

RATING ACTION COMMENTARY

Fitch Revises BOAD's Outlook to Negative; Affirms at 'BBB'

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Fitch Ratings - Paris - 25 Apr 2024: Fitch Ratings has revised the Outlook on Banque Ouest Africaine de Developpement (BOAD)'s Long-Term Issuer Default Rating (IDR) to Negative from Stable and affirmed the IDR at 'BBB'.

KEY RATING DRIVERS

Increased Credit Risk: The revision of the Outlook primarily reflects increased credit risk faced by the bank, as evidenced by a weakening in the credit quality of its loan portfolio and the temporary suspension of loan repayments to the bank by Guinea Bissau, accounting for 5% of total loans. While the ongoing capital increase should support the bank's solvency, in Fitch's view, there is an elevated risk that non-performing loans (NPL) increase to a level not compatible with the current rating.

SCP Drives Rating: BOAD's 'BBB' rating is driven by its Standalone Credit Profile (SCP) of 'bbb', which reflects the lower of its solvency (a-) and liquidity (a) assessment and a two-notch negative adjustment to reflect the 'high' risk business environment in which the bank operates.

Increased Credit Risk: Fitch has revised its assessment of credit risk to 'high' from 'moderate' previously, principally reflecting the decline in the average rating of loans to 'B-' from 'B'. In the context of its sovereign debt re-structuring, Guinea Bissau has reached an agreement with BOAD to suspend all remaining payments to the bank in 2024 following a payment in January.

In Fitch's view, this is the first breach of BOAD's preferred creditor status, currently

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NPLs Could Rise: Under Fitch's criteria definition, exposures subject to suspension of payments by more than six months are considered non-performing. Fitch expects the two sovereigns to resume payments relatively shortly (in 2024 for Niger and in 2025 for Guinea Bissau). However, the suspensions of payments highlight the deterioration in the bank's operating environment and the risk that NPLs might increase significantly from 2.6% as of end-2023.

Strengthening Capital Ratios: Fitch's own capital metrics, the equity-to-asset and Fitch's usable-to-risk weighted assets (FRA) ratios, markedly strengthened in 2023, at 35.1% and 34.1%, respectively, from 32.6% and 31.3% in 2022. This primarily reflected the start of the paid-in capital payment under the new capital increase, the issuance of a USD100 million (XOF60 billion) hybrid instrument purchased by Arab Bank for Economic Development in Africa and assigned 100% equity credit under Fitch's criteria, and for the FRA ratio, the increase in callable capital subscribed from 'AAA'-'AA' rated shareholders (France, Germany, Belgium, the European Investment Bank, and the African Development Bank).

Fitch expects the two capital ratios to be broadly stable in the medium term, reflecting paid-in capital payments spread over five years from 2023 and continued expansion of the bank operations.

'Moderate' Risk Overall: The bank's top five largest exposures (all sovereigns) accounted for 47% of total loans as of end-2023. The bank hedges its USD/EUR exchange rate risk (arising from its US dollar Eurobond issuances) with cross-currency swaps. The bank's main capital adequacy metrics are a Basel-type ratio (27% as of end 2023) and a leverage limit that caps debt at three times the level of equity (176% as of end 2023).

Access to Central Bank Refinancing: Fitch assesses the bank's liquidity at 'a'. The assessment reflects the 'strong' coverage of short-term debt by liquid assets and the bank's proven access to capital markets. Fitch only considers as liquid the deposits held at the regional central bank and regional sovereign debt securities that the bank can refinance with the central bank (after applying a 10% haircut). The liquidity assessment is enhanced by BOAD's access to the regional central bank's refinancing window.

High Risk Business Environment: The business environment is 'high risk' leading to a

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approved by shareholders. Non-borrowing highly-rated shareholders are expected to play a growing role in the bank's governance.

Dilution of BCEAO Affects Support: Fitch assesses BOAD's shareholders' capacity to support based on the average rating of key shareholders, i.e. those largest shareholders whose capital contribution totals at least 50% of subscribed capital. Following the subscription to the new capital increase, the Banque Centrale des Etats de l'Afrique de l'Ouest's (BCEAO) share in the capital has markedly reduced, to 36% from 47%, leading to a weakening in our assessment of shareholders' capacity to support to 'bb' (from 'bbb-' previously). Non-regional shareholders have significantly increased their share ownership, to 13% as of end-2023 from 6% last year.

Exceptional Propensity to Support: BCEAO's ability to tap the fiscal resources that it manages on behalf of the regional member states to secure payment of capital increases translates into an 'exceptional' propensity of shareholders to support, and a one-notch uplift over the capacity to support, leading to an overall support assessment of 'bb+'.

Short-Term Rating: The Short-Term rating of 'F2' is the higher option at the 'BBB' cusp point on Fitch's long-term rating correspondence table. The choice of the higher option results from the bank's liquidity assessment of 'a', which is higher than the level equivalent to the minimum Long-Term rating (BBB+), at which the higher Short-Term rating (F2) would always apply.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to negative rating action/downgrade:

SCP (Credit Risk): Deterioration in BOAD's credit risk profile, potentially stemming from NPLs growing into the criteria-defined 'high risk' category on a sustained basis and/or a revision in our assessment of the bank's strong preferred creditor status in case of weaker sovereign loan performance.

SCP (Business Environment): A downward revision of our assessment of the bank's business environment, based on increased risk associated with the bank's strategy in a deteriorating operating environment.

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SCP (Credit Risk): Improvement in the credit quality of the loan portfolio to the 'BB' category and a record of operations with NPLs towards the 1% threshold for 'very low' risk.

SCP (Capitalisation): A record of operations with a higher level of capitalisation, including a FRA ratio above 35%, consistent with an 'excellent' assessment under Fitch's criteria.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

BOAD has an ESG Relevance Score of '4[+]' for 'Human Rights, Community Relations, Access and Affordability'. BOAD provides concessional loans to its member states funded by concessional resources provided by its shareholders. This supports BOAD's policy importance and shareholders' propensity to support the bank. This has a positive impact on the credit profile, and is relevant to the ratings in conjunction with other factors.

BOAD has an ESG Relevance Score of '4' for 'Governance Structure'. A high share of capital ownership by borrowing countries with weak credit fundamentals and limited access to external funding has led to pressure to increase lending. This risk has been somewhat mitigated by a relatively high share of voting rights held by non-regional members at the board. This has a negative impact on the credit profile, and is relevant to the ratings in conjunction with other factors.

BOAD has an ESG Relevance Score of '4' for 'Rule of Law, Institutional and Regulatory Quality'. All supranationals attract a score of '4'. Supranationals are neither subject to bank regulation nor supervised by an external authority. Instead, supranationals comply with their own set of rules. Fitch pays particular attention to internal prudential policies, including compliance with these policies. This has a negative impact on the credit profile, and is relevant to the ratings in conjunction with other factors.

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The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit <https://www.fitchratings.com/topics/esg/products#esg-relevance-scores>.

RATING ACTIONS

ENTITY / DEBT ↕	RATING ↕			PRIOR ↕
Banque Ouest Africaine de Developpement	LT IDR	BBB Rating Outlook Negative		BBB Rating Outlook Stable
	Affirmed			
	ST IDR	F2	Affirmed	F2
senior unsecured	LT	BBB	Affirmed	BBB

[VIEW ADDITIONAL RATING DETAILS](#)

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APPLICABLE CRITERIA

[Suprationals Rating Criteria \(pub. 11 Apr 2023\) \(including rating assumption sensitivity\)](#)

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Banque Ouest Africaine de Developpement

EU Issued, UK Endorsed

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