MOODY'S
INVESTORS SERVICE

Rating Action: Moody's changes the outlook on the IBEC's rating to positive; affirms Baa3 rating

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London, 03 September 2021 -- Moody's Investors Service ("Moody's") has today changed the outlook on the International Bank for Economic Co-operation's (IBEC) rating to positive from stable and has affirmed IBEC's Baa3 long-term foreign currency issuer rating.

The decision to assign a positive outlook on the Baa3 rating is driven by:

1. IBEC's strengthening liquid asset buffer and ongoing diversification of funding sources which, if sustained, would improve resilience to liquidity shocks; and

2. Moody's expectation that IBEC's leverage will remain favourable relative to peers through its next growth phase, while ongoing diversification of the loan portfolio is reducing concentration risks.

Moody's affirmation of IBEC's Baa3 issuer rating balances its relatively strong capital position with the Bank's weak, but gradually improving, development asset credit quality and the risks to IBEC's asset performance from a challenging operating environment. The affirmation also reflects IBEC's low strength of member support given the absence of formal callable capital. The decision to affirm the rating also takes into account that the recent improvements to IBEC's liquidity buffer and funding structure are still at a relatively early stage.

Moody's will use the 12-18 month outlook period, and possibly going slightly beyond 18 months, to assess the extent to which the recent improvements in IBEC's liquidity buffer are sustained and the quality of IBEC's funding further improves. The outlook period will also help to confirm that leverage will remain moderate relative to peers over the next phase of the institution's development, while concentration risks further reduce.

RATINGS RATIONALE

RATIONALE FOR THE POSITIVE OUTLOOK

FIRST DRIVER: STRENGTHENING LIQUID ASSET BUFFER AND ONGOING DIVERSIFICATION OF FUNDING SOURCES

The first and main driver of the decision to assign a positive outlook is that the amount of high quality liquid assets which would be available in a stress scenario, albeit still limited relative to most other multilateral development banks (MDBs), has materially increased since the assignment of the rating in early 2020, while continued efforts to diversify funding sources are leading to a gradual improvement in IBEC's quality and structure of funding. If sustained, these improvements will help to improve IBEC's resilience to liquidity and funding shocks.

Treasury assets have risen in line with the growth in total assets, and continue to fully cover IBEC's short-term and currently maturing long-term debt. Importantly, IBEC's high quality liquid asset buffer has more than doubled from €28 million at the end of 2019 to €69 million at the end of 2020. As a result, Moody's assessment of the availability of unencumbered high quality liquid resources that would be available in a stress scenario and with minimal loss has improved notably. Based on Moody's definition, IBEC's cash and short-term bank deposits as well as securities rated A2 or higher at the end of 2020 cover a more manageable 31% of projected net cash outflows over the subsequent 18 months, compared with around 12% at the end of 2018. The credit quality of IBEC's overall treasury portfolio is also continuing to gradually improve, benefitting from an increasing share of European Union (EU, Aaa stable) issuers.

Moody's expectation that the improvements to the liquid asset buffer will be sustained over the medium term is supported by IBEC's relatively prudent, albeit still developing, liquidity risk-management framework. In particular, IBEC's liquidity risk management is focused on ensuring its liquidity coverage and net stable funding ratios remain above their internal risk triggers, alongside structural limits on the holdings of non-investment grade securities as well as an internal survival horizon requirement which ensures IBEC maintains sufficient liquidity over a 90-day window to cover contractual and planned outflows under the assumption of a 30%

haircut to liquidity.

Furthermore, IBEC's ongoing efforts to diversify its funding sources is helping to improve the quality and structure of its funding. In particular, the Bank is continuing to gradually establish a track record of market issuances after tapping the Russian bond market in October 2019 and June 2020. IBEC's bond issuance on Bulgaria's (Baa1 stable) capital market in June 2021, its first entry into the EU capital market, attracted a notable share of longer-term investors such as pension funds, and the Bank's strategy aims to further diversify its sources of long-term funding through bond issuances in other EU member states. IBEC is also benefitting from a broadening in its banking relationships and was able to access long-term bank funding during the pandemic to support its financing needs. The conclusion of a project specific financing arrangement with Eximbank of Russia (Ba1 long-term deposit rating, stable) for a term of 11 years is a further sign of the institution's improving ability to attract longer-term funding.

The diversification of funding has supported a gradual lengthening in the maturity of IBEC's funding structure, with long-term borrowings (greater than one year) accounting for around 50% of total funding as at end June 2021, up markedly since the end of 2018 when funding was predominantly on a short term basis.

Finally, IBEC's liquidity management continues to benefit from a naturally high asset turnover implicit in its focus on trade finance. These comparatively short maturities provide scope for the Bank to rapidly deal with liquidity shocks by adjusting planned lending disbursements. IBEC further benefits from access to a range of credit and repo arrangements across a number of lenders, including indicative limits from P-1 rated banks, which, while on a relatively short term basis, proved to be broadly reliable through the pandemic. Furthermore, IBEC's role as trustee of the International Fund for Technological Development may also provide the Bank, in agreement with Russia's (Baa3 stable) Ministry of Finance, with temporary access to unutilised liquidity within the fund, which can serve as an additional source of liquidity when needed.

SECOND DRIVER: LEVERAGE WILL REMAIN FAVOURABLE RELATIVE TO PEERS WHILE ONGOING PORTFOLIO DIVERSIFICATION IS REDUCING CONCENTRATION RISKS

The second driver supporting the positive outlook is Moody's expectation that IBEC's leverage will remain favourable relative to peers through the institution's next growth phase and continue to support the Bank's relatively strong capital position. Furthermore, the continuing diversification of the loan portfolio is helping to reduce concentration risks.

