

CREDIT GUARANTEE AND INVESTMENT FACILITY

No. 225/2023
21 November 2023

SUPRANATIONALS

Issuer Rating: AAA
Outlook: Stable

Last Review Date: 28/11/22

Company Rating History:

Date	Rating	Outlook/Alert
28/08/14	AAA	Stable

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RATIONALE

TRIS Rating affirms the issuer rating on Credit Guarantee and Investment Facility (CGIF), a trust fund of Asian Development Bank (ADB), at “AAA”, with a “stable” rating outlook. The rating reflects CGIF’s status as a supranational institution owned by the governments of the ASEAN+3 countries and ADB, together referred to as “contributors”. The rating also reflects CGIF’s very strong public policy mandate, strong governance and management expertise, solid capital position strengthened by conservative risk management as well as strong funding and liquidity profile. These should adequately meet the challenges from exposure to issuers and countries of high credit risks.

KEY RATING CONSIDERATIONS

Supranational status underpins the rating

CGIF’s Supranational status supports the assigned rating. CGIF was established by the governments of the ASEAN+3 countries and ADB with a policy mandate to promote financial stability and develop local capital markets in the ASEAN+3 region.

CGIF’s priorities are to support bond issuers in ASEAN and the frontier markets, especially first-time issuers, cross-border transactions, and new instruments. The latter includes thematic bonds, project bonds, real estate investment trust (REIT), green bonds, social bonds, and sukuk. As such, we do not foresee other private financial guarantors or supranational institutions to easily fulfil this role.

In 2017, CGIF’s contributors approved a capital increase proposal to raise paid-up capital on an uncommitted basis to USD1.2 billion by 2023 from USD700 million to support business expansion. To date, continuous payment for subscription of new shares under the capital increase program from contributors indicates the strong and stable relationship CGIF has with the shareholders and their commitment to CGIF’s development objectives. The discrete shareholding structure and zero-dividend practice also imply strong governance principles. The paid-up capital was USD1.1 billion as of 30 June 2023.

CGIF’s management team comprises a diverse team of internationally qualified personnel. The management team has been able to meet performance benchmarks and operate within risk-return targets. These include meeting financial targets and maintaining portfolio quality based on its internal risk rating (IRR).

Very strong capital buffer

We assess CGIF’s capital adequacy as very strong. CGIF has solid capital buffer to absorb potential losses from guarantee calls despite an absence of callable capital. CGIF maintains its conservative leverage ratio measured by total guarantee exposure to total capital at 1.35 times as of June 2023, slightly above 1.28 times as of June 2022. With CGIF’s conservative growth strategy, we expect the leverage ratio to remain within the internal limit of 2.5 times in the next few years. CGIF’s reported capital adequacy ratio or CGIF’s capital adequacy metric, was at 33.7% as of June 2023, down slightly from 35.7% as of June 2022. These were well above the internal floor of 8.8%.

Prudent risk management and conservative expansion

CGIF has a conservative growth strategy with thorough risk management standard, in our view.

CGIF has prudent risk management framework and operational policies to manage its exposures to credit risk, market risk, liquidity risk, and operational risk. The risk management framework contains comprehensive guidelines throughout the guarantee process from credit risk assessment, credit underwriting, credit risk management, claims on guarantee calls, and loss recoveries. CGIF has internal concentration limits for credit and investment risks. It also conducts quarterly liquidity stress test for scenarios in which CGIF has to meet lumpy obligations for guarantee calls.

CGIF is still in the process of asset recovery from its first guarantee call of KNM Group Berhad (KNM) occurred in December 2021. The payment under the guarantee should have limited impact on CGIF as the total gross exposure of around USD85 million is relatively small compared to its capital base. CGIF set aside additional expected credit loss (ECL) of USD25.0 million in 2022 due to the change in recovery assumption in addition to the USD9.5 million set in 2021.

Strong funding and liquidity profile

CGIF's guarantee activities and operations are funded by capital contribution from shareholders and its retained earnings. As of June 2023, CGIF does not have any borrowings. CGIF's policy is to only borrow necessary short-term funding from eligible counterparties. The short-term borrowing is mainly for cash management purposes such as liquidity for guarantee calls or other operational requirements.

Based on our assessment, CGIF has sufficient liquid assets to cover potential liquidity needs for guarantee calls in a stressed scenario. We also consider CGIF's liquidity risk management to be conservative. The two-tier approach requires regular monitoring of liquidity sufficiency for day-to-day requirements and a stress test in the event of major claims. The regular liquidity gap monitoring requires expected cash inflows from investments and guarantee fees to cover cash outflows from operating expenses and potential claim payments over the next six months. The stress test scenario assumes simultaneous defaults of the top 20% of guaranteed entities with the largest exposures and applies haircuts to investment portfolios.

