MOODY'S
INVESTORS SERVICE

Rating Action: Moody's changes outlook on West African Development Bank (BOAD)'s rating to negative from stable, affirms Baa1 ratings

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Paris, October 16, 2020 -- Moody's Investors Service, ("Moody's") has today changed the outlook on the West African Development Bank (BOAD)'s rating to negative from stable and has affirmed BOAD's long-term foreign currency issuer and senior unsecured Baa1 ratings.

The negative outlook reflects downside pressure on BOAD's asset quality and performance stemming from the coronavirus pandemic and heightened political instability in Mali (Caa1 negative), which accounts for 11% of BOAD's total loan exposures. Moreover, since BOAD's borrowers are also its main shareholders, any widespread stress on borrowers as a result of the pandemic that affects their capacity to reimburse loans would concurrently hamper their capacity to inject new capital. Ultimately, a deterioration in BOAD's asset quality and performance that is not compensated for by additional capital would likely lead to a lower rating level in future.

The rating affirmation reflects Moody's assessment that BOAD's degree of preferred creditor status, strong willingness of regional shareholders to support the bank, robust risk management and liquidity access in both local and foreign currency support its Baa1 rating.

BOAD is the development finance institution of the West African Economic and Monetary Union (WAEMU) promoting the development of its eight member states: Benin (B2 positive), Burkina Faso, Côte d'Ivoire (Ba3 stable), Guinea-Bissau, Mali (Caa1 negative), Niger (B3 stable), Senegal (Ba3 negative) and Togo (B3 stable). BOAD's shareholders comprise WAEMU member countries (47%), the central bank of the WAEMU (BCEAO) (47%) and eight non-regional members (6%).

RATINGS RATIONALE

RATIONALE FOR THE NEGATIVE OUTLOOK

PRESSURE ON ASSET QUALITY AND PERFORMANCE DUE TO THE IMPACT OF THE PANDEMIC

BOAD's capital adequacy risks deteriorating in the next 18 months in the absence of new capital injections as the quality of its loan portfolio deteriorates and provisioning weighs on profitability. Non-sovereign exposures are most at risk and represent about 30% of BOAD's loan portfolio, with the sectors most exposed to the pandemic - hospitality and transport - accounting for 8% of total loans. The credit quality of BOAD's sovereign loan portfolio also faces negative pressures as highlighted by Moody's recent downgrade of Mali's ratings to Caa1 from B3 and the change in the outlook on Senegal's Ba3 ratings to negative from stable. BOAD's leverage ratio as measured by total assets/usable equity stood at 324% as of June 2020 and 373% at end of 2019, higher than its Baa-rated peers' median of 283%, and up from 258% at end of 2015.

BOAD's asset performance is expected to deteriorate, as reflected in the strong increase in loans on its "watch list", a category that rose by 12% over the first half of 2020 and now represents 16% of total loans. Some of the loans classified in this bucket have already been restructured, mainly in the hospitality and transport sectors, indicating significant financial stress. So far, non-performing loans have remained stable in terms of vintage and size relative to BOAD's outstanding loans, at 2.5% as of end of June 2020, but Moody's expects the ratio to increase in the coming 18 months.

Provisioning will weigh on profitability at a time when BOAD is under pressure to provide concessional loans to member states. BOAD will likely continue to provision for impaired loans, which will affect profitability and capital levels through retained earnings. Provision coverage for non-performing loans rose to 77% of the exposures (93% after guarantees) in the first half of 2020 from 64% at the end of 2019 (79% after guarantees). Meanwhile, in order to help its member states to cope with the effects of the coronavirus pandemic, BOAD approved emergency measures in March 2020, including concessional loans to member states worth FCFA 200 billion, equivalent to 10% of the bank's loan book.

CAPACITY OF REGIONAL SHAREHOLDERS TO SUPPORT RISKS WEAKENING TOO

While BOAD may receive additional capital support from shareholders in response to weakening asset quality, shareholders have not yet formally approved a capital increase which would be sufficiently large and timely enough to offset the deterioration in its asset-related credit metrics.

