

Banque Ouest Africaine de Developpement (/gws/en/esp/issr/96173827)



Fitch Affirms Banque Ouest Africaine de Developpement at 'BBB'; Outlook Stable

Fitch Ratings-London-17 May 2018: Fitch Ratings has affirmed Banque Ouest Africaine de Developpement's (BOAD) Long-Term Issuer Default Ratings (IDR) at 'BBB' with a Stable Outlook and Short-Term IDR at 'F2'. Fitch has also affirmed BOAD's senior unsecured notes at 'BBB'.

KEY RATING DRIVERS

BOAD is a sub-regional multilateral development bank (MDB) based in Lome, Togo, providing financing for the West African Economic and Monetary Union's (Union Economique et Monetaire Ouest-Africaine; UEMOA) regional members states (RMS), Benin, Burkina Faso, Cote d'Ivoire (B+/Stable), Guinea Bissau, Mali, Niger, Senegal and Togo. The majority of financing comprises project loans to or guaranteed by these sovereigns. BOAD also extends loans to public corporations - often in the energy and transportation sectors - and to private entities, and holds a portfolio of equity participations. A significant share of sovereign loans is concessional.

BOAD's ratings are based on the support Fitch believes it would receive from its two key shareholders, Banque Centrale des Etats d'Afrique de l'Ouest (BCEAO), which is the regional central bank of UEMOA, and Cote d'Ivoire. With 47% of BOAD's capital, BCEAO is BOAD's main shareholder, and Cote d'Ivoire, the largest economy of the UEMOA, owns 6% of the bank's capital. Our assessment of the potential for extraordinary support from these shareholders reflects both BOAD's status and importance as a strategic development lender for the UEMOA and the strong relationship between it and the BCEAO.

Fitch assesses BOAD's key shareholders' support capacity at 'BBB-', reflecting the weighted average credit quality of its key shareholders. Our assessment of BCEAO's credit quality is based on its monetary agreement with France (AA/Stable) and the RMS, which provides the bank with access to emergency refinancing in euros. Our assessment also factors in the rating of Cote d'Ivoire, which is the only RMS rated by

Fitch. We perceive the credit quality of BOAD's other RMS as very low sub-investment grade.

In addition, we consider BCEAO's propensity to provide extraordinary support to BOAD as 'exceptional', which translates into a one-notch uplift over its shareholders' support capacity, resulting in a support rating of 'BBB'. The central bank plays a central role in BOAD's operations, as it ensures the timely payment of capital and loans due to the bank. In addition, BCEAO holds a significant portion of the bank's liquid assets and opens its emergency refinancing window to BOAD, a rare feature within the supranationals universe.

Fitch has revised BOAD's solvency assessment to 'bbb+', from 'bbb' in 2017, reflecting the bank's improving credit risk. The high-risk business environment in which the bank operates translates into a three-notch negative adjustment below BOAD's solvency assessment, resulting into an intrinsic rating of 'bb+'.

We assess BOAD's operating environment as 'high-risk'. The bank chiefly lends to its eight UEMOA sovereigns, whose average credit quality and political risk indicators are deemed very low. Fitch considers BOAD's business profile as 'high-risk', in line with the bank's expected rapid lending growth relative to the growth of its capital base, as we expect BOAD's banking exposures to grow by 7.5% per year on average in 2018-2021. However, the bank's sovereign lending focus, through which it benefits from preferred-creditor status (PCS) mitigates the risk associated with the bank's rapid-lending growth strategy.

Our assessment of BOAD's solvency combines its 'excellent' capitalisation levels with its 'high-risk' profile. The bank's equity to assets ratio deteriorated to 25.3% in 2017 (2016: 28.8%), largely due to its USD850 million 10-year Eurobond issuance, which increased the bank's leverage ratio to 277% in 2017 (2016: 234%), as well as the size of its treasury assets cushion.

We expect that the bank will successfully achieve its capital increases initiated in 2010 and in 2013, extending the track record of timely disbursements by RMS in 2017. The bank's paid-in capital base increased by 5.1% in 2017. This amount includes the payment of Guinea Bissau, which was BOAD's only shareholder with arrears on its capital disbursements, and which is now current on all of its payment obligations to BOAD as of end-April 2018. We project the bank will limit its recourse to additional debt to finance its lending growth in the coming years, and will gradually convert its large treasury asset buffer into loans, hence preserving its equity/assets ratio slightly above 25% by 2021, at the end of the forecast period.

Fitch assesses BOAD's risk profile at 'high'. We estimate BOAD's average credit quality of loans at very low sub-investment grade levels before adjustment, at 'B-', reflecting the large share of loans disbursed to its RMS sovereigns (65% of gross loans as of end-2017), as well as its lending exposures to non-sovereign entities, which are considered low-credit quality borrowers. As BCEAO maintains a firm level of control on RMS' loans repayment to BOAD, we assess the bank's PCS as 'strong', which translates into a positive adjustment of 2 notches above BOAD's estimated average credit quality of loans, at 'B+'.

