S&P Global
Ratings

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Research Update:

Arab Bank for Economic Development in Africa Outlook Revised To Positive On Rising Policy Importance; 'AA/A-1+' Affirmed

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PRIMARY CREDIT ANALYST

Leon Bezuidenhout
Johannesburg
837975142
leon.bezuidenhout
@spglobal.com

SECONDARY CONTACT

Alexander Ekbom
Stockholm
+ 46 84 40 5911
alexander.ekbom
@spglobal.com

ADDITIONAL CONTACT

Sovereign and IPF EMEA
SOVIPF
@spglobal.com

S&PGR Revises BADEA Outlook To Positive; 'AA/A-1+' Affirmed

Overview

- Arab Bank For Economic Development in Africa (BADEA) has substantially increased its disbursements to sub-Saharan African sovereigns over the past 18 months and shareholders have further demonstrated their strong support via the introduction of callable capital, which points to BADEA's increasing role and policy importance in the region.
- Shareholders have also provided logistical, technical and diplomatic support to mitigate the impact of the conflict in Sudan, BADEA's previous headquarters and its relocation to Saudi Arabia, which significantly reduces the risk of future operational disruptions.
- This has been critical in maintaining continuity in operations and disbursements of loans in 2023.
- We assess the bank's financial risk profile as extremely strong based on a very high risk-adjusted capital ratio of 93.5% and very strong liquidity coverage on a six- and 12-month basis.
- We therefore revised the outlook to positive from stable and affirmed our 'AA/A-1+' long- and short-term issuer credit ratings on the bank.

Rating Action

On Sept. 20, 2023, S&P Global Ratings revised the outlook to positive from stable and affirmed its 'AA' long-term and 'A-1+' short-term issuer credit ratings on Arab Bank For Economic Development in Africa (BADEA).

Outlook

The positive outlook reflects our expectation that, over the next two years, there is a greater than one-in-three likelihood BADEA will continue expanding its lending footprint in sub-Saharan Africa (SSA) through year-on-year increases in disbursements, backed by broad-based shareholder support, which could lead to a stronger role and policy importance. In our view, this could be further supported if the expected balance sheet growth continues to shift in favor of lending over treasury investments, and BADEA further enhances its role as a catalyst for the League of Arab states' investments into Africa.

Additional paid-in capital increases to support growth could also strengthen our view of the bank's policy relevance and shareholder support. This presupposes that beneficiaries will treat BADEA as a preferred creditor and maintain robust capital and liquidity ratios.

Downside scenario

We could revise the outlook back to stable if we observe signs of a weakening role and public policy mandate, for instance, due to a sustained slowdown in lending.

We could also lower the ratings if the bank's preferred creditor treatment (PCT) weakens. This could stem from greater financial risk at less-creditworthy sovereigns, to which BADEA is exposed.

Rationale

Our ratings on BADEA reflect our assessment of its enterprise risk profile as adequate and its financial risk profile as extremely strong. The bank has increased disbursements of purpose-related loans significantly over the past 18 months to 52.5% of total assets as of June 30, 2023, from 40.4% at year-end 2021. It focuses lending on SSA sovereigns, government-related entities, and multilateral development banks, while having minimal private sector exposure of about 5% of purpose-related loans. The remaining 45% of its assets are held in liquid Organisation for Economic Co-operation and Development (OECD) securities, the majority fixed income and to a lesser extent in listed equities.

The rising disbursements to SSA sovereigns underpin the increasingly important role BADEA plays as the leading Arab institution focused on African lending and engagement. The bank's objective is to provide concessional financing and technical assistance to SSA countries to foster economic development and enhance relations between the League of Arab States and SSA. While lending growth may moderate, we expect it will continue increasing given the signals provided by shareholders in support of a stronger and larger balance sheet. This was shown by shareholders increasing BADEA's capital base to $5 billion of paid-in capital from $91 million in 1975, and adding callable capital worth $5 billion in April 2022.

