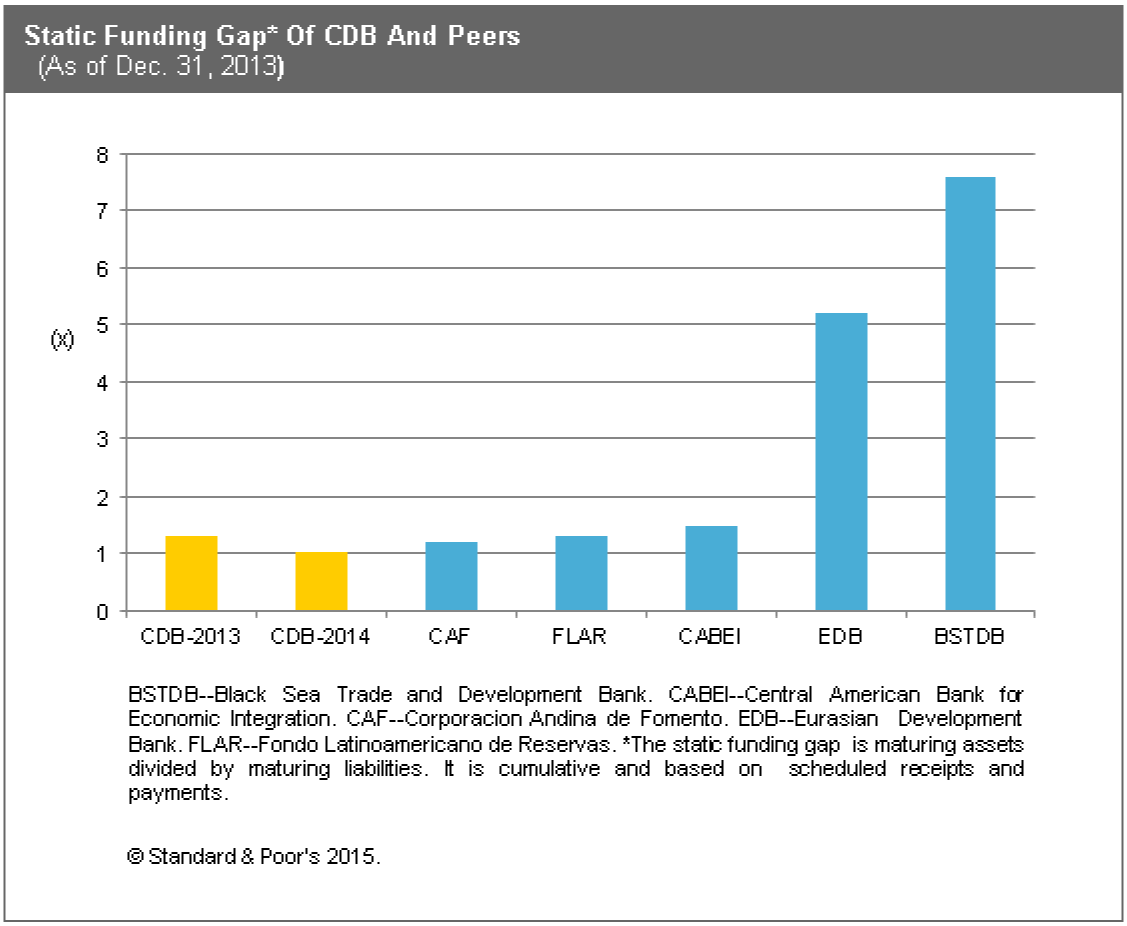
**Table 9**

**Liquidity Ratios**

| | --As of Dec. 31-- | | | | |
|---|---|---|---|---|---|
| **(%)** | **2014** | **2013** | **2012** | **2011** | **2010** |
| Liquid assets / adjusted total assets (%) | 19 | 24 | 29 | 21 | 9 |
| Cash and cash equivalents / liquid assets (%) | 16 | 22 | 20 | 26 | 13 |
| Securities / liquid assets (%) | 84 | 78 | 80 | 74 | 87 |
| Liquid assets / gross debt (%) | 51 | 54 | 54 | 38 | 18 |
| Liquid assets / short-term debt by remaining maturity* (%) | 898 | 243 | 238 | 141 | 854 |