In our view, BOAD's credit risk has been on an improving trend in recent years, as evidenced by the bank's low NPL ratio at 2.3% of total gross loans in 2017 (average 2013-2016: 3.1%). This improvement in asset quality chiefly reflects the gradual improvement in the bank's underwriting standards, especially related to non-sovereign borrowers, which account for all of the bank's loans impairments. In addition, the bank is consolidating the robustness of its internal risk assessment methodologies, as evidenced by its participation in an international credit risk database alongside highly-rated supnationals, such as the European Investment Bank (AAA/Stable), the African Development Bank (AAA/Stable) and the International Bank for Reconstruction and Development (AAA/Stable). We expect BOAD's NPLs to remain below 3% of the bank's gross loans in the medium term, which corresponds to a 'low' NPL risk assessment as set out in Fitch's supnationals criteria.

BOAD's concentration risk is 'moderate' in our view, with its five largest exposures expected to account for 45% of total banking exposures by 2021 (stable from 2017's level). BOAD's loan diversification is constrained by its focus on a limited number of sovereign RMS. This translates into large single exposures, in particular to Togo, Niger and Senegal.

In our view, BOAD has 'moderate' exposure to market risk. Fitch assesses BOAD's vulnerability to market risks as medium risk. BOAD's loans are entirely denominated in CFA francs, but an increasing share of its debt is US dollar-denominated. BOAD mitigates foreign exchange (FX) risk using several hedging instruments, which almost fully offsets the impact of FX variations on future revenue generation.

BOAD abides by moderately conservative risk management policies, including its maximum borrowing limits, which caps the bank's outstanding debt at three times its equity. This prudential rule is only slightly more conservative than peers, but it is expected to effectively limit BOAD's debt-funded lending growth in the coming years, with debt/equity expected to remain below 2.7x in 2021. In addition, although we

expect the bank to increase its coverage of impaired loans by loan loss reserves, to 75% of NPLs in 2021, we consider that this would still represent a modest level relative to the bank's high-risk operating environment. Our assessment also reflects our view of the BOAD's management team's high level of competence and credibility.

BOAD's liquidity profile, assessed at 'a', is a rating strength. In our view, the bank will maintain a 'strong' liquidity buffer, amounting to 1.4x of its short-term liabilities, by 2021 (stable from current levels). In Fitch's view, less than 60% of BOAD's treasury cushion in 2017 was considered as liquid, a proportion corresponding to the bank's deposits at the BCEAO, in addition to a discounted share of its UEMOA's sovereign debt securities holdings, which are eligible as collateral as part of the bank's access to the central bank's refinancing window. We expect a temporary deterioration in BOAD's liquidity buffer in 2020, due to the maturation of international market issuances, but believe the bank will maintain liquidity metrics in line with its ratings throughout the forecast period.

The average quality of BOAD's treasury assets was relatively weak in 2017, as evidenced by the absence of instruments rated 'AA-' and above. The bank invested a substantial share of the proceeds of its 2017 international debt issuances in short-term loans to regional commercial financial institutions, whose credit quality is perceived as weak. In our view, these interbank loans represent a one-off liquidity management strategy, and we expect BOAD to gradually increase its holding of deemed-liquid assets, which we believe will account for at least 75% of its treasury cushion by 2021.

Our assessment of BOAD's liquidity profile incorporates the bank's 'strong' access to external liquidity sources, as evidenced by its statutory access to BCEAO's refinancing window, which considerably enhances the bank's liquidity profile although it has never been used. Our assessment also factors in the bank's relatively favourable borrowing conditions in 2017.

RATING SENSITIVITIES

The Outlook is Stable. Consequently, Fitch's sensitivity analysis does not currently anticipate developments with a material likelihood, individually or collectively, of leading to a rating change. However, future developments that may, individually or collectively, lead to positive rating action include:

- An improvement in BOAD's 'bbb' support rating, driven by upgrades of its key shareholders, BCEAO and/or Cote d'Ivoire.
- A three-notch improvement in BOAD's intrinsic rating.

- A combined improvement in BOAD's support and intrinsic ratings.

Conversely, future developments that may, individually or collectively, lead to negative rating action include:

- A weakening of BCEAO's credit quality or a very significant downgrade of Cote d'Ivoire's rating.
- A weakening in the monetary agreements between France and UEMOA.
- A deterioration in the coverage of its short-term debt by deemed-liquid assets, which could primarily stem from a failure to restore the proportion of treasury assets that we consider as liquid, and/or from a marked reduction in the size of its treasury assets as a share of the bank's balance sheet.
- A marked deterioration in BOAD's solvency assessment, potentially stemming from higher than expected lending growth, which would affect the bank's excellent capitalisation, or from a softening of its self-imposed prudential rules.

KEY ASSUMPTIONS

The ratings and Outlooks are sensitive to a number of assumptions. In particular, Fitch assumes that the average sovereign rating of the seven non-rated countries of the UEMOA is very low speculative grade. It also assumes that the French treasury will honour its commitment to provide liquidity to BCEAO and preserve the convertibility of the CFA franc into euro in the event of a depletion of its international assets.

The full list of rating actions is as follows:

Long-Term IDR affirmed at 'BBB'; Outlook Stable

Short-Term IDR affirmed at 'F2'

Issue ratings on long-term senior-unsecured foreign-currency bonds affirmed at 'BBB'

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In addition to the Supranationals Rating Master Criteria, this action was additionally informed by information from Banque Ovest Africaine de Developpement.

Applicable Criteria

Supranationals Rating Criteria (pub. 23 Mar 2018)
(<https://www.fitchratings.com/site/re/10024431>)

Additional Disclosures

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