Furthermore, the bank plays a leading role in coordinating broader Arab development funding into Africa, thereby increasing the overall impact of lending into the continent. There is significant co-financing among BADEA, Arab funds, and Arab states with about $4-$5 of additional financing made available from partners for each dollar that BADEA provides. In recent years, BADEA has also ramped up the provision of trade loans at concessional rates across the continent.

BADEA has a strong relationship with its shareholders, and it is viewed as a critical institution in advancing SSA developmental finance and as a vehicle to improve international relations. Shareholders have been supportive, most recently by aiding in the relocation of staff and the bank's headquarters to avoid the negative effects of the conflict in Sudan. No shareholders have withdrawn from BADEA since its inception.

We assess the bank's PCT as strong, underpinned by an improving track record of arrears management since 2016. BADEA's arrears ratio stands at 2.06%, which is slightly lower than the 2.68% in 2022. The institution is heavily exposed to low-rated SSA sovereigns. However, its nonperforming loan (NPL) ratio has improved marginally despite the rising number of sovereign defaults and increasing sovereign risk across SSA, remaining at a low 0.58% of purpose-related loans. Since inception, no credit losses or loans have been written off. Occasional technical arrears occur due to administrative challenges in SSA sovereigns but, since the implementation of stricter management policies in 2016, all such arrears are generally resolved before becoming material or above 180 days. Nevertheless, significant and rising exposure to low-rated SSA sovereigns exposes BADEA to potential deteriorations in its arrears ratio.

The bank employs financial and risk management policies that are in line with global practices. We believe BADEA could effectively withstand the loss of key personnel, and there is a long track record of stable and conservative management within the organization.

The bank has also mitigated instability in Sudan through fast implementation of business continuity plans, including relocating staff and making use of back-up offices and information technology infrastructure in Cairo, Egypt. We understand that no business operations have been affected and that all disbursements for 2023 have taken place as planned.

BADEA also enjoys privileges given to multilateral lending institutions (MLIs), such as exemptions from taxes, appropriations, moratoriums, and foreign exchange controls. It was established in 1974 by treaty and is owned by 18 members of the League of Arab States.

The bank's financial risk profile is extremely strong, driven by one of the highest risk-adjusted capital (RAC) ratios among all MLIs rated by S&P Global Ratings. The RAC ratio after adjustments was 93.5% using data from June 30, 2023, and parameters as of Aug. 30, 2023. The ratio benefits from a sizable securities portfolio of $2.45 billion, comprising $1.6 billion in fixed-income securities, $695 million in listed equities, and $110 million in cash. The ratio is also supported by geographical diversification and preferential treatment from sovereigns, and we believe it will remain high over the next 24 months. While BADEA benefits from callable capital, we do not include this in our RAC ratio because the financial risk profile is already extremely strong.

The bank's funding profile is almost entirely dependent on its shareholders' equity. BADEA has only borrowed €30 million via a syndicated loan facility and does not currently borrow from capital markets. That said, we understand the bank is looking to raise funds through a capital market issuance and has started accepting deposits from some central banks. We understand BADEA is unlikely to materially change its funding profile in favor of debt financing and that borrowing will likely be on a small scale and incremental.

Our liquidity ratio calculations as of June 30, 2023, show very strong coverage of 2.6x for the six-month and 1.69x for the 12-month periods. These are above the coverage ratios of similarly rated peers and allow BADEA to potentially accelerate disbursements, reflecting its sizable and highly liquid asset portfolio.