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 issuer credit rating on CDB does not incorporate additional notching uplift above CDB's 'aa' SACP. Although CDB's higher-rated shareholders have provided the bank $328 million eligible callable capital (enough to raise its capital adequacy by one notch), CDB's balance-sheet capital adequacy (RAC ratio after adjustments of 26%) already reaches the top of our scale. Therefore, we do not need to incorporate any uplift for our expectation of extraordinary shareholder support.

## Appendix

**Table 10**

| Summary Balance Sheet | | | | | |
|---|---|---|---|---|---|
| | --As of Dec. 31-- | | | | |
| **(Mil. US$)** | **2014** | **2013** | **2012** | **2011** | **2010** |
| **Assets** | | | | | |
| Cash and money market instruments | 43 | 81 | 101 | 84 | 16 |
| Securities | 226 | 283 | 394 | 242 | 101 |
| Liquid assets | 269 | 364 | 495 | 327 | 117 |
| Net loans | 983 | 968 | 981 | 1,013 | 994 |
| Equity investments | 0 | 0 | 0 | 0 | 0 |
| Purpose-related assets (gross) | 995 | 979 | 994 | 1,019 | 998 |
| Purpose-related assets (net) | 989 | 975 | 987 | 1,014 | 996 |
| Derivative assets | 54 | 54 | 95 | 120 | 97 |
| Accrued receivables | (1) | (3) | (3) | 4 | 5 |
| Total assets | 1,379 | 1,452 | 1,641 | 1,535 | 1,269 |
| Total adjustments to shareholders' equity | (51) | (41) | (54) | (56) | (39) |
| Total adjusted assets* | 1,430 | 1,493 | 1,694 | 1,592 | 1,308 |
| **Liabilities** | | | | | |
| Total deposits | 32 | 52 | 81 | 59 | 7 |
| Other borrowings (gross debt) | 529 | 674 | 917 | 857 | 652 |
| Other liabilities | 28 | 35 | 29 | 12 | 12 |
| Memo: Derivative liabilities | N.A. | 7 | ** | ** | ** |
| Total liabilities | 557 | 709 | 947 | 869 | 664 |
| **Shareholders' equity** | | | | | |
| Paid-in capital and surplus | 299 | 256 | 219 | 186 | 157 |
| Retained earnings | 522 | 487 | 488 | 488 | 447 |
| Shareholders' equity | 822 | 744 | 694 | 666 | 605 |
| **Memo:** | | | | | |
| Eligible callable capital | 328 | 328 | 328 | 328 | 210 |
| Total guarantees | 12 | 12 | 12 | 12 | 8 |
| Undisbursed loans (100%) | 307 | 290 | 285 | 132 | 150 |

*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 liabilities (cross currency interest rate swaps) in the presentation of its debt liabilities. N.A.--Not available.

**Table 11**

## Adjusted Common Equity (ACE)

| | --As of Dec. 31-- | | | | |
|---|---|---|---|---|---|
| **(Mil. US$)** | **2014** | **2013** | **2012** | **2011** | **2010** |
| Shareholders' equity (reported) | 822 | 744 | 694 | 666 | 605 |
| **Plus (+):** | | | | | |
| Capital subscription payments received in advance | 9 | 13 | 4 | 5 | 6 |
| **Less (-):** | | | | | |
| Capital payments due but not yet received | 11 | 7 | 11 | 16 | N.A. |
| Promissory notes receivable* | 45 | 44 | 44 | 44 | 44 |
| Maintenance of value receivables on currency holdings§ | 4 | 3 | 3 | 1 | 1 |
| Total adjustments to shareholders' equity | (51) | (41) | (54) | (56) | (39) |
| Adjusted common equity (ACE) | 771 | 702 | 640 | 610 | 565 |

*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. N.M.--Not meaningful.