BOAD's shareholding structure, skewed towards regional shareholders BCEAO and WAEMU member states, means that there is a high correlation between the capacity of borrowers to repay their loans and their capacity as shareholders to provide additional capital. The negative impact of the pandemic crisis in the WAEMU risks simultaneously weakening the ability of shareholders to support BOAD through new capital injections.

The central bank, BCEAO, as the largest single shareholder plays an important role, to some extent mitigating this risk. Currently, its capacity to support BOAD, both in foreign and local currency is relatively strong due to its own equity, covering more than six times its callable capital commitment to BOAD. Additional strong features include the BCEAO's high level of net foreign exchange reserves, equivalent to 5-6 months of the union's imports, and the long-standing guarantee of currency convertibility provided by France (Aa2 stable). However, the coronavirus crisis is affecting the external and fiscal positions as well as economic prospects of WAEMU member states.

RATIONALE FOR AFFIRMING THE Baa1 RATING

Moody's expectation that sovereign borrowers -- which account for 71% of the loan portfolio -- will continue to treat BOAD as a preferred creditor will mitigate the negative impact of the pandemic shock on asset quality. BOAD's non-performing loans have all been concentrated on non-sovereign exposures and there has been no debt restructuring offered to sovereigns. Only the capital contributions due by Guinea-Bissau were re-scheduled once.

Moreover, BOAD has access to a refinancing window at the BCEAO, which means BOAD can afford somewhat lower liquidity requirements and ratios in the first place. While the institutions have never tested the window, BOAD has a large pool of assets on its balance sheet that are eligible to be posted as collateral, which could effectively double the liquid assets Moody's takes into account in its liquidity assessment.

Moreover, Moody's believes that the willingness of shareholders to support BOAD remains solid, even in the face of potentially waning capacity to provide it. BOAD holds a key economic role in the region because of its mandate to finance the integration and economic development of WAEMU member states including important infrastructure, water and energy related projects. This role reinforces the strong incentive for shareholders to provide support in the event of need. WAEMU countries, together with the BCEAO, have a track record of providing financial support to BOAD through capital contributions, in addition to the presence of callable capital.

ENVIRONMENTAL, SOCIAL AND GOVERNANCE CONSIDERATIONS

Many of BOAD's borrowers in Sub-Saharan Africa are exposed to environmental risks, mostly because of their reliance on agriculture, which is exposed to extreme weather conditions and natural disasters. This exposure is assessed within the individual credit profiles of each sovereign issuer and is thus also taken into account in BOAD's credit profile.

Social risks also inform BOAD's credit profile via the credit assessments of both borrower and shareholder sovereigns. Some are affected by unrest, low wealth levels, income disparity and low voice and accountability scores, captured by our institutional and governance factor and political risk assessments. Moreover, Moody's regards the coronavirus outbreak as a social risk under its ESG framework, given the substantial implications for public health and safety.

In terms of governance, BOAD's relatively solid management, including its prudent risk management framework, is taken into account in the assessment of its credit profile. BOAD's governance is fostered by its strategic shareholder, the BCEAO, and by its non-regional shareholders.

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

The negative outlook suggests an upgrade is unlikely in the near term. The outlook could be changed to stable if BOAD manages to broadly maintain its capital adequacy metrics close to current levels, which could either be the result of a stabilization of asset quality and performance close to current levels or a compensation of deteriorating metrics through sufficient capital infusion. Under such a scenario, BOAD's liquidity position would probably also stabilise, if not improve.

BOAD's rating would likely be downgraded if asset performance were to deteriorate significantly and shareholders proved unable to provide capital support sufficiently large and timely enough to compensate for that deterioration. Signs that BOAD's liquidity will further tighten would also exert downward pressure on the rating, as would any other sign that the strength of regional shareholders' support has weakened. These developments could for instance result from a widespread deterioration in the WAEMU's fiscal, external or economic prospects beyond what Moody's currently expects.

The principal methodology used in these ratings was Multilateral Development Banks and Other Supranational Entities published in June 2019 and available at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1147813 . 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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Moody's general principles for assessing environmental, social and governance (ESG) risks in our credit analysis can be found at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1133569 .

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