High-quality investment portfolio

CGIF only invests in high-grade marketable fixed-income securities, which can be liquidated with minimal loss. According to its treasury risk management guidelines, the required credit ratings range from "A+" to "AA-" (based on ratings of S&P Global Ratings), with a minimum rating requirement of "A+" allowed for debts issued by the government-related entities (GREs) of contributing countries.

CGIF aims for stable investment income with its strategy to buy and hold to maturity with a target effective duration of around three years. There are also explicit concentration limits on countries, single issuers, issuer types, and credit ratings, and conservative limits on the value-at-risk (VAR) and unrealized market loss.

As of June 2023, over half of its investments is in fixed-income securities issued by the sovereigns or government-related entities with credit ratings of "AA-" or above. CGIF's average portfolio duration was 3.04 years as of June 2023, longer than 2.73 years as of June 2022. These remain within the internal ceiling of 5.0 years.

BASE-CASE ASSUMPTIONS

- Leverage ratio to be 1.4 to 1.6 times.
- New guarantees to be around USD500-USD600 million per annum.
- Investment yields to be around 2.5%-3.0% per annum.

RATING OUTLOOK

The "stable" outlook reflects TRIS Rating's view on CGIF's strong and stable relationship with major contributors for the continued support of CGIF's operations. The outlook also indicates our expectation that CGIF will continue to perform its important public policy mandate in developing regional bond markets and maintain prudent governance and risk management standards. The outlook also takes into account our expectation that CGIF will maintain a strong capital position, sound funding and liquidity management, and healthy financial performance.

RATING SENSITIVITIES

The rating could face downward pressure if losses in the guarantee portfolio cause CGIF's risk position to deteriorate significantly, or if there is evidence of weakening capital support from the contributors as well as in the governance and risk management framework.

ORGANIZATION OVERVIEW

CGIF was founded in November 2010 by the governments of the ASEAN+3 countries (10 ASEAN countries plus China, Japan, and Korea) and ADB, together referred to as “contributors”. CGIF’s main objective is to provide credit guarantees which allow eligible issuers to access local currency bond markets. Issuers can thus avoid currency and maturity mismatches by issuing bonds within the region. The establishment of CGIF was a continual development process following the Asian Bond Markets Initiative (ABMI) introduced in 2003 by the ASEAN+3 countries. The aims of ABMI are to develop and strengthen the local currencies and regional bond markets to promote economic growth and financial development, and to prevent disruptions to the international financial order so as to enable savings in the region to be used within the region.

CGIF has four business functions:

1. Guaranteeing bonds in local currencies, issued by entities with local-scale and investment-grade ratings, to help issuers reduce currency and maturity mismatches;
2. Guaranteeing bonds not in local currencies, issued by entities with local-scale and investment-grade ratings, given that issuers have natural or financial hedges in place, such as a currency matching their underlying business;
3. Making investments for the development of the regional bond markets; and
4. Undertaking other activities and services consistent with the objectives.

Since its inception, CGIF has focused mainly on the first two functions. The latter two functions are for the future.

In a typical guarantee contract, CGIF’s insurance services will provide coverage only when an issuer breaches the non-payment event clause. In addition, when a non-payment event occurs, CGIF retains the sole right to decide whether it will early redeem the bonds or continue to pay bondholders according to the original bond schedule. Upon payment by CGIF of all or any part of the guaranteed amounts, CGIF will be entitled to all the rights, powers, and security that bondholders had against the issuers and co-indemnity providers to an amount equal to the paid guaranteed amount.

CGIF finances its operations solely from capital contributions. CGIF is not allowed to borrow from any source, except for cash management purposes.

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS

Unit: Mil. USD

	Jan-Jun* 2023	-----Year Ended 31 December -----			
		2022	2021	2020	2019
Interest income	17.9	28.5	27.3	28.9	26.2
Guarantee income	10.1	20.0	19.4	17.4	12.9
Other revenue**	1.2	2.6	4.4	3.4	2.8
Total revenue	29.2	51.1	51.1	49.6	41.9
Net income from operations	23.1	15.2	32.0	23.7	22.6
Total assets	1321.2	1,305.0	1,372.8	1,351.7	1,255.1
Total liabilities	76.1	81.8	80.4	87.1	76.6
Shareholders' equity	1,245.1	1,223.2	1,292.4	1,264.5	1,178.4

* Unaudited and not annualized

** Including realized gain (loss) from securities, fair value changes from derivatives, commission from reinsurance, and miscellaneous income

RELATED CRITERIA

- Supranational Institutions Rating Methodology, 15 November 2022

Credit Guarantee Investment Facility (CGIF)

Issuer Rating:	AAA
Rating Outlook:	Stable

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