Ratings Score Snapshot

- Issuer credit rating: AA/Positive/A-1+
- SACP: aa
- Enterprise risk profile: Adequate

- Policy importance: Adequate
- Governance and management: Adequate
- Financial risk profile: Extremely strong
- Capital adequacy: Extremely strong
- Funding and liquidity: Strong
- Extraordinary support: 0
- Callable capital: 0
- Group support: 0
- Holistic approach: 0

Related Criteria

- Criteria | Governments | General: Multilateral Lending Institutions And Other Supranational Institutions Ratings Methodology, Jan. 31, 2022
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Abridged Supranationals Interim Edition 2023: Comparative Data For Multilateral Lending Institutions, May 23, 2023

Ratings List

Ratings Affirmed; Outlook Action

	To	From
Arab Bank for Economic Development in Africa		
Sovereign Credit Rating		
Foreign Currency	AA/Positive/A-1+	AA/Stable/A-1+

Regulatory Disclosures

Arab Bank for Economic Development in Africa

Primary Credit Analyst: Leon Bezuidenhout, Associate Director

Rating Committee Chairperson: Alexis Smith-juvelis

Date initial rating assigned: Oct. 4, 2022

Date of previous review: Oct. 4, 2022

Disclaimers

This rating has been determined by a rating committee based solely on the committee's independent evaluation of the credit risks and merits of the issuer or issue being rated in accordance with S&P Global Ratings published criteria and no part of this rating was influenced by any other business activities of S&P Global Ratings.

This credit rating is solicited. The rated entity did participate in the credit rating process. S&P Global Ratings did have access to the accounts, financial records and other relevant internal, non-public documents of the rated entity or a related third party. S&P Global Ratings has used information from sources believed to be reliable but does not guarantee the accuracy, adequacy, or completeness of any information used.

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Glossary

- Asset-liability mismatch: Occurs when financial terms of an institution's assets and liabilities do not correspond.
- Asset quality: A key measure of the quality and performance of the assets of an MLI.
- Arrears: Exposures (typically a loan or a claim for insurance or sovereign guarantees provided to an MLI) in which either interest or principal is overdue beyond 180 days. Cross-default is assumed, meaning that the full amount of outstanding exposure is considered overdue and not only the payable share.
- Callable capital: The portion of an MLI's capital subscriptions that is not "paid-in" but that each

shareholder has committed to provide in certain circumstances (generally, only to prevent a default on an MLI's debt).

- Capital and earnings: A measure of an MLI's ability to absorb losses.
- Cost of funds: Interest expense as a percentage of average interest-bearing liabilities.
- Credit losses: Losses arising from credit risk.
- Credit risk: Risk that a borrower will default on its payment obligations.
- Date initial rating assigned: The date S&P Global Ratings assigned the long-term foreign currency issuer credit rating on the entity.
- Date of previous review: The date S&P Global Ratings last reviewed the credit rating on the entity.
- Enterprise risk profile: The strength of an MLI's business operations in relation to the rest of the MLI sector globally. This assessment is informed by S&P Global Ratings' view of an MLI's policy importance and governance and management expertise.
- Extraordinary support: The likelihood that an MLI would receive extraordinary shareholder support to service its debt obligations if needed, typically in the form of an injection of callable capital, and less often in the form of guarantees or other types of support.
- Financial risk profile: This includes S&P Global Ratings' assessment of the MLI's capital adequacy and its funding and liquidity.
- Funding and liquidity: A combined assessment of the strength and stability of an MLI's funding mix and its ability to manage its liquidity needs in adverse market and economic conditions over an extended period.
- Governance and management expertise: A qualitative assessment of an MLI's bylaws, internal governance rules, strategy, and risk management policies. An MLI's governance and strategy is assessed in the context of its public mission, which is typically to foster economic development and integration.
- Group support: An assessment of whether an MLI is a subsidiary of a group.
- High risk exposure cap (HREC): Adjustment to S&P Global Ratings' RAC framework by capping the risk weight so that the capital allocated to such exposures (for example, private equity) does not exceed the exposed amount.
- Holistic analysis: Recognizes S&P Global Ratings' forward-looking view of sustained, predictable operating and financial underperformance or outperformance and helps capture a more comprehensive analysis of creditworthiness.
- Issuer credit rating: A forward-looking opinion about an obligor's overall creditworthiness.
- MLI adjustments: Include several amendments to the risk capital framework used for financial