**Table 12**

## Summary Statement of Income

| **(Mil. US$)** | **2014** | **2013** | **2012** | **2011** | **2010** |
|---|---|---|---|---|---|
| Interest income | 43 | 43 | 43 | 43 | 46 |
| Interest expense | 20 | 21 | 13 | 8 | 8 |
| Net interest income | 23 | 22 | 30 | 36 | 38 |
| Operating noninterest income | 10 | 8 | 6 | 0 | 1 |
| Other noninterest income | 0 | 2 | 1 | 0 | 0 |
| Operating revenues | 53 | 51 | 49 | 43 | 47 |
| Noninterest expenses | 12 | 11 | 11 | 10 | 10 |
| Credit loss provisions (net new) | 2 | 1 | 3 | 3 | 0 |
| Operating income after loss provisions | 20 | 17 | 22 | 23 | 29 |
| Net income | 20 | 17 | 22 | 23 | 29 |
| Other comprehensive income | 21 | (6) | (11) | 18 | 13 |
| Comprehensive income | 41 | 12 | 10 | 41 | 41 |
| **Memo:** | | | | | |
| Net increase (decrease) in cash and cash equivalents during the year | (34) | (29) | 17 | 70 | (89) |

**Table 13**

## Membership, Capital, And Voting Shares

| | --As of Dec. 31, 2014-- | |
|---|---|---|
| | **Subscribed capital (mil. US$)** | **% voting shares** |
| **Total shareholders** | | |
| Total shareholders | 1,630 | 100 |
| Borrowing eligible members | 922 | 57 |

**Table 13**

| Membership, Capital, And Voting Shares (cont.) | | |
|---|---|---|
| Nonborrowing-eligible members | 709 | 43 |
| **Borrowing-eligible members** | | |
| Jamaica | 292 | 18 |
| Trinidad & Tobago | 292 | 18 |
| Bahamas | 86 | 5 |
| Guyana | 63 | 4 |
| Barbados | 55 | 3 |
| 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 | 13 | 1 |
| Anguilla*¶ | 3 | 0 |
| Montserrat* | 3 | 0 |
| British Virgin Islands* | 3 | 0 |
| Cayman Islands* | 3 | 0 |
| Turks and Caicos Islands* | 3 | 0 |
| Haiti | 5 | 0 |
| Subtotal | 922 | 57 |
| **Nonborrowing-eligible members** | | |
| Venezuela | 47 | 3 |
| Colombia | 47 | 3 |
| Mexico | 19 | 1 |
| Canada | 157 | 10 |
| U.K. | 157 | 10 |
| Italy | 94 | 6 |
| Germany | 94 | 6 |
| People's Republic of China | 94 | 6 |
| Subtotal | 709 | 43 |

*These territories collectively share one governor and have 0.96% of shares and 1.00% of votes. ¶Anguilla was formerly part of St. Kitts-Nevis-Anguilla but became an overseas British territory in 1980 and also shares a governor with the four other territories. Source: Caribbean Development Bank Financial Statements 2014 of the Ordinary Capital Reserves.

## Related Criteria And Research

### Related Criteria

- Methodology For Linking Short-Term And Long-Term Ratings For Corporate, Insurance, And Sovereign Issuers, May 7, 2013
- Multilateral Lending Institutions And Other Supranational Institutions Ratings Methodology, Nov. 26, 2012



1401988 | 301977158

- Bank Capital Methodology And Assumptions, Dec. 6, 2010

## Related Research

- Introduction to Supranationals Special Edition 2014, Oct. 8, 2014
- How An Erosion Of Preferred Creditor Treatment Could Lead To Lower Ratings On Multilateral Lending Institutions, Aug. 26, 2013

| Ratings Detail (As Of June 3, 2015) | | |
|---|---|---|
| **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. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.