IBEC has seen a rapid expansion in its business activities and lending portfolio since its relaunch in 2018, with a correspondingly marked rise in Moody's definition of leverage to around 246% at the end of 2020, up from around 196% in 2019, albeit still remaining moderate relative to peers. The Bank's new five-year strategy, adopted in late 2020 and covering through to 2025, provides greater visibility around IBEC's next development phase, with plans for a marked further increase in the Bank's loan and documentary portfolio, to reach €728 million by 2025 from €418 million at the end of 2020. The emphasis will be to grow IBEC's trade finance and settlement operations, alongside a significant role for direct and syndicated lending.

That said, the pace of asset growth will moderate relative to 2019-2020 which will help maintain leverage at a favourable level compared to peers. Moody's forecasts leverage will rise to around 290% by end-2023, still below the median for Baa-rated peers and significantly lower than the leverage ratios of other MDBs with a similar trade finance focus such as African Export-Import Bank (Afrexim, Baa1 stable) and Eastern and Southern African Trade and Development Bank (TDB, Baa3 negative). According to IBEC's own estimates, the Bank's capital adequacy ratio is expected to fall to around 35% by 2025, still above the internal limit of 25%.

The continuing diversification of IBEC's loan portfolio will also support a gradual improvement in credit quality indicators, helping to mitigate the risks stemming from the Bank's weak weighted average borrower rating. Notably, both geographical and sectoral diversification have improved alongside the rapid expansion of the Bank's operations. Russia's share in the total loan and guarantees portfolio has more than halved since 2018, although Russia is still expected to remain one of IBEC's largest markets of operation. Furthermore, according to Moody's estimates, the Bank's top 10 exposures accounted for 57% of total development related assets on a gross basis at the end of 2020, down from 88% in 2018, and Moody's expects concentration risks in the portfolio will continue to decline during the next phase of IBEC's development.

Moreover, Moody's expects IBEC's improved risk management practices, which have been gradually enhanced since the institution's relaunch and tested to some extent by the disruptions engendered by the pandemic, will support the Bank in managing the risks to leverage and asset quality associated with the continued expansion of its loan portfolio. These enhancements include improvements to the procedure for controlling transaction limits, the implementation of new internal rating models, and the development of risk appetite parameters to guide the implementation of its strategy.

RATIONALE FOR AFFIRMING THE Baa3 RATING

The decision to affirm IBEC's issuer rating balances its relatively strong capital position with the Bank's weak, but gradually improving, development asset credit quality. In particular, the credit quality of IBEC's loan portfolio remains low, with a weighted average borrower rating of B1 at the end of 2020.

Furthermore, IBEC's asset performance will face risks from a challenging operating environment amid the still developing risk management framework and the relatively small overall number of borrowers. IBEC is exposed to the risk of a deteriorating operating environment in Belarus (B3 stable) amid the country's heightened political instability given that, while declining, the share of Belarus in total loans and guarantees still remains sizeable at around 10% as at end 2020 and relatively concentrated in a few counterparties. There is also the potential for the pandemic to have a delayed impact on borrower quality given the imposition of loan payment moratoriums by many countries in IBEC's territories. Moody's expects these pressures will likely push IBEC's non-performing asset ratio in the coming years above the current level of 1.7% of development related assets as at end 2020.

Furthermore, the rating affirmation reflects that the strength of member support remains low, with the absence of formal callable capital remaining a key weakness in IBEC's credit profile, albeit one that does not preclude a potential upgrade to a Baa2 rating. The support from shareholders for the relaunch of the institution in 2018, including agreeing to write-off the entire amount of legacy non-performing loans, and the approval of a further material expansion of the asset base (albeit with no additional capital) as part of IBEC's new development strategy, demonstrates a degree of commitment by the member states to the institution. That said, IBEC's shareholders are under no contractual obligation to fulfil a capital call in line with their shareholding, which weighs on Moody's overall assessment of the strength of member support.

Finally, the decision to affirm the rating at this time also takes into account that the recent improvements to IBEC's high quality liquid resources are still at a relatively early stage, while IBEC's track record of market issuance and repayment is still being established.

ENVIRONMENTAL, SOCIAL AND GOVERNANCE CONSIDERATIONS

Notwithstanding environmental issues being material for many of IBEC's borrowers and shareholders, environmental considerations do not have a material impact on IBEC's credit profile given the Bank's portfolio diversification.

Social considerations are not material to IBEC's rating.

Governance considerations are material for IBEC given the important role played by its enhancing risk-management practices in helping to manage the challenges posed by a rapid growth in the credit portfolio as well as the difficulties posed by the pandemic to its operating environment.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATING

IBEC's rating would likely be upgraded if the recent increase in the amount of high quality liquid assets which would be available in a stress scenario were to be sustained, and there was continued progress in improving the quality and structure of its funding. An upgrade would also likely be conditioned on IBEC's balance sheet evolving under the new development strategy in a way which helps to enhance the credit quality of the loan portfolio and preserves the Bank's capital adequacy, in particular with leverage remaining moderate relative to peers and ongoing diversification of the loan book which helps to further reduce concentration risks. While not a prerequisite for a Baa2 rating, the introduction of a formal callable capital framework in line with industry practice would also give rise to positive rating pressure.

The positive outlook suggests a downgrade is unlikely in the near term. The outlook could be changed to stable if the recent improvements to IBEC's liquidity and funding were not sustained or if there were indications that the expansion of its balance sheet was weighing on credit metrics, including a substantially larger than expected increase in the Bank's leverage or if asset quality pressures were to rise materially above Moody's expectations.

The principal methodology used in this rating was Multilateral Development Banks and Other Supranational

Entities Methodology published in October 2020 and available at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1232238 . Alternatively, please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found at: https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_79004.

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