CREDIT GUARANTEE AND INVESTMENT FACILITY

No. 214/2024
20 November 2024

SUPRANATIONALS

Issuer Rating: AAA
Outlook: Stable

Last Review Date: 21/11/23

Issuer 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 Association of Southeast Asian Nations+3 countries and ADB, together referred to as "contributors". The rating also reflects CGIF's very strong public policy mandate, strong governance and experienced management team, solid capital position strengthened by prudent risk management, as well as strong funding and liquidity profile. These factors should enable CGIF to effectively manage risks associated with high-risk issuers and countries.

KEY RATING CONSIDERATIONS

Supranational status supports the rating

CGIF's supranational status underpins its rating. CGIF was established in November 2010 by the governments of the ASEAN countries, China, Japan, North Korea, and the ADB with a policy mandate to promote financial stability and develop local bond markets in the ASEAN+3 region.

In our opinion, it is unlikely that other private or supranational institutions could easily replace CGIF's role. Its long-term commitment to developing regional bond markets and promoting economic growth in the ASEAN+3 region, coupled with its higher risk tolerance in emerging markets, sets it apart. CGIF's priorities are to support bond issuers in ASEAN and the frontier markets, especially first-time issuers in local currencies, cross-border transactions, and new instruments. The latter includes thematic bonds, project bonds, securitization, real estate investment trusts (REIT), green bonds, social bonds, and sukuk.

Consecutive rounds of capital increases by CGIF's contributors highlight their strong support and commitment to CGIF's objectives. In 2017, CGIF's contributors approved a capital increase proposal to raise paid-up capital on an uncommitted basis from USD700 million to USD1.2 billion by 2023 to support business expansion. The paid-up capital stood at USD1.158 billion as of 30 June 2024. Contributors have agreed not to distribute any dividends to date, demonstrating their strong commitment to CGIF.

CGIF's management team, made up of experienced international professionals, has successfully met its performance targets and managed risk effectively. This includes achieving financial goals and maintaining a high-quality portfolio as measured by its internal risk rating (IRR).

Very strong capital base underpins rating

We expect CGIF to maintain its very strong capital position supported by earnings retention and steady guarantee expansion. CGIF has a robust capital buffer to cover potential losses from guarantee calls, notwithstanding the absence of callable capital. CGIF's reported capital adequacy ratio stood at 4.60 as of June 2024, down slightly from 4.63 as of June 2023 but well above the management action trigger of 1.1.

As of June 2024, CGIF maintained a conservative leverage ratio of 1.15 times, slightly higher than the 1.12 times recorded in June 2023. Despite a more active guarantee expansion strategy in 2023 and a target of USD600- USD700 million in new guarantees for 2024-2026 (compared with USD403 million in 2023), we expect the leverage ratio to remain below the internal limit of 2.5 times in the near future.

Prudent risk management

In our view, CGIF maintains a prudent growth strategy and risk management framework, even with a more active guarantee expansion in 2023. CGIF adopts a risk management framework and operational policies to manage its credit, market, liquidity, and operational risks. The risk management framework encompasses comprehensive guidelines covering the guarantee process. This includes credit risk assessment and underwriting, risk monitoring, handling claims on guarantee calls, and recovering losses.

CGIF enforces internal concentration limits on credit and investment risks to maintain a well-diversified exposure. To further mitigate its credit risk, CGIF cedes a portion of its exposure to reinsurers with strong credit profiles. Additionally, CGIF conducts various forms of liquidity stress tests on a quarterly basis to assess its ability to meet potential lumpy obligations arising from guarantee calls.

CGIF's good prospects of recovery on the first two guarantee calls reflect this careful risk and recovery management practice. We expect these calls to have only minimal impacts on CGIF's capital and liquidity. CGIF is in the process of asset recovery from its first guarantee call of KNM Group Berhad (KNM), which occurred in December 2021. The recovery is contingent on the successful sale of KNM's assets, which could lead to a reversal of all KNM-related expected credit loss (ECL) provision currently held by CGIF. Further, the total gross exposure of the guarantee payment of THB2.8 billion would have limited impact on CGIF's capital due to its relatively small size. In its second guarantee call, CGIF has set aside a small amount of loss provision for its payment of THB82 million on XJ International Holdings Co., Ltd. (XJ INTL), which took place in March 2024. As of October 2024, the entire exposure to XJ INTL has been fully recovered.

Strong funding and liquidity profile

We assess CGIF's funding as neutral as the institution is primarily equity-funded. CGIF does not have an established capital market access since its financial policy does not permit borrowing other than for cash-management purposes. CGIF can only obtain short-term funds from eligible counterparties for specific purposes, such as managing liquidity for guarantee calls or other operational needs.

Based on our assessment, CGIF has a very strong liquidity buffer of over 3.0 times to cover potential liquidity needs from guarantee calls in a stressed scenario. We view CGIF's liquidity risk management approach as conservative. The two-tier framework mandates regular monitoring of liquidity adequacy for day-to-day operations and a stress test in the event of significant claims. The regular liquidity gap monitoring necessitates that expected cash inflows from investments and guarantee fees cover cash outflows from operating expenses and potential claim payments within the following 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. The ADB oversees CGIF's investment portfolio, primarily composed of bonds issued by highly-rated government-related entities (GREs). This portfolio serves as CGIF's source of liquid assets.

High-quality investment portfolio

CGIF's investment policy is to only invest 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 GREs of contributing countries.

CGIF aims to achieve stable investment income by adopting a buy-and-hold-to-maturity strategy with a target effective duration of approximately three years. It has also implemented explicit concentration limits on countries, individual issuers, issuer types, and credit ratings, along with conservative limits on value-at-risk (VaR) and unrealized market loss.

As of June 2024, the majority of its investments were in fixed-income securities issued by sovereigns or GREs with credit ratings of "AA-" or above. CGIF's average portfolio duration was 3.33 years as of June 2024, longer than 3.04 years as of June 2023 but still within the internal ceiling of 5.0 years.

BASE-CASE ASSUMPTIONS

- Leverage ratio of 1.4 to 1.6 times.
- New guarantees of around USD600-USD700 million per annum.
- Investment yields of around 2.5%-3.0% per annum.

RATING OUTLOOK

The "stable" outlook reflects TRIS Rating's view of CGIF's strong and stable relationship with its major contributors and the likelihood of continued operational support. The outlook also takes into consideration 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. We also expect CGIF to 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. Any evidence of reduced capital support from the contributors or signs of weakening in the governance and risk management framework could also lead to a downgrade scenario.

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 provides 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 2024 *	-----------Year Ended 31 December ---------- 2023	2022	2021	2020
Interest income	21.0	37.5	28.5	27.3	28.9
Guarantee income	11.0	20.5	20.0	19.4	17.4
Other revenue**	1.1	0.5	2.6	4.4	3.4
Total revenue	33.1	58.5	51.1	51.1	49.6
Net income from operations	22.4	44.9	15.2	32.0	23.7
Total assets	1,398.1	1,387.4	1,305.0	1,372.8	1,351.7
Total liabilities	85.4	84.9	81.8	80.4	87.1
Shareholders' equity	1,312.6	1,302.5	1,223.2	1,292.4	1,264.5

* *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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